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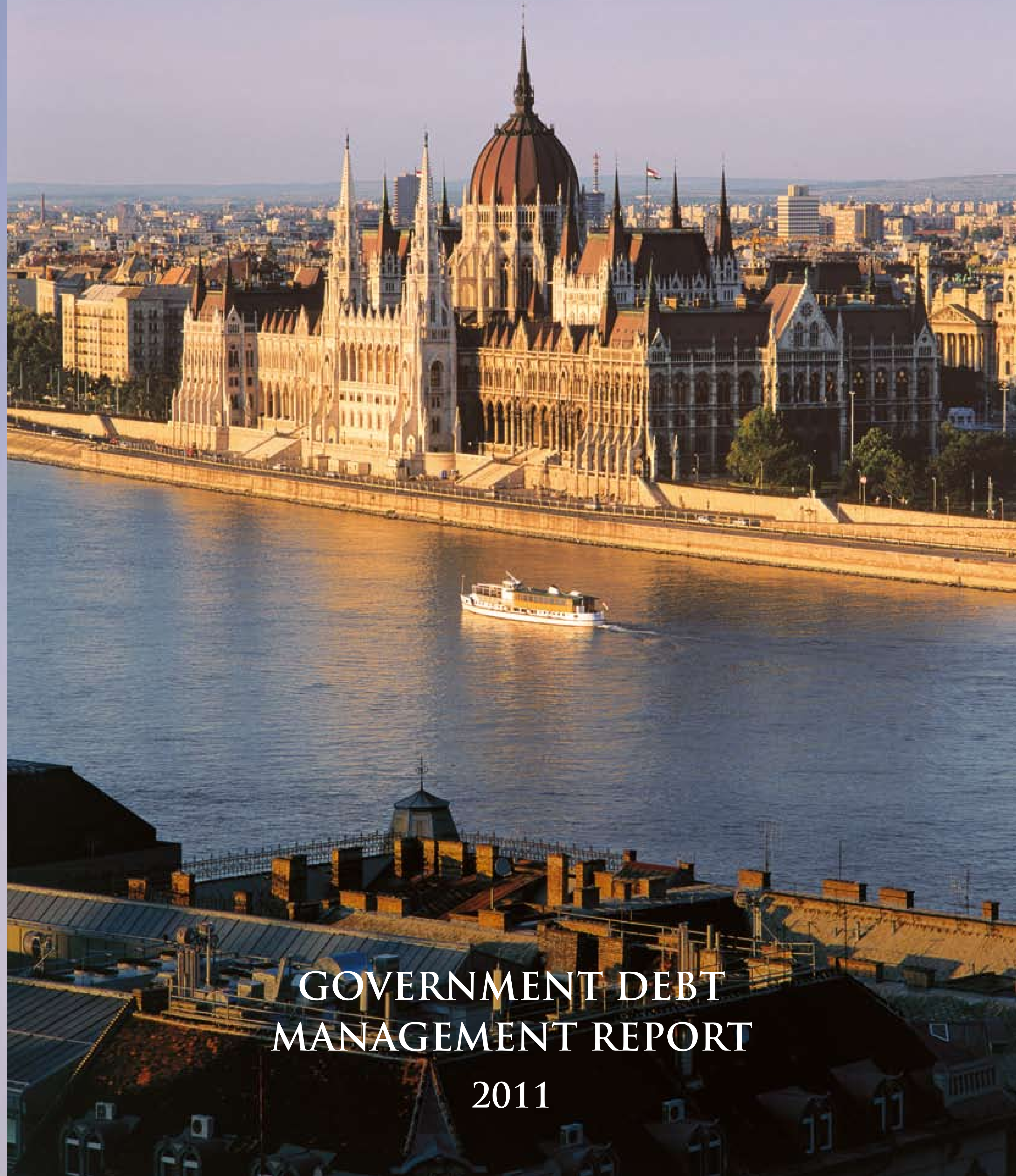
GOVERNMENT DEBT MANAGEMENT AGENCY
PRIVATE COMPANY LIMITED BY SHARES



GOVERNMENT DEBT MANAGEMENT REPORT

2011

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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 2011.

2011 was a particularly important year for public debt management. The international financial crisis hit hard the Hungarian securities market in 2008 in the form of substantial capital outflow and domestic bond sell-off by non-resident investors. After the full return to market financing in 2010, the Hungarian public debt management started to repay the international assistance in 2011 – the first country to do so with the redemption of EUR 2 bn to the European Community. This goal was fully met: the total annual foreign currency issuance target of EUR 4 billion was achieved already by May with a series of highly successful international bond transactions. Investors' demand was also favourable during the year in the domestic bond market and the actual net domestic bond issuance well exceeded the annual plan.

It is clear that the most important objectives for last year were achieved, however, the task of managing the public debt for a small and very open economy like Hungary in the period of the EMU crisis is still challenging.

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:

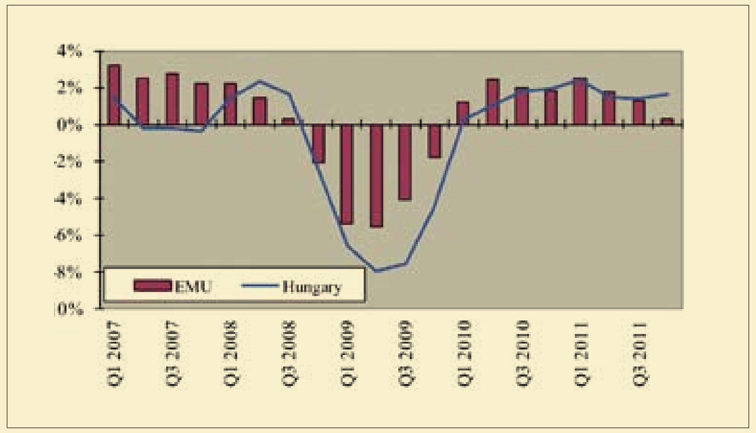
- Government bonds and retail government securities are recorded at nominal value.
- Discount treasury bills are recorded at the *average sale* price (at discount value), which is recalculated after every transaction involving the security concerned.
- Repo and reverse repo transactions actually increase 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 calculated by ÁKK is the central government gross debt (i.e. it does not include either local government debt or the debt of state-owned enterprises) 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 differ 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 calculated in accordance with ESA '95 principles is jointly produced and published by the Hungarian Central Statistical Office (HCSO), the National Bank of Hungary (NBH) and the Ministry for National Economy, and is based only partly on information provided by ÁKK.

I. MACROECONOMIC DEVELOPMENTS IN 2011

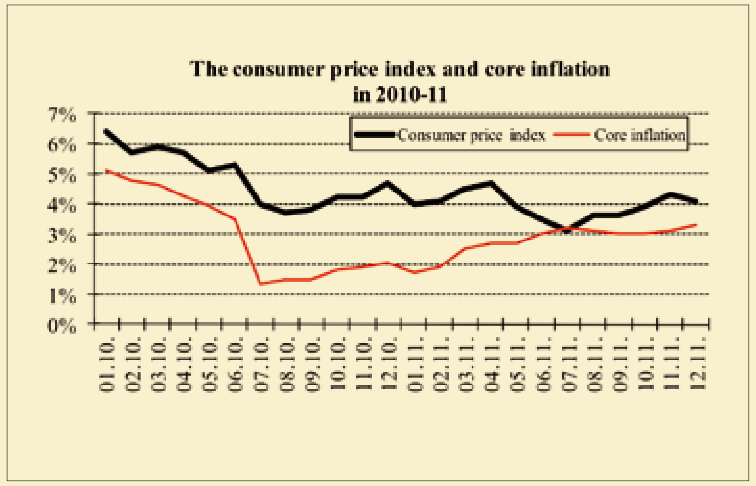
Improving investor sentiment observed in the first half of 2011 gave way to increased concerns regarding the public debt situation in the Eurozone amid rising uncertainties regarding the possibilities of a Greek default. Ireland, Portugal, Spain and Italy also served as cause for concern for investors. This situation, which made it clear that a tighter fiscal cooperation and at the same time a looser monetary policy is needed in the European Union, also had an impact on the local government bond markets in the CEE region.

Economic Growth



Source: HCSO, Eurostat

Compared to the previous year the Hungarian economy grew by 1.7% in 2011. The main sources of growth were net exports and investments. Exports grew by 14.1% in Q1 2011, and by less than 10% afterwards; investments also peaked in the first quarter with an increase of 8.8%, but decreased slightly afterwards. Consumption remained roughly unchanged over the year.

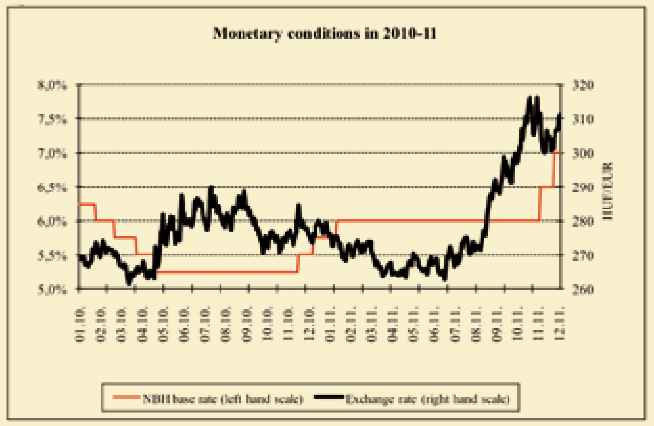


Source: HCSO

Inflation oscillated between 3.1% and 4.7% in 2011. Globally increasing energy and food prices pushed inflation upwards, while ailing domestic demand weakened the inflationary pressure. In the first half of the year the strong domestic currency also helped to decrease inflation. From the autumn of 2011 the good harvest made the food price increase decelerate, but the depreciation of the HUF contributed to rising inflationary pressures. In December, the CPI stood at 4.1%, while core inflation – excluding food and energy prices – was 3.3%. In 2011 the yearly average inflation was 3.9%.

