



HUNGARIAN WATCH

Winter 2014



Hungarian Watch Winter 2014

Editor: Endre Várady

Publisher: János Tamás Varga, VJT & Partners Law Firm

1126 Budapest

Kernstok Károly tér 8.

Hungary

T: +36 1 501 9900

F: +36 1 501 9901

E: office@vjt-partners.com

Hungarian Watch is a quarter yearly issued brochure. It contains comprehensive, up-to-date information about Hungary, focusing on breaking news in the fields of law, economics, business and other situations which could have a major impact on the course of Hungarian events.

Hungarian Watch is primarily prepared for those who are thinking about Hungary from an investment point of view. The investment perspective runs through this newsletter by leading the reader through the actual Hungarian business climate including current business and investment opportunities.

We hope that Hungarian Watch will keep you regularly informed on relevant Hungarian news, enabling you to know how and when to seize a business opportunity before it vanishes.

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Summary



The Government is willing to take over 6-7 major utility service providers

Turbulent times in the energy sector

*The Hungarian retail energy sector is still in trouble. After the hectic summer the Government continued with its price cut policy which resulted in a total reduction of 20% of energy costs for retail consumers. Utility service providers complain that they have come to their financial wall. Prime Minister Viktor Orban said that the Government is currently in talks with 6-7 major utility service providers willing to sell their Hungarian operations to the Hungarian state. **Read more...***



Banking sector may still face consolidation

Raiffeisen and MKB plan to exit the Hungarian banking market

*The recent market events evidence that the long promised consolidation of the Hungarian banking industry is closer than ever. Bayern LB, the parent bank of MKB announced that it will split MKB in a way that will increase its chance of being sold. Raiffeisen is currently considering some purchase offers in order to exit the market. On the other hand, one of the few profitable banks, OTP announced again that it would grab any opportunity for growth. Taking all into account the next couple of months may bring important changes to the Hungarian banking industry. **Read more...***



4G mobile spectrum auction to be held in Hungary soon

Frequency rights for sale within the 800, 900, 1800, 2600 MHz and 26 GHz spectrum

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The largest energy deal in Central Europe and the Balkans

The Hungarian blue-chip energy company, MOL, may sell its stake in the Croatian INA

*On 4 October 2013, the Hungarian prime minister, Viktor Orban announced in his regular Friday morning radio speech that the Hungarian state, as a major shareholder of MOL gave instructions to the board of directors to make preparations for the sale of its stake in its Croatian partner INA. The sale of INA's share would raise important questions regarding the future perspective of the regional oil industry. Will the sale become a reality? Who could be the potential buyer? **Read more...***

Hungarian pharmacy industry still booming

Strong appeal for investors to buy Hungarian pharmaceutical stocks

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Hungary's economic forecast for 2014

Stable economic growth in 2014

*The Central Bank of Hungary expressed its strong financial outlook that the next year will be a promising year in Hungary. It predicted 7.4% increase of investment growth, historic low level of interest rates, moderate GDP growth, low inflation rate and the deficit of 2.5% of the GDP which is still below the 3% of GDP reference value to stay beyond the excessive deficit procedure. It seems that the Hungarian stable economic growth will continue in 2014. **Read more...***



A new financial watchdog

Merger of the Central Bank of Hungary and the Hungarian Financial Supervisory Authority

*The Hungarian Parliament has recently decided on the full merger of the Central Bank of Hungary and the Hungarian Financial Supervisory Authority. Both the Central Bank of Hungary and the European Central Bank welcomed the merger. They believe that the integration has compelling benefits for the whole Hungarian financial system. **Read more...***



No barriers for cross-border company transformation

The Supreme Court decision may result in a more investor-friendly application of Hungarian Law

*According to the ruling of the Supreme Court cross-border transformation cannot be banned by national law. The ruling set a Hungarian precedent by approving cross-border company transformation in respect of companies who are registered in other Member States and want to move their seat and business to Hungary. **Read more...***



The Government is willing to take over 6-7 major utility service providers

Turbulent times in the energy sector

Key players:

GDF SUEZ,
RWE,
E.ON,
EDF,
ENI

The Hungarian retail energy sector is still in trouble. After the hectic summer the Government continued with its price cut policy which resulted in a total reduction of 20% of energy costs for retail consumers. Utility service providers complain that they have come to their financial wall. Prime Minister Viktor Orban said that the Government is currently in talks with 6-7 major utility service providers willing to sell their Hungarian operations to the Hungarian state.



In our previous edition, we reported that the summer was a challenging period for the Hungarian retail energy sector. The Government was extremely determined to enforce its 10% price cut in respect of regulated prices for households in the field of electricity, gas and district heating sector. In order to efficiently ensure the enforcement of the price cuts

a new bill has been passed banning utility service providers to pass on their extra burdens to consumers. As the result of these measures, some energy firms have already in summer expressed their willingness to sell their unprofitable Hungarian retail units to the Hungarian state.

Banning utility
service providers to
pass on their extra
burden to consumers

After this hectic summer the Government has been resolved to continue with its price cut policy. The second price cut of 11.1% implemented as of 1 November 2013 together with the previous 10% price cut have resulted in a total reduction of 20% of energy costs to retail consumers.

