EGYÜTT. VELED

CONSOLIDATED ANNUAL REPORT

OF MAGYAR TELEKOM TELECOMMUNICATIONS
PUBLIC LIMITED COMPANY

FOR THE YEAR ENDED DECEMBER 31, 2018

EGYÜTT. VELED

CONSOLIDATED FINANCIAL STATEMENTS AND MANAGEMENT REPORT

OF MAGYAR TELEKOM TELECOMMUNICATIONS PUBLIC LIMITED COMPANY

FOR THE YEAR ENDED DECEMBER 31, 2018

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EGYÜTT. VELED

CONSOLIDATED FINANCIAL STATEMENTS

OF MAGYAR TELEKOM TELECOMMUNICATIONS PUBLIC LIMITED COMPANY

FOR THE YEAR ENDED DECEMBER 31, 2018

PREPARED IN ACCORDANCE WITH

INTERNATIONAL FINANCIAL REPORTING STANDARDS

AS ENDORSED BY THE EUROPEAN UNION (EU IFRS)

INDEPENDENT AUDITOR'S REPORT

To the shareholders of Magyar Telekom Telecommunication Public Limited Company

Report on the audit of the consolidated financial statements

Opinion

We have audited the accompanying consolidated financial statements of Magyar Telekom Telecommunication Public Limited Company (the "Company") and its subsidiaries (together the "Group") which comprise the consolidated statements of financial position as at 31 December 2018 (in which the total of consolidated statements of financial position is MHUF 1 155 966), the consolidated statements of profit or loss and other comprehensive income (in which the total comprehensive income for the year is MHUF 49 837 profit), the consolidated statements of cash flows, the consolidated statements of changes in equity for the year then ended and the notes to the consolidated financial statements including a summary of the significant accounting policies.

In our opinion, the accompanying consolidated financial statements give a true and fair view of the consolidated financial position of the Group as at 31 December 2018, and of its consolidated financial performance and its consolidated cash flows for the year then ended in accordance with International Financial Reporting Standards ("IFRS") as adopted by the EU and they have been prepared, in all material respects, in accordance with the supplementary requirements of Act C of 2000 on Accounting ("Accounting Act") relevant for the consolidated annual financial statements prepared in accordance with IFRS as adopted by the EU.

Our opinion is consistent with our additional report to the audit committee.

Basis for opinion

We conducted our audit in accordance with Hungarian National Standards on Auditing ("HNSA") and with applicable laws and regulations in force in Hungary. Our responsibilities under those standards are further described in the "Auditor's responsibilities for the audit of the consolidated financial statements" section of our report.

We are independent of the Group in accordance with the applicable laws of Hungary, with the Hungarian Chamber of Auditors' Rules on ethics and professional conduct of auditors and on disciplinary process and, for matters not regulated in the Rules, with the Code of Ethics for Professional Accountants issued by the International Ethics Standards Board (IESBA Code of Ethics) and we also comply with further ethical requirements set out in these.

The non-audit services that we have provided to the Group, in the period from 1 January 2018 to 31 December 2018, are disclosed in note 21 to the consolidated financial statements.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Group are in accordance with the applicable laws and regulations in Hungary and that we have not provided non-audit services that are prohibited under Article 5 of Regulation of the European Parliament and Committee No 537/2014 and Subsection (1) and (2) of Section 67/A of Act LXXV of 2007 on the Chamber of Hungarian Auditors, the Activities of Auditors, and on the Public Oversight of Auditors.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Our audit approach

Overview

Overall group materiality	Materiality applied was MHUF 4 600, which is approximately 2.5% of the consolidated EBITDA (Earnings before Interest, Taxes, Depreciation and Amortization)
Group Scoping	In addition to the parent company, Magyar Telekom Telecommunication Plc., we included two subsidiaries in our audit, Makedonski A.D. and T-Systems Magyarország Zrt., which are operating in Macedonia and Hungary. These three companies account for 97% of the consolidated revenues and for 97% of the consolidated EBITDA.
Key Audit Matters	• Goodwill impairment assessment • Accuracy of revenue recognition due to complex billing systems and adoption of IFRS 15 Revenue from contracts with customers

As part of designing our audit, we determined materiality and assessed the risks of material misstatement in the consolidated financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. As in all of our audits, we also addressed the risk of management override of internal controls, including among other matters, consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the consolidated financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the consolidated financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the consolidated financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, both individually and in aggregate on the consolidated financial statements as a whole.