Until the end of August the exchange rate of the Hungarian forint against the euro moved in a band between 260 and 280 HUF/EUR. In this period the exchange rate was relatively stable, due to the favourable market reactions to fiscal policy data.

In January the National Bank of Hungary raised its base rate by 25 basis points to 6%, and kept the rate at this level until November 2011.



Source: NBH

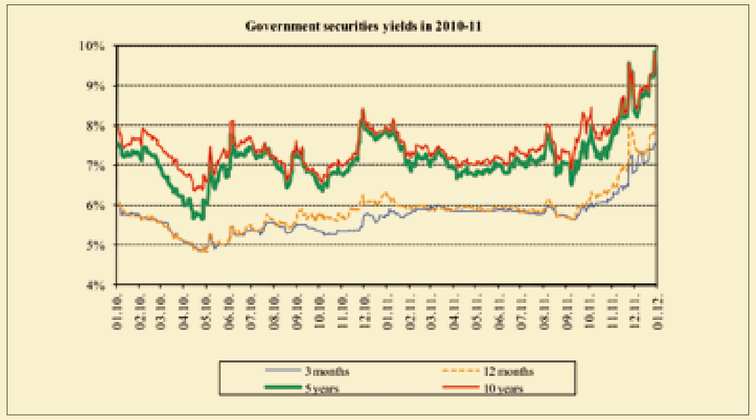
Starting in September CEE currencies weakened substantially, partly as a result of the escalation of the Eurozone debt crisis and because of the deterioration of both the global and the domestic growth prospects. The central bank's Monetary Council raised the base rate two times in November and December by 50-50 basis points citing rising inflation expectations and the deterioration of Hungary's risk profile. As a result, at the end of the year the central bank's base rate stood at 7% and the exchange rate was around 310 HUF/EUR.

The cash-flow based deficit of the central government (excluding local governments) reached HUF 1,734 billion in 2011, amounting to 6.2% of GDP according to data compiled by the Hungarian State Treasury. Several one-off measures increased the deficit: the purchase of the shares of MOL, the reimbursement of VAT following the decision of the Court of Justice of the European Union, the capital increase of the Hungarian Development Bank and the assumption of the debt of the regional municipalities and MÁV. These measures accounted for HUF 1,115 billion in deficit. The accrual-based surplus of the general government (including local governments and taking into account the restructuring of the pension fund system) according to ESA'95 methodology reached HUF 1,180 billion in 2011, amounting to 4.2% of GDP. The net financing needs of the state for the year 2011 increased compared to the previous year.[1]

Households became net borrowers in 2011 to the tune of 4.3% of GDP, mainly because of the capital transfers in connection with the pension reform. Without this effect the net savings of households would have increased from 4.4% in 2010 to 5.2% in 2011. At the same time the net financing capacity of the corporate sector reached 2.5% of GDP as a result of falling investment activity, up from the 2.1% in 2010. The Hungarian economy as a whole showed a net financing capacity of 1.9% of GDP. The current account balance reached a surplus of EUR 1.4 billion in 2011 equalling 1.4% of GDP.

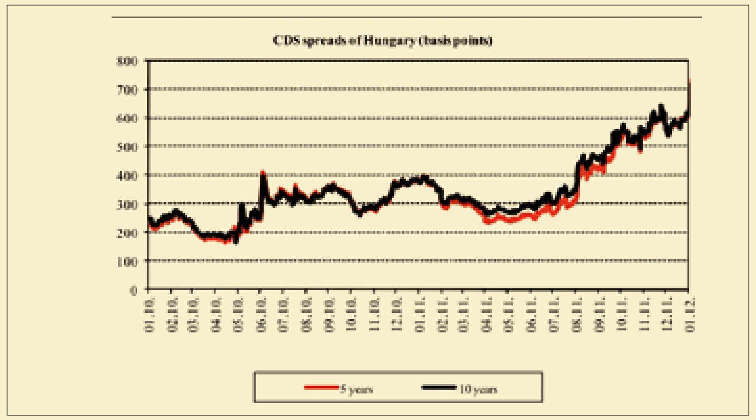
1 The components of the net financing need are described in detail in Chapter III.

The first eight months of the year was a time of further post-crisis consolidation. Investors' confidence towards Hungary strengthened and the country issued several international bonds denominated in US Dollar and euro in the spring. In the autumn tension appeared in the government securities markets and it continued to grow. On the whole, demand for government securities was strong in 2011, enabling ÁKK to cover its net domestic financing needs by bond issues. However, in the fall the demand at auctions was generally lower and there were also unsuccessful auctions.



Source: ÁKK

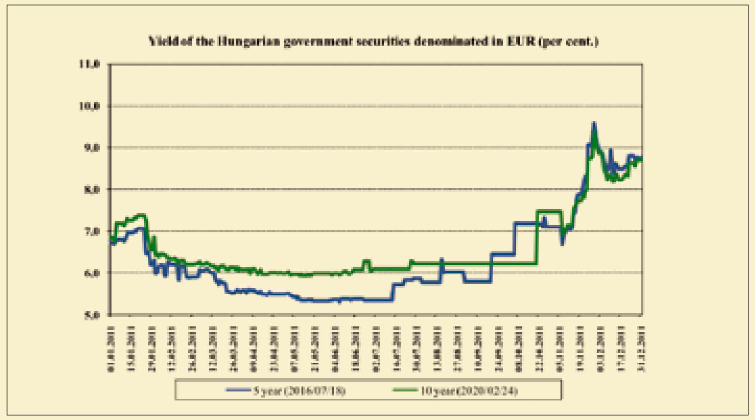
Government securities yields in the secondary market fell significantly in the first months of 2011. Short-term yields decreased below 6% and yields on the longest – 10-year and 15-year – tenors also hovered around the 7% level, due to the good reception of the "Széll Kálmán Plan". Starting in mid-September both short-term and long-term yields started to increase. The most important factors behind this were the same that caused the depreciation of the forint: the escalation of the Eurozone debt crisis and the deteriorating global and domestic growth prospects. By the end of the year the further rise of the short-term yields was also the consequence of the central bank's monetary tightening with investors pricing in further possible rate hikes; and the long-term yields also rose to above 9%.



Source: Bloomberg

In the spring of 2011 the 5-year CDS spread decreased from 278 bps to 234 bps, backed by the favourable global investors' sentiment and the announcement of the "Széll Kálmán Plan". Until August the CDS spreads remained in a relatively low range, but afterwards rose sharply to 610 bps by the end of the year amidst a worsening international investor sentiment.

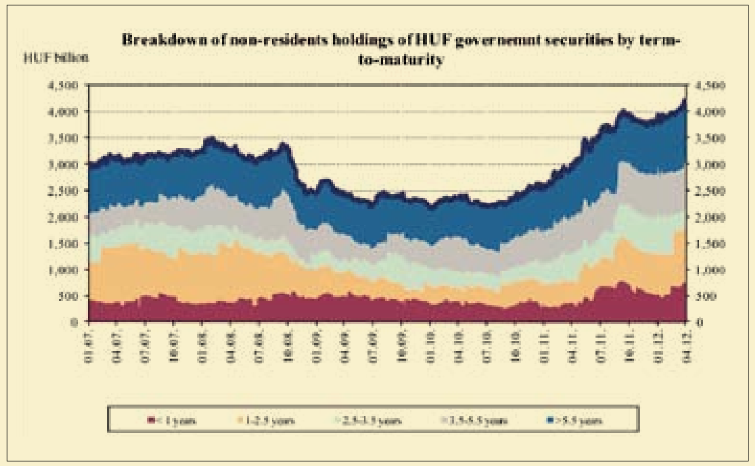
Beside the CDS spreads the yields of the euro denominated bonds issued by the Hungarian sovereign were influenced by the euro benchmark bond yields as well.



Source: Bloomberg

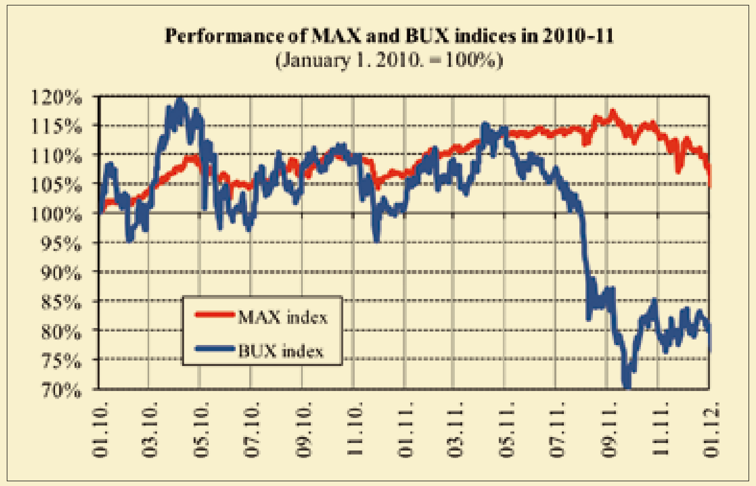
The yield of the July 2016 euro bond rose from 6.7% to 7.0% and then fell back to around 5.5% by end-March. In November the yield increased steeply to above 9.5%, which was followed by a partial correction.

The stock of government securities held by non-residents grew dynamically by HUF 1,482 billion to 4,015 billion from the end of 2010 until the end of September 2011. This was followed by a period of decrease and the non-resident holdings stood at HUF 3,797 billion at the end of 2011, up by HUF 1,264 billion from the previous year. It is still very favourable that foreign investors prefer to buy longer dated government securities; bonds make up 92% of their holdings while by T-bills account for only 8%.



