MAGYAR NEMZETI BANK

SENIOR LOAN OFFICER SURVEY ON BANK LENDING PRACTICES

SEPTEMBER 2008

Summary of the aggregate results of the survey on 2008 H1

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Analysis prepared by Dániel Homolya

Financial Stability

Summary

In the spring of 2003, the Magyar Nemzeti Bank launched its Senior Loan Officer survey in the interests of more deeply understanding developments and processes related to the lending market. This survey is conducted every six months. The latest survey was conducted in July and examined the household and corporate lending segments as well as the financing of municipalities by banks.

In relation to the household lending market, the results of the survey indicated that banks' willingness to lend increased both in respect of housing loans and consumer loans in 2008 H1. In the last half year, credit brokers' role in sales activity and in the process of replacing loans with new loans continued to become increasingly important. Price terms of loans (fees, spreads over funding costs) were eased further. Interest rates of households' credits increased, but the increase is not reached the level of increase in funding costs.Some of the responding banks moved to tighten their non-price loan terms, although the summarily slight easing was observable on the market. The fierce competition experienced in the banking sector continues to be a motivation to ease conditions, but the banks envisage tightening steps in H2 2008, mainly due to the cost increase and shortening in funding and deterioration in customers' creditworthiness. The appreciation of the forint in 2008 Q2 did not lead to customers shifting away from foreign currency loans, and at the same time it encouraged more active prepayment of foreign currency loans which had been taken out at a weaker exchange rate.

The recent planned tightening tendencies in household lending conditions were appeared earlier in foreign lending surveys. Banks reported a clear trend towards tighter household lending conditions in the euro area, the United States, Great Britain, Poland and Lithuania.

According to the survey, willingness to lend is not increasing in the corporate segment. Moreover, one institution reported restrained lending activity in this segment. Responding banks considered the sectors of small, micro- and medium-sized enterprises riskier than large enterprises and the good-quality segment of commercial real estate loans. Respondents perceived a further strengthening in the demand for corporate loans, mainly for the purpose of financing inventories and receivables, rather than for investment. As a result of the strengthening of the forint in 2008 Q2, respondents perceived a stronger increase in demand for forint loans compared to the previous half year. Similarly to the previous half year, banks reported that they tightened their credit conditions (in spreads over funding costs in the corporate segment), because of the unfavourable economic prospects, industry-specific problems (especially in the construction industry) and a deterioration in banks' liquidity position. In respect of commercial real estate loans, senior loan officers reported unchanged willingness to lend and unchanged lending conditions. Respondents experienced a slight improvement in the loan repayment rate in 2008 H1, although the majority of banks experienced a deterioration of this parameter in the small and micro-sized enterprises segment, and this trend is expected to continue in the next half year as well. The tightening trends in the corporate segment found in this survey for Hungary

were similar to the results of foreign lending surveys, which showed credit conditions tightening in the corporate segment.

In the municipal segment, the strong increase in exposure observed in 2007 H2 continued in 2008 H1 as well, albeit at a lower rate than in the previous half year. Banks continued to tighten their credit conditions in the municipal segment in 2008 H1. Moreover, looking ahead to the next half year banks expect a moderated level of demand for loans to the municipal sector.

Depending on the character of funding by parent banks, the vast majority of respondents were still affected by the impacts of the turbulence triggered by the subprime mortgage market crisis in H1, and started to transfer the increase in funding costs to customers, to an extent depending on the competitive situation.

The methods of the Lending Survey are being reviewed. A study backtesting the efficiency of the Hungarian Lending Survey with statistical methods will be published at the end of the year. Based on these results, the survey conducted among banks and international comparison, the survey will be conducted within an improved framework in 2009.

Aggregate results of the questionnaire

Based on the answers, the results of the survey are presented in the form of a descriptive analysis and with the help of charts illustrating the answers. Annex 1 contains the figures of the total amount of outstanding loans in each segment and the shares of the responding banks. Annex 2 describes the methodological background,[1] numerical data on the segments are contained in Annex 3, while answers to questions are presented in detail in Annexes 4, 5 and 6 (in a separate Excel file attachment).

The retrospective questions in the questionnaire refer to 2008 H1, while the forward-looking questions contain projections for 2008 H2. The questions concentrate on the changes in comparison of the previous half-year: thus the basis period for retrospective questions is 2007 H2, and in case of forward-looking questions 2008 H1 is the basis period.[2]

1. Household lending market

In the domestic environment, which is determined by macroeconomic stabilisation measures and the financial market turbulences on the international markets, banks' activity in the household segment continues to strengthen, both in the housing loan and consumer credit markets. With regard to housing loans, fewer institutions indicated increases in the willingness to lend than in the survey for the previous half year. As far as consumer credit is concerned, willingness to lend varies according to product category: nearly half of the banks active in granting general purpose mortgage loans reported increasing willingness to lend, while institutions' willingness to lend increased more moderately in respect of other consumer credit segments (mainly in case of personal loans, hire purchase loans and credit cards). Looking at the average picture, it was found that creditworthiness standards were maintained at nearly the same level, although 3 banks tightened and 2 banks eased their housing loan conditions, whereas for consumer loans 2 institutions tightened and 2 institutions relaxed their lending conditions.

Respondents left their credit standards almost completely unchanged, but noted some relaxation of credit conditions, albeit to a minor degree. To a great degree, however, the perceived relaxation is attributable to the fact that market participants could not or did not want to completely transfer the increase in funding costs to their customers. Consequently, the spread between the funding cost and lending rate somewhat decreased. All in all, in the previous half year nearly half of the institutions perceived a decline in demand for housing loans, while compared to the stronger demand observed in the previous half year, they experienced a further increase in demand in the consumer loan market (excluding the participants specialising in motor vehicle and hire purchase loans as well as credit card and overdraft credit products).

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[1] Some keywords in the methodological notes are worth highlighting. Willingness to lend reflects the intention of respondents to expand in the given segment of lending. Credit standards cover the internal policies that determine the types of customers and customer groups (based on sector, geographical location, size, financial indicators, etc.) and grantable credit products (only collateralised, investment, overdraft loans, etc.). Among credit conditions we can differentiate between price-related factors and non-price related factors. Non-price related conditions (e.g. collateralisation requirements, loan covenants, maximum size of loan/credit line, etc.) are concrete contract conditions; the bank is ready to extend the loan only under these conditions. In case of price-related conditions, we survey the spread between the interest rate level and the funding cost and the risk premium.

[2] 13 banks gave answers for the household segment (housing loans: 9 institutions, consumer credit: 13 banks and 5 financial enterprises owned by banks), while there were 7 responding banks for the corporate segment. We asked 6 institutions about the trends in lending to municipalities.

Chart 1: Willingness of banks to grant housing loans and consumer loans (difference between the ratios of those reporting higher and lower willingness to lend)

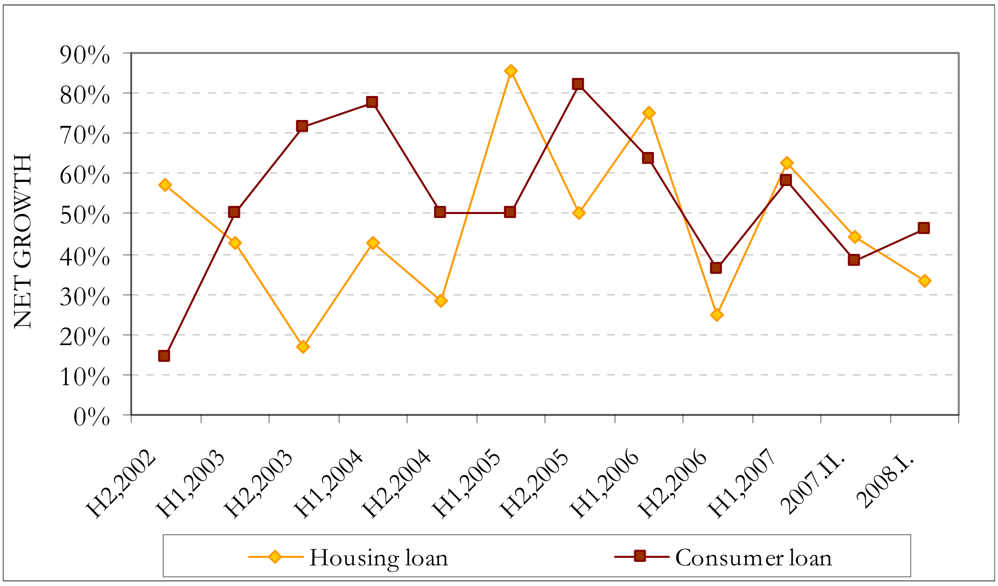
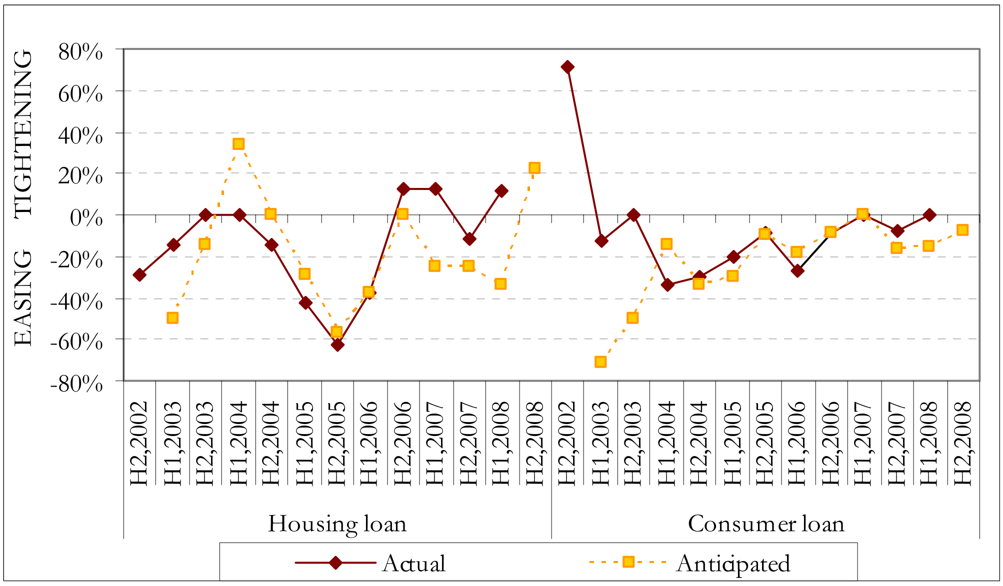


Chart 2: Changes in credit conditions/creditworthiness standards of housing loans and consumer loans (ratio of banks indicating tightening minus those reporting easing in lending standards)



Housing loans

(Questions 1–9 and 14 of Annex 4)

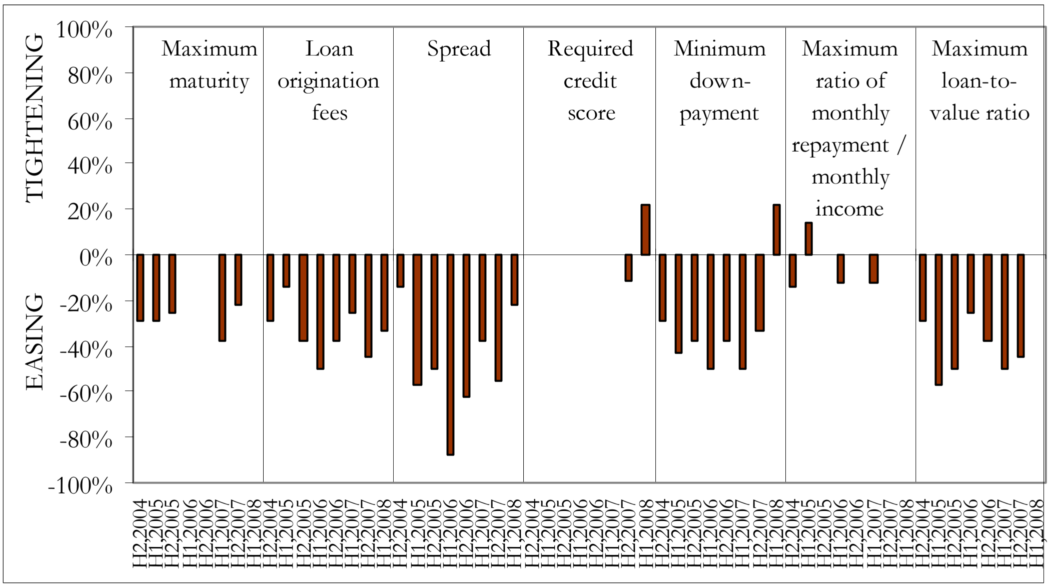
Supply side

For 2007 H2, banks indicated a more subdued increase in willingness to lend. Based on the answers received, even fewer institutions reported an increase in willingness to lend in 2008 H1 (Chart 1): four respondents reported that their lending policy was more expansive than before, while another four maintained their willingness to lend at the high level reached earlier. At the same time, one institution reduced its willingness to lend to some extent. Activity in lending for housing continued to be basically related to foreign currency loans, while lending in forints was referred to by the participants as an irrelevant market.

Contrary to the previous results of the surveys, creditworthiness standards were eased by two banks and somewhat tightened by three institutions (Chart 2).

In line with the longer-term trend, however, there was further significant easing in ***conditions for housing loans***, although the extent of this easing can be considered more moderate than before, and signs of tightening also appeared.[3] Banks continued to ease price-related lending conditions (spread over cost of funds, fees). This partly stems from the fact that institutions were unable to transfer to customers the increase in funding costs perceived in the last half year. In respect of other lending conditions, the easing trend experienced in the previous half years seems to have come to an end.

Chart 3: Lending conditions in the market of housing loans (ratio of those reporting tightening minus those reporting easing)



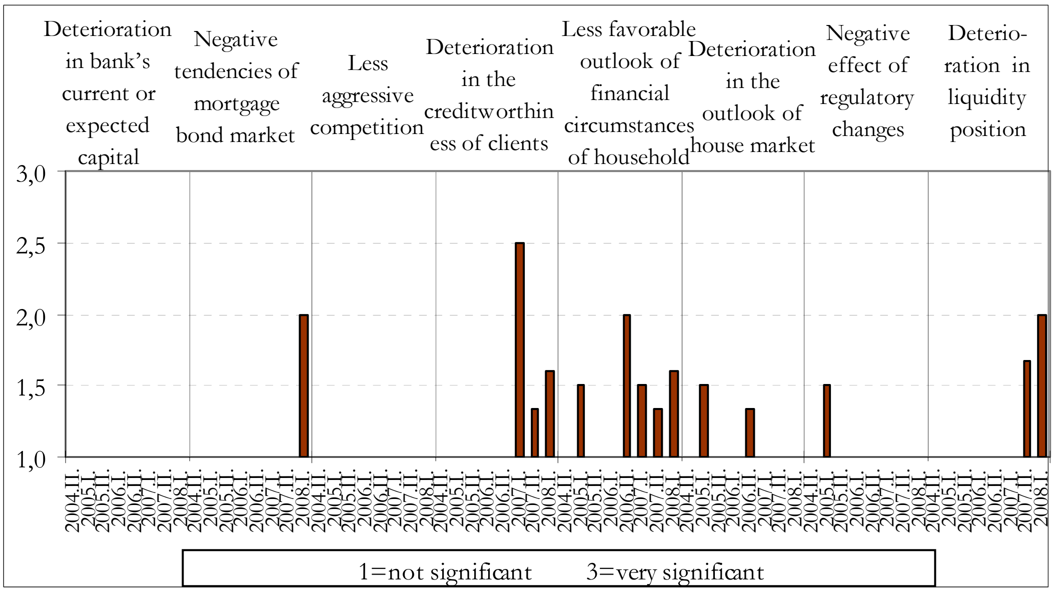
- In the past half year, no institution changed the maximum maturity of its housing loan products.
- Three banks continued to reduce or remit loan origination fees in the framework of promotional campaigns. Most of the banks surveyed already have so-called 'handling charge free' schemes ('only interest type product').
- Participants' pricing behaviour shows the same pattern both for HUF and FX (typically CHF) housing loans. A smaller proportion of participants (3 banks) eased the contract conditions in terms of the spread, while 5 institutions left them nearly unchanged, and one increased them.
- In respect of the minimum required downpayment and the maximum loan-to-value ratio (so-called LTV), the responses suggest that the general trend of easing has come to a halt. While the maximum LTV was increased and reduced by two institutions each, seven institutions required an unchanged minimum downpayment, and two reported an increase in the minimum downpayment.

[3] Almost all banks treat the HUF and FX schemes the same way in determining standards and conditions, and as the demand for HUF housing loans is very low, the conclusions basically apply to both product types equally, except fees charged for granting the loans and the spread. In the case of HUF loans, these two parameters were only eased by one bank each in the same way, as for FX loans as well.

- In the previous survey, we indicated that another institution had made a move towards asset based financing, but in the latest survey there was an institution which cancelled this product due to risks which were higher than expected. At the same time, the majority of participants surveyed continue to use products based on indirect examination of income.
- The survey also included a question on the minimum required level of creditworthiness. Due to the various levels of maturity of their portfolios, institutions have demonstrated different behaviours in this respect. In contrast to the past, however, there were no institutions which reported easing: two banks tightened, while the remaining seven institutions left the required level of creditworthiness nearly unchanged.
- Market participants surveyed also reported changes in other conditions: some participants reported a narrowing of the range of real estate which can be financed (narrowing the list of settlements and ruling out funding for adobe houses), while one institution reported a reduction in the requirement for the length of current employment, which had previously been relatively strict.

In the banks' opinion, easing of lending conditions continued to be pushed mainly by strong competition. However, those institutions which introduced certain tightening measures, typically explained their decision with the expected or actual deterioration in the liquidity position (availability and price) and with the unfavourable income outlook and expectations of declining creditworthiness (Chart 4).

