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GOVERNMENT DEBT MANAGEMENT AGENCY
PRIVATE COMPANY LIMITED BY SHARES

GOVERNMENT DEBT MANAGEMENT REPORT 2013

FOREWORD

The objective of this annual Government Debt Management Report of the Government Debt Management Agency Pte. Ltd. (ÁKK) is to inform investors and other stakeholders in the government securities market about the financing of the central government, to analyse the characteristics of the government debt and to describe the developments in the Hungarian government securities market in 2013.

2013 was an important year for public debt management since all loans from the International Monetary Fund were repaid before their final maturity. The repayment of these loans that were drawn in the period of 2008–9 was funded by the very successful domestic retail debt program and the higher than planned issuance of a new domestic euro denominated bond.

2013 was also a successful year for debt management since the public debt ratio continued to decline. According to EUROSTAT the public debt ratio decreased from 79.8 per cent to 79.3 per cent – a rare example nowadays in the European Union. Not only did indebtness decline, but the cost of funding as well: medium term bond yields fell from 6 per cent to about 5 per cent during the year, which means that the evolution of debt service costs supports the fiscal objectives of the government.

All in all, it is clear that the most important objectives for last year were achieved, which provides a solid grounding for the coming years of public debt management.

István Töröcskei
Chief Executive Officer

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GENERAL INFORMATION

Both deficit and debt data are preliminary until the Act on Final Accounts for the relevant year is approved by Parliament, which occurs usually during the second half of the following year. Fiscal data used in this report were still preliminary when this report was compiled.

Some of the data in this report are cash–flow based and some are accrual–based. When using the cash–flow approach, expenditures and revenues are accounted for the very period in which they are actually paid or received, regardless of the periods to which their economic content relates. Under the accrual approach on the other hand, the amount of an expenditure or revenue item related to several periods is divided up on a pro rata basis and allocated to the relevant periods.

ÁKK publishes data about government debt in accordance with Hungarian accounting standards, the principles of which are summarised as follows:

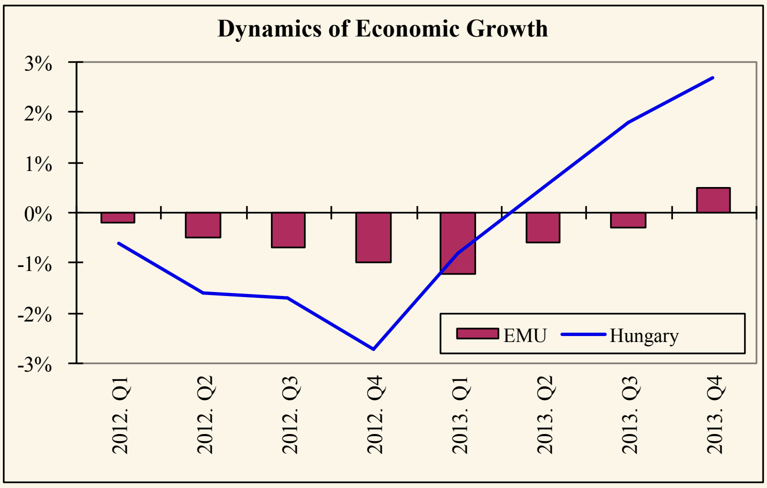
- Government bonds and retail government securities are recorded at nominal value.
- Discount treasury bills are recorded at the average sale price (at discount value), which is recalculated after every transaction involving the security concerned.
- Repo and reverse repo transactions actually increase or reduce outstanding government debt.
- Foreign currency debt is taken into account after swaps and is converted into HUF at the official exchange rate published by the National Bank of Hungary (NBH) at the end of the month or year in question.
- The debt published by ÁKK is the central government gross debt managed by ÁKK according to the Act No. CXCIV of 2011 on the Economic Stability of Hungary (i.e. it does not include either local government debt or the debt of state–owned enterprises and does not include debt under section 3 paragraph (1) c, d, and f, of the Stability Act and it is not a consolidated indicator (i.e. debt between various public sector subsystems is not netted)).

The debt data published by ÁKK in accordance with Hungarian and international accounting standards differs from the debt data used by EUROSTAT (the European Union's institute of statistics), which is calculated according to different principles and is essentially the result of statistical calculations. Public debt data is calculated and published in accordance with ESA '95 principles by the National Bank of Hungary.

I. MACROECONOMIC DEVELOPMENTS IN 2013

During 2013 most developed economies went through economic recovery. Major central banks (Fed, Bank of England, Bank of Japan, ECB) were loosening the monetary policy through quantitative easing and interest rate cuts. During the course of the year the Fed's announcements regarding the tapering of the quantitative easing were the most important market moving factor. In May Ben Bernanke, the chairman of the Fed announced that the tapering of the quantitative easing may begin earlier than expected. Following the announcement yields in the developed markets increased and spreads of risky assets grew. In the autumn – contrary to the announcement – the Fed actually did not start the tapering, which caused a partial correction of rates and risk premia in the markets.

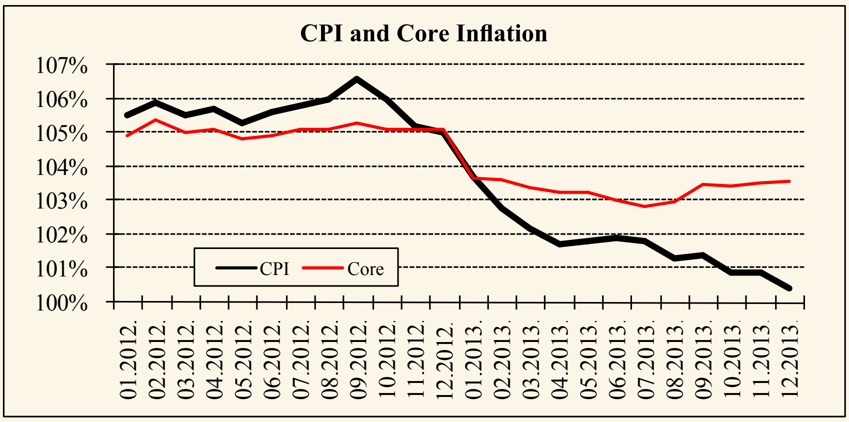
Economic Growth



Source: CSO, Eurostat

In the first quarter of 2013 the recession ended in Hungary and over the year, GDP grew by 1.2% compared to the previous year, which exceeded analysts' forecasts. The structure of economic growth also became healthier, almost exclusively export driven growth became more diversified as consumption and investments also contributed to economic growth. Consumption and investments increased by 0.5% and 2.1%, respectively; as a result domestic use grew by 0.8%. Net exports contributed 0.3 percentage points to economic growth, both exports and imports increased by 5.3%.

Inflation

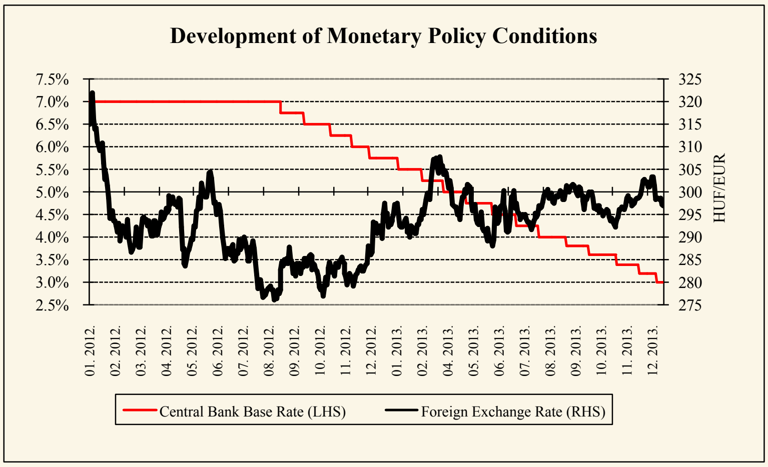


Source: CSO

Inflation declined from 3.7% in January 2013 to 0.4% in December 2013. The decrease of regulated prices significantly pushed inflation downwards. The food price dynamics slowed to 0.1% as a result of the good harvest in 2013 and favourable global food price developments. These two factors resulted in dropping headline inflation well below core inflation. The price level of clothing and durable goods fell partly as a result of weak domestic demand and the relatively stable forint. Inflation was subdued in case of fuels and services. The price level of alcohol and tobacco grew by 12.0% mainly as a result of indirect tax hikes. The yearly average inflation rate fell to 1.7% in 2013 from 5.7% in the previous year.

Monetary Conditions

During 2013 the forint weakened by 1.9% from 291.3 HUF/EUR to 296.9 HUF/EUR.



Source: NBH

The forint weakened from the 290 HUF/EUR level of early 2013 to the level of 308 HUF/EUR in March mainly as a result of uncertainties regarding monetary policy measures after the new leadership would take over the central bank. After the appointment of the new governor the NBH indicated that they would keep on conducting a cautious monetary policy and the forint recovered from its losses. The market reception of the NBH's Funding for Growth Programme was positive, and Hungarian macroeconomic data published in this period were favourable. By the end of May after the Fed's announcement on possible early tapering the forint weakened and fluctuated inside the band of 295–300 HUF/EUR for the rest of the year. Domestic developments (e.g. Hungary's exit of the EDP procedure and the gradual monetary easing resulting all time low central bank base rate) did not have a significant effect on the exchange rate. Fiscal policy remained tight, the Government repeatedly committed itself to the deficit target and took adequate measures to secure this target. However, the Fed announcement in autumn only had a short term positive effect on the forint. The main reasons were increasing political risks in Turkey and the Fed's December decision to start the tapering of the quantitative easing. Both events weighted on emerging market assets and weakened the forint.

Since the middle of 2012 the NBH had been able to reduce the central bank base rate continuously thanks to benign global liquidity conditions, decreasing inflation pressure in Hungary and improving risk assessment. Interest rate expectations weakened during the course of the year, market analysts lowered their forecasts for the bottom of the interest rate cycle. The Monetary Council cut the central bank base rate by 25 basis points each month from 7.0% in the middle of 2012 to 4.0% in July 2013. For the rest of the year the central bank base rate was cut by 20 basis points each month reaching 3.0% by the end of the year.

Fiscal Policy

In 2013 the ESA'95 deficit of the public sector was 2.5 per cent of GDP. The cash–flow based (GFS) general government deficit (excluding local governments) amounted to HUF 929 billion (equalling 3.2% of GDP for the year 2013). In 2013 the accrual based (ESA) general government deficit (including local governments) amounted to HUF 681 billion (equalling 2.3% of GDP for the year 2013) according to preliminary data. The financing need of the state for the year 2013 increased compared to the previous year.[1]

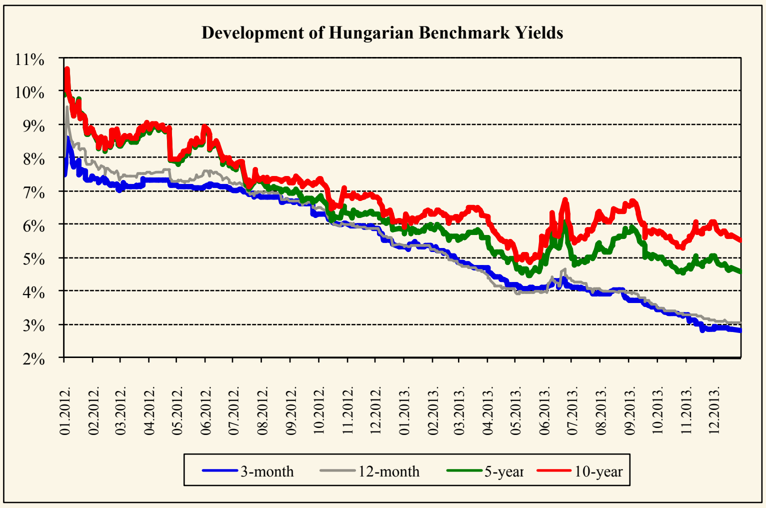
1 The components of the net financing need are described in detail in Chapter III.

Financing Position of the Economy

The households' savings to GDP ratio amounted to 5.4% in 2013. The net financing capacity of the corporate sector reached 3.8% in 2013 mainly as a result of weak investment activity. The economy of Hungary as a whole was a net lender towards the rest of the world in the amount of 7.4% of GDP. The current account posted a surplus of EUR 3.0 billion or 3.1% of GDP in 2013.

Forint yields

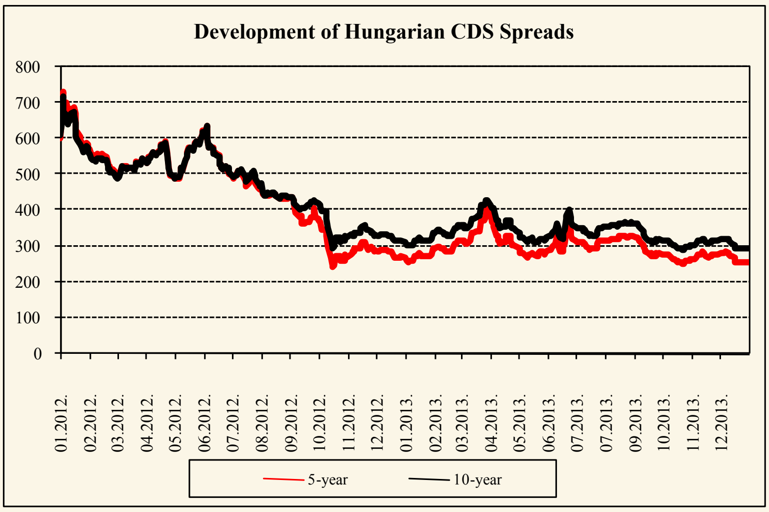
At the beginning of 2013 short–term yields fluctuated slightly above 5%, long–term yields fluctuated around 6%. The evolution of short term yields was driven by the monetary easing cycle of the National Bank of Hungary while long term yield movements were driven by international developments. By the end of the year the 3–month and 12–month reference yields declined to 2.9% and 3.0%, respectively; the 5–year and 10–year government bond yields stood at 4.7% and 5.6%, respectively.



