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GOVERNMENT DEBT MANAGEMENT AGENCY
PRIVATE COMPANY LIMITED BY SHARES

GOVERNMENT DEBT MANAGEMENT REPORT 2012

FOREWORD

The objective of this annual Government Debt Management Report of the Government Debt Management Agency Pte. Ltd. (ÁKK) is to inform investors and other stakeholders in the government securities market about the financing of the central government, to analyse the characteristics of the government debt and to describe the developments in the Hungarian government securities market in 2012.

2012 was specific year for public debt management, as ample demand in the domestic bond market and the extraordinary demand from retail investors made it possible to finance not only the net financing requirement and maturing domestic debt, but also most of the foreign currency debt redemptions from the domestic market. That resulted in a decline of the share of foreign currencies in the total public debt portfolio from 49 per cent to 41 per cent. It is also worth noting that the Hungarian public debt ratio declined in 2012 – a rare phenomenon in the European Union. Government debt yields and spreads also declined substantially, that should lower the cost of public debt in the coming years.

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

István Töröcskei
Chief Executive Officer

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GENERAL INFORMATION

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

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

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

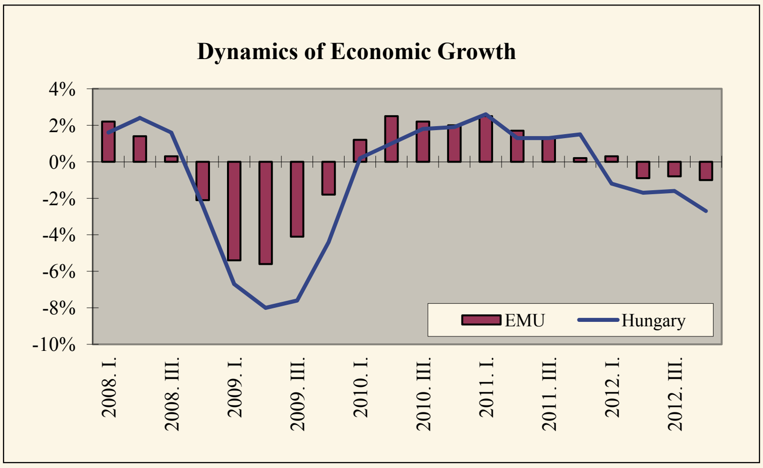
- Government bonds and retail government securities are recorded at nominal value.
- Discount treasury bills are recorded at the average sale price (at discount value), which is recalculated after every transaction involving the security concerned.
- Repo and reverse repo transactions actually increase or reduce outstanding government debt.
- Foreign currency debt is taken into account after swaps and is converted into HUF at the official exchange rate published by the National Bank of Hungary (NBH) at the end of the month or year in question.
- The debt 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 it is not a consolidated indicator (i.e. debt between various public sector subsystems is not netted).

The debt data published by ÁKK in accordance with Hungarian and international accounting standards differ from the debt data used by EUROSTAT (the European Union's institute of statistics), which is calculated according to different principles and is essentially the result of statistical calculations. Public debt data calculated in accordance with ESA '95 principles is jointly produced and published by the Hungarian Central Statistical Office (HCSO), the National Bank of Hungary (NBH) and the Ministry for National Economy, and is based only partly on information provided by ÁKK.

I. MACROECONOMIC DEVELOPMENTS IN 2012

During the first half of 2012 the global economic situation improved as a consequence of coordinated monetary easing of the central banks of the developed economies. At the same time the most important risk factors – high unemployment rate and fiscal deficit in the USA, economic slowdown in China, sovereign debt problems in the Eurozone – still lingered. In the middle of the year a significant part of the Greek government debt was written down and Chinese growth slowed, resulting in an increase of risk aversion. Global market sentiment improved significantly when Mario Draghi, governor of the European Central Bank announced that the ECB is ready to intervene in the Eurozone government securities market within its mandate. The central banks of several countries (including the UK, Japan, Switzerland and the USA) resorted to quantitative easing. By the end of the year Western European economies cooled down and mid-term prospects deteriorated. In December investor sentiment worsened due to the risk of the US "fiscal cliff" – automatic fiscal stabilisers entering into force in the USA.

Economic Growth



Source: HCSO, Eurostat

Having grown by 1.3% in 2010 and by 1.6% in 2011 the Hungarian economy shrunk by 1.7% decline in 2012 partly as a result of the growth problems in Western Europe and partly on domestic developments (domestic consumption dropped by 1.7%, investments declined by 3.8% and domestic use fell by 3.7%). Net exports on the other hand contributed significantly to economic growth as exports increased by 2.0% while imports stagnated, although the export sector's favourable effect vanished in the last quarter of the year as the dynamics of exports and imports became essentially the same.

Fiscal Policy

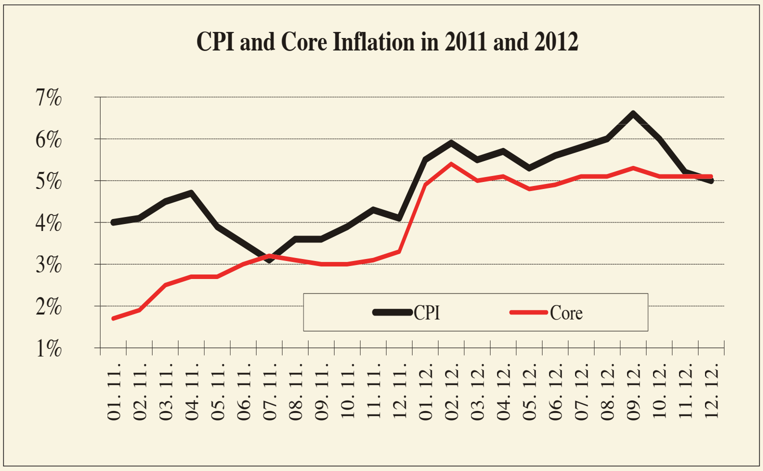
In 2012 the cash-flow based (GFS) general government deficit (excluding local governments) amounted to HUF 607.5 billion (equalling 2.1% of GDP for the year 2012) according to data compiled by the State Treasury. In 2012 the accrual based (ESA) general government deficit (including local governments) amounted to HUF 593.4 billion (equalling 2.1% of GDP for the year 2012) according to preliminary data. The financing need of the state declined slightly compared to the previous year.1

Financing Position of the Economy

The savings to GDP ratio of households improved slightly in 2012 reaching 4.8% compared to 4.6% in 2011. The net financing capacity of the corporate sector increased from 2.0% in 2011 to 2.7% in 2012 mainly as a result of falling investment activity. The economy of Hungary as a whole was a net lender towards the rest of the world in the amount of 5.1% of GDP. The current account posted a surplus of EUR 1.6 billion in 2012 equalling 1.6% of GDP.

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

Inflation

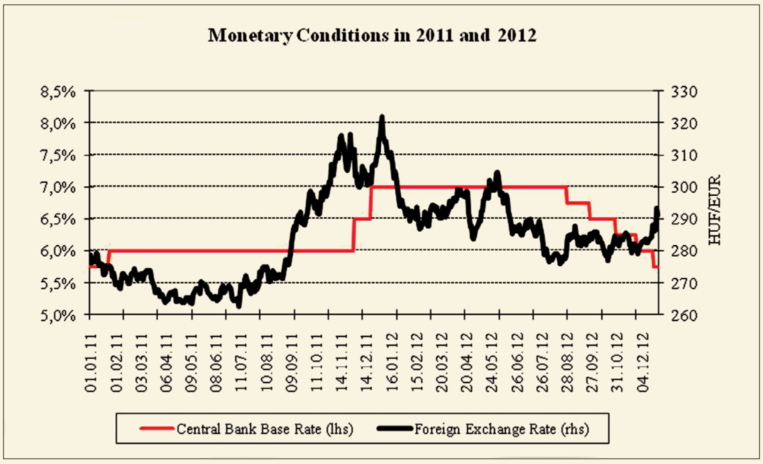


Source: HCSO

During 2012 inflation fluctuated between 5.0% and 6.6%. Tax changes (mainly excise duties and the 2 percentage point VAT hike) and high global food and energy prices pushed the inflation rate upwards, while weak local demand decreased the inflationary pressure at the same time. In the first quarter of the year the weakness of the forint contributed to the increase of price levels. After the spring of 2012 the strengthening of the forint and decreasing oil prices had a decreasing effect, but the weak expected harvest accelerated the inflation. In December 2012 inflation decreased to 5.0%, core inflation reached 4.9% and the constant tax rate index amounted to 3.2%. The yearly average inflation was 5.7% in 2012.

Monetary Conditions

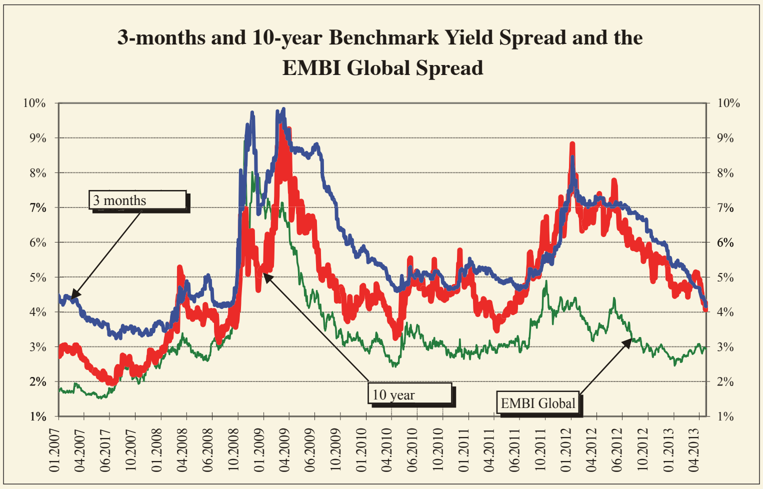
During 2012 the exchange rate of the forint strengthened by 6.4% from 311.1 HUF/EUR to 291.3 HUF/EUR. By the beginning of the year the exchange rate weakened temporarily above the rate of 320 HUF/EUR, but afterwards the rate strengthened below 290 HUF/EUR reflecting the improving investor confidence towards the country.



Source: NBH

Later in the year the global investor confidence worsened mainly due to increasing perceived risks concerning the sustainability of the government debt of several countries of the Euro zone periphery, weakening the forint as well. Worries concerning global growth prospects also weighed on the forint. On the other hand, the favourable stability indicators of the Hungarian economy and the commitment of the Hungarian Government to a strict fiscal policy strengthened the forint.