Source: KELER

The share of HUF denominated government securities held by non-residents increased from 24% to 39% within the total marketable domestic debt (or 18% of the total government debt). Adding their foreign currency holdings as well to that (including the EU/IMF loans), foreign lenders account for 68% of the total government debt (including both HUF and foreign currency denominated debt).



Source:
ÁKK, Bloomberg

BUX, the main index of the Budapest Stock Exchange (BSE), increased rapidly to above 24,000 points from 22,000 points in the first quarter of 2011. However, by August-September the index fell to below the 15,000 point level, but later showed a partial correction upwards. Over the whole year the BUX index value decreased by 20%.

II. DEBT MANAGEMENT STRATEGY IN 2011

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 may 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 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 2011 the composition of the central government debt conformed to the benchmarks.

Public debt management benchmarks

Benchmarks	Tolerance band	End 2010	End 2011
1. Foreign currency debt ratio	25-50% FX	43.4%	49.6%
2. Foreign currency debt composition	95-105% EUR	99.8%	99.6%
3. Fixed coupon part of foreign currency debt	62.7- 67.7%	65.7%	64.7%
4. Fixed coupon part of domestic debt	61-83%	70.2%	70.5%
5. Duration of domestic debt	2-3 years	2.65	2.58

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 2011 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 500-800 billion (approximately EUR 2-3 billion) in 2011, 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.

III. THE FINANCING REQUIREMENTS IN 2011

THE COMPONENTS OF THE FINANCING REQUIREMENTS

The most important part of the net financing requirements is the deficit of the central government. The balance of the central government consists of the balances of three subsystems of government administration: the central budget, social security funds and extra-budgetary funds.[2] ÁKK is responsible for financing the central government and maintaining its continuous liquidity, while local authorities manage their own budgets, financing and debt management.

The total annual net financing requirement financed by ÁKK is the sum of the central government deficit and other, extra-budgetary transfers (privatisation revenues, 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 2007 and 2011:

	2007	**2008**	**2009**	**2010**	**2011**
Central government balance*	-1,394.4	-864.7	-739.9	-837.8	-1,718.4*
Balance of the Social Security funds	35.6	-73.4	-151.0	-95.6	-83.3
Balance of the extra-budgetary funds	63.0	28.0	-30.4	61.6	67.2
Net financing need of the central* government*	**-1,295.8**	**-910.0**	**-921.3**	**-871.9**	**-1,734.4***
Capital transfers to NBH	-20.6	-2.8	0.0	0.0	-29.1
Privatisation revenues	67.3	3.1	1.1	30.1	36.7
Net EU transfers	217.8	29.2	35.7	-125.1	406.6
Total net financing requirements*	**-1,031.3**	**-880.5**	**-884.5**	**-966.9**	**-1,320.2***
Short term debt redemptions	-2,343.2	-2,262.3	-1,988.7	-2,048.6	-1,922.3
Long term debt redemptions	-1,817.5	-1,280.4	-2,349.4	-1,752.7	-2,500.6
Gross financing requirements*	**-5,192.0**	**-4,423.3**	**-5,222.6**	**-4,768.2**	**-5,743.2***

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

2 The definitions of the government sub-systems and the tasks of ÁKK are stipulated in Act no. XXXVIII of 1992 on Public finances, as amended several times. Certain relevant provisions are quoted in Part 4 of the Appendix of this publication.

THE NET FINANCING REQUIREMENT

In 2011 the total cash-flow based deficit of the central government was HUF 1,734 billion (or 6.2 per cent of GDP according to preliminary data), while the total net financing requirement amounted to HUF 1,320 billion (or 4.7 per cent of GDP). The central government deficit significantly exceeded the original plan. However, the higher deficit was basically due to one-off items, like the purchase of the shares of MOL – Hungarian Oil Company – and the assumption of loans from the MÁV state railway company and from municipal authorities. These transactions actually did not require market financing. The net financing requirements – the net of these transactions - were actually lower than the original plan.

Borrowing requirements in 2011 - plans and outturn:

	Plan published in Dec. 2010 (HUF billion)	Outturn (HUF billion)	Outturn/Plan (per cent)	Outturn (HUF billion)*	Outturn/Plan (per cent)*
Central government balance	-605.0	-1,718.4	284%	-973.7	161%
Balance of the Social Security funds	-98.0	-83.3	85%	-83.3	85%
Balance of the extra-budgetary fund	15.0	67.2	448%	67.2	448%
Net financing need of the central government	**-689.0**	**-1,734.4**	**252%**	**-989.8**	**144%**
Capital transfers to NBH	0.0	-29.1	-	-29.1	-
Privatisation revenues	0.0	36.7	-	36.7	-
Net EU transfers	-171.0	406.6	-238%	406.6	-238%
Total net financing requirements	**-860.0**	**-1,320.2**	**154%**	**-575.6**	**67%**
Short term debt redemptions	-1,851.0	-1,922.3	104%	-1,922.3	104%
Long term debt redemptions	-2,166.0	-2,500.6	115%	-2,500.6	115%
Gross financing requirements	**-4,877.0**	**-5,743.2**	**118%**	**-4,998.5**	**102%**

* Excluding the assumption of local authorities' and MÁV's (state railway) debt and the purchase of shares of the company MOL in 2011 (these transactions did not require market financing).
Source: Hungarian State Treasury, Ministry for National Economy, ÁKK

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, 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.

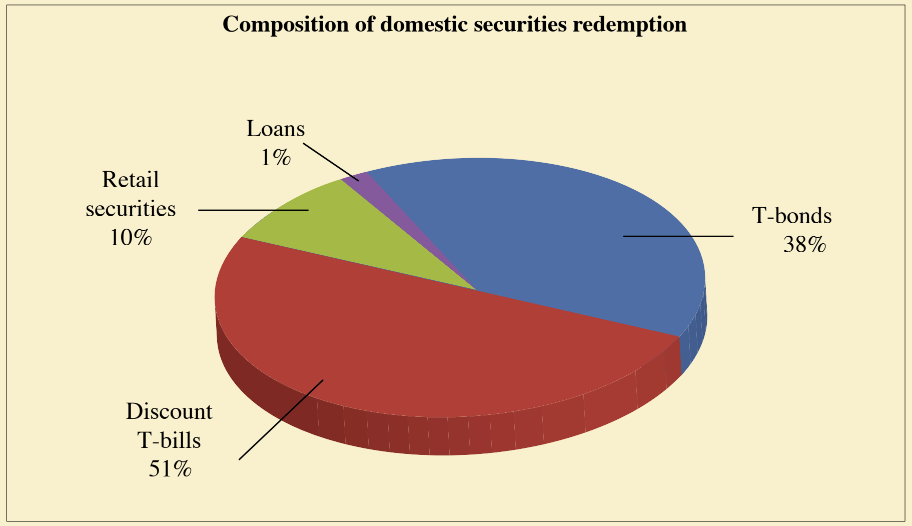
Government debt redemptions

HUF billion

	2010	2011 plan	2011 outcome
Domestic debt	**3,432.3**	**2,820.6**	**3,158.5**
T-bonds	1,383.3	925.0	1,191.6
Discount T-bills	1,647.3	1,618.2	1,618.2
Retail securities	401.7	276.7	304.2
Loans	0.0	0.0	44.5
Foreign currency debt	**369.0**	**1,187.7**	**1,264.5**
Bonds	331.6	557.9	552.1
Loans	37.3	629.8	712.4
Total	**3,801.3**	**4,008.3**	**4,422.9**

Source: ÁKK

Total domestic debt redemptions exceeded the plan by HUF 339 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 51 per cent of the total forint redemptions of HUF 3,159 billion, due to their renewals within the year. Foreign currency redemptions only changed due to the movement of exchange rates. In 2011 2 foreign currency bonds – EUR 1 billion each – matured and a EUR 2 billion loan was repaid to the European Community. Beside these items other smaller repayments took place in the case of IFI project financing loans and foreign currency loans taken over from local authorities.



Source: ÁKK

BOND BUY-BACKS

A large series of bonds 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 therefore includes a regular bi-weekly bond buy-back program, the actual outcome of which depends on the quantity and quality of bids from Primary dealers. In 2011 on 17 occasions ÁKK bought back a total of HUF 181 billion bonds before their maturity. 86 per cent of the repurchased bonds had an original maturity after 2011, i.e. these buy-backs also helped to smooth maturities from one year to another and to reduce the volume of outstanding bonds maturing in 2012. At exchange auctions ÁKK exchanged HUF 104 billion short-term bonds to long-term ones on 6 occasions in 2011.

DEBT CANCELLATION FROM THE PENSION REFORM AND DEBT REDUCTION FUND

As a result of the reform of the pension system the state-run Pay-As-You-Go system took over the vast majority of pension obligations from the mandatory (2nd pillar) private pension funds and the assets previously managed by these funds amounting to HUF 2,957 were transferred to the Pension Reform and Debt Reduction Fund. Close to 50 per cent of these assets consisted of Hungarian government securities that were transferred by the Fund to the state and immediately cancelled. Also, after the Fund fulfilled its payment obligations to the budget, all additional revenues were used to reduce public debt. Altogether there were 3 transactions in 2011 that reduced the public debt. In June HUF 1,354 billion of securities were cancelled. Next month HUF 10 billion and EUR 7 million were cancelled. The last transaction was in December when a further HUF 53 billion of domestic government securities were cancelled. Despite the fact that these securities were mainly liquid domestic bonds, according to trading data the cancellations had a minor effect on the secondary market liquidity.

