GOVERNMENT DEBT MANAGEMENT AGENCY PTE LTD.

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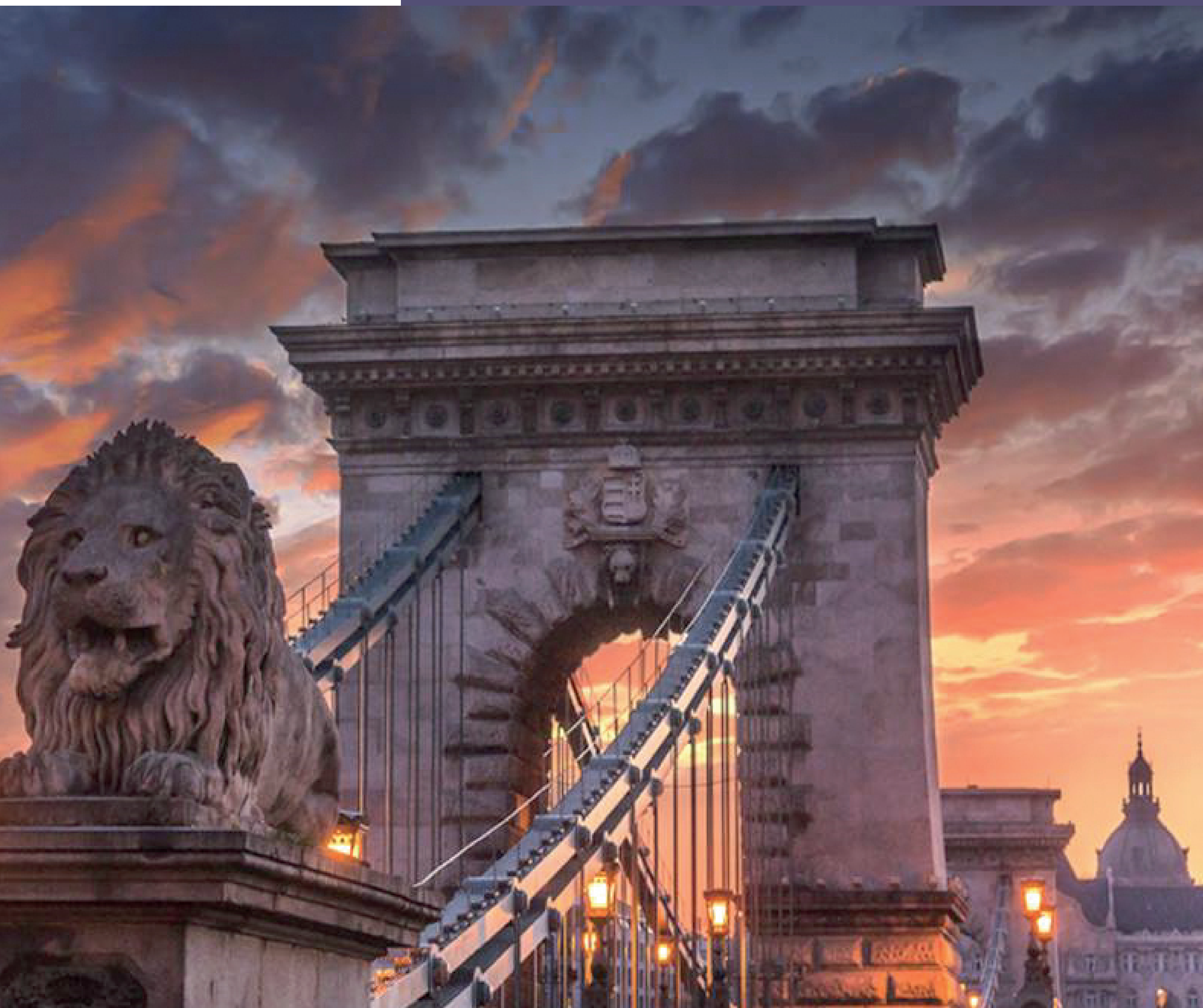
GOVERNMENT DEBT MANAGEMENT REPORT **2017**



Foreword

The objective of this Government Debt Management Report 2017 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 public debt and to describe the developments in the Hungarian government securities market in 2017.

One of the most important objectives of the Hungarian government is to reduce the public debt, increase domestic financing and improve debt metrics. 2017 was a very successful year in these respects: according to EUROSTAT the public debt ratio continued to decrease from 76.0 per cent to 73.6 per cent. Not only did indebtedness decline, but the share of foreign currency debt also declined from 24.6 per cent to 21.6 per cent. At the same time Hungary issued its first sovereign panda bond in the Chinese interbank bond market with the issuance of a CNY 1 billion panda bond in July 2017.

Hungary's first ever International Bond Exchange transaction was executed in October, where USD 1.16 billion USD bonds were bought back and issued an EUR 1 billion 10 year euro bond. The domestic ownership of public debt increased further due to the successful retail debt program – now more than 60 per cent of the public debt is in the hand of domestic investors. All of these results were achieved with even lower funding costs, as the yields decreased to historical low levels.

All in all, it is clear that the most important objectives for the last year were achieved, which provides a solid grounding for the coming years of public debt management. These achievements were also acknowledged by credit rating agencies, since two CRAs changed Hungary's outlook from stable to positive of the sovereign credit ratings.

György Barcza
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. Therefore fiscal data used in this report were still preliminary when this report was compiled.

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

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

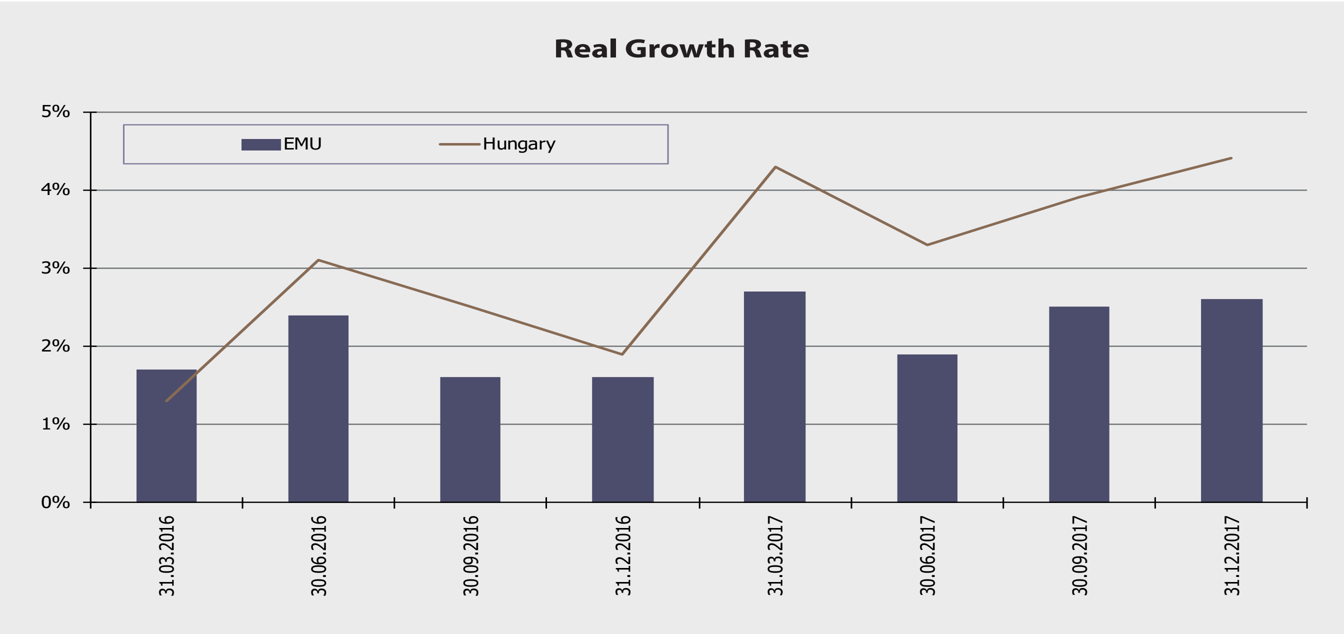
- Government bonds and retail government securities are recorded at nominal value.
- Discount treasury bills are recorded at the average sale price (at discount value), which is recalculated after every transaction involving the security concerned.
- Repo and reverse repo transactions actually increase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

The debt data published by ÁKK in accordance with Hungarian and international accounting standards differs from the debt data used by EUROSTAT (the European Union's institute of statistics), which is calculated according to different principles and is essentially the result of statistical calculations. Public debt data is calculated and published in accordance with ESA '2010 principles by the National Bank of Hungary.

I. Macroeconomic developments in 2017

During 2017, global monetary policy conditions continued to be tighter: In the US the rate hike cycle that started in 2015 continued. At the same time, the ECB announced the gradual termination of the quantitative easing (by the end of 2018). The first rate hike took place in the UK. Besides softening deflationary pressure and strong growth outlooks time lags of monetary policy phases were mainly driving the evolution of foreign exchange rates, interest rates and the stock markets.

Economic Growth

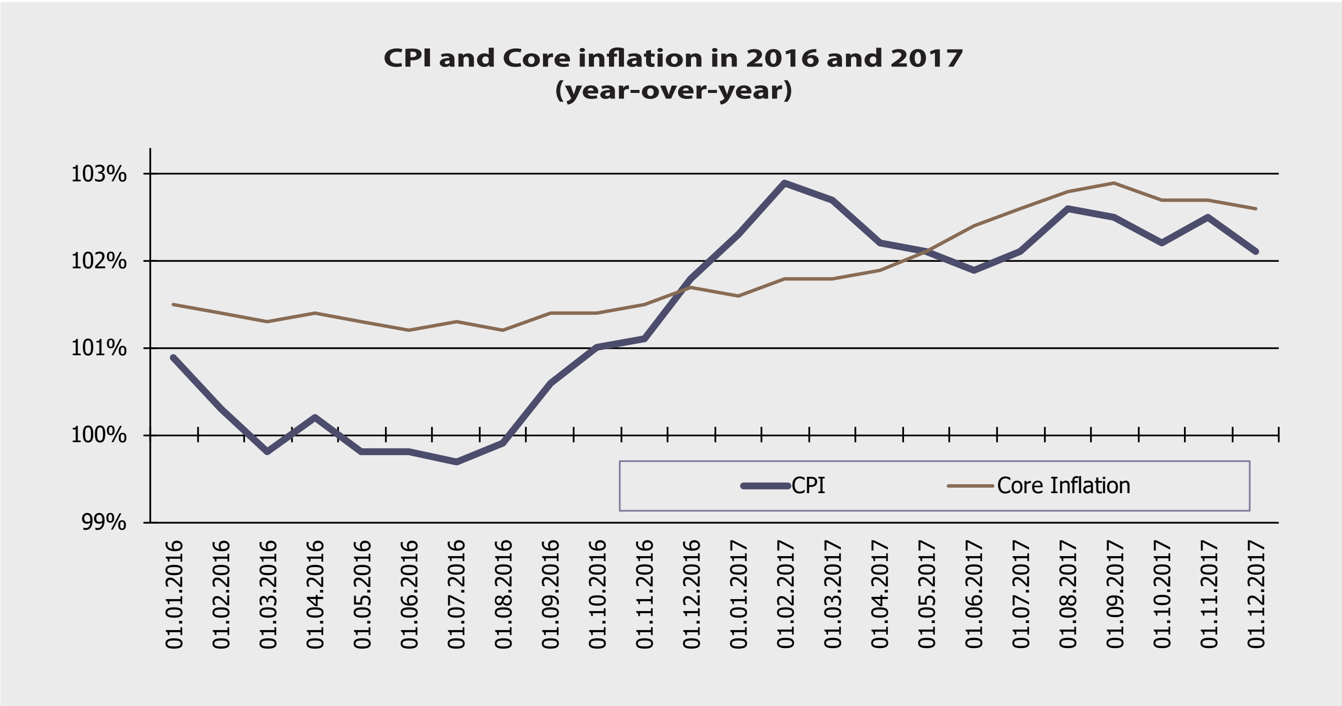


Source: CSO, Eurostat

Growth rate amounted to 2.2% in 2016 and accelerated to 4.0% in 2017 that exceeded significantly the average growth rate of the EU (and the Eurozone). In 2017, all sectors except for agriculture contributed significantly to economic growth. Industry and services sector both increased significantly (by 3.9% and 3.3%). Dynamics in construction was high (31.6%) caused by relatively low base of the previous year and government spending and EU disbursements. The favourable weather conditions (and consequently high basis) in 2016 led to a decrease (of 9.0%) in the agriculture sector. Regarding expenditures consumption and investments contributed to economic growth. Dynamics of consumption (3.4%) exceeds slightly that of the previous year (3.3%). In case of investments, a 14.9% increase took place in 2017 partly caused by the low base (in 2016 investments dropped by 3.7%). The dynamics of export and import both increased (from 3.4% to 7.1% and from 2.9% to 9.7%) but net exports decreased GDP growth rate by 2.0 percentage points in 2017 because the growth rate of imports exceeded significantly that of exports.

