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## THE HUNGARIAN BANKING SYSTEM AND REGIONAL DEVELOPMENT IN TRANSITION (1987-1997)

ZOLTÁN GÁL

In this essay I would like to give a short overview of the spatial structure and the development tendencies of the banking network on the regional and settlement level which occurred during the first decade of two-tier banking. Allocation of branches of the banking institutions plays an important role, not only in the development of the national economy as a whole, but in the development of the local and regional economy, in innovation and, last but not least, in the organisation of production and service sectors. The elements of the banking network connect to regional development as the supply section of the business services therefore the density and the number of banks and their branches are an important indicator of regional economic development.

Surveys on the regional structure of banking are all the more important because in the last decade the Hungarian banking system underwent fundamental transformation followed by bankruptcies, bank consolidation, privatisation processes, sometimes accompanied by strong state intervention. The role of the state in these processes very often became a bone of political contention.

### *DEVELOPMENT AND SPATIAL STRUCTURE OF THE HUNGARIAN BANKING SYSTEM (1987-1997)*

The first important step forward in the modernisation of the Hungarian financial sector was the creation of the two-tier banking system in 1987, which was more adapted to a market environment. Following this Act, the National Bank of Hungary, performing primarily central bank functions, and the institutionally-separated commercial banks were set up in January 1987. Commercial banks who originally had corporate clientele were admitted to the retail market, while financial institutions were given commercial banking licenses.

If we take ten years of development in the banking system into consideration it can be divided into different periods. The short period between 1989-1992 was the peak time for foundation of new banks. Competition was also increased by the entrance of the new foreign-owned and joint-venture banks founding their own subsidiary banks in Budapest.

After the period of rapid and extensive expansion the banking system was characterised between 1992-1995 by the first bankruptcies and failures. This automatically

led to the loss of market shares of the Hungarian owned banks and strengthened the position of foreign banks. Pecuniary difficulties of the mainly state-owned banks made inevitable the restructuring of the Hungarian banking sector, together with the loan, bank and debtor consolidation. The main purpose of bank consolidation and privatisation was to decrease the percentage of state ownership in the banking sector to at least below 25%.

In the third period, commencing in 1995, a stabilised and a more competitive banking system emerged, characterised by successful privatisation of the banking system resulting a slower expansion in the banking from 1996 onward. In this latter period of development the branch network expansion was one of the major phenomena. This was due to business policies of banks shifting from the corporate to the retail market, intending to gain more of the market shares through easier access to retail customers, and on the other hand strengthening the competition which force mainly foreign banks without branches to build networks in order to hold their ground.

One of the most important alterations in the Hungarian banking system was that the role of foreign capital in ownership was determined. (Table 1) As the consequence of foreign capital inflow into the Hungarian banking, the structure of ownership was entirely transformed; parallel with the process of the significant decrease in state ownership (17% recently), shares of foreign capital attained 65% of the banking system,

**Table 1**  
*Proportion of foreign capital in the Hungarian banking system*

	1987			1991			1996		
	1	2	3	1	2	3	1	2	3
<b>Europe</b>									
Germany	2	260	0.4	3	884	0.7	7	15 503	7.4
Austria	2	260	0.4	5	3 817	3.1	6	14 508	6.9
France	1	110	0.2	3	884	0.7	4	4 987	2.4
Italy	1	110	0.2	4	1 419	1.1	5	4 427	2.1
Holland	0	0	0.0	4	1 220	1.0	2	2 701	1.3
Russia	0	0	0.0	0	0	0.0	1	3 500	1.7
<b>America</b>									
USA	1	806	1.3	1	1 660	1.3	2	9 802	4.7
<b>Far East</b>									
Japan	1	110	0.2	3	1 434	1.2	3	4 893	2.3
Korea	0	0	0.0	1	3 154	2.5	3	6 094	2.9
<b>International banks</b>									
EBRD, IFC, CECD	1	150	0.2	4	803	0.6	3	8 510	4.0
Others	0	0	0.0	2	1 652	0.8	10	9 759	4.6
<b>Sum-total</b>	3	1 910	3.1	17	16 685	13.6	29	84 684	40.0

1 Foreign bank shares in number of Hungarian banks

2 Amount of foreign capital in registered capital (million HUF)

3 Proportion of foreign capital in the total registered capital of Hungary (%)

gaining a majority of market shares within a short time. This very high proportion of foreign capital is unique not only compared with Poland (where it was 8.5% in 1994) but in the European context it is also one of the highest. (In the UK 53% of ownership is foreign, but in Finland it is only 1%, in Germany 2%). The main investors are, according to the portion of invested capital, still the leading German and Austrian entrepreneurs, following by the American, Dutch, French, Japanese and Korean investors. Activity of the Dutch banks is indicated by the fact that all the top-ranking Dutch banks opened subsidiaries in Hungary (ABN Amro, ING, Rabobank) but British banks are conspicuous by their absence.