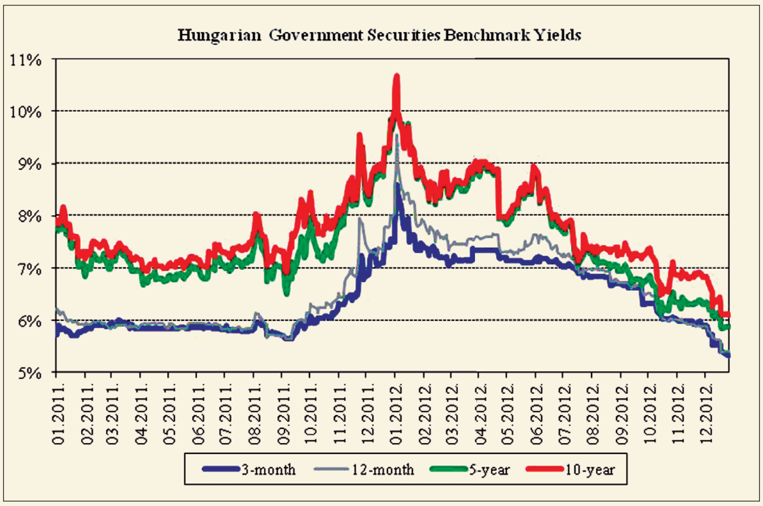
During the first half of the year the central bank kept the central bank base rate stable amidst a faltering investment environment, but it started to cut the interest rate gradually in August. As a result, the central bank base rate declined from 7% to 5.5% by the end of the year. Global liquidity supported the easing cycle. These monetary policy developments had an effect on government bond yields and spreads too.



Source: Bloomberg

Government Securities Market Developments

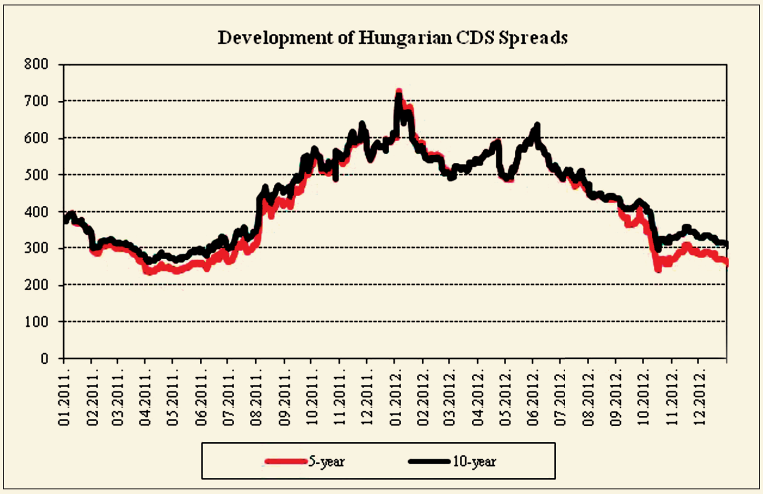
In January government securities yields increased reaching double-digit levels in the secondary market for a short period. After a substantial correction yields remained at a relatively high level in the first half of the year. In the second half of the year government bond yields plummeted sharply backed by market stabilization based on international and local developments and by increasing investor demand; the decline gained impetus after the central bank's rate-cutting cycle started. By the end of the year long-term yields stood around 6%, short-term yields were slightly below 5.5%.



Source: ÁKK

CDS Spreads

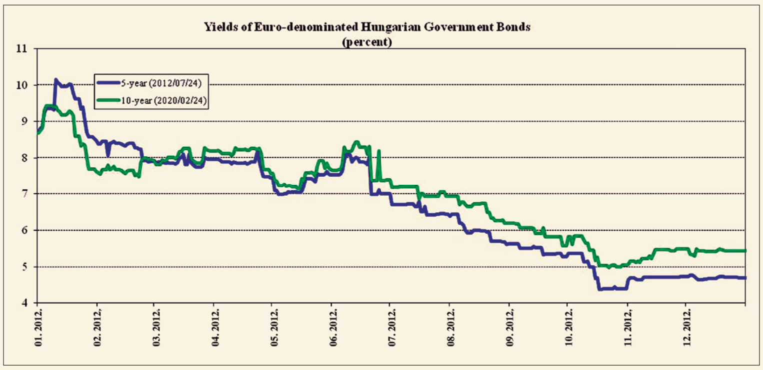
The 5 year CDS spread increased from 600 basis points to 730 basis points during the first days of 2012. By the end of January, the spread declined to below the level seen at the beginning of the year. In the second half of the year CDS spreads fell sharply and fluctuated between 250 and 300 basis points during the last months of the year, and the 5-year CDS spread stood around 270 basis points by the end of the year.



Source: Reuters

Yields of Foreign Currency Denominated Bonds

Besides CDS spreads the evolution of long-term yields in Western European markets played a significant role in the yield movements of the euro-denominated Hungarian government bonds.

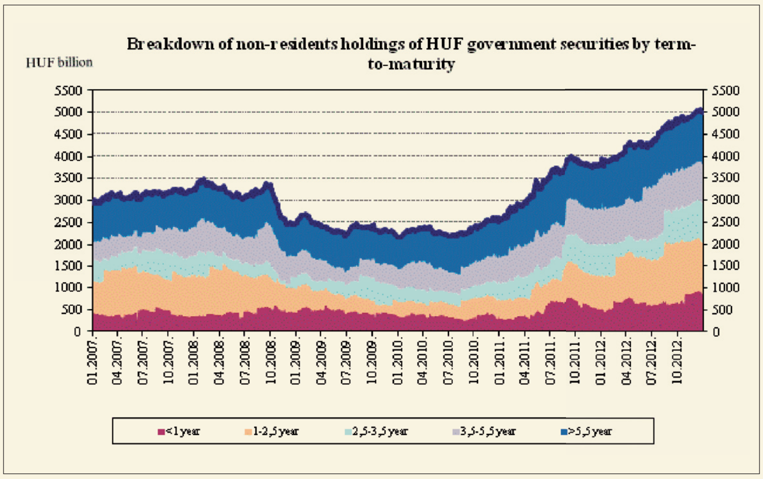


Source: Bloomberg

The yield of the euro-denominated Hungarian government bond maturing in July 2016 increased from 8.7% to 10.1% during the first few days of 2012, but retreated to around 8.7% by the end of January. Afterwards, foreign currency yields fluctuated around a high level driven by global and local factors, but from June 2012 they followed a declining trend until October. The yield of the euro-denominated Hungarian government bond maturing in July 2016 stood at 4.7% at the end of the year.

Government Securities Holdings of Foreign Investors

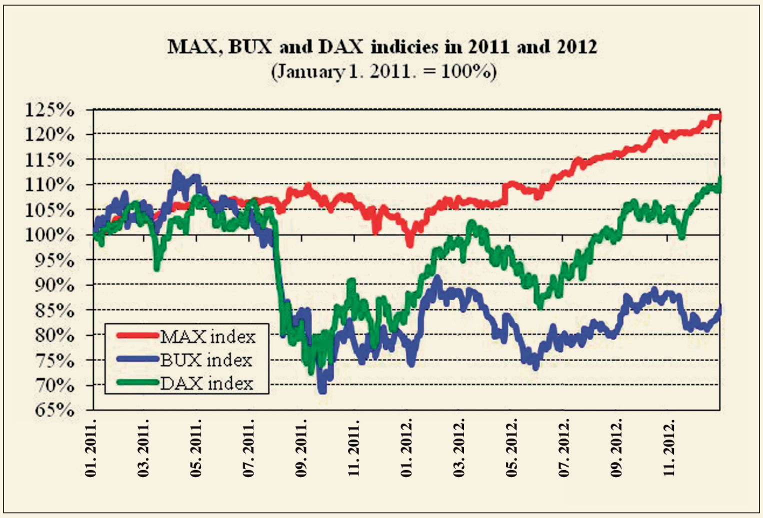
The volume of forint-denominated government securities held by non-residents had been increasing steadily since the middle of the year 2010 and this process carried on in 2012 as well. By the end of the year the non-resident holdings of forint denominated government securities amounted to HUF 5,009 billion up by HUF 1,212 billion from the end of the previous year (i.e. by more than 30%).



Source: KELER Zrt.

The share of foreign holdings of forint-denominated debt increased from 39% to 46%. Adding the foreign exchange denominated debt held by non-residents (including the EU-IMF financial assistance package) to this resulted in the total foreign holdings within the total debt ratio reaching 65%.

Equity Market



Source: ÁKK, Bloomberg

During the course of the year the main stock market index of the Budapest Stock Exchange, the BUX index fluctuated between 16,000 and 20,000 points. The index followed the global trends in most of the year, but by the end of the year the trends of the CEE region were driving primarily the Hungarian bourse. Regarding the whole year the BUX index posted a 7% increase.

II. DEBT MANAGEMENT STRATEGY IN 2012

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

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

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

The most important risk factors are as follows:

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

ÁKK has developed various benchmarks reflecting its strategic objectives based on an optimal portfolio model which consider risks and costs simultaneously. In order to filter out short-term effects, these benchmarks are monitored as 90-day moving averages. The benchmarks approved by the Minister for National Economy are also used to quantify strategic objectives and to set intermediate targets. During the course of 2012 the composition of the central government debt conformed to the benchmarks.

Public debt management benchmarks

Benchmarks	Tolerance band	End 2011	End 2012
1. Foreign currency debt ratio	25-50% FX	49.6%	40.6%
2. Foreign currency debt composition	95-105% EUR	99.6%	100.8%
3. Fixed coupon part of foreign currency debt	62.7-67.7%	64.7%	66.2%
4. Fixed coupon part of domestic debt	61-83%	70.5%	67.6%
5. Duration of domestic debt	2-3 years	2.58	2.49

Benchmark No. 6. is to maintain a secure level of funds on the Single Treasury Account (STA). For a detailed description of liquidity management in 2012 see Chapter VI.

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TRATEGIC PRINCIPLES

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

As regards liquidity, ÁKK aims to ensure that government securities have a sufficiently liquid secondary market. A liquid secondary market can be supported by the debt manager by two ways. The first measure is the continuous two-way price quotation by Primary dealers that reflects real market prices; the second is building-up sufficiently large volumes of government securities series (benchmarks). In order to achieve this latter goal, ÁKK reopens individual series – i.e. it issues additional bonds that are fully fungible with previously issued series. The targeted volume of bond series was around HUF 600-800 billion (approximately EUR 2-3 billion) in 2012, with greater volumes targeted for securities with a longer tenor (5 or 10 years). Secondary market operations were also enhanced by bond buy-back and bond exchange transactions by ÁKK.