I. Macroeconomic developments in 2017

Inflation



Source: CSO

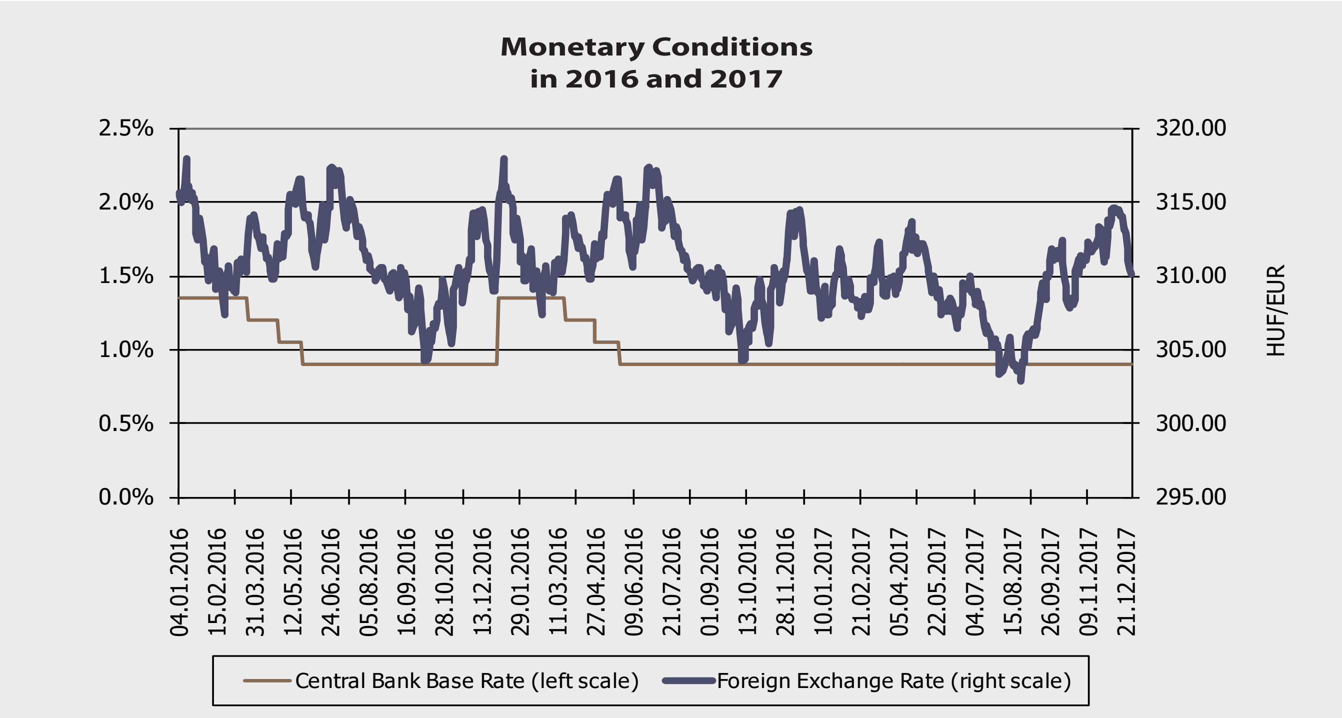
Inflation accelerated from 1.8% in December 2016 to 2.1% in 2017; the inflation still below the 3% inflation target of the central bank. Durable goods was the only group with decreasing price level (by 0.4%). The inflation rate amounted to 0.5% in case of clothing, 0.8% in case of other goods including motor fuel, 1.1% in case of services and 1.6% in case of fuel and power. Food prices increased by 3.5%, the price level of alcoholic beverages and tobacco grew by 6.8% partly as a result of indirect tax increases. For most groups inflationary pressure was moderate, yearly average inflation amounted to 2.4% in 2017. Yearly average core inflation in 2017 reached 2.3%; it was close to CPI inflation.

Monetary Conditions

During 2017, monetary policy in Hungary relied on non-conventional measures. The central bank held forint liquidity providing FX swap tenders regularly during the course of the year, and capped the availability of the three-month sterilisation instrument to a minimal level (of HUF 75 billion) by the end of 2017. Due to excess liquidity the overnight deposit rate representing the lower bound of the interest rate corridor became the key interest rate; the Monetary Council decreased this rate from -0.05% at the beginning of the year to -0.15% in September. This pushed short-term government bond rates into negative territory supported by low issuance. The Monetary Council introduced several measures to decrease long-term interest rates during 2017. In May the NBH launched the second phase of Market-based Lending Scheme including an interest rate swap instrument in addition to preferred loans. In November the central bank announced a program consisting of an unconditional interest rate swap instrument and mortgage bond purchasing; the program aimed among others to decrease the steepness of the government yield curve.

I. Macroeconomic developments in 2017

The exchange rate of the forint strengthened during 2017 (by 0.3%) from EUR/HUF 311.02 to EUR/HUF 310.14.



Source: NBH

During the first half of the year, the foreign exchange rate of the forint fluctuated between EUR/HUF 308 and 312 without a prominent trend. During this period of time favourable macroeconomic data on Hungary were published: GDP and industrial output increased at a high pace, unemployment rate kept on declining. Besides favourable growth data, inflation was under the target enabling the commitment of the central bank to persistently lax monetary conditions. Government deficit was low, external trade posted a significant surplus month by month. In addition to Hungarian fundamentals, favourable external environment contributed to the strengthening of the forint. The Eurozone and the US were both posting strong growth data. The high growth was accompanied by moderate inflation pressure, as a result the monetary policy of the Fed and the ECB was both considered lax. The Fed tightened the monetary conditions cautiously in small steps and the ECB still had not started the tapering of the quantitative easing programme. Loose monetary policy on the developed markets accompanied by favourable global growth prospects strengthened the investor appetite towards risky assets and strengthened emerging market currencies including the Hungarian forint.

During the summer, the forint strengthened significantly. Growth indicators in Hungary as well as in Western Europe were favourable. The ECB and the NBH both used verbal intervention to dampen the strengthening of the euro and the forint.

From September to mid-December, a weakening trend manifested in the foreign exchange rate of the forint versus the euro dotted with temporary corrections. The intense verbal intervention of the Monetary Council of the NBH and their repeated commitment to lax monetary conditions was the main reason for the weakening of the forint.

During September Polish zloty weakened, similar to the Hungarian forint although the extent was lower (1.7% compared to the 2.2% weakening of the forint). In addition to geopolitical tensions (mainly between North Korea and the USA), developments in the internal policy of France and Germany and the uncertainties regarding the BREXIT, the impending monetary policy tightening in the Eurozone was also weakening the forint. During the last days of the year, a partial correction took place.

Fiscal Policy

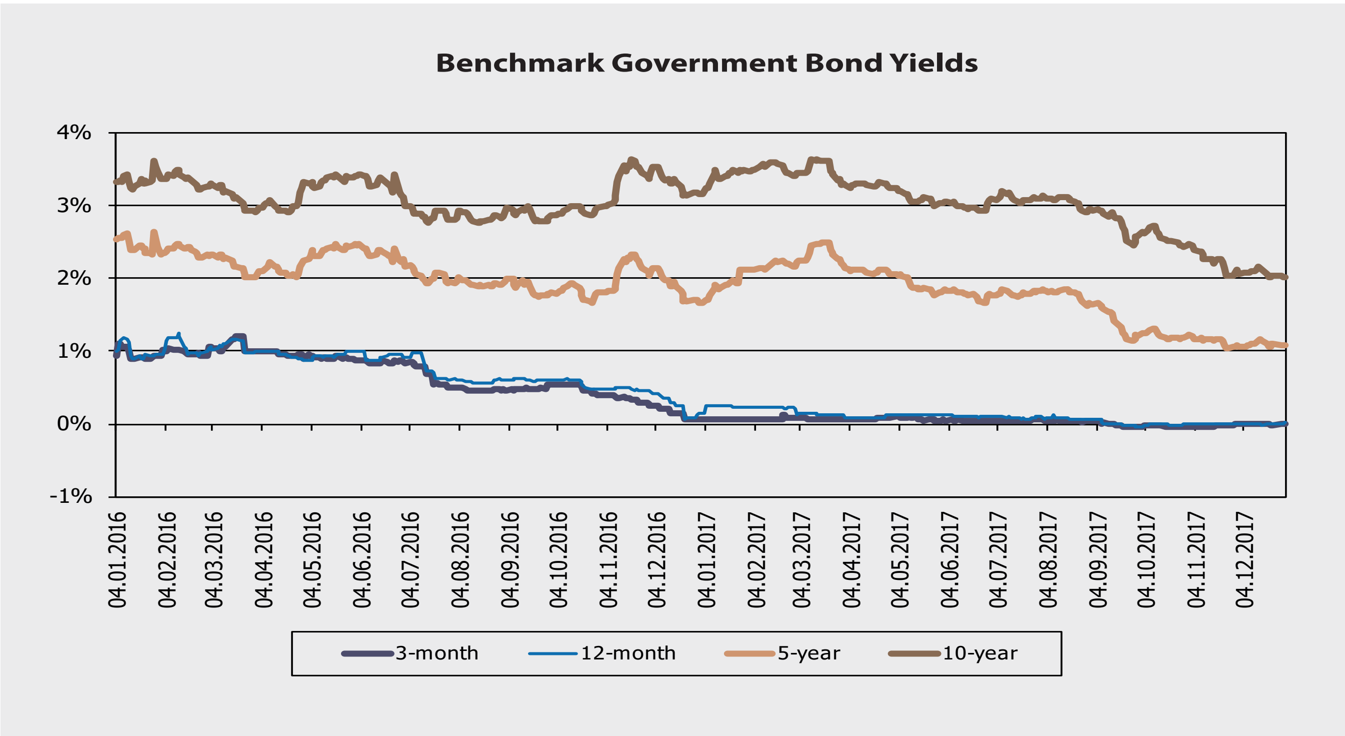
The deficit of the public sector was 1.8% of GDP based on the financial accounts methodology. The cash-flow based (GFS) general government deficit amounted to HUF 1,973.9 billion (equalling 5.2% of GDP for the year 2017) mostly because pre-funding of EU related payments. In 2017, the accrual based (ESA) general government deficit (including local governments) amounted to HUF 746.3 billion (equalling 2.0% of GDP for the year 2017) according to preliminary data. The financing need of the state for the year 2017 increased compared to the previous year.[1]

Financing Position of the Economy

The households' savings to GDP ratio amounted to 5.1%. The net financing need of the corporate sector reached 1.1%. The economy of Hungary as a whole was a net lender towards the rest of the world in the amount of 2.1% of GDP resulting in a declining external indebtedness of Hungary. The current account posted a surplus of EUR 3.6 billion or 2.9% of GDP.

Developments of Government Securities Markets and Yields

During the course of the year, short-term forint rates declined slightly to a level close to zero, long-term forint rates decreased significantly driven by external and local factors.



Source: ÁKK

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

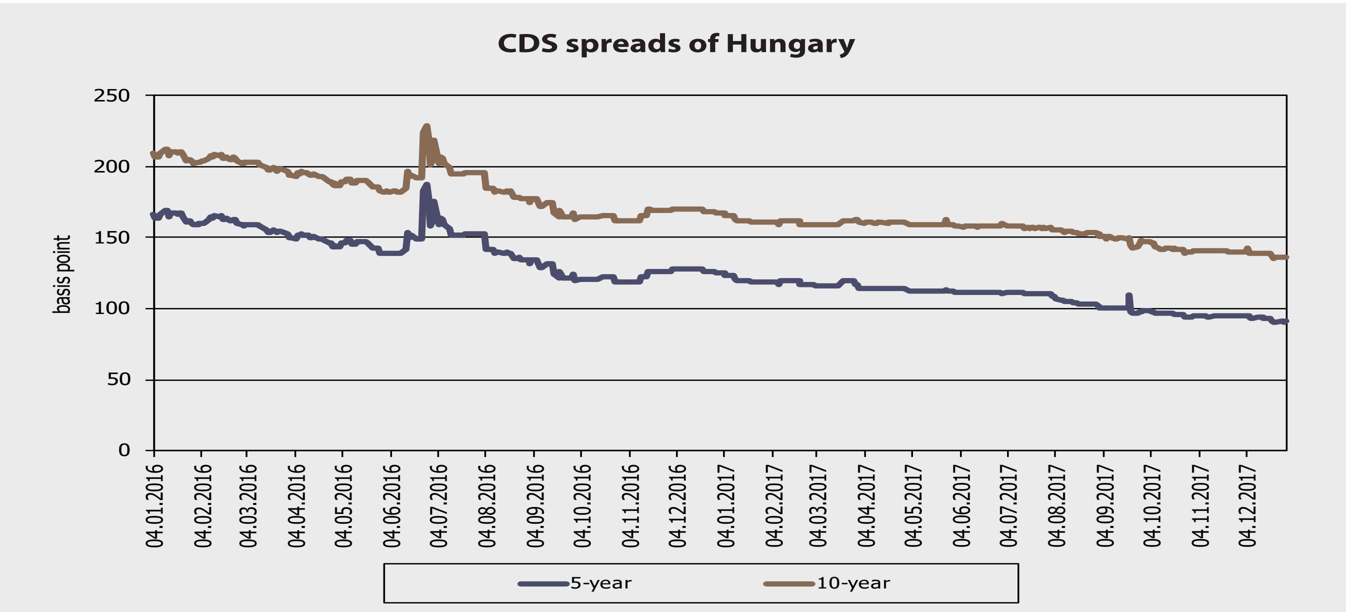
I. Macroeconomic developments in 2017

During the first three quarters of 2017, short-term government bond yields fluctuated at a low level, mainly between 0.05% and 0.15%. The central bank continuously increased forint liquidity with forint liquidity providing FX swap tenders and a cap on the three-month sterilisation instrument. Due to excess liquidity the overnight deposit rate representing the lower bound of the interest rate corridor became the key interest rate; the Monetary Council decreased this rate from -0.05% at the beginning of the year to -0.15% in September. As a result, short-term government bond yields dipped into negative territory in September.

Long-term government bond yields increased in Q1 2017. During this period, risks regarding the growth prospects in 2017 were elevated in light of weak growth data related to the end of 2016, although global environment was supportive. Beginning the spring of 2017 however, incoming local growth data were favourable – apart from a temporary slowdown by the end of summer – improving the investor sentiment towards Hungary and decreasing long-term government bond yields. Favourable macro stability indicators – especially the massive surplus in the current account – increased the demand for local government bonds. The demand for local bonds was strengthened by the favourable global (and local) business sentiment indices and stock exchanges reaching new historic highs. The NBH also used several measures to decrease long-term yields. The expectations for a prolonged loose monetary policy in America and Europe also pushed local government bond yields downwards.

By the end of 2017, 3-months and 12-months reference yields dropped to -0.01% and 0.02%, respectively; 5-year and 10-year reference yields were 1.09% and 2.02%, respectively a historically low level.

CDS Spreads

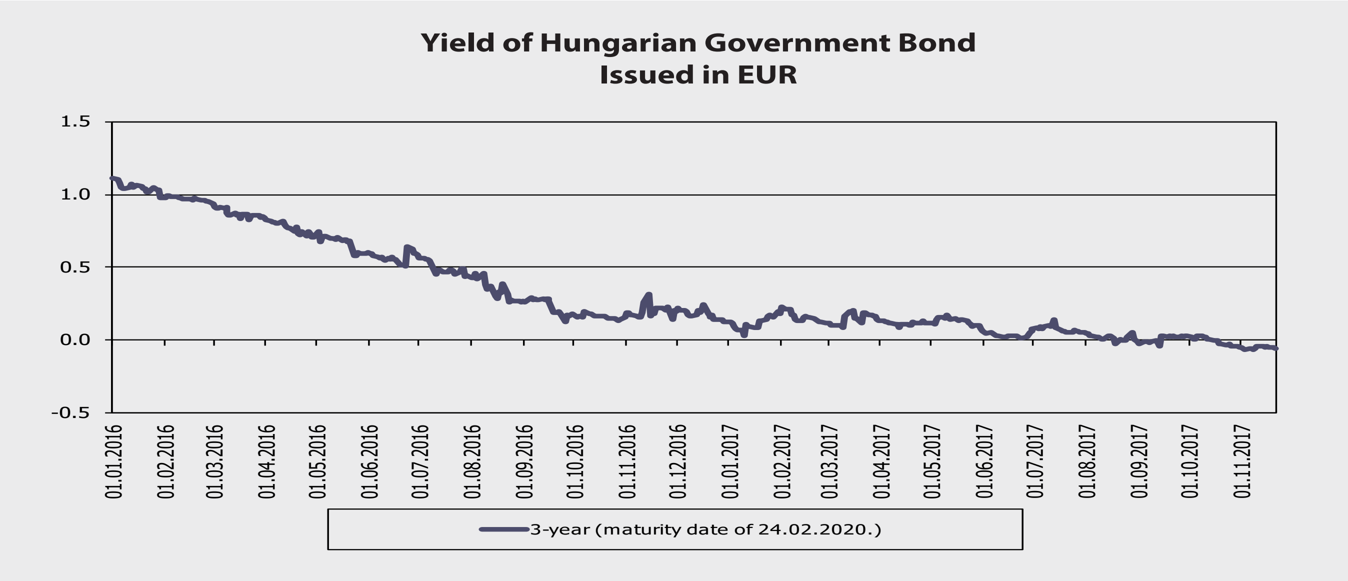


Source: Reuters

During the course of the year, 5-year CDS spread dropped from 125 basis points to 91 basis points. International investor sentiment and the macroeconomic indicators of the country (strong growth accompanied by favourable macro balance indicators) were all essentially favourable. During the course of the year CDS spreads were declining gradually driven by a steady flow of favourable macroeconomic news.