Chart 4: Reasons for easing creditworthiness standards and lending conditions for housing loans



In the respondents' opinion, residential property leasing is still present as a supplementary product only, and it does not represent a serious market force in the case of households. In terms of the standards related to real estate leasing, the institutions apply basically the same principles, and it is product-specific features which account for the differences in standards and lending conditions. One institution's subsidiary, which provides leasing services, introduced some easing (in respect of maturity), and there was also one institution which plans easing for the next half year. Overall, respondents continue to expect a modest rise in demand for residential property leasing, which, due to the weight of the product, will not move the market as a whole.

Based on plans for 2008 H1, three banks are to tighten creditworthiness standards/lending conditions in 2008 H2, while one institution indicated intentions to ease its conditions, basically driven by the goal of keeping existing customers and acquiring new ones. Based on what the senior loan officers said, tightening may basically appear in pricing. As the increase in the costs of funds comes to a halt, spreads can be increased, and thus, following the narrowing, margins can be widened somewhat.

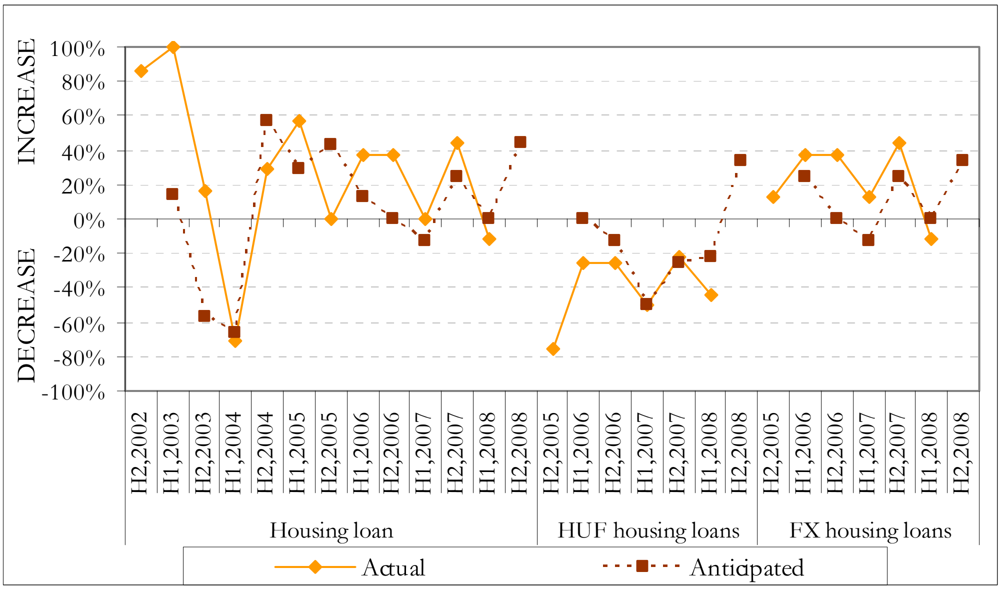
Demand side

In the interviews conducted in January 2008, respondents expected unchanged demand on average, with some decline in demand for forint loans.

Looking back to 2008 H1, participants found that their expectations were correct: in general, and in the case of foreign currency loans, three participants perceived an increase in demand compared to the previous half year (apart from seasonal effects), two institutions perceived unchanged demand, while four institutions experienced some weakening. Banks still only experienced an increase in the number of loan applications for foreign exchange loans. As far as forint loans are concerned, similarly to the previous half year, the banks interviewed did not indicate any special interest in these products. Four of the respondents believed that demand for forint-denominated housing loans was even weaker than in the previous half year, although five institutions perceived unchanged demand. In the opinion of the respondents, the appreciation of the forint in 2008 Q2 was not reflected in demand for forint housing loans, and this factor increased more the prepayment activity.

Institutions which experienced an increase in demand mainly emphasised supply reasons: more intense competition has a demand increasing effect.

Chart 5: Demand for housing loans
(ratio of banks indicating an increase vs. banks indicating a decrease)



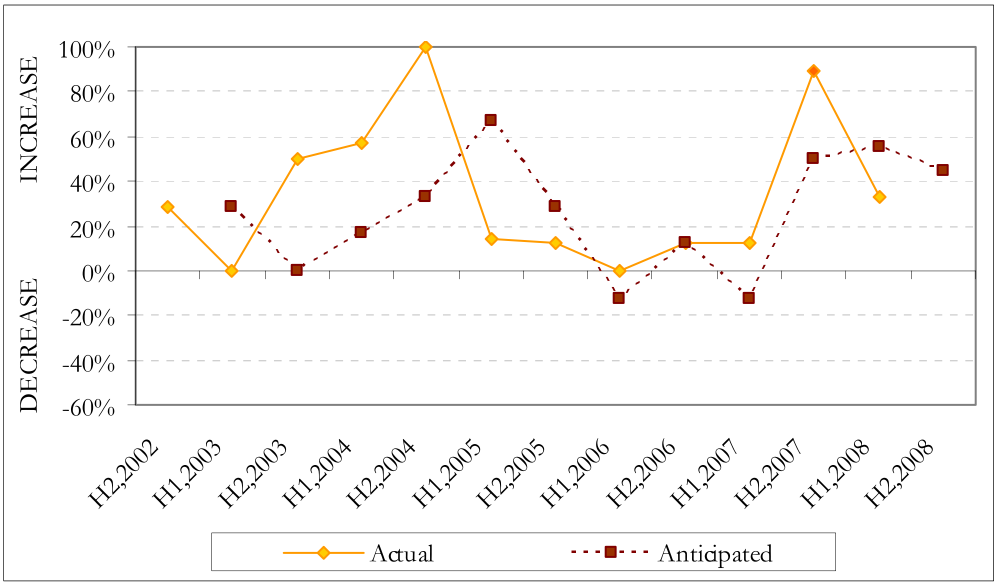
With regard to demand in the next half year, respondents' expectations were more optimistic: five participants had optimistic forecasts, one projected a decline in demand, which means an increase in expected demand on average, compared to earlier expectations. Contrary to earlier opinions, presumably as a result of the effects of the appreciation of the forint and the related expectations, market participants now consider an increase in forint loans possible as well: four institutions forecasted an increase in demand, while only one institution indicated an expected decline in demand.

Nominal housing prices

Overall, the banks participating in the survey – based on the sample available for them – perceived a modest increase in real estate prices. Similarly to earlier surveys, there were significant differences in perceived price movements in terms of new and used homes. While as many as four banks experienced a slight nominal price increase in the market of new homes, in the market of used homes only one bank perceived low price increases and two banks perceived a nominal decline in prices.

Most institutions forecasted modest price appreciation for the next half year. An upswing in prices is still expected more in the market of new homes, where four banks projected a slight additional nominal increase. According to seven banks, prices will not change in the market of used housing; one bank expects a small increase, and one expects a slight decline in the prices of used homes.

Chart 6: Nominal housing prices according to senior loan officers
(ratio of those reporting higher minus those reporting lower prices)



As in the previous surveys, some of the respondents once again mentioned that there are considerable differences in developments in housing prices according to location and size of the real estate. For example, the area in which the given bank finances real estate developments for housing plays an important role in the assessment of the prices of new homes.

Consumer and other loans

(Questions 15–21 of Annex 4)

The questions regarding lending for consumption were analysed according to the following product groups: general purpose mortgage loans (9 participating banks), personal loans (10 participating banks), motor vehicle loans (2 participating banks and 6 financial enterprises with banking backgrounds), hire purchase loans (3 participating banks), credit cards (10 participating banks) and the overdraft credit product (with 9 banks responding), which was first included in the previous half year. Longer time series are not available for all product groups. Consequently, this analysis basically presents the last one-year trends of the market segment.

Supply side

Similarly to the market of housing loans, banks' willingness to lend continues to strengthen in the market of consumer lending as well (Chart 1). Based on the answers, similarly to the previous half year, the increase in willingness continues to be spectacular in general purpose mortgage loans, where one institution reported significant opening, while three indicated somewhat increasing willingness to lend. This result is in line with the fact that several institutions reported an increasing role of 'debt consolidation' loans again, and that the existing stock of real estate as assets provides a potential for further lending. It should be noted that this phenomenon of loan replacement is basically not about a restructuring within one's own portfolio, but rather about acquiring one another's loans.[4]

The increase in willingness to lend was usually coupled with nearly unchanged ***lending standards***[5] (Chart 2). However, the 'nearly unchanged' overall picture is composed of changes in the various product groups. The overall picture, which is different from the nearly unchanged state, can be seen in the case of two products: in hire purchase lending, one out of the three respondents indicated easing, while the other two institutions reported a trend to leave their standards unchanged. In case of the credit card product, three out of the responding ten institutions indicated a tightening of standards, six indicated leaving the standards unchanged, and one institution reported easing. Institutions indicated a more moderate easing of lending conditions than before in this segment as well. With regard to motor vehicle loans, two out of seven respondents reported a slight increase in willingness, while the willingness to lend of other respondents did not change in this segment. Institutions indicated a basically similar, modest increase in willingness to lend in the segment of loans without collateral. An exception is overdraft credit, where three out of nine respondents indicated an increase in willingness, with the other respondents reporting no change. All this may be related to the fact that, in accordance with a more conscious risk assessment and as a result of an increase in the range of available data, behaviour-based rating procedures related to overdraft credit can be used in an increasingly professional manner. Thus, an increase in willingness may be coupled with maintaining the risk level as well. With regard to the supply side, marketing campaigns continued to play a significant role, together with cross selling connected to the bank's other products in the case of credit cards and hire purchase loans as well as co-branding with service providers operating in other sectors. With regard to hire purchase lending, respondents emphasised that due to the high levels of commission this product group by itself cannot be considered as profitable, so the role of cross selling is of key importance.

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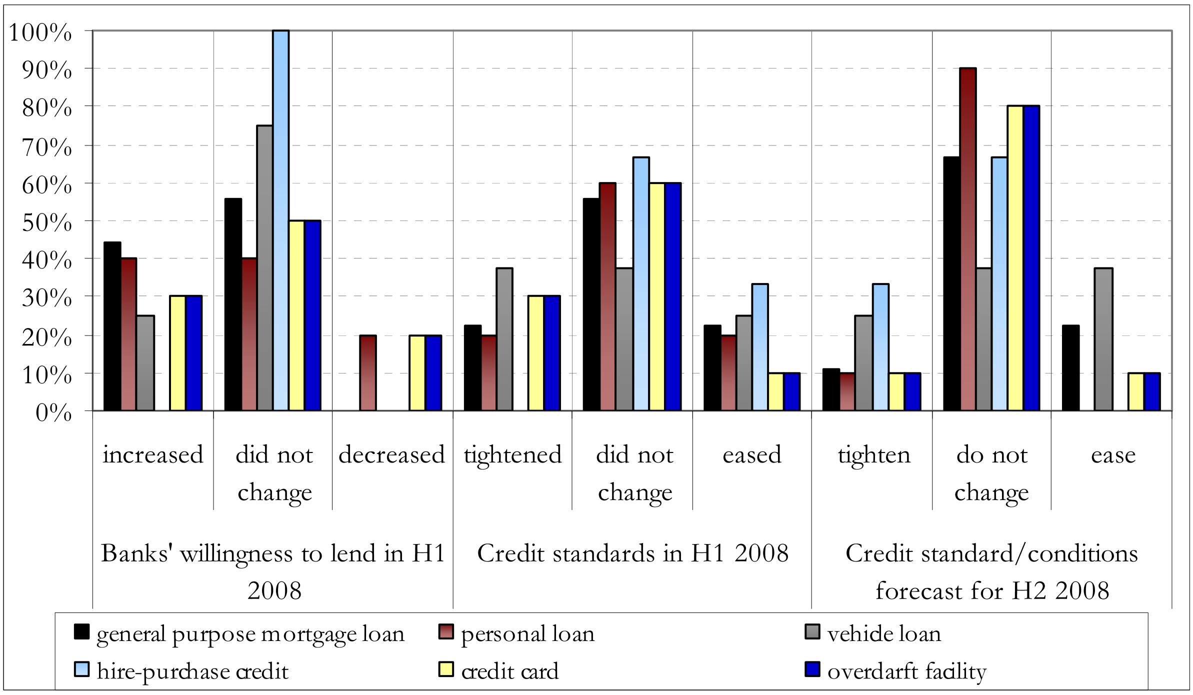
[4] Current loan refinancing trends are discussed in more detail in the section on current issues.

[5] Banks typically change the standards of general purpose mortgage loans together with those of the lending for housing. Thus, in accordance with the market strategy, at the bank where easing took place, it also took place in general purpose mortgage loans.

Chart 7: Willingness to lend and creditworthiness standards for different consumer loan products (ratio of banks giving the relevant answer)



In terms of ***lending conditions***, on the whole the level was broadly maintained with a more cautious degree of easing than previously. Five banks noted easing in the lending rate and the spread between the funding costs, while three banks indicated easing in the fees charged. Institutions eased significantly in terms of price-related factors: on the one hand, in line with the market competition trends, nine respondents indicated leaving their conditions unchanged, three institutions indicated an easing in relevant fees, and only one institution reported tightening. However, in net terms, more than one fifth of the respondents indicated easing in the spread between the lending rate and funding costs, which is basically attributable to the fact that in the first half of the year they could transfer only a part of the perceived increase in funding costs to their customers. One institution indicated an easing in the minimum downpayment. Tightening or easing for certain products was related to the changes in the riskiness of the bank's portfolio (Chart 27).

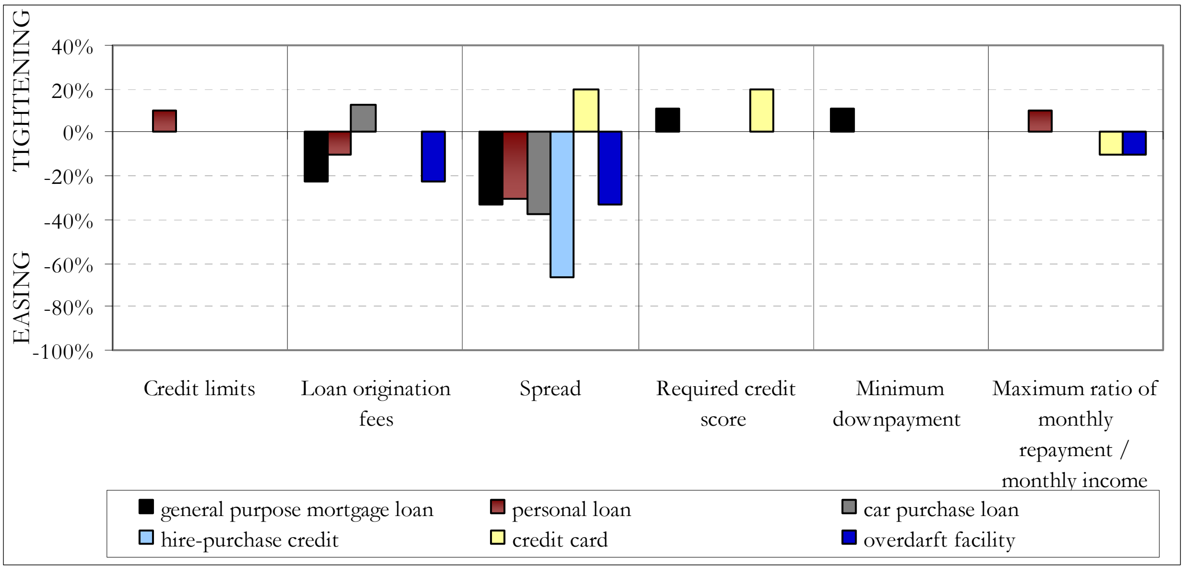
As far as the details are concerned, the following changes can be observed in the lending conditions not mentioned above:

- One bank slightly tightened the credit limit, is in line with the calibration process related to the products.
- Overall, one institution eased the downpayment size. The change affected general purpose mortgage loans and vehicle loans: there was an institution which carried out tightening in general purpose mortgage loans along with easing by two institutions, and the only institution which reported a change in vehicle loans indicated easing.
- In terms of the minimum required level of creditworthiness, 3 of the 13 respondents indicated tightening. This occurred in certain cases and for certain products. Reacting to an increase in the riskiness of the portfolio, several institutions introduced tightening in terms of the level of minimum creditworthiness in the credit cards segment. Overall, this represents a net 20% tightening. One institution reported tightening in the case of general purpose mortgage loans. Two institutions indicated tightening and two institutions indicated easing in vehicle loans.

- With regard to general purpose mortgage loans and vehicle loans we also inquired about developments in maximum maturity. None of the institutions indicated any change in the maturity of general purpose loans, while one institution reported an extension of maturity of vehicle loans. Motor vehicle financing institutions said that the issue of changing the maturity has to be judged carefully, as a significant part of customers often effect prepayment. Consequently, the effective maturity of the portfolio is shorter than the contractual maturity when extending the loan.

It is important to emphasise that some of the participants eased conditions for new placements basically for customers with a credit history, i.e. different conditions apply to completely new customers and ones with an established relationship. This is in line with the fact that banks are using so-called 'behavioural scoring' techniques to an increasing degree.

Chart 8: Lending conditions for various consumer loan products
(ratio of those reporting tightening minus those reporting easing)



Similarly to previous half years, respondents almost exclusively indicated the increasingly keen competition as the reason for relaxing their lending policy. They particularly emphasised the role of agents, who contributed to the significant increase in refinancing between banks to a great extent. Similarly to the previous half year, banks emphasised stiffer competition from financial enterprises to a lesser extent, because, as they said, they are active in different segments, with different target groups (Chart 28).