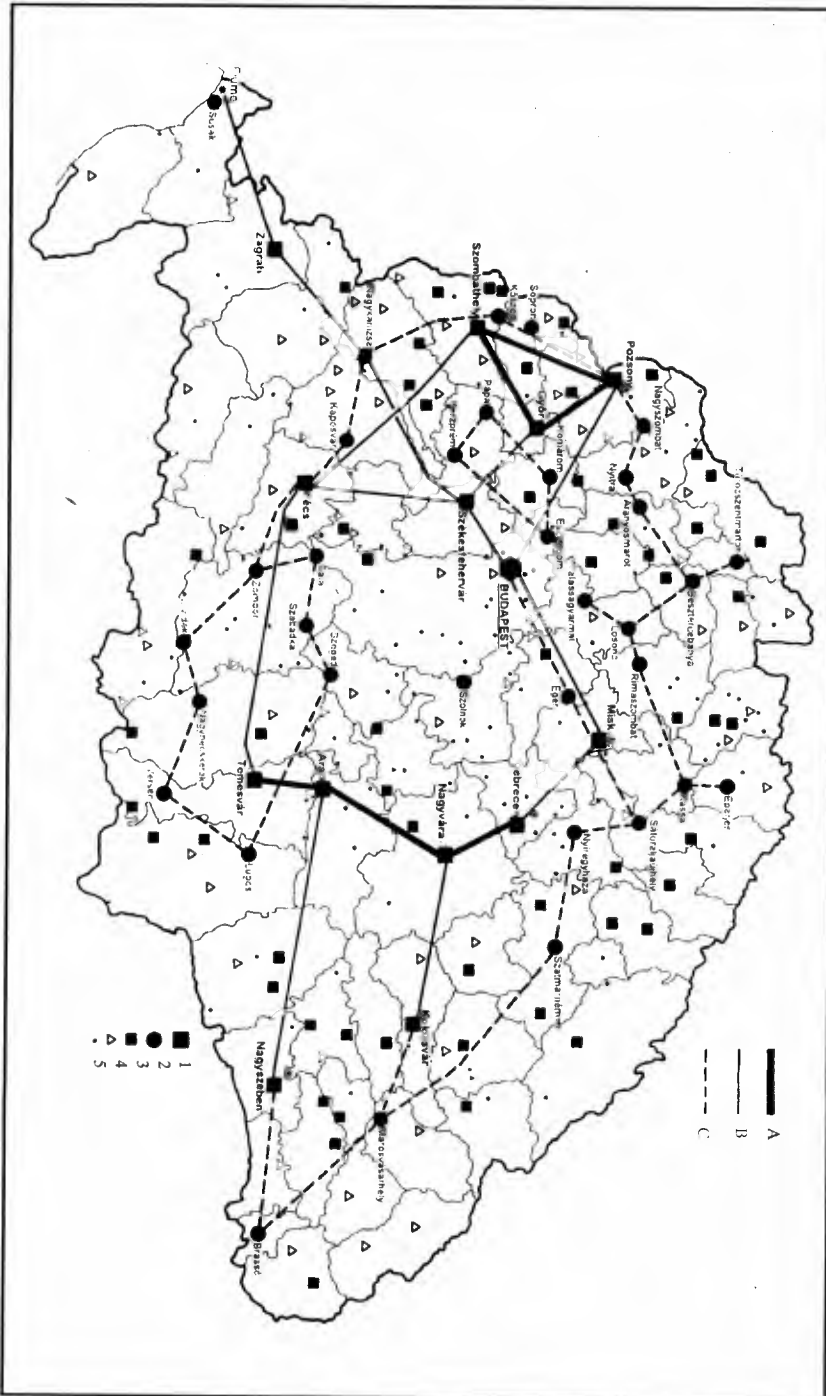
To summarise the role of foreign capital in the Hungarian banking system it can be said that such a rapid process of privatisation of banking without foreign capital inflow would have been impossible. Foreign capital investment has contributed significantly to the growth of international competitiveness of Hungarian banking. (Per capita investment of foreign capital accounted for 1,520 USD in Hungary, compared to 680 USD in the Czech Republic and 318 USD in Poland till 1996.)

In contrast to Hungarian traditions, a specialised rather than universal banking system has been created, sorting different type of banks by functions (32 commercial banks, 8 specialised banks, mortgage banks and building societies, 246 co-operative savings banks). Compared to the network which existed at the turn of the century (when the number of independent banks scattered throughout the countryside were overshadowed within the banking network, and there were proportionally few branches in banking before World War I, consequently only 5.7% of the network was concentrated in Budapest), the recent banking system is characterised by strong spatial concentration. (*Figure 1*)

The fact that all the banks except one are based and headquartered in Budapest results in a deformed structure in the banking system. Banking in Hungary is still the most centralised branch of the economy with a definite centre in Budapest. The leading position of Budapest in the financial sectors, especially in banking and insurance, is more striking than in any other sectors. Consequently local and regional banks are missing from the Hungarian banking system. (However, this strongly monopolistic structure is more in line with international tendencies, which are characterised by overconcentration at the global level; in contrast to other transitional economies, such as Poland, where the role of regional banking is significant.) Branches of banks based in Budapest have much less room for making independent decisions than the branches of county seats during the communist period.

In contrast to the concentration processes in the global markets the growing significance of regionalism requires establishment of the regional money markets and institutions financing regional policies. The boom of private enterprise, privatisation, the necessity of their presence in the local markets and competition for the retail markets also requires the expansion of the banking network in the countryside. Besides the corporate and the retail market project, financing will be one of the most profitable businesses for banks which have to support the regional development programmes through

Figure 1  
 Hungarian urban hierarchy based on financial functions, 1910



1 – innovation zones, 2 – inner circle of regional financial centres, 3 – outer circle of secondary financial centres  
 4 – regional financial centres, 5 – secondary financial centres, 6 – tertiary financial centres, 7 – quaternary financial centres, 8 – towns without financial centres

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financing infrastructural, power and telecommunicational investment and co-operating with regional and local administrations.