Source: ÁKK

CDS Spreads

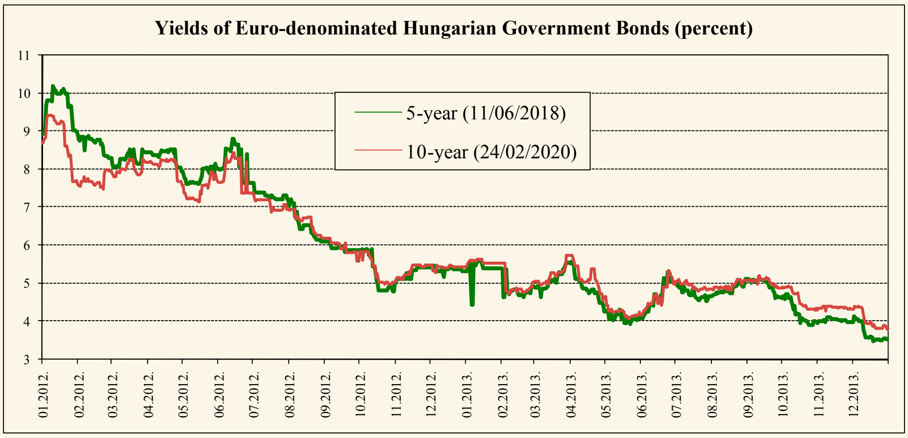
The 5–year CDS spread fluctuated between 250 and 300 basis points in the first quarter of the year and increased above 400 basis points until the end of March. By the end of April the CDS spread declined to 300 basis points, where it stayed for most part of the year. During the last months of the year the CDS spread fluctuated between 250 and 280 basis points.



Source: Reuters

Yields of Foreign Currency Denominated Bonds

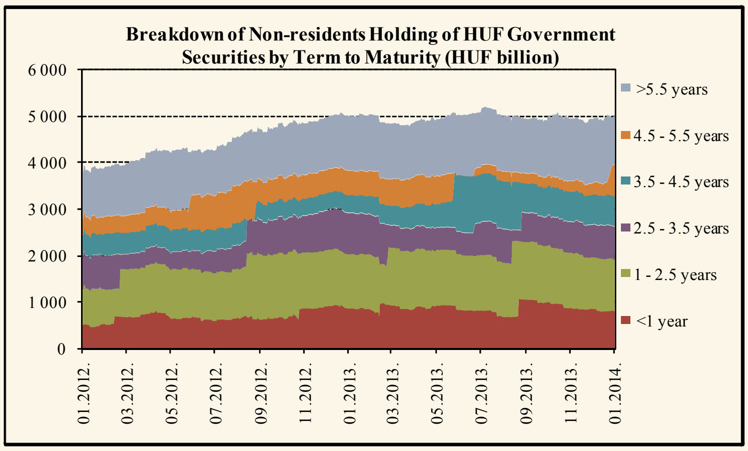
Besides CDS spreads the evolution of long–term yields in the European capital market played a significant role in the yield movements of euro–denominated Hungarian government bonds. The yield of the euro–denominated Hungarian government bond maturing in June 2018 decreased from 5.3% to 3.5% during 2013.



Source: Bloomberg

Government Securities Holdings of Foreign Investors

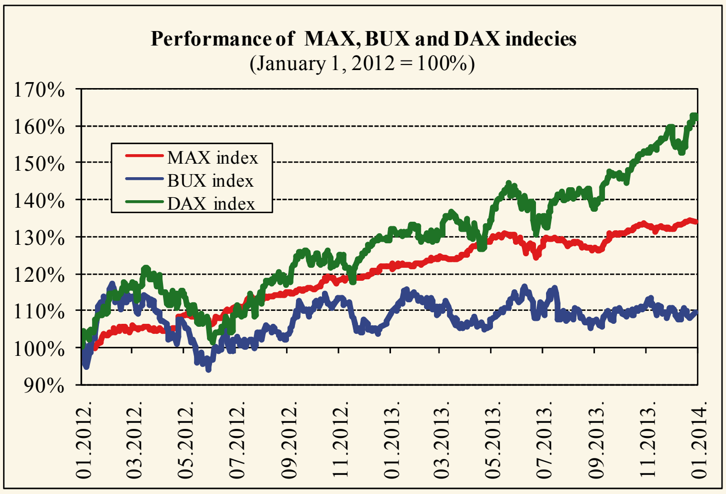
The value of forint–denominated government securities held by non–residents did not change significantly during the year 2013. Non–resident holdings reached their historical high of HUF 5,202 billion on July 8, 2013. By the end of the year, however, non–resident holdings declined to HUF 4,994 billion, meaning a slight decline during the year as a whole.



Source: KELER Zrt.

The share of foreign holdings of forint–denomiated debt decreased from 46% to 42% within the total debt. Adding to this the foreign exchange denominated debt held by non–residents the foreign holdings amounted to 61 per cent of the total public debt portfolio.

Equity Markets



Source: ÁKK, Bloomberg

Emerging markets underperformed all around the world and the performance of certain companies listed on the Hungarian stock exchange (including OTP, MOL, Magyar Telekom) was dragged down by company–specific factors. For the year as a whole, the BUX index posted a small 2% increase.

II. DEBT MANAGEMENT STRATEGY IN 2013

ÁKK plans and performs its financing transactions in accordance with the Debt Management Strategy approved each year by the Minister responsible for Public Finances, the Minister for National Economy.

ÁKK's main objective is to finance the central government at the lowest costs in the long run, taking account of risks. Taking the economic policy as a framework, the strategy must focus on the best possible achievement of this objective.

In the trade–off between costs and risks, the aim is to develop a debt structure with the most favourable long–term cost–risk characteristics. The emphasis is on the long term: no transaction should be done to achieve lower costs in the short term at the expense of higher costs or greater risks in the future.

The most important risk factors are as follows:

- Refinancing risk consists of the risk of renewing maturing debt and the risk associated with meeting net financing requirements. In extreme cases, refinancing risk may become liquidity risk, but in general it is only interest rate risk.
- Interest rate risk relates to fluctuations in the yields and interest rates of government debt.
- Liquidity risk is the result of fluctuations in the cash–flows of the central government and the capital market operations of debt management.
- Foreign exchange rate risk arises out of fluctuations of the exchange rates of the forint versus the euro, as well as other foreign currencies.
- Credit risk (counterparty risk) is an important risk factor in the case of hedging transactions concluded directly with partners in the international capital markets and in the case of repo operations in the domestic money market.

ÁKK has developed various benchmarks reflecting its strategic objectives based on an optimal portfolio model which consider risks and costs simultaneously. In order to filter out short–term effects, these benchmarks are monitored as 90–day moving averages. The benchmarks approved by the Minister for National Economy are also used to quantify strategic objectives and to set intermediate targets. During the course of 2013 the composition of the central government debt conformed to the benchmarks.

Public debt management benchmarks

Benchmarks	Tolerance band	End 2012	End 2013
1. Foreign currency debt ratio	25–45% FX	41.0%	40.3%
2. Foreign currency debt composition	95–105% EUR	100.8%	101.0%
3. Fixed coupon part of foreign currency debt	62.7–67.7%	66.2%	63.6%
4. Fixed coupon part of domestic debt	61–83%	67.6%	65.2%
5. Duration of domestic debt	2–3 years	2.49	2.47

Benchmark No. 6. is to maintain a secure level of funds on the Single Treasury Account (STA). For a detailed description of liquidity management in 2013 see Chapter VI.

Strategic principles

ÁKK executes its financing policy governed by the three main principles of simplicity, transparency and liquidity. In the interest of simplicity and transparency, ÁKK only issues a limited number of plain vanilla instruments in a transparent manner that conforms to market practice, i.e. it sells fixed coupon and floating rate forint bonds and zero–coupon discount treasury bills according to a fixed annual issuance calendar announced in advance.

As regards liquidity, ÁKK aims to ensure that government securities have a sufficiently liquid secondary market. A liquid secondary market can be supported by the debt manager by two ways. The first measure is the continuous two–way price quotation by Primary dealers that reflects real market prices; the second is building–up sufficiently large volumes of government securities series (benchmarks). In order to achieve this latter goal, ÁKK reopens individual series – i.e. it issues additional bonds that are fully fungible with previously issued series. The targeted volume of bond series was around HUF 600–800 billion (approximately EUR 2–3 billion) in 2013, with greater volumes targeted for securities with a longer tenor (5 or 10 years). Secondary market operations were also enhanced by bond buy–back and bond exchange transactions by ÁKK.

Due to the international financial crisis, the volatility of yields and spreads has increased and the government markets are more prone to becoming unstable. This has also increased the uncertainties in connection with debt financing. Owing to this, ÁKK has raised the flexibility of its operations. This way it can react to changes in market demand to a greater extent as regards the offered and the accepted amounts at auctions. The non competitive top–up phase of bond auctions had been introduced for a similar reason, to be able to react to a stronger than expected demand.

III. THE FINANCING REQUIREMENTS IN 2013

The components of the financing requirements

The most important part of the net financing requirements is the deficit of the central government. ÁKK is responsible for financing the central government and maintaining its continuous liquidity, while local authorities (the other subsystem of the public sector) manage their own budgets, financing and debt.

The total annual net financing requirement financed by ÁKK is the sum of the central government deficit and other, extra–budgetary transfers (net transfers from the EU, special transfers to the NBH etc.). The gross financing requirement, in addition, also includes debt redemptions, the majority of which is contributed by short–term debt, which may be renewed several times a year. During recent years, cash–flow based financing requirements were as follows:

Borrowing requirements between 2009 and 2013: **HUF billion**

	2009	2010	2011	2012	2013
Central government balance*	–739.9	–837.8	–1,718.4*	–620.1	–979.8
Balance of the Social Security funds	–151.0	–95.6	–83.3	–117.8	0.0
Balance of the extra–budgetary funds	–30.4	61.6	67.2	130.4	50.5
Net financing need of the central government*	**–921.3**	**–871.9**	**–1,734.4***	**–607.5**	**–929.2**
Capital transfers to NBH	0.0	0.0	–29.1	0.0	0.0
Privatisation revenues	1.1	30.1	36.7	0.0	0.0
Net EU transfers	35.7	–125.1	406.6	–238.8	–296.6
Total net financing requirements*	**–884.5**	**–966.9**	**–1,320.2***	**–846.3**	**–1,225.8**
Short term debt redemptions	–1,988.7	–2,048.6	–1,922.3	–1,808.4	–2,594.8
Long term debt redemptions	–2,349.4	–1,752.7	–2,500.6	–2,782.2	–4,096.6
Gross financing requirements*	**–5,222.6**	**–4,768.2**	**–5,743.2***	**–5,436.9**	**–7,917.2**

** Including the assumption of local authorities' and MÁV's (state railway) debt and the purchase of shares of the company MOL in 2011. These transactions – with a total value of HUF 744.7 billion – did not require market financing.*

Source: Hungarian State Treasury, Ministry for National Economy, ÁKK

The net financing requirement

In 2013 the total cash–flow based deficit of the central government was HUF 929.2 billion (or 3.2 per cent of GDP according to preliminary data), while the total net financing requirement amounted to HUF 1,225.8 billion (or 4.2 per cent of GDP) including large negative net EU transfers.

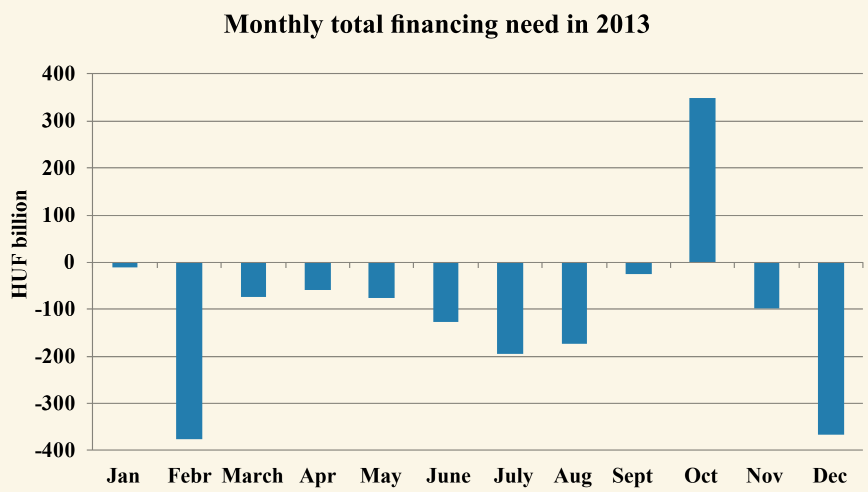
Borrowing requirements in 2013:

	Plan published in December 2012 (HUF billion)	Actual (HUF billion)	Actual/Plan (per cent)
Central government balance	– 834.0	–979.8	117%
Balance of the Social Security funds	0.0	0.0	–
Balance of the extra–budgetary funds	–7.0	50.5	–722%
Net financing need of the central government	**–842.0**	**–929.2**	**110%**
Gross financing requirements	0.0	0.0	–
Privatisation revenues	0.0	0.0	–
Net EU transfers	223.0	–296.6	–133%

	Plan published in December 2012 (HUF billion)	Actual (HUF billion)	Actual/Plan (per cent)
Total net financing requirements	**–619.0**	**–1,225.8**	**198%**
Short term debt redemptions	–2,507.3	–2,594.8	103%
Long term debt redemptions	–2,609.5	–4,096.6	157%
Gross financing requirements	**–5,735.8**	**–7,917.2**	**138%**

Source: Hungarian State Treasury, Ministry for National Economy, ÁKK

The monthly financing needs showed a significant fluctuation in 2013 as well; large part of the financing requirement materialized in the first quarter of the year.