Banks which tightened their creditworthiness standards or credit conditions explained their moves with the following underlying reasons: deterioration in the liquidity situation, the current deterioration in the availability and conditions of sources or deterioration of this nature expected in the near future, deterioration in customers' creditworthiness and worsening prospects for households' income situation (Chart 29).

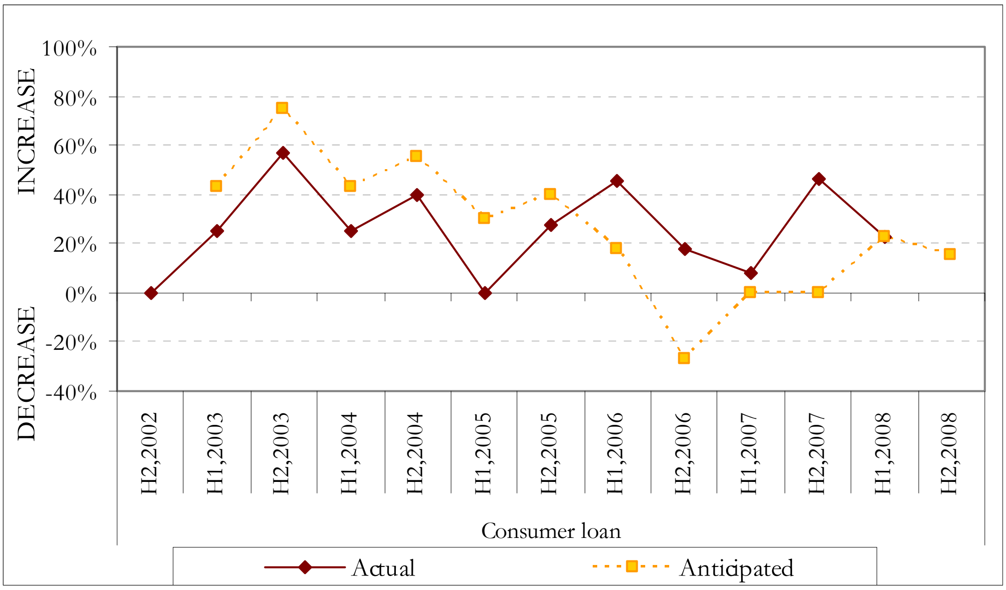
Based on the respondents' aggregated answer, a further slight easing can be expected for 2008 H2. In almost all segments there are institutions which indicated tightening and ones which indicated easing. In terms of general purpose mortgage loans, which dominate in consumer lending, two institutions envisaged further easing, while one forecasted tightening (Chart 7).

Demand side

In the previous survey, respondents' expectations regarding 2008 H1 were quite diverse, although basically optimistic, apart from the vehicle and hire purchase loan markets. In January 2008, most respondents expected a further increase in demand for general purpose mortgage loans and credit cards.

Looking at the average picture, these expectations proved to be correct, as institutions reported a slight increase in demand in 2008 H1: five participants indicated an increase in demand, while another three reported a fall in the number of loan applications.

Chart 9: Demand for consumer loans
(ratio of banks indicating an increase vs. banks indicating a decrease)

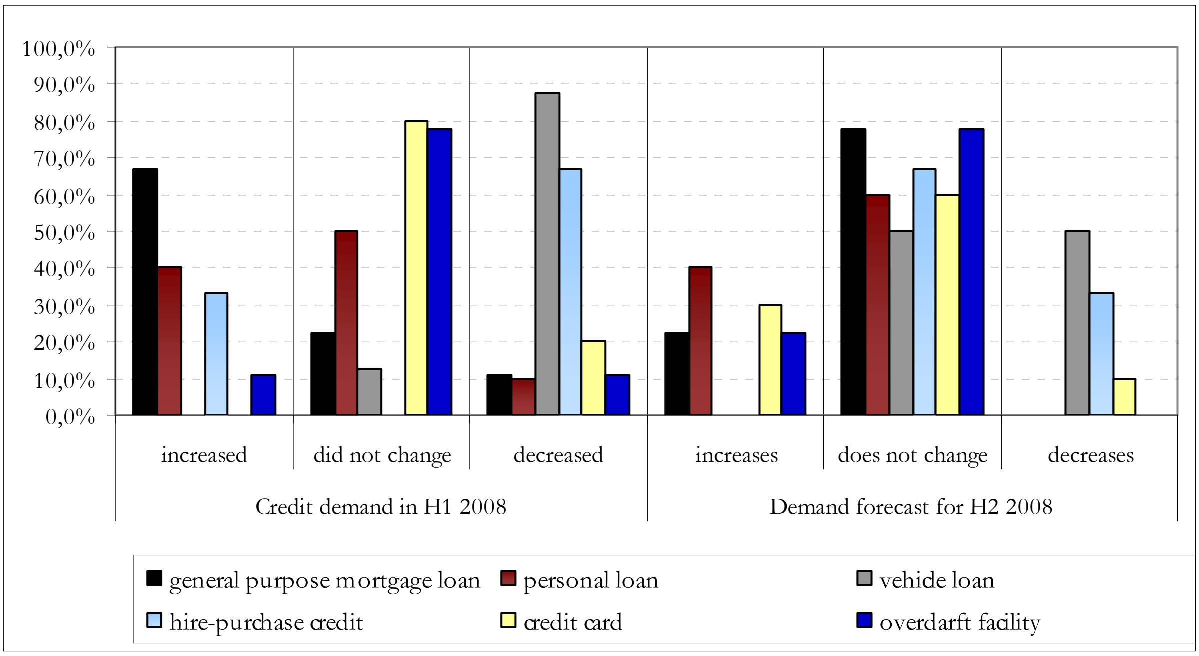


However, the extent of this slight overall increase in demand was different in the various product groups:

- In vehicle lending, similarly to the experience of the previous two half years, almost all participants perceived a decline in the number of new loan applications (only one respondent perceived unchanged demand, while the others perceived falling demand).
- The decline was also considerable in hire purchase loans. Two of the three respondents perceived a decline in demand, a part of which in certain customer segments may have been caused by the substituting effect of other products (mainly general purpose mortgage loans).
- Credit cards did not become more popular. Moreover, 20% of the participants perceived a decline in demand (eight respondents experienced unchanged demand, while two indicated decrease in the demand for credit cards).
- Some upswing in demand was perceived in the segment of personal loans, which may partly be attributable to consumption smoothing reasons. Four participants reported increasing demand, while one respondent indicated declining demand.
- Similarly to the previous two half years, respondents perceived a significant strengthening in demand for general purpose mortgage loans: two thirds of the 9 respondents perceived an increase in demand, while only one institution perceived a decline in demand. The increase in demand is coupled with the popularity of foreign exchange schemes.

- The opinion of the two participants that indicated a change was split, as one perceived a decline in demand and one indicated an increase in demand for credit card products.

Chart 10: Demand for various consumer loan products (ratio of banks specifying the given answer)



Expectations for the next half year (2008 H2) can be considered moderately optimistic: four out of the thirteen respondents expect an overall increase in demand, while two institutions expect a decline in demand. Respondents continue to expect an upturn in demand for general purpose mortgage loans and personal loans and, contrary to the experiences in the previous half year, for credit cards and overdraft facilities. Participants active in lending for vehicle purchase and hire purchase expect a continued decline in demand.

The riskiness of the household portfolio

(Questions 10–13 and 22–25 of Annex 4)

Continuing the practice which started in January 2008, in our survey we asked more detailed questions regarding changes in riskiness. We inquired about the Basel risk parameters, the default rate (PD) and the loss given default (LGD) in the survey. We emphasise that we asked about risk perception and trends based on available data, rather than about validated risk parameters, as most institutions were not able to implement the method based on more advanced internal ratings (IRB). The questions focus on the changes, thus information is received only with regard to risk perception. A complete picture would be provided if risk levels were also available, which, in parallel with banks' IRB preparation, are presumed to become more widely available later.

Based on the answers, a slight deterioration in the default rate was seen in 2008 H1 as well, similarly to institutions' experiences in 2007 H2. Institutions forecasted a continuation of this trend of deterioration (Chart 11). Deterioration mostly took place in the segments of mortgage loans (mainly as a result of the maturation of the portfolio) as well as personal loans and vehicle loans. In terms of credit card and overdraft credit products, institutions perceived a nearly unchanged default rate for the last half year. However, for the next half year, 40% of the respondents (four banks) forecasted deterioration for credit cards, while only 10% of institutions (one bank) indicated a decline in the default rate.

Overall, looking at the products, the institutions did not report any drastic deterioration in loss given default (LGD). With the strengthening of monitoring activity and an increase in the efficiency of collection, the majority of respondents experienced stable development in the past one-half year, and expect the same for 2008 H2. Overall, market participants experienced trends of deterioration in the segments of motor vehicle loans, hire purchase loans and personal loans, and they also expect further deterioration in these portfolio segments (Chart 12).

Chart 11: Default rate of loans to households

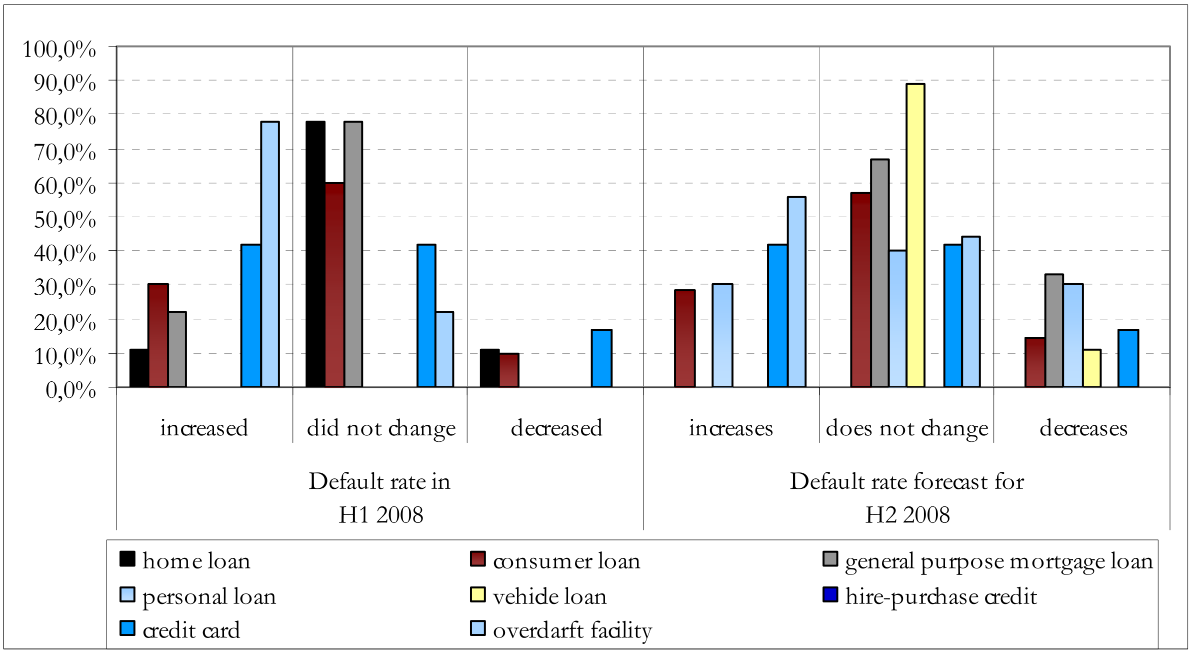
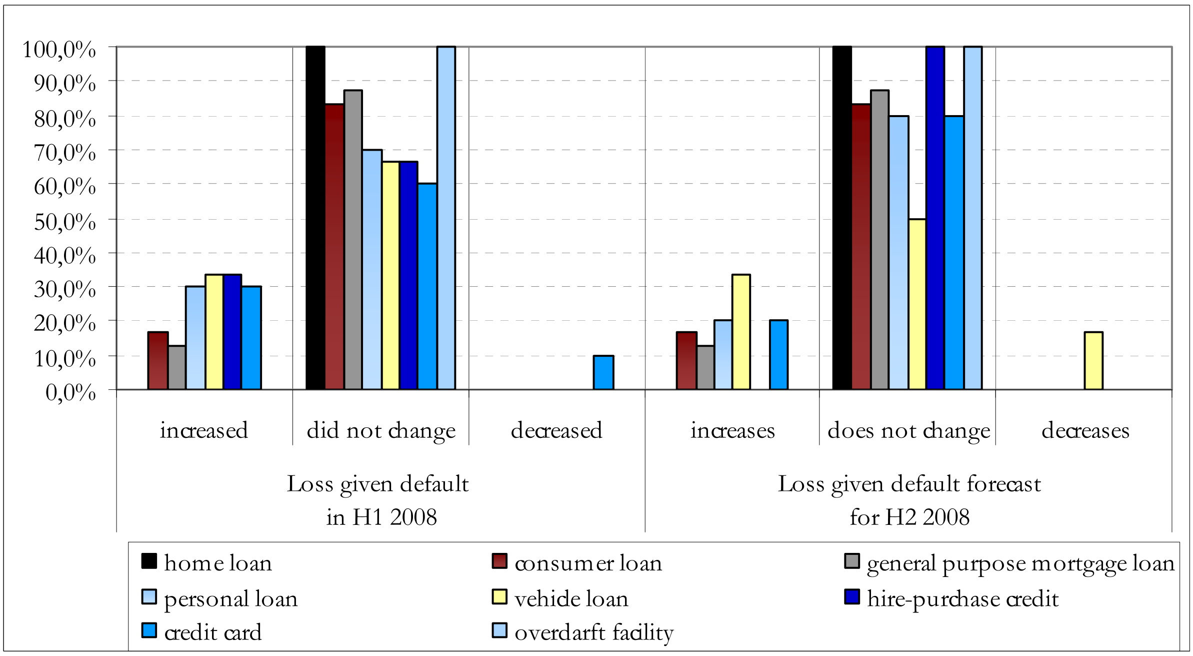


Chart 12: Loss given default of loans to households



2. Corporate lending market

In the corporate lending market, in contrast to the previous periods, willingness to lend increased only in case of large enterprises and commercial real estate loans, while the increase in willingness to lend in the financing of small and micro-sized enterprises came to a halt. At the same time, willingness to lend slightly declined in the segment of medium-sized enterprises. The overall picture is extremely multi-faceted, as in the survey there was one institution which indicated a significant decline in its willingness to lend to large enterprises. Most respondents only fine-tuned the elements of the corporate credit rating system (partly in conformity with the Basel II IRB preparations). However, in line with earlier expectations, tightening of creditworthiness standards was observed in all corporate segments. Based on the plans for the next half year, banks are maintaining the tightening measures which have already been taken. Moreover, respondents envisaged additional tightening in the segment of small and micro-sized enterprises. Banks also tightened their lending conditions, and in accordance with the results of the survey conducted at the beginning of the previous half year, the tightening measures apply to the segment of small and micro-sized enterprises as well. In 2008 H1, the current and expected deterioration in banks' liquidity situation (availability and conditions of sources), the less favourable economic prospects and increasingly serious sector-specific problems played an important part in the tightening of standards and lending conditions. In 2008 H1, demand for loans somewhat increased, and compared to the previous half year, forint-based loans accounted for a higher share in the increase, as a result of the appreciation of the forint in 2008 Q2. Demand for loans in the period under review was basically aimed at liquidity financing (increase in assets), while no demand for investment loans was perceived. At the same time, two banks indicated that changes in individual banks' risk tolerance levels can be perceived, so the underlying reason for the increased demand from customers which these two banks receive is that other banks or non-bank sources of credit have become less attractive due to their decreased tolerance for risk.

The answers of banks active in financing commercial properties were rather diverse. Some increase in willingness to lend was registered in respect of commercial real estate, while, similarly to the previous half year, moderate overall tightening took place in lending standards. As reported by the respondents, in an environment marked by stricter refinancing conditions it is felt more strongly that banks carry out a more thorough selection in order to mitigate risks in respect of projects. Based on the answers, demand for loans shows an increase, but the developments in demand are different, depending on the type of project: demand for loans for housing projects declined, whereas demand for office buildings, logistics centres and shopping centres increased. Opinions on shopping centres varied, as two of the respondents reported a saturated market and a decline in demand for loans, while three respondents experienced an increase in demand.

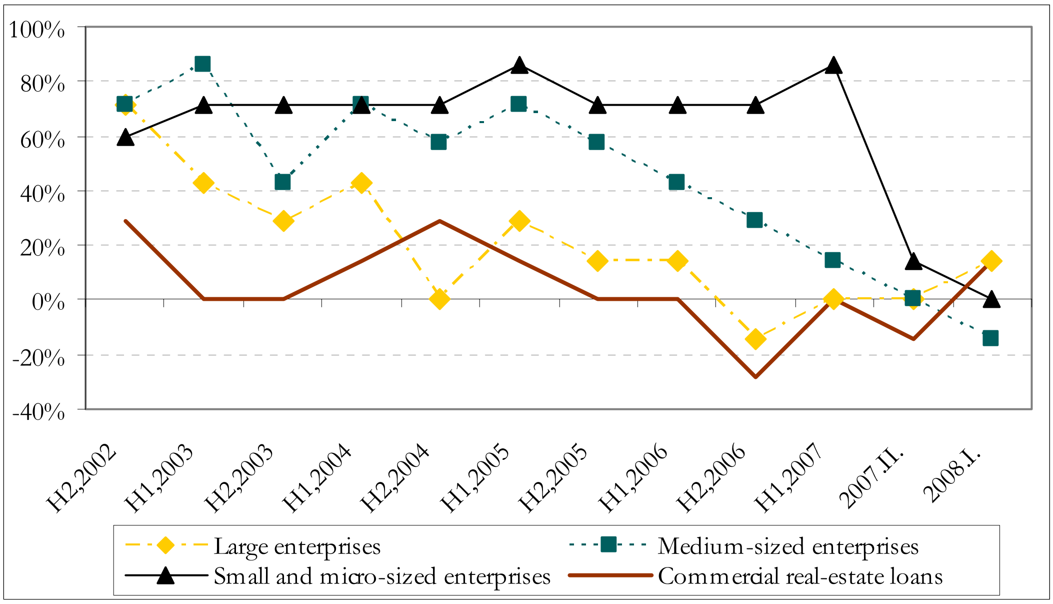
Corporate lending excluding commercial real estate loans

(Questions 1–9 of Annex 5)

Supply side

In 2008 H1, most of the responding banks restrained the increase in their willingness to lend even compared to the previous half year. Moreover, there were institutions which expressly reported a decline in willingness to lend.