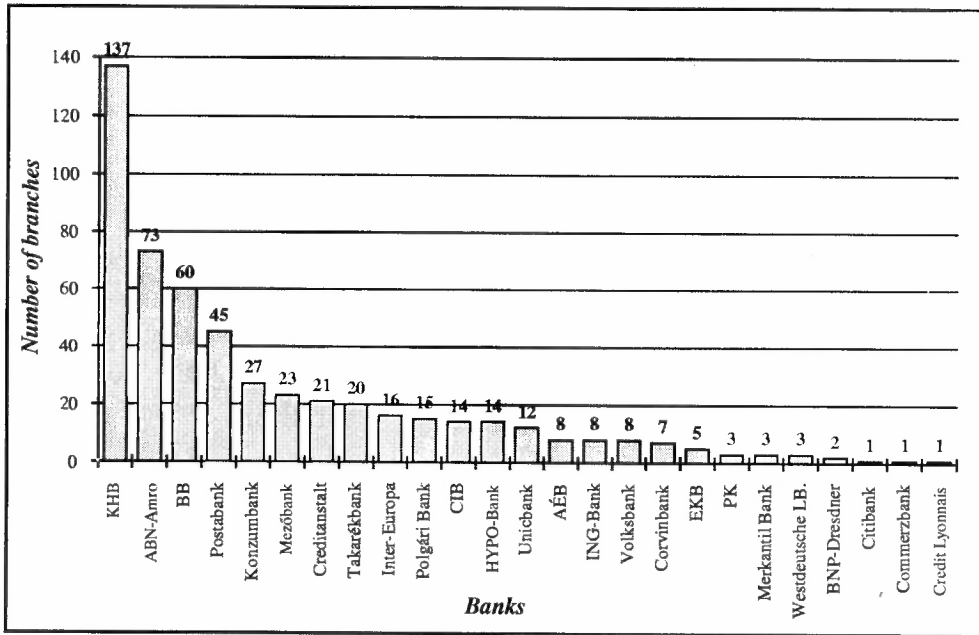
From the deformed spatial structure of the banking network of the early 1990s arose more difficulties:

- Lower density of the network meant both the low level of availability of branch offices and the higher structural polarisation of the branch network. On the one hand this meant that the rapid expansion of banking, initially concentrated almost exclusively in Budapest, was not followed by the extension of the branch network at a rapid pace in the countryside. On the other hand the new banks established in 1987 inherited a particular branch network from the National Bank of Hungary, since branches were missing from certain county seats, accompanied with a spatial-regional asymmetry.
- The other marginal pole of the national banking system is the dense network of the co-operative savings banks scattered throughout the countryside. The most important disadvantages of these are their weak financial standing and lack of strong centres or headquarters. Despite the number of co-operative savings banks being 1,740, thereby accounting for 64% of the total national network, most of these small savings banks situated in the smaller towns and villages have a very low capital circulation and can supply only a narrow range of services.

The start of the 1980s and 1990s was the first period of boom in the establishment of banks: 17 commercial banks founded about 350 branches, concentrating 85% of the new offices into the provincial cities. During the next period of the two-tier banking system between 1992–1996 the network was considerably restructured. Expansion of the banking system was restricted very much by the huge inherited debt imposed a large burden on the institutions. The smaller banks went bankrupt (Ybl Bank), others were liquidated (Dunabank, Iparbankház) or some of them were merged. The big banks rescheduled their policy of network building and a few closed some of their branch offices, but the other banks such as Budapest Bank and Postabank started a spectacular growth in network expansion. Accordingly, between 1992–1996 the number of banking institutions decreased due to the bankruptcies, mergers and the purchasing processes of privatisation. In only two years (1995–1996), six banks were liquidated or merged into other commercial banks. (*Figure 2*)

The foreign-owned banks started to expand their branch network (by purchase through privatisation and opening new branches) later and more cautiously. There are different reasons for this policy. On the one hand, these banks were strong enough in terms of capital intensiveness, therefore they could adjust the pace of network building to their own pace of development. On the other hand, foreign-owned banks were first of all interested in corporate banking supplying services for the joint-stock companies. However, the foreign owned banks switched to rapid expansion, gaining both larger market shares and leading positions in terms of profitability, and grew more rapidly than the bigger banks<sup>1</sup>.

**Figure 2**  
*Branch network of Hungarian commercial banks, 1997 (not including OTP)*



Recently, the tendency of concentration has decreased due to the successful expansion of the foreign-owned and medium-sized banks<sup>2</sup>. The balance of power in the banking system which held sway at the end of the first decade of two-tier banking will be expected to readjust according to growing competition for larger market shares. According to surveys, a shift from the moderate deconcentration will emerge and the few large banks (from the group of the medium-sized and the foreign-owned ones) with considerable financial standing will dominate in the retail market. Besides these, 10-15 banks will play an important role in the banking system. (Table 2)

**REGIONAL STRUCTURE OF THE  
 HUNGARIAN BANKING NETWORK**

Surveying the diffusion of the banking system by means of its geographical location and settlement hierarchy is very important.

At the birth of the two-tier banking system the network was characterised by a certain spatial balance due to the evenly-allocated branches of the OTP Bank (National Savings Bank), located in more than 270 settlements. After the foundation of the new commercial banks significant spatial asymmetry occurred within the country since cer-

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**Table 2**  
*Annual balance sheet footings and number of employees in the Hungarian banking, 1991-1996*

