GOVERNMENT DEBT MANAGEMENT AGENCY PTE LTD.

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REVISED DEBT MANAGEMENT OUTLOOK 2020

BUDAPEST, August 2020

Contents

1. Net financing requirements in 2020

The Government of Hungary adjusted the deficit target of the 2020 budget, because of the unfavorable economic outlook caused by the COVID-19 pandemic as well as fiscal policy actions intended to mitigate its economic impact. Due to the increased funding requirement and the partly changed market situation, the Government Debt Management Agency (ÁKK) updated its funding plan.

The deficit of the central government calculated on a ***cash basis*** is increased by HUF 1,710 billion, from HUF 1,890 billion **to HUF 3,600 billion**.

The total cash basis net financing requirement for the year 2020 is equal to the deficit of the central government and other items, such as the balance of EU transfers. These other financing needs are considered items that are to be handled by liquidity management (e.g. with discount T-bills).

2. Government debt redemptions

The total amount of government debt redemptions and pre-financing in 2020 is planned at **HUF 8,057 billion,** 17.5% of GDP, 21% less than in 2019.[1]

	2019 plan (HUF bn)	2019 actual (HUF bn)	May 2020 plan (HUF bn)	August 2020 plan (HUF bn)	August 2020 modified plan (EUR bn)
HUF debt maturities	6,823	7,685	6,134	6,068	17.0
Government bonds	1,204	1,309	1,086	1,081	3.0
Retail securities	4,355	5,124	4,344	4,283	12.0
Discount T-bills	1,250	1,237	657	657	1.8
HUF loans	14	14	47	47	0.1
FX debt redemptions	666	674	772	801	2.2
International bonds	423	415	545	546	1.5
Domestic bonds	207	214	143	145	0.4
IFI and other loans	36	45	83	111	0.3
Total maturities	7,489	8,385	6,906	6,869	19.3
Government bond buy-backs	250	744	285	285	0.8
Switch auctions	250	841	600	600	1.7
FX bond buy-backs		222	244	303	0.8
Total pre-financing	500	1,807	1,129	1,188	3.3
Total redemptions including pre-financing	7,989	10,165	8,034	8,057	22.6

[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 to avoid multiple counting.

The redemptions of domestic currency debt will amount to **HUF 6,068 billion,** 21% less than in 2019. FX currency debt maturities will amount to HUF 801 billion (EUR 2.2 billion), 19% more than in 2019**.** ÁKK will remain active in active debt management, HUF 885 billion domestic bond buy-backs and exchanges are planned and ÁKK have already executed USD bond buy-backs with a value of HUF 303 billion to reduce short term debt outstanding.

Domestic currency bond redemptions will amount to HUF 1,081 billion (HUF 228 billion less than the actual in 2019), discount T-bill redemptions will amount to HUF 657 billion (almost half of the 2019 plan). In order to reduce future refinancing risk, ÁKK plans to buy back (HUF 285 billion) and switch (HUF 600 billion) bonds maturing in 2021 or later (pre-financing). Large, but decreasing part of the domestic debt redemptions is the redemption of retail securities, out of which 80 per cent has already been executed by mid-August.

Foreign currency debt redemptions will total **EUR 2.2 billion** (HUF 801 billion) – a bit higher than the original maturities in 2019 –, out of which international bond redemptions will amount to EUR 1.5 billion, domestic bond redemptions will amount to EUR 0.4 billion, while the redemption of IFI and other loans will amount to EUR 0.3 billion. It is important to note that ÁKK has already paid back most international bond redemptions in Q1 2020.