Chart 13: Willingness of banks to lend in each sector (ratio of banks indicating a higher vs. a lower willingness to lend)

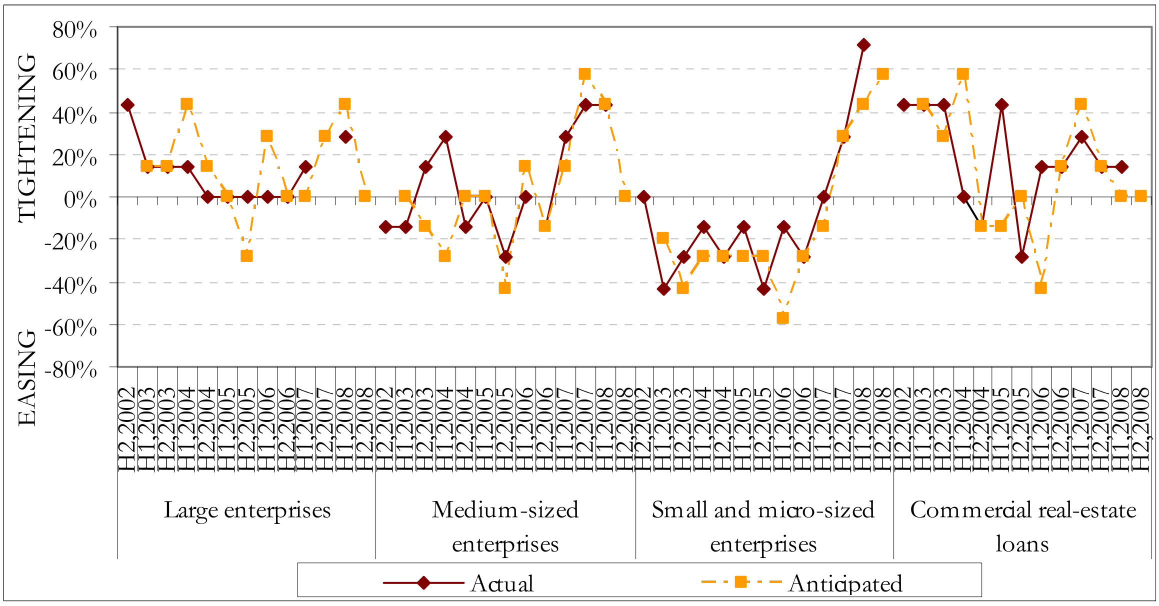


The above chart demonstrates that some kind of restructuring is visible in the change in willingness to lend. In respect of large enterprises, a moderate increase in willingness to lend is observed. At the same time, the declining trend observed earlier continued in the segments of small and micro-sized as well as medium-sized enterprises. As reported by the respondents, developments in willingness to lend are related to the changes in the perceived risk. However, the picture is not a uniform one, as in each segment there are one or two institutions which reported an increase in willingness. In the case of medium-sized enterprises and small and micro-sized enterprises, two banks reported a decrease in willingness to lend, however the institutions with decreasing willingness to lend were not the same in the two segments. One bank reported a strong decline in willingness to lend in the large enterprises segment.

A significant number of the banks interviewed tightened their lending standards as well as their price-related lending conditions in particular. This is also a sign of a continuation of the previously noted phenomenon that institutions are trying to compete in the development of systems which allow quick services and standardisation, rather than in price-related factors.

Therefore, the phenomenon seen in 2007 H2, when banks carried out an overall tightening of their standards, continued. No banks indicated easing in any of the standards which were examined. Interestingly, banks indicated tightening of standards in an inversely proportional manner to the size of the financed corporation, i.e. fewer banks tightened in the large enterprises segment than in the segment of small and micro-sized enterprises.

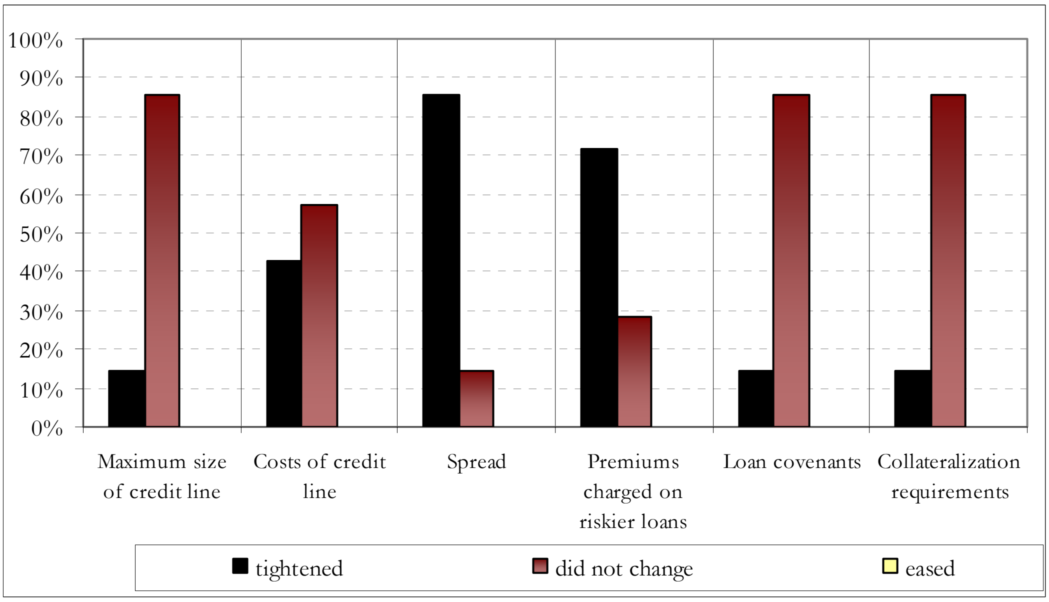
Chart 14: Creditworthiness standards by corporate category and in the field of commercial real estate loans
(ratio of those reporting tightening minus those reporting easing)



The experiences in 2008 H1 conformed with the expectations stated by the respondents in the January 2008 survey. At the same time, respondents envisage maintaining the level of creditworthiness standards in the second half of the year, except for the segment of small and micro-sized enterprises, in respect of which half of the respondents plan tightening.

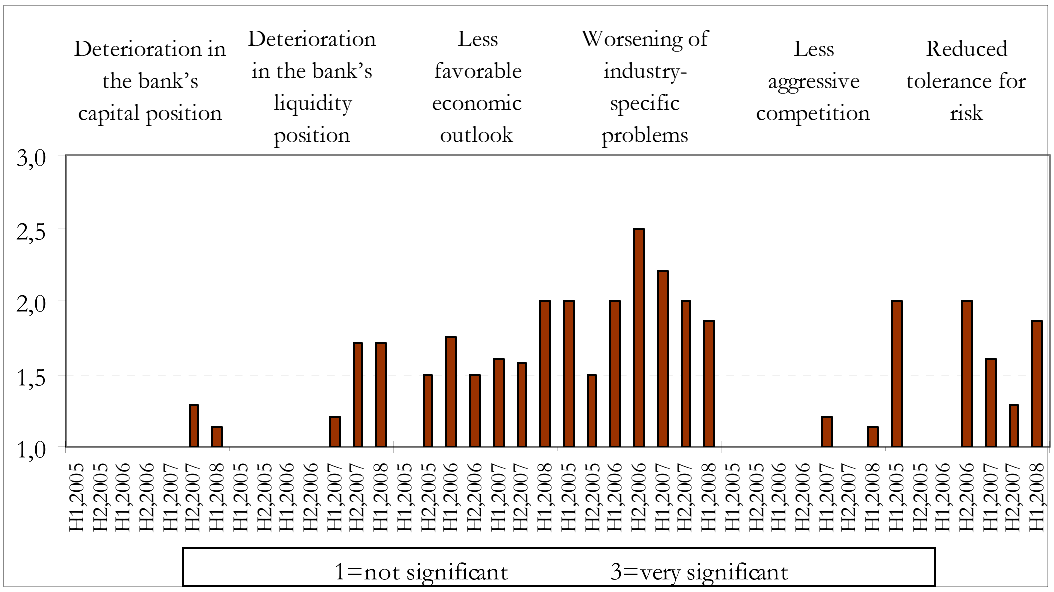
Similarly to the previous half year, some banks slightly tightened their ***lending conditions*** (Chart 32 – Chart 37) in 2008 H1. Based on banks' answers, tightening is mainly typical in the spread between the funding cost and the lending rate as well as in the premium for risky loans (Chart 15). Tightening affected all segments, but in contrast to the change in standards, the changes in lending conditions did not show a pattern which depended on the size of the enterprise. It is observed that while in the medium-sized and large enterprises segments banks intended to tighten price-related factors, in the small and micro-sized enterprises segment more institutions indicated a tightening of collateral criteria.

Chart 15: Lending conditions in the corporate business in 2008 H1 (ratio of banks specifying the given answer)



All institutions indicated tightening in their lending conditions. Over the pre-defined lending condition categories some institutions carried out tightening by strengthening its monitoring. An increase in the riskiness of certain industries and size categories (segment of small and medium-sized enterprises) and the unfavourable domestic economic prospects were highlighted as the most important underlying reasons for this tightening. In addition, similarly to the last survey, the deterioration in the liquidity position stemming from the subprime mortgage crisis continues to play an important role, driving banks to introduce tighter conditions. At five banks out of the responding seven, developments in portfolio quality led to a stronger focus on risk management aspects, which resulted in a decline in these banks' willingness to lend. One bank mentioned again that it introduced tightening measures as a result of applying the Basel II standards and the development of risk assessment methods.

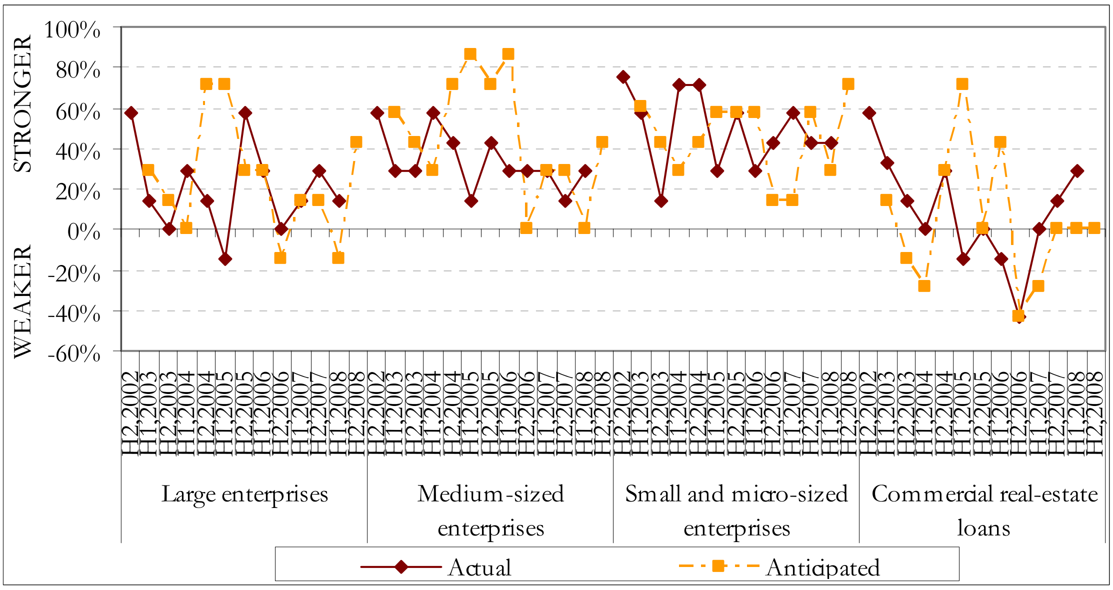
Chart 16: Reasons for tightening lending conditions in the corporate business as a whole



In 2008 H2, institutions intend to maintain the basically tighter standards, while banks envisage further tightening in the segment of small and medium-sized enterprises. Only one participant forecasted easing, and only in the medium-sized enterprises segment, as a result of strengthening its monitoring system and in the hopes that the prospects of non-financial corporations will be improved. Most banks plan tightening with regard to the spread between the lending rate and funding costs, and several banks also indicated strengthening of the risk premium, fees and contractual requirements, such as covenants, and market collapse clauses (Chart 32 – Chart 37).

Demand side

Chart 17: Loan demand by corporate size
(ratio of banks indicating an increase vs. banks indicating a decrease)



Demand in 2008 H1 proved to be stronger than anticipated by participants in January 2008. In our previous survey, the majority of banks expected nearly unchanged demand (excluding seasonal effects). Some institutions indicated a moderate decline in demand for loans by medium-sized and large enterprises, while two banks expected an increase in loans to small and micro-sized enterprises.

Overall, in our current survey, in all the three corporate categories, participants reported some increase in demand, which was perceived by banks mainly in the segment of small and micro-sized enterprises (by 4 respondents). In the large enterprises and medium-sized enterprise segments one and two institutions, respectively, perceived an increase in demand, while the others reported unchanged demand. On average, the observed growth rate of demand was higher than expected in each segment. However, in a forint- and foreign exchange-based breakdown a different pattern appeared: both in the medium-sized as well as small and micro-sized categories it was perceived that the increase in demand (in net terms, nearly 30% of respondents perceived stronger demand, i.e. two banks from the seven respondents) appeared in the demand for forint loans, while in net terms also 30% of participants perceived a decline in the demand for foreign currency loans. In the opinion of participants active in corporate lending, the increased demand for forint loans is attributable to the appreciation of the forint in 2008 Q2 and to the related exchange rate expectations. The so-called 'multicurrency' loans provide an opportunity of flexible conversion for customers. Some participants strongly felt the exchange of the type of currency performed in order to realise the profit between the forint amount of the loan taken at a weaker exchange rate and the current forint amount. At the same time, respondents indicated that these products are used in an active manner by more sophisticated, major customers, while smaller customers usually use single-currency products. Conversions are typically performed on the basis of indications by customers, although several banks offer complementary derivative products, which allow automatic conversion.

With regard to the changes in the structure of demand for loans, the institutions experiencing stronger demand for loans explained the trends with increases in customers' inventory financing needs, the financing requirements of receivables and customers leaving other banks.

Looking forward to the next half year, nearly one half of respondents (3 institutions) expect an increase in demand compared to the previous half year. In the second half of the year, the ratio of those participants that expect an increase in demand for forint loans (3 institutions) is higher than the number of those who expect an increase in demand for foreign currency loans (2 institutions expect somewhat stronger demand, while one expects somewhat weaker demand).

Commercial real estate loans

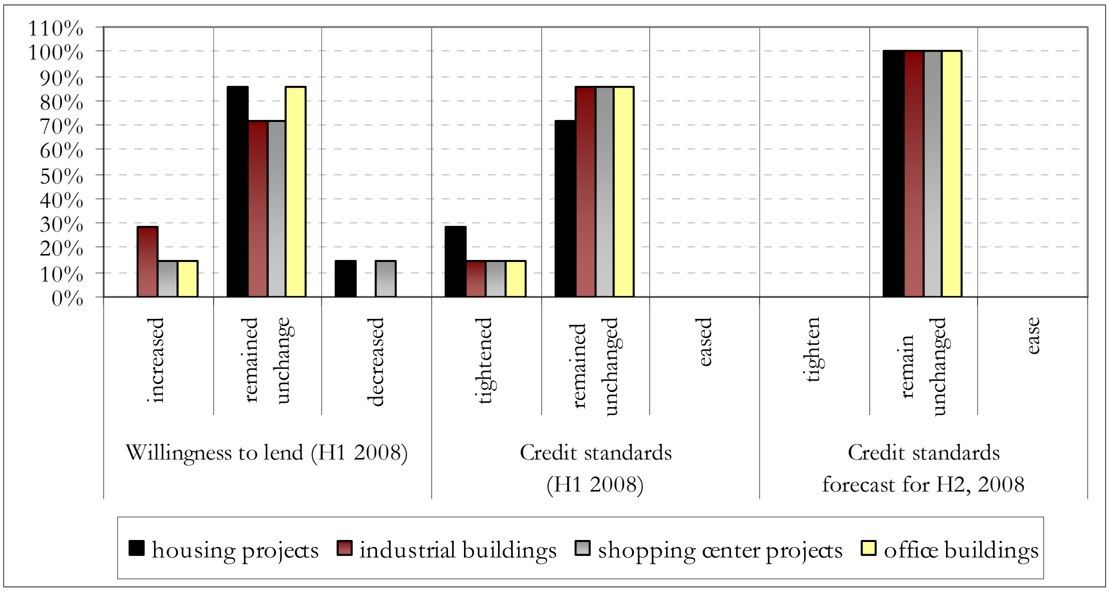
(Questions 14–19 of Annex 5)

From 2006 H2 on, the questions on commercial real estate loans contain a breakdown according to the following real estate categories: housing projects, office, logistics centre and shopping centre projects. As longer time series are not available on these real estate categories, and smaller shifts may also look more significant than necessary in short time series, we present only the last year's trends in these market segments.

