

Hungary

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Macroeconomic overview

Hungary's accession to the European Union in 2004 bolstered the outlook for the economy. The residential debt to GDP ratio increased after 2004 as residential mortgage finance was fueled by cheap international credit (foreign currency-denominated loans were mainly in CHF and EUR). Foreign direct investment continued to flow to Hungary, which, thanks also to the increase in EU funds, provided their contribution to economic growth. Until September 2008 household consumption funded by loans had continued to increase, but at the same time industrial production, employment and exports were falling. The Hungarian economy was close to recession even before the credit crunch and this is why the global financial crisis hit Hungary the hardest among EU economies. A USD 25 billion agreement was signed with the IMF in 2008, because the Hungarian financial sector suffered when credits began to dry up in the middle of 2008. The government successfully decreased the budget deficit from 9.2% to 4.0% of GDP from 2006 to 2009, and kept inflation under control at 4.0% in 2009 (compared to 6.0% in 2008). The Hungarian real GDP grew only by just 1.0% in 2007 and 0.6% in 2008, but in 2009 it contracted by 6.3%.

Housing and mortgage markets

The home ownership rate is relatively high in Hungary (around 92%). After the housing market slowdown at the end of the 1990s, from 2000 the mortgage market boosted partly because of the mortgage subsidies provided by the government, partly as a result of the available non-subsidised but cheaper foreign-currency loans. By 2009, the outstanding housing loans to GDP ratio in Hungary increased to 16.7% and the share of foreign-denominated loans rose to 60% of the total stock of housing loans. Moreover, from 2005 the volume of foreign currency denominated home equity loans increased rapidly, and by 2009 the total mortgage loans taken by the household sector (housing loans plus home equity loans) increased to 24% of GDP. Banks started to use financial intermediaries (i.e. brokers) from 2006. As a new phenomenon, after this period traditional mortgage loans were increasingly replaced by loans with real estate collateral used for consumption, and not for housing (through mortgage equity withdrawal).

Housing construction activity started to decrease in 2008 (from 36,159 housing completions in 2007 to 36,075 in 2008), and such slowdown continued in 2009 (down to 31,994 units), but it is expected that the cut will be much higher in 2010 as the number of building permits decreased by 35% between 2008 and 2009. There are other signs of difficulty in the construction sector as well, such as the stocks of unfinished buildings. It is expected that real fixed housing investment will fall further in 2010.

After October 2008 banks tightened their underwriting criteria; they restricted their LTV criteria and the client scoring, some banks even stopped issuing mortgage loans in underdeveloped areas (where house prices and the number of transactions are lower). The mortgage boom had an effect on house prices but did not lead to a speculative house price bubble. The year-on-year decrease in house prices between 2008 and 2009 was therefore 'only' 6.6% in nominal terms and 11.7% in real terms. Housing transactions decreased by 42% and housing construction by 11% between 2008 and 2009. The Hungarian government's response to the crisis focused on managing the fiscal deficit, which was a condition to get an IMF loan. The government drastically cut housing subsidies as part of the fiscal adjustment programme, under which both the interest subsidy and the homeownership down payment grants were suspended; the cuts were made effective as of the start of 2010.

On the other hand, the government introduced several programmes to soften households' conditions under the economic recession. The act on the Direct and Unconditional Surety Undertaken by the Hungarian State in relation to Mortgage Loans targets homeowners who are unable to service their mortgage payments due to unemployment or other temporary income shocks. Under this scheme, eligible borrowers can conclude so-called "bridging loans" with banks enabling them to redeem part of their mortgage instalments for a period of up to two years. Thus, the bridging loan backed by a state guarantee provides a breathing space to restructure their mortgage. However, the banks reacted to the government model by developing their own solutions: out of the 24,000 restructured loans, only 3,000 qualified for this government programme.

There were other initiatives aimed at easing the toughness of the economic crisis too. One of them was to set up a "crisis fund", to which well-off individuals and companies could contribute. The crisis management fund would provide one-off assistance to some 30,000 of Hungary's most disadvantaged families whose members had lost their job after October the 1st, 2008 or for whom the loan repayment instalments had increased by more than 20%.

The government also launched a temporary moratorium on evictions and suspended forms of foreclosure except for the judicial foreclosure until April the 15th, 2011. However, banks have put considerable effort into devising their own restructuring programmes in order to decrease the number of foreclosures (only mortgage brokers, who typically bought the stock of outperforming loans, were interested in continuing the foreclosures). The government launched another programme which offers preferential loans to local governments so that they can buy repossessed homes and let the original owner remain as a tenant in the property. Local governments have typically rejected this option, as there is no long-term guarantee that the central government will continue to support this newly-created rental stock.

In September 2009, banks adopted a Code of Conduct in compliance with government guidelines, in which they introduced more consumer-friendly procedures (e.g. putting an end to the practice of unilaterally changing loan contract conditions; giving defaulting borrowers 115 days to sell their home before foreclosing on it; improving the information given to borrowers, etc.). The government has strictly regulated the mortgage market since March 2010, by setting the maximum Loan-to-Value ratio for HUF-denominated loans at 70%, for loans in EUR at 60%, and for other foreign currency denominated loans at 45%.

Funding

Covered bonds are a common form of mortgage finance on the Hungarian market. According to the legal regulation covered bonds are issued by mortgage banks in Hungary. In 2009, the covered bonds issuance was EUR 3,209 million, the highest in the EU, and the total volume of covered bonds outstanding went at EUR 7,116 million. This means that almost 46% of all mortgage loan portfolio is financed by covered bonds. This proportion is higher in the refinancing of HUF and lower in case foreign currency mortgage loans, as commercial banks have more often used their own funding sources in case of EUR and CHF loans.

	EU27, 2009	Hungary, 2009	Hungary, 2008
GDP growth (%)	-4.2	-6.3	0.6
Unemployment rate (%)	8.9	10.0	7.8
Inflation (%)	1.0	4.0	6.0
% owner occupied	68.2	92.0	92.0
Residential Mortgage Loans as % GDP	51.9	16.7	14.8
Residential Mortgage Loans per capita, EUR thousand	12.37	1.55	1.56
Total value of residential loans, EUR million	6,125,727	15,543	15,626
Annual % house price growth	-6.8	-6.5	1.0
Typical mortgage rate (euro area), %	2.71	10.70 ⁴¹	11.20 ⁴²
Outstanding Covered Bonds as % outstanding residential lending	23.2	45.8	45.5

Source: EMF, Eurostat, ECB, Hungarian National Bank,
Hungarian Statistical Office, National Census

Notes:

- Typical mortgage rate in the euro area refers to the APRC (Source: ECB)
- EU owner occupation rate average derived from EMF calculations based on latest available data.

Hungary= 2003

⁴¹ Loans issued in HUF, not subsidised.

⁴² *Idem*