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

III. THE FINANCING REQUIREMENTS IN 2012

THE COMPONENTS OF THE FINANCING REQUIREMENTS

The most important part of the net financing requirements is the deficit of the central government. The balance of the central government consists of the balances of three subsystems of government administration: the central budget, social security funds and extra-budgetary funds. ÁKK is responsible for financing the central government and maintaining its continuous liquidity, while local authorities 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 (privatisation revenues, transfers from the EU, special transfers to the NBH etc.). The gross financing requirement, in addition, also includes debt redemptions, the majority of which is contributed by short-term debt, which may be renewed several times a year. During recent years, cash-flow based financing requirements were as follows:

Borrowing requirements between 2008 and 2012

	2008	2009	2010	2011	2012
Central government balance*	-864.7	-739.9	-837.8	-1,718.4*	-620.1
Balance of the Social Security funds	-73.4	-151.0	-95.6	-83.3	-117.8
Balance of the extra-budgetary funds	28.0	-30.4	61.6	67.2	130.4
Net financing need of the central* government*	**-910.0**	**-921.3**	**-871.9**	**-1,734.4***	**-607.5**
Capital transfers to NBH	-2.8	0.0	0.0	-29.1	0.0
Privatisation revenues	3.1	1.1	30.1	36.7	0.0
Net EU transfers	29.2	35.7	-125.1	406.6	-238.8
Total net financing requirements*	**-880.5**	**-884.5**	**-966.9**	**-1,320.2***	**-846.3**
Short term debt redemptions	-2,262.3	-1,988.7	-2,048.6	-1,922.3	-1,808.4
Long term debt redemptions	-1,280.4	-2,349.4	-1,752.7	-2,500.6	-2,782.2
Gross financing requirements*	**-4,423.3**	**-5,222.6**	**-4,768.2**	**-5,743.2***	**-5,436.9**

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

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

THE NET FINANCING REQUIREMENT

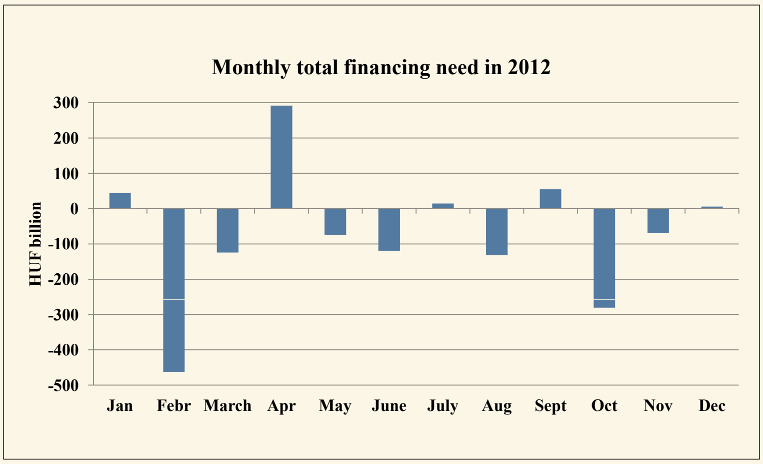
In 2012 the total cash-flow based deficit of the central government was HUF 607.5 billion (or 2.1 per cent of GDP according to preliminary data), while the total net financing requirement amounted to HUF 846.3 billion (or 3.0 per cent of GDP) due to net transfers to the EU. This difference, however, in itself had no adverse effect on the conditions of financing and on maintaining a securely high level of liquidity reserves thanks to the favourable market environment.

Borrowing requirements in 2012:

	Plan published in December 2011 (HUF billion)	Actual (HUF billion)	Actual/Plan (per cent)
Central government balance	-594.0	-620.1	104%
Balance of the Social Security funds	-35.0	-117.8	337%
Balance of the extra-budgetary funds	53.0	130.4	246%
Net financing need of the central government	**-576.0**	**-607.5**	**105%**
Capital transfers to NBH	0.0	0.0	-
Privatisation revenues	0.0	0.0	-
Net EU transfers	-98.0	-238.8	244%
Total net financing requirements	**-674.0**	**-846.3**	**126%**
Short term debt redemptions	-1,806.6	-1,808.4	100%
Long term debt redemptions	-2,139.3	-2,782.2	130%
Gross financing requirements	**-4,619.9**	**-5,436.9**	**118%**

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

The monthly financing needs showed a significant fluctuation in 2012 as well; large part of the financing requirement materialized in the first quarter of the year.



Redemptions

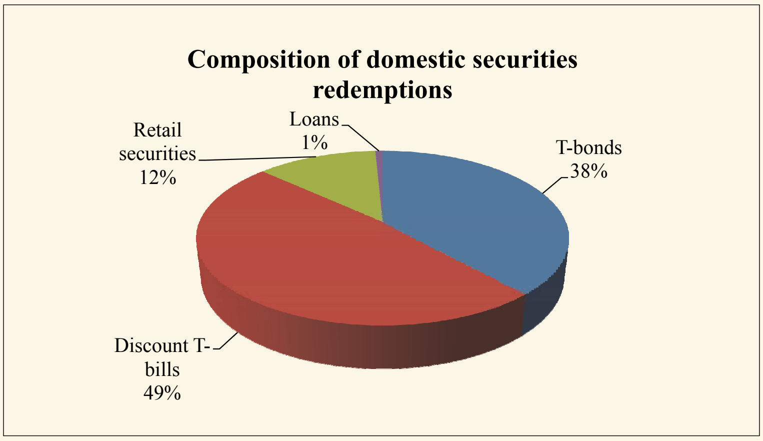
Redemptions in any given year are largely the function of debt financing operations in previous periods and of the sales of short-term instruments renewed within the year. Prepayments, buy-backs of bonds and the early repurchasing/redemption of retail securities and other securities in the Treasury network may also influence the final sum. As a result of these operations redemptions of domestic debt in 2012 were higher than planned. In the case of the foreign currency debt higher repayment was due to the weaker than projected exchange rate.

Government debt redemptions[2] **HUF billion**

	2011	2012 plan	2012 actual
Domestic debt	**3,158.5**	**2,538.4**	**3,176.2**
T-bonds	1,191.6	663.9	1,215.3
Discount T-bills	1,618.2	1,544.1	1,540.9
Retail securities	304.2	330.3	396.0
Loans	44.5	0.0	24.0
Foreign currency debt	**1,264.5**	**1,407.6**	**1,414.4**
Bonds	552.1	399.8	412.5
Loans	712.4	1,007.8	1,001.9
Total	**4,422.9**	**3,945.9**	**4,590.6**

Source: ÁKK

Total domestic debt redemptions exceeded the plan by HUF 638 billion, due to higher bond redemptions as a result of the bond buy back and exchange programs and increased retail debt maturities. Within the HUF debt portfolio, discount treasury bills contributed to 49 per cent of the total forint redemptions of HUF 3,176 billion, due to their renewals within the year.

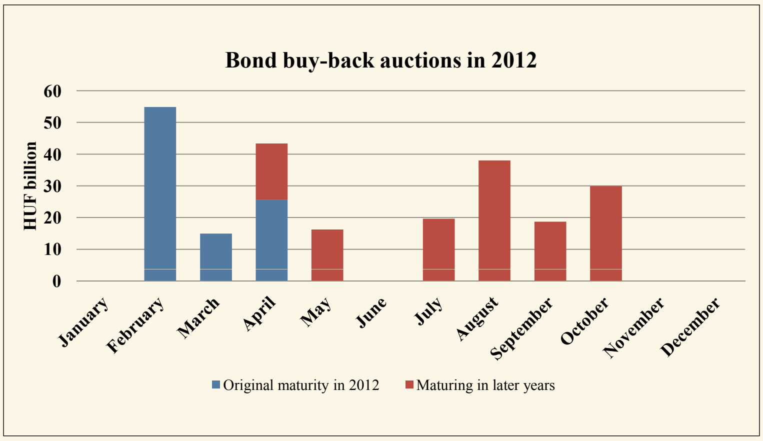


Source: ÁKK

Bond Buy-Backs

A large bond series maturing at a given time creates refinancing risk. This risk can be reduced by repurchasing a proportion of the bonds before maturity. ÁKK's normal financing plan therefore includes a regular bi-weekly bond buy-back program, the actual outcome of which depends on the quantity and quality of bids. In 2012 ÁKK bought back a total of HUF 236 billion bonds before their maturity on 25 occasions. 60 per cent of the repurchased bonds had an original maturity after 2012, i.e. these buy-backs also helped to smooth maturities from one year to another, since the original volume of bond maturities in 2012 was lower than in the next years.

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



ÁKK has been holding exchange (or switch) auctions that also decrease refinancing risk on a regular basis since 2009. In these switch auctions the investors can exchange their bonds with short remaining term-to-maturity into 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 2012 13 exchange auctions were held at which ÁKK exchanged a total of HUF 91 billion short-term bonds to long-term ones.

Foreign currency debt redemptions

In 2012 two foreign currency bonds – EUR 1 billion and JPY 45 billion respectively – matured and SDR 2.9 billion worth of loans were repaid to the IMF. Beside these items other smaller repayments took place in the case of IFI project financing loans.

The Pension Reform and Debt Reduction Fund

The Pension Reform and Debt Management Fund has the objective to liquidate the assets in its portfolio and may use the revenues exclusively for reducing government debt.

In 2012 HUF 31.2 billion worth of government securities were transferred by the Fund to the state and were immediately cancelled. (The above tables do not include these cancellations as they did not require any financing.)

Revenues from the sales of its assets and other sources enabled the Fund to transfer HUF 324 billion in cash to the state, which sum was used for bond buy-backs and the repayments of the loans from the IMF (see www.akk.hu for details).

IV. FINANCING

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

In 2012 debt management activities were significantly determined by the prevailing macroeconomic environment and the situation in the government securities market – in particular the effects of the international financial market crisis taking new turn in the EU. The means of financing were also influenced by the negotiations about new financial support from the EU/IMF that eventually ended without results. On the other hand, the programme that aimed at boosting the direct sales of retail government securities was an overwhelming success, and resulted in a large increase in domestic financing by households.

In 2012 the HUF denominated issuance amounted to HUF 4,889 billion (95%), while foreign currency issuance was HUF 233 billion (5%).

Gross debt issuance: **HUF billion**

	2011	2012 plan	2012 actual
Domestic debt	**3,649.8**	**3,151.8**	**4,888.8**
T-bonds	1,766.4	1,230.0	2,073.6
Discount T-bills	1,540.9	1,555.3	1,906.5
Retail securities	342.5	366.5	908.7
Loans	0.0	0.0	0.0
Foreign currency debt	**1,277.8**	**1,437.1**	**232.7**
Bonds	1,063.0	1,197.6	88.3
Loans	214.8	239.5	144.5
Total	**4,927.6**	**4,588.9**	**5,121.5**

Source: ÁKK

Net HUF denominated financing totalled HUF 1,713 billion, while net foreign currency financing amounted to HUF -1,812 billion, i.e. the total net issuance in 2012 was HUF 531 billion.