Supply side

In terms of commercial real estate loans, in 2008 H1 no clear change could be identified in the developments in banks' ***willingness to lend***. Overall, answers showed a nearly unchanged picture: one of the seven respondents indicated an increase in willingness, while the others reported unchanged willingness. All in all, similarly to the previous half year, a slightly declining willingness was observed with regard to lending for housing projects, while an overall unchanged increase in willingness was experienced in lending for shopping centre projects. With respect to logistics centres and office buildings two and one institutions, respectively, indicated an increase in their willingness to lend, with the other respondents' willingness to lend remaining unchanged.

Chart 18: Willingness to lend and creditworthiness standards in commercial real estate loans (ratio of the banks giving the relevant answer)



Similarly to the previous half year, participants mainly see increased risks in housing project financing, which was coupled with tightening of lending standards at two banks. Even those banks which did not tighten their standards in this market segment continue to concentrate on high quality projects.

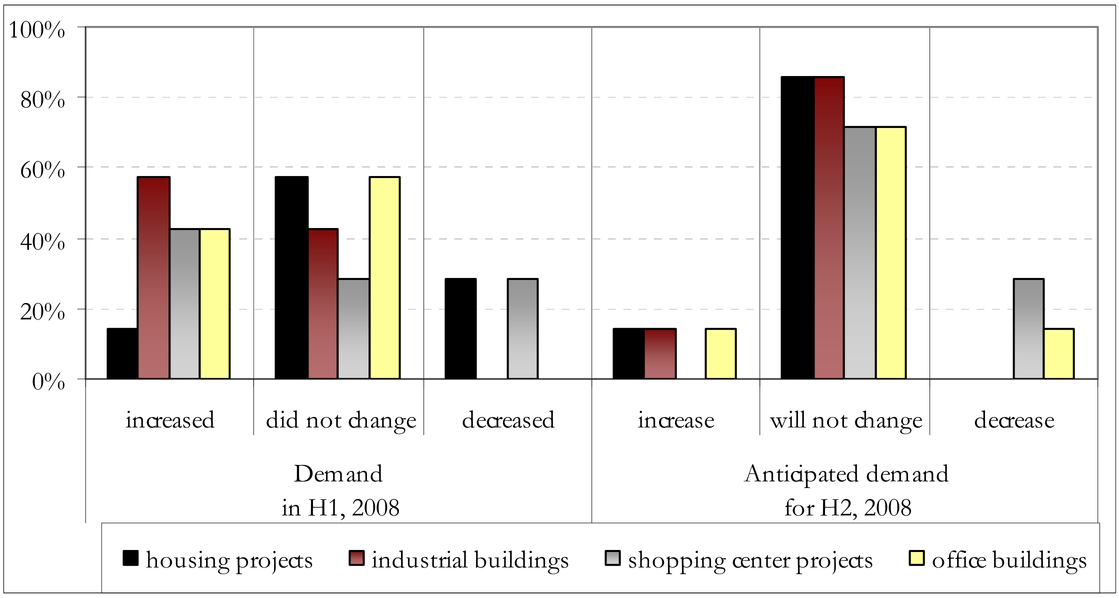
The participating banks (3 banks altogether) which indicated tightening in one of the segments mainly indicated increasing industry-specific problems and waning tolerance to risk as the underlying reasons for tightening standards. None of the respondents are planning any considerable changes in their lending standards for commercial real estate loans in the coming half year.

Demand side

Overall, compared to the previous half year, banks indicated a slight increase in demand in the market of commercial real estate loans. However, answers were somewhat spread according to individual participants and real estate categories (Chart 19). Similarly to the previous half year, for housing projects, the responding senior loan officers experienced a decline in demand for loans.

For logistics centres and office buildings, a strengthening in demand can be perceived in net terms as well: nearly half of the respondents felt there was an increase in demand in these two segments (four and three institutions, respectively). Opinions differed on shopping centres, as three institutions experienced an increase in demand, while two institutions perceived a decline in demand due to the presumed saturated nature of the shopping centre market. Overall, respondents expect unchanged demand for the next half year. One participant expects an upswing in demand with regard to housing projects and logistics centres each, while in case of office projects one participant forecasted an increase in demand and another a decline in demand. With respect to shopping centres, the forecast points to modestly declining demand: five institutions expect unchanged demand, while two institutions expect a decline in demand.

Chart 19: Demand for loans in the various market segments of commercial real estate lending (ratio of banks specifying the given answer)



Change in credit risk assessment of the various industrial sectors

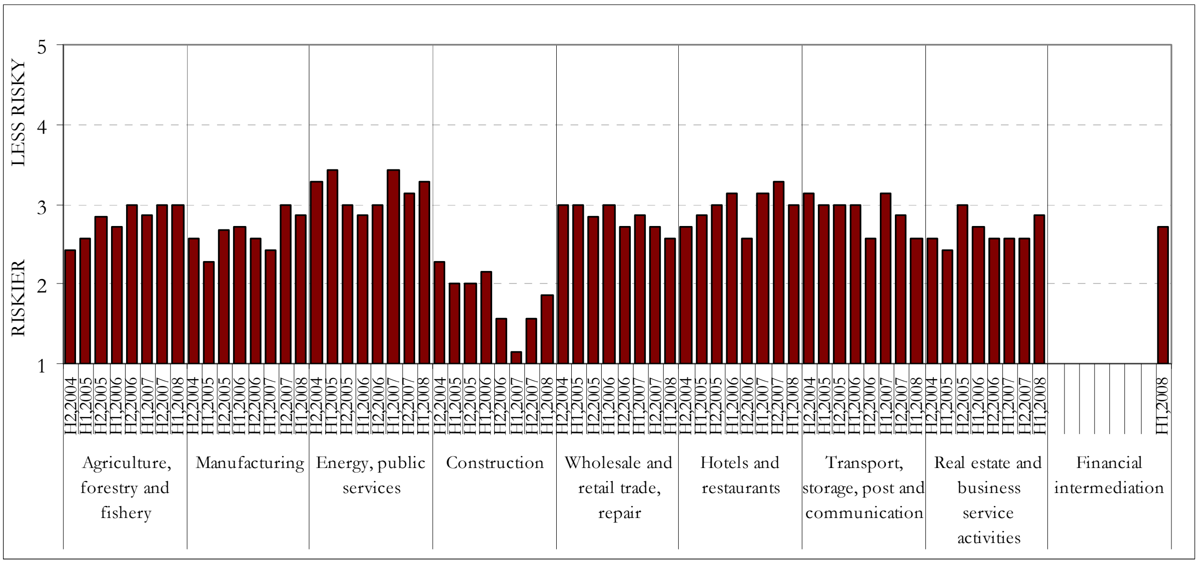
(Question 24 of Annex 5)

In the opinion of the banks interviewed, in 2008 H1 the risk assessment of the following sectors changed considerably:[6]

- As a continuation of the multi-annual trend, in 2008 H1 survey participants clearly indicated a significant increase in the riskiness of the construction industry. Only one respondent indicated that riskiness had not increased. The increase in riskiness is related to a decline in orders and the increase in the resulting gridlock in the past half year.
- Overall, survey participants reported a deterioration in the risk assessment of the branches 'trade and repair' as well as 'transport and storage'.
- 'Financial intermediation' and 'real estate and business activities', which had been in the same category, were separated in this round of the survey. While the assessment of real estate and business activities remained unchanged, two participants indicated an increase in risks with regard to financial intermediation. Similarly to construction, earlier trends continued in this sector as well.
- Overall, survey participants considered risks in manufacturing nearly unchanged, reporting at the same time a deterioration in risk assessment in the food, machine and light industry segments (textile industry, printing industry and other sub-sectors of light industry).
- Recently, based on the answers, an improvement in risk assessment was perceived in the 'hotels and restaurants' category: five banks' judgements remained unchanged, while two banks indicated that lending to this sector had become somewhat safer due to an upswing in domestic tourism.
- With regard to the electricity generation industry, three institutions indicated that it had become safer, and only one institution reported it becoming riskier.

Chart 20: Risk assessment of sectors[7]

(1 = became significantly riskier, 2 = became somewhat riskier, 3 = remained almost unchanged, 4 = became somewhat safer, 5 = became significantly safer)



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[6] We highlighted those sectors where at least two banks indicated changes.

[7] From H1 2008, financial intermediation became separated in the survey from the real estate and business service activities.

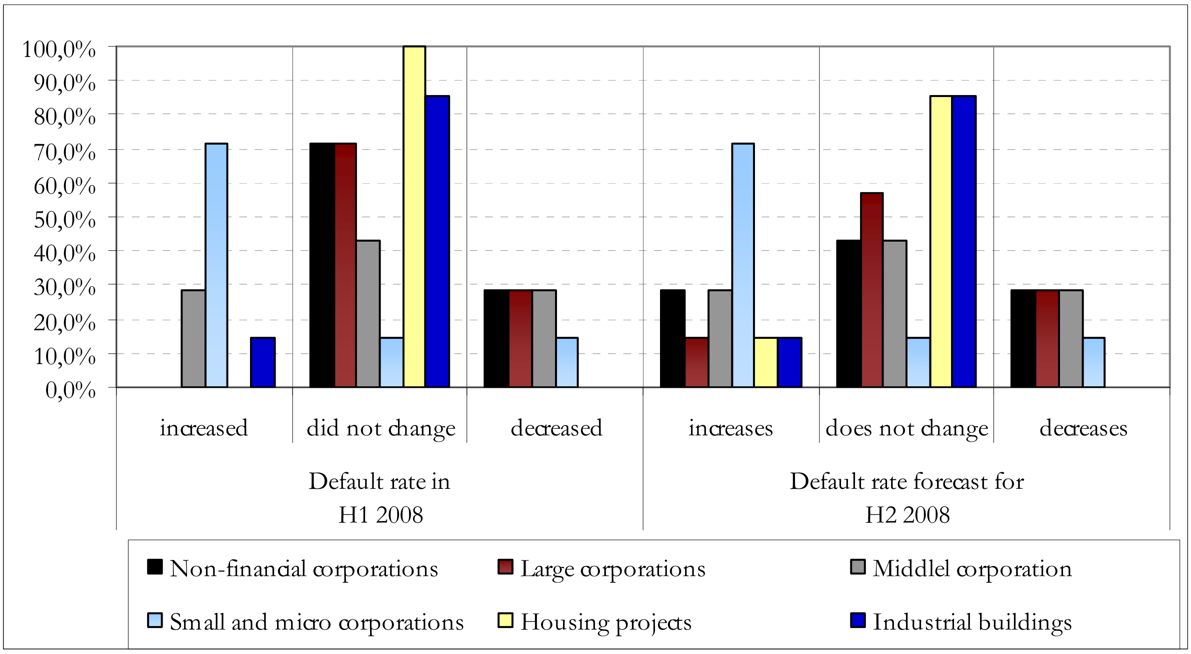
Developments in the riskiness of the corporate loan portfolio

(Questions 10–13 and 20–23 of Annex 5)

For the second time in the survey, we endeavoured to ask more detailed questions regarding changes in riskiness. Similarly to what was mentioned in the household segment, we asked about the Basel risk parameters, i.e. the default rate and the loss given default. We emphasise that we inquired about risk perception and trends based on available data, rather than about validated risk parameters, as most institutions could not implement the methods based on more advanced internal ratings (IRB). The questions focus on the changes, thus information is received only with regard to risk perception. A complete picture would be provided if risk levels were also available, which, in parallel with banks' IRB preparation, are presumed to become more widely available later.

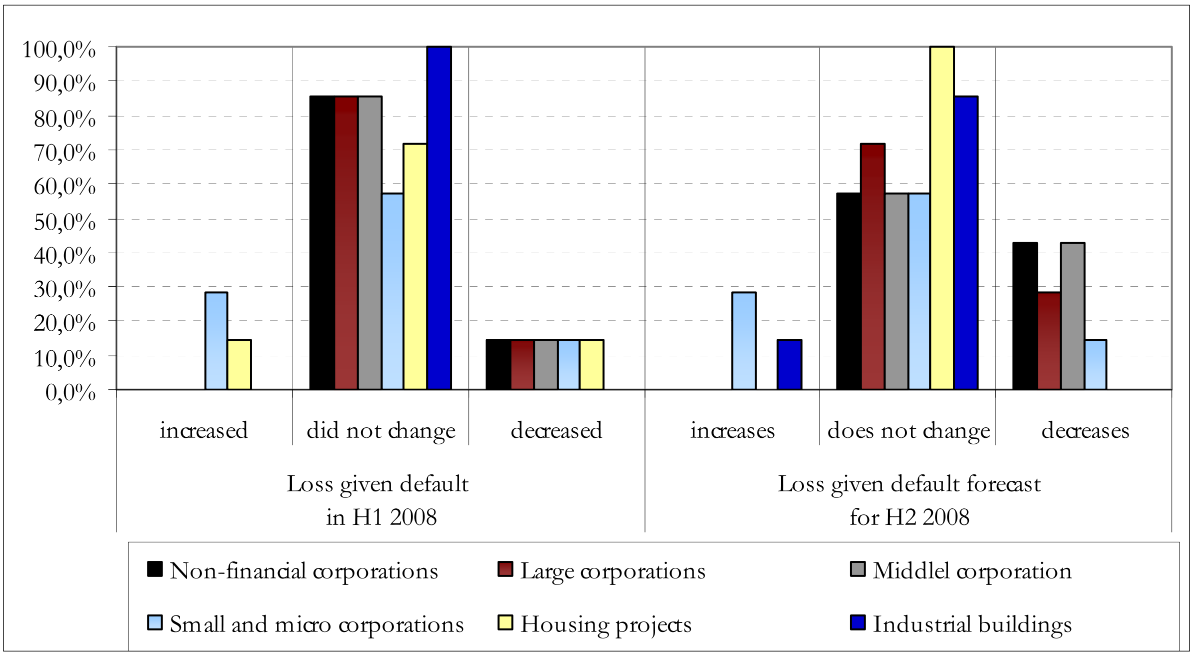
Based on the answers, a slight improvement in the default rate was seen in standard corporate financing in 2008 H1. However, the majority of respondents perceived deterioration in the segment of small and micro-sized enterprises. At the same time, nearly one third of the banks perceived a decline in the default rate for large enterprises. In the next half year, respondents predicted a nearly unchanged default rate in net terms, while more than two thirds of respondents forecasted an increase in default rate in the segment of small and micro-sized enterprises. With regard to commercial real estate loans, in the previous half year and for the next half year as well, a nearly unchanged picture is painted: one institution in each half year indicated an increase in risks in this parameter (Chart 21).

Chart 21: Default rate of corporate loans



Two banks indicated deterioration in the loss given default (LGD) in the case of small and micro-sized enterprises, while one respondent registered improvement. Overall, perception regarding this parameter was nearly unchanged in the other segments. With respect to the next half year, two institutions forecasted further deterioration in the LGD parameter in the case of small and micro-sized enterprises. However, in other corporate segments, presumably trusting the success of monitoring efforts, they expect a decline in the loss given default. With regard to commercial real estate loans, market participants expect a nearly unchanged situation: in the case of housing projects, none of the respondents expects any change in loss given default, while in the case of other commercial projects only one participant indicated a change, which predicting an increase in loss given default (Chart 22).

Chart 22: Loss given default of corporate loans



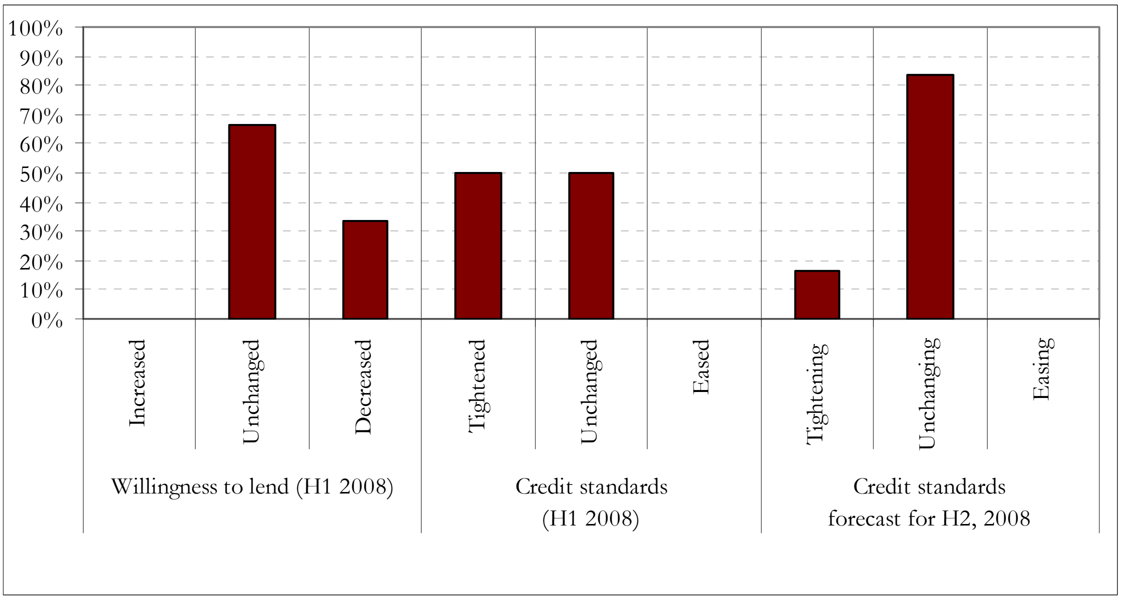
3. Market of loans to municipalities

(Annex 6)

The strong growth seen in municipal bond holdings in 2007 H2 continued in 2008 H1 as well, and thus the amount outstanding vis-à-vis municipalities increased to a total of HUF 533 billion. Accordingly, during the one and a half years since January 2007 an approximately 80% increase has been observed in nominal terms. Due in part to this fast growth, we have devoted a separate section in the survey to trends in lending to municipalities, starting from the previous half year. The continuation of the increase in exposure to municipalities in the previous half year confirmed that it is worth dealing with this subject separately.[8] As the interviews with municipalities senior loan officers revealed that there are no significant differences between bank-side standards of loan-based and bond-based funding, the popularity of bonds is attributable to the opportunity of evading public procurement rules. Therefore, as opposed to the previous round of the survey, now we inquired about the loans and municipal bonds together.