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. However, debt management activities were significantly influenced by the prevailing macroeconomic environment and the situation in the government securities market – in particular the effects of the international financial market crisis. In 2011 the HUF denominated issuance amounted to HUF 3,650 billion, while foreign currency issuance was HUF 1,278 billion. The domestic issuance exceeded the original plan mainly because of the increased bond issuance reflecting strong demand from investors, while foreign currency issuance was close to the plan.

Gross debt issuance:

HUF billion

	2010	2011 plan	2011 outcome
Domestic debt	**3,909.6**	**3,459.7**	**3,649.8**
T-bonds	1,798.6	1,373.5	1,766.4
Discount T-bills	1,618.2	1,803.5	1,540.9
Retail securities	390.6	282.7	342.5
Loans	102.1	0.0	0.0
Foreign currency debt	**406.0**	**1,344.0**	**1,277.8**
Bonds	387.3	1,120.0	1,063.0
Loans	18.7	224.0	214.8
Total	**4,315.6**	**4,803.7**	**4,927.6**

Source: ÁKK

Net HUF denominated financing totalled HUF 491 billion, while net foreign currency financing amounted to HUF 13 billion, i.e. the total net issuance in 2011 was HUF 505 billion.

Net issuance:

HUF billion

	2010	2011 plan	2011 outcome
Domestic debt	**477.3**	**639.2**	**491.3**
T-bonds	415.3	447.8	574.8
Discount T-bills	-29.1	185.3	-77.3
Retail securities	-11.0	6.0	38.3
Loans	102.1	0.0	-44.5
Foreign currency debt	**37.1**	**156.3**	**13.4**
Bonds	55.7	562.1	511.0
Loans	-18.6	-405.8	-497.6
Total	**514.3**	**795.5**	**504.7**

Source: ÁKK

In the net HUF issuance, the role of long-term debt (bonds) increased in line with the increasing investor demand. The total T-bond sales of HUF 575 billion actually exceeded the total net domestic issuance. The outstanding volume of discount Treasury bills decreased by HUF 77 billion as a reaction to the good liquidity position, while net issuance of retail securities increased by 38 billion in 2011 (for the first time for many years). Early redemptions of HUF loans taken over from local authorities reduced net issuance by HUF 45 billion.

In 2011 the net foreign currency financing was close to zero, the capital market issuance and project loan financing basically financed maturing foreign currency debt.

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 PDs. Three bond series were sold at each auction. Usually the 3, 5 and 10-year tenors were offered, but the 10-year bond was replaced quarterly with the 15-year fixed rate bond and the 5-year floating rate bond. ÁKK also used more actively 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 10 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 percent of their winning bids at the average price of the auction.

ÁKK sold a total of HUF 1,645 billion of bonds via auctions (including HUF 245 billion at non-competitive tenders). Total bond issuance – together with bond exchange auctions and the retail sales of the Hungarian State Treasury – was HUF 1,766 billion, against total bond maturities of HUF 1,192 billion resulting in a HUF 575 billion net issuance, i.e. HUF 127 billion higher than planned.

On-the-run bond series in 2011 (HUF billion):

	Tenor	No. of auctions	Auction sales in 2011	Non-competitive sales in 2011	Outstanding (end of 2011)
2014/C	3 year	1	20	2	677
2014/D	3 year	25	578	103	606
2015/B	5 year	12	75	14	118
2016/C	5 year	4	67	16	769
2017/A	5 year	13	214	35	419
2017/B	5 year	9	177	35	748
2020/A	10 year	1	10	2	506
2022/A	10 year	19	218	35	240
2028/A	15 year	6	41	3	41

Source: ÁKK

In line with the strategy benchmark bond sizes are between HUF 500 and 800 billion (EUR 2 to 3 billion), except for the 15-year bond (HUF 250 billion or EUR 1 billion). ÁKK adjusted the amounts accepted at the auctions according to demand, and the results show that the demand was higher 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 fluctuations in liquidity caused by the varying financing requirements over the year. For this purpose ÁKK may also use so-called liquidity discount treasury bills of even shorter tenor (usually 6 weeks). In addition to liquidity management, the stock of discount treasury bills outstanding on a longer term may also serve as an alternative source of financing.

In 2011 ÁKK sold discount treasury bills in a total of HUF 1,541 billion, less than in 2010. ÁKK originally planned a net discount T-bill issuance of HUF 185 billion, however, as a reaction to higher bond sales and the better than expected liquidity position, the outstanding T-bill stock actually decreased by HUF 77 billion over the year. Higher T-bond sales basically limited the role of Treasury bills to liquidity management, and to a lesser extent in financing, which helped to improve the duration characteristics of the domestic debt.

RETAIL SECURITIES

One of the strategic objectives of ÁKK is to maintain a retail government securities issuance programme, which constitutes a third financing channel beside the local and the international wholesale markets. With growing savings of households it is advantageous for the Government to tap this source of funds as well. In spite of the fierce competition of banks for retail savings, after a long period of decline the stock of retail government securities started to increase in 2011. Most of the net sales was due to the success of the new inflation-linked "Premium Government Bond" with a net sale of HUF 31 billion. The total retail debt stock grew by HUF 38 billion over the year.

FOREIGN CURRENCY FINANCING

In 2011 ÁKK issued three foreign currency bonds in the international capital markets, which covered the whole planned issuance of foreign currency debt for the year.

Foreign currency bond issued by the Republic of Hungary in 2011:

Currency	Amount	Date of issuance	Maturity	Tenor (years)	Coupon
USD	3,000,000,000	29.03.2011	29.03.2021	10	6.38%
USD	750,000,000	29.03.2011	29.03.2041	30	7.63%
USD	500,000,000	11.04.2011	29.03.2041	30	7.63%
EUR	1,000,000,000	11.05.2011	11.01.2019	7	6.00%

Source: ÁKK

In 2011 the government drew HUF 215 billion (EUR 800 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.

V. THE GOVERNMENT DEBT IN 2011

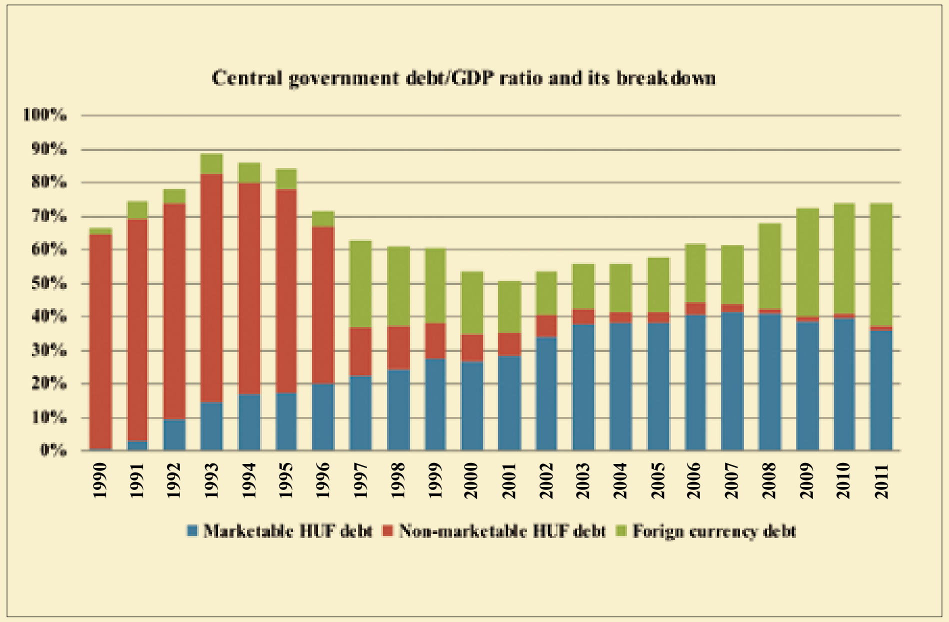
During 2011 the central government debt increased by HUF 914 billion (or by 4.6 per cent) to HUF 20,956 billion. The rise of the debt stock was due to deficit financing (accounting for 22 per cent of the total increase), the depreciation of the HUF in case of the foreign currency debt (56 per cent) and the increase of marked-to-market deposits (22 per cent).

Central government debt

	2010		2011		HUF billion Change
Domestic debt	**10,978.2**	**54.8%**	**10,362.2**	**49.4%**	**-616.0**
Loans	540.8	2.7%	590.8	2.8%	50.0
Government bonds	8,383.6	41.8%	7,756.7	37.0%	-626.9
Discount T-bills	1,618.2	8.1%	1,540.9	7.4%	-77.3
Retail securities	435.7	2.2%	473.8	2.3%	38.1
Foreign currency denominated debt	**8,842.8**	**44.1%**	**10,170.4**	**48.5%**	**1,327.7**
Loans	4,292.8	21.4%	4,458.1	21.3%	165.3
Bonds	4,550.0	22.7%	5,712.3	27.3%	1,162.3
Total debt	**19,821.0**	**98.9%**	**20,532.6**	**98.0%**	**711.6**
Other obligations	**220.0**	**1.1%**	**422.9**	**2.0%**	**202.9**
Grand total debt	**20,041.0**	**100.0%**	**20,955.5**	**100.0%**	**914.5**

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 peaked at 88.7 per cent in 1993, after the economic decline following the end of the centrally planned economy. From the mid-1990s the debt ratio decreased rapidly – thanks to the stabilisation of economic policy – until 2001, when it began to grow again until 2010. According to preliminary data, this trend stopped in 2011 and the debt/GDP ratio actually declined from 74.9 per cent at the end of 2010 to 74.4 per cent at the end of 2011.