Net issuance: **HUF billion**

	2011	2012 plan	2012 actual
Domestic debt	**491.3**	**613.4**	**1,712.6**
T-bonds	574.8	566.1	858.3
Discount T-bills	-77.3	11.2	365.6
Retail securities	38.3	36.2	512.7
Loans	-44.5	0.0	-24.0
Foreign currency debt	**13.4**	**29.5**	**-1,181.7**
Bonds	511.0	797.8	-324.2
Loans	-497.6	-768.3	-857.5
Total	**504.7**	**643.0**	**530.9**

Source: ÁKK

Within the net HUF issuance, the role of long-term debt (bonds) and retail securities increased in line with the better than expected investor demand. The total net T-bond sales of HUF 859 billion actually exceeded the total net domestic and foreign currency issuance. Besides that, the sales of retail securities provided funding in a historically high amount of HUF 513 billion. The outstanding volume of discount Treasury bills increased by HUF 366 billion, also contributing to financing, whereas early repayments of HUF loans reduced net issuance by HUF 24 billion.

In 2012 the net foreign currency financing was negative, due to the lack of capital market issuance, even though the plans calculated with a small positive net issuance.

DOMESTIC FINANCING

Gross domestic issuance was eventually 55% higher than planned originally and its structure was also quite different from the plans. The issuance of all kinds of instruments increased; bond issuance was higher than planned by 69%, discount T-bills by 23% and retail instruments by 148%. HUF loans were not drawn down in 2012.

GOVERNMENT BONDS

Treasury bond auctions were held every two weeks, but to increase issuance flexibility the tenors were not set in advance, but announced a week before the auction, after consultations with Primary Dealers. Three bond series were sold at each bond auction. Usually the 3, 5 and 10-year tenors were offered, but the 10-year bond was replaced on 5 occasions with the 15-year fixed rate bond. The 5-year floating rate bond was offered 10 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 10 billion). Another way to react to changes in market demand was the use of the non-competitive top-up phase in the afternoon of the auctions when successful bidders at the auction could buy additionally up to 40 per cent of their winning bids at the average price of the auction.

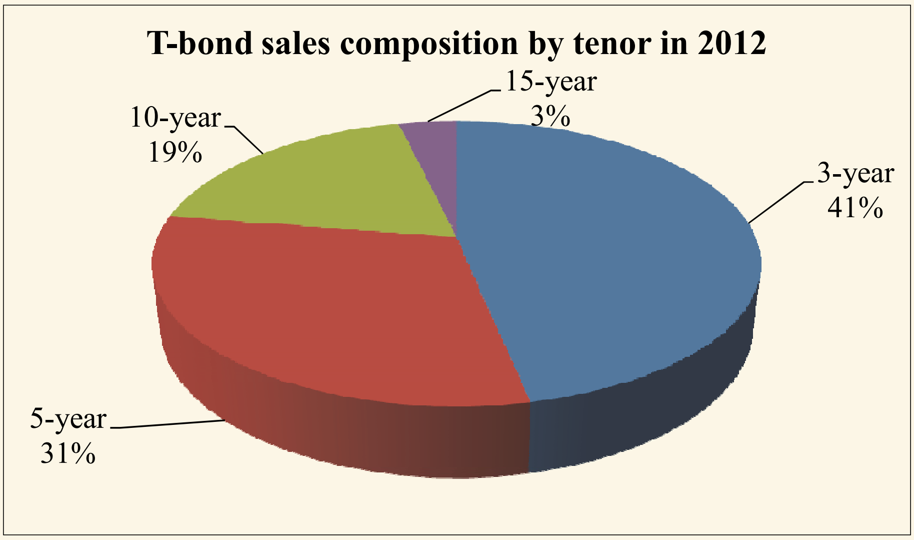
The bid-to-cover ratio at the bond auctions on average was 2.5. ÁKK sold a total of HUF 1,585 billion of bonds via auctions (including HUF 237 billion at non-competitive tenders). Total bond issuance – together with bond exchange auctions, the retail sales of the Hungarian State Treasury and secondary market operations – was HUF 2,074 billion, versus total bond maturities of HUF 1,215 billion, which resulted in a net issuance of HUF 859 billion (versus the planned HUF 566 billion).

On-the-run bond series in 2012 (HUF billion):

	Tenor	Number of auctions	Competitive sales in 2012	Non-competitive sales in 2012	Outstanding (end of 2012)
2014/D	3-year	3	40	9	655
2015/C	3-year	23	511	95	610
2015/B	5-year, FRN	10	70	16	202
2017/A	5-year	26	421	66	907
2022/A	10-year	21	257	41	533
2028/A	15-year	5	48	10	98

Source: ÁKK

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



Source: ÁKK

DISCOUNT TREASURY BILLS

The 3 and 12-month discount treasury bills are short-term instruments mainly used for liquidity management i.e. for smoothening fluctuations in liquidity caused by the varying financing requirements over the year. For this purpose ÁKK may also use so-called liquidity discount treasury bills of even shorter tenor (usually 6 weeks). In addition to liquidity management, the stock of discount treasury bills outstanding on a longer term may also serve as an alternative source of financing and can play a role in longer term financing.

In 2012 ÁKK sold discount treasury bills in a total of HUF 1,906 billion, more than in 2011. ÁKK originally planned a small net discount T-bill issuance of HUF 11 billion, however, since the foreign currency financing had to be substituted by domestic issuance, the outstanding T-bill stock actually increased by HUF 366 billion over the year, well above the plans.

RETAIL SECURITIES

One of the strategic objectives of ÁKK is to maintain a retail government securities issuance programme, which constitutes a third financing channel beside the local and the international wholesale markets. With growing savings of households it is advantageous for the Government to directly tap this source of funds as well.

Several years' experience shows that the demand for retail securities moves in an opposite direction as that of the wholesale instruments (bonds and discount T-bills). Issuing both types of instruments makes the financing more balanced and lowers the refinancing risk.

In spite of the fierce competition of banks for retail savings that was apparent in 2012 as well, the issuance of retail government securities showed a steep increase. ÁKK contributed to this success by an active marketing campaign, new products and competitive pricing for these instruments. The stock of the one-year interest bearing T-bill grew the most, by HUF 354 billion, while outstanding amount of other products like the 6 month interest bearing T-bill and the Treasury Savings Bills (securities available in the post office network) grew by HUF 10 billion and by HUF 58 billion respectively. The inflation-linked Premium Government Bond had a net sale of HUF 90 billion. The total retail debt stock grew by HUF 513 billion over the year, which compares to the HUF 36 billion planned, and contributed to a large extent to the year's successful financing from the domestic market.

FOREIGN CURRENCY FINANCING

In 2012 ÁKK, contrary to the plans, did not issue foreign currency bonds in the international capital markets. On the other hand, a new domestically issued foreign currency bond (the "Premium Euro Government Bond" was launched in November with a 3-year tenor and a floating rate coupon tied to the Eurozone inflation. The net sales of this bond reached HUF 88 billion in 2012. As a result of the lack of foreign capital market issuance, the net foreign currency issuance was negative; the foreign currency redemptions were financed by the increased domestic issuance and by funds from the Pension Reform and Debt Reduction Fund.

Foreign currency bond issued by Hungary in 2012:

Series	Currency	Date of issuance	Maturity	Tenor (years)	Coupon
2015/X	EUR	21.11.2012	21.12.2015	3	Floating rate

Source: ÁKK

In 2012 the government drew HUF 144 billion (EUR 509 million) in the form of project financing foreign currency loans from international financial organisations. The loans drawn from the European Investment Bank (EIB) and the Council of Europe Development Bank (CEB) were used, among others, to finance projects in infrastructure development and integration assistance.

V. THE GOVERNMENT DEBT IN 2012

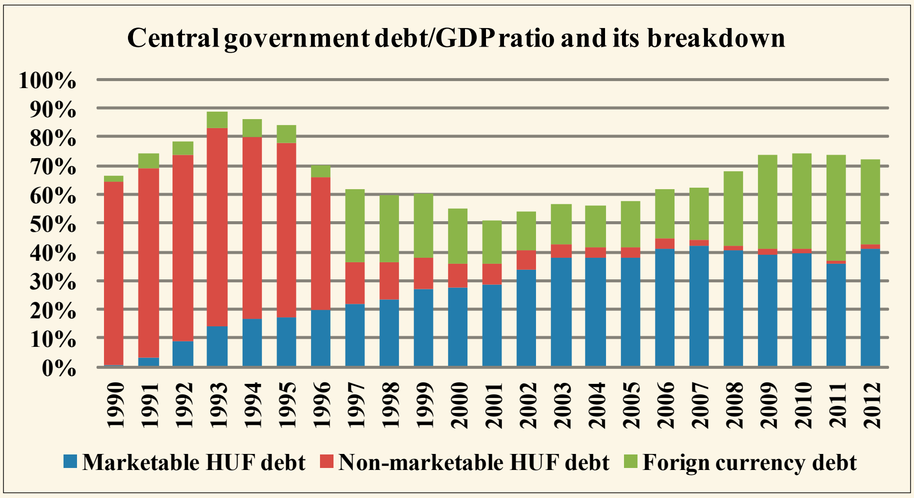
During 2012 the central government debt **decreased** by HUF 235 billion (or by 1.1 per cent) to HUF 20,720 billion. The size of the debt was influenced by several factors. The net issuance in itself increased the public debt by HUF 531 billion, although the net issuance was lower than the actual net borrowing requirement thanks to the debt repayments from the use of the funds from the Pension Reform and Debt Reduction Fund. The value of public debt decreased due to the appreciation of the forint against other currencies HUF 662 billion, transfer and cancellation of government securities held by the Pension Reform and Debt Reduction Fund through the Pension Fund (HUF 31 billion) and the declining stock of other obligations namely marked-to-market deposits (HUF 72 billion).