	Date of foundation	Ownership	Number of branches	Balance sheet footings (million HUF)				Number of employees		
				1991	1993	1995	1996	1991	1993	1995
<i>Big banks</i>										
1. OTP	1949	HT	423	669 599	830 958	1 072 777	1 256 085	12 659	14 367	..
2. Postabank	1988	HT	41	89 863	168 085	269 632	378 718	987	1 472	2 173
3. KIBB	1987	K	174	214 234	231 723	342 294	360 003	3 891	4 112	3 837
4. MKB	1950	KT	20	238 319	238 293	330 516	347 901	1 500	1 512	1 333
5. MHB <sup>a</sup>	1987	K	78	321 824	357 463	246 091	250 873	4 180	4 322	3 095
6. Budapest Bank	1986	KT	74	146 067	156 605	212 931	225 380	2 085	2 952	2 831
7. CIB	1979	KT	0	35 000	76 010	144 113	175 021	267	184	174
8. CIB Hungária	1988	KT	12	26 341	45 135	126 424	134 712	..	168	268
9. Creditanstalt	1990	K	12	28 400	27 202	77 074	116 119	111	193	343
<i>Medium-sized banks</i>										
10. Raiffeisen Unicbank	1986	KT	9	28 450	36 083	77 117	109 630	88	152	309
11. Mezőbank <sup>b</sup>	1986	K	81	29 984	34 544	80 883	97 152	401	657	720
12. Citibank	1985	K	0	35 248	36 474	59 628	93 196	97	150	216
13. MFB Rt.	1991	H	0	–	20 468	57 805	91 921	–	117	184
14. IEB	1980	KV	14	35 090	40 540	62 387	91 117	202	323	417
15. ING Bank	1991	K	14	2 564	20 283	64 558	84 005	..	80	..
16. Commerzbank	1993	K	0	–	11 027	57 994	75 270	–	40	74
17. ÁÉB	1922	K	8	19 766	26 148	37 970	71 657	270	294	279
18. Takarékbank	1989	H	22	36 760	37 323	40 360	66 789	281	509	613
19. BNP- Dresdner Bank	1990	K	0	9 836	15 014	35 252	50 639	..	90	115
20. Credit Lyonnais	1992	K	0	–	12 577	28 627	42 160	..	..	..
21. HYPO-Bank	1993	K	5	–	4 831	22 349	40 198	–	30	160
22. DAEWOO Bank	1989	K	0	11 291	12 854	25 048	38 774	44	54	76
23. ABN-Amro <sup>c</sup>	1993	K	0	–	5 566	29 826	38 430	–	19	50
24. EKB	1991	K	4	6 612	8 700	23 081	33 631	34	46	110
25. WestLB Hungária	1985	KT	1	12 890	9 186	20 372	31 975	113	122	110
26. Pénzügyi Központ	1983	H	3	–	15 364	24 001	29 768	–	354	244
27. Polgári Bank	1993	H	15	–	2 900	27 069	29 764	–	210	291
28. Konzumbank	1986	H	25	16 016	11 725	12 894	27 590	179	332	354
<i>Small banks</i>										
29. Realbank	1989	H	29	10 200	13 948	16 622	20 704	63	..	..
30. Volksbank	1992	K	5	–	1 227	9 356	15 579	–	24	52
31. Merkantil Bank	1988	H	3	4 508	5 530	11 772	13 689	66	90	93
32. EXIMBANK	1994	H	0	–	1 267	5 196	12 134	–	..	66
33. Corvinbank	1984	H	6	10 449	18 375	12 558	11 888	91	173	193
34. Porsche Bank	1994	K	0	–	500	7 834	7 072	–	..	52
35. Opel Bank							4 630			
36. Hanwha Bank	1990	KT	1	4 206	5 613	4 551	4 371	65	74	59
37. Kvantum Bank	1991	H	0	1 036	1 050	3 164	3 581	16	39	68
38. Deutsche Bank							2 994			
39. IC Bank	1993	K	0	–	979	1 087	2 330	–	..	22
40. Rákóczi Bank	1992	H	0	–	1 056	1 072	1 689	–	18	22
41. Nomura	1991	K	0	1 042	1 037	780	774	8	11	10

*H* – Hungarian ownership    *HT* – majority of Hungarian shares  
*K* – foreign ownership        *KT* – majority of foreign shares  
*KV* – joint-venture with foreign ownership

<sup>a</sup> State of development at the end of 1996

<sup>b</sup> In 1995 together with balance sheet footings of Agrobank

<sup>c</sup> ABN-Amro Bank purchased 89% of MHB in 1996

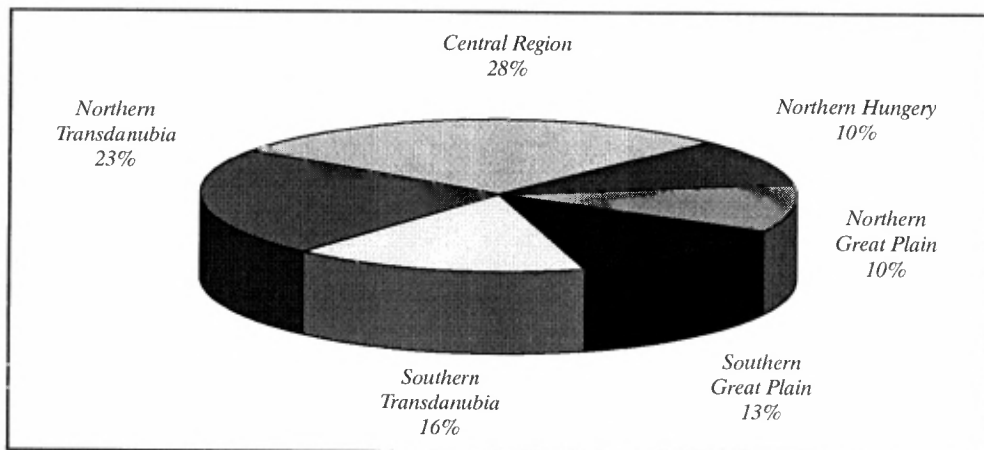
tain banks were missing from particular regions and county seats: KHB (Commercial Credit Bank) dominates in the Great Plain region, MHB (National Credit Bank) in Northern Transdanubia and BB (Budapest Bank) around Budapest.

The spatial appearance and the regional diffusion of the new branches of banks reflected the recent Hungarian economic processes:

- The prevailing majority of economic associations, within it the joint-venture companies and the accumulated capital outside Budapest flowed into the Transdanubian region, firstly into the north-western part.
- The structure of diffusion of the banking network had followed this spatial pattern for the first time by the beginning of the 1990s. At that time banks were interested mainly in building up branches in the Transdanubian region. This was evident because the largest unexploited territories of financial services were situated in Western Hungary. (*Figure 3*)
- Significant differences among the greater regions had practically evened out, except in Northern Hungary, by 1990, and the disadvantage of the Transdanubian region came to the end. From the mid-1990s, after saturation of Transdanubia, the larger cities of Eastern and Southern Hungary became the main targets of branch network expansion.

There were significant differences behind the well-balanced greater regions concerning network density within the regions and counties. In some counties the number of new branches exceeded ten between 1978-1990 (Győr-Moson-Sopron, Baranya, Hajdú-Bihar), while in other places only a few branches were opened (Fejér, Komárom-Esztergom, Tolna) and in some counties exclusively planted only in the county seats (Borsod, Fejér, Szabolcs-Szatmár-Bereg). An extreme exception was Esztergom-Komárom county where no branch was opened between 1987-1990 in

**Figure 3**  
*Distribution of banking network among Hungarian regions, 1996*





Tatabánya, the county seat, where economic depression affected its heavy industrial background. For instance, during the short period between 1995-1997 there was no increase of the branches in North-Western Transdanubia, as it was viewed as a saturated region.