The Government argues that the price cut is inevitable as utility costs in Hungary present disproportionately high figure in the aggregate household expenses, not seen in other European countries. Indeed, according to the data of the Hungarian Central Statistic Office, 20% of the average Hungarian household budget went for energy bills in 2012 (in comparison to Germany where energy bills compose about 5% of the average household budget). Supporters of this price cut policy also add that another energy poor country in the EU, namely Great Britain, also follows a similar model to deal efficiently with high utility costs.

On the other hand, utility service providers complain that the 20% cut is unbearable for them, as they had come to their financial wall already after the first cut. Eric Depluet, the CEO of E.ON notes that utility service providers can operate unprofitably from their reserves for a couple of years, but they need clear vision in order to be sure that it is worth staying in the Hungarian market.

The Government also announced that in order to make utility costs bearable for households utility service providers should be converted into non-profit entities. Most market analysts agree that non-profit operation could be sustainable only if utility service providers are state owned. Therefore they believe that the aim of the Government is to return natural monopolies to the public sector.

Utility service providers should be converted into non-profit entities.

After these speculations Prime Minister Viktor Orban announced that the Government is currently in talks with 6-7 major utility service providers willing to sell their Hungarian operations to the Hungarian state. Allegedly negotiations were initiated by the major players of the energy market. The names of the companies having initiated negotiations for a potential sale are not public, but the press speculates that amongst others RWE, EDF and ENI were at the negotiation table.

The Government is in talks with 6-7 major utility service providers

Analysts point out that the recent events evidence that the parties have been preparing to close the transactions:

Parties have been preparing to close the transactions

- *The proposal of a bill was submitted to the Hungarian Parliament stating that transactions of a national strategic significance shall not be investigated by the Competition Authority. Therefore, acquisitions of utility service providers by state owned companies will be not hindered by the competition authority in the course of its competition clearance procedure.*
- *The proposal of a bill regulating the non-profit retail energy sector is also expected to be submitted to the Parliament in the spring session.*
- *Recently energy firms have strongly refocused their activity on the non-retail sector.*

However, according to market rumours closing the transactions are at a difficult stage, as there is a huge gap between the price expectations of the parties involved:

Huge gap between the price expectations of the parties involved

- *On the one hand, analysts believe that the Government wants to avoid a potential new excessive deficit procedure and accordingly wants to purchase the Hungarian retail units of the utility service providers at the lowest possible price.*
- *On the other hand, analysts also highlight that shareholders who invested significant amounts in the recent years into their Hungarian branches/subsidiaries are determined to get the best possible return on their investment. In this context, the CEO of E.ON Eric Depluet pointed out that utility service providers would not sell their assets to the state below market value. At the same time, analysts add that utility service providers are well aware of the fact that they would be hard-pressed to find any other buyer under current deteriorating market conditions.*

Taking all this into account, it seems that unless the Hungarian government changes its course, some energy firms may exit from the Hungarian retail energy market. The only remaining question is when and how it could happen.

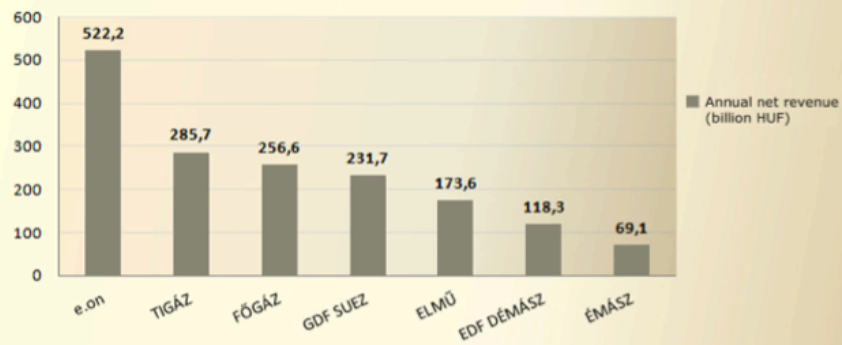
Data of the main utility service providers

Year 2012

(source: Népszabadság)

Profit after tax
(billion HUF)

↓ -15,5 ↓ -75,7 ↑ 7,1 ↓ -1,2 ↑ 8,4 ↑ 12,2 ↑ 4,3



Banking sector may still face consolidation

Raiffeisen and MKB plan to exit the Hungarian banking market

The recent market events evidence that the long promised consolidation of the Hungarian banking industry is closer than ever. Bayern LB, the parent bank of MKB announced that it will split MKB in a way that will increase its chance of being sold. Raiffeisen is currently considering some purchase offers in order to exit the market. On the other hand, one of the few profitable banks, OTP announced again that it would grab any opportunity for growth. Taking all into account the next couple of months may bring important changes to the Hungarian banking industry.

Key players:
OTP,
Erste,
Raffaelsen,
Intesa San Paolo,
Unicredit,
KBC,
Bayerische Landes-
bank



In our previous edition we reported that the CEO of OTP Bank, Sandor Csanyi asserted that the sector's lack of profit could drive to consolidation, so that in the next couple of years there may be only four or five large banks. Now the consolidation of the banking industry has become closer than ever.

There may be only four or five large banks

Market analysts are not surprised that when poten-

tial news arise regarding the potential exit of any of the players from the Hungarian banking market it is usually related to CIB, Raiffeisen or MKB Bank.

Namely, after the credit crunch in 2008 the Hungarian banking sector has been divided into two parts: banks such as OTP, K&H and Unicredit which despite the serious market and regulatory hurdles (such as lending in Swiss Franc when the value of the Hungarian Forint dramatically decreased, introduction of the extra tax and the prepayment right allowing retail borrowers to repay foreign loans under favorable exchange rates) remained profitable and banks such as CIB, Raiffeisen and MKB Bank which have been operating with losses for years and which without their parent companies' funding would have become insolvent already years ago.