Looking at the supply side, regarding the municipal sector, responding institutions indicated an unchanged average ***willingness to lend*** compared to 2007 H2. One institution indicated that its willingness had declined somewhat. The institutions (three of the responding six) carried out some tightening of **standards** in the past half year, in accordance with the forecasts of January 2008. Tightening in standards entailed an average tightening in the specified **lending conditions**. Responding institutions indicated the strongest tightening in price-related factors, i.e. in the fee(s) charged for granting the credit facility, in the spread of the cost of fund and in the premium of riskier loans. No respondent reported any easing. One institution indicated tightening in parameters other than the aforementioned ones: this institution requires a guarantee issued by Garantiqa Credit Guarantee Plc. as a compulsory condition for financing. The institutions which reported tightening mainly indicated deterioration in the liquidity position as an underlying reason (Chart 23).

Chart 23: Willingness to lend and creditworthiness standards in municipal financing (ratio of the banks specifying the given answer)



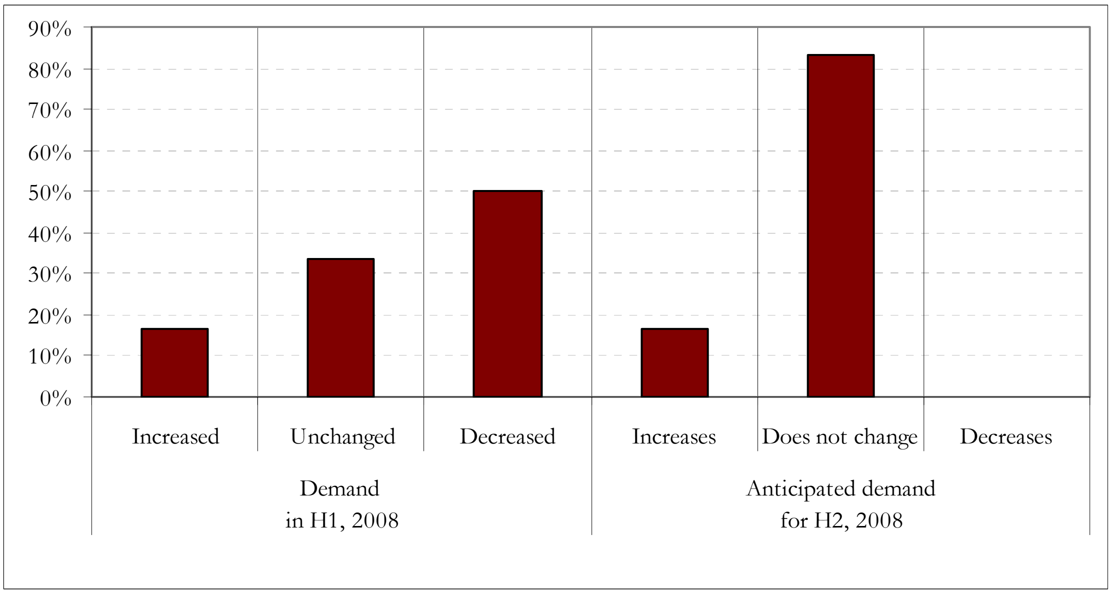
For the next half year, one of the surveyed banks indicated that it intends to somewhat tighten its creditworthiness standards and (mainly price-related) lending conditions. Along with price-related

[8] The following article to be published in the MNB Bulletin in September 2008 will provide a more detailed picture of the financing of the municipalities sector by banks: Dániel Homolya – Gábor Szigel [2008]: Lending to municipalities: risks and banks' behaviour (*Önkormányzati hitelezés: kockázatok és banki viselkedés*), forthcoming.

factors, one institution each indicated tightening in collateralisation requirements, covenant requirements and the amount of the credit limit.

In the last half year, banks experienced some decline in demand for loans to municipalities; three institutions perceived a decline in demand, while one perceived an increase in demand. The banks which perceived a decline in demand mainly indicated the fading away of the municipal 'bond issue boom'. At the same time, the still relatively strong increase in exposure experienced in 2008 H1 is related to the fact that transactions launched in 2007 Q4 were carried forward to 2008 Q1. Participants indicated a decline in propensity to invest as one of the other factors. At the same time, the only institution which perceived an increase in demand indicated grants from the European Union, an increase in current financing requirement, a decline in own funds and a presumed future increase in propensity to invest as important factors. Overall, responding banks expect somewhat unchanged demand for the next half year. Only one institution indicated a change; in their opinion, demand will somewhat increase. (Chart 24) Similarly to the previous half year, the institutions did not perceive any significant changes in the municipal **loan portfolio quality** in 2008 H1.

Chart 24: Demand for loans in municipal financing (ratio of banks specifying the given answer)



4. Current issues and trends

As in the earlier surveys, we used open questions to ask the participating banking specialists about current developments, such as demand motives underlying the increase in lending to households, the well-foundedness of households' borrowing behaviour, the comparison of the increase in housing and general purpose mortgage loans, the driving force of non-financial corporations' growth, the effects of market turbulence as well as trends in sales (selling through agents and refinancing of loans). The following is a summary of the answers received from the heads of various business branches of the thirteen banks surveyed, highlighting the main trends. In addition to the usual current questions, we asked the participating senior loan officers about the practices in the survey (for example in connection with the methodology, questions and the structure of the publication). We will use the relevant answers in the development of the Survey on Lending practices.

Demand reasons underlying the steadily high growth rate of loans to households

Responding senior loan officers stated that, on the one hand, they continued to consider consumption smoothing reasons important, i.e. with the decline in real income and a moderate level of savings, the consumption level which had become usual can continue to be financed from loans in the future as well. On the other hand, in addition to consumption smoothing, some customers intend to lift their usual consumption level even higher, to an even better quality level, financed through borrowing. In any case, the strong borrowing behaviour shows that customers are basically optimistic. At the same time, the senior loan officer at one of the banks emphasised that saving for unexpected situations often appears among the intentions to draw general purpose loans. In terms of housing loans, in certain age groups it is natural and stems from their life situation that they move to larger homes, simultaneously generating demand for loan. All these factors contributed to the fact that the increase in loans to households continued to remain at a high level in 2008 H1 as well.

The well-foundedness of households' borrowing behaviour in terms of their income and financial situation

With regard to the well-foundedness of borrowing decisions, senior loan officers painted a rather negative picture. There is an increasingly perceptible segment, the budget of which is becoming stressed, i.e. these households undertake too much. An institution indicated that with regard to new loan applications, refusals because of being registered in the Central Credit Information System have increased markedly recently. In addition, several senior loan officers emphasised that the real estate holdings owned by Hungarian households still allows an extension of households' credits, and due to the relatively high ratio of grey incomes the indebtedness situation is not as bad as it seems from official data.

Reasons for the higher-than-expected increase in housing loans experienced in 2008 Q1

Institutions reported different experiences. Not all of them perceived a higher increase in housing loans than in general purpose mortgage loans in the first quarter. The institutions which still experienced these types of trends listed several factors as an explanation: the already mentioned autonomous demand factors, demand brought forward from 2007 Q4, the decline in demand for loans with a business-related intention but appearing among general purpose mortgage loans and the increase in the LTV ratio of housing loans. Of course, all these factors may explain partial effects.

Reasons for the recent high level of borrowing by non-financial corporations

In the respondents' opinion, current assets financing requirements is underlying the high growth rate of corporate borrowing, on the one hand, while on the other hand, another relevant factor is that with the relatively low domestic level of margins it becomes possible that within a group of companies other companies can be financed through domestic companies. Some participants emphasised that several commercial real estate projects implemented abroad are financed through companies registered in Hungary or through the subsidiaries of the latter, thus the well-established business and financing model can be used in high-growth markets. Such quasi 'cross-border' financing activity may be limited by the division of tasks and responsibilities within the banking group. With respect to the increase in on-balance sheet exposures, there is a possibility that the increase may be attributable to the drawing of credit facilities awarded earlier, before the market turbulences. Some institutions clearly perceived this trend, while others did not. At any rate, respondents indicated almost clearly that there had been no material increase in demand for investment loans in the past half year.

Effects of the recent market turbulence

Respondents unanimously indicated that the increase in the risks and costs of obtaining funds continued in 2008 H1 as well, although it affected the responding banks to varying degrees, depending on the funding received from the parent bank. Some of the respondents did not perceive an increase in funding costs in 2007 H2, but they did in 2008 H1. Some banks indicated that with respect to renewals and new applications they renegotiated earlier loan charges with their customers. However, the magnitude of passing the costs on is clearly influenced by the customer's bargaining position and the strength of competition. Contrary to earlier expectations, passing on started more strongly in the household segment, but, due to the fierce competition, responding institutions could not do it completely; thus, banks reported an express narrowing of the margin. Accommodation is indicated by the answers to the standard questions; several institutions intend to increase the spreads over funding costs in the next half year, with funding cost levels remaining at the current level.

Trends in housing loan sales: selling through agents and loan refinancing

According to the institutions participating in the survey, the role of agents in the household segment continued to grow in the past half year as well. Most new loans are sold through this channel. Due to the typical financial incentive of agents, i.e. the high one-off initial fees, they are ready to undertake higher risks. Due to agents' strong bargaining position, over the short term, banks do not consider the shift to risk-reducing incentive solutions (e.g. initial fee with maintenance commission, deduction of commission, commission system depending on the riskiness of the portfolio) feasible. Some institutions consider a strengthening of self-regulation necessary, while others would prefer stronger intervention by regulatory authorities. In any case, the introduction of a risk-based incentive system may be enhanced by the fact that the majority of institutions are better and better able to measure the efficiency of sales channels and the riskiness of the portfolio they generate, although several institutions indicated that further development is necessary. Respondents consider exclusive agents (who are related to one given bank), i.e. so-called mobile bankers, more stable than independent agents who work for more than one bank. Overall, the weight of this channel has slightly increased recently; at the same time, however, exclusive agents continue to be of little importance at several institutions.

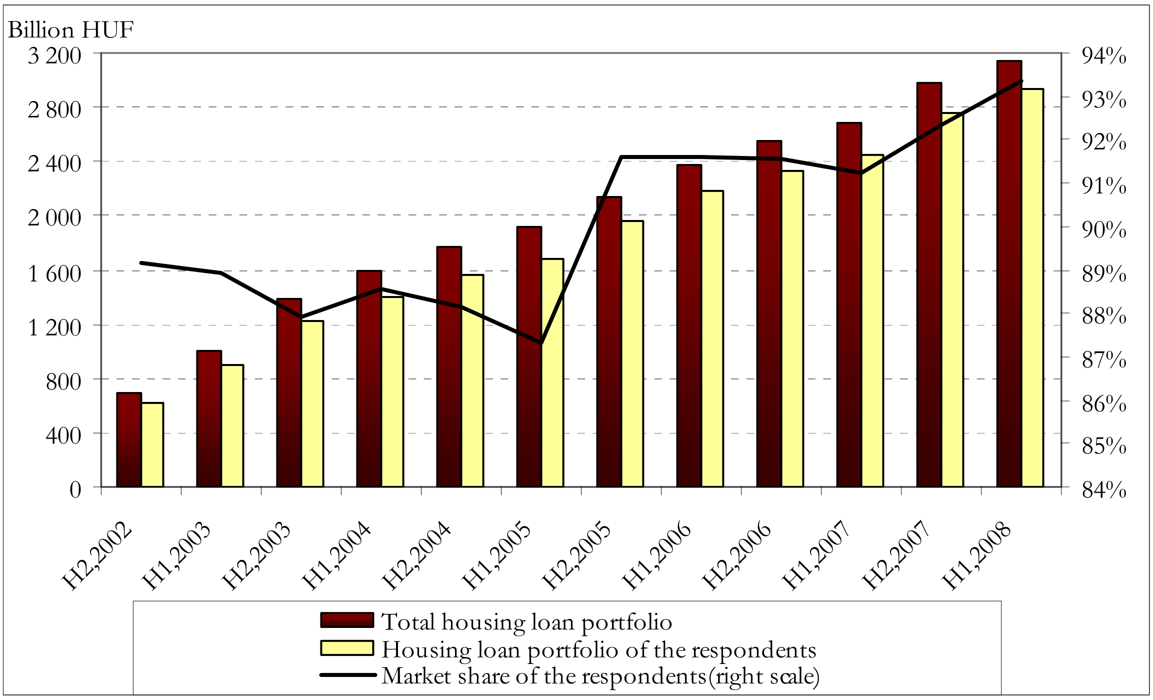
Within new loans, the proportion of loans for replacing debts at other banks continued to increase in the last half year as well. As participants said, banks' self-regulatory initiative is not fully developed yet, and effects cannot really be perceived at this stage. Agents play an important role in the loan refinancing trends and in moving a customer several times. Some respondents called the attention to the fact that customers often find themselves in a less favourable situation following loan replacement, as their burdens become even heavier.

In addition to the aforementioned current issues, the effects of the appreciation of the forint experienced in 2008 Q2 also appeared. With regard to corporate customers, respondents clearly indicated that in the case of 'multicurrency' types of transactions converting the loans to forint was seen. In the household segment, a rather important factor was an increase in prepayments with an intention to realise exchange rate gains, but, overall, households' behaviour seemed to be less sensitive to exchange rate changes than that of corporations.

ANNEX 1: CHARTS ON THE LOAN PORTFOLIO AND ANSWERS TO THE QUESTIONNAIRE

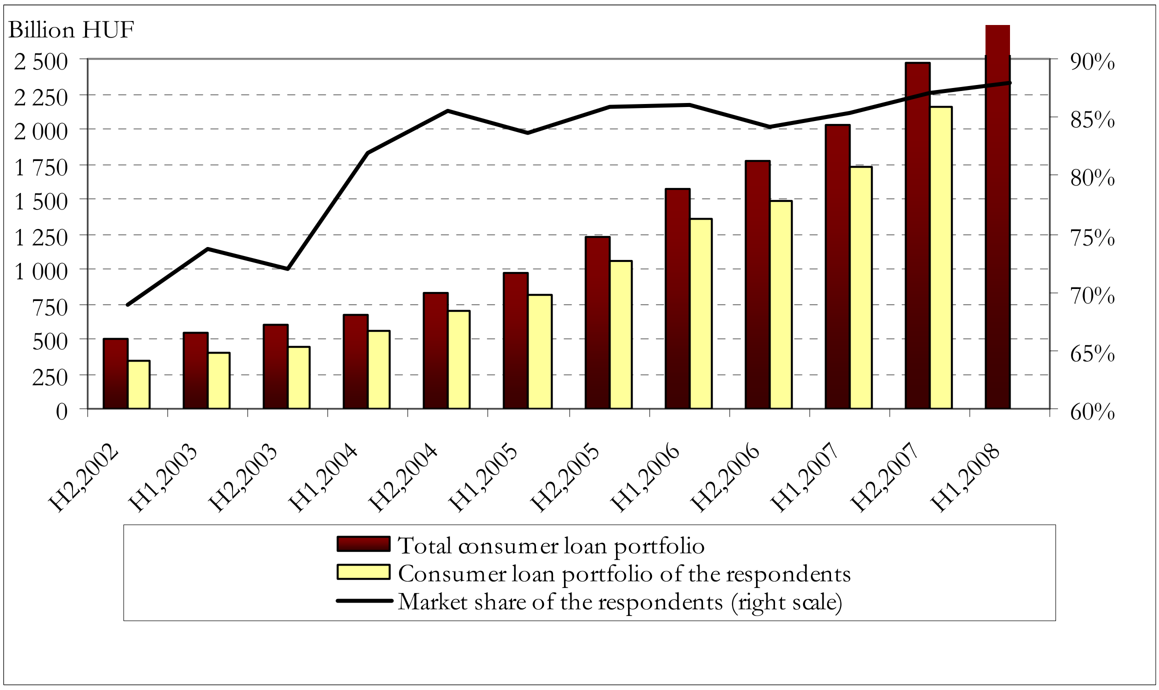
Household segment

Chart 25: Housing loans and market share of banks completing the questionnaire



Note: During the half years under review, the number and scope of banks surveyed changed (e.g. as a result of mergers and the involvement of a new bank). On the last occasion there were nine participating banks.

Chart 26: Consumer loans and the market share of banks completing the questionnaire



Note: During the half years under review the number of banks interviewed changed. On the last occasion, the number of institutions providing an expert assessment was thirteen. The chart only shows the share of banks interviewed within the banking portfolio; the share of financial enterprises is not shown.