Yields of Foreign Currency Denominated Bonds

In 2017, the yields of government bonds denominated in euro issued by Hungary declined gradually.



Source: Bloomberg

The yield of the Hungarian euro-denominated government bond maturing in February 2020 declined from 0.13% into negative territory reaching -0.17% during 2017. The significant reduction of yields was driven by the declining spreads and also by the negative yields of risk-free mid-term securities in the Eurozone as a result of the monetary policy of the European Central Bank. The yield of the euro-denominated government bond was pushed downwards by the decision of two credit rating agencies (Standard&Poor's in August and Fitch in November) to revise the outlook of Hungary from stable to positive.

Government Securities Holdings of Foreign Investors

The The value of forint-denominated government securities held by non-residents declined during 2017. Non-resident holdings reached their historical high of HUF 5,202 billion on July 8, 2013. During 2017, non-resident holdings declined by HUF 57 billion reaching HUF 3,385 billion. At the same time average term to maturity of foreign investors' portfolio decreased from 5.51 to 5.38.

The share of foreign holdings in forint denominated debt declined from 23% to 21%. Including foreign holdings in foreign exchange denominated debt, the share of foreign holdings in total debt amounts to 37%.

II. DEBT MANAGEMENT STRATEGY IN 2017

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 accordance with the economic policy of the government ÁKK set three secondary objectives:

1. According to the fundamental law of Hungary if the debt to GDP ratio is higher than 50 percent, only such budget can be approved, which leads to the reduction of the debt ratio year by year. The primary objective of debt management is to support the debt reduction accordingly.
2. One of the main factors that led to the vulnerability of Hungary in recent years was that the higher part of the government debt had been financed by non-resident investors. Increasing domestic savings and the domestic financing of the debt reduce the risks of public debt and support macroeconomic stability in the long term. Thus the second objective of ÁKK is to develop further the domestic investor base, and especially to increase the retail debt program.
3. Decreasing debt ratio and increasing domestic financing enable to further reduce the share of foreign currency debt within the total debt, which is the third objective of ÁKK.

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

The most important risk factors are as follows:

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

ÁKK has developed various benchmarks reflecting its strategic objectives 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 2017 the composition of the central government debt was in line with the benchmarks.

Public debt management benchmarks in 2017

Benchmarks	Tolerance band	End 2016	End 2017
1. Foreign currency debt ratio	15-25%	25.3%	22.3%
2. Foreign currency debt composition	95-105% EUR	99.9%	99.7%
3. Fixed coupon part of foreign currency debt	61.0-71.0%	66.1%	67.6%
4. Fixed coupon part of domestic debt	56-66%	61.8%	58.9%
5. Duration of domestic debt	2.5-3.5 years	3.0	2.9

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

Strategic Principles

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

As regards liquidity, ÁKK aims to ensure that wholesale 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 to consolidate domestic bonds into sufficiently large 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 650-1000 billion (approximately EUR 2-3 billion) in 2017. Smaller size of HUF 2-300 billion is targeted in the 15-year tenor reflecting lower investors' demand. Secondary market operations were also enhanced by regular bond buy-back and bond exchange programs.

After the international financial crisis, based on the experiences, ÁKK raised the flexibility of its operations. This way it can react to changes in market demand to a greater extent as regards the announcement of auctions, and the accepted amounts at auctions. The purpose of the non-competitive top-up phase of bond auctions is similar, to be able to react to a stronger than expected demand.

DEVELOPMENT OF NEW OPTIMAL DEBT PORTFOLIO MODEL

The Hungarian Government Debt Management Agency (ÁKK) developed a mathematical-economic model between 2001-2003 to set optimal values for debt portfolio benchmarks based on modern risk management methods. This model was then used from end-2004 to set government debt benchmarks. Following the Global Financial Crisis of 2008, market conditions changed rapidly and permanently, the volatility of interest rates and foreign currency exchange rates grew, the spread between HUF and foreign currency fund raising narrowed and also the goal to join the EMU has been dropped from the planning horizon. Meanwhile, the high share of non-resident holdings presented a new type of risk, and - as part of the IMF-EU loan - a high volume of short-term foreign currency debt got included in the overall debt. These changes made the old model obsolete in 2009.

ÁKK decided that the development for a new optimal debt portfolio model is required due to the changes in goals and market conditions. The development began after the stabilization of the market in 2013. The first version was ready by the end of 2015. In September 2016 the first analysis for the share of foreign currency debt was prepared based on the results of the model, while an analysis was presented at the end of 2016 regarding the fix-floating share of domestic debt. In September 2017 the results of the model covered the whole range of benchmarks used by ÁKK, while at the end of 2017 an analysis was presented with the results of the final version of the model. As of 2017 the setting of benchmarks is based on the new optimal portfolio model.

A basic requirement regarding the new model is that the results are to be used in practice, while being scientifically sound. The time horizon of the new model aligns with goals of the 5-year medium-term framework set by ÁKK. All this reflects the debt management's basic goal of mid-term approach which includes avoiding low cost but high risk strategies for short-term benefits.

Considering the structure of debt, the share of FX or the share of different interest rate types or maturities can be used to distinguish strategies. Thus, it is straightforward for the model to specify (1) the optimal share of FX debt, (2) the optimal share of fixed-floating interest rate domestic debt and (3) the optimal share of fixed-floating interest rate FX debt. An important strategic goal is the boosting of retail debt, because though financing through the retail segment is more expensive, the interest rate risk and refinancing risk of retail debt is lower. Another important goal is to increase the maturity of the debt, because a more balanced maturity profile makes the debt portfolio less vulnerable to the short-term effects of economic shocks in periods of higher volatility. The calculation of the aforementioned benchmarks is required for the proper measurement of costs and risks arising through different compositions of financing. The minimization of costs and risks is contradictory by nature as lower costs can usually be achieved by taking on higher risks. Therefore a single optimal composition of financing does not exist. Thus, the goal of the new optimal portfolio model is to find possible financing compositions which carry the lowest risk given the cost in-between the framework of the simulation. The set of optimal cost and risk compositions make for an excellent ground to choose from in alignment with the preferences of the decision maker.

The model operates in three phases.

The first phase is the model fitting, where we define the parameters used for forecasting. The goal is to be able to forecast cash flows and all pricing features of future instruments. For that we need HUF and EUR yield curves, HUF and Eurozone CPI, Hungarian CDS as well as EUR/HUF exchange rates. The forecast of the EUR/HUF exchange rate is required for the calculation of costs and risks of FX debt. We use a rotated 3-factor Nelson-Siegel model for the HUF and EUR yield curves and a 2-factor Nelson-Siegel for the Hungarian CDS curve. The basic assumption of the model is the existence of economic cycles. We distinguish between two different economic states, one for longer periods of growth (expansion) and another for shorter crisis periods of contraction (recession).

In the second phase we generate scenarios. Realizations of economic and market parameters are generated based on the results of the first phase. The set of initial financing compositions are also generated in this phase, defining the initial set for the optimization phase. The financial need for the simulation of issuances in a given year is equal with the sum of maturing debt and the yearly net financing need defined in the financing plans of ÁKK. The cost and risk indicators are calculated based on the initial portfolio handled by ÁKK, as well as the financing compositions and economic realizations.

During the last phase a set of optimal financing compositions are defined based on the initially set optimization goals. The model takes into account that excess issuance comes with a premium, and that demand specifies thresholds and constraints on issuances. The optimization goals are minimizing the expected cost, the volatility of costs and the refinancing risk, while maximizing the average time to re-fixing of the portfolio at the end of the time horizon. The resulting optimal financing compositions outline the attainable debt portfolio structures on the chosen time horizon, which serves as a basis for the setting of benchmarks.

III. The financing requirements in 2017

The components of the financing requirements

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

The total annual net financing requirement financed by ÁKK is the sum of the central government deficit and other, extra-budgetary transfers (net transfers from the EU, special transfers to the NBH etc.). The gross financing requirement, in addition, also includes debt redemptions, the majority of which is contributed by short-term debt, which may be renewed several times a year.

The net financing requirement

In 2017 the total cash-flow based deficit of the central government was HUF 1,973.5 billion (or 5.6 per cent of GDP according to preliminary data), while the total net financing requirement amounted to HUF 1,906.7 billion (or 5.4 per cent of GDP) including net EU transfers and other funding sources.

Borrowing requirements in 2017:

	Outturn 2016 (HUF billion)	Plan December 2016 (HUF billion)	Outturn 2017 (HUF billion)	Outturn/Plan (per cent)
Central government balance	-771.60	-1,310.00	-1,906.03	1.45
Balance of the Social Security funds	-75.20	150.00	-139.94	-0.93
Balance of the extra-budgetary funds	-1.50	-6.00	72.48	-12.08
Net financing need of the central government	-848.30	-1,166.00	-1,973.49	1.69
Capital transfers to NBH / divident of NBH	50.00	-	-	-
Net EU transfers	272.10	-	66.80	-
Total net financing requirements	-526.20	-1,166.00	-1,906.69	1.64
Short term debt redemptions	-3,114.30	-4,302.00	-4,312.56	1.00
Long term debt redemptions	-3,817.80	-2,375.99	-3,563.78	1.50
Gross financing requirements	-7,458.30	-7,843.99	-9,783.03	1.25

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 of loans, buy-backs of bonds and the early repurchasing/ redemption of retail securities and other securities in the Treasury network may also influence the final sum.

The total debt redemption was HUF 7,877 billion, 18 per cent higher than planned in 2016. In the case of domestic debt redemptions the excess was the result of bond buy-backs and switch auctions, which significantly reduce the refinancing risk. In the case of foreign currency denominated debt the redemption was also higher than planned due to foreign currency bond buybacks and due to the international bond exchange program.

Government debt redemptions: [2]

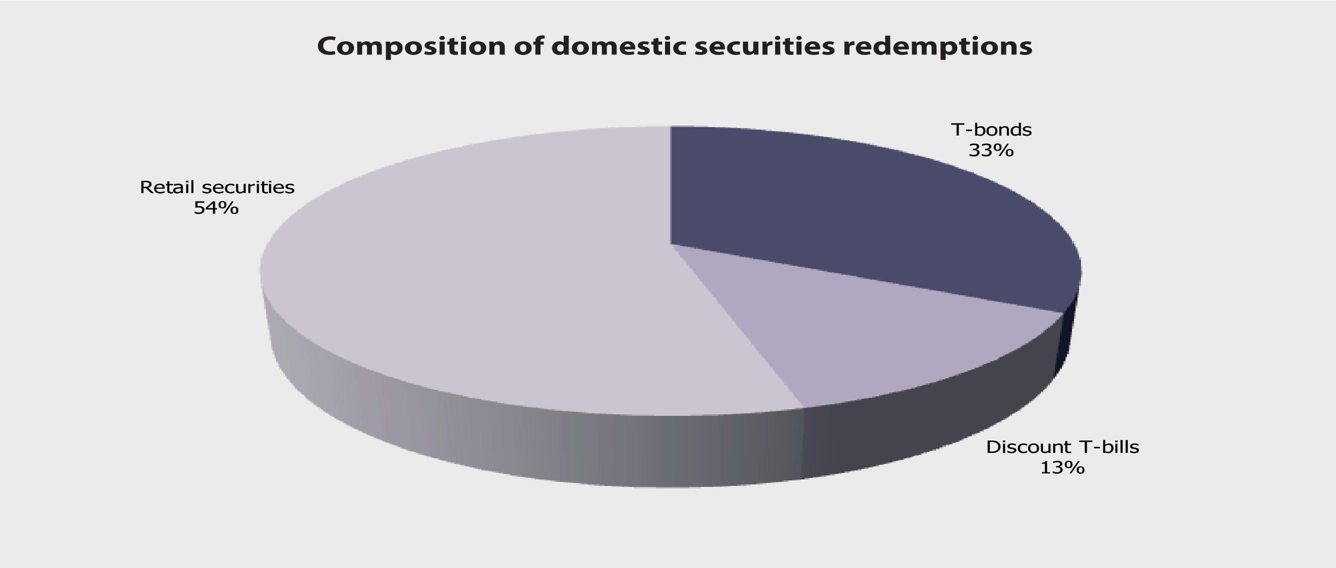
HUF billion

	2016	2017 plan	2017 outcome
Domestic debt	**5,268.3**	**5,942.7**	**6,828.8**
T-bonds	2,042.0	1,364.2	2,219.2
Discount T-bills	901.6	883.4	896.4
Retail securities	2,324.7	3,695.1	3,713.2
Loans	0.0	0.0	0.0
Foreign currency debt	**1,663.8**	**735.3**	**1,047.6**
Bonds	1,076.9	547.0	853.4
Loans	586.9	188.3	194.1
Total	**6,932.1**	**6,678.0**	**7,876.3**

Source: ÁKK

Total domestic debt redemptions exceeded the plan by HUF 886 billion due to higher bond redemptions as a result of the bond buy back and exchange auctions. Within the HUF debt portfolio discount treasury bills contributed to 13 per cent of the total forint redemptions of HUF 6.829 billion, while redemption of domestic retail debt was 54 per cent.

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



Source: ÁKK

Bond buy-backs and exchanges

A large bond series maturing at a given time creates refinancing risk. This risk can be reduced by repurchasing a proportion of the bonds before maturity. ÁKK's normal financing plan includes a regular bi-weekly bond buy-back program, and the actual repurchase amount depends on the quantity and quality of bids. In 2017 ÁKK bought back a total of HUF 733 billion (by HUF 633 billion more than planned) bonds before their maturity on 17 occasions. 100 per cent of the repurchased bonds had a maturity after 2017, i.e. these buy-backs also helped to smooth maturities from one year to another.

In order to decrease refinancing risk ÁKK has been holding bond exchange (or switch) auctions on a regular basis. In these switch auctions the investors can exchange their bonds with short remaining term-to-maturity for longer term bonds. This improves the investment possibilities of investors and at the same time lengthens the average term-to-maturity (ATM) of the government debt. In 2017 19 exchange auctions were held at which ÁKK exchanged a total of HUF 597 billion short-term bonds for long-term ones.

