EUROPEAN COMMISSION

Brussels, 17.12.2009
C(2009)10276 final

Subject: **State aid N 662/2009 - Hungary**
Prolongation and modification of the Hungarian bank support scheme N 355/2009

Sir,

1. PROCEDURE

(1) On 22 December 2008 Hungary notified a recapitalisation and guarantee scheme for banks (hereinafter: "the Scheme") which was approved by Commission decision of 12 February 2009 in State aid case N 664/2008 (hereinafter "the original decision")[1]. An amendment to the Scheme and a prolongation was notified on 15 June 2009, which was approved by Commission decision of 3 September 2009 in State aid case N 355/2009[2].

(2) On 27 November 2009, Hungary notified a request to prolong the recapitalisation measure of the Scheme.

2. DESCRIPTION OF THE NOTIFIED MEASURE

2.1 Objective of the Scheme

(3) In response to the ongoing exceptional turbulence in world financial markets, the Scheme brought forward by the Hungarian authorities consisted of two measures designed to ensure the stability of the Hungarian financial system. They had two objectives: on the one hand, building and maintaining an adequate buffer of capital for the credit institutions concerned, and thus enhancing their solvability and their ability to lend to the real economy (recapitalisation measure) and, on the other hand, ensuring that funding is available to banks by alleviating concerns about the security of those funds to prevent problems stemming from maturity mismatch (guarantee measure).

1 Commission decision C(2009) 993 final; OJ C 147, 27.06.2009, p.2.
2 Commission decision C(2009) 6740 final; OJ C 235, 30.09.2009, p.2.

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(4) Beneficiaries of the Scheme are fundamentally sound credit institutions of systemic importance established in Hungary[3].

(5) Both measures are to expire on 31 December 2009.

2.2 The guarantee measure

(6) Under the guarantee scheme, the Hungarian State was empowered to make available a State guarantee to the credit institutions covering new debt.

(7) The guarantees could cover new debt issued up to 31 December 2009. Only interbank lending activities are guaranteed, subordinated loans and capital investment are not covered by the measure. The maximum amount that can be guaranteed is HUF 1500 billion[4].

(8) The guarantee measure has not been applied to date.

(9) As the Hungarian authorities see no sign of future demand for the measure either, the guarantee measure will expire on 31 December 2009.

2.3 The recapitalisation measure

(10) Under the recapitalisation scheme, the Hungarian State was empowered to undertake the recapitalisation of certain financial institutions with an overall budget of HUF 300 billion[5]. The measure aimed at increasing the capital adequacy ratio of the participating banks in order to strengthen the credit institutions' capital base and thereby boost the confidence of other market players. The recapitalisation could take the form of preference shares, designed to be classified as Tier 1 capital. The objective of the recapitalisation is to bring the participating banks' Capital Adequacy Ratio up to [...][*].

(11) Only one bank participated in the recapitalisation measure to date, FHB Jelzálogbank Nyrt. The capital injection provided to this bank was HUF 30 billion[6], and the remuneration (return on the preference shares) was set at 10.49%. The recapitalisation decision was made on 31 March 2009 by the Hungarian authorities.

(12) The Hungarian authorities are of the view that it is necessary to extend the application deadline for the measure until 30 June 2010, since the original goals of the measure are still valid. The Hungarian Central Bank in a letter of 3 December 2009 confirmed the necessity of the continuation of the scheme for financial stability reasons.

(13) All other conditions as approved by the Commission on 3 September 2009 remain unchanged and Hungary confirms that all the commitments made in relation to the original decision continue to apply.

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3 Including subsidiaries of foreign banks but excluding banks operating in the form of branch offices.
4 HUF 1500 billion is equivalent to approximately EUR 5.6 billion using exchange rates of 28 July 2009.
5 HUF 300 billion is equivalent to approximately EUR 1.1 billion using exchange rates of 28 July 2009
* Confidential information.
6 HUF 30 billion is equivalent to approximately EUR 0.6 billion using exchange rates of 28 July 2009

3. POSITION OF HUNGARY

(14) In line with the original decision, Hungary accepts that the Prolonged Scheme constitutes State aid within the meaning of Article 107(1) TFEU[7].

(15) Hungary seeks the authorisation of the prolongation of the recapitalisation measure to 30 June 2010. According to the Hungarian authorities, the measure is necessary and proportionate to restore financial stability in Hungary.

(16) The Hungarian authorities claim that the prolongation, like the Scheme, is compatible with the internal market, because due to the ongoing crisis it is necessary to remedy a serious disturbance in the Hungarian economy pursuant to Article 107(3)(b) TFEU.

(17) The letter submitted by the national Bank of Hungary, dated 3 December 2009, states that given the fragility of global and Hungarian financial markets, the availability of government capital injection is a necessary measure to ensure financial stability in Hungary even in adverse conditions.

(18) Hungary notes that all conditions under the recapitalisation measure of the Scheme remain unchanged.