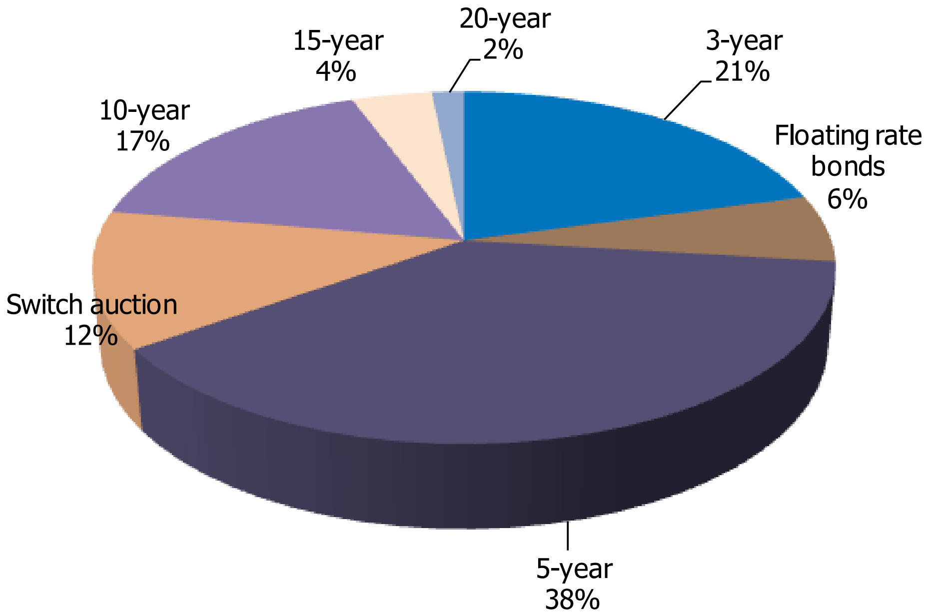
3. Gross issuance

Total gross issuance is planned at **HUF 11,946 billion** in 2020, 9% more than the actual in 2019. 86% of the total gross issuance (**HUF 10,301 billion**) will be in domestic currency and only 14% (**HUF 1,645 billion** or EUR 4.6 billion) will be in foreign currencies.

	2019 plan (HUF bn)	2019 actual (HUF bn)	May 2020 plan (HUF bn)	August 2020 plan (HUF bn)	2020 modified plan (EUR bn)
Domestic issuance	9,217	10,834	8,479	10,301	28.9
Government bonds	2,650	3,440	4,088	5,157	14.5
out of which via switch auction	*250*	*771*	*581*	*623*	*1.7*
Retail securities	5,155	6,683	3,344	4,165	11.7
Discount T-bills	1,250	657	873	801	2.2
HUF loans	162	55	174	178	0.5
FX issuance	32	146	1,621	1,621	4.6
International Bonds	0	0	1,408	1,404	4.0
Domestic Bonds	32	92	35	35	0.1
IFIs loans	0	54	178	206	0.5
Grand total	9,249	10,980	10,100	11,946	33.5