A general characteristic of the period between 1992-1996 was the growing importance of Budapest in the expansion of the branch network (319 bank offices made up 26% of the national network in 1997). All banks starting to open new branches have opened 2-3 new offices in the capital city in the past five years, and last year 20 banks had branches there.

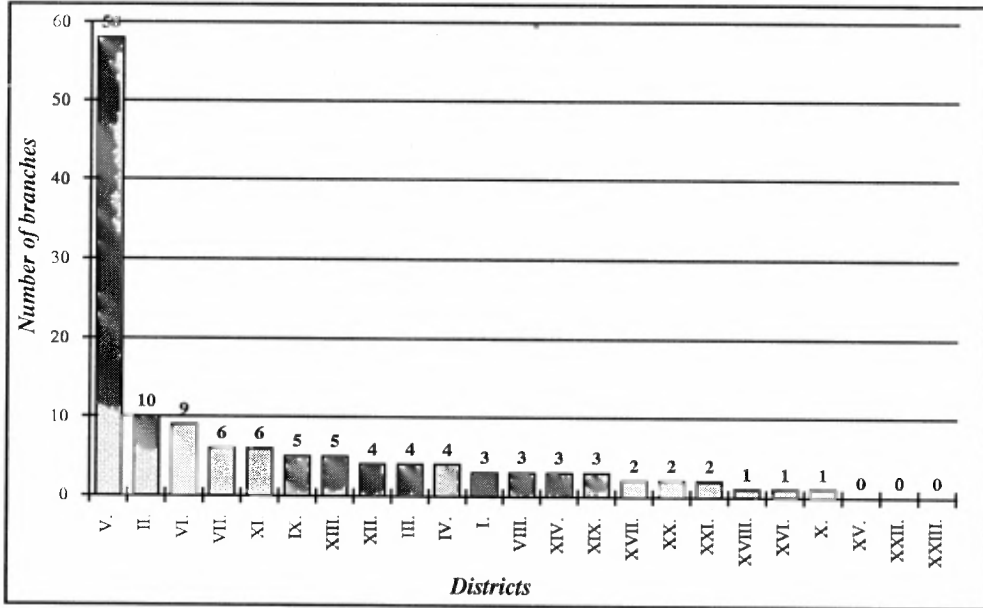
Within Budapest most of the principal offices of banks are based in the inner districts. The spatial concentration of the institutions gives a strong impetus to the formation of the central business district, where the office buildings of banks became an important functional-morphological element of the townscape. In 1990 about two thirds of the financial organisations were based in the 5th District, namely in the core area of the city centre itself which is still the most popular domicile for new banks. By the end of the 1990s business (financial) functions of the 5th District had become saturated and a few years ago the financial organisations started to diffuse towards the surrounding inner city districts. Despite the expansion of banks the low density of network in Budapest is surprising, namely one office per 7,758 inhabitants (15,000 without the OTP). This fact unambiguously demonstrates the low level of the extension of the banking network in the capital city. The lack of banking services is more striking in the outer area of Budapest, resulting in overcrowded city centre branches. (*Figures 4, 5*)

In Hungary the number of banking institutions is 1,319, together with 1,800 co-operative savings banks, stands at about 3,100. Taking the figures of the network density into account, there is one office per 3,200 inhabitants, which is still a much lower density than in the Western European counterparts, where there is one bank per 1,400-1,500 inhabitants. In spite of the boom in the foundation of new branches (last year a branch office opening ceremony took place every week on average) mainly by the foreign and joint-ventures banks. These banks still do not have enough branches in Hungary, although spectacular progress has been made, especially since 1996. 24 banks had a nation-wide branch network in 1997. (*Figure 6*)

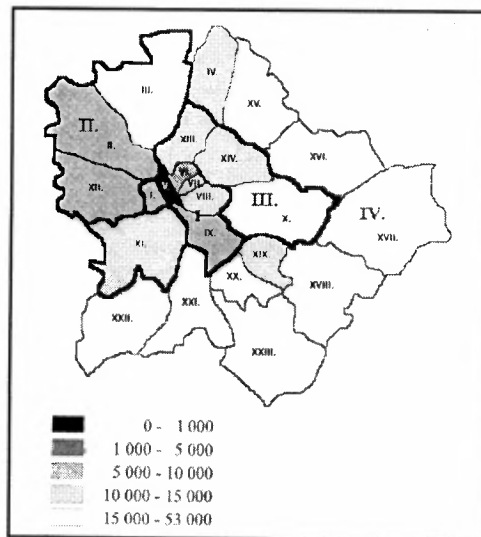
Surveying the banking network according to the network density figures we can find a few counties with lower density of banks. Szabolcs-Szatmár-Bereg and Pest counties are the most unsupplied areas, accounting for half of the national average in 1995. In the case of the former, its economic and geographical situation, the activity of entrepreneurs, the low level of foreign capital inflow etc. would be the explanation for the smaller interest of the banks. In the case of Pest county, the capital city causes backwash effects which influence the development of the banking network. Relative to population, Hajdú-Bihar, Borsod-Abaúj-Zemplén, Komárom-Esztergom, Nógrád and Fejér counties were also badly supplied by banking services. These counties could be the main target areas of expansion in the near future.

