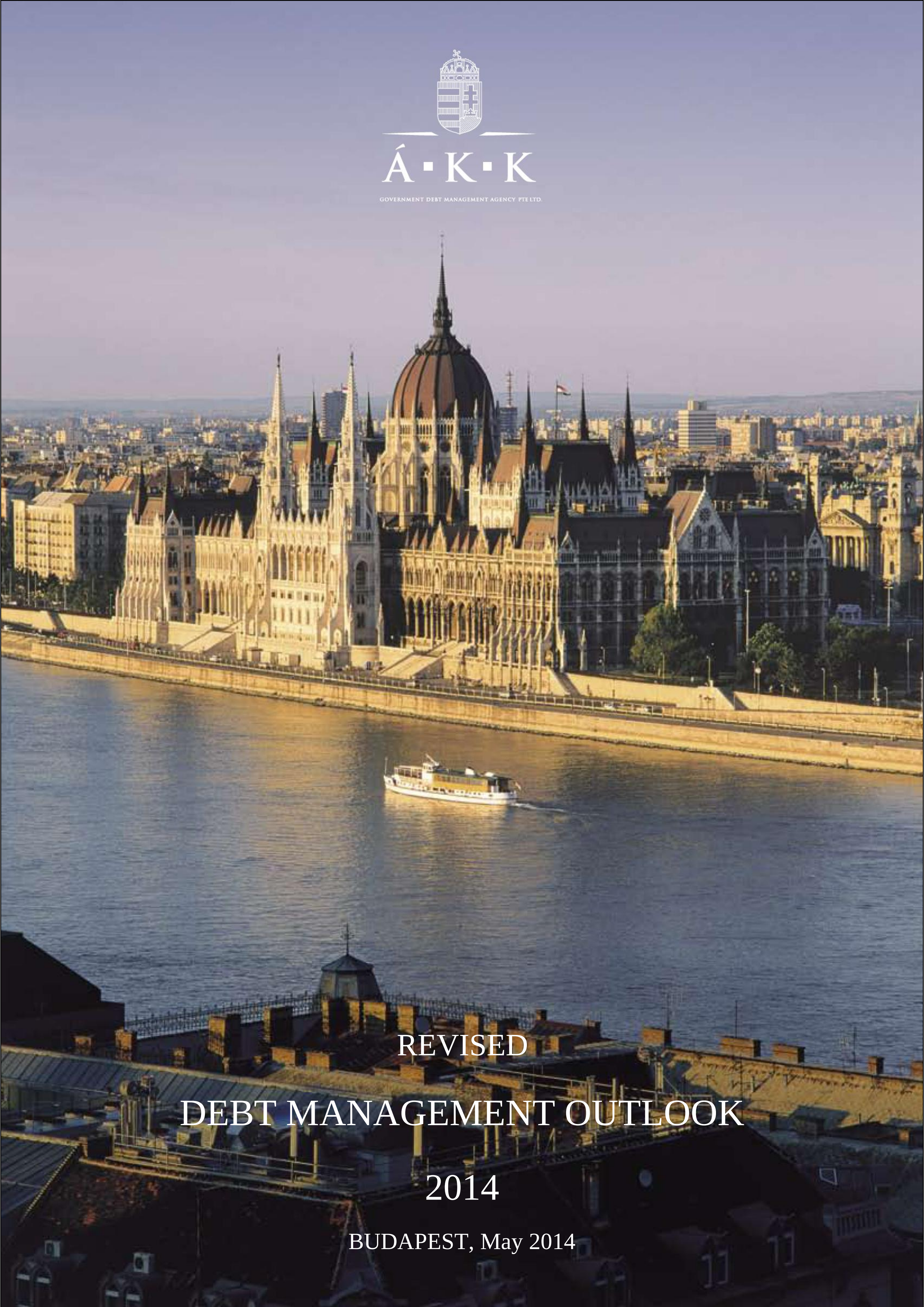
Á▪K▪K

GOVERNMENT DEBT MANAGEMENT AGENCY PTE LTD.



REVISED

# DEBT MANAGEMENT OUTLOOK

# 2014

BUDAPEST, May 2014

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## 1. Net financing requirements in 2014

The net financing requirements is the sum of the deficit of the central government and the other net financing requirements. The deficit of the central government on a ***cash-flow basis*** is planned at **HUF 985 billion**, equaling to 3.2% of the GDP.