Redemptions

Redemptions in any given year are largely the function of debt financing operations in previous periods and of the sales of short–term instruments renewed within the year. Prepayments of loans, buy–backs of bonds and the early repurchasing/redemption of retail securities and other securities in the Treasury network may also influence the final sum. As a result of these operations redemptions of domestic debt in 2013 were higher than planned. In the case of the foreign currency debt higher repayment was due to the early and full repayment of the IMF loans, prepayments of other foreign currency loans and repurchases from the euro–denominated domestic bond series.

Government debt redemptions[2]

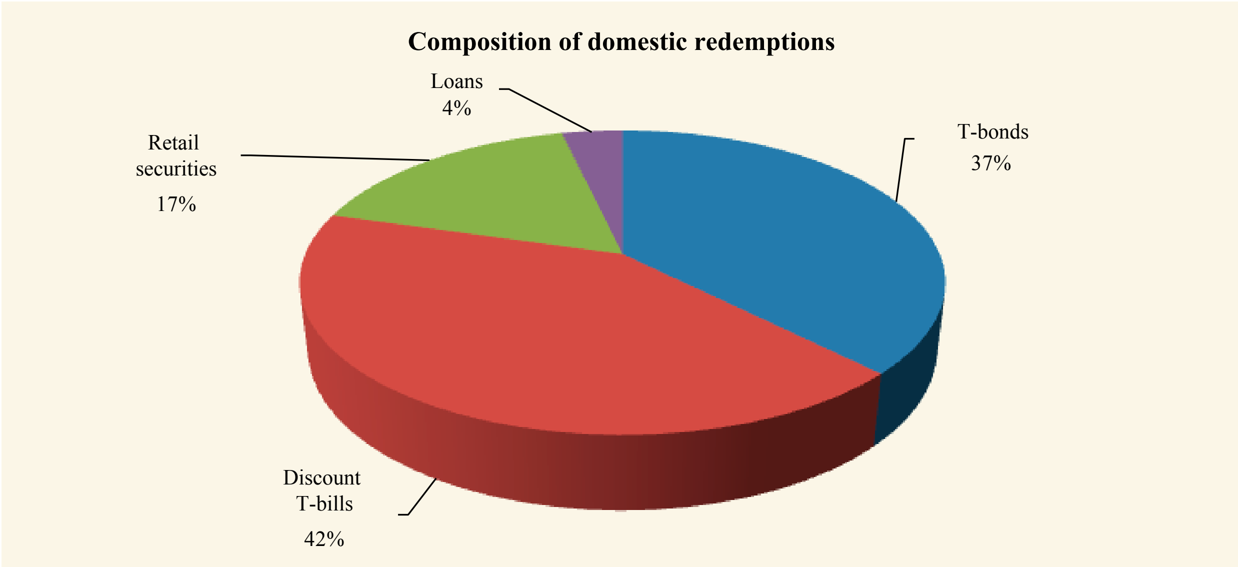
HUF billion

	2012	2013 plan	2013 actual
Domestic debt	**3,176.2**	**3,662.2**	**4,544.1**
T–bonds	1,215.3	1,056.4	1,704.4
Discount T–bills	1,540.9	1,846.9	1,906.5
Retail securities	396.0	744.9	767.9
Loans	24.0	14.0	165.3
Foreign currency debt	**1,414.4**	**1,454.6**	**2,147.3**
Bonds	412.5	409.9	884.4
Loans	1,001.9	1,044.7	1,262.9
Total	**4,590.6**	**5,116.8**	**6,691.4**

Source: ÁKK

2 In this publication the redemption and gross issuance of short–term debt is reported according to the OECD methodology. The amount of redemption of T–bills equals the outstanding volume of the short–term debt at the beginning of the year and gross issuance equals the sum of the redemption figure and the net issuance in the given year.

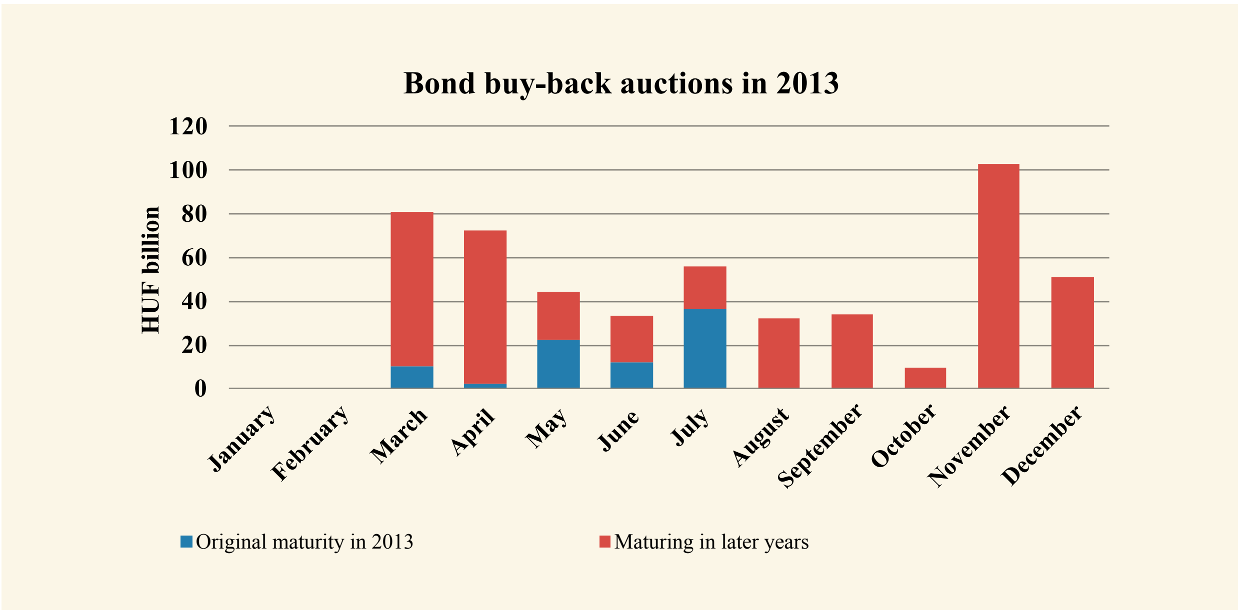
Total domestic debt redemptions exceeded the plan by HUF 882 billion, due to higher bond redemptions as a result of the bond buy back and exchange programs and increased retail debt maturities. Within the HUF debt portfolio, discount treasury bills contributed to 42 per cent of the total forint redemptions of HUF 4,544 billion, due to their renewals within the year.



Source: ÁKK

Bond buy-backs

A large bond series maturing at a given time creates refinancing risk. This risk can be reduced by repurchasing a proportion of the bonds before maturity. ÁKK's normal financing plan includes a regular bi–weekly bond buy–back program, and the actual repurchase amount depends on the quantity and quality of bids. In 2013 ÁKK bought back a total of HUF 518 billion bonds before their maturity on 22 occasions. 84 per cent of the repurchased bonds had an original maturity after 2013, i.e. these buy–backs also helped to smooth maturities from one year to another, since the original volume of bond maturities in 2013 was lower than in the next years.



In order to decrease refinancing risk ÁKK has been holding exchange (or switch) auctions since 2009 on a regular basis. In these switch auctions the investors can exchange their bonds with short remaining term–to–maturity for longer term bonds. This improves the investment possibilities of investors and at the same time lengthens the average term–to–maturity (ATM) of the government debt. In 2013 11 exchange auctions were held at which ÁKK exchanged a total of HUF 120 billion short–term bonds for long–term ones.

Foreign currency debt redemptions

In 2013 three foreign currency bonds – a EUR 1 billion, a JPY 50 billion and a CHF 150 million respectively – matured and a total of SDR 3.5 billion worth of loans were repaid to the IMF. Beside these items other smaller repayments took place in the case of IFI project financing and other loans.

The pension reform and debt reduction fund

The Pension Reform and Debt Reduction Fund has the objective to liquidate the assets in its portfolio and may use the revenues exclusively for reducing government debt. It started its operation in 2011 and the remaining assets in the Fund were sold in 2013, which means that the operation of the Fund was basically completed by the end of 2013.

In 2013 HUF 87 million worth of government securities were transferred by the Fund to the state and were immediately cancelled. (The above tables do not include these cancellations as they did not require any financing.)

Revenues from the sales of its assets and other sources enabled the Fund to transfer HUF 349 billion in cash to the state, which sum was used for bond buy–backs and the repayments of the loans taken over from local authorities (see www.akk.hu for details).

IV. FINANCING

The issuance of government securities and the drawdowns of loans were planned and implemented in accordance with the approved debt management strategy and benchmarks. The strategy states that foreign currency redemptions should be financed by foreign currency issuance, domestic redemptions and the net financing needs should be financed by local currency issuance. This ensures the gradual decrease of the share of foreign currency debt. Nevertheless, if market conditions allow, the increased issuance of local debt may substitute foreign currency borrowing and facilitate a faster decrease of the relatively high share of foreign currency debt.

In order to develop the domestic investor base the government programme aiming to boost the direct sales of retail government securities to retail investors was continued in 2013. This program has been an overwhelming success, and has resulted in a large increase in domestic financing by households.

In 2013 the HUF denominated issuance amounted to HUF 5,252 billion (71%), while foreign currency issuance was HUF 2,131 billion (29%).

Gross debt issuance:

HUF billion

	2012	2013 plan	2013 actual
Domestic debt	**4,888.8**	**4,393.7**	**5,251.7**
T–bonds	2,073.6	1,530.0	1,846.5
Discount T–bills	1,906.5	1,868.8	1,904.9
Retail securities	908.7	994.9	1,471.0
Loans	0.0	0.0	29.3
Foreign currency debt	**232.7**	**1,502.0**	**2,130.6**
Bonds	88.3	1,388.7	1,921.0
Loans	144.5	113.4	209.6
Total	**5,121.5**	**5,895.7**	**7,382.3**

Source: ÁKK

Net HUF denominated financing totalled HUF 708 billion, while net foreign currency financing amounted to HUF –17 billion, so the total net issuance was HUF 691 billion in 2013.

Net issuance:

HUF billion

	2012	2013 plan	2013 actual
Domestic debt	**1,712.6**	**731.5**	**707.6**
T–bonds	858.3	473.6	142.0
Discount T–bills	365.6	21.9	-1.5
Retail securities	512.7	252.0	703.1
Loans	-24.0	-14.0	-136.0
Foreign currency debt	**-1,181.7**	**47.4**	**-16.8**
Bonds	-324.2	978.8	1,036.6
Loans	-857.5	-931.3	-1,053.3
Total	**530.9**	**778.9**	**690.8**

Source: ÁKK

Within the net HUF issuance, the role of retail securities increased in line with the better than expected investor demand, while the role of long term bonds also increased. Total net T–bond sales was HUF 142 billion (higher sales were partially offset by higher buy–backs). Beside that, sales of retail securities set a new historical record of HUF 703 billion. The outstanding volume of discount Treasury bills was stable, whereas early repayments of HUF loans reduced net issuance by HUF 136 billion.

In 2013 the net foreign currency financing was negative, even though the plans calculated with a small positive net issuance.

Domestic financing

Gross domestic issuance was eventually 20% higher than planned originally. The issuance of all kinds of instruments increased; bond issuance was higher than planned by 21% and that of retail instruments by 48%. Project financing loans of HUF 29 billion – originally planned in foreign currencies – were drawn in HUF in 2013.

Government bonds

Treasury bond auctions were held every two weeks, but to increase issuance flexibility the tenors were not set in advance, but announced a week before the auction, after consultations with Primary dealers. Three bond series were sold at each bond auction. Usually the 3, 5 and 10–year tenors were offered, but on 3 occasions the 10–year bond was replaced by the 15–year fixed rate bond. The 5–year floating rate bond was offered 12 times during the year. ÁKK actively used its right to modify the accepted amount as a reaction to bids (+/– 34 per cent or +/– 50 per cent if the announced amount was not more than HUF 20 billion). Another way to react to changes in market demand was the use of the non–competitive top–up phase in the afternoon of the auctions when successful bidders at the auction could buy additionally up to 40 per cent of their winning bids at the average price of the auction.

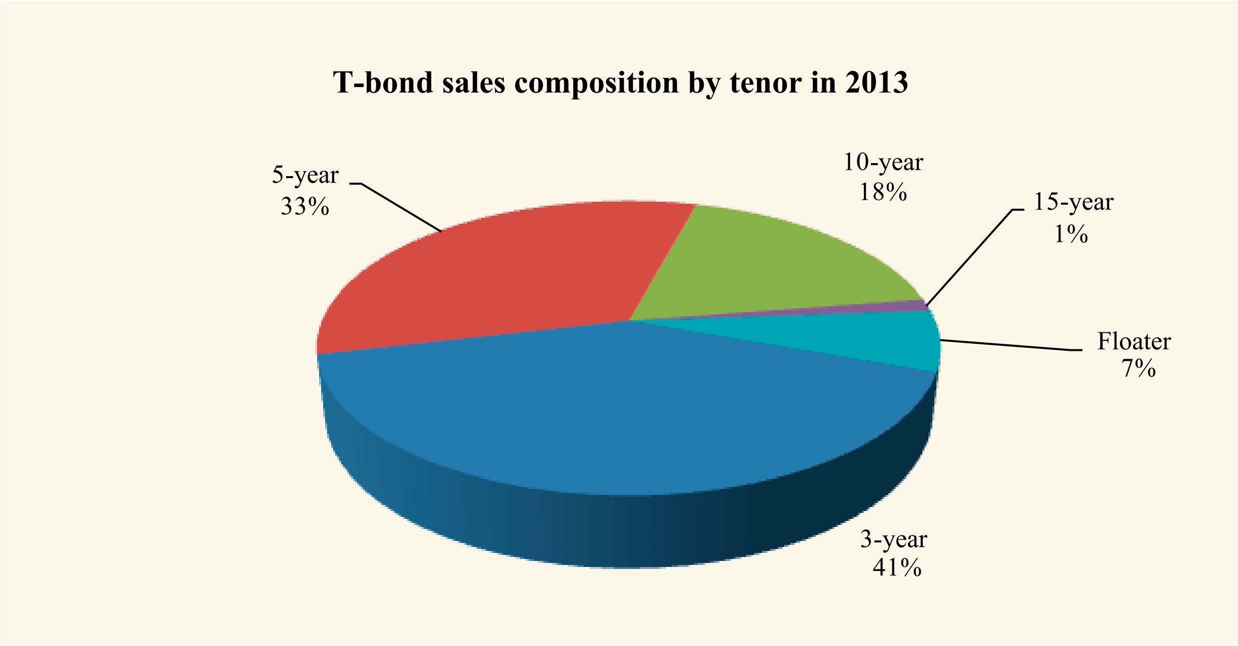
The bid–to–cover ratio at the bond auctions on average was 3.1. ÁKK sold a total of HUF 1,598 billion of bonds via auctions (including HUF 258 billion in the additional non–competitive phase). Total bond issuance – together with bond exchange auctions, the retail sales of the Hungarian State Treasury and secondary market operations – was HUF 1,846 billion, versus total bond maturities of HUF 1,704 billion, which resulted in a net issuance of HUF 142 billion.