Surveying the distribution of the banking network according to the settlement types is more expedient than investigating at county level; all the more so as banking institu-

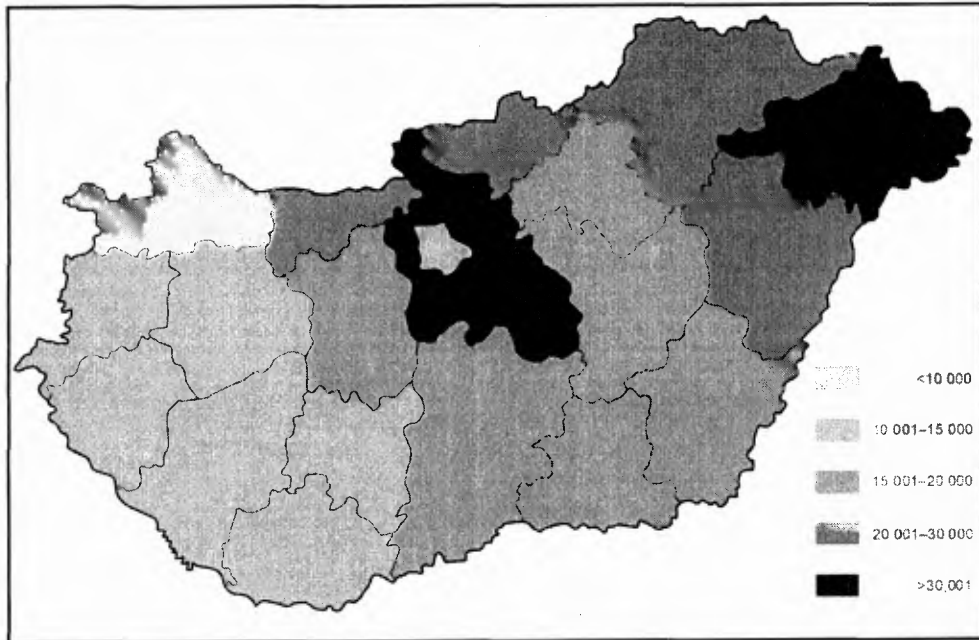
**Figure 4**  
 Spatial distribution of branches in Budapest, 1996  
 (without branches of OTP and mutual savings banks)



**Figure 5**  
 Banking network density of Budapest  
 (number of inhabitants per office)



**Figure 6**  
*Density of the Hungarian banking network, 1995*  
*(number of inhabitants per office)*



tions have more links to the cities and towns, therefore capital flows is an important indicator of the different urban processes. Since by the beginning of the 1990s the number of branches had exceeded the number of larger cities which had been the main targets of the earlier expanding banks, consequently these banks turned their interest towards the smaller settlements. (Table 3)

The first branches in villages were also opened. The selected villages usually have some special function: Piliscsaba, where the IEB (Inter-Európa Bank) operates an office, is located in the agglomeration of Budapest and is the seat of the Catholic University. The German-owned Volksbank has been operating a branch in Pilisvörösvár, a village with a Swabian background.

Those banks just recently started to develop their network – most of them are foreign owned – situating themselves solely in regional centres. As a consequence of this, certain larger cities (Pécs, Győr, Szeged, Székesfehérvár), despite not being seats of a regional bank, have been started to play significant roles in the operation of financial services in which different organisations of the financial sector (banks, insurance companies, consulting) attract each other mutually. This also induces increased competition in the local-regional market.

At the beginning of the 1990s the banking network was rather more polarised, both hierarchically and regionally, than nowadays. A more developed network existed in the

**Table 3**  
*Banking services in Hungarian cities, 1996*

	1	2	3	4	5	6	7	8	9	10
<b>Hungary</b>	10 212 300	255 043	305	3 216	630	3 175	16 210	79	405	249.7
<b>Budapest</b>	1 906 798	108 865	64	253	125	7 537	15 254	430	871	570.9
<b>Countryside</b>	8 305 502	146 178	278	2 548	505	3 260	16 447	57	289	176.0
<b>Cities - altogether</b>	2 082 932	61 951	...	436	274	4 777	7 602	142	226	297.4
<b>- in Danubian counties*</b>	<b>736 898</b>	<b>22 225</b>	<b>127</b>	<b>199</b>	<b>305</b>	<b>4 107</b>	<b>8 215</b>	<b>118</b>	<b>230</b>	<b>296</b>
<b>Debrecen</b>	214 228	5 481	20	29	16	7 387	13 389	189	343	255.8
<b>Dunaiújváros</b>	57 970	1 508	5	8	4	7 246	14 493	189	377	260.1
<b>Hódmezővásárhely</b>	50 631	4 374	5	8	4	6 329	12 658	547	1 094	863.9
<b>Miskolc</b>	193 905	4 280	19	31	18	6 255	10 773	138	238	220.7
<b>Tatabánya</b>	75 258	1 679	9	13	5	5 789	15 052	129	336	223.1
<b>Salgótarján</b>	48 488	1 060	8	9	6	5 388	8 081	118	177	218.6
<b>Szolnok</b>	81 336	2 213	10	16	10	5 084	8 134	138	221	272.1
<b>Nagykanizsa</b>	55 624	875	6	12	6	4 635	9 271	73	146	157.3
<b>Nyíregyháza</b>	119 317	3 650	16	26	14	4 589	8 523	140	261	305.9
<b>Székesfehérvár</b>	108 543	3 625	17	25	17	4 342	6 385	145	213	334.0
<b>Kaposvár</b>	70 529	2 135	11	17	10	4 149	7 053	126	214	302.7
<b>Szombathely</b>	84 745	1 996	16	22	12	3 852	7 062	91	166	235.5
<b>Szeged</b>	173 820	7 267	21	46	20	3 779	8 691	158	363	418.1
<b>Pécs</b>	164 872	5 595	25	45	23	3 664	7 168	124	243	339.4
<b>Kecskemét</b>	108 345	3 413	19	30	15	3 612	7 223	114	228	315.0
<b>Zalaegerszeg</b>	62 077	1 663	13	19	14	3 267	4 434	88	119	267.9
<b>Győr</b>	130 244	3 725	26	43	23	3 029	5 663	87	162	286.0
<b>Eger</b>	60 445	1 345	15	20	10	3 022	6 045	67	135	222.5
<b>Békéscsaba</b>	67 621	1 638	13	23	13	2 940	5 202	71	126	242.2
<b>Sopron</b>	54 311	1 338	12	19	9	2 858	6 035	70	149	246.4
<b>Veszprém</b>	63 553	1 749	14	25	15	2 542	4 237	70	117	275.2
<b>Szekeşzárd</b>	37 070	1 342	12	16	10	2 317	3 707	84	134	362.0