Foreign currency debt redemptions

In 2017 one Eurobond (originally EUR 1 billion), one GBP bond (GBP 500 million) and one JPY bond (JPY 25 billion) matured. Due to FX bond buy-backs in previous years the actually matured amount of the Eurobond was smaller than the originally issued, and amounted to EUR 760 million. The fourth series of Premium Euro Hungarian Government Bond matured in 2017 in a total amount of EUR 126 million. Moreover, in order to reduce the share of foreign currency debt within the total debt ÁKK bought back a total of EUR 120 million FX bonds (EUR and USD) from the market. In order to reduce the refinancing risk and the average cost of the FX debt ÁKK executed an international liability management transaction, where USD 1.16 billion USD bonds were bought back and an EUR 1 billion 10 year euro bond was issued. Larger repayments totalling EUR 620 million took place in the case of IFI project financing and other loans in 2017.

IV. Financing

In 2017 the HUF denominated issuance amounted to HUF 9,141 billion (94%), while foreign currency issuance was HUF 589 billion (6%) (including switch auctions and International Bond Exchange).

Gross debt issuance:

HUF Billion

	2016	2017 plan	2017 outcome
Domestic debt	**7,517.0**	**7,713.2**	**9,141.4**
T-bonds	2,574.5	2,118.0	2,478.0
Discount T-bills	896.4	1,045.9	1,039.2
Retail securities	3,875.2	4,395.3	5,448.2
Loans	170.9	154.1	176.1
Foreign currency debt	**222.9**	**369.8**	**588.6**
Bonds	222.9	369.8	564.2
Loans	0.0	0.0	24.4
Total	**7,739.9**	**8,083.1**	**9,730.0**

Source: ÁKK

Net HUF denominated financing totalled HUF 2,313 billion, while net foreign currency financing amounted to HUF -459 billion, so the total net issuance was HUF 1,854 billion in 2017.

Net issuance:

HUF Billion

	2016	2017 plan	2017 outcome
Domestic debt	**2,248.7**	**1,770.6**	**2,312.7**
T-bonds	532.4	753.8	258.9
Discount T-bills	-5.2	162.5	142.8
Retail securities	1,550.5	700.2	1,734.9
Loans	170.9	154.1	176.1
Foreign currency debt	**-1,440.9**	**-365.5**	**-459.0**
Bonds	-854.0	-177.1	-289.2
Loans	-586.9	-188.3	-169.7
Total	**807.8**	**1,405.1**	**1,853.7**

Source: ÁKK

Within the net HUF issuance, the role of retail securities increased in line with the higher than forecast investor demand. Total net T-bond issuance was HUF 259 billion (by HUF almost 500 billion lower than planned due to the buy-backs), while the net sales of retail securities set a new historical record of HUF 1,735 billion. Due to the ample demand for retail securities ÁKK was able to cover the higher than planned net financing need, to repay a large amount of marked-to-market deposits, to reduce the outstanding stock of FX bonds and to reduce the planned increase of discount Treasury bills. HUF loan drawdown exceeded the plan to a small extent.

In 2017 the net foreign currency redemption was higher than planned. Due to the favourable domestic financing ÁKK was able to issue less international FX bond than planned (excluding International Bond Exchange) and buy-back some FX bonds.

Domestic financing

Gross domestic issuance was eventually 20% higher than planned originally. The issuance of all kinds of instruments increased except that of discount T-bills; bond issuance was higher than planned by 17% and that of retail instruments by 24%. Project financing loans of HUF 176 billion were drawn in HUF, exceeding the plan by 14 per cent.

Following the decreasing trend of previous years the average cost of financing (the weighted average yield to maturity – including sales commissions – of debt instruments issued in 2017) decreased from 2.3 per cent to 2.2 per cent.

Government bonds

Treasury bond auctions were held every two weeks. Three bond series were sold at each bond auction. Usually the 3, 5 and 10-year tenors were offered, but on 6 occasions the 10-year bond was replaced by the 15-year fixed rate bond. The floating rate bonds were offered 24 times during the year. ÁKK actively used its right to modify the accepted amount as a reaction to bids (¬+/- 34 per cent or +/- 50 per cent if the announced amount was not more than HUF 20 billion). Another way to react to changes in market demand was the use of the non-competitive top-up phase in the afternoon of the auctions when successful bidders at the auction could buy additionally up to 40 per cent of their winning bids at the average price of the auction.

The bid-to-cover ratio at the bond auctions on average was more than 3. ÁKK sold a total of HUF 1,800 billion of bonds via auctions (including HUF 318 billion in the additional non-competitive phase). Total bond issuance – together with bond exchange auctions, the retail sales of the Hungarian State Treasury and secondary market operations – was HUF 2,478 billion, versus total bond maturities of HUF 2,219 billion, which resulted in a net issuance of HUF 259 billion, which is significantly less than the planned HUF 754 billion (due to bond buybacks).

On-the-run bond series in 2017:

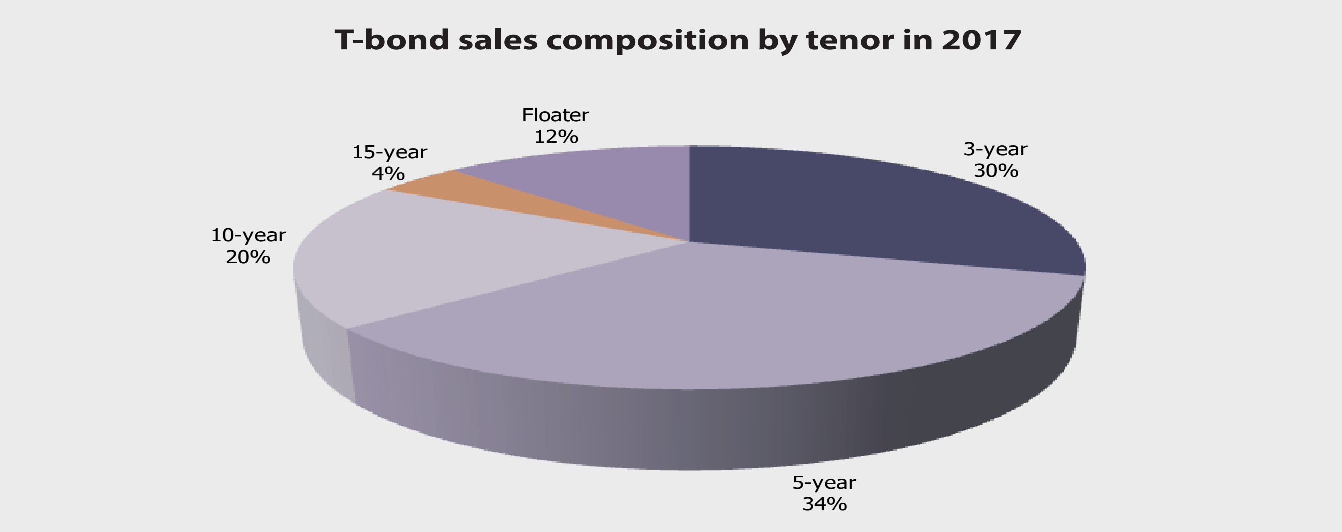
HUF Billion

	Tenor	Number of auctions	Competitive sales in 2017	Non-competitive sales in 2017	Outstanding (end of 2017)
2020/C	3-years	25	441	90	533
2019/D*	3-years	4	32	9	148
2021/A*	5-years	20	141	40	394
2022/B	5-years	25	511	107	622
2027/A	10-years	19	292	58	648
2031/A	15-years	6	64	13	201

Source: ÁKK

*Floating rate bonds

ÁKK adjusted the accepted amounts at the auctions according to demand, and the results show that investors' demand decreased for the 3-year fixed bonds, while in the case of floating rate bonds the demand increased significantly:



Source: ÁKK

Discount treasury bills

The 3 and 12-month discount treasury bills are short-term instruments mainly used for liquidity management, i.e. for smoothening the fluctuations in liquidity caused by the varying financing requirements over the year. For this purpose ÁKK may also use the so-called liquidity discount treasury bills of even shorter tenor (usually 6 weeks) in an ad hoc manner, this was used on 6 occasions in 2017.

In 2017 ÁKK sold discount treasury bills in a total of HUF 1,039 billion, by HUF 143 billion more than in 2016. The outstanding T-bill stock actually increased by HUF 143 billion over the year as due to the increased net bond and retail issuance ÁKK did not have to increase T-bill stock to such an extent as planned as a reaction to excess liquidity.

Retail securities

One of the strategic objectives of ÁKK is to develop further its retail debt programme, which constitutes an important source of domestic financing. With growing domestic savings it is natural for the Government to tap this secure source of funds directly.

The issuance of retail government securities showed a steep increase in 2017. ÁKK contributed to this success by using a broad selling network and competitive pricing for these instruments and also the supportive role of retail banks. The stock of the 1-year Hungarian Government Security grew by HUF 473 billion, the outstanding amount of Treasury Savings Bills (securities available in the post office network) grew by HUF 15 billion, while the stock of the half-year Hungarian Government Security decreased by HUF 77 billion.

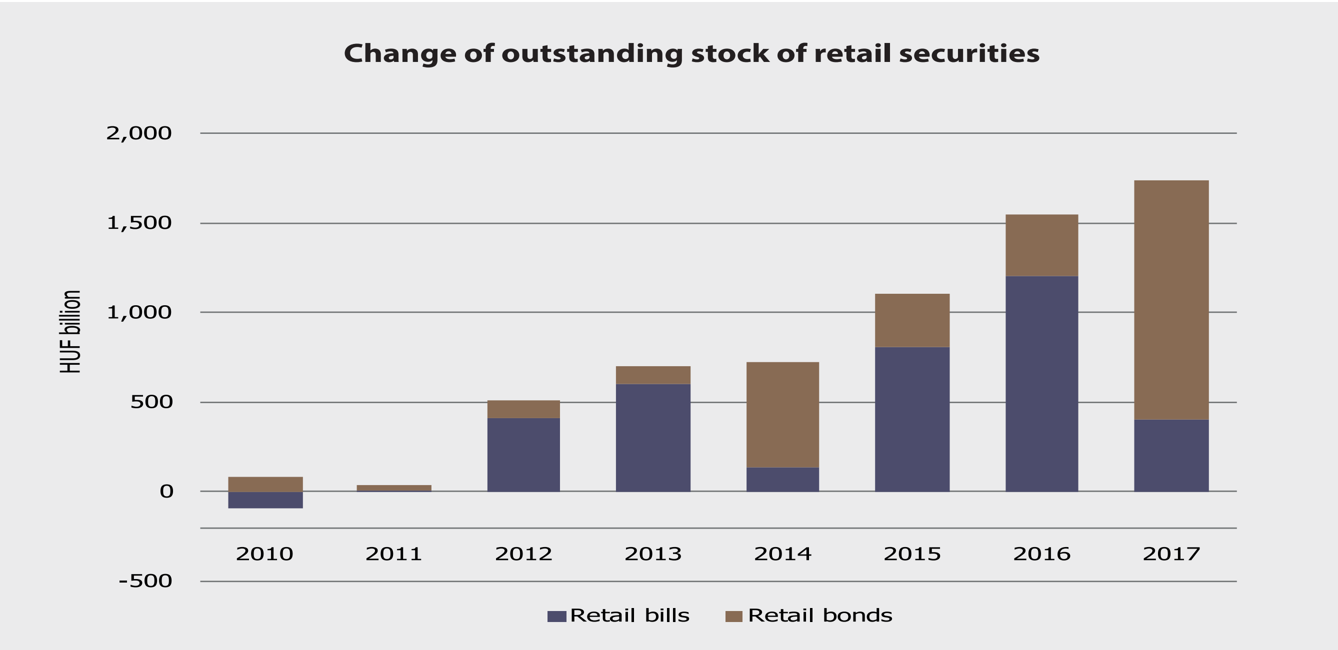
In line with the objectives of public debt management, medium to long term bonds continued to play an important role in the retail scheme in 2017. The inflation-linked Premium Hungarian Government Security and the floating rate Bonus Hungarian Government Security had a total net sale of HUF 936 billion. The very long term Babybond (with a maturity of 19 years) added an additional HUF 11 billion to funding. In 2017 ÁKK introduced a new, fixed rate retail bond with 2-years tenor. The total issuance of the 2-year Hungarian Government Security was HUF 377 billion. The total retail debt stock grew by HUF 1,735 billion over the year, which is more than two times higher than the HUF 700 billion planned, and contributed to a large extent to the year's successful financing from the domestic market.

Gross retail issuance:

HUF Billion

	2014	2015	2016	2017
Retail bills	**1 402**	**2 213**	**3 416**	**3 816**
1-year Hungarian Government Security	1 089	1 816	2 637	3 110
Half-year Hungarian Government Security	29	81	429	352
Treasury Savings Bills (1-year)	252	236	230	251
Treasury Savings Bills Plus	32	80	120	103
Retail bonds	**647**	**537**	**459**	**1 632**
2-year Hungarian Government Security	-	-	-	377
Premium Hungarian Government Security	226	396	367	1 172
Bonus Hungarian Government Security	372	83	26	11
Babybonds	9	8	9	11
Treasury Savings Bills (2-year)	40	49	57	61
Retail securities total	**2 049**	**2 749**	**3 875**	**5 448**

Source: ÁKK



Source: ÁKK

Unified name of retail government securities

From 2nd October 2017 ÁKK changed the name of some retail securities to create the Hungarian Government Securities umbrella brand in the retail market. With the unified names it became easier to identify, transparent and interpret the broad range of retail securities. After the unification the new names became the following:

Original name	Original short name	New name	New short name
Half-year Interest Bearing Treasury Bill	FKJ	Half-year Hungarian Government Security	FMÁP
1-year Interest Bearing Treasury Bill	KKJ	1-year Hungarian Government Security	1MÁP
2-year Government Bond	2MÁP	2-year Hungarian Government Security	2MÁP
Bonus Hungarian Government Bond	BMÁK	Bonus Hungarian Government Security	BMÁP
Premium Hungarian Government Bond	PMÁK	Premium Hungarian Government Security	PMÁP

Foreign currency financing

ÁKK planned to issue a total of EUR 1.2 billion of foreign currency denominated bonds in 2017, out of which EUR 1 billion was planned to be issued in the international market. Due to the ample demand for domestic (especially retail) securities, ÁKK issued less international FX bonds than planned, only one Panda bond of CNY 1 billion (EUR 127 million), by which transaction Hungary became the first country to have issued both in the Dim Sum and the Panda market.

Hungary's first ever International Bond Exchange transaction was executed in October, where USD 1.16 billion USD bonds were bought back and issued an EUR 1 billion 10 year euro bond. This transaction increased both the gross foreign currency denominated issuance and the redemption.