Central government debt — HUF billion

	2011		2012		Change
Domestic debt	**10,362.2**	**49.4%**	**12,042.4**	**58.1%**	**1,680.2**
Loans	590.8	2.8%	566.8	2.7%	-24.0
Government bonds	7,756.7	37.0%	8,582.5	41.4%	825.9
Discount T-bills	1,540.9	7.4%	1,906.5	9.2%	365.6
Retail securities	473.8	2.3%	986.6	4.8%	512.8
Foreign currency denominated debt	**10,170.4**	**48.5%**	**8,326.6**	**40.2%**	**-1,843.9**
Loans	4,458.1	21.3%	3,312.5	16.0%	-1,145.6
Bonds	5,712.3	27.3%	5,014.1	24.2%	-698.2
Total debt	**20,532.6**	**98.0%**	**20,369.0**	**98.3%**	**-163.6**
Other obligations	**422.9**	**2.0%**	**351.1**	**1.7%**	**-71.8**
Grand total debt	**20,955.5**	**100.0%**	**20,720.1**	**100.0%**	**-235.5**

Source: ÁKK

The debt of the central government compared to the GDP (debt ratio) that measures the stock of debt against the actual economic performance declined as well in 2012. According to preliminary data, the central government debt started to decrease already in 2011 to 75.1 per cent and in 2012 went further down to 73.3 per cent, which is a very favourable trend in the present international background.



Source: ÁKK

CHARACTERISTICS OF THE HUF DEBT PORTFOLIO

During 2012 the HUF-denominated debt that accounts for 58 per cent of the total debt increased by HUF 1,680 billion (16 per cent) to HUF 12,042 billion. The deficit and the increased net issuance of domestic debt in order to substitute the foreign currency funding significantly increased the stock of HUF debt.

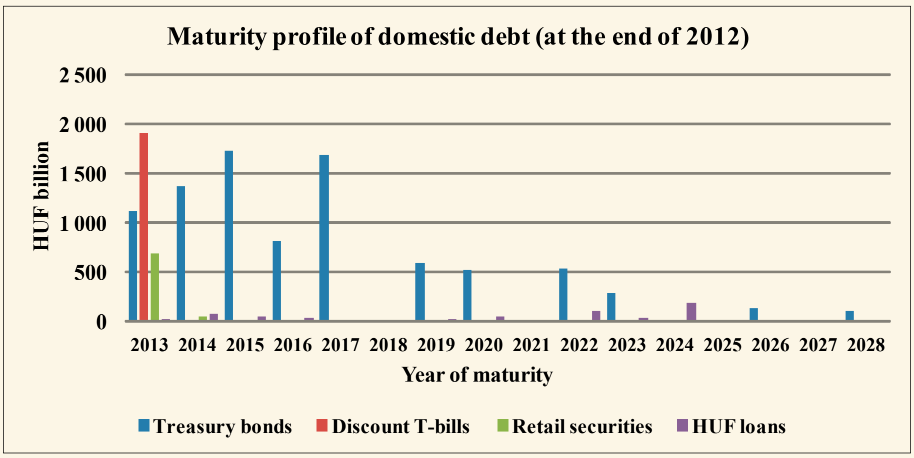
By the end of 2012 41 per cent of the entire debt was in the form of long-term HUF government bonds. The total domestic bond portfolio of HUF 8,583 billion consisted of 24 bond series, so the average size of a series was HUF 357 billion (ca. EUR 1.2 billion), a substantial increase from the previous year. Ten series had a volume in excess of HUF 500 billion (ca. EUR 1.7 billion), and the largest bond series reached HUF 907 billion (or EUR 3.0 billion).

The HUF 1,907 billion discount T-bill stock consisted of eighteen series. There were six larger series with an average volume of HUF 205 billion (or EUR 700 million).

In 2012 the portfolio of retail government securities increased to HUF 987 billion, up from HUF 474 billion at the end of the previous year. In terms of their share, the retail securities accounted for 8.2% of the total domestic debt in comparison to their 4 per cent share at the end of 2011.

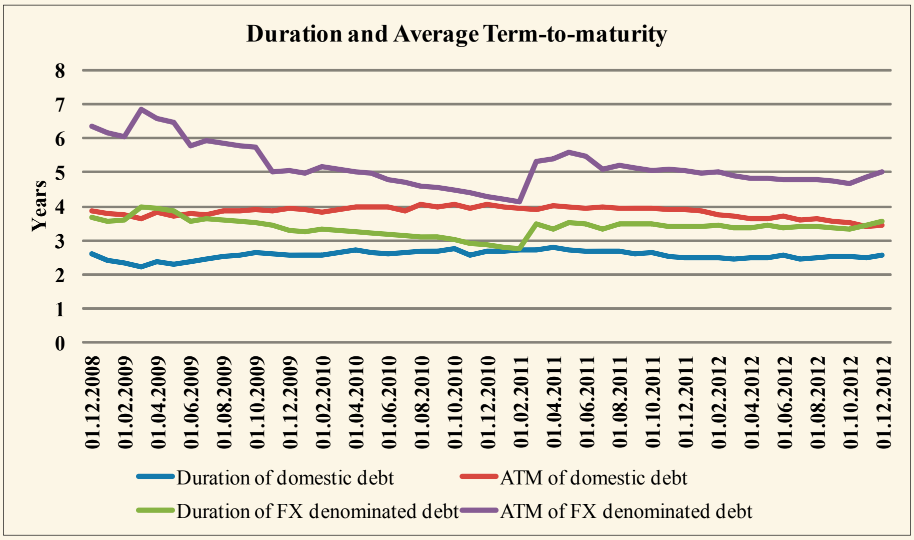
The non-marketable component of the HUF bond portfolio continued to decrease in amount and proportion in 2012 as well, as there are no new issuances of such government bonds and the existing portfolio matures continuously. The end-of-year volume of non-marketable government bonds was HUF 398 billion, which was only 1.9 per cent of the total debt. The volume of loans denominated in Hungarian forint decreased in 2012 by HUF 24 billion to HUF 567 as a result of redemptions.

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



Source: ÁKK

Due to the increased domestic bond issuance in 2012, the duration and average term-to-maturity characteristics of the domestic debt remained stable; the natural shortening of these measures of the debt was counterbalanced by the primary market operations (auctions, exchange auctions). The duration of the HUF denominated debt portfolio decreased from 2.58 years to 2.49 years in 2012. The average term-to-maturity decreased to 3.5 years.

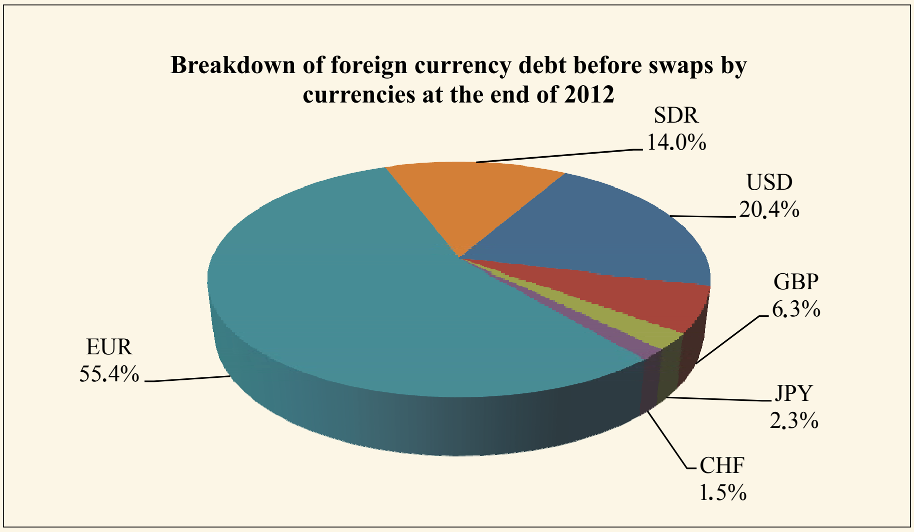


Source: ÁKK

CHARACTERISTICS OF THE FOREIGN CURRENCY DEBT PORTFOLIO

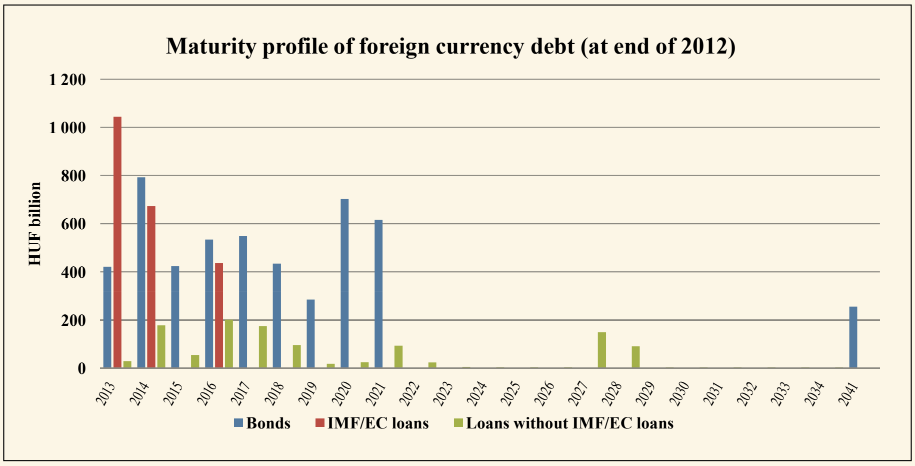
The gross foreign currency government debt decreased by HUF 1,844 billion in 2012, reaching HUF 8,327 billion (EUR 27 billion) by the end of the year. Accordingly, the share of foreign currency debt within the total gross government debt (excluding marked-to-market deposits) was 41 per cent at the end of 2012, a significant drop from the 49.6% share at the end of 2011. The decrease in the foreign currency debt was due the negative net issuance and the appreciation of the HUF against other currencies.

The volume of outstanding foreign currency bonds (after swaps) reached HUF 5,014 billion by the end of the year, significantly lower than at the end of 2011 (HUF 5,712 billion), as a result of two bond maturities and no new issuance. The original plan calculated with foreign currency bond issues to cover the maturing foreign currency bonds and IMF loans. On 31 December 2012 there were 20 series of foreign currency bonds outstanding, 9 of which had been issued in euro (including the domestic euro bond as well), four in US dollars, two in Swiss francs, three in Pound sterling and two in Japanese yen. In accordance with the strategy and benchmarks, all non-euro bonds have been converted into euro liabilities through swap transactions. Bonds accounted for 60% of the total foreign currency debt portfolio.



At the end of 2012 close to 100% of the foreign currency debt was denominated in euro (after swaps).
Source ÁKK

The foreign currency loan portfolio consisted of long-term project financing loans from international financing institutions (e.g. EIB and CEB), as well as loans from the IMF and the European Commission. As a result of large repayments to the IMF the share of loans within the total foreign currency debt declined from 44 to 40 per cent.