On–the–run bond series in 2013 (HUF billion):

	Tenor	Number of auctions	Competitive sales in 2013	Non–competitive sales in 2013	Outstanding (end of 2013)
2016/D	3–year	25	544	107	659
2018/A	5–year	25	438	87	531
2019/B	5–year (floater)	12	89	18	107
2023/A	10–year	22	248	45	577
2028/A	15–year	3	20	1	121

Source: ÁKK

ÁKK adjusted the accepted amounts at the auctions according to demand, and the results show that the investors' demand was highest for the 3 and 5–year bonds:



Source: ÁKK

Discount treasury bills

The 3 and 12–month discount treasury bills are short–term instruments mainly used for liquidity management, i.e. for smoothening the fluctuations in liquidity caused by the varying financing requirements over the year. For this purpose ÁKK may also use the so–called liquidity discount treasury bills of even shorter tenor (usually 6 weeks).

In 2013 ÁKK sold discount treasury bills in a total of HUF 1,905 billion, the same amount as in 2012. ÁKK originally planned a small net discount T–bill issuance, however, the outstanding T–bill stock actually declined by HUF 2 billion over the year.

Retail securities

One of the strategic objectives of ÁKK is to maintain a retail government securities issuance programme, which constitutes a more and more important source of financing beside the domestic and the international capital markets. With growing domestic savings it is advantageous for the Government to tap this source of funds directly.

The issuance of retail government securities showed a steep increase in 2013. ÁKK contributed to this success by an active marketing campaign, new products, a broader selling network and competitive pricing for these instruments. The stock of the one–year interest bearing T–bill grew the most, by HUF 553 billion, while outstanding amount of other products like the 6–month interest bearing T–bill and the Treasury Savings Bills (securities available in the post office network) grew by HUF 11 billion and by HUF 50 billion respectively.

In line with the objectives of public debt management, long term bonds started to play an even more important role in the retail scheme in 2013. The inflation–linked Premium Government Bond had a net sale of HUF 86 billion. A new very long term bond (with a maturity of 19 years) was also introduced which added an additional HUF 2 billion to funding. The total retail debt stock grew by HUF 703 billion over the year, which is almost three times higher than the HUF 250 billion planned, and contributed to a large extent to the year's successful financing from the domestic market.

Foreign currency financing

In 2013 ÁKK issued 3 international bonds to finance maturing foreign currency bonds and the loan repayment to the International Monetary Fund.

Foreign currency bonds issued by Hungary in 2013:

Currency	Amount	Date of issuance	Maturity	Tenor (years)	Coupon
USD	2,000,000,000	19.02.2013	21.02.2023	10	5.375%
USD	1,250,000,000	19.02.2013	19.02.2018	5	4.125%
USD	2,000,000,000	22.11.2013	22.11.2023	10	5.75%

Source: ÁKK

The domestic foreign currency bond (the “Premium Euro Government Bond” launched in November 2012) was a big success in 2013 and having reached the offered amount a new series was opened also with a 3–year tenor. Together with a new euro–denominated private placement bond (Residence bond) it provided HUF 329 billion in net funding.

Series	Currency	Date of issuance	Maturity	Tenor (years)	Coupon
2016/X	EUR	17.01.2013	25.05.2016	3	Floating rate
2016/Y	EUR	21.05.2013	25.10.2016	3	Floating rate
2018/T	EUR	19.06.2013	20.12.2018	5	Fixed

Source: ÁKK

In 2013 the government drew a total of HUF 210 billion (EUR 707 million) in the form of project financing foreign currency loans from international financial organisations. The loans drawn from the European Investment Bank (EIB) and the Council of Europe Development Bank (CEB) were used, among others, to finance projects in infrastructure development and integration assistance. Net FX issuance in 2013 was HUF –17 billion.

V. THE GOVERNMENT DEBT IN 2013

During 2013 the central government debt increased by HUF 1,279 billion (or by 4.4 per cent) to HUF 21,999 billion. The size of the debt was influenced by several factors. The net issuance in itself increased the public debt by HUF 691 billion, although the net issuance was lower than the actual net borrowing requirement as a result of using funds from the Pension Reform and Debt Reduction Fund for debt repayment. Central government debt increased by HUF 593 billion due to debt assumptions from local governments (however, this transaction had no effect on the size of the total public debt). The value of public debt also increased due to the depreciation of the forint against other currencies by HUF 175 billion, while the declining stock of other obligations, namely marked–to–market deposits decreased the central government debt by HUF 234 billion.

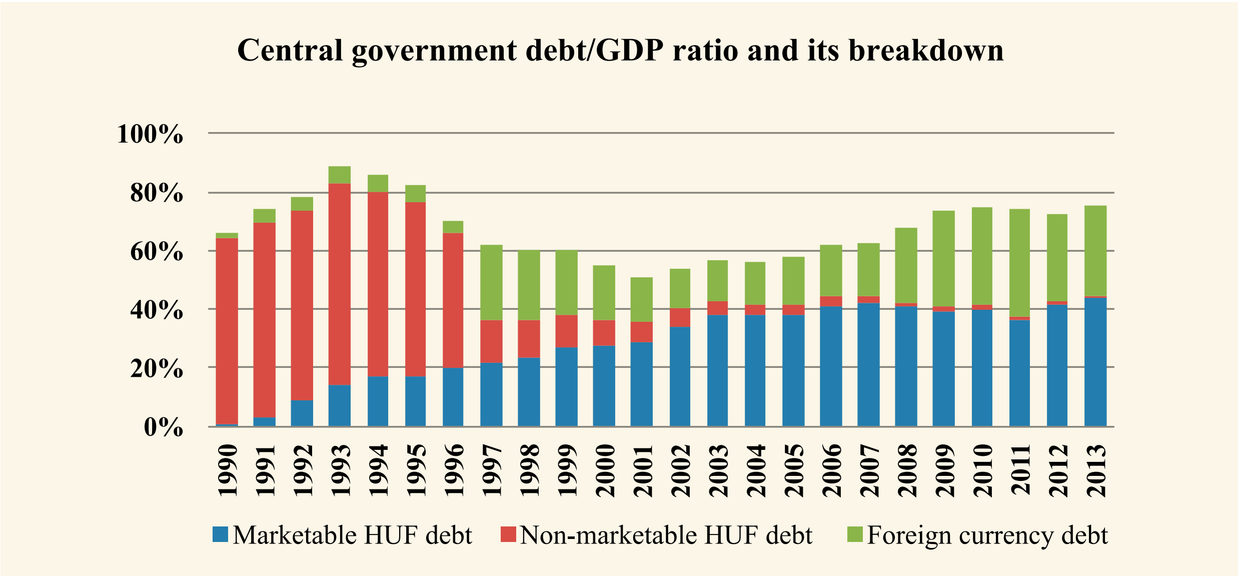
Central government debt

HUF billion

	2012		2013		Change
Domestic debt	**12,042.4**	**58.1%**	**12,976.4**	**59.0%**	**934.0**
Loans	566.8	2.7%	603.6	2.7%	36.8
Government bonds	8,582.5	41.4%	8,779.4	39.9%	196.8
Discount T–bills	1,906.5	9.2%	1,904.9	8.7%	-1.5
Retail securities	986.6	4.8%	1,688.5	7.7%	702.0
Foreign currency denominated debt	**8,326.6**	**40.2%**	**8,904.9**	**40.5%**	**578.4**
Loans	3,312.5	16.0%	2,735.6	12.4%	-576.9
Bonds	5,014.1	24.2%	6,169.3	28.0%	1,155.2
Total debt	**20,369.0**	**98.3%**	**21,881.4**	**99.5%**	1,512.4
Other obligations	351.1	1.7%	117.3	0.5%	-233.8
Grand total debt	20,720.1	100.0%	21,998.6	100.0%	1,278.6

Source: ÁKK

The debt of the central government compared to the GDP (debt ratio) that measures the stock of debt against the actual economic performance increased in 2013 mostly as a result of debt assumptions. According to preliminary data, the central government debt increased from 73.9 to 75.7 per cent.



Source: ÁKK

Characteristics of the HUF debt portfolio

During 2013 the HUF–denominated debt that accounts for 59 per cent of the total debt increased by HUF 934 billion (8 per cent) to HUF 12,976 billion.

41 per cent of total public debt was in the form of long–term HUF government bonds (excluding retail bonds). The total domestic bond portfolio of HUF 8,779 billion consisted of 23 bond series, the average size of a series was HUF 382 billion (ca. EUR 1.3 billion). 12 series had a volume in excess of HUF 500 billion (ca. EUR 1.7 billion), and the largest bond series reached HUF 910 billion (or EUR 3.0 billion).

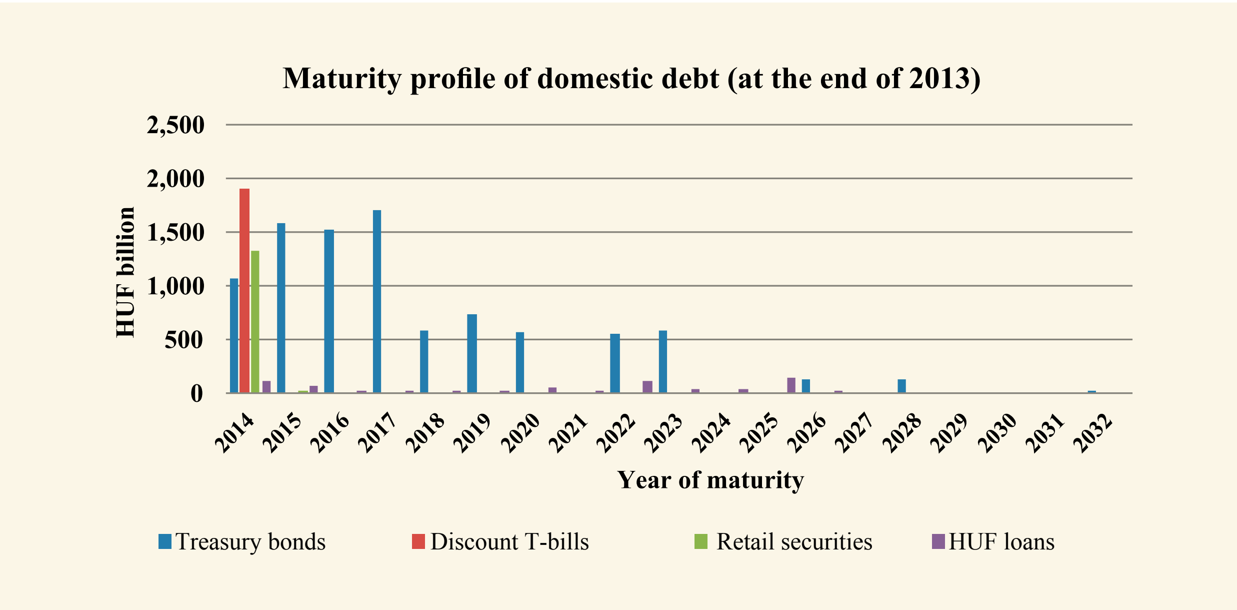
The HUF 1,905 billion discount T–bill stock consisted of eighteen series. There were six larger series with an average volume of HUF 229 billion (or EUR 800 million).

In 2013 the portfolio of retail government securities jumped from HUF 987 billion to HUF 1,689 billion. Retail securities accounted for 13% of the total domestic debt in comparison to their 8 per cent share at the end of 2012.

The non–marketable component of the HUF bond portfolio continued to decrease in amount and proportion in 2013 as well, as there are no new issuances of such government bonds and the existing portfolio matures gradually. The end–of–year volume of non–marketable government bonds was HUF 191 billion, 1.5 per cent of the total debt.