Foreign currency international bond issued by Hungary in 2017:

Currency	Amount	Date of issuance	Maturity	Tenor (years)	Coupon
CNY	1,000,000,000	27.07.2017	27.07.2020	3	4.85%
EUR	1,000,000,000	10.10.2017	10.10.2027	10	1.75%

New series of the domestic Premium Euro Government Bond and the Residency Bond were issued in 2017. The net domestic foreign currency bond issuance was significantly higher than planned and amounted to HUF 172 billion (EUR 55 million). ÁKK finished selling Residency Bonds in September 2017.

Series	Currency	Date of issuance	Maturity	Tenor (years)	Coupon
2020/X	EUR	04.04.2017	22.09.2020	3	Floater (Premium)
2021/X	EUR	03.10.2017	22.09.2021	4	Floater (Premium)
2022/T1-T3	EUR	2017	2022	5	Fixed (Zero coupon)

Source: ÁKK

According to the plan ÁKK did not draw any project financing loans in foreign currency except the draw down from the Paks 2 project totalling HUF 24 billion (EUR 80 million). The redemption of foreign currency denominated loans amounted to HUF 194 billion, thus the net redemption totalled HUF 170 billion, higher than planned by HUF 19 billion.

Due to the less than planned international FX bond issuance (without International Bond Exchange) and the FX bond buy-backs the net FX issuance was much lower than planned and amounted to HUF -461 billion (compared to the plan of HUF -200 billion) in 2017. The lower than planned net FX issuance contributed to higher reduction of the foreign currency debt.

V. The government debt in 2017

During 2017 the central government debt increased by HUF 1,316 billion (or by 5.2 per cent) to HUF 26,746 billion. The size of the debt was influenced by several factors.

Funding the net financing requirement of the budget totalling HUF 1,907 billion increased the debt, while the return of marked-to-market deposits placed at ÁKK (so-called 'other obligations') decreased the debt by HUF 468 billion. The appreciation of the Hungarian Forint against other currencies also decreased the HUF value of the debt by HUF 16 billion. As a consequence of the net financing need exceeding the net issuance and due to the repayment of a significant amount of marked-to-market deposits the safety reserves of the central government decreased by HUF 400 billion in 2017.

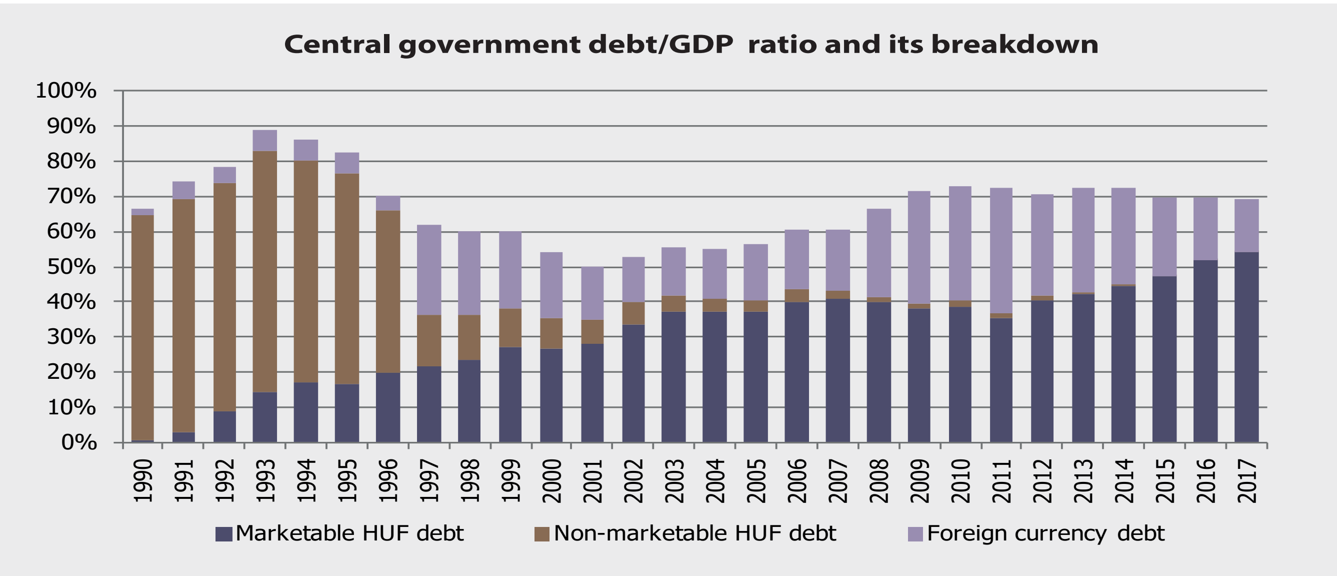
Central government debt

HUF Billion

	2016		2017		Change
Domestic debt	**18,431**	**72%**	**20,689**	**77%**	**2,259**
Loans	865	3%	1,041	4%	176
Government bonds	11,602	46%	11,806	44%	205
Discount T-bills	5,068	20%	6,803	25%	1,735
Retail securities	896	4%	1,039	4%	143
Foreign currency denominated debt	**6,257**	**25%**	**5,783**	**22%**	**-474**
Loans	1,102	4%	929	3%	-173
Bonds	5,155	20%	4,853	18%	-301
Total debt	**24,687**	**97%**	**26,472**	**99%**	**1,785**
Other obligations	743	3%	274	1%	-468
Grand total debt	**25,430**	**100%**	**26,746**	**100%**	**1,316**

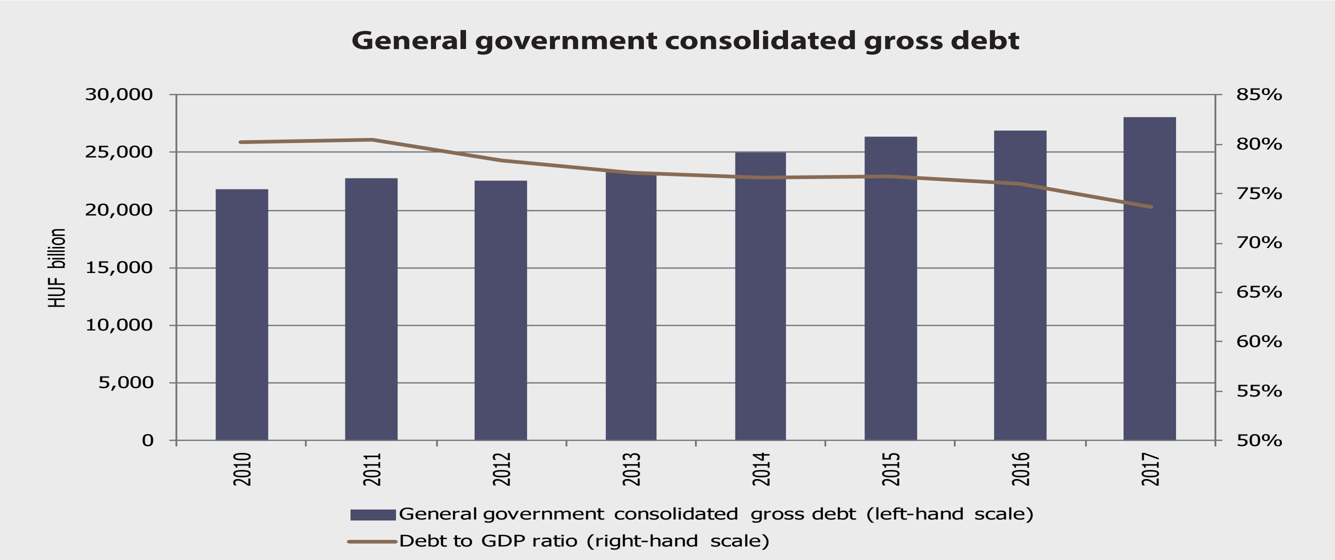
Source: ÁKK

According to preliminary data, the central government debt (without marked-to-market deposits) managed by ÁKK decreased from 71.8 to 70.0 per cent of GDP, while the general government gross debt to GDP ratio decreased by 2.4 per cent to 73.6 per cent in 2017.



Source: ÁKK

V. The government debt in 2017



Source: EUROSTAT (including debt of EXIM Bank)

Characteristics of the HUF debt portfolio

During 2017 the HUF denominated debt – which accounts for 77 per cent of the total debt – increased by HUF 2,259 billion (12.3 per cent) to HUF 20,689 billion. The net HUF issuance was higher than the net financing requirement and covered a large part of the FX redemption.

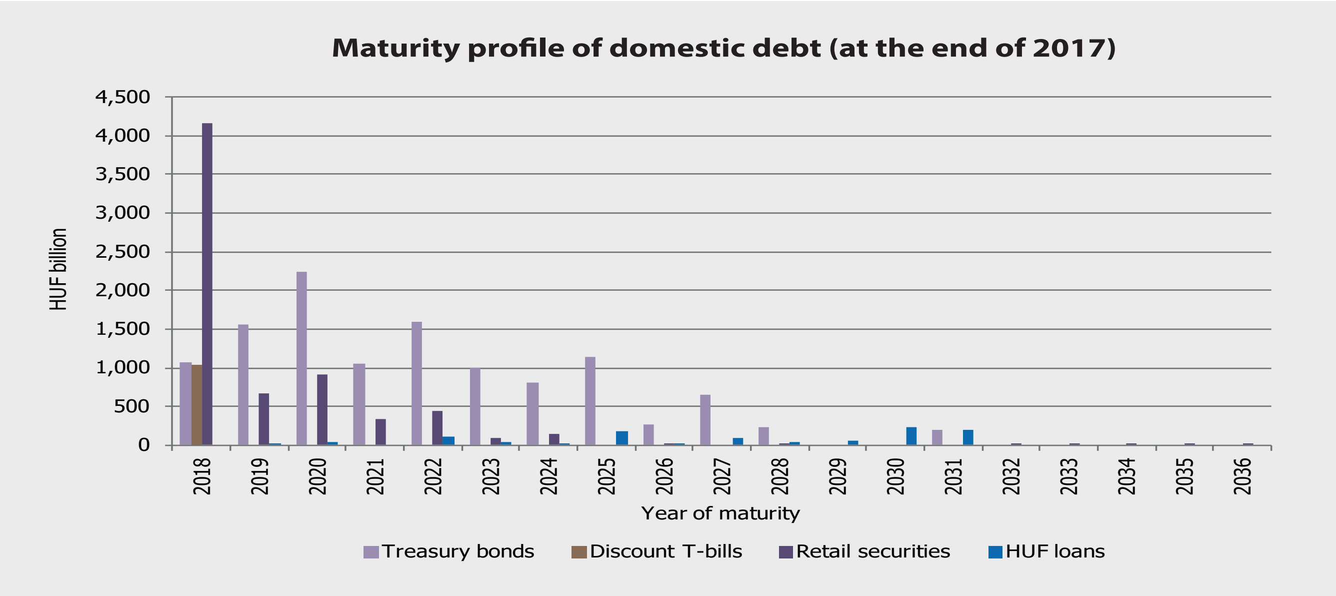
44 per cent of the total public debt was in the form of long-term HUF government bonds (excluding retail bonds). The total domestic wholesale bond portfolio of HUF 11,806 billion consisted of 23 bond series, the average size of a series was HUF 513 billion (ca. EUR 1.7 billion). 10 series had a volume in excess of HUF 600 billion (ca. EUR 2 billion), and the largest bond series reached a volume of HUF 1,137 billion (or EUR 3.7 billion).

The HUF 1,039 billion discount T-bill stock consisted of 17 series with an average outstanding amount of HUF 61 billion.

In 2017 the portfolio of retail government securities jumped from HUF 5,068 billion to HUF 6,803 billion. Retail securities accounted for 32.9% of the total domestic debt in comparison to their 27.5 per cent share at the end of 2016. Within the retail securities the stock of Treasury Savings Bills (securities available in the post office network) grew by HUF 15 billion and amounted to HUF 469 billion. The stock of inflation-linked Premium Hungarian Government Security and the floating rate Bonus Hungarian Government Security increased by HUF 936 billion and amounted to HUF 2,458 billion, while the outstanding amount of the Baby-bond (with a maturity of 19 years) totalled HUF 38 billion at the end of 2017. The introduction of the fixed rate 2-year Hungarian Government Security in spring 2017 was a success, its outstanding amount grew up to HUF 377 billion in its first year. The outstanding amount of the 1-year Hungarian Government Security grew by HUF 473 billion and amounted to HUF 3,110 billion, while the stock of the Half-year Hungarian Government Security decreased by HUF 77 billion and amounted to HUF 352 billion.

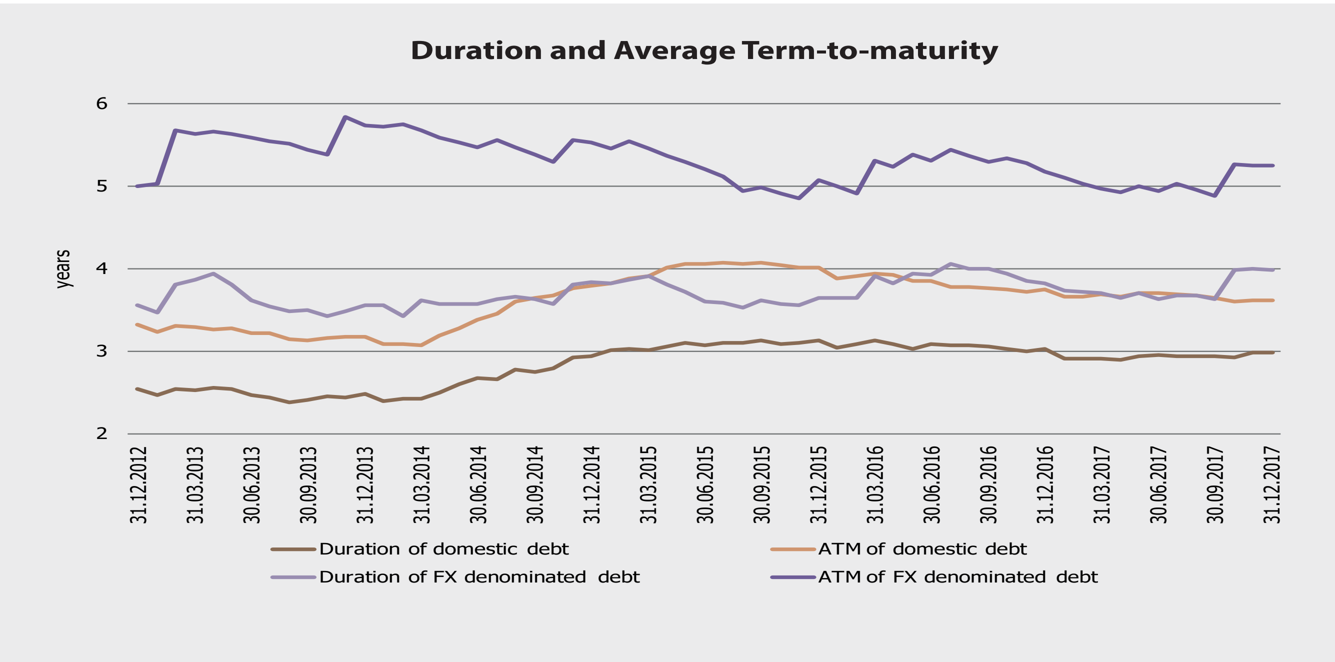
The non-marketable component of the HUF bond portfolio did not change in amount, but its proportion continued to decrease in 2017 as well, as there are no new issuances of such government bonds and the existing portfolio matures gradually (but there was not any maturities in 2017). The end-of-year volume of non-marketable government bonds was HUF 39 billion, less than 0.2 per cent of the total debt.