The total cash-flow based net financing requirement for the year 2014 – that comprises of the deficit of the central government and other net financing requirements (projected net-financing need of EU transfers, capital operations) – will amount to **HUF 1,192 billion**. The net financing requirement has increased by the change in the other net financing requirement of HUF 207 billion from the January 2014 plan, which forecast total net financing requirement of HUF 985 billion only.

**Cash-flow based financing requirements in 2014 (plan)**

| | **HUF billion** |
|---|---|
| Balance of the central government budget | -962 |
| Balance of the social security funds | 0 |
| Balance of the extra-budgetary funds | -23 |
| **Net financing requirement of the central government** | **-985** |
| Other net financing requirements(EU transfer, capital operations) | -207 |
| **Total net financing requirement** | **-1,192** |

## 2. Government debt redemptions

The total amount of government debt redemptions in 2014 is planned at **HUF 6,679 billion**.[1] The redemption of domestic currency debt will amount to **HUF 4,694 billion**, of which domestic bonds account for HUF 1,220 billion (including increased bond buy-backs), discount T-bills for HUF 1,905 billion, retail government securities for HUF 1,353 billion and HUF loans for HUF 216 billion (including redemptions of debt assumed from local authorities in February).

Foreign currency debt redemptions are expected to be **HUF 1,985 billion** (**EUR 6.4 billion**). International foreign currency denominated bond redemptions will amount to EUR 2.7 billion, European Commission's loan redemptions will be EUR 2.0 billion, buy-back of the domestic euro denominated is planned at EUR 0.9 billion, while the redemption of IFI and other loans will amount to EUR 0.8 billion.

[1] ÁKK provides gross issuance and redemption data according to the methodology recommended by OECD which takes redemptions of short-term securities - typically Treasury bills - only once into account avoiding multiple counting.

| | HUF billion | In EUR billion |
|---|---|---|
| **Domestic redemptions** | 4,694 | 15.2 |
| T-bonds | 1,220 | 4.0 |
| Retail securities | 1,353 | 4.4 |
| Discount T-bills | 1,905 | 6.2 |
| Loans | 216 | 0.7 |
| **FX redemptions** | 1,985 | 6.4 |
| International bonds | 873 | 2.7 |
| EC loans | 616 | 2.0 |
| Domestic FX bond | 260 | 0.9 |
| IFI and other loans | 236 | 0.8 |
| **Total** | 6,679 | 21.7 |

(at 308 HUF/EUR exchange rate)

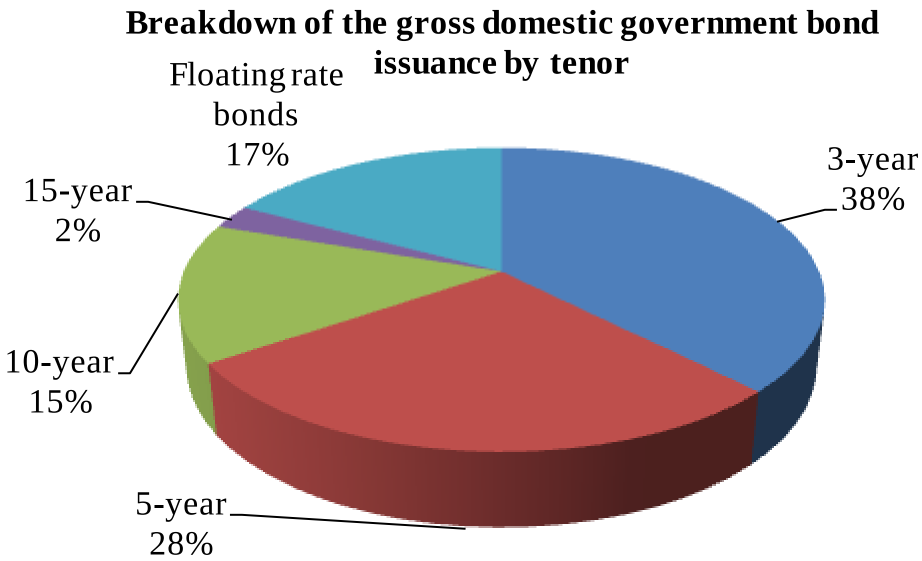
## 3. Gross issuance

Total gross issuance is planned at **HUF 7,920 billion** in 2014, of which 86 per cent (or **HUF 6,820 billion**) will be in domestic currency and 14 per cent (**HUF 1,100 billion** or EUR 3.6 billion) will be in foreign currencies. The revision of the financing plan is based on the ample demand for domestic securities which makes it possible to increase domestic issuance. Higher domestic issuance can replace issuance in foreign currencies, which results in a faster reduction of the foreign currency part of Hungarian public debt than it is envisaged by the public debt management strategy.