Materiality	MHUF 4 600 (2017: MHUF 5 100)
Determination	Approximately 2.5% of the consolidated EBITDA
Rationale for the materiality benchmark applied	We chose consolidated EBITDA as the benchmark because, in our view, it is the benchmark against which the performance of

	the Group is most commonly measured by users, and is a generally accepted benchmark in the telecommunication industry. We chose 2.5%, which is consistent with quantitative materiality thresholds used for profit-oriented companies in this sector. This is consistent with the basis for our materiality calculation in the previous year.

Group audit scope

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the consolidated financial statements as a whole, taking into account the structure of the Group, the accounting processes and controls, and the industry in which the Group operates.

We have identified two subsidiaries: Makedonski A.D. operating in Macedonia and T-Systems Magyarország Zrt. operating in Hungary, which, in our view, required an audit of their complete financial information, due to their financial significance to the Group.

For the remaining components we performed analytical review at the Group level. This together with additional procedures performed at the Group level, including testing of consolidation journals and intercompany eliminations, gave us the evidence we needed for our opinion on the Group consolidated financial statements as a whole.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the consolidated financial statements of the current period. These matters were addressed in the context of our audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matter	*How our audit addressed the key audit matter*
Goodwill impairment assessment As at 31 December 2018, goodwill relating to the Hungarian and Macedonian segments amounted to MHUF 192 905 and MHUF 20 199 respectively out of a total goodwill balance of MHUF 213 104. Impairment assessments involve significant estimates, as they are sensitive to the change in assumptions (in particular the input variables and long term growth rates, discount rates and assumptions underlying future operating cash flows). Management concluded that there was no need for impairment of goodwill.	We agreed the cash flow forecasts used in the impairment assessment to forecasts approved by the board of directors. We considered management's expectations in respect of material impacts of the external environment and planned operational improvements and whether these were appropriately reflected in the cash flow forecasts. We compared actual historical cash flow performance with previous forecasts and determined whether any differences fell within an acceptable range. We independently calculated a weighted average cost of capital with reference to market data and compared the long term growth rate to market data.

Details of the nature of the goodwill impairment assessment performed by management are given in notes 3.2 and 10.4 to the consolidated financial statements.	We assessed the sufficiency of the sensitivity analysis performed by management and performed further sensitivity analysis, primarily focused on changes in operating cash flows. We read notes 3.2 and 10.4 of the consolidated financial statements in order to assess whether they are in line with the requirements of the IAS 36.
Accuracy of revenue recognition due to complex billing systems and adoption of IFRS 15 Revenue from contracts with customers The accuracy of revenues recorded is an inherent industry risk. This is because telecommunication billing systems are complex and process large volumes of data with a combination of different products sold and price changes during the year, through a number of different systems. The Group adopted IFRS 15 as at 1 January 2018, applying the modified retrospective method. The Group opted for the portfolio approach. The adoption resulted in a material initial catch-up adjustment and required booking of such amendments which involve management estimates and assumptions as well. Total revenue of the Group was MHUF 657 104. Detailed disclosures and related accounting policies are in notes 2.1.1. and 18 of the consolidated financial statements.	We evaluated the relevant IT systems and the design of controls, and tested the operating effectiveness of controls over the: • Capturing and recording of revenue transactions; • Authorization of price changes and the input of those to the billing systems; • Calculation of amounts billed to the customers; and • Monitoring of assumptions and judgements related to IFRS 15, including those related to contract assets, contract costs, and contract liabilities. We also tested a sample of items from the customer billing systems to the invoices raised and checked these to the cash received from the customers. Our testing included customer bills for consumers and corporate customers. In respect of adoption of IFRS 15, we performed detailed testing, on a sample basis, of the catch-up adjustment as at the transition date, and of the contract assets, contract costs, and contract liabilities as at 31 December 2018.