The volume of loans denominated in Hungarian forint increased in 2017 (as a result of new draw downs) by HUF 176 billion to HUF 1,041 billion.



Source: ÁKK

As a result of the normal shortening and the increasing share of retail securities the duration and average term-to-maturity characteristics of the domestic debt decreased to a small extent. The duration of the HUF denominated debt portfolio decreased from 3.03 years to 2.98 and the average term-to-maturity also decreased from 3.75 years to 3.61 years in 2017.

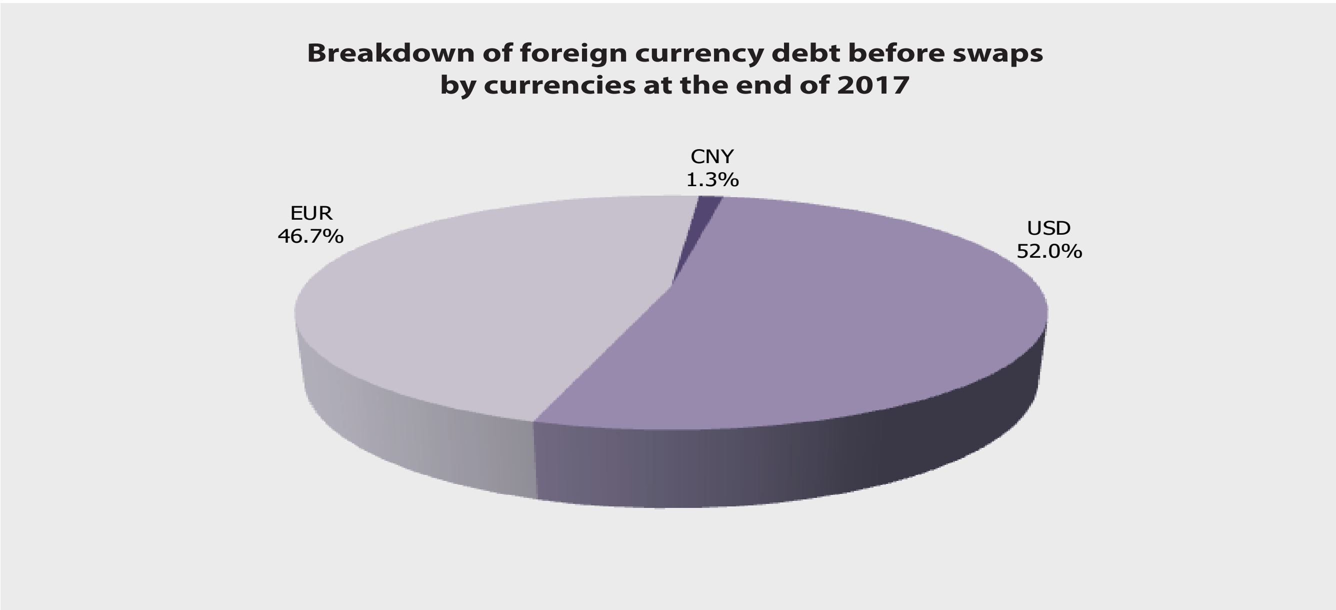


Source: ÁKK

Characteristics of the foreign currency debt portfolio

The gross foreign currency government debt decreased by HUF 474 billion in 2017, reaching HUF 5,783 billion (EUR 19 billion) by the end of the year. The share of foreign currency debt within the total gross government debt (excluding marked-to-market deposits) declined from 24.6 to 21.6 per cent during 2017.

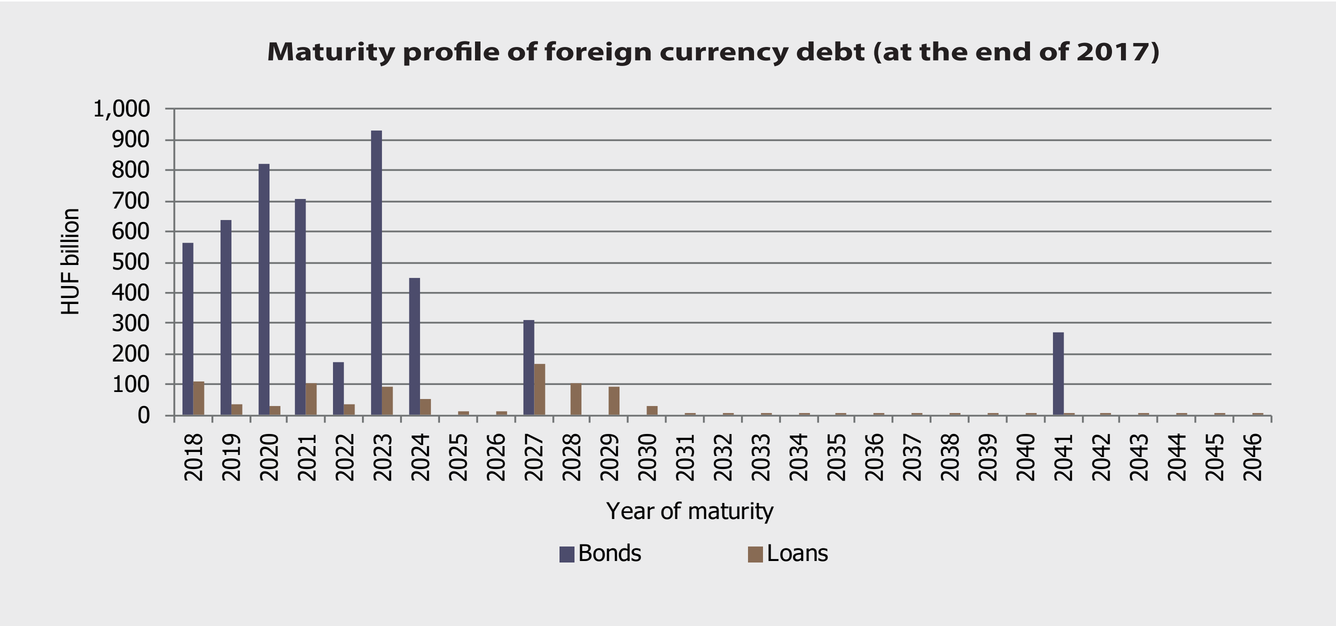
The volume of outstanding foreign currency bonds (after swaps) reached HUF 4,853 billion by the end of the year, decreasing significantly from the end of 2016 (HUF 5,155 billion), mainly as a result of less than planned international foreign currency denominated bond issuance, the maturities, buy-backs and also the appreciation of the forint. On 31 December 2017 there were 29 series of foreign currency bonds outstanding. 19 of which had been issued in euro (including the domestic euro bonds as well), 8 in US dollars, and 2 in Chinese Yuan Renminbi. In accordance with the strategy and benchmarks, all non-euro bonds had been converted into euro liabilities through swap transactions. Bonds accounted for 84% of the total foreign currency debt portfolio.



Source: ÁKK

At the end of 2017 100% of the foreign currency debt was denominated in euro (after swaps).

The foreign currency loan portfolio consisted of long-term project financing loans from international financing institutions (e.g. EIB and CEB) and from the loan drawn down in the Paks 2 project. As a result of the low amount of new foreign currency loans and the large redemptions took place in 2017 the share of loans within the total foreign currency debt declined from 18 to 16 per cent in 2017.



Source: ÁKK

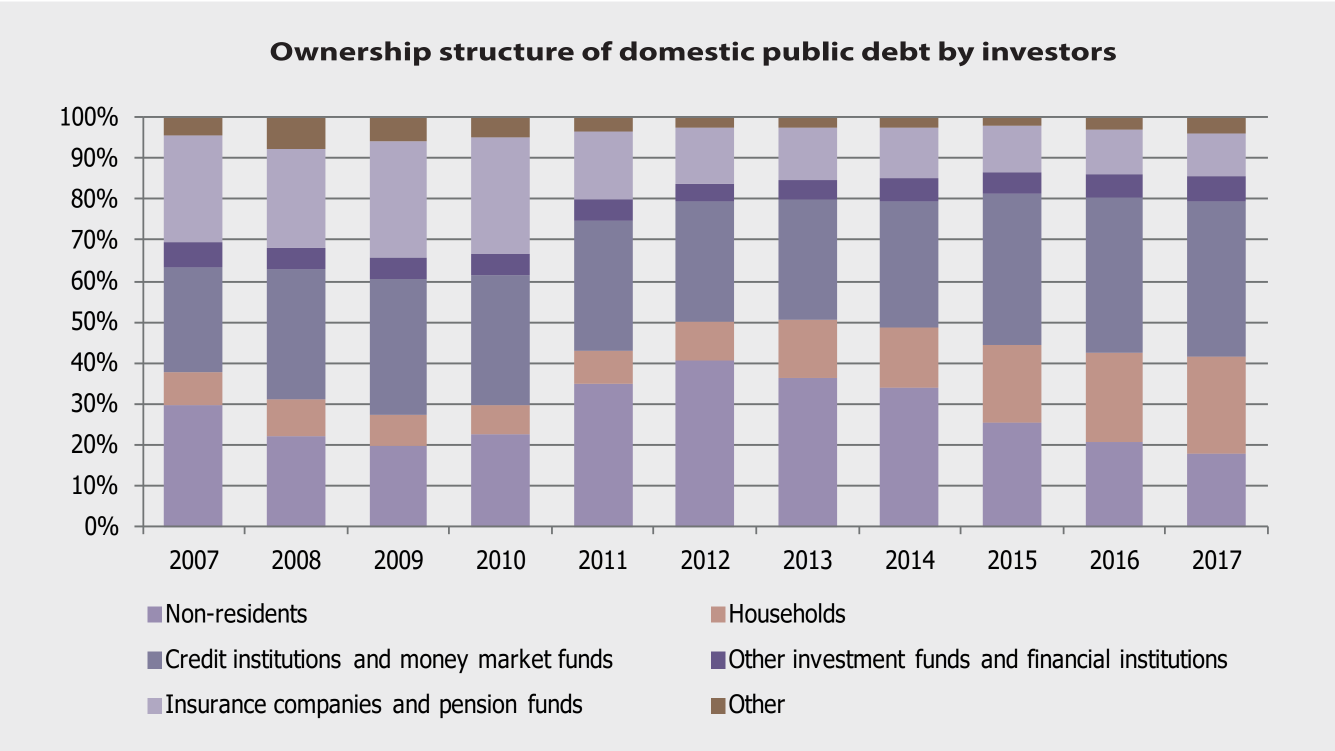
During 2017 the average term to maturity of the foreign currency portfolio increased from 5.2 years to 5.3 years and the duration also increased from 3.8 years to 4.0 years.

Other obligations

In order to reduce counterparty risk associated with the swap transactions concluded by ÁKK, so-called marked-to-market deposits are being placed as collateral covering the net value of their swap positions. Such deposits placed with ÁKK are shown as part of the government debt among 'other obligations'. Due to the appreciation of the euro against other currencies ÁKK had to pay back a significant part of the deposits placed at ÁKK to its swap partners. As of 31 December 2017 marked-to-market deposits placed with ÁKK totalled HUF 274 billion (EUR 0.9 billion), by HUF 468 billion less than at the end of 2016.

The ownership structure of government debt

According to statistics published by the National Bank of Hungary, the following changes took place in the ownership structure of the domestic government securities in 2017. The share of the formerly largest investor group – namely non-resident investors – continued to decline from 21 per cent to 18 per cent. Domestic retail investors, however, increased further their share significantly to 24 per cent. The share of credit institutions and insurance companies/pension funds remained almost the same.



Source: NBH, KELER, ÁKK

In 2017 non-residents decreased their share both in nominal and relative terms. Non-resident holdings of HUF denominated government securities decreased by HUF 57 billion to HUF 3,385 billion. At the same time the duration of their holdings remained the same at 4.8 years, while the ATM of their holdings decreased by 0.1 year to 5.4 years in 2017. Foreign investors keep holding primarily longer dated bonds, and both the duration and the ATM of the non-resident holdings are longer than that of the total outstanding stock of government securities.

VI. Liquidity management

According to the Act on the Economic Stability of Hungary, liquidity management of the central government is also the responsibility of ÁKK. The goal of ÁKK is to maintain the balance of the Treasury Single Account (TSA) which serves as a financing reserve at a targeted level and the excessive volatility of the cash balance is managed with liquidity management operations. These operations may be active (placement of funds) or passive (fund-raising) transactions, however, ÁKK only invests temporary excess liquid funds from the TSA if repo partners show adequate demand, otherwise it keeps the extra cash on the TSA.

In 2017 ÁKK used the following instruments to manage the end-of-day balance of the TSA:

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

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

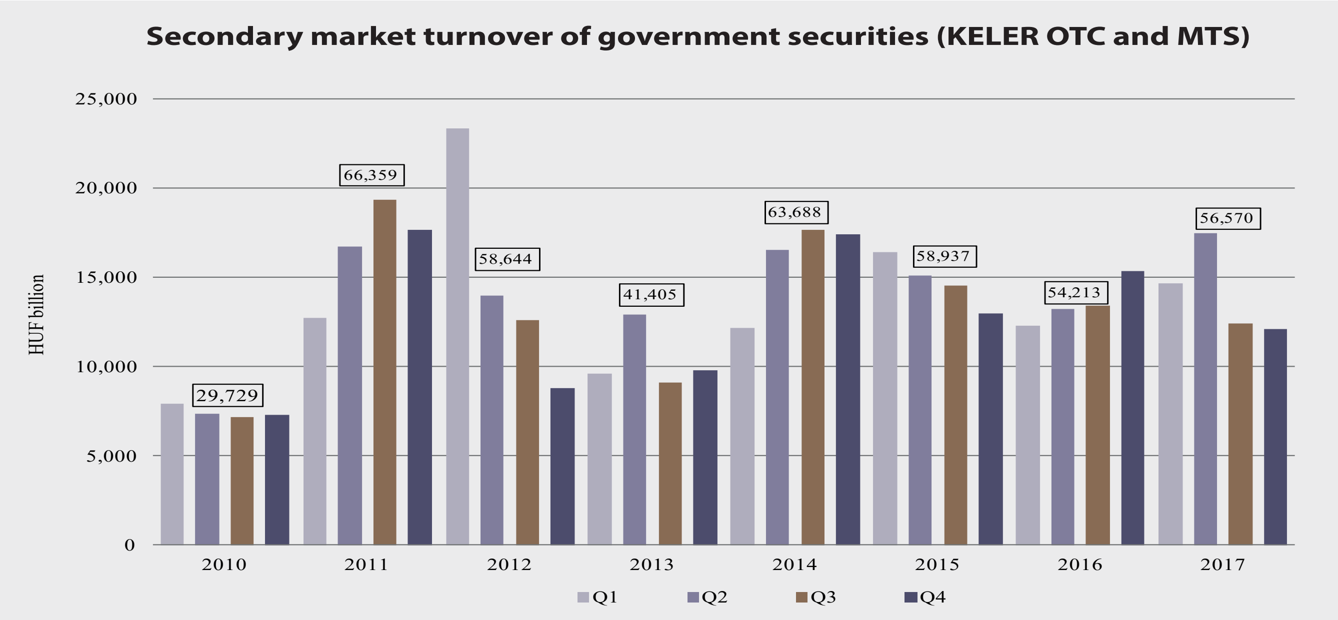
Sales of liquidity discount treasury bills took place six times in 2017 – only from October - with a total volume of HUF 265 billion. Ample liquidity in the TSA made it unnecessary to increase liquidity of the TSA with bills before October.