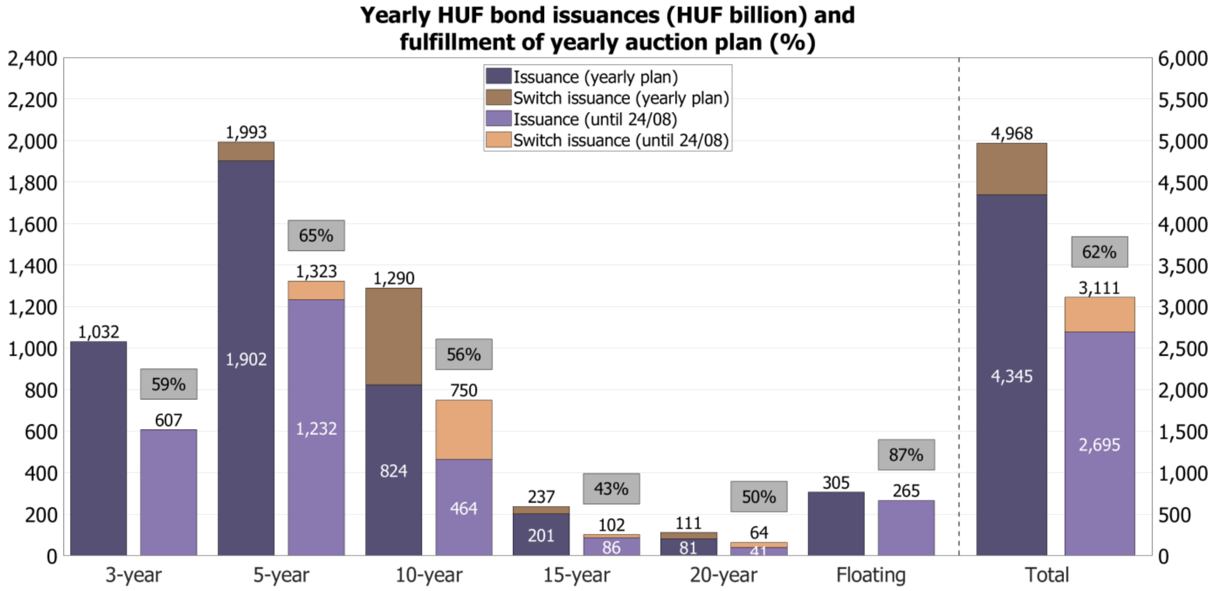
Domestic currency government bond issuance is planned at **HUF 5,157 billion**, which is 50% higher than in 2019. Including in this target, HUF 4,345 billion of government bonds will be offered at auctions, HUF 623 billion of bonds is expected to be sold at switch auctions, while other issuances (e.g. government bond for local authorities) are also included. The breakdown by tenor is expected to move towards longer terms in the original plan, for example a new 20-year bond was introduced. As a reaction to the COVID-19 pandemic, ÁKK changed the auction calendar in April 2020 and increased the flexibility of bond issuance. Fixed rate bond auctions will be held every week, 3- and 5-year bonds will be offered expectedly at all auctions. 10-year bond auctions will be offered in every second week, while 15- and 20-year auctions in every 8th week in general, but the actual volume of issuance will depend on market demand.

Breakdown of gross domestic government bond issuance by maturity



ÁKK have launched a new 3-year and 20-year fixed bond series in 2020, while for other tenors the currently on-the-run bonds will be offered until they reach the targeted volume. Therefore a new 5-year and a reopened 10-year (originally 15-year) bond series have been offered at auctions since the end of August due to the increased bond issuance. A new, longer term floating rate bond was issued in 2020, auctioned once a month. 12 months auctions are held every second Wednesday. The issuance calendar contains only the dates of bond and bill auctions. ÁKK may decide on the amounts offered after consultations with Primary Dealers.

ÁKK will hold both bond-buyback and exchange (switch) auctions – similar to the practice followed recently – in order to support a balanced government bond issuance pattern, manage the maturity profile, and reduce the refinancing risk of the bond portfolio by extending its average term-to-maturity. ÁKK's exchange auctions will also support the increasing demand for longer term and lower demand for shorter term government bonds of investors who will follow the new HMAX government bond benchmark index introduced in January 2020.



The financing plan contains EUR 4.6 billion equivalent of foreign currency debt issuance in 2020. International bond issuance is EUR 4 billion, out of that EUR 2 billion was already executed in April and further EUR 1.5 billion was executed in June (Green Bond). The remaining issuance will be in Japanese Yen. The issuance of the domestic FX bond (Premium Euro Hungarian Government Bond) is expected to provide a funding of EUR 100 million. ÁKK also plans to draw down IFI project financing loans (EUR 500 million) in foreign currency.

4. Net issuance

Net government debt issuance is planned in an amount of **HUF 3,888 billion**, almost five times higher that of the net issuance of HUF 814 billion in 2019. Out of this, net domestic debt issuance will reach **HUF 3,347 billion** (214% more than the HUF 1,564 billion in 2019), and net foreign currency borrowing will amount to **HUF 541 billion** (EUR 1.5 billion, as opposed to HUF -750 billion in 2019).

ÁKK will closely monitor the market and will decide on the amounts accepted at auctions according to bids. Net issuance covers the deficit of the central government and increases the liquidity reserves of the government. If there will be favorable liquidity conditions in the last months of 2020, ÁKK will increase the pro-active market operations to reduce the refinancing risk of coming years.