| | HUF billion | In EUR (billion) |
|---|---|---|
| Gross issuance | | |
| **Domestic debt** | 6,820 | 22.1 |
| T-bonds | 2,434 | 7.9 |
| Retail securities | 1,960 | 6.4 |
| Discount T-bills | 2,202 | 7.1 |
| Loans | 224 | 0.7 |
| **FX currency debt** | 1,100 | 3.6 |
| International bonds | 679 | 2.2 |
| Domestic FX bonds* | 375 | 1.2 |
| IFIs loans | 46 | 0.1 |
| **Total** | 7,920 | 25.7 |

* Residence Bond and Premium Euro Hungarian Government Bond

**HUF 2,321 billion** worth of Hungarian Forint government bonds will be offered at auctions (excluding switch auctions), with a breakdown by tenor similar to that of the previous year. But the share of floating rate bond issuance will increase in line with the increased demand of domestic banks.




The planned issuance of HUF-denominated government bonds are as follows:

| Tenor | Issuance (HUF billion) |
|---|---|
| 3-year (fixed) | 873 |
| Floating rate bonds | 398 |
| 5-year (fixed) | 646 |
| 10-year | 344 |
| 15-year | 60 |
| Total | 2,321 |

ÁKK has launched a new 3-year and a 10-year bond series, while for the 5-year tenor an off-the-run bond has been reopened and for the 15-year tenor the current benchmark bond continues to be offered. Based on expected demand for floaters ÁKK has issued a new floating rate bond linked to the Bubor. Floating rate bonds will be offered more frequently, biweekly together with the 1-year discount Treasury–bill. The issuance calendar includes only the dates of bond auctions. ÁKK will decide on the actual bond series and the amounts offered at the auctions after consultations with Primary Dealers prior to the auction. The current practice, i.e. regular simultaneous sales of the 3, 5 and 10-year bonds is likely to be continued in 2014 and the 15 year bond may be offered bi-monthly or quarterly replacing the 10 year bond. ÁKK will hold both bond-buyback and exchange auctions – similar to the practice followed since 2010 – in order to support a balanced government bond issuance as well as to manage the maturity profile and to reduce the refinancing risk of the bond portfolio.

ÁKK intends to drawdown project financing loans totaling EUR 0.85 billion of which EUR 0.7 billion is expected to be drawn in HUF).

Foreign currency issuance in the international capital markets is **HUF 679 billion (EUR 2.2 billion),** which was executed in the first quarter of the year. ÁKK intends to drawdown project financing loans totaling EUR 0.15 billion in foreign currency (the larger part of loan disbursements will be in HUF in order to further reduce the share of FX debt). The issuance of Residence Bond and the domestic Premium Euro Hungarian Government Bond is expected to amount to EUR 1.2 billion, out of which EUR 1 billion was already sold in the first quarter of the year. Foreign currency redemptions are covered partly by foreign currency issuance (including the pre-financing in 2013) and partly by domestic currency denominated issuance.

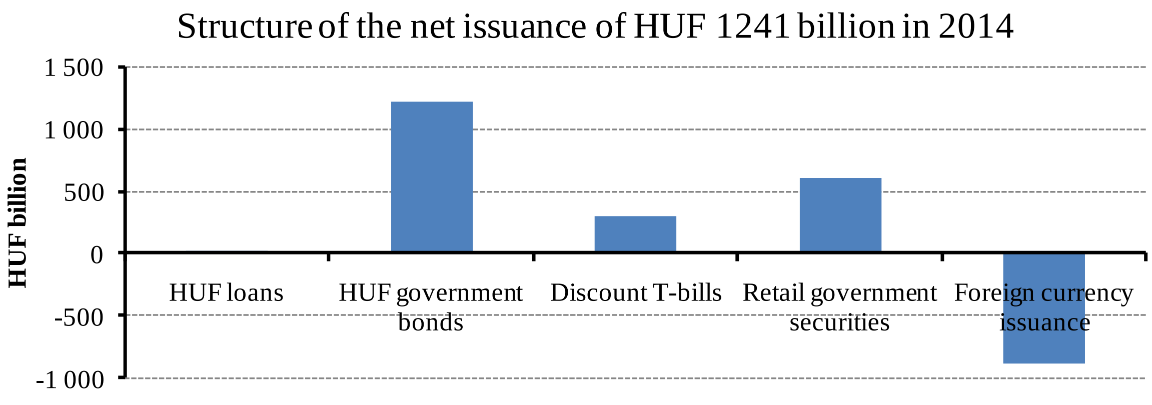
## 4. Net issuance

Net government debt issuance is planned in an amount of **HUF 1,241 billion**, out of which domestic debt issuance will reach **HUF 2,126 billion** (or 171 per cent of total), and net foreign currency borrowing will amount to **HUF -885 billion** (EUR -2.8 billion).