Source: ÁKK

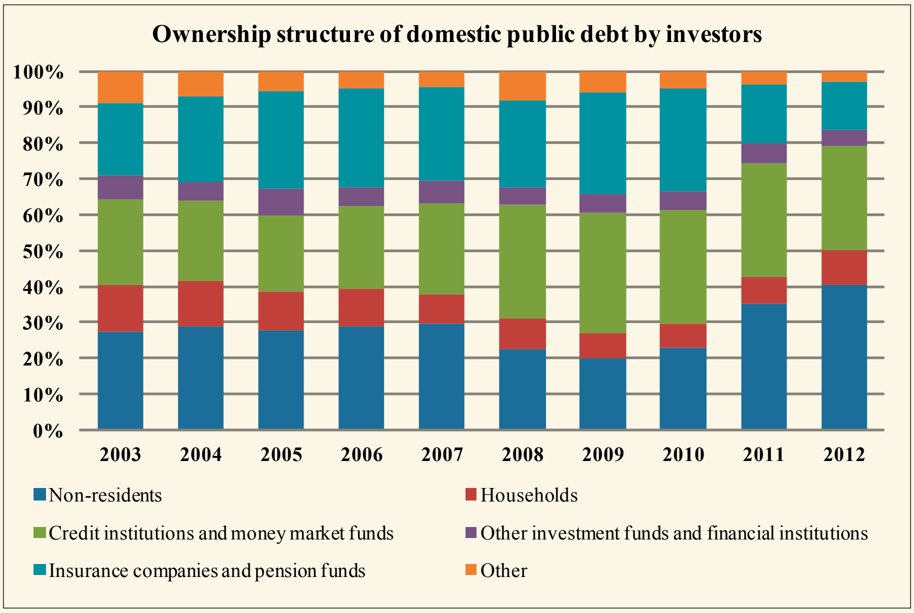
During 2012 the average life of the foreign currency portfolio lengthened as a result of the redemptions of the relatively short term IMF loan: ATM remained 5 years, while the duration increased by 0.1 years to 3.6 years.

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. Hungary has bilateral CSAs and in a few cases similar mark-to-market agreements supplementing the ISDA Master Agreement. Such deposits placed with ÁKK are non-financing funds and they are shown as part of the government debt among 'other obligations'. As of 31 December 2012 marked-to-market deposits placed with ÁKK totalled HUF 351 billion (EUR 1.2 billion), which was HUF 72 billion smaller than at the end of 2011.

The ownership structure of government debt

According to statistics published by the National Bank of Hungary, the following changes took place in the ownership structure of domestic government securities in 2012: since Q4 2010 non-resident investors have continued to increase their portfolio and now they are the biggest investors with a 40 per cent share in the local market up from 35 per cent a year before. Credit institutions constitute the second largest investor group with a declining 29 per cent share. Pension funds / insurance companies also had a decreasing share from 16 per cent to 14 per cent. Domestic retail investors, however, increased their share significantly from 7 per cent to 10 per cent and maintained their fourth place among the holders of government securities.



Source: NBH, KELER, ÁKK

In 2012 non-residents increased their share both in nominal and relative terms. Non-resident holdings of HUF denominated government securities grew by HUF 1,212 billion to HUF 5,009 billion. The duration of their holdings decreased by 0.1 year to 3.2 years, while the ATM of their holdings decreased by 0.2 years to 3.9 years in 2012. Even though their holdings of discount T-bills increased a somewhat, it is still not significant compared to their bond holdings. Thus it remains true that foreign investors hold primarily longer dated bonds, 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

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

Beside the STA, foreign currency deposits also serve as financing reserves. Such foreign currency deposits stemming from the drawn but unused part of the IMF loan facility amounted to EUR 1.5 billion at the end of 2012. Stand-by credit facilities with banks serve as further liquidity reserves, but in 2012 there were no withdrawals from these facilities.

In 2012 ÁKK used the following instruments to manage the end-of-day balance of the STA:

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

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

Sales of liquidity discount treasury bills took place relatively evenly throughout the year: ÁKK sold HUF 600 billion on 13 occasions in 2012 (down from HUF 650 billion in 2011).

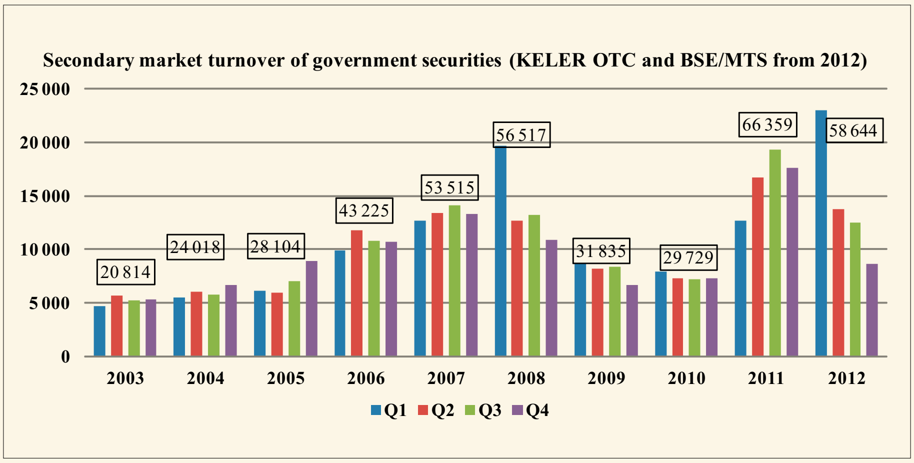
Liquidity repo transactions are ÁKK's main tool for fine-tuning the end-of-day balance of the Single Treasury Account. In 2012 the use of repo transactions decreased further to a total of HUF 5,177 billion concluded on 246 business days, down from HUF 5,597 billion in 2011. Liquidity management was effective, since the end-of-day STA balance was higher than the minimum target level on every day.

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

VII. THE SECONDARY MARKET OF HUNGARIAN GOVERNMENT SECURITIES

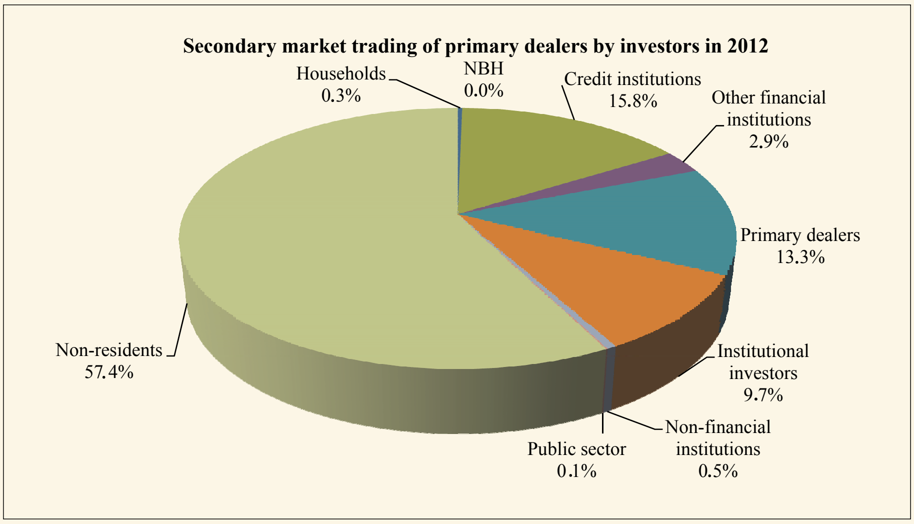
TRADING DATA

In 2012 MTS Hungary was introduced as the main electronic platform of trading government securities and Primary dealers fulfil their price quotation obligations on this platform. Primary dealers may also trade in the Budapest Stock Exchange's electronic trading system (MMTS), however more than 90% of all secondary trade is still executed in the over-the-counter (OTC) market. According to data from the Central Clearing House and Depository (Budapest) Ltd. (KELER), the total volume of OTC trading in government securities was HUF 57,979 billion in 2012 (about 5.5 times the size of the total outstanding marketable debt), out of which 74 per cent was in government bonds and 26 per cent in discount treasury bills. After the rapid decline in 2008-9, secondary market turnover reached its pre-crisis volume by 2011.



Source: KELER, BSE

The average size of deals with primary dealers (excluding retail transactions) was HUF 858 million, a 10 per cent decline in comparison with the previous year. Over the year, the 2014/C government bond with a 2 year remaining term-to-maturity had the largest turnover (HUF 6,294 billion), followed by the 5-year 2017/B and the 2014/D bond with a 2 year remaining term-to-maturity.



Source: Primary dealers, ÁKK

The most active Primary Dealer and the winner of the title 'Primary Dealer of the Year' for 2012 was Citibank Europe Plc.

VIII. THE INSTITUTIONAL FRAMEWORK FOR THE ISSUANCE OF GOVERNMENT SECURITIES

ÁKK sells government securities through intermediaries. In the domestic market, 84 per cent of HUF-denominated government securities were sold through the primary dealers in 2012, 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 2012 6 out of the 14 primary dealers were non-resident institutions.

PRIMARY DEALERS AT THE END OF 2012:

BNP Paribas SA
CIB Bank Zrt.
Citibank Europe Plc.
Deutsche Bank AG.
Erste Befektetési Zrt.
ING Bank N.V.
Goldman Sachs International
K&H Bank Zrt.
MKB Bank Zrt.
Magyar Takarékszövetkezeti Bank Zrt.
OTP Nyrt.
Raiffeisen Bank Zrt.
The Royal Bank of Scotland Plc
UniCredit Bank Hungary Zrt.

Only primary dealers may:

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

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

RETAIL DEBT PROGRAMMES

The State Treasury’s branch network provides direct access to government securities for retail investors. Managed by ÁKK, the 21 Treasury branch offices in Budapest and the county seats quote two-way prices for retail investors for publicly issued bonds, Premium Government Bonds, discount treasury bills and Interest Bearing Treasury Bills. Since December 2008 gov-

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

ernment securities may also be purchased and sold through the Hungarian State Treasury's internet-based securities service. As a part of the new government initiative to develop the retail debt program, the Treasury opened 2 new branch offices in the capital in 2012, which are included into the above number.
The Hungarian Post Office participates in the sale of two retail government securities. The 1 and 2-year Treasury Savings Bills are the only printed government securities, designed specifically for retail investors.

THE DEALERS OF FOREIGN CURRENCY BOND ISSUES

In 2012 Hungary did not issue international bonds in the international capital markets. On 20 November 2012, however, the sale of a new 3-year inflation linked domestic bond denominated in EUR ('Premium Euro Government Bond', P€MÁK) started. The bond is available for non-resident investors as well. Dealers may sell P€MÁKs on the basis of a separate agreement with KK.