The stock of retail government securities is expected to **decrease by HUF 119 billion** (showing significant stabilisation based on the development of retail sales in the last months in comparison with the May plan of HUF 1,001 billion decline). The decline is due to the redemptions of retail securities held by non-household sectors (institutions) totaling HUF 900 billion, while the outstanding amount of retail government securities held by individuals is expected to increase significantly this year too.

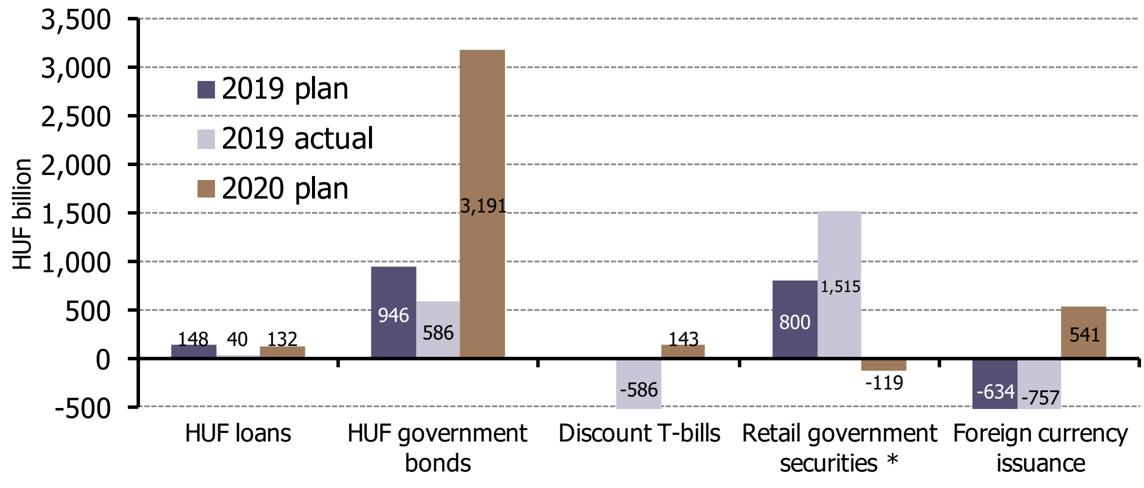
Due to the higher deficit ÁKK intends to increase net issuance of domestic debt, out of which net issuances of wholesale bonds are planned at **HUF 3,191 billion** (vs HUF 2,118 billion planned in May).

According to the plan the outstanding amount of discount T-bills will increase by **HUF 143 billion** (HUF 73 billion less than according to the plan in May), however, their outstanding volume can be increased more if needed for liquidity management purposes.

Net issuance of HUF loans will be **HUF 132 billion** from International Financing Institutions.

The total foreign currency redemption will amount to EUR 2.2 billion which is increased by the US dollar bond buy-backs. Gross foreign currency issuance is planned at EUR 4.6 billion, thus **the net foreign currency issuance is expected to amount to EUR 1.5 billion (HUF 541 billion) in 2020**. This amount may change in case of pre-financing by buying back bonds that have a short remaining term-to-maturity in the last months of the year.

Structure of the net issuance in 2020



* The outstanding amount of retail government securities held by individuals is expect to increase significantly this year too. The total outstanding stock of retail securities decreases due to the redemption of retail securities held by institutions.

5. Debt management strategy and benchmarks

ÁKK's mission is to finance the central government at the lowest costs in the long run, taking account of risks. In accordance with the economic policy of the government, ÁKK has set four main objectives:

1. According to the fundamental law of Hungary, if the debt to GDP ratio is higher than 50 percent, only such a budget can be approved, which

leads to the reduction of the debt ratio year by year. During the present state of danger due to COVID-19 and in case of a substantial decline of GDP, however, the basic law allows a temporarily increase of public debt. **The primary objective of debt management is still to support the reduction of the debt ratio**.