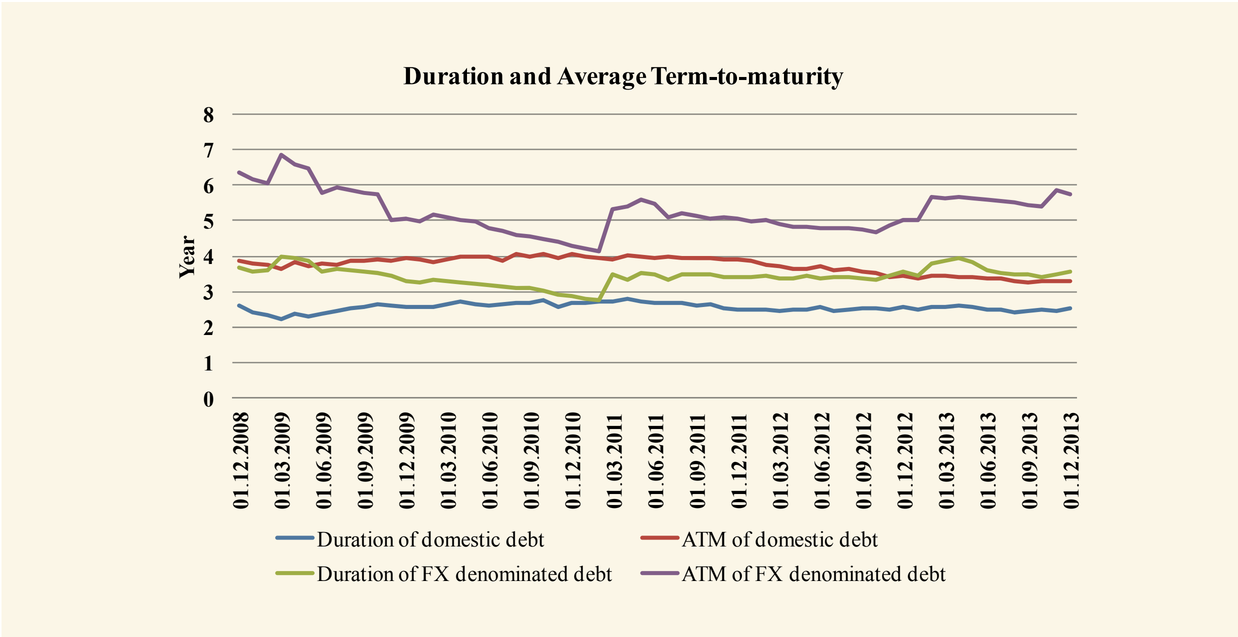
The volume of loans denominated in Hungarian forint increased in 2013 mainly as a result of debt assumptions by HUF 37 billion to HUF 604 billion.

As a result of the bond buy–back and exchange auction programmes, the maturity profile of the bond portfolio remained balanced:



Source: ÁKK

As a result of the increased domestic bond issuance in 2013, the duration and average term–to–maturity characteristics of the domestic debt remained relatively stable. The duration of the HUF denominated debt portfolio stood at 2.47 years and the average term–to–maturity also decreased slightly to 3.3 years in 2013.

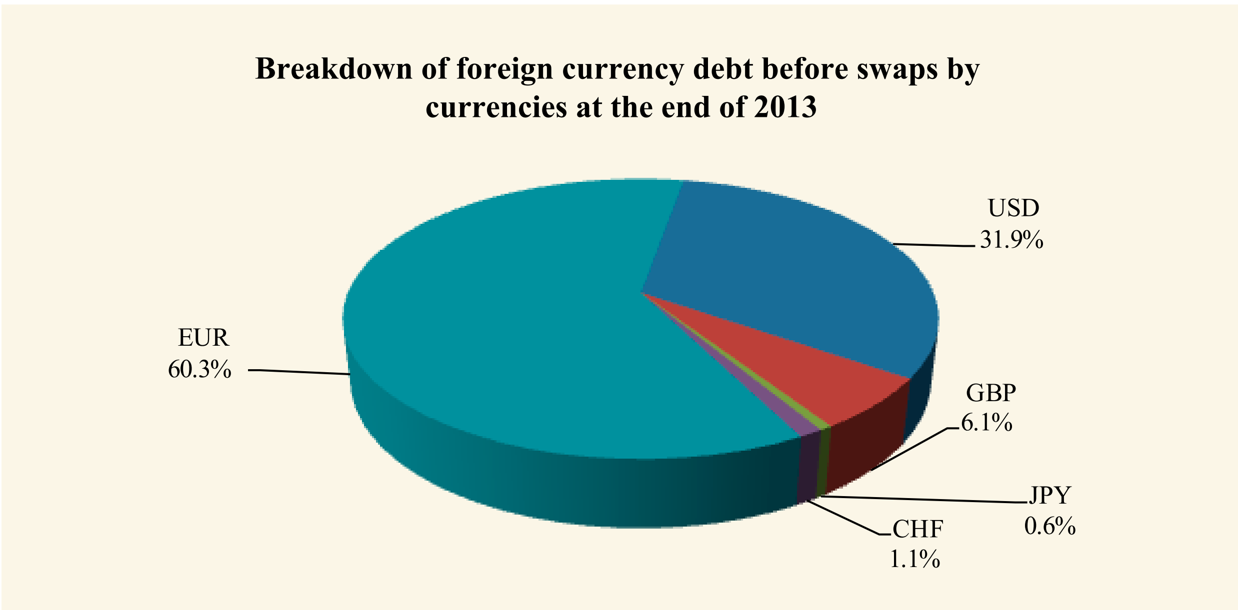


Source: ÁKK

Characteristics of the foreign currency debt portfolio

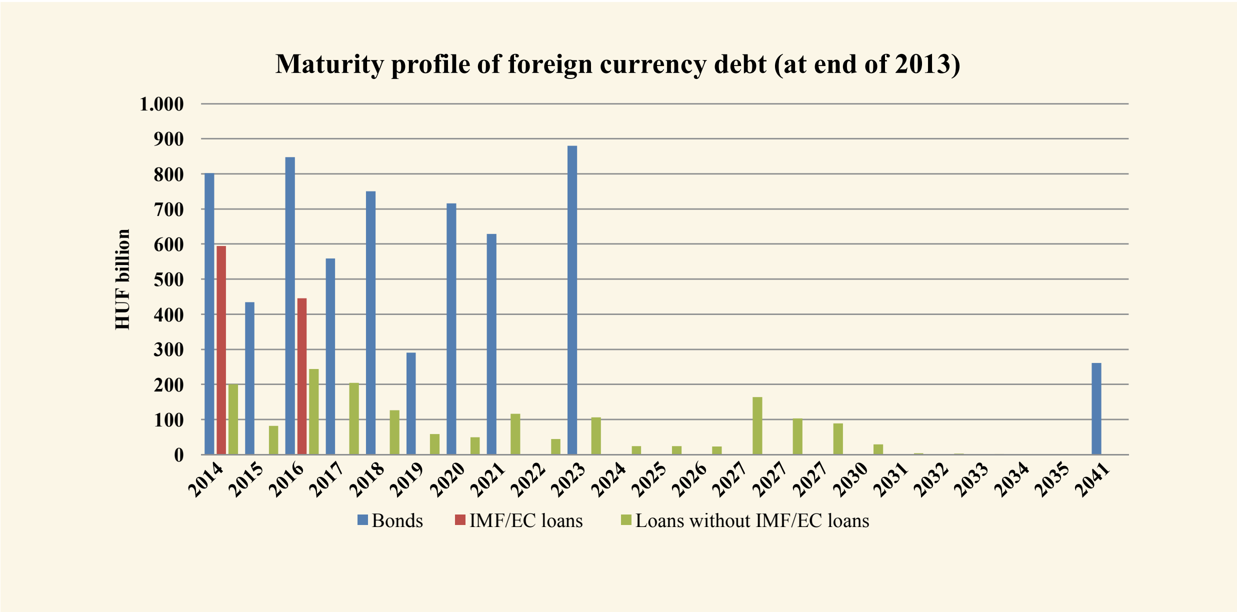
The gross foreign currency government debt increased by HUF 578 billion in 2013, reaching HUF 8,905 billion (EUR 30 billion) by the end of the year. The share of foreign currency debt within the total gross government debt (excluding marked–to–market deposits) declined from 41 to 40 per cent during 2013.

The volume of outstanding foreign currency bonds (after swaps) reached HUF 6,169 billion by the end of the year, significantly higher than at the end of 2012 (HUF 5,014 billion), mainly as a result of financing loan redemptions by bonds and also the depreciation of the forint. On 31 December 2013 there were 23 series of foreign currency bonds outstanding, 11 of which had been issued in euro (including the domestic euro bonds as well), 7 in US dollars, 3 in Pound sterling, one in Swiss francs, and one in Japanese yen. In accordance with the strategy and benchmarks, all non–euro bonds had been converted into euro liabilities through swap transactions. Bonds accounted for 69% of the total foreign currency debt portfolio.



At the end of 2013 close to 100% of the foreign currency debt was denominated in euro (after swaps).
Source ÁKK

The foreign currency loan portfolio consisted of long–term project financing loans from international financing institutions (e.g. EIB and CEB), as well as loans from the European Commission. As a result of the full repayment of the IMF loan the share of loans within the total foreign currency debt declined steeply from 40 to 31 per cent.



Source: ÁKK

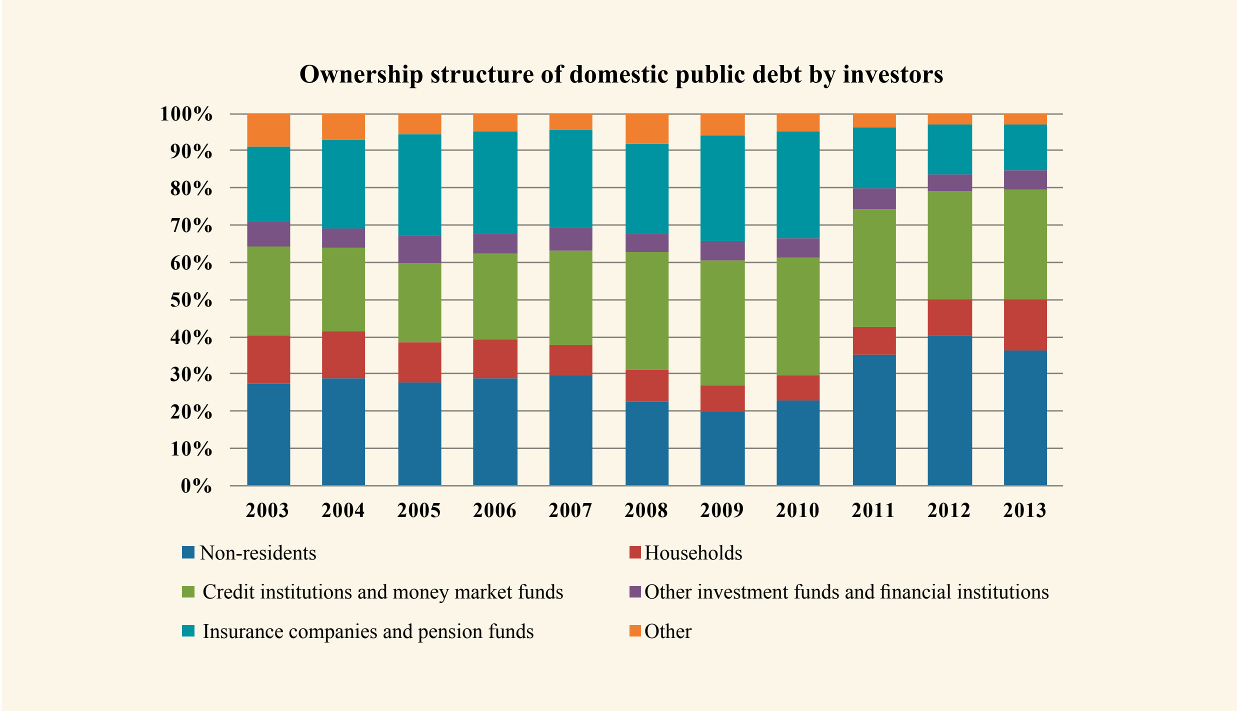
During 2013 the average life of the foreign currency portfolio improved as a result of the redemptions of the relatively short term IMF loan: the duration remained 3.6 years, while the ATM rose by 0.7 years to 5.7 years.

Other obligations

In order to reduce counterparty risk associated with the swap transactions concluded by ÁKK, so–called marked–to–market deposits are being placed as collateral covering the net value of their swap positions. Such deposits placed with ÁKK are non–financing funds and they are shown as part of the government debt among ‘other obligations’. As of 31 December 2013 marked–to–market deposits placed with ÁKK totalled HUF 117 billion (EUR 0.4 billion).

The ownership structure of government debt

According to statistics published by the National Bank of Hungary, the following changes took place in the ownership structure of domestic government securities in 2013. The share of the largest investor group – namely non–resident investors – declined from 40 per cent to 36 per cent. The share of credit institutions and insurance companies/pension funds remained the same. Domestic retail investors, however, increased further their share significantly from 10 per cent to 14 per cent.



Source: NBH, KELER, ÁKK

In 2013 non–residents decreased their share both in nominal and relative terms. Non–resident holdings of HUF denominated government securities slightly decreased by HUF 14 billion to HUF 4,994 billion. At the same time the duration of their holdings increased by 0.1 year to 3.3 years, while the ATM of their holdings remained 3.9 years in 2013. Foreign investors keep holding primarily longer dated bonds, and both the duration and the ATM of the non–resident holdings are longer than that of the total outstanding stock of government securities.

VI. LIQUIDITY MANAGEMENT

According to the Act on the Economic Stability of Hungary, liquidity management of the central government is also the task of ÁKK. The goal of ÁKK is to maintain the balance of the Single Treasury Account (STA) which serves as a financing reserve at a so–called optimal level with liquidity management operations. These operations may be active (placement of funds) or passive (fund–raising) transactions, however, ÁKK only invests temporary excess liquid funds from the STA if repo partners show adequate demand, otherwise it leaves the extra cash on the STA. Since the financial crisis, the banks have accumulated massive liquidity, and as a result ÁKK's repo tenders are regularly unsuccessful.

Beside the STA, foreign currency deposits could also serve as financing reserves. At the end of 2013 ÁKK had EUR 1.6 billion in foreign currency deposits placed with the National Bank of Hungary. Stand–by credit facilities with foreign banks serve as further liquidity reserves, but in 2013 there were no withdrawals from these facilities.

In 2013 ÁKK used the following instruments to manage the end–of–day balance of the STA:

- repo and reverse repo transactions with government securities;
- the issuance of liquidity discount treasury bills, usually with a 6–week tenor;
- regular bond buy–backs;
- active adjustment of the volume of discount treasury bills at auctions;
- temporary use of FX deposits.

The adequate instruments are chosen mainly as a function of the duration of the required liquidity adjustment; repos are very short term instruments, while liquidity discount T–bills, regular T–bills and buy–backs have longer term liquidity effects.