\* *Dunaiújváros, Tatabánya, Székesfehérvár, Pécs, Kecskemét, Győr, Sopron, Szekeşzárd*

1 *Population on January 1, 1996*

2 *Number of enterprises with legal and non-legal entity*

3 *Number of banks*

4 *Number of all institutions of banking network*

5 *Number of all institutions of banking network counted without OTP Bank and mutual savings banks*

6 *Network density 1: population decline per branch*

7 *Network density 2: population decline per branch without the branches of OTP Bank and mutual savings banks*

8 *Network density 3: enterprise decline per branch*

9 *Network density 4: enterprise decline per branch without the branches of OTP Bank and mutual savings banks*

10 *Enterpreneurial activity: enterprise decline per population of 10,000*

Sources: *Statistical Yearbook 1994*

*Hungarian Almanac of Financial and Capital Markets 1995–1996*

county seats and in the cities of Western Hungary (which were targets of foreign companies and banks); while in Northern Hungary and in the northern part of the Great Plain the banking network is less developed than in Pest county, where the central role of Budapest counterbalances its disadvantage. In recent years a shift has taken place, levelling out the expansion of the banking network in favour of the eastern parts of the country. During these years the number of branches in the cities of Eastern and Southern Hungary increased more rapidly than in the western counterparts which were previously the most saturated parts of the country, considering the number of branches. Two years ago, Győr, Pécs, and Székesfehérvár were considered the largest financial centres outside Budapest, while recently Miskolc gained the leading position in the number of branches (37), followed by Győr and Kecskemét (each with 32 branch offices), then Pécs and Szeged (31-31), and finally by Debrecen (28)<sup>3</sup>.

In conclusion it can be said that the network building expansion of branches initially followed the pattern of the spatial-economic division of the country, as banks mainly were opening branches in Western Hungary. Since the mid-1990s, owing to the process of nivellation, banks have started their expansion towards the eastern and southern parts of the country along the urban hierarchy<sup>4</sup>. (Figures 7, 8)

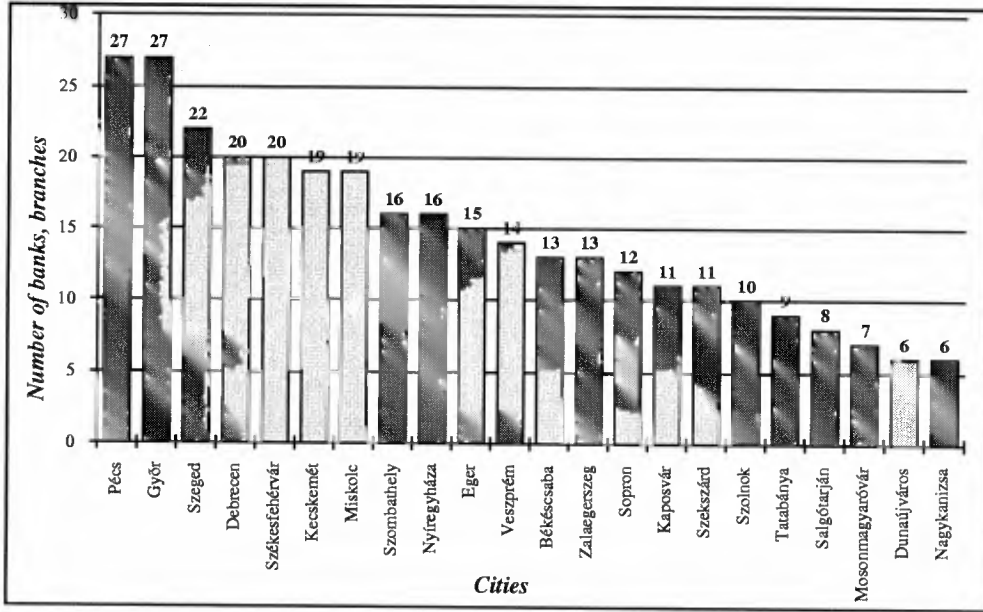
The next group of cities attracting banks consists of the other cities around the population mark of 100,000: Székesfehérvár, Nyíregyháza, Szombathely. In the third city group 8-11 banks operate 9-15 branches: Veszprém, Kaposvár, Békéscsaba, Eger, Szolnok, Zalaegerszeg and finally Sopron figure in this group.

The banking sector shows little interest in certain larger cities: Salgótarján (6 banks – 6 branches), Tatabánya (6 banks – 5 branches), Szekszárd (9 banks – 10 branches), Nagykanizsa (4 banks – 6 branches), Dunaújváros (7 banks – 5 branches) and Hódmezővásárhely (4 banks – 4 branches). A few smaller towns have stronger financial functions concerning the number of branches. (Mosonmagyaróvár, which is situated alongside the innovational axis between Budapest and Vienna, has 6 banks, and in the Danubian region in Baja, Kalocsa and Vác 4-4 banks operate.)