> *ÁKK will monitor closely the market and will decide on the amounts accepted at auctions according to the demand.*

Out of the net domestic issuance of government securities issuance net bond issuance will be HUF 1,214 billion and net discount T-bill issuance will amount to HUF 297 billion, while the stock of retail government securities will increase by HUF 607 billion. Net redemptions of HUF loans will be close to zero (HUF 8 billion).

The total foreign currency redemption will amount to EUR 6.4 billion. The gross foreign currency issuance is planned at EUR 3.6 billion, thus **the net foreign currency issuance is expected to amount EUR -2.8 billion in 2014**.



## 5. Debt management strategy

ÁKK's main objective is to finance the central government at the lowest costs in the long run taking account of risks. This objective is quantified by setting benchmarks, which are in part based on an optimal portfolio model using Value-at-Risk (VaR) and Cost-at-Risk (CaR) for taking into account both costs and risks. ÁKK has determined the following benchmark values for government debt management in 2014:

- ***Share of foreign currency debt:*** The share of the foreign currency denominated debt within the total central government debt should be below 45 per cent and declining. Declining foreign currency debt ratio can be reached by financing the net financing requirements from the domestic market. In case of ample demand for domestic securities a part of foreign currency debt issuance may be replaced by HUF issuance. The actual ratio of foreign currency debt was 40 per cent at the end of 2013. Due to the increased demand for domestic bonds, ÁKK has been able to finance a significant part of maturing foreign currency denominated debt from the domestic market.

- ***Currency mix of the foreign currency denominated debt:*** In order to mitigate cross-currency exchange rate risk, foreign currency obligations after swaps should be 100% in EUR, allowing for a 5% deviation from this target.

- ***Fixed / floater composition:*** Within the **HUF debt**, the share of the fixed rate elements should be in the range of 61-83%, that of floating rate debt, which includes all short-term debt, between 17% and 39%. Within the **foreign currency denominated debt**, the optimal share of fixed rate debt is 66%, with a 5% tolerance band.

- ***Duration:*** In order to keep an acceptable level of refinancing risk, the Macaulay duration of the HUF debt portfolio is targeted at 2.5 years +/- 0.5 year.

- ***Liquidity:*** So as to maintain a continuously safe level of cash funds in the Single Treasury Account (STA), a minimal target STA balance has been determined and ÁKK's objective is to keep the end-of-day STA balance over the minimal level. Due to international market risks ÁKK has increased substantially the level of cash funds in the Single Treasury Account.

In the case of the first five benchmark values ÁKK takes into account their 3-month moving average values, to avoid unnecessary reaction to one-off or temporary market movements that actually would not need a response in the medium or longer term.

## 6. Further information

This Debt Management Outlook was compiled based on information available by the middle of May 2014. The projected figures for 2014 may change according to the outturn of the financing needs and debt issuances. Even though the structure of financing may change compared to the plans, the issuance calendar is fixed (see next chapter), and ÁKK will not change the set of instruments used, its strategic objectives and its strategic behavior in the markets either.

ÁKK's website (www.akk.hu, www.gdma.hu) and its regular publications and reports (monthly and quarterly publications; monthly report on debt transactions) provide updated information on the financing needs, the debt transactions and the government debt. ÁKK also discloses until the 15th of each month the detailed domestic market issuance plan for the next 3 months, which shows the amounts to be issued for each tenor.