According to the last report, Hungarian banks were profitable overall in the first half of 2013 (74% of the overall profit is connected to three successful banks: OTP, K&H and Unicredit) but 17 banks recorded losses and 80% of these losses were realized by CIB, Raiffeisen and MKB Bank. These figures are particularly interesting when we take into account that both groups of banks face the same market and regulatory conditions.

80% of the overall losses were realized by CIB, Raiffeisen and MKB Bank

Analysts emphasize that CIB, Raiffeisen and MKB Banks are in most trouble as they

had an extensive increase of credit portfolio (e.g. one year CIB extended its portfolio by 45% while the total industry's portfolio was increased by only 21%) and an over flexible lending policy of foreign currency loans (such as only 10% of down payment requirement, minimum examination of credit standing), which had an adverse result after the credit crunch. In addition, analysts also point out that these banks financed significant projects (such as building of hotels or residential developments) which were never finished after the credit crunch.

For these reasons the potential exit of CIB, Raiffeisen and MKB has been speculated for long time. However, the recent announcements evidence that the potential exits have become closer than ever:

Bayern LB may split MKB

Split of MKB

Bayern LB the parent bank of MKB announced that it would split MKB in a way to increase its chance of being sold. The CFO of Bayern LB, Stephan Winkelmeier observed that it could not be sold as a whole. Parts of the Hungarian subsidiary would be transferred into a so-called "bad bank" which would make the selling more digestible he added. There are speculations that the creation of "the bad bank" will most probably affect MKB's project finance division which generated significant losses in the last years.

Raiffeisen Bank is considering purchase offers

Raiffeisen has probably received some purchase offers

Raiffeisen may also exit Hungary. The news was unexpected. However, it was not a particular surprise for the analysts as Raiffeisen Bank was one of the most unsuccessful banks in the Hungarian market. However, what comes as a major surprise is the speculation that Raiffeisen has already received some purchase offers. Similarly to MKB, analysts believe that it would be reasonable for Raiffeisen to sell its Hungarian units in parts.

Other foreign banks' position

Right now other banks did not reveal their intention that they would like to exit from the Hungarian market. However, analysts highlight that the Government has recently taken some new measures which will be hardly sustainable for banks which have been already operating with losses:

- *The Government has recently passed a bill allowing cash withdrawal free of charge up to 150 000 HUF (approximately EUR 400-500). This may generate significant loss of revenue.*
- *The Government is looking for new ways to establish a new general foreign currency loan relief scheme which will probably include releasing part of the debt by fixing the exchange rate by a predetermined rate. Although the complete scope and extent of this scheme has not yet been worked out, analysts believe that this scheme will also generate significant losses for banks.*

Introduction of new regulatory hurdles could hasten the consolidation of the industry

OTP plans to grow

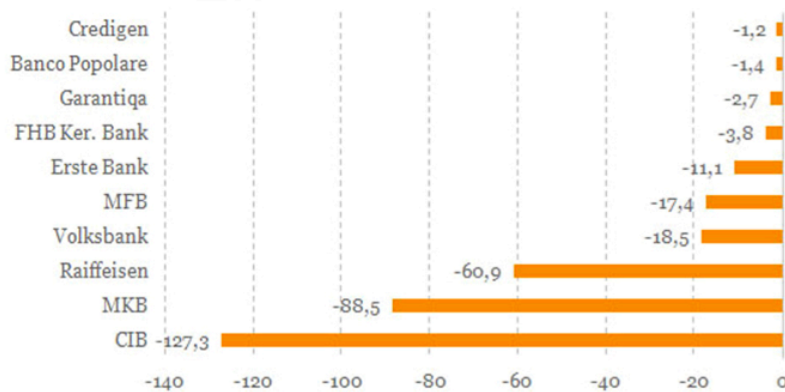
Laszlo Bencsik the deputy CEO of the successful OTP Bank observed that any further losses caused by the relief scheme could hasten the consolidation of the industry.

At the same time he noted that OTP Bank would grab any new opportunity for growth.

There is no question that consolidation is under way and that the banking landscape will soon be significantly changed. As Mr. Csanyi predicted, it is highly likely that in the near future there will only be four or five large banks in the Hungarian banking sector.

OTP would grab any opportunity for growth

Top 10 of credit institutions (operating as companies limited by shares) with the biggest losses in Hungary in 2012 (billion HUF)



Source: PSZÁF, Portfolio.hu

4G mobile spectrum auction to be held in Hungary soon

Frequency rights for sale within the 800, 900, 1800, 2600 MHz and 26 GHz spectrum

The National Media and Communications Authority has recently published the draft of the tender document for the frequency rights within the 800, 900, 1800, 2600 MHz and 26 GHz spectrum. It is expected that the auction will be significant, as it can bring approximately half billion Euros to the state budget. The main potential applicants are Vodafone, Telenor and T-Mobile. Still the Authority categorically stated that it would create an equal opportunity for both incumbents and new entrants.



Long awaited

In line with the EU legislation Hungary undertook the obligation to ensure the required spectrums for wireless broadband services until the end of 2013. Further, as Hungary has recently switched from analogue to digital broadcasting, a significant portion of the spectrum has become available.