Source: : ÁKK

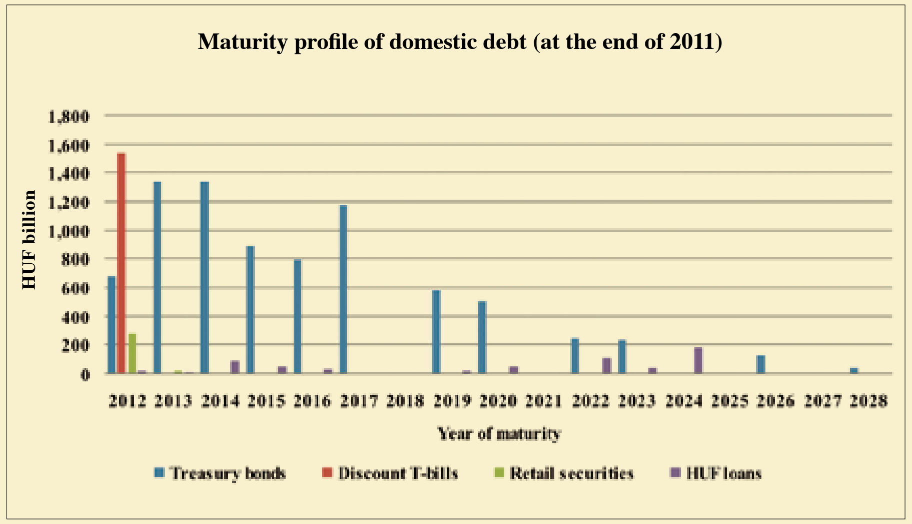
CHARACTERISTICS OF THE HUF DEBT PORTFOLIO

During 2011 the HUF-denominated debt that accounts for 50 per cent of the total debt decreased by HUF 616 billion (5.6 per cent) to HUF 10,362 billion. Deficit financing alone would have increased domestic debt, however, as a result of debt cancellations in connection with the pension reform, the domestic debt stock actually decreased. 37 per cent of the entire debt was in the form of long-term HUF government bonds at the end of 2011. The total domestic bond portfolio of HUF 7,757 billion consisted of 26 bond series, so the average size of a series was HUF 298 billion (EUR 1 billion). Eight series had a volume in excess of HUF 500 billion (ca. EUR 1.7 billion), and the largest bond series reached HUF 769 billion (or EUR 2.5 billion).

The HUF 1,540 billion discount T-bill stock consisted of eighteen series, with an average volume of HUF 86 billion at the end of 2011. Out of these five series had a volume in excess of HUF 100 billion, their average volume being HUF 200 billion. The total portfolio of retail government securities was worth HUF 474 billion at the end of the year, which corresponded to 4 per cent of the total HUF debt.

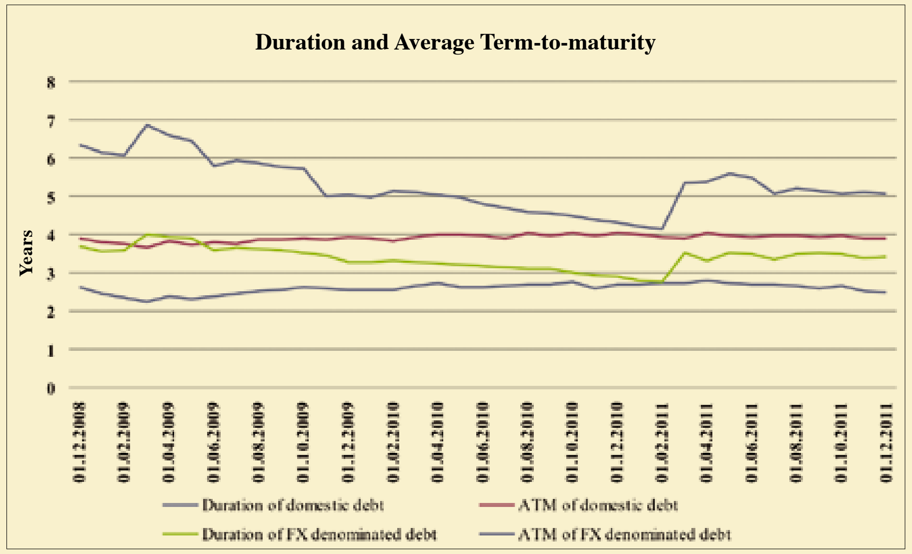
The non-marketable component of the HUF bond portfolio continued to decrease in amount and proportion in 2011 as well, as there are no new issuances of such government bonds and the existing portfolio matures continuously. The end-of-year volume of non-marketable government bonds was HUF 403 billion, which was only 4 per cent of the total HUF denominated debt. The volume of loans denominated in Hungarian forint increased in 2011 by HUF 50 billion to HUF 591 as a result of debt assumptions.

As a result of the increased bond issuance and the bond buy-back and exchange auction programmes, the maturity profile of the bond portfolio remained balanced. Bond maturities in 2012 are low and the share of bonds maturing after 2014 increased.



Source: ÁKK

The duration of the HUF denominated debt portfolio decreased from 2.65 years to 2.58 years in 2011. The average term-to-maturity also decreased a little from 4 to 3.9 years.

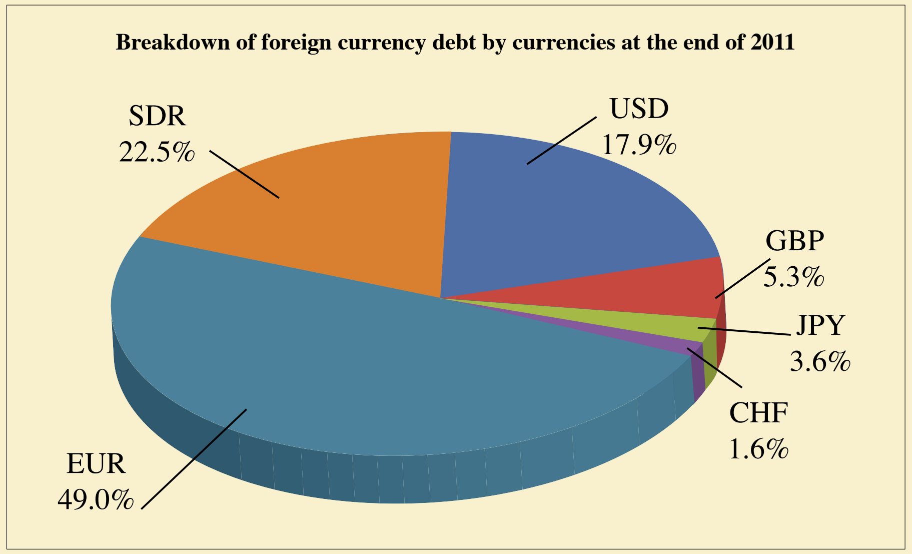


Source: ÁKK

CHARACTERISTICS OF THE FOREIGN CURRENCY DEBT PORTFOLIO

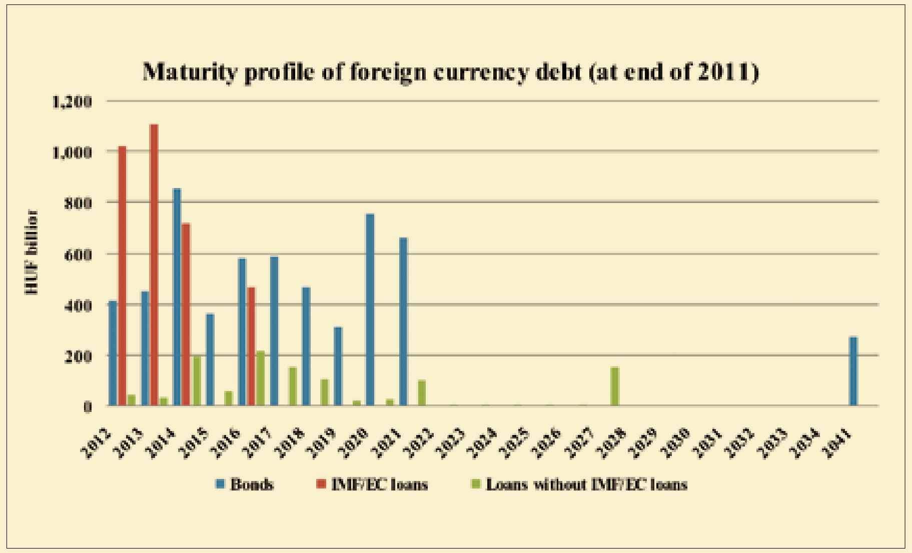
The gross foreign currency government debt increased by HUF 1,328 billion in 2011, reaching HUF 10,170 billion (EUR 33 billion) by the end of the year. Accordingly, within the total gross government debt, the share of foreign currency debt (excluding marked-to-market deposits) was 49 per cent at the end of 2011. The increase in the foreign currency debt was largely due the depreciation of the HUF, net issuance had only an insignificant effect on the value of the foreign currency debt.

The volume of outstanding foreign currency bonds (after swaps) reached HUF 5,712 billion by the end of the year, significantly higher than at the end of 2010 (HUF 4,550 billion), as a result of refinancing of the maturing EUR 2 billion EC loan from the market. On 31 December 2011 there were 22 series of foreign currency bonds outstanding, 10 of which had been issued in euro, four in US dollar, two in Swiss franc, three in Pound sterling and three in Japanese yen. In accordance with the strategy and benchmarks, all non-euro bonds have been converted into euro liabilities through swap transactions.



Source: ÁKK

The foreign currency loan portfolio of HUF 4,458 billion (EUR 15 billion) consisted of long-term project financing loans from international financing institutions (e.g. EIB and CEB loans), as well as loans from the IMF and EC and made up 44 per cent of the total foreign currency debt.