DEALERS OF P€MÁK IN DECEMBER 2012:

Citibank Europe Plc.
Erste Befektetési Zrt.
ING Bank N.V.
Magyar Takarékszövetkezeti Bank Zrt.
OTP Nyrt.
Raiffeisen Bank Zrt.
and
the Hungarian State Treasury

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

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

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

According to the decision-making mechanism in place, the government debt management strategy, the annual financing plan and the benchmarks are approved by the Board of Directors, followed by approval from the Minister for National Economy.

THE FOUNDATION AND THE ORGANISATIONAL STRUCTURE OF ÁKK

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

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

THE RESPONSIBILITIES OF ÁKK

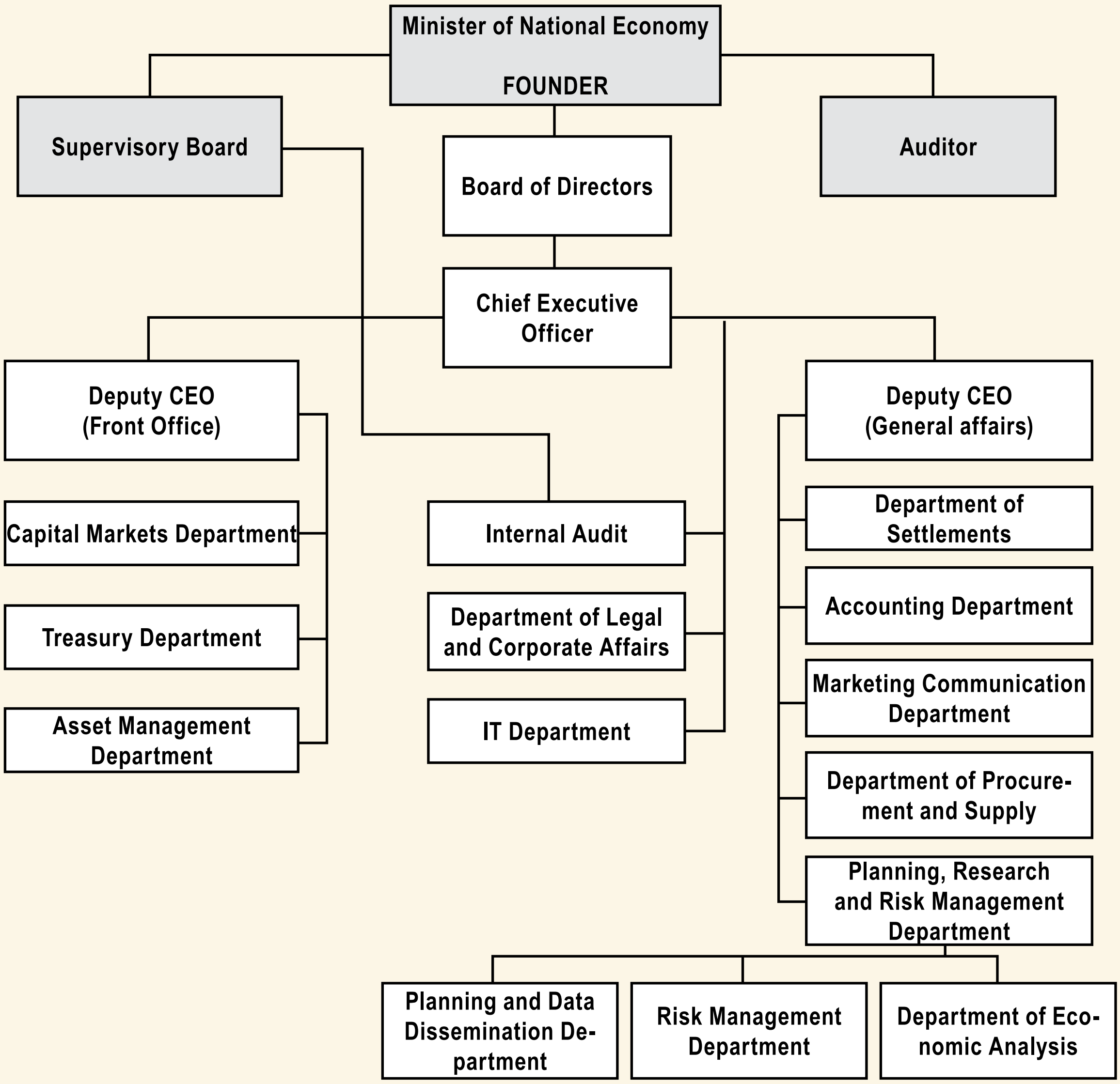
According to the provisions of Article 13 of the Act on the Economic Stability of Hungary, the responsibilities of ÁKK include the following major tasks:

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

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

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

Organisational structure of GDMA Ltd.



X. THE INFORMATION SERVICES OF ÁKK

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

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

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

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

The 'Publications, Statistics' menu provides access to the publications of ÁKK in electronic (pdf) format, along with an ample range of statistical data about, among others, government debt, the volumes of various types of instruments and securities trading statistics. The menu also contains the public analyses prepared by ÁKK. From 2011 a new 'Pension Reform Fund' menu was added, which provides information about the Pension Reform and Debt Reduction Fund managed by ÁKK.

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

ÁKK launched its special website for retail investors (www.allampapir.hu in Hungarian only) in an easy to understand, user-friendly form for small investors.

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 in electronic form on the website:

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

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

For further information, please contact

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

APPENDIX

1. The Central government gross debt as at 31.12.2012 (HUF million)

HUF denominated debt

Hungarian Government Bonds	Maturity	Coupon	Outstanding amount
2013/A	20. 03. 2013	Floating rate	76,666.97
2013/C	20. 12. 2013	Floating rate	127,928.00
2013/D	12. 02. 2013	6.75%	365,661.39
2013/E	24. 10. 2013	7.50%	473,040.45
2013/I	25. 01. 2013	Floating rate	32,389.03
2013/J	26. 08. 2013	Floating rate	24,514.53
2014/A	02. 05. 2014	Floating rate	29,576.06
2014/B	20. 12. 2014	Floating rate	16,612.00
2014/C	12. 02. 2014	5.50%	653,773.90
2014/D	22. 08. 2014	6.75%	654,735.39
2014/I	11. 08. 2014	Floating rate	3,754.79
2015/A	12. 02. 2015	8.00%	752,395.41
2015/B	22. 12. 2015	Floating rate	201,924.27
2015/C	24. 08. 2015	7.75%	609,588.72
2015/I	08. 12. 2015	Floating rate	11,466.30
2015/J	11. 01. 2015	Floating rate	98,979.41
2015/L	28. 11. 2015	Floating rate	2,914.42
2015/K	19. 03. 2015	Floating rate	39,817.68
2016/A	31. 12. 2016	Floating rate	13,360.00
2016/B	02. 01. 2016	Floating rate	9,000.00
2016/C	12. 02. 2016	5.50%	800,218.24
2016/I	28. 11. 2016	Floating rate	5,239.76
2017/A	24. 11. 2017	6.75%	907,320.13
2017/B	24. 02. 2017	6.75%	738,812.23
2017/I	05. 03. 2017	Floating rate	37,270.73
2019/A	24. 06. 2019	6.50%	583,069.23
2020/A	12. 11. 2020	7.50%	519,349.87
2022/A	24. 06. 2022	7.00%	533,451.73
2023/A	24. 11. 2023	6.00%	279,857.74
2026/A	28. 02. 2026	Floating rate	51,165.00
2026/B	24. 04. 2026	Floating rate	70,177.72
2026/C	24. 10. 2026	Floating rate	3,975.04
2028/A	22. 10. 2028	6.75%	98,247.75

Matured, but unclaimed government bonds	175.14
Total	**8,826,429.02**
Repos with government bonds (repos actually increase or decrease the total amount)	12,462.00
Discount Treasury Bills	**1,906,420.75**
Out of which matured, but unclaimed discount Treasury bills	3,701.06
Repos with discount Treasury bills (repos actually increase or decrease the total amount)	**49.22**
Interest Bearing Treasury Bills	**435,442.19**
Out of which matured, but unclaimed	966,65
Semi-annual Interest Bearing Treasury Bills	**10,381.36**
Out of which matured, but unclaimed	133,42
Treasury Savings Bills (1-year)	**220,066.47**
Treasury Savings Bills (2-year)	**64,230.83**
HUF loans	**566,825.47**
Matured, but unclaimed other retail government securities	112.00
Total HUF debt	**12,042,419.30**

Foreign currency	Outstanding amount (HUF Million)	Outstanding amount (EUR Million)
Loans granted by International Financial Institutions*	**3,183,058.78**	**10,927.46**
of Which: IMF and EC loans	**2,154,096.72**	**7,395.02**
Loans assumend from the market*	**129,409.00**	**444.26**

Government bonds

Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF Million)	Outstanding amount (EUR Million)
113	EUR	06. 02. 2013	10	4.50%	285,746.75	980.97
115	EUR	29. 01. 2014	10	4.50%	282,414.39	969.53
116	GBP	06. 05. 2014	10	5.50%	177,685.40	609.99
120	USD	03. 02. 2015	10	4.75%	331,395.00	1,137.68
121	EUR	24. 02. 2020	15	3.88%	288,377.10	990.00
122	GBP	09. 05. 2017	12	5.00%	177,695.00	610.03
126	EUR	18. 07. 2016	10.5	3.50%	280,512.27	963.00
127	JPY	18. 03. 2013	7	1.67%	128,480.00	441.07
128	GBP	30. 03. 2016	10	5.00%	177,695.00	610.03
129	EUR	04. 07. 2017	10	4.375%	289,833.55	995.00
130	JPY	26. 10. 2017	10	2.11%	64,240.00	220.54
131	CHF	21. 05. 2013	5	3.50%	36,159.00	124.13
132	CHF	20. 05. 2016	8	4.00%	48,212.00	165.51
133	EUR	11. 06. 2018	10	5.75%	434,505.06	1,491.66
134	EUR	28. 07. 2014	5	6.75%	290,360.49	996.81
135	USD	29. 01. 2020	10	6.25%	441,860.00	1,516.91
136	USD	29. 03. 2021	10	6.375%	662,790.00	2,275.36
137	USD	29. 03. 2041	30	7.625%	276,162.50	948.07
138	EUR	11. 01. 2019	7	6.00%	284,590.33	977.00
Total					**4,958,713.85**	**17,023.29**
Cross-currency swaps					**-34,548.72**	

Prémium Euro Hungarian Government Bond

Code	Currency	Maturity date	Maturity (years)	Coupon	Outstanding amount (HUF Million)	Outstanding amount (EUR Million)
2015/X	EUR	21. 12. 2015.	3	Floaing rate	89,932.70	308.74
Total					**89,932.70**	**308.74**