Accordingly, the release of additional spectrum has

Calls for tenders for the frequency rights within the 800, 900, 1800, 2600 MHz and 26 GHz spectrum

been long awaited. The National Media and Communications Authority has recently published the draft of the tender document for the frequency rights within the 800, 900, 1800, 2600 MHz and 26 GHz spectrum. It will likely be a significant auction as it can bring approximately EUR half billion Euros to the state budget. The Authority has been currently examining the feedbacks of the market players regarding this draft document. Soon the Authority will commence the calls for tenders.

In the professional circles it is widely accepted that the main potential applicants are Vodafone, Telenor and T-Mobile. However, the Authority was positive that it would create an equal opportunity for both incumbents and new entrants.

Main potential applicants: Vodafone, Telenor and T-Mobile

There is no question that this long awaited opportunity can bring significant developments to the Hungarian mobile telecommunication industry.

The main details of the draft of the tender document:

Language of the tendering procedures	The language of the procedure is Hungarian The applicant can submit its application in Hungarian or in other language (official translation is required)
Participants	Any domestic or foreign natural person/entity on the condition that they meet the tender specifications. Participants can apply individually or via consortium.
Subject	790-821/832-862 MHz (800 MHz spectrum), 880-885,1/925-930,1 MHz (900 MHz spectrum), 1725-1740/1820-1835 MHz (1800 MHz spectrum), 2500-2690 MHz (2600 MHz spectrum) 24549-24605/25557-25613 MHz (26 GHz spectrum).
Minimum tender fees	From HUF 150 million (approx. EUR 480 000) to HUF 39 billion (approx. EUR 125 million).
Participation fees	HUF 40 million (approx. EUR 130 000) + VAT
Collaterals	Securing the performance of procedural obligations by paying amounts from HUF 25 million (approx. EUR 80 000) to HUF 100 million (approx. EUR 320 000), Securing the payment by amounts which correspond to the relevant minimum tender fee
Duration of frequency rights	15 February 2029
Deadline for submission of bids	22 January 2014 (However, taking into account that the final tender documentation has not yet been published, it is believed that the deadline will be extended)

The largest energy deal in Central Europe and the Balkans

The Hungarian blue-chip energy company, MOL, may sell its stake in the Croatian INA

Key players:

MOL,

ÖMV,

British Petroleum,

Shell,

Gazprom,

Rosneft,

Socar,

Zarubezhneft

On 4 October 2013, the Hungarian prime minister, Viktor Orban announced in his regular Friday morning radio speech that the Hungarian state, as a major shareholder of MOL gave instructions to the board of directors to make preparations for the sale of its stake in its Croatian partner INA. The sale of INA's share would raise important questions regarding the future perspective of the regional oil industry. Will the sale become a reality? Who could be the potential buyer?



The Hungarian oil company MOL may sell its stake in the Croatian INA. For years the relation between the Hungarian and Croatian parties has been far from good. However, nobody in the market expected that the cooperation between MOL and the Croatian government would end permanently. This would certainly open an uncertain chapter regarding the future per-

spective of both MOL and the Croatian INA.

MOL, the largest Hungarian oil company

MOL is considered the largest Hungarian company active in the oil industry, mainly in the downstream field (processing and trade). MOL was the first national oil and gas company in Central Europe which was privatized (at the beginning in the mid-nineties). After the privatization it launched a very ambitious expansion policy which resulted in obtaining stakes in several big regional players (such as the acquisition of Shell Romania or Slovnaft) and exploration licences in Russia, Kurdistan and Cameroon.

Apart from this, as a result of an almost 10-year acquisition process MOL has acquired a 49.08% share in the Croatian INA. The other biggest shareholder of INA is the Croatian state which possesses 44.84% of share in the company.

The two major participants signed a shareholders' agreement in 2009 as a result of which the control of the company came under the dominance of MOL (the directory board consists of 6 directors: 3 nominated by MOL and 3 by the Croatian government, however the president of the board is nominated by MOL and in case of a tie vote, the presidential vote decides).

Regrettably for MOL, the takeover of the managing rights was disputed by the Croatian state. The Croatian state alleged that the takeover was carried out by fraudulent acts of the CEO of MOL, Zsolt Hernadi. On the other hand, the Hungarian government denied the Croatian accusations, claiming that everything was conducted in line with international and national law and the contractual provisions.

Takeover of the managing rights was disputed

Although the circumstances surrounding the takeover are still unclear, the majority of analysts agree that the conflict was of both a political and an economical nature. On the one hand, analysts believe that the Croatian government intends to gather political votes by raising the flag of protecting their national interests against MOL. On the other hand, MOL and the Croatian state have opposing views in respect of the near-and medium-term future of INA.

Political and economic nature of the conflict

MOL would like to modernize and restructure INA as its facilities are not in line with the present industry requirements, its refineries are non-rentable and its gas line business has for years created only losses.

The Croatian Government thinks quite the opposite. It would slow down the pace of modernization as mass redundancies and the sale of the gas line business would cost the Government a lot in terms of election votes (e. g. the country already suffers from a 17% unemployment rate).

The press speculated that the announcement of the Prime Minister might be only a political bluff as neither MOL nor the Croatian state would benefit from the sale of MOL's INA portion.

MOL would give up its largest strategic expansion move and lose one of its highest development potentials in respect of upstream field (research and exploitation) development. It is also worth mentioning that 36-38 % of MOL's aggregated stores and exploitation as well as two refineries are provided by INA.

