Introduction and legal basis

On 15 December 2017 the European Central Bank (ECB) received a request from the Magyar Nemzeti Bank (the ‘MNB’) for an opinion on a draft MNB decree on the regulation of the reliance of credit institutions on funds originating from financial corporations (hereinafter the ‘draft decree’).

The ECB’s competence to deliver an opinion is based on Articles 127(4) and 282(5) of the Treaty on the Functioning of the European Union and the sixth indent of Article 2(1) of Council Decision 98/415/EC 1, as the draft decree contains rules applicable to financial institutions insofar as they materially influence the stability of financial institutions and markets. In accordance with the first sentence of Article 17.5 of the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. Purpose of the draft decree

1.1 The draft decree is a targeted macro-prudential measure aimed at preventing the build-up of excessive reliance by credit institutions on wholesale funding. To this end, the draft decree sets a maximum limit on the share of the total funding of credit institutions originating from financial corporations. The MNB considers that although wholesale funding is not currently at an excessive level in the Hungarian banking sector, the potentially significant role of such funding in the banks’ funding structure and composition justifies the need for preventive macro-prudential measures.

1.2 The draft decree lays down a limit for an interbank funding ratio (IFR), which is defined as the weighted amount of liabilities originating from financial corporations, divided by the balance sheet total excluding own funds, and which is set to be at a maximum of 30% as of 1 July 2018.

1.3 The limit will apply in respect of entities covered by the scope of the draft decree, which includes: credit institutions operating as limited companies (with specific enumerated exceptions); Hungarian branches of foreign credit institutions; and entities belonging to groups which include credit institutions and fall under consolidated supervision pursuant to Law CCXXXVII of 2013 on credit institutions and financial enterprises 2 and Law CXXXV of 2013 on the integration of cooperative

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credit institutions 3. The limit will not be applicable to entities exempt from the scope of the draft decree, which includes: credit institutions with a balance sheet total of less than HUF 30 billion (approx. EUR 100 million); home savings and loan associations; two Hungarian institutions outside the scope of Directive 2013/36/EU of the European Parliament and of the Council 4 (Magyar Fejlesztési Bank Zártkörűen Működő Részvénytársaság and Magyar Export-Import Bank Zártkörűen Működő Részvénytársaság); and KELER Ltd., the Hungarian central securities depository.

1.4 For the purposes of calculating the IFR, the draft decree also specifies those items that are not to be considered as liabilities originating from financial corporations and are therefore exempt from being included in the numerator of the IFR formula. This includes for example: mortgage bonds; refinancing mortgage loans; bonds issued with a maturity of two years or longer; or any funds provided by foreign branches to Hungarian parent companies. In addition, with respect to the numerator of the IFR formula, the draft decree also specifies certain weightings of liabilities originating from financial corporations according to a six-pronged classification 5, in which each category has a different weighting. The weighting of 0 to 100 percentage points generally depends on whether the liability is denominated in forint (HUF) or in another currency and on the remaining maturity of the funds (liabilities), with short-term and non-HUF denominated liabilities assigned a higher weighting. 6 Moreover, the specific weighting of 0 to 20 percentage points lower than the weighting of 0 to 100 percentage points is to be assigned to either: (i) any funds received from parent companies, as defined in Law CCXXXVII of 2013 on credit institutions and financial enterprises 7 or, in the case of a Hungarian branch of a foreign credit institution, from the establishing institution; or (ii) the balance of ‘loro’ accounts other than those in point (i), defined as demand deposit or payment accounts maintained by a credit institution or a member of a group of credit institutions for credit institutions established outside Hungary for the purpose of providing financial services.

1.5 The IFR limit should be complied with by both individual and, in case of group members established in Hungary, on a consolidated level.