Kingdom of Hungary 1924 bond issue	**0.64**
Total foreign currenc debt	**8,326,566.25**
Total central government debt	**20,368,985.55**
Other obligations of ÁKK (marked-to-market deposits placed at ÁKK)	351,071.27
Grand total	**20,720,056.82**

**With swaps.*

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

Foreign currency denominated debt

Date of change	Moody's	Standard and Poor's	Fitch Ratings
20. 04. 1992	-	BB+	-
27. 12. 1993	Ba1	BB+	-
25. 04. 1996	Ba1	BB+	BBB-
28. 10. 1996	Ba1	BBB-	BBB-
19. 12. 1996	Baa3	BBB-	BBB-
24. 06. 1997	Baa3	BBB-	BBB
08. 05. 1998	Baa2	BBB-	BBB
11. 12. 1998	Baa2	BBB	BBB
25. 06. 1999	Baa1	BBB	BBB
29. 10. 1999	Baa1	BBB	BBB+
02. 02. 2000	Baa1	BBB+	BBB+
14. 11. 2000	A3	BBB+	BBB+
29. 11. 2000	A3	BBB+	A-
19. 12. 2000	A3	A-	A-
12. 11. 2002	A1	A-	A-
06. 12. 2005	A1	A-	BBB+
22. 01. 2006	A1	A-	BBB+
26. 01. 2006	A1	A-	BBB+
15. 06. 2006	A1	BBB+	BBB+
22. 12. 2006	A2	BBB+	BBB+
05. 11. 2007	A2	BBB+	BBB+
17. 03. 2008	A2	BBB+	BBB+
17. 10. 2008	A2	BBB+	BBB+
07. 11. 2008	A3	BBB+	BBB+
10. 11. 2008	A3	BBB+	BBB
17. 11. 2008	A3	BBB	BBB
02. 03. 2009	A3	BBB	BBB
30. 03. 2009	A3	BBB-	BBB
31. 03. 2009	Baa1	BBB-	BBB
02. 10. 2009	Baa1	BBB-	BBB
23. 07. 2010	Baa1	BBB-	BBB
06. 12. 2010	Baa3	BBB-	BBB
23. 12. 2010	Baa3	BBB-	BBB-
06. 06. 2011	Baa3	BBB-	BBB-
11. 11. 2011	Baa3	BBB-	BBB-
24. 11. 2011	Ba1	BBB-	BBB-
21. 12. 2011	Ba1	BB+	BBB-
06. 01. 2012	Ba1	BB+	BB+
23. 11. 2012	Ba1	BB	BB+
20. 12. 2012	Ba1	BB	BB+

Moody's assigned a 'negative' rating outlook, while Fitch Ratings and Standard and Poor's assigned a 'stable' rating outlook to the long-term foreign currency debt of Hungary at the end of 2012

HUF denominated debt

Date of change	Moody's	Standard and Poor's	Fitch Ratings
25. 04. 1996	-	-	BBB+
28. 10. 1996	-	A-	BBB+
24. 06. 1997	-	A-	A-
22. 06. 1998	A1	A-	A-
02. 07. 1998	A1	A-	A
11. 12. 1998	A1	A	A
29. 11. 2000	A1	A	A+
19. 12. 2000	A1	A+	A+
19. 11. 2002	A1	A	A+
12. 01. 2005	A1	A	A
27. 05. 2005	A1	A-	A
06. 12. 2005	A1	A-	A-
22. 01. 2006	A1	A-	A-
26. 01. 2006	A1	A-	A-
15. 06. 2006	A1	BBB+	A-
22. 12. 2006	A2	BBB+	A-
05. 11. 2007	A2	BBB+	A-
17. 03. 2008	A2	BBB+	A-
17. 10. 2008	A2	BBB+	A-
07. 11. 2008	A3	BBB+	A-
10. 11. 2008	A3	BBB+	BBB+
17. 11. 2008	A3	BBB	BBB+
02. 03. 2009	A3	BBB	BBB+
30. 03. 2009	A3	BBB-	BBB+
31. 03. 2009	Baa1	BBB-	BBB+
02. 10. 2009	Baa1	BBB-	BBB+
23. 07. 2010	Baa1	BBB-	BBB+
06. 12. 2010	Baa3	BBB-	BBB+
23. 12. 2010	Baa3	BBB-	BBB
06. 06. 2011	Baa3	BBB-	BBB
11. 11. 2011	Baa3	BBB-	BBB
24. 11. 2011	Ba1	BBB-	BBB
21. 12. 2011	Ba1	BB+	BBB
06. 01. 2012	Ba1	BB+	BBB-
23. 11. 2012	Ba1	BB	BBB-
20. 12. 2012	Ba1	BB	BBB-

Moody's assigned a 'negative' rating outlook, while Fitch Ratings and Standard and Poor's assigned a 'stable' rating outlook to the long-term domestic currency debt of Hungary at the end of 2012

3. THE ADDRESSES OF PRIMARY DEALERS

Primary dealer	Address
BNP Paribas SA	Budapest, H-1051 Széchenyi tér 7-8.
CIB Bank Zrt.	Budapest, H-1027 Medve utca 4-14.
Citibank Europe Plc., Hungarian Branch Office	Budapest, H-1054 Szabadság tér 7.
Deutsche Bank AG	Budapest, H-1054 Hold u. 27.
ERSTE Befektetési Zrt.	Budapest, H-1138 Népfürdő u. 24-26.
ING Bank N.V.	Budapest, H-1068 Dózsa György út 84/b
Goldman Sachs International	133 Fleet Street London EC4A 2BB
K&H Bank Zrt.	Budapest, H-1052 Vigadó tér 1.
MKB Bank Zrt.	Budapest, H-1056 Váci u. 38.
Magyar Takarékszövetkezeti Bank Zrt.	Budapest, H-1122 Pethényi köz 10.
Nomura International Plc	One Angel Lane, London EC4R 3AB
OTP Bank Nyrt.	Budapest, H-1876 Nádor u. 16.
Raiffeisen Bank Zrt.	Budapest, H-1054 Akadémia u. 6.
The Royal Bank of Scotland Plc	135 Bishopsgate, London EC2M 3UR
UniCredit Bank Hungary Zrt.	Budapest, H-1054 Szabadság tér 5-6.

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

ACT NO. 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,

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

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

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

(...)

CHAPTER III
THE GOVERNMENT DEBT MANAGEMENT AGENCY

4. Legal status of the Government Debt Management Agency

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

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

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

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

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

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

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

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

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

b) other revenues.

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

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

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

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

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

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

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

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

e) organises the secondary market of government securities,

f) executes dealing on own account on the secondary market of government securities, concludes security lending, repo and reverse repo transactions, concludes prompt, forward, hedge, swap and derivative transactions, and executes custodial and deposit management tasks,
g) analyses the tendencies of the government debt service falling under point a) and the government securities market,
h) participates in the calculation of the government debt, provides information on developments of government debt of the central subsystem of public finances arising out of debt transactions falling under point a) b) e) and g) of paragraph (1) of Section 3, and on the tendencies in the government securities market,
i) opines the terms and conditions of loans and bonds secured by individual government suretyship or guarantee,
j) executes credit and deposit operations,
k) participates in performing duties related to borrowing loans and credits and issuance of debt securities guaranteed by government suretyship or guarantee,

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

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

(4) In addition to its duties specified in paragraph (1), GDMA Pte. Ltd:
a) upon authorisation by a separate law may organize issuance of debt securities secured by government suretyship or government guarantee, or may fulfil advisory tasks related thereto,
b) may participate in performing duties – advice related to business strategy also implied – related to borrowing loans and credits, or issuance of debt securities by the state, municipality and business organizations owned thereby through majority ownership, for a remuneration to such extent as determined in paragraph (2),
c) may participate in the management of the free cash funds of the State Deposit Insurance Fund, and performing duties – advice related to business strategy also implied - related to borrowing loans and credits, or issuance of debt securities of such Fund,
d) may participate in management and sale of the assets of the Pension Reform and Debt Reduction Fund,
e) may participate in the management of cash funds of the Investor Protection Fund.

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

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

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

(...)

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

I. BALANCE SHEET

data in HUF thousand

	Assets	**2011**	**2012**
	A) Fixed assets	**73,623**	**73,564**
I	Intangible assets	16,822	14,903
II	Tangible assets	39,069	43,617
III	Invested financial assets	17,732	15,044
	B) Current assets	**412,429**	**325,314**
I	Inventories	0	0
II	Receivables	5,571	15,497
III	Securities	0	0
IV	Cash and cash equivalents	406,858	309,817
	C) Accrued and deferred assets	**26,614**	**88,632**
Assets in total		**512,666**	**487,510**

data in HUF thousand

	Liabilities	**2011**	**2012**
	D) Capital and reserves	**354,914**	**354,914**
I	Subscribed capital	300,000	300,000
IV	Profit reserve	54,914	54,914
VII	Balance-sheet profit or loss	0	0
	E) Provisions	**0**	**0**
	F) Liabilities	**132,444**	**112,015**
I	Subordinated liabilities	0	0
II	Long-term liabilities	0	0
III	Short-term liabilities	132,444	112,015
	G) Accrued and deferred liabilities	**25,308**	**20,581**
Liabilities in total		**512,666**	**487,510**

Budapest, 29 May 2013

István Töröcskei
CEO

II. PROFIT AND LOSS ACCOUNT

data in HUF thousand

	Liabilities	**2011**	**2012**
I	Net sales revenue	958,209	1,011,570
III	Other revenue	102,732	156,669
IV	Material expenses	331,106	420,237
V	Personnel expenses	645,701	703,554
VI	Depreciation and amortisation	33,279	29,283
VII	Other expenses	4,053	5,804
A	**Operating profit or loss**	**30,880**	**9,361**
B	**PROFIT OR LOSS FROM FINANCIAL TRANSACTIONS**	**28,335**	**23,764**
C	**PROFIT OR LOSS ON ORDINARY ACTIVITIES**	**59,215**	**33,125**
D	**EXTRAORDINARY PROFIT OR LOSS**	**0**	**0**
E	**PROFIT OR LOSS BEFORE TAXATION**	**59,215**	**33,125**
XII	Tax payable	6,346	3,322
F	**PROFIT OR LOSS AFTER TAXATION**	**52,869**	**29,803**
23	Approved dividends	52,869	29,803
G	**BALANCE-SHEET PROFIT OR LOSS**	**0**	**0**

Budapest, 29 May 2013

István Töröcskei
CEO

6. SENIOR OFFICIALS OF ÁKK ON 31 DECEMBER OF 2012

Members of the Board of Directors:

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

Members of the Supervisory Board:

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

The Company's auditor:

KPMG Hungária Kft.
Budapest, 1139 Váci út 99.

Responsible auditor:

Gábor Agócs Audit Director