The sale of INA would go against both Hungarian and Croatian interests

On the other hand, the Croatian state can also only lose by the sale. According to various experts, the Croatian state does not have funds to buy the shares and it cannot find a better partner than MOL that already has spent significant sums to develop INA's out of date facilities.

As for the 49.08% share, there are only a couple of potential purchasers in sight:

- *the Austrian ÖMV which would hardly give a reasonable price for the purchase of the stake as it has recently lost its interest in the region,*
- *the British Petroleum or Shell would be highly welcomed by the Croatian government; however, the press speculates that they are not keen to make an investment far under their business scales.*
- *the remaining potential aspirants would be the Azeri Socar, and the Russian players: Gazprom, Rosneft and Zarubezhneft.*

Market analysts highlight that Russians have already gained a foothold in the Balkans. Gazprom chose the Serbian NIS as an investment target, already spending a fortune on its refinery facilities. Thus, analysts believe that a Russian takeover would provide INA with a subordinate role in the future oil industry of the Balkans. They also believe that when the regional energy dependence from Russia is already a burning

issue, a stronger regional presence of Russia would obviously go against both Hungarian and Croatian interests.

The sale of MOL's
stake in INA has
become highly
plausible

However, despite all of the above, the sale of MOL's stake in INA has become highly plausible. Namely the board of directors of MOL has recently ordered the executive department to prepare the documentation for the sale. The CEO of MOL is categorical that there are only two scenarios: INA will either choose to follow a modern business model suggested by MOL or a state-owned run model in which case MOL will certainly sell its stake in the company.

It cannot be predicated what will be the outcome of this situation, but one thing is sure. If the speculated deal will be closed in the next few months, the landscape of the regional oil industry will be significantly changed

Hungarian pharmacy industry still booming

Strong appeal for investors to buy Hungarian pharmaceutical stocks

Like other Hungarian industries, the Hungarian pharmaceutical industry is facing a challenging regulatory and tax environment. However despite this fact, the Hungarian pharmaceutical industry is still one of the leading industries in Hungary. The strong economic figures and recent market events – including the purchase of Egis by Servier and the rapid increase of Richter's stock – undoubtedly evidence that makes it worth keeping an eye on the industry developments in the Hungarian pharmaceutical industry.



Hungarian drug makers have been very successful for years. Still, nowadays the Hungarian pharmaceutical companies face a challenging regulatory and tax environment. The key problem is the blind bidding system operated by the state owned health care fund – the bidders have to offer the lowest possible price without knowing the competitors' offers – where

only the lowest price receive financial support from the state. Needless to say this system caused massive decrease of prices and significantly lower profit margins for pharmaceutical products. Hungarian pharmaceutical companies also objected that they reduced prices as low as economically viable, but the Asian competitors could still squeeze them out with their extremely low prices. In addition, the introduction of extra tax put further strains on Hungarian drug makers.

However despite this challenging market environment, the Hungarian pharmaceutical industry is still one of the leading industries in Hungary. The key of the industry's success is that Hungarian drug makers remain relatively unaffected by the domestic market and regulatory hurdles given that a large portion of their revenues (70-80%) are generated by export activity. Thus, Hungarian drug producers continue to perform well, according to experts, the four major drug makers Richter, Egis, Teva and Sanofi generate approximately 3.7% of the country's gross domestic product.

Moreover, the Government has recently made several amicable gestures to this industry. Drug makers can expect an increase in drug supports (from HUF 49 to HUF 56 billion) in accordance with the budget draft for 2014. The Government also concluded strategic partnership agreements with the market leading firms Richter, Egis, Teva

Key players:

Richter,
Sanofi,
TEVA,
Servier,
Bayer AG

Challenging regulatory and tax environment

70-80% of their revenues are generated by export activity

and Sanofi. Such agreements usually have incentives such as job incentives or R&D incentives. The Government also organized a public procurement scheme to centrally manage the supply of drug products to healthcare institutions. The winning bidders such as Hungaropharma or Teva were cited as saying that they will certainly benefit from the new supply scheme.

The Government
has made several
amicable gestures to
this industry

Last but not least, the recent events on the Budapest Stock Exchange ("BSE") in particular reflect that the Hungarian pharmacy industry is still booming.

First of all, Servier the majority owner of Egis has recently offered to completely buy out Egis. Servier made a very generous offer of HUF 28000 per/share (overall offered a purchase price of HUF 107 billion). Experts believe that the timing and the generosity of this offer makes perfect sense as Servier is probably aware of the possibility of further increase in Egis share price taking into account that Egis has recently had tremendous successes in the market. Egis has a significant cross-border venture with the South-Korean Celltrion and a high chance to conclude a very lucrative Russian deal soon. It has also a strong cash-flow portfolio, which makes it possible to extend its investments without the need of credit or equity capital finance.

The timing and
the generosity of
the purchase offer
of Servier makes
perfect sense

Secondly, Servier plans to delist Egis from the BSE given that Egis has no need to use the equity capital market. This is outstanding news for the market leader Richter. Egis potential exit would be very fruitful for Richter as it would remain the only listed drug maker on the BSE and needless to say the only choice for investments funds wishing to have Hungarian pharmaceutical stocks in their portfolio. Richter has already benefited from the Egis buyout announcement as its share prices has gone up 6% in just two days, but Egis' potential exit from the BSE may lead to a historic increase in Richter share prices.