Chart 27: Lending conditions in the market of consumer loans (ratio of those reporting tightening minus those reporting easing)

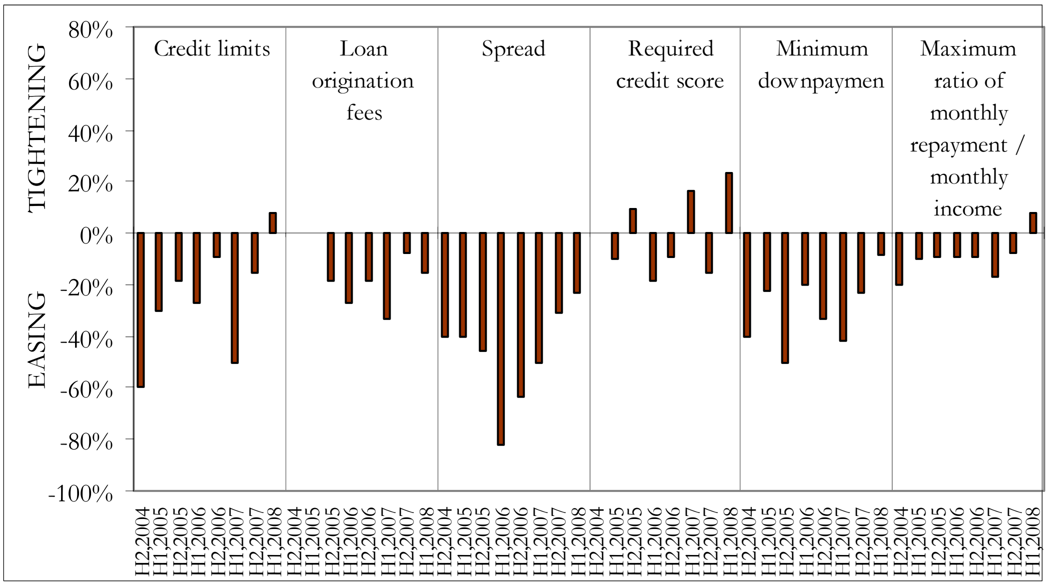


Chart 28: Reasons for easing of creditworthiness standards and lending conditions for consumer loans

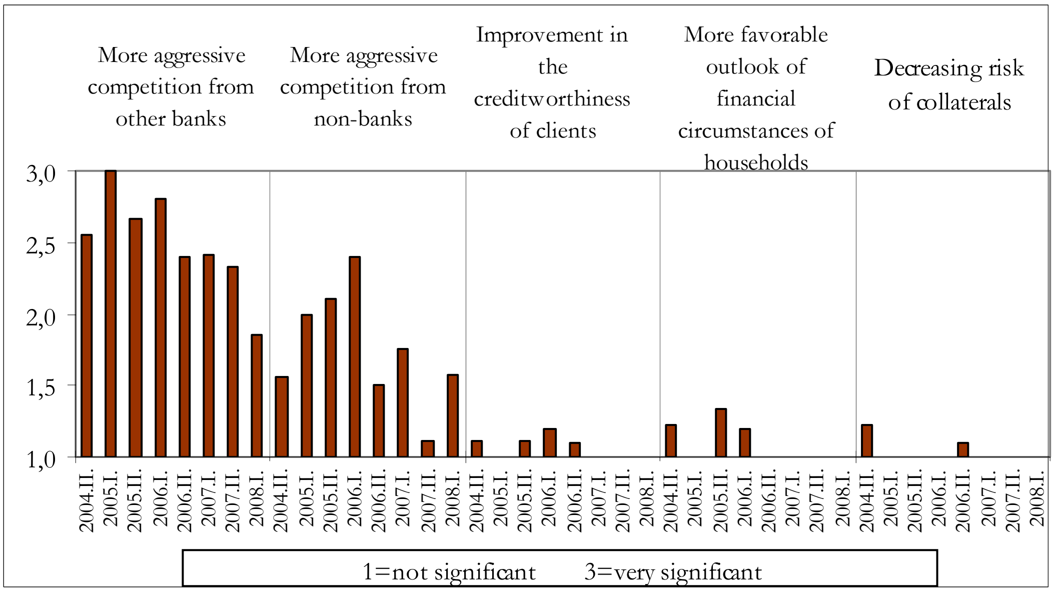
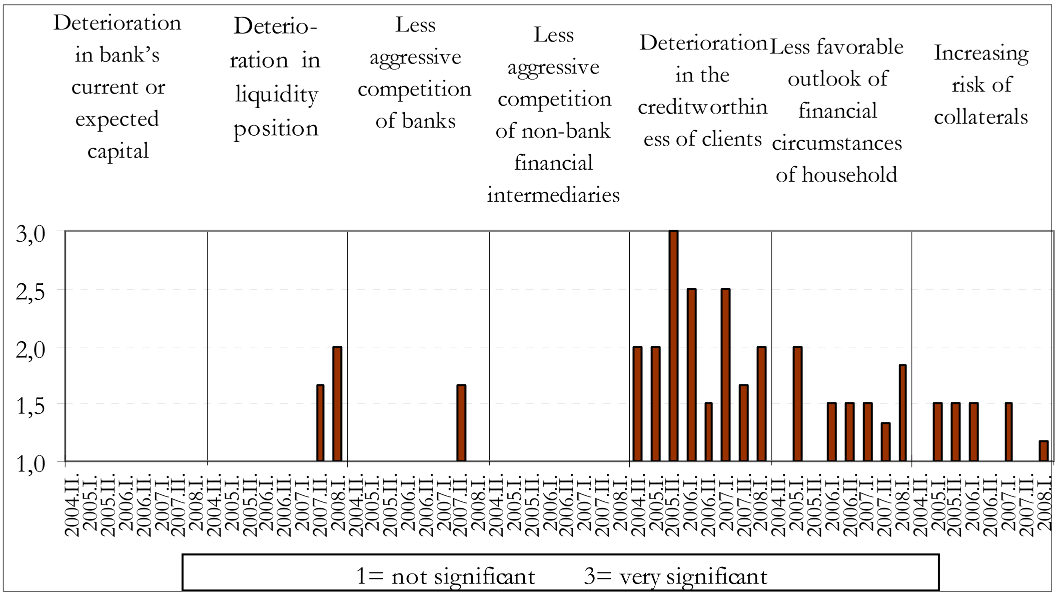


Chart 29: Reasons for tightening of creditworthiness standards and lending conditions for consumer loans



Corporate segment

Chart 30: Shares of responding banks in the total corporate lending portfolio

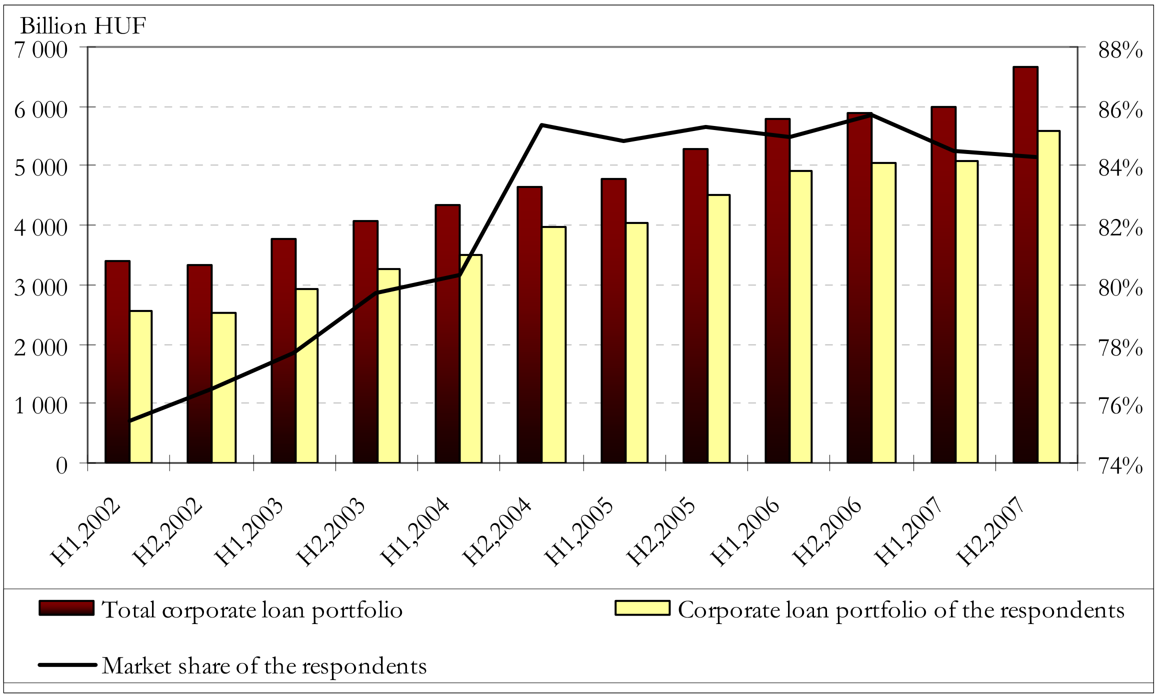


Chart 31: Shares of responding banks in the total commercial real estate loan portfolio

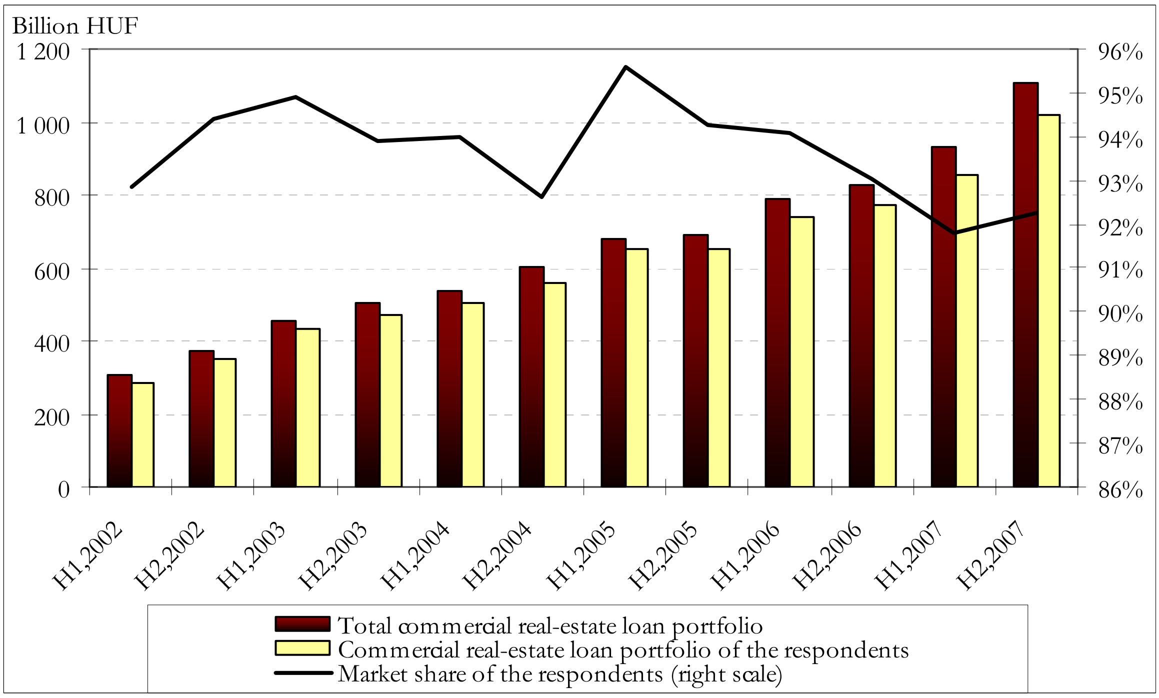


Chart 32: Maximum size of loans/credit lines by corporate category (ratio of those reporting tightening minus those reporting easing)

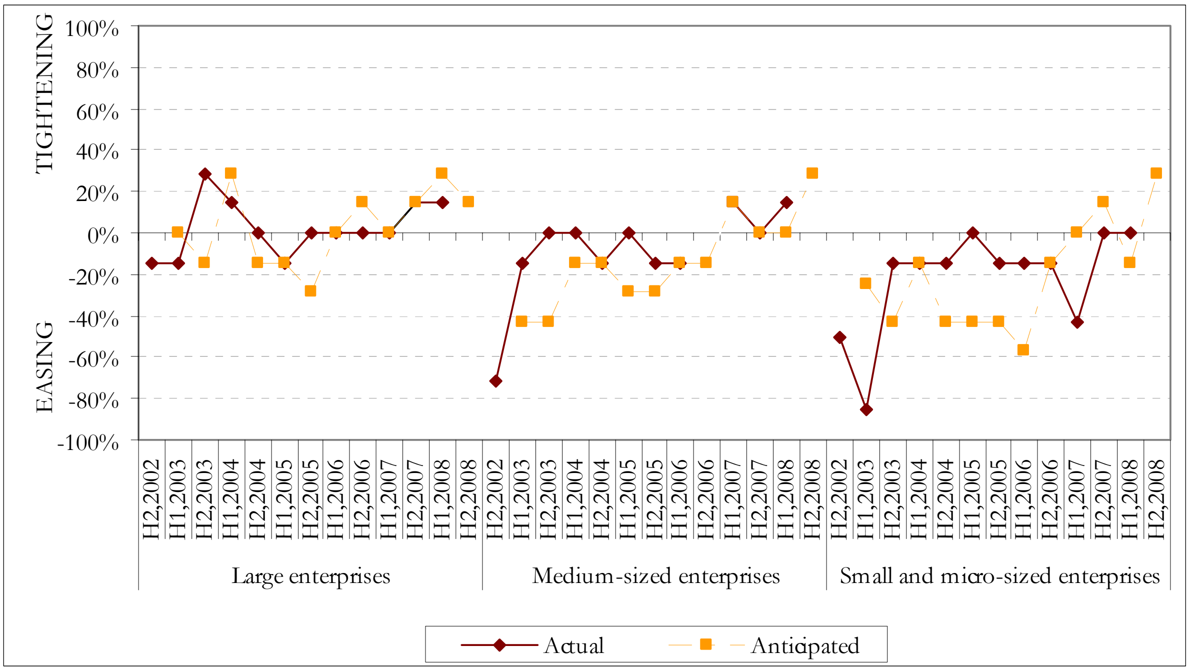


Chart 33: Fee(s) charged for extending the loans/credit lines by corporate category (ratio of those reporting tightening minus those reporting easing)

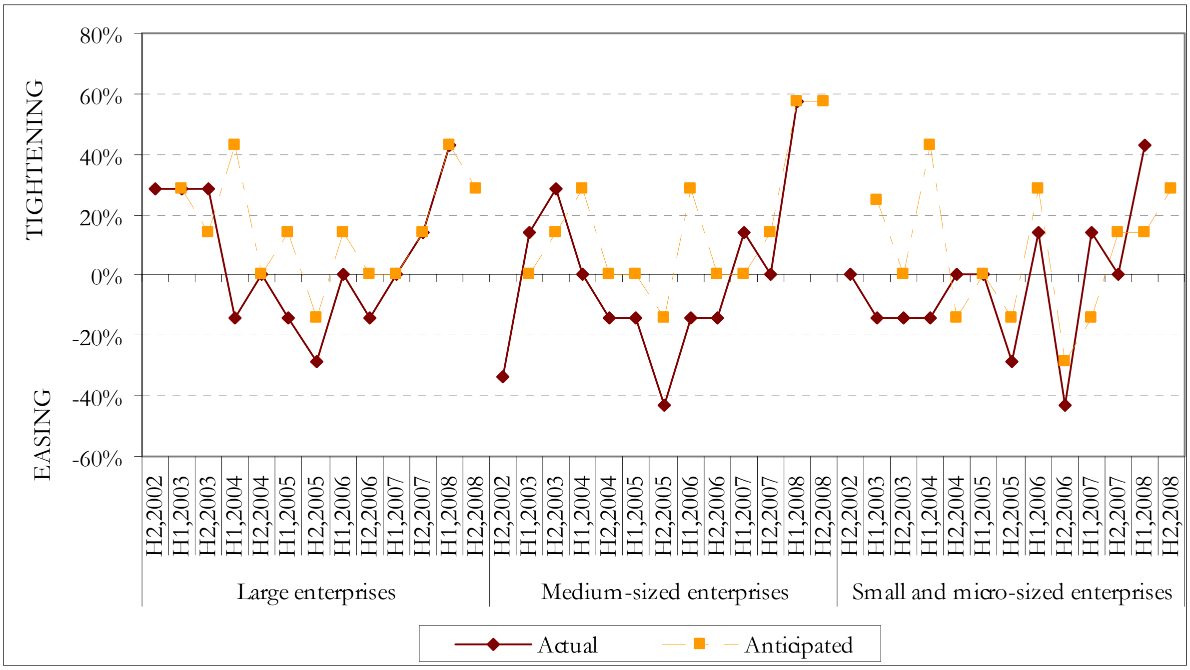


Chart 34: Spread between lending rates and costs of funds in a breakdown by corporate category (ratio of those reporting tightening minus those reporting easing)