Source: ÁKK

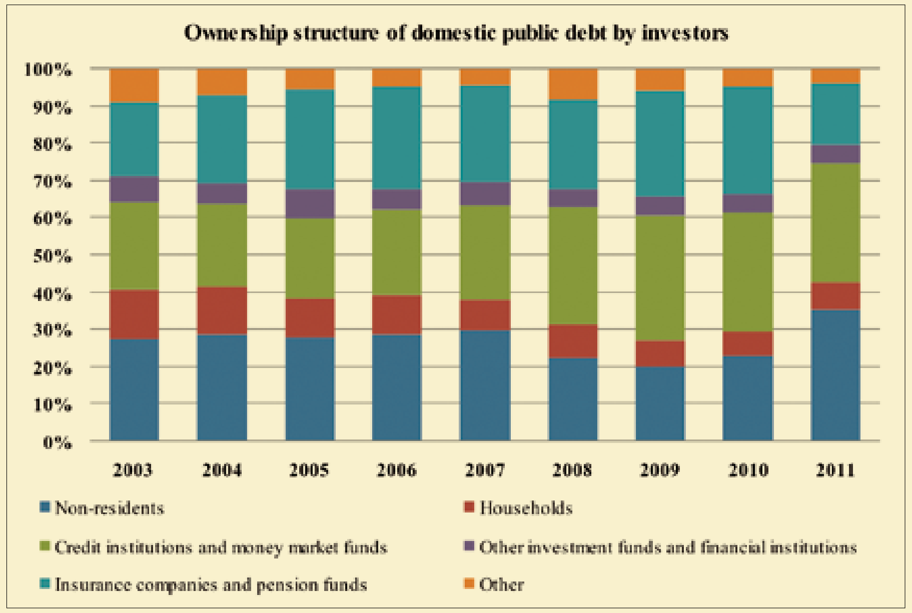
During 2011 the average life of the foreign currency portfolio increased substantially as a result of long term market financing: ATM increased by 0.8 years to 5.1 years, while its duration increased by 0.5 years to 3.4 years.

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. The Republic of Hungary has bilateral CSAs and similar mark-to-market agreements supplementing the ISDA Master Agreement. Such deposits placed with ÁKK are non-financing funds and they are shown as part of the government debt along with other obligations. As of 31 December 2011 marked-to-market deposits placed with ÁKK totalled HUF 423 billion (EUR 1.5 billion), which was HUF 203 billion higher than at the end of 2010.

THE OWNERSHIP STRUCTURE OF GOVERNMENT DEBT

According to statistics published by the National Bank of Hungary, the ownership structure of domestic government securities changed substantially in 2011. Since Q4 2010 non-resident investors have continued to increase their portfolio and now they are the biggest investors with a 35 per cent share in the local market up from 23 per cent a year before. Credit institutions constitute the second largest investor group with a stable 32 per cent share. Pension funds / insurance companies had a decreasing share – mainly as a result of the pension reform – from 29 per cent to 16 per cent. After a decline in the previous years, retail investors increased their share from 6.7 per cent to 7.4 per cent and maintained their fourth place among the holders of government securities.



Source: NBH, KELER, ÁKK

VI. LIQUIDITY MANAGEMENT

Under the Public Finances Act, liquidity management of the central government is also the task of ÁKK. The goal of ÁKK[3] is to maintain the balance of the Single Treasury Account (STA) which serves as a financing reserve for the budget at a so-called optimal level by using liquidity management operations if needed. 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 the banking system has sufficient demand, and otherwise it leaves the extra cash on the STA. In 2011 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.

Sales of liquidity discount treasury bills took place relatively evenly throughout the year: ÁKK sold HUF 650 billion on 13 occasions in 2011 (up from HUF 430 billion in 2010).

Liquidity repo transactions are ÁKK's main tool for fine-tuning the end-of-day balance of the Single Treasury Account. In 2011 the use of repo transactions decreased significantly to a total of HUF 5,597 billion concluded on 166 business days, down from HUF 11,351 billion in 2010. Liquidity management was effective, since the end-of-day STA balance was higher than the minimum target level on each day and the 50% original relative variance of the daily STA balance was reduced to 28% by liquidity T-bill and repo operations.

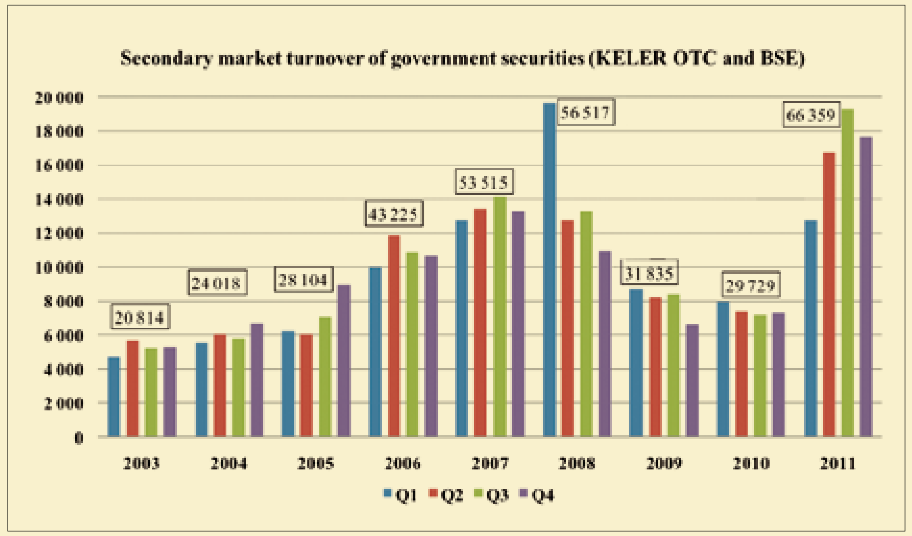
ÁKK concludes repo transactions not only for liquidity management purposes. The objective of the so-called stand-by repo transactions is to support the price quotation of primary dealers and to promote trading in government securities. If a primary dealer needs temporary access to a quoted government 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.

[3] Article 113/A, paragraph (1), section b).

VII. THE SECONDARY MARKET OF HUNGARIAN GOVERNMENT SECURITIES

TRADING DATA

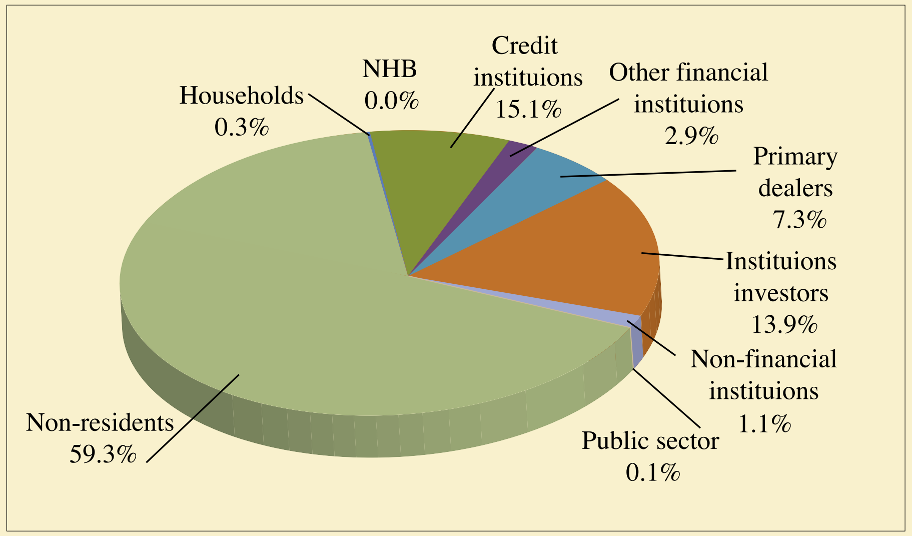
Primary dealers trade in the Budapest Stock Exchange's electronic trading system (MMTS) and also directly in the over-the-counter (OTC) market. As in previous years, the vast majority of secondary trading in government securities took place in the OTC market in 2011. According to data from the Central Clearing House and Depository (Budapest) Ltd. (KELER), the total volume of OTC trading in government securities was HUF 66,075 billion in 2011 (about 6 times the size of the total outstanding marketable debt), out of which 74 per cent was in government bonds and 26 per cent in discount treasury bills. After the rapid decline in 2008-9, secondary market turnover continued to increase in 2011 and reached the pre-crisis volume. In 2011 government securities trading on the Budapest Stock Exchange (BSE) amounted to HUF 284 billion.



Source: KELER, BSE

The average size of deals with primary dealers (excluding retail transactions) was HUF 983 million, 70 per cent higher than the HUF 582 million a year before showing increased foreign interest on the market. Over the year, the 3-year 2014/C government bond had the largest turnover (HUF 9,604 billion), followed by the 5-year 2016/C and 3-year 2014/D bonds.

The most active Primary Dealer and the winner of the title 'Primary Dealer of the Year' for 2011 was Citibank Europe Plc.



Source:
Primary dealers,
ÁKK

VIII. THE INSTITUTIONAL FRAMEWORK FOR THE ISSUANCE OF GOVERNMENT SECURITIES

ÁKK sells government securities through intermediaries. In the domestic market, 90 per cent of HUF-denominated government securities were sold through the primary dealers in 2011, 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.

PRIMARY DEALERS AT THE END OF 2011:

BNP Paribas SA
CIB Bank Zrt.
Citibank Europe Plc.
Deutsche Bank AG.
Erste Befektetési Zrt.
ING Bank N.V.
Goldman Sachs International
K&H Bank Zrt.
MKB Bank Zrt.
Magyar Takarékszövetkezeti Bank Zrt.
Nomura International Plc
OTP Nyrt.
Raiffeisen Bank Zrt.
The Royal Bank of Scotland Plc
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 auctions and exchange auctions; [4]
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'.