Liquidity repo transactions are ÁKK's main tool for fine-tuning the end-of-day balance of the Treasury Single Account. In 2017 the use of repo transactions decreased slightly and totalled of HUF 22,445 billion. Liquidity management was effective and the end-of-day TSA balance was always higher than the minimum target level in 2017.

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

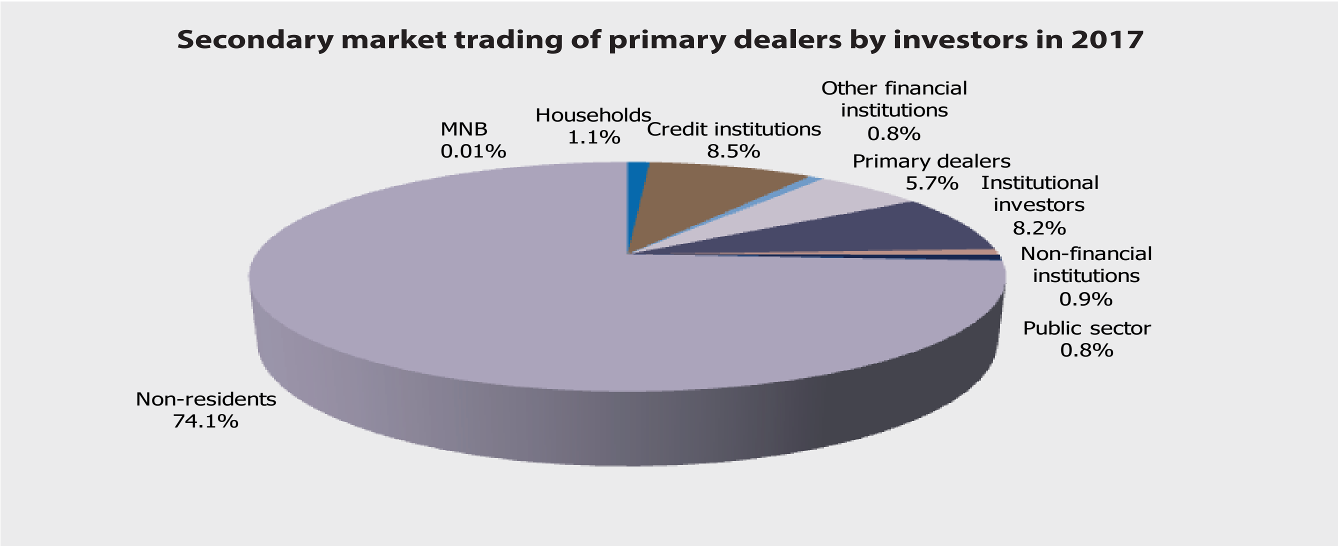
VII.The secondary market of Hungarian government securities

MTS Hungary is the main electronic platform of trading government securities and Primary dealers fulfil their price quotation obligations on this platform, however more than 99% of all secondary trade is executed in the over-the-counter (OTC) market. According to data from the KELER Central Depository Ltd., the total volume of OTC trading in government securities was HUF 56,444 billion in 2017 (more than 4 times the size of the total outstanding marketable debt), out of which 95 per cent was in government bonds and 5 per cent in discount treasury bills.



Source: KELER, BSE

The average size of deals with Primary dealers (excluding retail transactions) was HUF 798 million, which is lower by HUF 240 million than in the previous year. Over the year, the 2025/B government bond with an 8-year remaining term-to-maturity had the largest turnover (HUF 6,492 billion), followed by the 10-year 2027/A and the 7-year 2024/B bond.



Source: Primary dealers, ÁKK

The most active Primary dealer and the winner of the title 'Primary dealer of the Year' for 2017 was ING Bank N.V., while in the retail program the winner was OTP Bank.

VIII. The institutional framework for the issuance of government securities

ÁKK sells government securities through intermediaries to investors. In the domestic market, 87 per cent of HUF-denominated government securities were sold through the Primary dealers in 2017, the rest through retail channels.

The primary dealer system

The Primary dealer system for government securities was set up in 1996 in order to establish a more secure institutional base for the financing of government debt, to reduce the costs of debt management and to improve the transparency and liquidity of the secondary market in government securities.

Since May 2004, any investment firm or bank registered in any European Union or an OECD Member State may become a Primary dealer in Hungarian government securities if it meets the contractual requirements and signs a Primary dealer contract with ÁKK. Along with a number of obligations in the primary and secondary market, the Primary dealer status also guarantees exclusive rights. In 2017 7 out of the 15 Primary dealers were non-resident institutions.

Primary dealers at the end of 2017:

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

Only Primary dealers may:

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

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

VIII.The institutional framework for the issuance of government securities

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 some of its retail government securities, the Half-year Hungarian Government Securities, the 1-year Hungarian Government Securities, the new 2-year Hungarian Government Securities, the Premium Hungarian Government Securities and the Bonus Hungarian Government Securities.

Retail debt programmes

The State Treasury's branch network provides direct access to government securities for retail investors. Supervised by ÁKK, the Treasury branch offices in Budapest and the county seats and other major cities quote two-way prices for retail investors for publicly issued bonds, Premium- and Bonus Hungarian Government Securities, Baby-bonds, discount treasury bills, the Half-, 1- and 2-year Hungarian Government Securities. Government securities may also be purchased and sold through the Hungarian State Treasury's online banking service, mobile application or by phone.

The Hungarian Post Office participates in the sale of three retail government securities. The 1 and 2-year Treasury Savings Bills are the only printed government securities, designed specifically for retail investors. Post Office also sells Treasury Savings Bill Plus, a dematerialised 1-year treasury bill.

The dealers of foreign currency bond issues

Lead managers of international EUR and USD bond issuances are selected from among the primary dealers individually for each transaction. In 2017 Hungary issued EUR 1 billion Eurobond in the international capital markets (via an international liability management operation). The lead managers of the international bond exchange were: BNP Paribas, Citigroup, Deutsche Bank and ING. The lead managers of the Panda bond issuance of CNY 1 billion were Bank of China Limited and HSBC Bank (China).

On 20 November 2012, the sale of a new 3-year inflation linked domestic bond denominated in EUR ('Premium Euro Government Bond', P€MÁK) started, which became a success among investors. The bond is available in the Hungarian State Treasury network.

In 2013 the sale of a new euro denominated bond was started (so called Residency bonds). Further information can be found in the website of ÁKK (www.akk.hu). In September 2017 ÁKK finished selling Residency Bond.

IX.The institutional framework and the objectives of government debt management

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

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

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

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

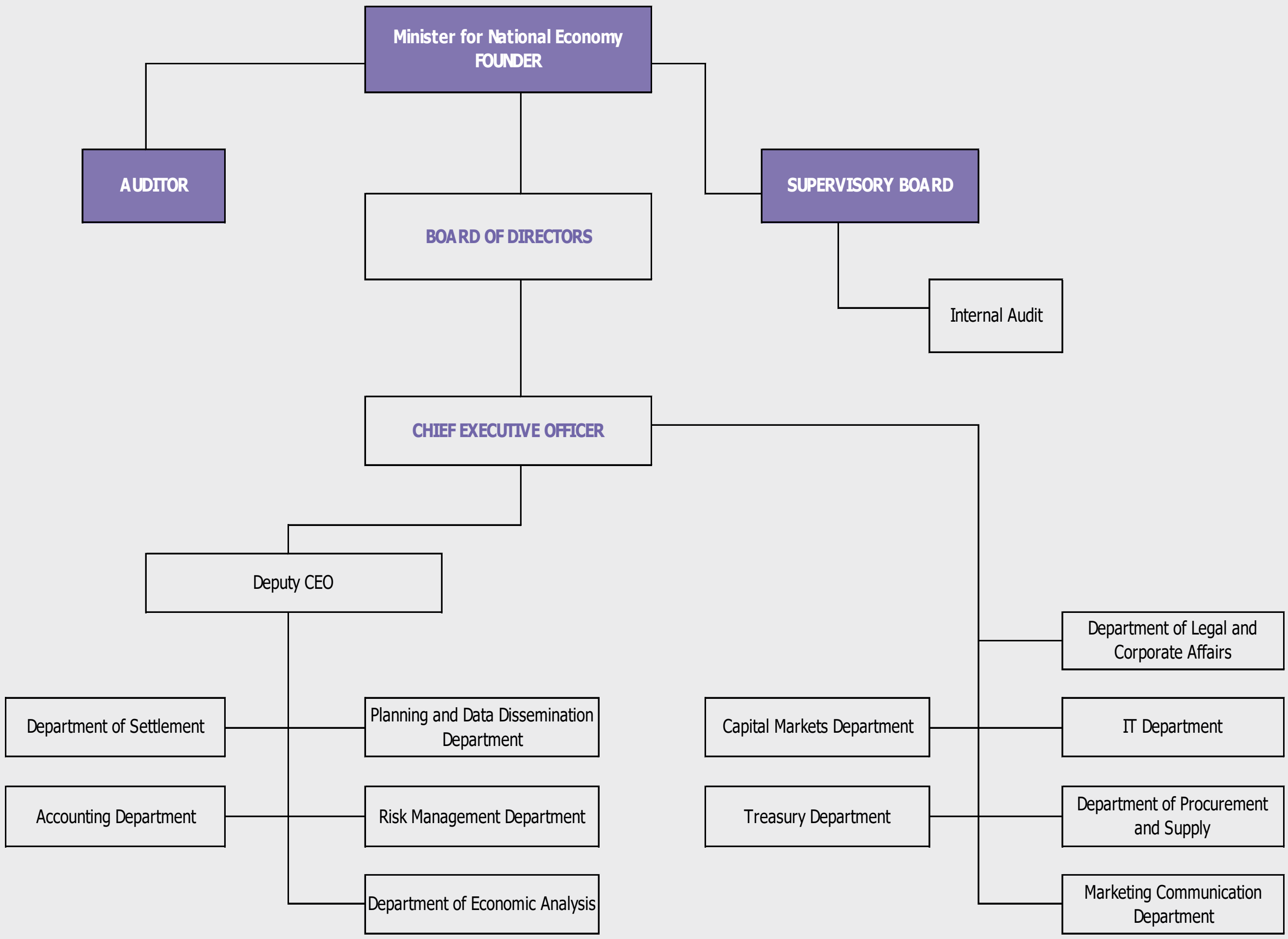
IX.The institutional framework and the objectives of government debt management

The responsibilities of ÁKK

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

- developing a long-term financing strategy in line with economic policy, which determines the objectives of debt management and the means of their implementation;
- preparing the annual and medium-term financing plans and planning the annual interest expenditure based on the annual Budget Act and in line with the strategy;
- performing the required financing operations, i.e. organising and implementing both domestic and international government securities issuance and raising of loans;
- ensuring the payment obligations burdening the central government debt;
- managing the temporarily free cash funds of the state (liquidity management);
- effecting debt redemptions and interest payments;
- organising and continuously developing the government securities market (the primary dealer system, sales channels, secondary market etc.);
- expressing its opinion on the financial terms and conditions of borrowings with a state guarantee; on request, organising transactions with individual guarantees (with a lesser role for guarantees prescribed by legislation).
- may participate in the management of the free cash funds of the National Deposit Insurance Fund and the Reorganization Fund;
- may participate in management of cash funds of the Investor Protection Fund;
- may participate in financing related to MVM Paks II. Nuclear Power Plant Development.

Organisational structure of ÁKK as at 31 December 2017



X.The information services of ÁKK

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

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

Other pages of the website provide information on ÁKK as a company, the goals, activities, legal framework and the organisational structure of ÁKK.

The "Statistics' menu provides access to main features of the government securities, the results of the auctions and subscriptions, yields, government security indices and statistics related to the secondary market, government debt and financing.

The 'Government securities issuance and trading' menu includes the description of types of government securities, rules of procedure and information about the sales system of government securities (Primary dealers, retail sale).

The 'Publications' menu provides access to the publications of ÁKK in electronic (pdf) format. The menu also contains the public analyses prepared by ÁKK.

The 'Releases' menu contains the press releases of the 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.

For retail investors ÁKK set up another website, www.allampapir.hu, where they can find all relevant information about retail instruments (types, list of retail security dealers, descriptions etc.), but it is available only in Hungarian.