(19) In addition, in relation to each bank recapitalised under the measure, Hungary undertakes to submit an assessment of the bank's business model and further information including the bank's prospective capital adequacy in order to enable an assessment of the bank's risk profile and viability.

(20) Finally, Hungary undertakes to inform the Commission before a recapitalisation is taking place in the framework of the Scheme about the risk profile of the beneficiary bank, so that the Commission can assess its situation and draw the necessary consequences in terms of the need to provide a restructuring plan, pay an adequate remuneration according to its risk profile and the non-payment of coupon on hybrid capital with the use of reserves.

4. ASSESSMENT OF THE MEASURE

4.1 State aid character of the Scheme

(21) As set out in Article 107(1) TFEU, any aid granted by a Member State or through State resources in any form whatsoever which distorts or threatens to distort competition by favouring certain undertakings or the production of certain goods shall, in so far as it affects trade between Member States, be incompatible with the internal market.

[7] With effect from 1 December 2009, Articles 87 and 88 of the EC Treaty have become Articles 107 and 108, respectively, of the Treaty on the Functioning of the European Union ("TFEU"). The two sets of provisions are, in substance, identical. For the purposes of this Decision, references to Articles 107 and 108 of the TFEU should be understood as references to Articles 87 and 88, respectively, of the EC Treaty where appropriate.

(22) For the reasons indicated in the original decision, the Commission considers that the Scheme constitutes State aid within the meaning of Article 107(1) TFEU. Hungary shares this position.

4.2 Compatibility

(23) In its decision of 3 September 2009 the Commission considered the notified measures, including the recapitalisation measure, compatible with the internal market under Article 107(3)(b) TFEU.

(24) The recapitalisation scheme's objective is to restore market confidence in banks through improved capital buffers and ultimately to avoid any negative spill-over to the Hungarian real economy.

(25) The prolongation of the recapitalisation measure of the Scheme does not contain any modification of the measure previously approved. The Commission notes that Hungary confirms that all the commitments made in relation to the Scheme will continue to apply, in particular those related to presenting every six months a report on the operation of the Scheme and submitting individual restructuring or liquidation plans within six months for banks that default on their liabilities.

(26) The Commission must ensure that the distortions of competition created by the scheme are limited to remedying a serious disturbance in the economy and that a return to market conditions takes place as soon as such disturbance is terminated. Although there are already signs for a recovery of the financial markets, there remain doubts on the sustainability of this positive trend.

(27) The Commission considers that the exceptional circumstances at the origin of the notified measures persist and therefore recognises the need for the prolongation of the Scheme. The letter from the National Bank confirms this (see point 17 above). In particular, the National Bank states that while the Hungarian banking system is well capitalised for a baseline scenario, it would require an additional capital base under the more severe but still plausible stress scenario. Therefore, the Commission considers that the prolongation of the measure is appropriate and necessary to remedy the serious disturbance of the Hungarian economy.

(28) The Commission notes that the extension is limited in time (not exceeding six months) which will limit the potential distortion of competition. Accordingly, recapitalisations under this scheme may be undertaken during an entry window of 6 months, until 30 June 2010. Any further extension will require the Commission's approval and will have to be based on a review of the scheme's effectiveness in view of the monitoring report Hungary has undertaken to submit to the Commission.

(29) The Commission therefore does not object to prolonging the recapitalisation measure under the Scheme until 30 June 2010.

(30) The Commission recalls that, as indicated the Annex to the Restructuring Communication, restructuring plans should contain all State aid received as individual aid or under a scheme during the restructuring period and all such aid needs to be justified as satisfying all criteria prescribed by the Restructuring Communication (i.e. return to viability, own contribution by the beneficiary and limitation of competition distortion). This means that, as soon as a Member State

is under an obligation to submit a restructuring plan for a certain aid beneficiary, the Commission needs to take a view in its final decision as to whether any aid granted during the restructuring period satisfies the criteria required for the authorisation of restructuring aid. To this end, an individual ex ante notification is necessary.

(31) Furthermore, based on paragraph 16 of the Restructuring Communication, the Commission recalls that should further aid not initially foreseen in a notified restructuring plan be necessary for the restoration of viability, this cannot be granted under an approved scheme but needs to be subject to individual ex ante notification and any such further aid will be taken into account in the Commission's final decision on that bank.

5. DECISION

The Commission concludes that the prolongation in question does not alter its previous assessment in the decision of 3 September 2009 in State aid case N 355/2009 that the recapitalisation measure under the Scheme is compatible with the internal market. The Commission has accordingly decided not to raise objections. The Commission notes that Hungary exceptionally accepts the decision to be adopted in the English language.

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http://ec.europa.eu/community_law/state_aids/state_aids_texts_hu.htm .

Your request should be sent by registered letter or fax to:

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Yours faithfully,
For the Commission

Neelie KROES
Member of the Commission