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EUROPEAN CENTRAL BANK
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Template for notifying national macroprudential measures not covered by CRR/CRD

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1. Notifying national authority and scope of the notification		
1.1	Name of the notifying authority.	Magyar Nemzeti Bank
1.2	Name of the macroprudential measure that is notified.	Amendment of the regulation on payment-to-income (PTI) ratio and loan-to-value ratio limits
2. Description of the measure		
2.1	Description of the measure.	The payment-to-income (PTI) ratio cap determines the maximum volume of monthly instalments vis-à-vis borrowers' regular, certified monthly income. The currently existing limits are differentiated by the net income of the borrowers and the currency denomination of the loans. As the result of the planned amendment, a new dimension of differentiation will be applicable in the case of HUF mortgage loans with over 5 years of maturity: loans with an interest rate fixation period shorter than 10 years and loans with an interest rate fixation period shorter than 5 years will be treated according to new, separate limits, whereas the actual limits continue to apply for loans with interest rate fixation periods of 10 years or more. New differentiated PTI limits pertaining to mortgage loans denominated in EUR or other foreign currencies with over 5 years of maturity will also be introduced pending on whether their interest fixation period is at least 5 years or below that.

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The proposed amendments would also modify – with a longer phase-in period – the threshold of the net income of borrowers above which a higher level – 60 percent instead of 50 percent for HUF loans – of indebtedness is allowed to account for the rise of the nominal and real wages in Hungary since the introduction of the measure in 2015.

Table 1: PTI limits pertaining to mortgage loans denominated in HUF with over 5 years of maturity

	Length of fixation of interest rates		
	Floating or fixed for less than 5 years	**At least 5 years, but less than 10 years**	**At least 10 years or fixed for the whole term**
Limits set for loans denominated in **HUF** set from **1 October 2018**			
Income below **HUF 400,000**	**25%**	**35%**	**50%**
Income at least **HUF 400,000**	**30%**	**40%**	**60%**
Limits set for loans denominated in **HUF** set from **1 July 2019**			
Income below **HUF 500,000**	**25%**	**35%**	**50%**
Income at least **HUF 500,000**	**30%**	**40%**	**60%**

EUR limits for the relevant income categories: for below 5 years interest fixation period 15/20%, for 5 years or longer interest fixation period 25/30%. Limits for mortgage loans denominated in other FX: for below 5 years interest fixation period 5/10%, for 5 years or longer interest fixation period 10/15%.

Additional amendments are proposed to ensure and improve the effectivity of the regulation and its smooth application, including specifying requirements for special cases of loan contract amendments and interest rate determination types, clarifying the scope of application of the regulation, and other technical changes.

2.2	Legal basis and process of implementation of the measure.	As macroprudential authority in Hungary, the MNB in the event of any disturbance in the credit market shall adopt measures to control excessive credit growth to ensure that the financial intermediary system functions in a balanced way in financing the economy, as stipulated in Law CXXXIX of 2013 on the Magyar Nemzeti Bank (the MNB Act). In line with this, Section 171 (1) k) ka) of the MNB Act empowers the Governor of the MNB to decree measures for the reduction of risks stemming from excessive credit growth if these measures are required to prevent the build-up of systemic risks and to mitigate systemic risks, and to increase the resilience of the financial intermediary system within the strategic framework defined by the Monetary Council, based on the decision of the Financial Stability Board. The MNB, based on credit market trends of the past 3 years, made a proposal on the introduction of differentiated PTI limits, held consultations with market participants and formulated a draft decree. It was sent to the ECB for the required consultation procedure. Afterwards, the finalised decree will be approved by the Financial Stability Board of the MNB, and the decree will be published in the Official Gazette.
2.3	Coverage	The newly issued mortgage loans with above 5 years of maturity and financial leasing carried out by Credit institutions and Financial Enterprises to consumers will be covered.
2.4	Any other relevant information.	-
3. Timing		

3.1	Timing of the decision	The Financial Stability Board of the MNB reached a decision regarding the proposed amendments on 5 June 2018, whereas the final decision is expected to be made in August 2018.
3.2	Timing of the publication	The date of publication of the measure is expected to be in August 2018, following the adoption of the final decree.
3.3	Disclosure	Consultations have already been held with market participants before the finalisation of the draft decree. A press release is also to be issued about the planned changes at the beginning of the ECB consultation. Following the conclusion of the consultation procedure with the ECB according to the Council Decision 98/415/EC, the final decree will be approved by the Financial Stability Board of the MNB, and the decree will be published in the Official Gazette.
3.4	Timing of the application	The differentiated PTI limits shall be applicable from 1 October 2018, and the limits determining the new net income threshold will be applicable from 1 July 2019.
3.5	End date (if applicable)	-
4. Reason for the activation of the measure		
4.1	Description of the macroprudential risk to be addressed.	Mortgage loans that are usually disbursed with longer maturities and floating interest rates or with short term interest rate fixation periods expose consumers to interest rate risk. Because of the lower initial monthly instalments of loans with floating interest rates or with shorter interest rate fixation periods, these loans seem to be a more affordable deal for consumers, while it is difficult for them to understand and manage the inherent interest rate risk of such products. A potential sudden increase of the interest rates results in a sudden increase of monthly instalments that can lead to repayment problems and even to a mass default of these exposures. Current low interest rates on the market imply an elevated risk of an increase in interest rates in the future.