2. One of the main factors that led to the vulnerability of Hungary in the past was that a higher part of the government debt had been financed from abroad. Domestic savings and the domestic financing of the debt can support macroeconomic stability in the long term. Thus, the second objective of ÁKK is to enhance the domestic investor base by funding large part of the deficit via **retail financing**. During the COVID-19 pandemic, however, the retail program slowed down temporary in spring, it picked up again in the summer and based on this development ÁKK expects that the outstanding amount of retail government securities held by individuals will increase significantly this year too (the total outstanding stock of retail government securities decreases due to the redemption of retail instruments held by institutions totaling HUF 900 billion). Thus, the medium term objective of retail debt (held by households) reaching HUF 11,000 billion by 2023 is maintained.

3. The decreasing debt ratio and the increasing domestic financing enable to **maintain at a low level the share of foreign currency debt** within the total debt, which is the third objective of ÁKK.

4. From 2020 ÁKK introduced the objective to **increase the average life of the public debt**. In international comparison, the average term-to-maturity of the Hungarian debt is low, the share of maturing debt within one year is relatively high. ÁKK makes efforts to improve the maturity structure of the debt, and reduce the refinancing risk by increasing the ATM of the public debt.

In recent years, the debt to GDP ratio and the share of FX debt decreased significantly due to the prudent fiscal policy and the pursued debt management strategy. The share of FX debt is already favorable in regional comparison, acknowledged also by the major credit rating agencies, which upgraded Hungary to the investment-grade category in 2016 and upgraded Hungary's sovereign debt rating to BBB in 2019 (S&P and Fitch).

The mission of Hungary's government debt management is quantified by setting portfolio benchmarks, which are mainly based on a general optimal portfolio model taking into account both costs and risks. ÁKK has determined the following benchmark targets for government debt management in 2020, which were not modified:

- ***Share of foreign currency debt:*** The share of the foreign currency denominated debt within the total central government debt should be in the 10-20% range.

- ***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 60-80%, and that of the floating rate debt, which includes all short-term debt, between 20% and 40%. Within the **foreign currency denominated debt**, the share of the fixed rate elements should be in the range of 65-85%, and that of floating rate debt between 15% and 35% (this range changed considering the increased FX issuance and the swap market conditions this year).

- ***Average Time to Re-fixing (ATR):*** ÁKK measures the re-pricing (interest rate) risk with the common ATR indicator. In order to keep an acceptable level of refinancing risk, the ATR of the HUF debt portfolio is targeted to be above 3.5 years. In case of adequate demand, ÁKK can increase the ATR, without an upper limit.

- ***Average Term to Maturity (ATM):*** ÁKK introduced a new benchmark in 2020 to measure the refinancing risk of the debt as well. To reduce the refinancing risk the average term to maturity of the domestic debt should be above 4 years. In case of adequate demand, ÁKK intend to increase the ATM of the domestic currency debt portfolio.

- ***Liquidity:*** In order to maintain the continuously safe financing of the budget, a minimum target balance of the Treasury Single Account has been determined and ÁKK's objective is to keep the end-of-day actual balance over this level. Due to COVID-19 pandemic ÁKK intends to increase the level of TSA.

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

To maintain a safe level of liquidity reserves and access to several financing channels also remain the emphasized goals of financing in 2020. Besides keeping a liquidity buffer more than at least 6-weeks' financing requirements FX deposits are also available for liquidity management. Liquidity buffer was increased with the early execution of international bond issuances during 2020. These ensure that financing is secured even in the case of a few uncovered auctions. Successful bond buy-backs and switch auctions also increase financing safety by substantially decreasing the volume of domestic currency debt maturities.

