



Dear CEO Letter No. 4/2009

on the Expected Conduct Aiming at the Strengthening of Credit Institutions

The Hungarian Financial Supervisory Authority (hereinafter: HFSA) – in compliance with its responsibilities – draws the attention of the credit institutions in a Dear CEO letter that it is especially important in the current financial crisis that the credit institutions shall take all steps to ensure their prudent operation and the stability of their liquidity position as well as their capital status.

With respect to increasing credit risks, moreover to the difficulties of raising additional liquidity and capital the HFSA expects the following from the credit institutions by emphasizing prudential arguments:

1. During the period of increasing risks, the sustainability of the volume of the credit activity raises the requirement of additional capital towards credit institutions, when it is becoming more and more difficult and expensive to raise external capital. In situations like that internal capital-raising becomes more appreciated and therefore it is especially important that credit institutions use the obtained profit for the stabilization of their capital status. Therefore the HFSA advises that even the institutions that are otherwise eligible to request exemption from the obligation to create general reserves pursuant to Subsection 3 Section 75 of Act No. CXII of 1996 on Credit Institutions and Financial Enterprises, use the possibility to create such reserves. The HFSA will not endorse any requests for such an exemption in 2009.
2. Besides creating general reserves, another method for strengthening the capital status of the institutions is if the credit institutions do not declare and pay dividends from the after tax profit but leave such amount with the institution. Therefore the HFSA expects that the executive officers of the credit institutions will not advocate the disbursement of dividends to the owners. Moreover the HFSA proposes to the owners of the credit institutions to render self restraint with respect to the disbursement of dividends and refrain from this possibility.
3. During the period of increasing credit risk it is especially important to ensure risk transparency. Therefore the HFSA does not consider it an advisable business policy if the credit institutions market such innovative products the risks of which are difficult to be assessed either by the credit institution itself, the buyer of such innovative product or by the HFSA. These products include those structured securities which in their designs are similar to those structures behind the current crisis and which definitely proved inadequate in the crisis both as to their ratings and their pricings. Similar problems can be relevant with other products as well, including structured FX linked swaps and the speculative FX options which –by their seemingly favourable conditions – encourage speculation with the exchange rate and may cause great

potential loss to inexperienced customers. Before structuring such or similar products it is advisable that the credit institutions consult the HFSA to ensure that the possible risks are visualized, transparent and hedged to the greatest possible extent.

Please be informed that the contents of this letter are not legally binding on the institutions falling under the scope of the acts set out in Section 4 of Act No. CXXXV of 2007 on the Hungarian Financial Supervisory Authority. The purpose of this letter is to foster prudent operation of the institutions however, the HFSA will review its implementation during supervisory inspections.

The HFSA publishes this Dear CEO letter on its website under the following menu points: "Regulation/CEO Letters", moreover a copy of this letter will be sent directly to the executive officers and owners of the credit institutions furthermore to the foreign supervisory authorities of such owners.

Budapest, 25 February 2009

VARGA Csaba
Director General of the HFSA