		Hence, the high volume of long term household exposures with floating interest rates or shorter interest rate fixation periods can lead to the build-up of systemic level default risks. In Hungary, the share of floating interest rate mortgage loans within new lending has been declining for the past few months but is still material. By the end of Q1 2018 the share of housing loans with an interest rate fixation period of up to one year accounted for 28 percent, while the share of housing loans with an interest rate fixation period of up to 5 years reached 71 percent of newly disbursed housing loans, which might pose a significant interest rate risk for borrowers. Therefore, there is a need to introduce direct measures to ensure that debt holders who choose to take out floating rate mortgage loans would have sufficient buffers for the situation when interest rates would be on the increase in the future. This can contribute to the healthy structure of credit growth, which is especially important given the dynamics currently seen in the market.
4.2	Description of the indicators on the basis of which the measure is activated.	Albeit the share of housing loans with floating interest rates or with interest rate fixation periods up to 1 year have declined from the average level of 45 percent in the last year to 21 per cent in April 2018, the share of housing loans with floating interest rate or with interest rate fixation periods up to 5 years accounted for 71 percent of the newly disbursed housing loans. Therefore, there is a need to further lower the share of and prevent the future expansion of loans with significant interest rate risk. The MNB using a micro dataset based on credit registry data has assessed the potential impact of different interest rate shocks of the past 10 years on the instalments of the current loans. The data shows that the risk of over-indebtedness due to such shocks would increase significantly compared to the initial period of the loan term for borrowers with a PTI ratio higher than 25 percent at loan origination. The examined shocks would push 25-30 percent of borrowers near the 50/60 percent PTI limits. Based on these results, the new limits were

		set so as to preserve adequate income buffers of the borrowers even in stressed situations.
4.3	Effects of the measure.	As the modification affects the interest rate fixation attributes of mortgage lending, not credit quantity, the estimated lending effects of the measure are low. According to the estimations based on credit registry data, the modification would have restrained effect on the amount of distributed credit volumes if it had been in force since 2016. This calculation takes into account all three possible adaptation techniques. (1) Borrowers constrained by the new limits could either choose mortgage loans with longer interest rate fixation periods, which – due to the higher interest rate of these loans – would increase their monthly instalments. Since the average PTI level was at 27 per cent in 2017, the small minority of debtors only at the 50/60 per cent limit would have been affected and would have faced lowered possible loan amount. (2) Other theoretical response to this problem could have been to not to take out the mortgage loan at all. (3) Have borrowers opted for not to lengthen the interest rate fixation period, they would have faced a lower available loan amount due to the lower PTI limits for these loans. Based on our expectations, the most likely option borrowers would choose would be to opt for loans with a longer interest rate fixation period and decrease the loan amount in case of reaching the upper 50/60 percent PTI limits. It means that only the disbursement of the riskiest loans would be restrained by the modified regulation. Consequently, the regulation would not have a material negative impact on credit growth.
5. Cross-border and cross-sector impact of the measure		

5.1	Assessment of cross-border effects and the likely impact on the internal market (Article 133(11)(d) of the CRD IV and Recommendation ESRB/2015/2)	The modified PTI regulation is expected to have limited cross-border effects. Given the geographical distribution of the Hungarian mortgage loans, no material cross-border effect can be identified.

5.2	Assessment of leakages and regulatory arbitrage within the notifying Member State	During the calibration of debt cap rules, three types of possible regulatory arbitrage channels should be assessed: (1) "cross-jurisdiction" arbitrage, (2) cross-sectoral business activities, (3) exploitation of loopholes within the regulatory framework.
		• Cross jurisdiction arbitrage: as mentioned in pont 5.1, no material cross-border effect can be identified.
		• Cross sectoral arbitrage: as the Hungarian debt cap regulation has a broad institutional scope which applies to all creditor's contracts concluded with consumers in the context of granting credit and loans on the territory of Hungary (Decree Section 1 (1)), no material cross sectoral arbitrage effect can be expected.
		• Exploitation of loopholes within the regulation: as the modified PTI regulation introduces new limits to mortgages with maturities over 5 years and interest rate fixation period shorter than 10 years the regulation can be circumvented by the following ways:
		  o Shortening the interest rate fixation period following the loan disbursement: the regulation explicitly controls for this kind of adaptation, as it necessitates the recalculation of PTI eligibility in case of loan amendments aiming at shortening the interest rate fixation period.
		  o Shifting to credit types not targeted by the modification: As the other possible credit types (e.g. cash loans) are more expensive than mortgage loans with lengthened interest rate fixation period, this effect would probably be very limited.
		  o Shortening the maturity of the loan to below 5 years: This kind of adaption is possible in

		principle, but it leads to much higher instalment amounts, therefore the expected effect would not be material.
5.3	Request for reciprocation	-
6. Miscellaneous		
6.1	Contact person(s) at notifying authority.	**Ms Anikó Szombati**, Executive Director for Macroprudential Policy Phone: +36 (1) 428 2662 Mobile: +36 (20) 211 3444 E-mail: szombatia@mnb.hu **Mr Péter Fáykiss**, Director, Macroprudential Directorate Phone: +36 (1) 428 2600/2239 Mobile: +36 (30) 449 8830 E-mail: faykissp@mnb.hu
6.2	Any other relevant information.	-