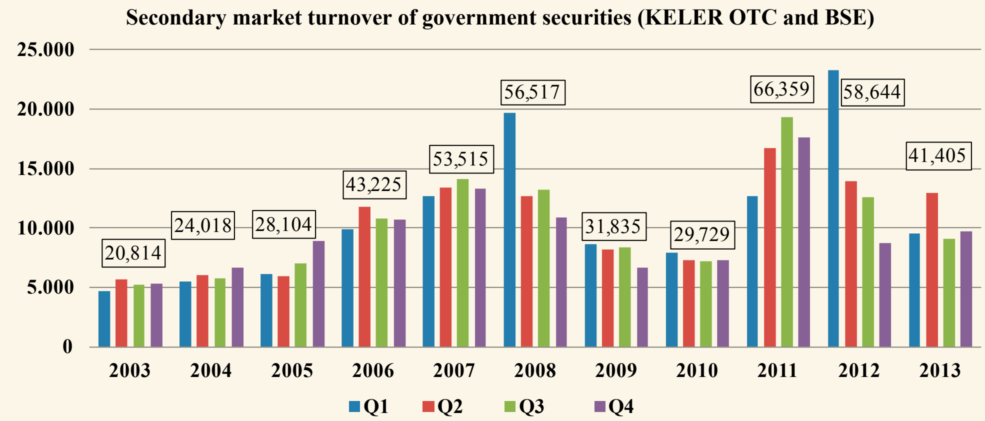
Sales of liquidity discount treasury bills took place twice in 2013 with a total volume of HUF 100 billion.

Liquidity repo transactions are ÁKK's main tool for fine–tuning the end–of–day balance of the Single Treasury Account. In 2013 the use of repo transactions increased by almost 50 per cent to a total of HUF 7,621 billion concluded on 251 business days. Liquidity management was effective and the end–of–day STA balance was higher than the minimum target level except on only 4 days in 2013.

ÁKK concludes repo transactions not only for liquidity management purposes. The objective of the so–called stand–by repo transactions is to support the price quotation of Primary dealers and to promote trading in government securities. If a Primary dealer needs temporary access to a quoted government security, but it is unable to obtain it in the market, that dealer may turn to ÁKK to provide the required security in a one–week repo transaction.

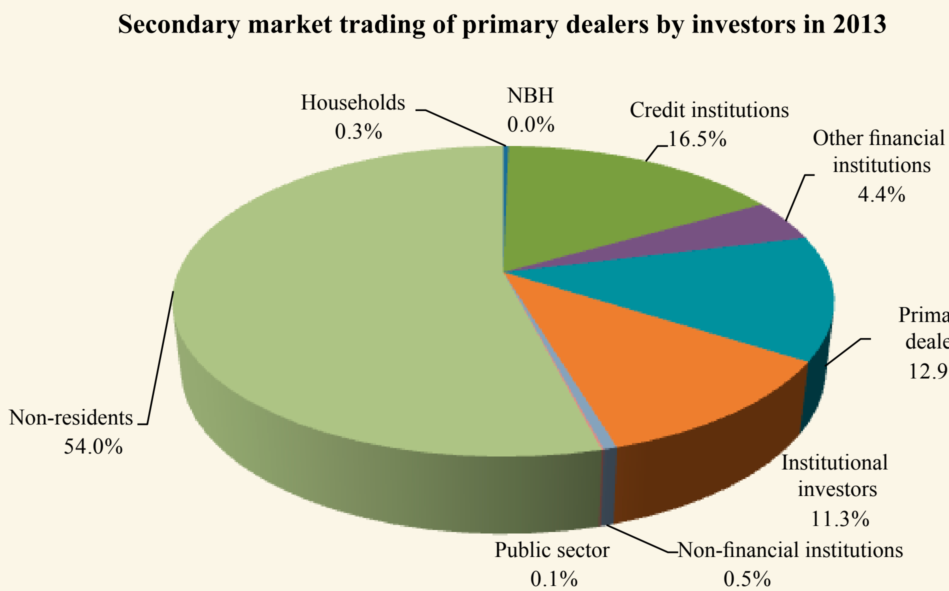
VII. THE SECONDARY MARKET OF HUNGARIAN GOVERNMENT SECURITIES

MTS Hungary is the main electronic platform of trading government securities and Primary dealers fulfil their price quotation obligations on this platform. Primary dealers may also trade in the Budapest Stock Exchange's (BSE) electronic trading system (MMTS), however more than 90% of all secondary trade is still executed in the over–the–counter (OTC) market. According to data from the Central Clearing House and Depository (Budapest) Ltd. (KELER), the total volume of OTC trading in government securities was HUF 40,845 billion in 2013 (about 4 times the size of the total outstanding marketable debt), out of which 83 per cent was in government bonds and 17 per cent in discount treasury bills.



Source: KELER, BSE

The average size of deals with Primary dealers (excluding retail transactions) was HUF 845 million, which is about the same as in the previous year. Over the year, the 2023/A government bond with a 10 year remaining term–to–maturity had the largest turnover (HUF 6,905 billion), followed by the 10–year 2022/A and the 2018/A bond with a 5 year remaining term–to–maturity.



Source: Primary dealers, ÁKK

The most active Primary dealer and the winner of the title 'Primary dealer of the Year' for 2013 was Citibank Europe Plc.

VIII. THE INSTITUTIONAL FRAMEWORK FOR THE ISSUANCE OF GOVERNMENT SECURITIES

ÁKK sells government securities through intermediaries. In the domestic market, 87 per cent of HUF–denominated government securities were sold through the Primary dealers in 2013, the rest through retail channels.

The primary dealer system

The Primary dealer system for government securities was set up in 1996 in order to establish a more secure institutional base for the financing of government debt, to reduce the costs of debt management and to improve the transparency and liquidity of the secondary market in government securities.
Since May 2004, any investment firm or bank registered in any European Union or an OECD Member State may become a Primary dealer in Hungarian government securities if it meets the contractual requirements and signs a Primary dealer contract with ÁKK. Along with a number of obligations in the primary and secondary market, the Primary dealer status also guarantees exclusive rights. In 2013 6 out of the 14 Primary dealers were non–resident institutions.

Primary dealers at the end of 2013:

BNP Paribas SA
CIB Bank Zrt.
Citibank Europe Plc.
Deutsche Bank AG.
Erste Befektetési Zrt.
Goldman Sachs International
ING Bank N.V.
J.P. Morgan Securities Plc.
K&H Bank Zrt.
MKB Bank Zrt.
Magyar Takarékszövetkezeti Bank Zrt.
OTP Nyrt.
Raiffeisen Bank Zrt.
UniCredit Bank Hungary Zrt.

Only Primary dealers may:

1. directly submit bids at government bond and discount treasury bill auctions and submit offers at bond buy–back and exchange auctions;[3]
2. directly submit non–competitive bids at auctions and submit bids at the non–competitive phase after bond auctions;
3. use the stand–by repo facility provided to Primary dealers by ÁKK to support their secondary market trading and price quotation;
4. participate at the consultations organised by ÁKK;
5. use the title ‘Primary dealer’.

In addition to their exclusive rights, Primary dealers are also ÁKK’s main partners for international capital market transactions and liquidity management (repo) and other transactions. Primary dealers with broad distribution networks may also conclude a separate agreement with ÁKK for the trading of one of its retail government securities, the Interest Bearing Treasury Bills.

Retail debt programmes

The State Treasury’s branch network provides direct access to government securities for retail investors. Managed by ÁKK, the 21 Treasury branch offices in Budapest and the county seats quote two–way prices for retail investors for publicly issued bonds, Premium Government Bonds, discount treasury bills and Interest Bearing Treasury Bills. Since December 2008 government securities may also be purchased and sold through the Hungarian State Treasury’s online banking service.

3 Other investors may submit bids at an auction indirectly, through a Primary dealer.

The Hungarian Post Office participates in the sale of three retail government securities. The 1 and 2–year Treasury Savings Bills are the only printed government securities, designed specifically for retail investors. Post Office started to sell Treasury Savings Bill Plus, a dematerialised 1–year treasury bill in autumn 2013.

The dealers of foreign currency bond issues

In 2013 Hungary issued 3 USD bonds in the international capital markets. Lead managers of international bond issuances are selected from among the primary dealers individually for each transaction.

In 2013 the lead managers of the bonds were as follows:

BNP Paribas, Citigroup, Deutsche Bank, Goldman Sachs (for all 3 bonds)

On 20 November 2012, the sale of a new 3–year inflation linked domestic bond denominated in EUR (‘Premium Euro Government Bond’, P€MÁK) started, which became a success among investors in 2013. The bond is available for non–resident investors as well. Dealers may sell P€MÁKs on the basis of a separate agreement with ÁKK.

Dealers of P€MÁK in December 2013:

Citibank Europe Plc.
Concorde Értékpapír Zrt.
Erste Befektetési Zrt.
FHB Bank Zrt.
the Hungarian State Treasury
ING Bank N.V.
Magyar Takarékszövetkezeti Bank Zrt.
MKB Bank Zrt.
OTP Nyrt.
Raiffeisen Bank Zrt.
Sopron Bank Zrt.

IX. THE INSTITUTIONAL FRAMEWORK AND THE OBJECTIVES OF GOVERNMENT DEBT MANAGEMENT

The government debt management is regulated by Act no. CXCIV. of 2011 on the Economic Stability of Hungary (the Stability Act). Among other provisions, this law authorises the minister responsible for the public finances (the Minister for National Economy) to provide for the implementation of the budget, financing of the deficit, continuous solvency of the budget, the recording of the government's debt and repayment obligations, the repayment of debt and the management of temporarily free state funds. Annual budget acts make this authorisation more specific by stipulating the annual financing requirement. According to the provisions of the Stability Act, the minister responsible for public finances performs these tasks through the Government Debt Management Agency Pte. Ltd. (ÁKK).[4]

Pursuant to an amendment of the Public Finances Act, the Government Debt Management Agency Pte. Ltd. was established on 1 March 2001 as the legal successor of a government agency that had performed the same tasks. The organisation, which operates as an independent corporate entity, is a single–member corporation limited by shares registered at the Court of Registration. Its shares may not be traded, the Hungarian State is their sole and permanent owner, and these ownership rights are exercised by the minister responsible for the public finances (the Minister for National Economy). The rules governing the operations of ÁKK as a company are stipulated by general legislation on the operation of companies. Accordingly, the management's activities are controlled by the Board of Directors, while ÁKK's operation is under the supervision of a Supervisory Board and an auditor pursuant to the corporate status. In addition to these internal management and audit mechanisms, the debt management activity is regularly audited by the State Audit Office. The operation of ÁKK is closely linked to the Ministry for National Economy and the Hungarian State Treasury. The co–ordination of the professional activity of these organisations is carried out by the Minister for National Economy.

According to the decision–making mechanism in place, the government debt management strategy, the annual financing plan and the benchmarks are approved by the Board of Directors, followed by approval from the Minister for National Economy. All responsibilities of ÁKK, which are not the responsibilities of the Board are carried out by the Management of ÁKK.

The foundation and the organisational structure of ÁKK

The Government Debt Management Agency was established in May 1995 as a budgetary institution under the supervision of the Ministry of Finance. In 1996 supervision of the agency was taken over by the Chairman of the Hungarian State Treasury. The amendment of the Public Finances Act that prescribed the foundation of ÁKK Ltd. allowed government debt management to be implemented through a more flexible organisation that would be able to react better to market developments. The purpose of creating a separate institution was to implement the strategy through a faster decision–making mechanism with clearly defined responsibilities and enhanced accountability. From 2003 onward ÁKK became responsible for liquidity management as well. Within this system the Minister for National Economy (before 2010 the Minister of Finance) approves the strategy (or, if needed, its revision), the performance indicators (benchmarks), and the annual financing plan. Within this framework and certain predetermined limits all other decisions are delegated to the Board of Directors and the management of ÁKK.

The organisational structure of ÁKK is similar to that of banks and investment companies. Market operations are conducted by the Front Office; deals are booked and settled by the Back Office; planning, risk management and the analysis of market and macroeconomic trends are tasks for the Middle Office, which is separated from the previous two.