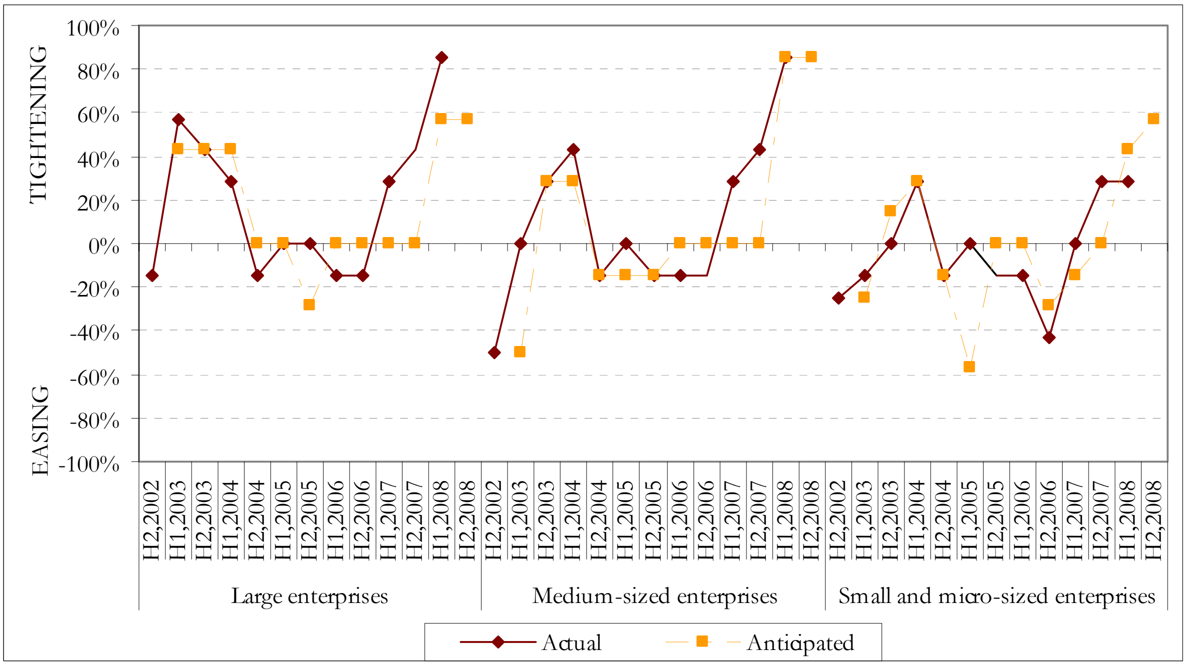


Chart 35: Premium on higher-risk loans in a breakdown by corporate sector (ratio of those reporting tightening minus those reporting easing)

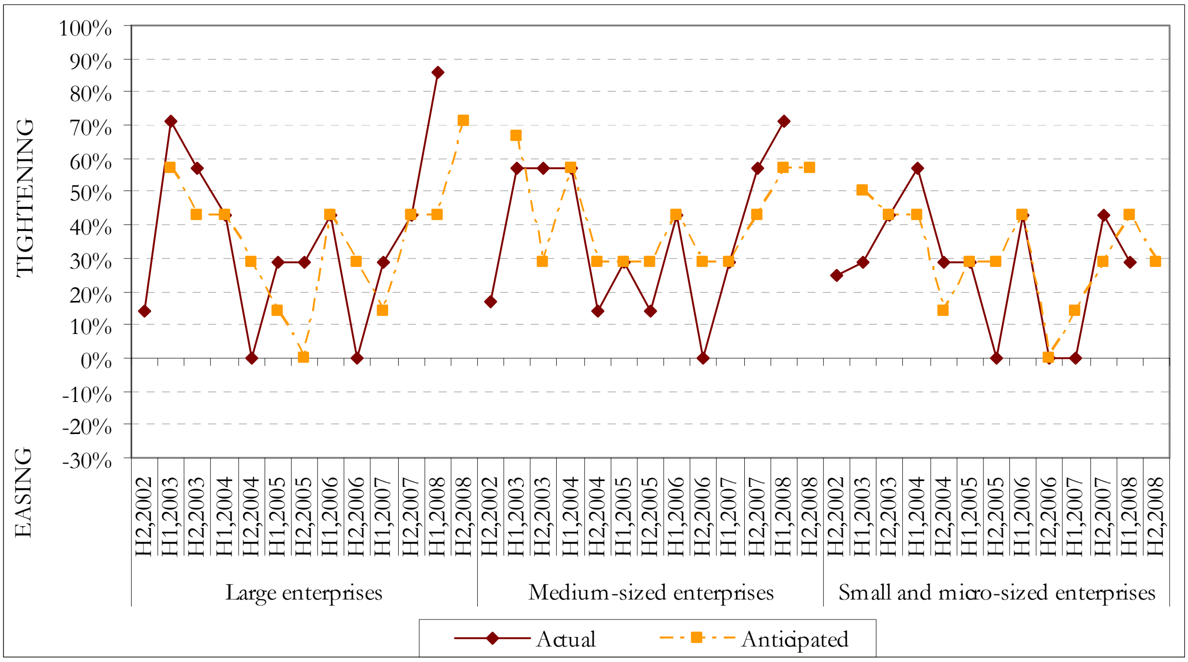


Chart 36: Collateral requirements in a breakdown by corporate sector (ratio of those reporting tightening minus those reporting easing)

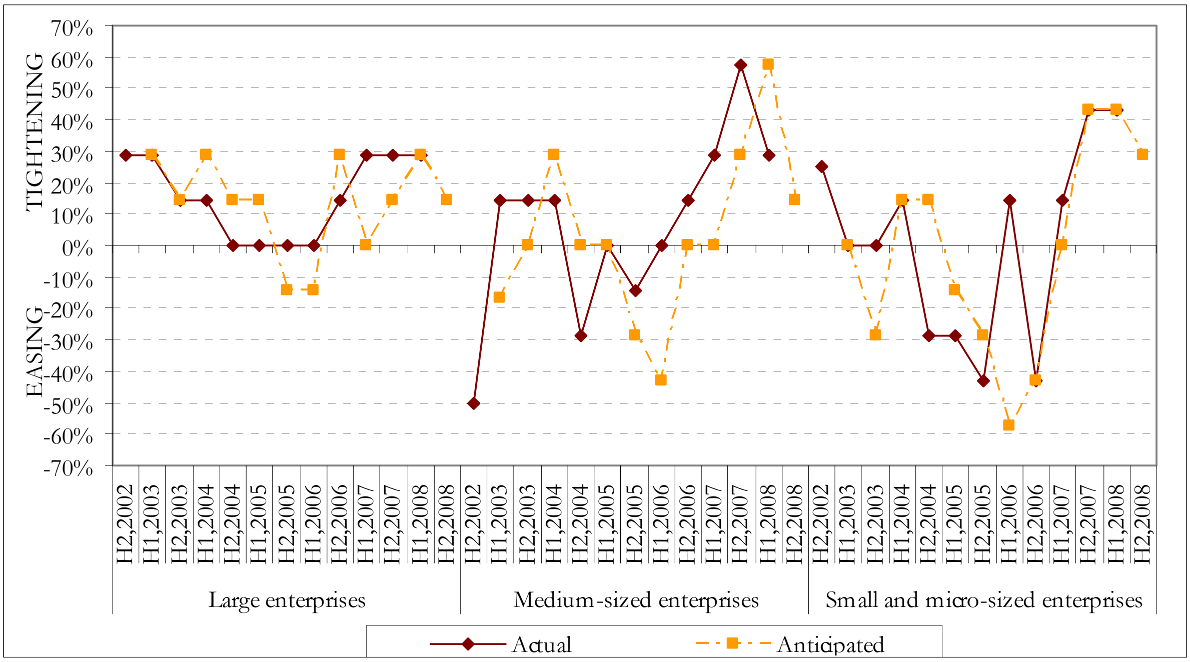
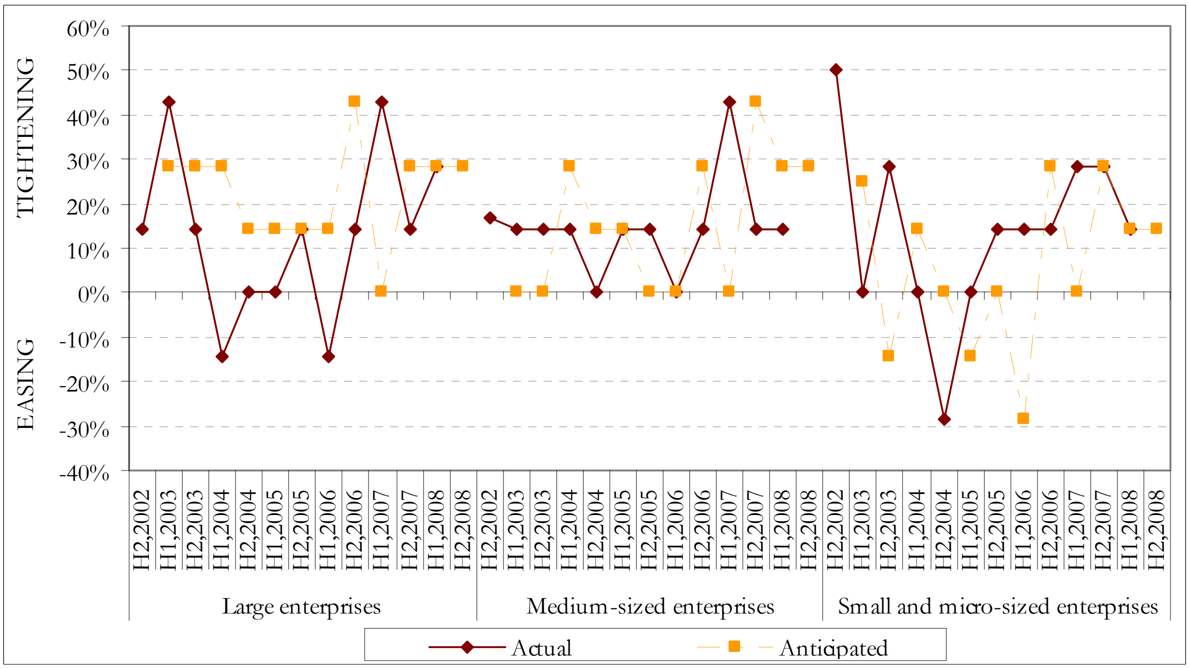
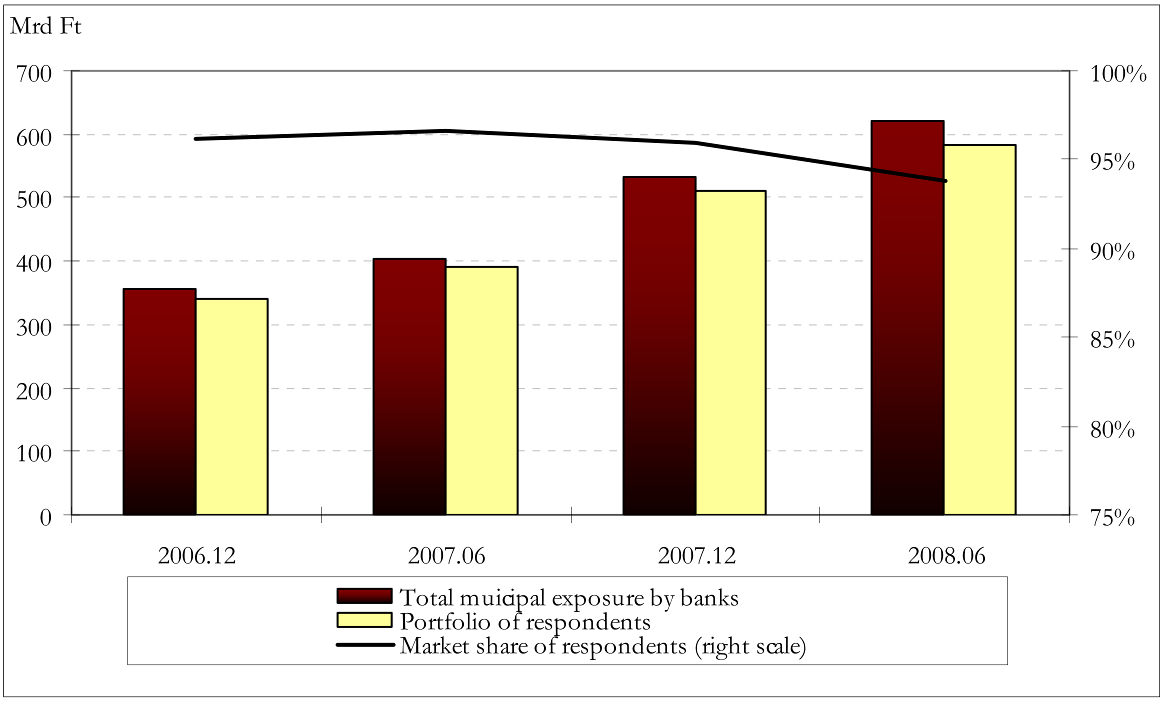


Chart 37: Covenant requirements by corporate category (ratio of those reporting tightening minus those reporting easing)



Municipality segment

Chart 38: Total municipal exposure and the share of banks completing the municipality questionnaire



ANNEX 2: METHODOLOGICAL NOTES

The survey allows for an analysis of how major banks perceive and evaluate market developments, and, based on the management's and owners' assessment of the situation, how they formulate their respective strategies and lending policies in particular. Aggregating individual, micro-level answers helps us to draw conclusions regarding the directions and trends in the changes in the market. The conclusions of this analysis always present the senior bank officers' replies rather than our own professional opinion. The survey covers household, corporate and municipal lending activities.

In accordance with the previous practice, the questionnaires were sent to the senior loan officers of the credit institutions involved in the survey. The questions were answered and the questionnaire, which also contained fixed questions, was filled in during an interview, providing an opportunity for more thorough explanations. Written answers were given by competent senior loan officers to the questions relating to lending to municipalities and by leasing companies belonging to the banks surveyed relating to motor vehicle financing.

The household questionnaire was completed by 13 banks altogether, with 9 answering the questions related to housing loans, while 13 banks and 5 financial enterprises owned by banks answered those on consumer loans[9] (Charts 23 and 24). In terms of housing loans, based on data from the end of 2008 H1, the surveyed institutions cover 93.3% of the banking sector,[10] while their percentage share in consumer credit was 88.0%.
The questionnaire was completed by seven banks, with a total market share of 86.7% and 93.1% of the markets of corporate loans and commercial real estate loans, respectively (Charts 27 and 28).

Altogether, we interviewed 6 banks in the segment of loans to municipalities. Based on data from the end of 2008 H1, the institutions surveyed cover 93.8% of the banking sector's municipal exposures (Charts 36 and 37).

As for methodology, in each segment the survey consists of a so-called standard questionnaire and a questionnaire which contains current issues.

In the standard part of the questionnaire, we survey the changes in willingness to lend, in lending standards, in the conditions of lending/extending loans as well as changes (observed and expected for the next half year) in demand perceived by the responding bank, changes in portfolio quality and the risk assessment of different sectors in case of the corporate questionnaire. Two different types of scaling are applied for multiple choice questions:

Five-step scaling: this scale is applied for assessment of changes in willingness to lend, demand, credit standards/credit conditions, risk parameters and trends in risk assessment of different sectors:

- 1: This evaluation reflects considerable increase in demand, in willingness to lend, considerable tightening in credit standards / credit conditions, a considerable increase in housing prices, risk parameters, and in the case of risk assessment of the sectors assessment 1 stands for a considerable increase in risk perception compared to the half year preceding the survey or compared to the current half year in the case of the forecast for the next half year.

[9] During the half years under review, the number and scope of banks surveyed changed (e.g. as a result of mergers). Regarding the subject of housing loans, from the launch of the survey (except for December 2003) we conducted the interviews with 7 banks, then in December 2005 the number of banks surveyed increased to 8 and later, from December 2007, to 9. In the beginning we interviewed 7 banks about consumer credit, increasing to 9 from 2004 H1, to 10 from end-2004, to 11 from end-2006, and to 12 from June 2007. The number of banks surveyed has been 13 since January 2008.

[10] In our analysis the banking sector does not include the Eximbank, KELER and the Hungarian Development Bank (MFB).

- 3: This evaluation means no change in the assessed parameters both for the given half year and for the forecast for the next half year.
- 5: This evaluation means considerable decrease in credit demand, in willingness to lend, considerable easing of credit standards / credit conditions, a considerable decline in housing prices, in risk parameters, and in the case of risk assessment of the sectors assessment 5 means becoming significantly safer compared to the half year preceding the survey or compared to the current half year in the case of the forecast for the next half year.

  Ratings of 2 and 4 provide an intermediate assessment (e.g. somewhat increasing demand).

Three-step scaling: this scale is applied for the assessment of reasons for changes in credit standards/conditions and demand:

- 1: This evaluation means that the evaluated factor did not contribute significantly to the changes.
- 2: This evaluation means that the evaluated factor contributed to a certain extent to the changes.
- 3: This evaluation means that the evaluated factor contributed considerably to the changes.

The keywords of the questionnaire could be defined in the following way:

Willingness to lend reflects the intention of respondents to expand in the given segment of lending.

Credit standards cover the internal policies that determine the types of the bank's customers and customer groups (based on sector, geographical location, size, financial indicators etc.) and grantable credit products (only collateralised, investment, overdraft loans, etc.).

Among credit conditions we can differentiate between non-price related factors and price-related factors. Non-price related conditions (e.g. collateralisation requirements, loan covenants, maximum size of loan/credit line, etc.) are concrete contract conditions; the bank is ready to extend the loan only under these conditions. In the case of price-related conditions we survey the spread between the interest rate level and the funding cost and the risk premium.

The attached Annexes 4, 5 and 6 contain the whole questionnaire and the aggregated answers (in the case of numeric answers).

In the second survey of 2008, through the questions about current concern we concentrated on domestic lending trends (demand trends, well-foundedness of borrowing behaviour, the role of the agent channel, loan refinancing) and on the effects of the subprime mortgage loan market crisis (a.k.a. the subprime crisis). In addition, in order to develop our methods and practices, we interviewed the participating institutions regarding the survey itself.

In presenting the results, we follow the structure of the relevant questionnaire in all three lending segments (households, corporate and municipal segments). The retrospective questions in the questionnaire always refer to the previous half year (e.g. for 2008 H1 in July 2008), whereas the forward-looking questions contain projections for the coming half year (e.g. for 2008 H2 in July 2008), compared to the trends of the previous half year.

To indicate the changes, we use the so-called net change indicator, expressed as a percentage of banks responding. We calculated this indicator by deducting from the number of persons projecting a change (tightening / growing / strengthening) the number of persons projecting the opposite (easing / decreasing / weakening), and dividing the result by the total number of persons responding (the answers are not weighted).