## 7. Issuance calendar

**Issuance calendar of fixed rate government bonds in 2014**

| Date of auction | Date of settlement |
|---|---|
| 09.01.2014 | 15.01.2014 |
| 23.01.2014 | 29.01.2014 |
| 06.02.2014 | 12.02.2014 |
| 20.02.2014 | 26.02.2014 |
| 06.03.2014 | 12.03.2014 |
| 20.03.2014 | 26.03.2014 |
| 03.04.2014 | 09.04.2014 |
| 17.04.2014 | 23.04.2014 |
| 30.04.2014 | 07.05.2014 |
| 15.05.2014 | 21.05.2014 |
| 29.05.2014 | 04.06.2014 |
| 12.06.2014 | 18.06.2014 |
| 26.06.2014 | 02.07.2014 |
| 10.07.2014 | 16.07.2014 |
| 24.07.2014 | 30.07.2014 |
| 07.08.2014 | 13.08.2014 |
| 21.08.2014 | 27.08.2014 |
| 04.09.2014 | 10.09.2014 |
| 18.09.2014 | 24.09.2014 |
| 02.10.2014 | 08.10.2014 |
| 16.10.2014 | 22.10.2014 |
| 30.10.2014 | 05.11.2014 |
| 13.11.2014 | 19.11.2014 |
| 27.11.2014 | 03.12.2014 |
| 11.12.2014 | 17.12.2014 |

**Issuance calendar of floating rate government bonds in 2014**

| Date of auction | Date of settlement |
|---|---|
| 16.01.2014 | 22.01.2014 |
| 13.02.2014 | 19.02.2014 |
| 13.03.2014 | 19.03.2014 |
| 27.03.2014 | 02.04.2014 |
| 10.04.2014 | 16.04.2014 |
| 24.04.2014 | 30.04.2014 |
| 08.05.2014 | 14.05.2014 |
| 22.05.2014 | 28.05.2014 |
| 05.06.2014 | 11.06.2014 |
| 19.06.2014 | 25.06.2014 |
| 03.07.2014 | 09.07.2014 |
| 17.07.2014 | 23.07.2014 |
| 31.07.2014 | 06.08.2014 |
| 14.08.2014 | 21.08.2014 |
| 28.08.2014 | 03.09.2014 |
| 11.09.2014 | 17.09.2014 |
| 25.09.2014 | 01.10.2014 |
| 09.10.2014 | 15.10.2014 |
| 06.11.2014 | 12.11.2014 |
| 20.11.2014 | 26.11.2014 |
| 04.12.2014 | 10.12.2014 |
| 18.12.2014 | 23.12.2014 |

**Issuance calendar of discount treasury bills in 2014**

**12-mont discount T-bills**

| Code | Date of auction | Date of settlement | Date of maturity |
|---|---|---|---|
| D141126 | 02.01.2014 | 08.01.2014 | 26.11.2014 |
| D141126 | 16.01.2014 | 22.01.2014 | 26.11.2014 |
| D150121 | 30.01.2014 | 05.02.2014 | 21.01.2015 |
| D150121 | 13.02.2014 | 19.02.2014 | 21.01.2015 |
| D150121 | 27.02.2014 | 05.03.2014 | 21.01.2015 |
| D150121 | 13.03.2014 | 19.03.2014 | 21.01.2015 |
| D150401 | 27.03.2014 | 02.04.2014 | 01.04.2015 |
| D150401 | 10.04.2014 | 16.04.2014 | 01.04.2015 |
| D150401 | 24.04.2014 | 30.04.2014 | 01.04.2015 |
| D150401 | 08.05.2014 | 14.05.2014 | 01.04.2015 |
| D150527 | 22.05.2014 | 28.05.2014 | 27.05.2015 |
| D150527 | 05.06.2014 | 11.06.2014 | 27.05.2015 |
| D150527 | 19.06.2014 | 25.06.2014 | 27.05.2015 |
| D150527 | 03.07.2014 | 09.07.2014 | 27.05.2015 |
| D150722 | 17.07.2014 | 23.07.2014 | 22.07.2015 |
| D150722 | 31.07.2014 | 06.08.2014 | 22.07.2015 |
| D150722 | 14.08.2014 | 20.08.2014 | 22.07.2015 |
| D150722 | 28.08.2014 | 03.09.2014 | 22.07.2015 |
| D150916 | 11.09.2014 | 17.09.2014 | 16.09.2015 |
| D150916 | 25.09.2014 | 01.10.2014 | 16.09.2015 |
| D150916 | 09.10.2014 | 15.10.2014 | 16.09.2015 |
| D150916 | 22.10.2014 | 29.10.2014 | 16.09.2015 |
| D151111 | 06.11.2014 | 12.11.2014 | 11.11.2015 |
| D151111 | 20.11.2014 | 26.11.2014 | 11.11.2015 |
| D151111 | 04.12.2014 | 10.12.2014 | 11.11.2015 |
| D151223 | 18.12.2014 | 23.12.2014 | 23.12.2015 |

**3-month discount T-bills are auctioned every Tuesday, settlement is on the Wednesday of the following week.**

**Liquidity discount T-bills are auctioned upon decision of the Issuer, generally on Monday with settlement on Wednesday.**