1.6 The IFR will be calculated on the basis of regular reporting of credit institutions to the MNB.

1.7 The IFR aims to rule out the overreliance of the banking system on funds originating from financial corporations which are a highly volatile type of funding. Overall, the IFR does not cover the whole liability side of the balance sheet, but only items originating from financial corporations, which, in the MNB’s view, have proven to be excessively volatile during crisis situations. The IFR is not regarded as a preliminary stable funding or a net stable funding ratio (NSFR) type requirement or a

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3  2013. évi CXXXV. Törvény a szövetkezeti hitelintézetek integrációjáról és egyes gazdasági tárgyú jogszabályok módosításáról published in Magyar Közlöny 120/2013 on 12 July 2013.
5 See Point 4 of the Annex to the draft decree.
6 It is specified that amounts on a deposit account shall be considered as having a maturity equalling to the earliest possibility of withdrawal.
7 See Section 6, point 3 of 2013. évi CCXXXVII. Törvény a hitelintézetekről és a pénzügyi vállalkozásokról.
requirement aimed at the general diversification of funding sources, but rather as a measure
targeting one specific funding risk. The draft decree also intends to set differentiated requirements
for funds with between 0 to 1 year and 1 to 2 year remaining maturities. The MNB does not
consider the IFR to be a derivation or early implementation of the NSFR, as provided for in
Article 413(3) of Regulation (EU) No 575/2013 of the European Parliament and of the Council,\(^8\),
since in its current calibration it serves as a backstop measure aimed at limiting the possibility of a
build-up of systemic risks and is therefore of a macro-prudential nature.

2. General observations

2.1 The ECB understands that the MNB intends to introduce the IFR as a national measure, based on
national law, targeting different systemic risks than those addressed by the standards for liquidity
coverage requirements and net stable funding requirements laid down in the relevant EU regulatory

2.2 The IFR is intended to complement the foreign funding adequacy ratio (FFAR), a requirement that
is currently applicable for credit institutions in respect of foreign exchange assets and that is
regulated by MNB Decree 14/2014\(^9\). The FFAR is a systemic risk mitigation measure which aims to
regulate the maturity mismatches and foreign currency positions of credit institutions.\(^10\) The ECB
has previously noted that the FFAR is similar in concept to the NSFR developed by the Basel
Committee on Banking Supervision, since it builds upon structural funding metrics that require
banks to hold stable funding in relation to the composition of their assets. However, there are a
number of differences between the NSFR and the FFAR\(^11\).

3. Specific observations

3.1 The ECB notes that the risk of unstable funding sources is to be addressed by the NSFR pursuant
to Article 413 of Regulation (EU) No 575/2013. Article 413(3) specifically provides that Member
States may maintain or introduce national provisions in the area of stable funding requirements
before binding minimum standards for net stable funding requirements are specified and
introduced in the Union in accordance with Article 510 of the same Regulation.

3.2 The ECB agrees that the IFR is less complex than the NSFR being developed under the European
Union regulatory framework as the NSFR addresses risk stemming from undiversified funding
more generally and also considers the funding needs of the assets held on the balance sheet. Both

\(^8\) Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential
requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (OJ L 176,
27.6.2013, p. 1).

\(^9\) 14/2014. (V. 19.) MNB rendelet a hitelintézetek devizapozícióbeli lejáratú összhangjának szabályozásáról, valamint a
pént- és hitelpiaci szervezetek által a jegybanki információs rendszerhez elsődlegesen a Magyar Nemzeti Bank
felügyeleti feladatai ellátása érdekében teljesítendő adatszolgáltatási kötelezettségekről szóló 43/2013. (XII. 29.)
MNB rendelet módosításáról, published in Magyar Közlöny 72/2014 on 19 May 2014.

\(^10\) In the light of the fact that the volume of foreign currency-denominated mortgage lending to households expanded
rapidly in Hungary until 2008 resulting in significant maturity mismatches, consequently increasing Hungary’s need
for foreign currency reserves. See Opinion CON/2014/15, as well as Opinions CON/2011/87 and CON/2012/27. All
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metrics, nevertheless, address the risk stemming from the excessive reliance by credit institutions on wholesale funding from financial corporations. In the light of this, the ECB suggests that the need for the IFR, as well as its calibration, be reassessed once the NSFR has been fully implemented as a binding minimum ratio at the Union level.

3.3 As a separate matter, the ECB reiterates that the need for and calibration of the FFAR laid down in MNB Decree 2014/14 should be reassessed with the implementation of the binding NSFR in the European Union, as expressed in its previous opinions.12

This opinion will be published on the ECB’s website.

Done at Frankfurt am Main, 6 February 2018.

[signed]

The President of the ECB

Mario DRAGHI

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12 See Opinions CON/2014/15 and CON/2015/15.