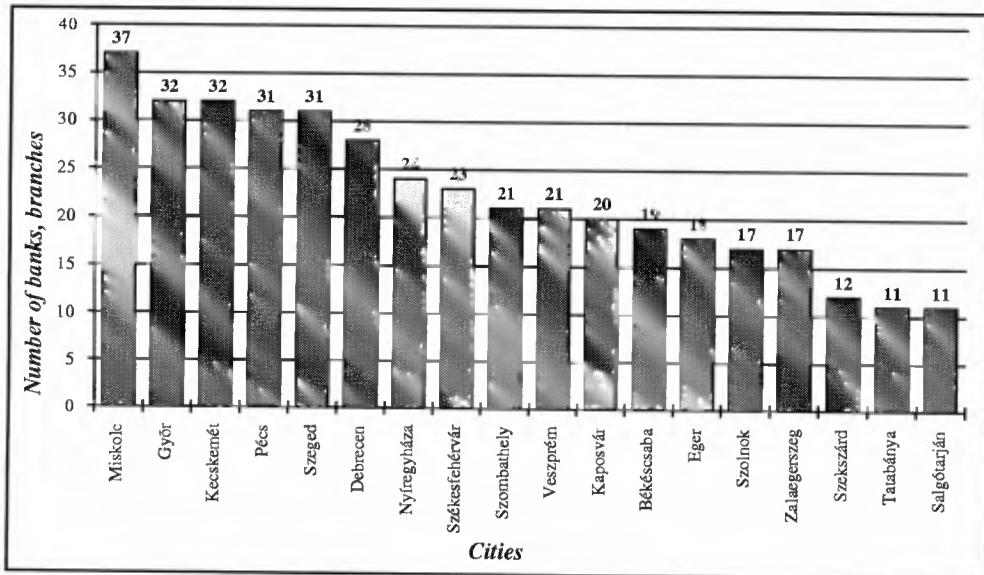
In conclusion it can be seen that different banks are situated on different levels of network construction in the recent period of development. The share of the larger cities from the banking network intensively increased from 35-40% to about 50% (with Budapest 66%) between 1987 and the early 1990s owing to the fact that at least a dozen new banks entered the market and started their network development. Bankruptcies and the rationalisation policy of network development in the following period mainly affected these larger cities as the major beneficiaries of the boom in banking expansion. Despite several new branches opening, the proportion of larger cities within the banking network fell to 43% (or 63% including Budapest), parallel with the network diffusion towards the smaller settlements.

Taking the expansion of the banking network into account, some experts believe that the spread of electronic home banking will counterbalance the traditional way of branch office building. According to others, whose opinion I share, there is a brighter future for the traditional expansion of the branch network since customers are much more devoted to a personal style of administration and rely more on branch offices.

**Figure 7**  
 Banking network of Hungarian cities, 1996



**Figure 8**  
 Banking network of Hungarian county seats, 1998



Despite the probability that virtual banking will be widespread in the future, building a more cost-intensive branch network is still very important. In addition, about 40% of the population has as yet no contact with banking. The figures for the year 1998 justify both these theories of the future prospects of banking.

### SUMMARY

In surveying the spatial characteristics of the Hungarian banking system, it can be stated that the economic changes are very much dependent on the financial services which reflect the processes of economic transformation. Financial services became the key sector of the business services differentiated by spatial and regional development characteristics. The overall concentration of financial services in Budapest is a direct result of the general concentration of business sectors into metropolitan centres. As the consequences of rapid restructuring and modernisation of the economy of Budapest, the capital city of Hungary has become the most important innovation centre of the region, with an important bridgehead role in foreign capital inflow and investment within the CEE countries.

The question is whether or not Budapest will become a regional financial centre. According to a number of banking experts Budapest could only hope to successfully apply for the position of a subordinated offshore-style regional financial centre. Subject to these conditions, services require a smaller amount of capital and highly qualified employees will come into prominence. To carry out all this, it is necessary to strengthen the banking system with businesslike state intervention, but the exact date of the integration into the European Union may influence the development of the Hungarian banking system and the international role of Budapest, too.

In evaluating the competitiveness of the Hungarian banking system, it can be said that the banking sector has been strengthened since 1994 and it has become a more profitable sector. However, progress in banking is significant only compared to the previous state of the banking system: by international standards, the quality of the sector is still very low. The proportion of outstanding claims, despite the significant decrease, is still higher than in any country of the European Union.

Despite the general recovery in banking, the sector has remained polarised. In 1995 70% of profit after tax was produced by banks with foreign ownership that at that time accounted for a quarter of the market. Their profitability and efficiency were that of banks with Hungarian ownership. Following the crisis, bankruptcies, consolidation and the redistribution of the banking market was begun and banks with backgrounds of foreign ownership have gained stronger positions. The strengthened competition decreased the interest margin and put the value of the non-interest incomes, such as charges and premiums, within the revenues of banks.

In summarising the experiences of Hungarian banking it can be said that the openness of this sector compared to others contributed more to the modernisation and competitiveness of the Hungarian banking system. Until now the activity of foreign

banks has been dependent on their subsidiary companies, which have to become established in Hungary before starting their operations. Recently the question has been whether the Hungarian banking system is ready to liberalise itself in order to fully open its market and stand its ground in the future competition within the European Union.

### NOTES

- <sup>1</sup> By the end of 1997, IEB, MKB, CIB, Unicbank and Creditanstalt (Bank Austria) had opened quite a few new offices in the provinces. ING Bank acquired 14 offices of Dunabank and HYPO-Bank increased its branches by 14 offices within 18 months.
- <sup>2</sup> While the share of the five largest banks in 1990 was 83% of the total banking sector assets, by 1997 the five largest and oldest banks' share had decreased to 54%, and the ten largest banks, including newly established and more dynamic institutions, accounted for 72% of banking assets.
- <sup>3</sup> In other banking institutions such as the State Treasury, representative branches of NBH, regional headquarters, single branches, representative or cash office, correct spatial differences derive from the number of banks or branches. Regional centres (Győr, Pécs) and greater county seats (Kecskemét, Székesfehérvár) usually have the complete range of these institutions.
- <sup>4</sup> As regards number of branches, 17 banks operate 23 branches in Győr but together with OTP and the representative of Raiffeisen Landesbank of Burgenland, the number of branches was 43. In Pécs similarly 17 banks appeared with 25 branches, but the number of branches stood at 46, including the OTP branches (6) and mutual savings banks (17). Concentration of services is higher here because of the central position of Pécs extending over South Transdanubia. There are several reasons why banks open branches in Pécs. Not only its economic environment but the highly qualified population with a multicultural background, and historical inner city areas with touristic interests provides a distinguished urban milieu for branch development.

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