The responsibilities of ÁKK

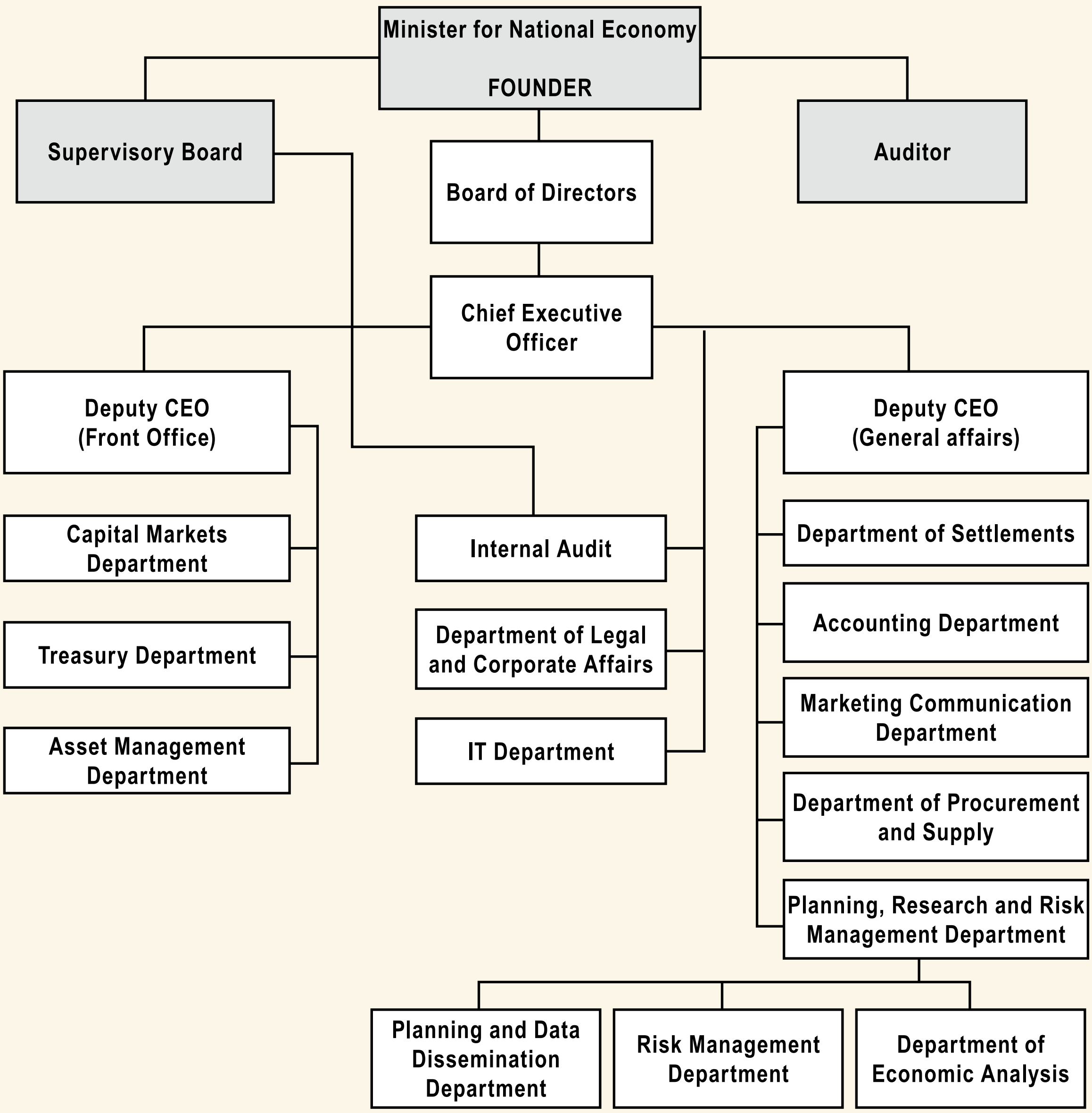
According to the provisions of Article 13 of the Act on the Economic Stability of Hungary, the responsibilities of ÁKK include the following major tasks:

- developing a long–term financing strategy in line with economic policy, which determines the objectives of debt management and the means of their implementation;
- preparing the annual and medium–term financing plans and planning the annual interest expenditure based on the annual Budget Act and in line with the strategy;

4 The most important provisions concerning the financing of the deficit and government debt management, effective as of December 2012, are provided in Section 4 of the Appendix.

- performing the required financing operations, i.e. organising and implementing both domestic and international government securities issuance and raising of loans;
- managing the temporarily free cash funds of the state (liquidity management);
- effecting debt redemptions and interest payments;
- organising and continuously developing the government securities market (the primary dealer system, sales channels, secondary market etc.);
- expressing its opinion on the financial terms and conditions of borrowings with a state guarantee; on request, organising transactions with individual guarantees (with a lesser role for guarantees prescribed by legislation).

Organisational structure of GDMA Pte. Ltd.



X. THE INFORMATION SERVICES OF ÁKK

ÁKK provides information to the general public about the central government debt and the developments in the government securities market. It fulfils these tasks using several media: its website, other electronic communications systems and its publications.

The website at www.akk.hu[5] provides a wide range of information for anyone interested in the government securities market or the government debt. Already the homepage shows the most important data, such as the latest news, the current volume of government debt, the latest auction results and daily market yields (benchmark fixings).

Other pages of the website provide information on ÁKK as a company, on the characteristics of government securities, a separate section covers retail securities and another offers a wide range of information on the trading of government securities.

The 'Government Securities' menu provides access to the cash–flow tables of all government securities in the market, along with the latest public offerings. The 'Retail Securities' menu provides information to small investors about retail government securities and the Treasury's security trading operation for retail investors. The 'Market Information' menu contains the issuance calendar for the current year, the results of auctions and the most important secondary market information. The website provides databases as well, so historical data and time series of data can also be searched.

The 'Publications, Statistics' menu provides access to the publications of ÁKK in electronic (pdf) format, along with an ample range of statistical data about, among others, government debt, the volumes of various types of instruments and securities trading statistics. The menu also contains the public analyses prepared by ÁKK. The 'Pension Reform Fund' menu provides information about the Pension Reform and Debt Reduction Fund managed by ÁKK.

A newsletter service is offered to registered users of the website free of charge. Subscribers receive newly uploaded data by e–mail or an e–mail notification about newly added contents.

In addition to its website, ÁKK publishes auction and secondary market price quotation data on the information pages of Bloomberg and Thomson Reuters.

ÁKK holds regular press conferences on annual financing, the ranking of primary dealers and on other special topics. The press conference materials can also be found on ÁKK's website.

ÁKK also regularly informs interested readers in free publications. The following publications are available on the website:

- Annual reports (released in the third quarter of the year following the actual year);
- Debt Management Outlook publications (At the beginning of the actual year);
- Quarterly reports (the second month after the actual quarter);
- Monthly reports (at the end of the next month);
- Desktop issuance calendar (in December of the year preceding the actual year).

The Annual reports and Issuance calendar are also available in printed form from ÁKK.

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5 The site is also available at www.gdma.hu

APPENDIX

1. The central government gross debt as at 31. 12. 2013 (HUF million)

HUF denominated debt Hungarian Government Bonds	Maturity	Coupon	Outstanding amount
2014/A	02.05.2014	Floating rate	29,576.06
2014/B	20.12.2014	Floating rate	16,612.00
2014/C	12.02.2014	5.50%	439,478.19
2014/D	22.08.2014	6.75%	509,814.78
2014/I	11.08.2014	Floating rate	3,636.74
2015/A	12.02.2015	8.00%	594,591.11
2015/B	22.12.2015	Floating rate	201,293.12
2015/C	24.08.2015	7.75%	574,884.80
2015/I	08.12.2015	Floating rate	11,302.28
2015/J	11.01.2015	Floating rate	98,044.89
2015/L	28.11.2015	Floating rate	53,067.51
2015/K	19.03.2015	Floating rate	39,293.12
2016/A	31.12.2016	Floating rate	10,020.00
2016/B	02.01.2016	Floating rate	9,000.00
2016/C	12.02.2016	5.50%	802,510.06
2016/D	22.12.2016	5.50%	658,721.63
2016/I	28.11.2016	Floating rate	5,112.13
2016/J	02.05.2016	Floating rate	42,143.58
2017/A	24.11.2017	6.75%	909,942.17
2017/B	24.02.2017	6.75%	750,728.64
2017/I	05.03.2017	Floating rate	47,677.62
2018/A	20.12.2018	5.50%	531,433.89
2018/I	25.04.2018	Floating rate	42,615.64
2019/A	24.06.2019	6.50%	631,853.87
2019/B	20.05.2019	Floating rate	106,746.17
2020/A	12.11.2020	7.50%	567,132.21
2022/A	24.06.2022	7.00%	545,182.75
2023/A	24.11.2023	6.00%	577,199.62
2026/A	28.02.2026	Floating rate	51,165.00
2026/B	24.04.2026	Floating rate	70,177.72
2026/C	24.10.2026	Floating rate	3,975.04
2028/A	22.10.2028	6.75%	120,641.86
2032/S	02.12.2032	Floating rate	1,484.14
Matured, but unclaimed government bonds			83.37
Total:			**9,057,141.70**
Repos with government bonds (repos actually increase or decrease the total amount)			**66,591.22**
Discount Treasury Bills			**1,904,931.88**
Repos with discount Treasury bills (repos actually increase or decrease the total amount)			0.00
Interest Bearing Treasury Bills			**988,123.38**
Out of which matured, but unclaimed			37.30
Semi–annual Interest Bearing Treasury Bills			**21,261.74**
Out of which matured, but unclaimed			0.00
Treasury Savings Bills (Plus)			**3,987.75**
Treasury Savings Bills (1–year)			**253,138.86**
Treasury Savings Bills (2–year)			**77,600.42**
HUF loans			**603,577.95**
Matured, but unclaimed other retail government securities			53.57
Total HUF debt			**12,976,408.46**

Foreign currency debt	Outstanding amount (HUF million)	Outstanding amount (EUR million)
Syndicated loan and loans drawn down from revolving credit facilities*	**0.00**	**0.00**
Loans granted by International Financial Institutions*	**2,269,515.95**	**7,643.78**
of which: IMF and EC loans	**1,037,441.33**	**3,494.13**
Loans assumed from the market*	**466,097.21**	**1,569.83**

Government bonds

Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
115	EUR	29.01.2014	10	4.50%	287,863.15	969.53
116	GBP	06.05.2014	10	5.50%	178,370.37	600.76
120	USD	03.02.2015	10	4.75%	323,505.00	1,089.57
121	EUR	24.02.2020	15	3.875%	293,940.90	990.00
122	GBP	09.05.2017	12	5.00%	178,380.00	600.79
126	EUR	18.07.2016	10.5	3.50%	282,941.57	952.95
128	GBP	30.03.2016	10	5.00%	178,380.00	600.79
129	EUR	04.07.2017	10	4.375%	295,425.45	995.00
130	JPY	26.10.2017	10	2.11%	51,355.00	172.96
132	CHF	20.05.2016	8	4.00%	48,428.00	163.11
133	EUR	11.06.2018	10	5.75%	442,888.18	1,491.66
134	EUR	28.07.2014	5	6.75%	290,067.41	976.95
135	USD	29.01.2020	10	6.25%	431,340.00	1,452.76
136	USD	29.03.2021	10	6.375%	647,010.00	2,179.15
137	USD	29.03.2041	30	7.625%	269,587.50	907.98
138	EUR	11.01.2019	7	6.00%	290,081.07	977.00
139	USD	21.02.2023	10	5.375%	431,340.00	1,452.76
140	USD	19.02.2018	5	4.125%	269,587.50	907.98
141	USD	22.11.2023	10	5.75%	431,340.00	1,452.76
Total					**5,621,831.10**	**15,120.96**
Cross–currency swaps					**115,037.29**	

Premium Euro Hungarian Government Bond

Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
2015/X	EUR	21.12.2015	3	Floating rate	94,620.26	318.68
2016/X	EUR	25.05.2016	3	Floating rate	182,103.42	613.33
2016/Y	EUR	25.10.2016	3	Floating rate	123,825.25	417.05
Total					**400,548.93**	**1,349.06**

Residence Bond

Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
2018/T	EUR	20.12.2018	5	2,53%	31,917.83	107.50
Total					**31,917.83**	**107.50**
Total foreign currency debt					**8,904,948.31**	
Total central government debt					**21,881,356.77**	
Other obligations of ÁKK (marked–to–market deposits placed at ÁKK)					117,253.10	
Grand total					**21,998,609.87**	

** Including swaps*

2. THE CREDIT RATING HISTORY OF THE LONG–TERM DEBT OF HUNGARY

Foreign currency denominated debt

Date of change	Moody's	Standard and Poor's	Fitch Ratings
20.04.1992	–	BB+	–
27.12.1993	Ba1	BB+	–
25.04.1996	Ba1	BB+	BBB–
28.10.1996	Ba1	BBB–	BBB–
19.12.1996	Baa3	BBB–	BBB–
24.06.1997	Baa3	BBB–	BBB
08.05.1998	Baa2	BBB–	BBB
11.12.1998	Baa2	BBB	BBB
25.06.1999	Baa1	BBB	BBB
29.10.1999	Baa1	BBB	BBB+
02.02.2000	Baa1	BBB+	BBB+
14.11.2000	A3	BBB+	BBB+
29.11.2000	A3	BBB+	A–
19.12.2000	A3	A–	A–
12.11.2002	A1	A–	A–
06.12.2005	A1	A–	BBB+
22.01.2006	A1	A–	BBB+
26.01.2006	A1	A–	BBB+
15.06.2006	A1	BBB+	BBB+
22.12.2006	A2	BBB+	BBB+
05.11.2007	A2	BBB+	BBB+
17.03.2008	A2	BBB+	BBB+
17.10.2008	A2	BBB+	BBB+
07.11.2008	A3	BBB+	BBB+
10.11.2008	A3	BBB+	BBB
17.11.2008	A3	BBB	BBB
02.03.2009	A3	BBB	BBB
30.03.2009	A3	BBB–	BBB
31.03.2009	Baa1	BBB–	BBB
02.10.2009	Baa1	BBB–	BBB
23.07.2010	Baa1	BBB–	BBB
06.12.2010	Baa3	BBB–	BBB
23.12.2010	Baa3	BBB–	BBB–
06.06.2011	Baa3	BBB–	BBB–
11.11.2011	Baa3	BBB–	BBB–
24.11.2011	Ba1	BBB–	BBB–
21.12.2011	Ba1	BB+	BBB–
06.01.2012	Ba1	BB+	BB+
23.11.2012	Ba1	BB	BB+
20.12.2012	Ba1	BB	BB+

Moody's and Standard and Poor's assigned a 'negative' rating outlook, while Fitch Ratings assigned a 'stable' rating outlook to the long–term foreign currency debt of Hungary at the end of 2013

HUF denominated debt

Date of change	Moody's	Standard and Poor's	Fitch Ratings
25.04.1996	–	–	BBB+
28.10.1996	–	A–	BBB+
24.06.1997	–	A–	A–
22.06.1998	A1	A–	A–
02.07.1998	A1	A–	A
11.12.1998	A1	A	A
29.11.2000	A1	A	A+
19.12.2000	A1	A+	A+
19.11.2002	A1	A	A+
12.01.2005	A1	A	A
27.05.2005	A1	A–	A
06.12.2005	A1	A–	A–
22.01.2006	A1	A–	A–
26.01.2006	A1	A–	A–
15.06.2006	A1	BBB+	A–
22.12.2006	A2	BBB+	A–
05.11.2007	A2	BBB+	A–
17.03.2008	A2	BBB+	A–
17.10.2008	A2	BBB+	A–
07.11.2008	A3	BBB+	A–
10.11.2008	A3	BBB+	BBB+
17.11.2008	A3	BBB	BBB+
02.03.2009	A3	BBB	BBB+
30.03.2009	A3	BBB–	BBB+
31.03.2009	Baa1	BBB–	BBB+
02.10.2009	Baa1	BBB–	BBB+
23.07.2010	Baa1	BBB–	BBB+
06.12.2010	Baa3	BBB–	BBB+
23.12.2010	Baa3	BBB–	BBB
06.06.2011	Baa3	BBB–	BBB
11.11.2011	Baa3	BBB–	BBB
24.11.2011	Ba1	BBB–	BBB
21.12.2011	Ba1	BB+	BBB
06.01.2012	Ba1	BB+	BBB–
23.11.2012	Ba1	BB	BBB–
20.12.2012	Ba1	BB	BBB–