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

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

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

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

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

1. The central government gross debt as at 31.12.2017 (HUF million)

HUF denominated debt			
Hungarian Government Bonds	Maturity	Coupon	Outstanding amount
2018/A	20.12.2018	5.50%	279,001.10
2018/B	25.04.2018	4.00%	352,683.73
2018/C	22.06.2018	2.50%	324,817.14
2018/D	24.10.2018	Floating rate	157,766.12
2018/I	25.04.2018	Floating rate (retail)	41,731.73
2018/J	05.07.2018	Floating rate (retail)	89,730.30
2018/K	21.11.2018	Floating rate (retail)	114,944.56
2018/N	20.04.2018	Floating rate (retail)	5,692.26
2018/O	20.04.2018	Floating rate (retail)	16,093.92
2018/P	23.07.2018	Floating rate (retail)	15,064.81
2019/A	24.06.2019	6.50%	721,844.39
2019/B	20.05.2019	Floating rate	366,070.77
2019/C	30.10.2019	2.00%	323,418.38
2019/D	28.08.2019	Floating rate	147,681.67
2019/H1	22.04.2019	2.50%	266,438.26
2019/H2	22.07.2019	2.50%	51,013.01
2019/H3	22.10.2019	2.50%	59,379.78
2019/I	03.02.2019	Floating rate (retail)	5,003.39
2019/J	03.02.2019	Floating rate (retail)	13,656.31
2019/K	03.02.2019	Floating rate (retail)	32,548.00
2019/L	21.10.2019	Floating rate (retail)	181,839.19
2020/A	12.11.2020	7.50%	816,813.22
2020/B	24.06.2020	3.50%	885,057.30
2020/C	23.09.2020	1.00%	533,260.26
2020/I	24.04.2020	Floating rate (retail)	109,453.07
2020/J	26.08.2020	Floating rate (retail)	161,138.90
2020/K	29.07.2020	Floating rate (retail)	367,455.22
2020/N	20.05.2020	Floating rate (retail)	32,321.68
2020/O	20.05.2020	Floating rate (retail)	112,428.01
2020/P	22.07.2020	Floating rate (retail)	85,502.37
2020/Q	22.09.2020	Floating rate (retail)	9,167.36
2020/R	23.07.2020	Floating rate (retail)	42,350.80
2021/A	23.06.2021	Floating rate	394,252.45
2021/B	27.10.2021	2.50%	652,085.59
2021/I	20.10.2021	Floating rate (retail)	259,260.72
2021/J	26.05.2021	Floating rate (retail)	80,563.16

2022/A	24.06.2022	7.00%	971,886.04
2022/B	26.10.2022	1.75%	621,545.08
2022/I	29.07.2022	Floating rate (retail)	226,886.38
2022/J	22.11.2022	Floating rate (retail)	205,477.08
2022/N	20.09.2022	Floating rate (retail)	9,609.18
2022/O	27.04.2022	Floating rate (retail)	2,145.48
2023/A	24.11.2023	6.00%	998,274.80
2023/I	22.03.2023	Floating rate (retail)	86,656.13
2024/B	26.06.2024	3.00%	803,906.07
2024/N	26.08.2024	Floating rate (retail)	138,123.01
2024/O	24.04.2024	Floating rate (retail)	243.02
2025/B	24.06.2025	5.50%	1,137,447.72
2026/B	24.04.2026	Floating rate	39,177.72
2026/D	22.12.2026	2.75%	235,728.38
2026/N	22.09.2026	Floating rate (retail)	11,904.64
2027/A	27.10.2027	3.00%	647,694.56
2028/A	22.10.2028	6.75%	236,036.36
2028/N	22.03.2028	Floating rate (retail)	520.47
2031/A	22.10.2031	3.25%	201,293.95
2032/S	02.12.2032	Floating rate, Babybond	29,953.45
2033/S	01.02.2033	Floating rate, Babybond	3,572.77
2034/S	01.02.2034	Floating rate, Babybond	2,318.20
2035/S	01.02.2035	Floating rate, Babybond	1,741.80
2036/S	01.02.2036	Floating rate, Babybond	644.03
Matured, but unclaimed government bonds			83.37
Total			**14,720,398.60**
Repos with government bonds (repos actually increase or decrease the total amount)			-41,509.75
Discount Treasury Bills			1,039,164.79
Repos with discount Treasury bills (repos actually increase or decrease the total amount)			0.00
1-year Hungarian Government Security			3,109,736.09
Out of which matured, but unclaimed			37.30
Half-year Hungarian Government Security			351,808.45
Treasury Savings Bills (Plus)			103,475.55
Treasury Savings Bills (1-year)			250,980.48

Treasury Savings Bills (2-year)	114,231.41
HUF loans	1,041,075.62
Matured, but unclaimed other retail government securities	52.80
Total HUF debt	20,689,414.04

Foreign currency debt					**Outstanding amount (HUF million)**	**Outstanding amount (EUR million)**
Syndicated loan and loans drawn down from revolving credit facilities*					**0.00**	**0.00**
Loans granted by International Financial Institutions*					**760,138.21**	**2,450.95**
Loans assumed from the market*					**168,927.96**	**544.68**
Government bonds						
Maturity date	Currency	Amount in original currency	Maturity (years)	Coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
24.02.2020	EUR	860,300,000	15	3.88%	266,813.44	860.30
11.06.2018	EUR	1,288,018,000	10	5.75%	399,465.90	1,288.02
29.01.2020	USD	1,975,000,000	10	6.25%	456,753.63	1,472.73
29.03.2021	USD	3,000,000,000	10	6.375%	680,236.42	2,193.32
29.03.2041	USD	1,250,000,000	30	7.63%	323,525.00	1,043.16
11.01.2019	EUR	940,000,000	7.0	6.00%	280,653.75	904.93
21.02.2023	USD	2,000,000,000	10	5.38%	497,953.63	1,605.58
19.02.2018	USD	713,130,000	5	4.125%	95,585.33	308.20
22.11.2023	USD	2,000,000,000	10	5.75%	517,640.00	1,669.05
25.03.2024	USD	2,000,000,000	10	5.375%	517,640.00	1,669.05
25.03.2019	USD	773,030,000	5	4.00%	131,390.49	423.65
25.04.2019	CNY	1,000,000,000	3	6.250%	39,730.00	128.10
27.07.2020	CNY	1,000,000,000	3	4.850%	39,730.00	128.10
10.10.2027	EUR	1,000,000,000	10	1.75%	310,140.00	1,000.00
Total					**4,557,257.60**	**14,694.19**
Cross-currency swaps					**-411,345.33**	
Premium Euro Hungarian Government Bond						
Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
2018/X	EUR	21.09.2018	3	Floating rate, Premium	51,153.69	164.94
2019/X	EUR	20.09.2019	3	Floating rate, Premium	60,604.00	195.41
2020/X	EUR	22.09.2020	3	Floating rate, Premium	19,090.33	61.55
2021/X	EUR	22.09.2021	3	Floating rate, Premium	4,821.57	15.55
Total					**135,669.59**	**437.45**

Residence Bond						
Code	Currency	Maturity date	Maturity (years)	Yield Zero coupon	Outstanding amount (HUF million)	Outstanding amount (EUR million)
2018/T	EUR	20.12.2018	5	2.53%	33,340.05	107.50
2019/T	EUR	20.12.2019	5	2.24%	138,167.37	445.50
2020/T	EUR	20.12.2020	5	2.00%	104,238.05	336.10
2021/T	EUR	20.12.2021	5	2.00%	2,791.26	9.00
2021/T1	EUR	27.03.2021	5	2.00%	5,396.44	17.40
2021/T2	EUR	27.06.2021	5	2.00%	18,701.44	60.30
2021/T3	EUR	27.09.2021	5	2.00%	30,517.78	98.40
2021/T4	EUR	27.12.2021	5	2.00%	67,641.53	218.10
2022/T1	EUR	27.03.2022	5	2.00%	36,193.34	116.70
2022/T2	EUR	27.06.2022	5	2.00%	108,300.89	349.20
2022/T3	EUR	27.09.2022	5	2.00%	26,610.01	85.80
Total					**571,898.16**	**1,844.00**
Total foreign currency debt					**5,782,546.19**	
Total central government debt					**26,471,960.22**	
Other obligations of ÁKK (marked-to-market deposits placed at ÁKK)					**274,245.87**	
Grand total					**26,746,206.09**	

* Including swaps

2. The credit rating history of the long-term debt of Hungary

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

Foreign currency denominated debt			
Változás dátuma	Moody's	Standard and Poor's	Fitch Ratings
24.11.2011	Ba1	BBB-	BBB-
21.12.2011	Ba1	BB+	BBB-
06.01.2012	Ba1	BB+	BB+
23.11.2012	Ba1	BB	BB+
20.12.2012	Ba1	BB	BB+
20.03.2015	Ba1	BB+	BB+
20.05.2016	Ba1	BB+	BBB-
16.09.2016	Ba1	BBB-	BBB-
04.11.2016	Baa3	BBB-	BBB-

Standard and Poor’s and Fitch Ratings assigned a ‘positive' rating outlook, while Moody’s assigned a ‘stable' rating outlook to the long-term foreign currency debt of Hungary at the end of 2017.

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-

HUF denominated debt			
Date of change	Moody's	Standard and Poor's	Fitch Ratings
10.11.2008	A3	BBB+	BBB+
17.11.2008	A3	BBB	BBB+
02.03.2009	A3	BBB	BBB+
30.03.2009	A3	BBB-	BBB+
31.03.2009	Baa1	BBB-	BBB+
02.10.2009	Baa1	BBB-	BBB+
23.07.2010	Baa1	BBB-	BBB+
06.12.2010	Baa3	BBB-	BBB+
23.12.2010	Baa3	BBB-	BBB
06.06.2011	Baa3	BBB-	BBB
11.11.2011	Baa3	BBB-	BBB
24.11.2011	Ba1	BBB-	BBB
21.12.2011	Ba1	BB+	BBB
06.01.2012	Ba1	BB+	BBB-
23.11.2012	Ba1	BB	BBB-
20.12.2012	Ba1	BB	BBB-
20.03.2015	Ba1	BB+	BBB-
16.09.2016	Ba1	BBB-	BBB-
04.11.2016	Baa3	BBB-	BBB-

Standard and Poor’s and Fitch Ratings assigned a ‘positive' rating outlook, while Moody’s assigned a ‘stable' rating outlook to the long-term foreign currency debt of Hungary at the end of 2017.

3. The addresses of primary dealers

Primary dealer	Address
BNP Paribas SA	3 Suwak, 02-676 Warsaw, Poland (Warsaw Branch)
CIB Bank Zrt.	Budapest, H-1027 Medve utca 4-14.
Citibank Europe Plc.	Budapest, H-1051 Szabadság tér 7. (Hungarian Branch)
Deutsche Bank AG	Winchester House, 1 Great Winchester Street, London, EC2N 2DB, United Kingdom (London Branch)
ERSTE Befektetési Zrt.	Budapest, H-1138 Népfürdő u. 24-26
Goldman Sachs International	133 Fleet Street, London EC4A 2BB, United Kingdom
ING Bank N.V.	Budapest, H-1068 Dózsa György út 84/B. (Hungarian Branch)
J.P. Morgan Securities Plc.	25 Bank Street, Canary Wharf, London E14 5JP, United Kingdom
K&H Bank Zrt.	Budapest, H-1095 Lechner Ödön fasor 9.
Magyar Takarékszövetkezeti Bank Zrt.	Budapest, H-1122 Pethényi köz 10.
Merrill Lynch International	2 King Edward Street, London, EC1A 1HQ, United Kingdom
MKB Bank Zrt.	Budapest, H-1056. Váci u. 38.
OTP Bank Nyrt.	Budapest, H-1051 Nádor u. 16.
Raiffeisen Bank Zrt.	Budapest, H-1054 Akadémia u. 6.
UniCredit Bank Hungary Zrt.	Budapest, H-1054 Szabadság tér 5-6.

4. Selected parts of legislation governing the legal status of ÁKK and government debt management*

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

CHAPTER II

Reduction of government debt

1. Definition and calculation of government debt

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

(...)

Chapter III

The government debt management agency

4. Legal status of the Government Debt Management Agency

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

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

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

(4) The operation of GDMA Pte. Ltd. – unless otherwise provided by the present Act – are governed by the provisions of the Civil Code related to the business associations.

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

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

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

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

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

b) other revenues.

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

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

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

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

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

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

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

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

e) organises the secondary market of government securities,

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

g) analyses the tendencies of the government debt service falling under point a) and the government securities market,

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

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

j) executes credit and deposit operations,

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

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

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

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

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

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

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

d) upon authorization of law may fulfill payment obligations related to the realisation of the capital increase provided on behalf of the state to MVM Paks II. Nuclear Power Plant Development Private Company Limited by Shares financing the investment as defined in Paragraph 1 of the Section 1. of Act No. VII. of 2015 on the investment related to the maintenance of the capacity of the Paks Nuclear Power Plant and the amendment of related Acts (including the payments set forth in Section 2. of Article 1 of the Agreement promulgated by the Act No. XXIV. of 2014 on the promulgation of the Agreement between the Government of the Russian Federation and the Government of Hungary on the extension of a state credit to the Government of Hungary for financing of the construction of nuclear power plant in Hungary), in accordance with the method, amount and timing defined by the instrumentality exercising the entirety of the ownership rights and obligations of the state

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

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

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

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

(…)

ACT No. CXCV. of 2011 on the public finances

Authorisation of the Minister responsible for the public finances

5.§ (2) In the central subsystem of public finances the minister responsible for the public finances ensures the consumption of the central budget surplus, financing the deficit of the central budget and the government debt management – without the establishment of financing revenues and expenses in the Central Budget Act.

5. The balance sheet and the profit and loss account of ÁKK

I. Balance sheet

data in HUF thousand

	Assets	2016	2017
	A) Fixed assets	97,669	88,596
I	Intangible assets	28,810	26,537
II	Tangible assets	54,686	49,464
III	Invested financial assets	14,173	12,595
	B) Current assets	465,254	458,147
I	Inventories	0	0
II	Receivables	20,548	14,519
III	Securities	0	0
IV	Cash and cash equivalents	444,706	443,628
	C) Accrued and deferred assets	10,499	16,201
	Assets in total	573,422	562,944

data in HUF thousand

	Liabilities	2016	2017
	D) Capital and reserves	483,553	444,295
I	Subscribed capital	300,000	300,000
IV	Profit reserve	54,914	54,914
VII	Balance-sheet profit or loss	128,639	89,381
	E) Provisions	0	0
	F) Liabilities	73,408	91,588
I	Subordinated liabilities	0	0
II	Long-term liabilities	0	0
III	Short-term liabilities	73,408	91,588
	G) Accrued and deferred liabilities	16,461	27,061
	Liabilities in total	573,422	562,944

Budapest, 13 March 2018

György Barcza
CEO

II. Profit and loss account

data in HUF thousand

	Liabilities	2016	2017
I	Net sales revenue	1,165,934	1,185,231
III	Other revenue	53,236	3,533
IV	Material expenses	252,514	261,767
V	Personnel expenses	781,920	781,911
VI	Depreciation and amortisation	39,249	40,946
VII	Other expenses	10,735	6,072
A	Operating profit or loss	134,752	98,068
B	Profit or loss from financial transactions	3,132	170
C	Profit or loss on ordinary activities	137,884	98,238
D	Extraordinary profit or loss	0	0
E	Profit or loss before taxation	137,884	98,238
XII	Tax payable	9,245	8,857
F	Profit or loss after taxation	128,639	89,381
23	Approved dividends	128,639	89,381
G	Balance-sheet profit or loss	0	0

Budapest, 13 March 2018

György Barcza
CEO

6. Senior officials of ÁKK in december of 2017

Members of the Board of Directors:

László Balogh, chairman

Péter Benő Banai, member

Viktor József Asztalos, member

Dr. Balázs Rákossy, member

Members of the Supervisory Board:

Judit Gondos, chairman

Dr. Viktor Várpalotai, member

Gergely Földiák, member

The Company's auditor:

DIAMANT Könyvvizsgáló Kft.

1223 Budapest, Gyula vezér u. 72.

Responsible auditor:

Terézia Bárány Director