Significant increase
of Richter's stock

There is no question that the strong economic figures and the recent market developments clearly evidence that is worth investors keeping an eye on the Hungarian pharmacy industry.

The top 10 Hungarian drug producers (source: Budapest Business Journal)

Ranked by total net revenue in 2012

Name of the company	Parent company / Foreign ownership	Total net revenue (Billion HUF)
Richter Gedeon Nyrt	Hungarian based company, no foreign parent	326,702
Sanofi-Aventis Zrt	Sanofi Aventis Europe (France)	212,962
Teva Gyógyszertár Zrt.	Teva Pharmaceutical Industries Inc. (Israel)	188,438
Egis Gyógyszertár Nyrt	Servier (France)	132,825
Bayer Hungária Kft	Bayer AG (Germany)	42,390
Janssen-Cilag Kft	Johnson & Johnson International Financial Services Company (Ireland)	42,222
Novartis Hungária Kft	Novartis International AG, (Switzerland)	37,420
Roche Hungary Kft	F Hoffman – La Roche Ltd (Switzerland)	32,131
Pfizer Pharmaceuticals Trade Kft	Pfizer Inc (USA)	32,088
GlaxoSmithKline Kft	Setfirst Ltd (England)	20,132

Hungary's economic forecast for 2014

Stable economic growth in 2014

The Central Bank of Hungary expressed its strong financial outlook that the next year will be a promising year in Hungary. It predicted 7.4% increase of investment growth, historic low level of interest rates, moderate GDP growth, low inflation rate and the deficit of 2.5% of the GDP which is still below the 3% of GDP reference value to stay beyond the excessive deficit procedure. It seems that the Hungarian stable economic growth will continue in 2014.



2013 was a promising year for the Hungarian economy. Hungary managed to exit the excessive deficit procedure, inflation and interest rates reached a historic low.

In addition, according to the reports of the Hungarian Central Statistic Office, the GDP increased by 1.8% and the volume of investments increased by 9.8% in the 3rd quarter of 2013

compared to the same period of the previous year. The figures of these reports well exceeded the expectations of the majority of analysts.

The Minister for National Economy states that the Hungarian economy has entered into a permanent growth path and that its structure has become healthier. He also adds that previously the growth was driven by export activity, but now domestic consumption is also catching up with the overall economic progress.

The majority of analysts agree that economic conditions in Hungary are constantly improving.

Pursuant to the above, it is not surprising that the Central Bank of Hungary (the "CBH") is positive that the Hungarian economic progress will continue in 2014. According to the CBH 4rd quarter report of 2013 the following favourable macroeconomic conditions are predicted for 2014:

Investment growth

Investment growth may be the main driving factor of the economic growth in the next year. 7.4% increase of investment rate is forecasted. The CBH believes that the new credit program of CBH offering favourable conditions to SMEs may give a major boost to investment growth. The CBH also believes that there is a great potential in

2013 brought economic growth

Favourable economic forecast for 2014

the growth of processing industry in 2014.

GDP growth may increase up to the level of 2.1%.

The CBH believes that the potential 2.1% GDP growth among others is intertwined with the investment growth mentioned above and the upswing of domestic consumption due to a set of governmental measures such as utility price cuts and tax incentives.

Inflation will remain low in 2014.

Inflation reached a historic low level of 1.7 % in 2013 primarily due to utility price cuts. As the utility price cut tendency continues, the CBH believes that inflation may even sink to 1.3%.

Deficit will remain below the 3% of GDP reference value.

Thanks to a series of consolidation measures Hungary managed to exit from the excessive deficit procedure ("EDP") in 2013. Apart from Hungary only a few countries have been released from the EDP in 2013. It is anticipated that in 2014 the deficit in Hungary will be not more than 2.5% of GDP which is still well below the above mentioned reference value to stay beyond the EDP. The CBH predicts that the position of the budget could be strengthened in 2014 by various revenues such as taxes or frequency fees.

Interest rate cut will reach historic low.

Due to several strong macroeconomic conditions (for example: low inflation rate, release from the EDP and stability of Hungarian currency) interest rates in Hungary were reduced to a historic low level of 3% in December 2013. According to the CBH report as long as real economy justifies it further cuts can be expected even in 2014. Analysts believe that interest rates may even sink below 3%.

Time will tell whether the macroeconomic forecast of CBH will pass the test. Hopefully the stable economic growth will continue and Hungary will be a promising place for investment.

Macroeconomic forecast of Hungary

Data of the 4rd quarter report of 2013 (Source: Central Bank of Hungary)

	2013	2014
Core inflation	3,3	3,0
Consumer price index	1,7	1,3
Economic growth		
External demand (based on GDP)	0,6	1,7
Household consumer expenditure	0,1	1,5
Investment	3,5	7,4
Domestic use	0,6	2,4
Export	5,2	5,4
Import	5,0	6,0
GDP	1,1	2,1
External balance (in percentage of GDP)		
Currency account balance	2,8	2,8
External financing capacity	6,0	5,5
Government budget deficit	2,6	2,5

A new financial watchdog

Merger of the Central Bank of Hungary and the Hungarian Financial Supervisory Authority

The Hungarian Parliament has recently decided on the full merger of the Central Bank of Hungary and the Hungarian Financial Supervisory Authority. Both the Central Bank of Hungary and the European Central Bank welcomed the merger. They believe that the integration has compelling benefits for the whole Hungarian financial system.