[4] Other investors may submit bids at an auction indirectly, through a 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 19 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 internet-based securities service.

The Hungarian Post Office participates in the sale of two retail government securities. The 1 and 2-year Treasury Savings Bills are the only printed government securities, designed specifically for retail investors.

THE DEALERS OF INTERNATIONAL BOND ISSUES

Lead managers of international bond issuances are selected from among the primary dealers individually for each transaction.

IN 2011 THE LEAD MANAGERS OF THE BONDS WERE AS FOLLOWS:

USD Bonds: BNP Paribas, Citigroup, Deutsche Bank
EUR Bond: Deutsche Bank, ING, Unicredit

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

The government debt management is regulated by Act no. XXXVIII of 1992 on Public Finances (the Public Finances 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 Public Finances Act, the minister responsible for public finances performs these tasks through the Government Debt Management Agency Pte. Ltd. (ÁKK).[5]

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 ÁKK's operations are stipulated partly by the Public Finances Act – which prescribed its establishment – and partly 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.

THE FOUNDATION AND THE ORGANISATIONAL STRUCTURE OF ÁKK

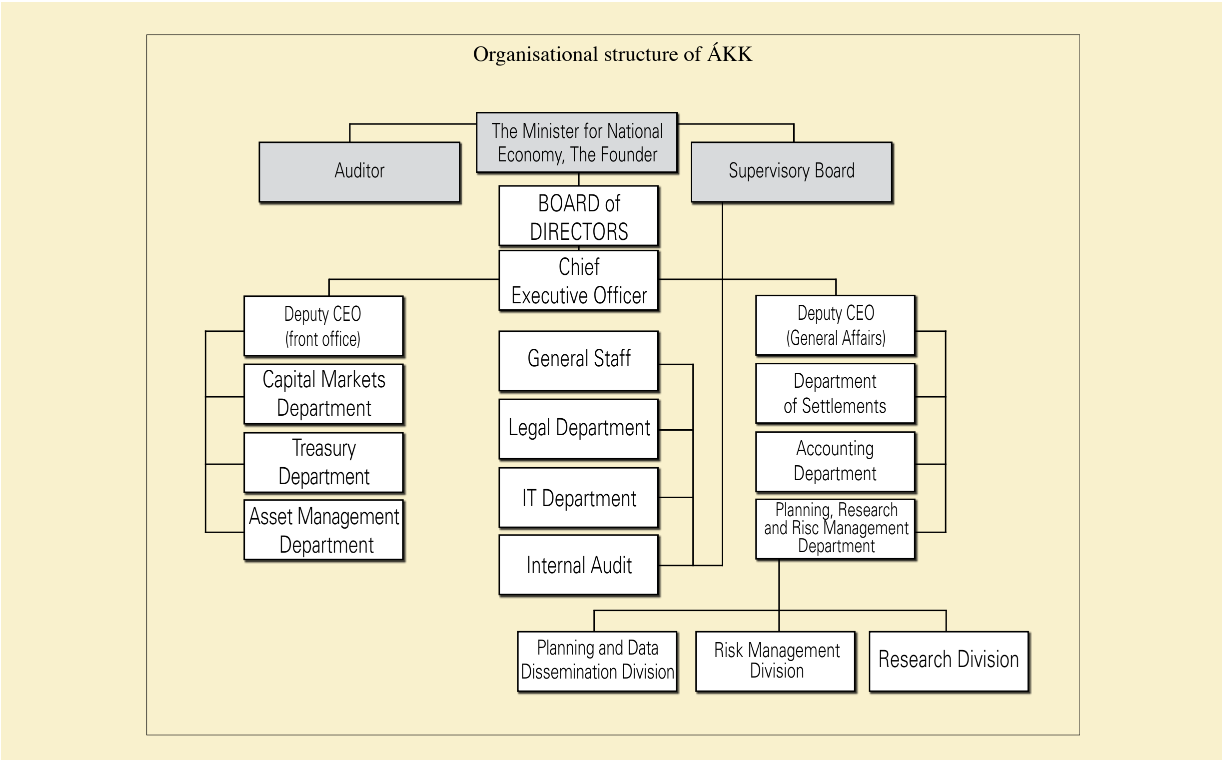
The Government Debt Management Agency was established in May 1995 as a budgetary institution under the supervision of the Ministry of Finance. In 1996 supervision of the agency was taken over by the Chairman of the Hungarian State Treasury. The amendment of the Public Finances Act that prescribed the 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. 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.

[5] The most important provisions concerning the financing of the deficit and government debt management, effective as of December 2011, are provided in Section 4 of the Appendix.

THE RESPONSIBILITIES OF ÁKK

According to the provisions of Article 113/A of the Public Finances Act, 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;
- 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 sys tem, 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).



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[6] 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. From 2011 a new *'Pension Reform Fund'* menu was added, which 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 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 in hard copy or can be downloaded from the website:

- annual reports (released in the third quarter of the year following the actual year);
- Debt Management Outlook publications (from the beginning of the actual year);
- quarterly reports (from the second month after the actual quarter);
- desktop issuance calendar (from December of the year preceding the actual year).

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

The Debt management Outlook and Monthly reports are available in electronic format on the ÁKK website.

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APPENDIX

1. The central government gross debt as at 31.12.2011 (HUF million)

HUF denominated debt

Hungarian Government Bonds	Maturity	Coupon	Outstanding amount
2012/A	31.12.2012	8.40%	1,426.43
2012/B	12.06.2012	7.25%	294,496.41
2012/C	24.10.2012	6.00%	321,526.46
2012/I	25.01.2012	Floating rate	38,385.70
2013/A	20.03.2013	Floating rate	76,666.97
2013/C	20.12.2013	Floating rate	127,928.00
2013/D	12.02.2013	6.75%	447,937.60
2013/E	24.10.2013	7.50%	579,858.55
2013/I	25.01.2013	Floating rate	70,607.24
2013/J	26.08.2013	Floating rate	28,946.69
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%	676,585.86
2014/D	22.08.2014	6.75%	606,302.55
2014/I	11.08.2014	Floating rate	4,195.73
2015/A	12.02.2015	8.00%	754,346.51
2015/B	22.12.2015	Floating rate	117,985.99
2015/I	08.12.2015	Floating rate	16,549.63
2016/A	31.12.2016	Floating rate	16,700.00
2016/B	02.01.2016	Floating rate	9,000.00
2016/C	12.02.2016	5.50%	769,288.90
2016/I	28.11.2016	Floating rate	7,501.84
2017/A	24.11.2017	6.75%	419,129.17
2017/B	24.02.2017	6.75%	747,732.30
2019/A	24.06.2019	6.50%	578,419.13
2020/A	12.11.2020	7.50%	506,052.86
2022/A	24.06.2022	7.00%	240,369.22
2023/A	24.11.2023	6.00%	237,056.35
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%	41,124.03
Matured, but unclaimed government bonds			317.27
Total:			**7,907,943.21**
Repos with government bonds (repos actually increase or decrease the total amount)			14,902.00
Discount Treasury Bills:			**1,540,097.56**
Repos with discount Treasury bills (repos actually increase or decrease the total amount)			1,689.46
Out of which matured, but unclaimed discount Treasury bills			820.29
Interest Bearing Treasury Bills			**81,217.92**
Out of which matured, but unclaimed			1,084.18
Treasury Savings Bills (1-year)			**176,403.89**
Treasury Savings Bills (2-year)			**49,927.80**
HUF loans			**590,825.47**
Matured, but unclaimed other retail government securities			54.83
Total HUF debt			**10,362,192.95**

Foreign currency debt	Outstanding amount (HUF million)	Outstanding amount (EUR million)
Loans granted by International Financial Institutions*	**4,280,756.61**	**13,758.74**
of which: IMF and EC loans	**3,314,480.95**	**10,653.04**
Loans assumed from the market*	**177,343.35**	**570.00**

Government bonds

Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
113	EUR	06.02.2013	10	4.50%	305,218.53	981.00
115	EUR	29.01.2014	10	4.50%	309,449.90	994.60
116	GBP	06.05.2014	10	5.50%	185,575.00	596.45
120	USD	03.02.2015	10	4.75%	361,020.00	1,160.35
121	EUR	24.02.2020	15	3.88%	311,130.00	1,000.00
122	GBP	09.05.2017	12	5.00%	185,575.00	596.45
124	JPY	12.07.2012	7	0.96%	139,729.50	449.10
125	EUR	02.11.2012	7	3-month EURIBOR+0,05%	310,160.52	996.88
126	EUR	18.07.2016	10.5	3.50%	311,130.00	1,000.00
127	JPY	18.03.2013	7	1.67%	155,255.00	499.00
128	GBP	30.03.2016	10	5.00%	185,575.00	596.45
129	EUR	04.07.2017	10	4.375%	311,130.00	1,000.00
130	JPY	26.10.2017	10	2.11%	77,627.50	249.50
131	CHF	21.05.2013	5	3.50%	38,386.50	123.38
132	CHF	20.05.2016	8	4.00%	51,182.00	164.50
133	EUR	11.06.2018	10	5.75%	466,695.00	1,500.00
134	EUR	28.07.2014	5	6.75%	311,130.00	1,000.00
135	USD	29.01.2020	10	6.25%	481,360.00	1,547.13
136	USD	29.03.2021	10	6.375%	722,040.00	2,320.70
137	USD	29.03.2041	30	7.625%	300,850.00	966.96
138	EUR	11.01.2019	7	6.00%	311,130.00	1,000.00
Total					**5,831,349.45**	**14,454.82**
Out of which: cross-currency swaps					-119,031.49	

Kingdom of Hungary 1924 bond issue	**12.61**
Total foreign currency debt	**10,170,430.53**
Total central government debt	**20,532,623.48**
Other obligations of ÁKK (marked-to-market deposits placed at ÁKK	**422,890.35**
Grand total	**20,955,513.83**

* With swaps.