Moody's and Standard and Poor's assigned a 'negative' rating outlook, while Fitch Ratings assigned a 'stable' rating outlook to the long–term domestic currency debt of Hungary at the end of 2013

3. THE ADDRESSES OF PRIMARY DEALERS

Primary dealer	Address
BNP Paribas SA	Budapest, H–1051 Széchenyi tér 7–8.
CIB Bank Zrt.	Budapest, H–1027 Medve utca 4–14.
Citibank Europe Plc., Hungarian Branch Office	Budapest, H–1054 Szabadság tér 7.
Deutsche Bank AG	Budapest, H–1054 Hold u. 27.
ERSTE Befektetési Zrt.	Budapest, H–1138 Népfürdő u. 24–26.
Goldman Sachs International	133 Fleet Street London EC4A 2BB UK
ING Bank N.V.	Budapest, H–1068 Dózsa György út 84/b
J.P.Morgan Securities Plc.	25 Bank Street Canary Wharf, London E14 5JP UK
K&H Bank Zrt.	Budapest, H–1052 Vigadó tér 1.
MKB Bank Zrt.	Budapest, H–1056 Váci u. 38.
Magyar Takarékszövetkezeti Bank Zrt.	Budapest, H–1122 Pethényi köz 10.
OTP Bank Nyrt.	Budapest, H–1876 Nádor u. 16.
Raiffeisen Bank Zrt.	Budapest, H–1054 Akadémia u. 6.
UniCredit Bank Hungary Zrt.	Budapest, H–1054 Szabadság tér 5–6

4. SELECTED PARTS OF LEGISLATION GOVERNING THE LEGAL STATUS OF ÁKK AND GOVERNMENT DEBT MANAGEMENT*

Act no. CXCIV of 2011 on the economic stability of Hungary

CHAPTER II
REDUCTION OF GOVERNMENT DEBT

1. Definition and calculation of government debt

2. § (1) The current government debt index that should be taken into consideration in the course of the execution of the provisions stipulated in paragraphs (4) and (5) of Article 36 and paragraphs (2) and (3) of Article 37 of the Fundamental Law (hereinafter: the government debt index) is a quotient rounded to one decimal digit where

a) the dividend includes the value of the consolidated debt (debts after setting off debts owed by the central subsystem of the public finances, the local government subsystem of the public finances, general government and other organisations classified in the governmental sector to each other) (hereinafter jointly: government debt);

b) the divisor includes the value of the gross domestic product – calculated in accordance with the Council Regulation on the European system of national and regional accounts in the Community – as specified in this Act.

(2) The debt of the central subsystem of the public finances shall be the consolidated value of all transactions resulting in debts undertaken by legal persons belonging to the central subsystem of the public finances, as at the date of recording.

(3) The debt of the local government subsystem of the public finances shall be the consolidated value of all transactions resulting in debts which were undertaken by local governments, self–governments of minorities, regional development councils as defined in the Act on regional development and regional planning, multi–purpose microregional associations and other associations with legal personality (hereinafter jointly: local government), as at the date of recording.

(4) The debt of other organisations classified in the governmental sector shall be the consolidated value of all transactions resulting in debts which were undertaken by them on their own behalf, as at the date of recording.

3. § (1) Transaction resulting government debt and its value:

a) borrowing, assumption of credit and loan facility as from the date of disbursement or the date of assumption to date of repayment, and the actual principal amount,

b) issuance of debt securities according to Act on Accounting (hereinafter: Accounting Act) from the date of issuance to the date of redemption, in case of interest–bearing security its nominal value, in case of other security its purchase price,

c) issuance of bill of exchange as from the date of issuance to the date of redemption, and the value of such obligation – excluding the interest – exchanged by such bill of exchange,

d) pursuant to the Accounting Act, finance lease concluded as lessee during the term of the lease, and outstanding principal amount stipulated in the lease contract,

e) concluding sale and repurchase agreement (stipulating repurchase obligation) as seller – real reverse transactions and repo transactions combined with security deposit as defined in Act on Accounting are also included – until the date of repurchase and the stipulated repurchase price,

f) three hundred and sixty–five days of grace – at least – for deferred payment and/or payment by instalments granted in contract, and the unpaid consideration,

g) mark–to–market deposits and their sum, deposited as the difference of derivative transactions with Government Debt Management Agency Pte. Ltd. (hereinafter: 'GDMA Pte. Ltd.') by credit institutions.

(2) The prefinancing of debt maturing in the first six months of the budget year – which has an amount not exceeding the amount of expected payments during the first six months of the budget year – shall not be deemed as transaction resulting government debt under paragraph 1 in the previous budget year.

* This translation of the selected legal provisions serves only information purposes and is not an official translation

(...)

CHAPTER III
THE GOVERNMENT DEBT MANAGEMENT AGENCY

4. Legal status of the Government Debt Management Agency

11. § (1) Through GDMA Pte. Ltd. the minister responsible for public finances ensures the fulfilment of funding requirement of the central subsystem of public finances and ensures the financial operations executed in order to management of the debt falling under point a) b) e) and g) of paragraph (1) of Section 3.

(2) GDMA Pte. Ltd. is a single shareholder company (limited by shares), the company's shares are registered and non–negotiable securities.

(3) GDMA Pte. Ltd. is owned by the state, and the minister responsible for public finances exercises the rights related to the establishment and the ownership by and on behalf of the state, however, not entitled to absorb the rights of the Board of Directors.

(4) The operation of GDMA Pte. Ltd. – unless otherwise provided by the present Act – are governed by the Act on Business Associations.

(5) Executives of the state – as specified in the Act on central administrative agencies and the legal status of the Members of the Government and Secretaries of State – may hold positions on the Board of Directors and on the Supervisory Board of GDMA Pte. Ltd.

(6) The scope of authority of the Supervisory Board of GDMA Pte. Ltd. does not include the report on the debt management strategy of the central subsystem of public finances, the associated performance indicators and financing plans.

12. § (1) GDMA Pte. Ltd. manages its assets autonomously within the framework of laws and regulations, the decisions of the shareholder and the decisions of the Board of Directors.

(2) The revenues of GDMA Pte. Ltd. are:

a) the appropriation assigned for this purpose in the Annual Central Budget Act, in relation to debt management of the central subsystem of public finances arising out of debt transactions falling under point a) b) e) and g) of paragraph (1) of Section 3, which is to be placed at the disposal of the company in equal monthly instalments,

b) other revenues.

(3) The interest, cost, fee and other expenses associated with revenues according to point a) of paragraph (2) shall be booked and paid by GDMA Pte. Ltd. to the charge of the chapter of the Act on the Annual Central Budget including budgetary revenues and expenditures of debt management of the central subsystem of public finances.

(4) GDMA Pte. Ltd. holds a bank account at the National Bank of Hungary [(hereinafter: 'NBH')] for its operations.

(5) GDMA Pte. Ltd. holds a securities custody account and a securities account at the Central Clearing House and Depository PTE Ltd. [(hereinafter: 'KELER')], may open a foreign currency account at the NBH or at credit institutions for its operations.

13. § (1) In order to finance the deficit of the central budget, the minister responsible for public finances, through GDMA Pte. Ltd.

a) upon the authorization of the Central Budget Act, organizes the issuance of government securities, borrowing of loans and debt assumptions which shall be settled as debt of the central subsystem of public finances arising out of debt transactions falling under point a) and b) of paragraph (1) of Section 3,

b) elaborates the annual and medium–term financing plan of the central budget , develops the financing strategy of debt falling under point a),

c) ensures the payment obligations burdening the debt of central subsystem of public finances arising out of debt transactions falling under point a) and b) of paragraph (1) of Section 3,

d) ensures the solvency of the central government budget upon the authorization of the Annual Central Budget Act and by taking into account the forecast rendered in point b) of paragraph (1) of Section 76 by Act on the Public Finance, and the management of the temporarily free cash–funds of the state,

e) organises the secondary market of government securities,

f) executes dealing on own account on the secondary market of government securities, concludes security lending, repo and reverse repo transactions, concludes prompt, forward, hedge, swap and derivative transactions, and executes custodial and deposit management tasks, *g)* analyses the tendencies of the government debt service falling under point a) and the government securities market,

h) participates in the calculation of the government debt, provides information on developments of government debt of the central subsystem of public finances arising out of debt transactions falling under point a) b) e) and g) of paragraph (1) of Section 3, and on the tendencies in the government securities market,

i) opines the terms and conditions of loans and bonds secured by individual government suretyship or guarantee,

j) executes credit and deposit operations,

k) participates in performing duties related to borrowing loans and credits and issuance of debt securities guaranteed by government suretyship or guarantee,

(2) For participation specified in point i) of paragraph (1), GDMA Pte. Ltd. receives remuneration – burdening the central government budget – equalling to – 0.025 per cent of the principal amount of the underlying transaction as a maximum. The Government shall determine the detailed regulation of such duties and remuneration of GDMA Pte. Ltd. in a decree.

(3) GDMA Pte. Ltd. may create debt securities on the separated sub–accounts of the securities account specified in paragraph (5) of Section 12 – without outright issuance and underlying financial claims – which may become objects of transactions specified in point f) of paragraph (1).

(4) In addition to its duties specified in paragraph (1), GDMA Pte. Ltd:

a) upon authorisation by a separate law may organize issuance of debt securities secured by government suretyship or government guarantee, or may fulfil advisory tasks related thereto,

b) may participate in performing duties – advice related to business strategy also implied – related to borrowing loans and credits, or issuance of debt securities by the state, municipality and business organizations owned thereby through majority ownership, for a remuneration to such extent as determined in paragraph (2),

c) may participate in the management of the free cash funds of the State Deposit Insurance Fund, and performing duties – advice related to business strategy also implied – related to borrowing loans and credits, or issuance of debt securities of such Fund,

d) may participate in management and sale of the assets of the Pension Reform and Debt Reduction Fund,

e) may participate in the management of cash funds of the Investor Protection Fund.

14. § (1) The minister responsible for public finances ensures the management of the temporarily free cash–funds of the state through GDMA Pte. Ltd.. Within such duty, GDMA Pte. Ltd. is entitled to execute operations falling under paragraph (1) of Section 13. Interests arising out of such operations shall be settled in favour of the central budget.

(2) In government debt management related civil law legal relationships, the state shall be represented by the minister responsible for public finances, who may exercise such incumbency right through GDMA Pte. Ltd., or may delegate such incumbency right in writing to GDMA Pte. Ltd..

(3) Transactions concluded by GDMA Pte. Ltd. within the framework of government debt management shall be deemed as concluded in favour of and charged to the state.

(...)

5. THE BALANCE SHEET AND THE PROFIT AND LOSS ACCOUNT OF ÁKK

I. Balance sheet

data in HUF thousand

	Assets	2012	2013
	A) Fixed assets	73,564	87,995
I	Intangible assets	14,903	17,973
II	Tangible assets	43,617	58,548
III	Invested financial assets	15,044	11,474
	B) Current assets	325,314	313,787
I	Inventories	0	0
II	Receivables	15,497	11,077
III	Securities	0	0
IV	Cash and cash equivalents	309,817	302,710
	C) Accrued and deferred assets	88,632	27,133
	Assets in total	487,510	428,915

data in HUF thousand

	Liabilities	2012	2013
	D) Capital and reserves	354,914	354,914
I	Subscribed capital	300,000	300,000
IV	Profit reserve	54,914	54,914
VII	Balance–sheet profit or loss	0	0
	E) Provisions	0	0
	F) Liabilities	112,015	61,545
I	Subordinated liabilities	0	0
II	Long–term liabilities	0	0
III	Short–term liabilities	112,015	61,545
	G) Accrued and deferred liabilities	20,581	12,456
	Liabilities in total	487,510	428,915

Budapest, 19 May 2014

István Töröcskei
CEO

II. Profit and loss account

data in HUF thousand

	Liabilities	2012	2013
I	Net sales revenue	1,011,570	1,033,400
III	Other revenue	156,669	108,836
IV	Material expenses	420,237	364,530
V	Personnel expenses	703,554	748,365
VI	Depreciation and amortisation	29,283	31,210
VII	Other expenses	5,804	5,787
A	Operating profit or loss	9,361	–7,656
B	PROFIT OR LOSS FROM FINANCIAL TRANSACTIONS	23,764	15,266
C	PROFIT OR LOSS ON ORDINARY ACTIVITIES	33,125	7,610
D	EXTRAORDINARY PROFIT OR LOSS	0	0
E	PROFIT OR LOSS BEFORE TAXATION	33,125	7,610
XII	Tax payable	3,322	783
F	PROFIT OR LOSS AFTER TAXATION	29,803	6,827
23	Approved dividends	29,803	6,827
G	BALANCE–SHEET PROFIT OR LOSS	0	0

Budapest, 19 May 2014

István Töröcskei
CEO

6. SENIOR OFFICIALS OF ÁKK IN DECEMBER OF 2013

Members of the Board of Directors:

Kornél Kisgergely, chairman*
Dr. György Naszvadi, member
Viktor József Asztalos, member
** retired from 15 December 2013*

Members of the Supervisory Board:

Judit Gondos, chairman
Péter Benő Banai, member
Péter Fáykiss, member
Viktor Várpalotai, member

The Company's auditor:

DIAMANT Könyvvizsgáló Kft.
1223 Budapest, Gyula vezér u. 72.

Responsible auditor:
Terézia Bárány Director

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