6. Further information

This Debt Management Outlook publication was compiled based on information available before the end of August 2020. Thus, the projected figures for 2020 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, ÁKK will not change the set of instruments used, its strategic objectives or 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 regularly updated information on the financing needs, the debt transactions and the government debt. ÁKK also discloses until the 15^{th} 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 government bonds in 2020

Fixed rate government bonds

Date of auction	Date of settlement
02.01.2020	08.01.2020
16.01.2020	22.01.2020
30.01.2020	05.02.2020
13.02.2020	19.02.2020
27.02.2020	04.03.2020
12.03.2020	18.03.2020
26.03.2020	01.04.2020
09.04.2020	15.04.2020
16.04.2020	22.04.2020
23.04.2020	29.04.2020
30.04.2020	06.05.2020
07.05.2020	13.05.2020
14.05.2020	20.05.2020
21.05.2020	27.05.2020
28.05.2020	03.06.2020
04.06.2020	10.06.2020
11.06.2020	17.06.2020
18.06.2020	24.06.2020
25.06.2020	01.07.2020
02.07.2020	08.07.2020
09.07.2020	15.07.2020
16.07.2020	22.07.2020
23.07.2020	29.07.2020
30.07.2020	05.08.2020
06.08.2020	12.08.2020
13.08.2020	19.08.2020
19.08.2020	26.08.2020
27.08.2020	02.09.2020
03.09.2020	09.09.2020
10.09.2020	16.09.2020
17.09.2020	23.09.2020
24.09.2020	30.09.2020
01.10.2020	07.10.2020
08.10.2020	14.10.2020
15.10.2020	21.10.2020
22.10.2020	28.10.2020
29.10.2020	04.11.2020
05.11.2020	11.11.2020
12.11.2020	18.11.2020
19.11.2020	25.11.2020
26.11.2020	02.12.2020
03.12.2020	09.12.2020
10.12.2020	16.12.2020

Floating rate government bonds

Date of auction	Date of settlement
09.01.2020	15.01.2020
23.01.2020	29.01.2020
06.02.2020	12.02.2020
20.02.2020	26.02.2020
05.03.2020	11.03.2020
02.04.2020	08.04.2020
29.04.2020	06.05.2020
13.05.2020	20.05.2020
27.05.2020	03.06.2020
10.06.2020	17.06.2020
24.06.2020	01.07.2020
08.07.2020	15.07.2020
22.07.2020	29.07.2020
05.08.2020	12.08.2020
19.08.2020	26.08.2020
02.09.2020	09.09.2020
16.09.2020	23.09.2020
30.09.2020	07.10.2020
14.10.2020	21.10.2020
28.10.2020	04.11.2020
11.11.2020	18.11.2020
25.11.2020	02.12.2020
09.12.2020	16.12.2020

Issuance calendar of discount treasury bills in 2020

12-month discount T-bills

Code	Date of auction	Date of settlement	Date of maturity
D201223	09.01.2020	15.01.2020	23.12.2020
D201223	23.01.2020	29.01.2020	23.12.2020
D201223	06.02.2020	12.02.2020	23.12.2020
D210224	20.02.2020	26.02.2020	24.02.2021
D210224	05.03.2020	11.03.2020	24.02.2021
D210224	19.03.2020	25.03.2020	24.02.2021
D210224	02.04.2020	08.04.2020	24.02.2021
D210421	15.04.2020	22.04.2020	21.04.2021
D210421	29.04.2020	06.05.2020	21.04.2021
D210421	13.05.2020	20.05.2020	21.04.2021
D210421	27.05.2020	03.06.2020	21.04.2021
D210421	10.06.2020	17.06.2020	21.04.2021
D210630	24.06.2020	01.07.2020	30.06.2021
D210630	08.07.2020	15.07.2020	30.06.2021
D210630	22.07.2020	29.07.2020	30.06.2021
D210630	05.08.2020	12.08.2020	30.06.2021
D210825	19.08.2020	26.08.2020	25.08.2021
D210825	02.09.2020	09.09.2020	25.08.2021
D210825	16.09.2020	23.09.2020	25.08.2021
D210825	30.09.2020	07.10.2020	25.08.2021
D211020	14.10.2020	21.10.2020	20.10.2021
D211020	28.10.2020	04.11.2020	20.10.2021
D211020	11.11.2020	18.11.2020	20.10.2021
D211020	25.11.2020	02.12.2020	20.10.2021
D211020	09.12.2020	16.12.2020	20.10.2021
D211229	23.12.2020	30.12.2020	29.12.2021

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 the following Wednesday.