In June 2013 the Minister for National Economy proposed the amendment of the Central Bank Act to the Hungarian Parliament. The aim of such proposal was to merge the Central Bank of Hungary (the “CBH”) and the Hungarian Financial Supervisory Authority (the “HFSA”) by integrating their functions and duties into a single organisation. The new Central

Bank Act merging CBH and HFSA came into force as of 1 October 2013. As a result of the merger, the HFSA was terminated without a legal successor.

The HFSA was terminated

The merger of the CBH and the HFSA is not a brand new and unique solution on an international level. After the crisis a number of countries reviewed and amended their supervisory systems and it seems that the integrated model is gaining ground: numerous countries (such as UK, Ireland, Belgium, France) have decided to consolidate their separate supervisory function into the central bank functions as a response to the crisis.

Numerous countries have decided to consolidate their separate supervisory function into the central bank functions

Due to the merger of the CBH and the HFSA, the financial supervisory powers and functions on the Hungarian market are strengthened. The CBH expects that the integration of the consumer protection and supervisory activities of the HFSA (in relation to banks, the capital market and insurance companies) with the macroprudential activities of the CBH over the whole financial system has several benefits.

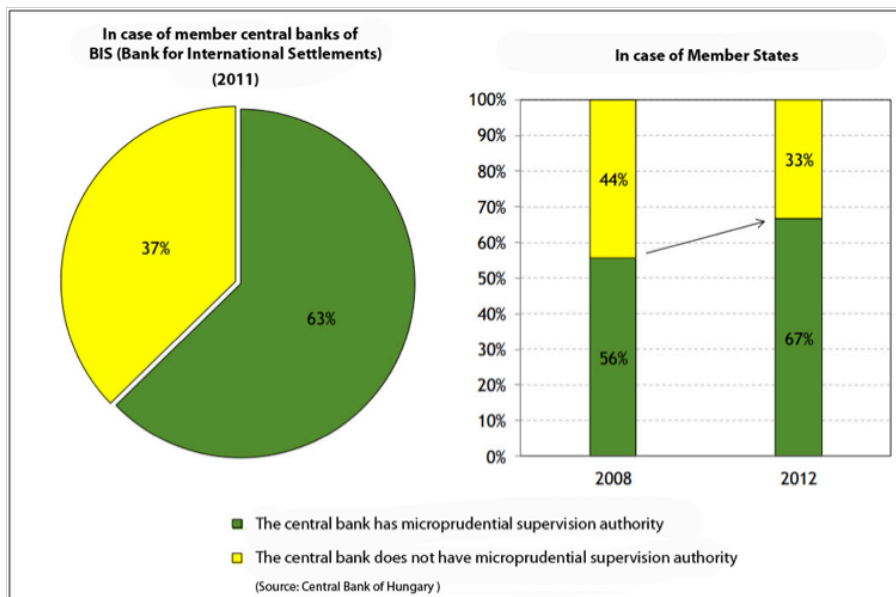
CBH emphasizes that deficiencies in the current regulation and also supervision of the financial system played an important role in the emergence of the financial crisis in Hungary. Due to the merger, broader information is available for the CBH as the new regulatory authority, which is expected to make the supervision and the regulation of the Hungarian financial system more efficient. The decision making procedure is also expected to improve. Last but not least, the integration provides CBH with a wide

Compelling benefits of the integration of micro and macroprudential activities

range of instruments to prevent the increase of risk at the individual and systematic level and to efficiently deal with crisis situations.

The European Central Bank (the “ECB”) criticized the procedure of the merger in respect of certain points, however it welcomed the merger overall. The ECB in its opinion stated the following: “this integrated institutional framework will improve the ability to safeguard financial stability and prevent or mitigate systematic risks. In Member States with a relatively small financial market such as Hungary, there are strong arguments for concentrating supervisory and macro-prudential responsibilities within a single authority”.

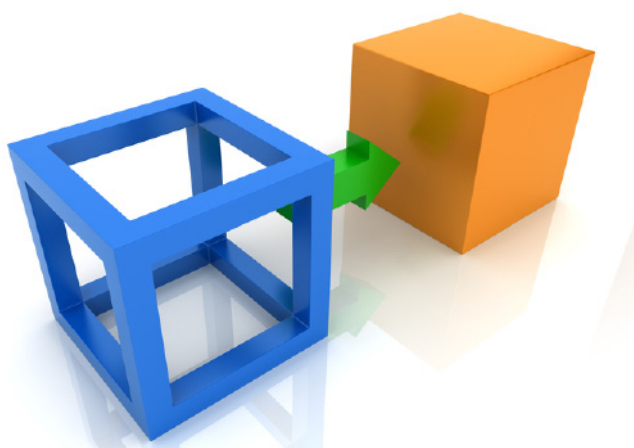
As a conclusion, through the merger of the CBH and the HFSA an adequately strong and independent supervisory body was established, which enables to strengthen the stability of the whole spectrum of the Hungarian financial system and to systematically control the financial institutions. Integration also empowers standard, constant and reliable communication. Such restructuring is in line with other countries’ recent practice that had reviewed their supervisory systems and strengthened them by way of integration.



No barriers for cross-border company transformation

The Supreme Court decision may result in a more investor-friendly application of Hungarian law

According to the ruling of the Supreme Court cross-border transformation cannot be banned by national law. The ruling set a Hungarian precedent by approving cross-border company transformation in respect of companies who are registered in other Member States and want to move their seat and business to Hungary.