2. THE CREDIT RATING HISTORY OF THE LONG-TERM DEBT OF THE REPUBLIC 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-

Moody's, Fitch Ratings and Standard and Poor's assigned a 'negative rating outlook to the long-term foreign currency debt of the Republic of Hungary at the end of 2011.

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

Moody's, Fitch Ratings and Standard and Poor's assigned a 'negative rating outlook to the long-term foreign currency debt of the Republic of Hungary at the end of 2011.

3. THE ADDRESSES OF PRIMARY DEALERS

Primary dealer	Address
BNP Paribas SA	Budapest, H-1051 Roosevelt 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.
ING Bank N.V.	Budapest, H-1068 Dózsa György út 84/b
Goldman Sachs International	133 Fleet Street London EC4A 2BB
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.
Nomura International Plc	One Angel Lane, London EC4R 3AB
OTP Bank Nyrt.	Budapest, H-1876 Nádor u. 16.
Raiffeisen Bank Zrt.	Budapest, H-1054 Akadémia u. 6.
The Royal Bank of Scotland Plc	135 Bishopsgate, London EC2M 3UR
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. XXXVIII OF 1992 ON PUBLIC FINANCES

(...)

18/F.§ (1) The Government Debt Management Agency Ltd. (hereinafter: 'ÁKK') is a single shareholder company (limited by shares). The company's shares are registered and non-negotiable securities.

(2) The founder of ÁKK is the minister responsible for public finances.

(3) The establishment and operation of ÁKK – unless otherwise provided by the present Act – are governed by the Act No. CXLIV of 1997 on Business Associations.

(4) The shareholder's rights are exercised by the Minister responsible for public finances, with the difference that the shareholder is not entitled to absorb the rights of the Board of Directors.

(5) State officials as specified in the Act on the Status and Responsibilities of the Members of the Government and State Secretaries may hold positions on the Board of Directors and on the Supervisory Board of ÁKK.

(6) The scope of authority of the Supervisory Board of ÁKK does not include the report on the government debt management strategy, the associated performance indicators and financing plans.

18/G.§ (1) ÁKK manages its assets autonomously within the framework of the applicable laws and regulations, the decisions of the shareholder and the decisions of the Board of Directors.

(2) The revenues of ÁKK are:

a) The appropriation assigned for this purpose in relation to government debt management i n the Annual Budget Act, which is to be placed at the disposal of the company in equal monthly instalments;

b) other revenues.

(3) *[Provision has been repealed]*

(4) The interests, costs, fees and other payments associated with government debt management are booked and paid by ÁKK to the charge of the current government debt chapter of the Annual Budget.

(5) ÁKK is the general legal successor of the Hungarian State Treasury Government Debt Management Agency as regards all rights and liabilities.

(6) ÁKK holds a bank account at the National Bank of Hungary (hereinafter: NBH) for its operations speci fied in paragraphs (1)-(3).

(7) ÁKK holds a securities custody account and a securities account at the Central Clearing House and Depository (Budapest) Ltd. (hereinafter: KELER) for its operations specified in Article 113/A of the Act on Public Finances.

(8) ÁKK may open a foreign currency account at the NBH or at credit institutions for its operations specified in Article 113/A of the Act on Public Finances.

(...)

* This translation of the selected legal provisions serves only information purposes and is not an official translation. Please note that the regulatory environment had been changed significantly from January 2012 and this chapter only wish to provide a general picture of laws valid the time of debt management operations in 2011.

110.§ (1) The general government debt is the sum of the public debt (of central government) and the debt of local authorties, which shall be consolidated so as to net the debts between the central government and local authorities.

(2) The debt of local authorities is the total debt owed by local governments and local minority governments, which shall be consolidated so as to net the debts between various local authorities.

(3) The Maastricht debt indicator is the debt indicator to be reported in accordance with Council Regulation (EC) No 3605/93 of 22 November 1993 on the application of the Protocol on the excessive deficit procedure annexed to the Treaty establishing the European Community.

111.§ (1) The minister responsible for public finances is responsible for managing, executing and recording the liabilities arising from the central government debt.

(2) Local governments are responsible for independently managing, executing and recording the liabilities arising from their debt.

112.§ The minister responsible for public finances shall publish the central government debt and the general government debt, including both individual data of the subsystems and consolidated figures, on a regular basis, but at least quarterly, as stipulated in government decree. Local authorities shall provide data to enable the minister esponsible for public finances to perform this task in the manner, with the frequency and with the content stipu lated in government decree.

113.§

113/A.§ (1) In the sphere of government debt management, the minister responsible for public finances, through ÁKK:

a) ensures the solvency of the central government budget on the basis of the annual Budget Act and by taking into account the forecast rendered in subsection p) of paragraph (1) of Article 18/B;

b) ensures that the central government debt and the temporarily free cash-funds of the state are properly managed;

c) records the central government debt.

(2) In executing the above duties, ÁKK:

a) prepares the annual and middle-term financial plan of the central government budget, works out the strategy of government debt financing;

b) organizes, within the limits of the annual Budget Act, the issuance of government securities, borrowing of loans and debt assumptions which constitute the central government debt;

c) provides for the payment of the liabilities of the central government debt;

d) organizes the secondary market of government securities;

e) executes dealing on own account on the secondary government securities market, concludes securities lending, repo and reverse repo transactions, concludes prompt, forward, hedge- and swap, and derivative transactions, and executes custodial and deposit management tasks;

f) analyses the developments of the debt services borne by the central government and of the government securities market;

g) participates in the calculation of the general government debt, informs about the developments regarding the central government debt and the general government debt and the developments of the government securities market in accordance with the Government Decree referred to in Section 112;

h) opines the terms and conditions of loans and bonds secured by individual government surety ship or guarantee;

i) executes credit and deposit transactions;

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

(3) ÁKK is remunerated by the central government budget for participation specified in subsection j) of paragraph (2). The rate of such remuneration is at most 0.025 per cent of the principal amount of the underlying transaction. The Government shall determine the detailed regulation of such duties and remuneration of ÁKK in a decree;

(4) ÁKK may perform the following functions beyond paragraph (2):

a) upon authorisation by a separate law may organize issuance of debt securities secured by government suretyship or government guar antee, 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 of business organization owned by local authorities or the state or local authorities through majority ownership, and is entitled for a remuneration to such extent as determined in paragraph (3) from such business organization;

c) may participate in the management of the free cash funds of the State Deposit Insurance Fund;

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

(5) ÁKK may create debt securities on the separated sub-accounts of the accounts specified in paragraph (6) ofArticle 18/G without outright issuance and underlying financial claims, which may become objects of transactions specified in subsection e) of paragraph (2).

6) As the subject of government debt management related civil law legal relationships, the Hungarian State shall be represented by the minister responsible for public finances, who may exercise such incumbency right through ÁKK, or may delegate such incumbency right to ÁKK.

(...)

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

I. BALANCE SHEET

data in HUF thousand

	Assets	2010	2011
	A) Fixed assets	**59,017**	**73,623**
I	Intangible assets	18,369	16,822
II	Tangible assets	26,409	39,069
III	Invested financial assets	14,239	17,732
	B) Current assets	**439,426**	**412,429**
I	Inventories	0	0
II	Receivables	3,496	5,571
III	Securities	0	0
IV	Cash and cash equivalents	435,930	406,858
	C) Accrued and deferred assets	**13,344**	**26,614**
Assets in total		**511,787**	**512,666**

data in HUF thousand

	Liabilities	2010	2011
	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	**113,897**	**132,444**
I	Subordinated liabilities	0	0
II	Long-term liabilities	0	0
III	Short-term liabilities	113,897	132,444
	G) Accrued and deferred liabilities	**42,976**	**25,308**
	Liabilities in total	511,787	512,666

Budapest, 17 April 2012

István Töröcskei
CEO

II. PROFIT AND LOSS ACCOUNT

data in HUF thousand

	Liabilities	2010	2011
I	Net sales revenue	927,674	958,209
III	Other revenue	2,150	102,732
IV	Material expenses	221,370	331,106
V	Personnel expenses	645,701	645,701
VI	Depreciation and amortisation	21,806	33,279
VII	Other expenses	5,342	4,053
A	OPERATING PROFIT OR LOSS	35,605	30,880
B	PROFIT OR LOSS FROM FINANCIAL TRANSACTIONS	24,162	28,335
C	PROFIT OR LOSS ON ORDINARY ACTIVITIES	59,767	59,215
D	EXTRAORDINARY PROFIT OR LOSS	-65	0
E	PROFIT OR LOSS BEFORE TAXATION	59,702	59,215
XII	Tax payable	9,116	6,346
F	PROFIT OR LOSS AFTER TAXATION	50,586	52,869
23	Approved dividends	50,586	52,869
G	BALANCE-SHEET PROFIT OR LOSS	0	0

Budapest, 17 April 2012

István Töröcskei
CEO

6. SENIOR OFFICIALS OF ÁKK ON 31 DECEMBER OF 2011

Members of the Board of Directors:

Gyula Pleschinger, chairman
Dr. György Naszvadi, member
Dr. Róza Nagy, member

Members of the Supervisory Board:

Helga Wiedermann, chairman
Norbert Csizmadia, member
Péter Benő Banai, member

The Company's auditor:

KPMG Hungária Kft.
Budapest, 1139. Váci út. 99.

Responsible auditor:

Gábor Agócs Audit Director

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