The case concerned an Italian company wanting to transform to a Hungarian company by transferring its seat and business activity to Hungary. Thus, the respective company was deleted from the Italian company register and a Hungarian company was founded. The Hungarian Court rejected its application for Hungarian company registration with the justification that

according to Hungarian law a non-Hungarian company cannot be registered as a legal predecessor into the Hungarian company registry. The Supreme Court of Hungary referred for a preliminary ruling to the European Court of Justice ("ECJ").

The ECJ ruled that the provision of Hungarian law that procedurally bans the transformation of a company registered in other Member States ("MS") into a Hungarian company infringes the EU principles of freedom of establishment.

The Supreme Court ruling accepted the findings of the ECJ ruling. The ruling stated that in compliance with the findings of the ECJ ruling the provisions of Hungarian law cannot make the cross-border company transformation impossible in respect of companies who are registered in other MS and want to move their seat and business to Hungary. The Supreme Court concluded that in order to ensure the legal continuity between the two companies from different MS, the law of the predecessor company shall apply for deletion of the predecessor company and the law of the successor company shall apply for formation and registration of the successor company.

It is evident that both the Supreme Court and the ECJ rulings are of significant importance as they allowed a new model of Hungarian company formation. The practical implications of these rulings will hopefully result in a more investor-friendly application of Hungarian law in respect of cross-border company transformations.

Hungarian law cannot make the cross-border company transformation impossible

A new model of Hungarian company formation

About VJT & Partners

The firm

VJT & Partners is a Hungarian commercial law firm advising international and domestic corporate clients and entrepreneurs. The firm was founded by Janos Tamas Varga, who has created a highly successful team based on values including inspiring leadership, striving for perfection, commitment, courage and harmony.

VJT & Partners is recognised as one of Hungary's leading commercial law firms and also as an excellent collaborative partner, working hand-in-hand with its clients. Clients value the firm's absolute commitment, leading to effective and enduring relationships. The firm combines the highest degree of professionalism, the efficient delivery of legal services with dynamism, flexibility, responsiveness and personal attention.

Lawyers in the firm have developed an in-depth understanding of both the legal and the commercial realities of business. The firm prides itself in giving direct, honest and practical advice, tailored to its clients' needs. The shared values of VJT & Partners are at the very core of the creativity and 'fresh thinking' approach of the firm.

As a member of the EU, but not the single currency, Hungary has a unique language and business culture and a complex legal system bringing particular challenges. All lawyers at VJT & Partners have extensive experience of working with international and domestic companies alike, to help navigate these challenges and to achieve their objectives in Hungary, and to ensure appropriate regulatory approvals.

The leading legal directories rank VJT & Partners highly across a range of practice areas.

VJT & Partners is a full-service law firm that satisfies the needs of clients across a broad range of industries and professions. The firm's legal services include commercial contracts, competition, corporate M&A, data protection, dispute resolution, finance, immigration, employment, intellectual property, outsourcing, private equity, real estate, regulatory, restructuring and insolvency, and technology.

Practice areas

The firm is especially active and highly ranked in the following areas:

Corporate mergers and acquisitions

VJT & Partners believes that advising on M&A transactions is to provide more than just legal advice. Understanding the logic and dynamics of the industry sector in which the client and other participants operate is a prerequisite for success.

Technology

The firm regularly advises clients operating in the technology sector on a wide variety of legal matters, ranging from corporate law issues to drafting industry-specific agreements on software development and licensing, system supply, database transfer and hosting, as well as maintenance and support services.

Employment

Highly rated employment lawyers at VJT & Partners have a wealth of experience in all aspects of contentious and non-contentious employment matters. Fully appreciated for understanding their clients' business goals, lawyers design structures and procedures that are watertight and defensible in many court proceedings.

Dispute resolution

VJT & Partners is well aware that effective management and resolution of disputes are of critical importance from a corporate risk management point of view. The firm regularly provides legal advice on pre-litigation. When it comes to litigation, lawyers focus on the business needs of clients, providing practical and cost-effective advice.

Business immigration

Business immigration to Hungary may in particular take place through investment in residency bonds ("Investor Residency Bond Program") or by establishing a business in Hungary ("Business Entrepreneur Residency Program"). VJT & Partners' immigration lawyers handle all aspects of business immigration cases, advising medium to high-net worth foreign individuals and multinational corporations.

How we work

Lawyers at VJT & Partners are encouraged to develop, to enjoy their work and to become real 'Masters of Collaboration'. Clients comment on the firm's cooperation, communication and its absolute commitment to what they are trying to achieve.

In turn, we find that this leads to effective and enduring relationships. We combine the highest degree of professionalism and the efficient delivery of legal services with dynamism, flexibility, responsiveness and personal attention.

Our values

The values that lie at the heart of our business ethos are the building blocks of our business. Nurturing the following values brings the 'hearts and minds' of VJT & Partners' lawyers together as one successful team. We would be happy to talk you through them, what they mean to us, to our business and our clients:

- *Inspiring leadership*
- *Striving for perfection*
- *Commitment*
- *Courage*
- *Harmony*

Office:

*1126 Budapest
Kernstok Károly tér 8.
Hungary*

Contact:

*Tel: +36 1 501 9900
Fax: +36 1 501 9901
E-mail: office@vjt-partners.com
Web: www.vjt-partners.com*