Other information: the consolidated business report

Other information comprises the consolidated business report of the Group. Management is responsible for the preparation of the consolidated business report in accordance with the provisions of the Accounting Act and other relevant regulations. Our opinion on the consolidated financial statements expressed in the "Opinion" section of our independent auditor's report does not cover the consolidated business report.

In connection with our audit of the consolidated financial statements, our responsibility is to read the consolidated business report and, in doing so, consider whether the consolidated business report is materially inconsistent with the consolidated financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated. If based on our work performed we conclude that the consolidated business report is materially misstated we are required to report this fact and the nature of the misstatement.

Based on the Accounting Act, it is also our responsibility when reading the consolidated business report to consider whether the consolidated business report has been prepared in accordance with the provisions of the Accounting Act and other relevant regulations, if any, and to express an opinion on this and on whether the consolidated business report is consistent with the consolidated financial statements.

Because the Company's transferable securities are admitted to trading on a regulated market of a Member State of the European Economic Area, our opinion on the consolidated business report shall cover the information prepared under Paragraphs e) and f) of Subsection (2) of Section 95/B, and state whether the information referred to in Paragraphs a)-d), g) and h) of Subsection (2) of Section 95/B of the Accounting Act has been provided.

As the Company is a public interest entity preparing consolidated financial statements and the conditions in Paragraph a) and b) of Subsection (5) of Section 134 of the Accounting Act are met at the balance sheet date, the Company shall publish a non-financial statement required by Section 95/C in its consolidated business report relating to the companies included in the consolidation. In this respect, we shall state whether the consolidated business report includes the non-financial statement required by Section 95/C, and Subsection (5) of Section 134 of the Accounting Act.

In our opinion, the 2018 consolidated business report of the Group, also including the information prepared under Paragraphs e) and f) of Subsection (2) of Section 95/B of the Accounting Act, is consistent with the 2018 consolidated financial statements in all material respects, and the consolidated business report has been prepared in accordance with the provisions of the Accounting Act. As there is no other regulation prescribing further requirements for the consolidated business report, we do not express an opinion in this respect.

We are not aware of any other material inconsistency or material misstatement in the consolidated business report, therefore we have nothing to report in this respect.

We state that the information referred to in Paragraphs a)-d), g) and h) of Subsection (2) of Section 95/B of the Accounting Act has been provided. The consolidated business report includes the non-financial statement required by Section 95/C, and Subsection (5) of Section 134 of the Accounting Act.

Responsibilities of management and those charged with governance for the consolidated financial statements

Management is responsible for the preparation of the consolidated financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the EU and to prepare the consolidated financial statements in accordance with the supplementary requirements of the Accounting Act relevant for the consolidated annual financial statements prepared in accordance with IFRS as adopted by the EU, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting in the consolidated financial statements unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

Auditor's responsibilities for the audit of the consolidated financial statements

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with HNSAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with HNSAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting in the consolidated financial statements and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that gives a true and fair view.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the Group audit. We remain solely responsible for our audit opinion.

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We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

We were first appointed as auditors of the Group on 31 December 1991. Our appointment has been renewed annually by shareholder resolutions representing a total period of uninterrupted engagement appointment of 27 years.

The engagement partner on the audit resulting in this independent auditor's report is Árpád Balázs.

Budapest, 27 February 2019

Armin Krug
Partner
PricewaterhouseCoopers Auditing Ltd.
1055 Budapest, Bajcsy-Zsilinszky út 78.
Licence Number: 001464

Árpád Balázs
Statutory auditor
Licence number: 006931

Note:

Our report has been prepared in Hungarian and in English. In all matters of interpretation of information, views or opinions, the Hungarian version of our report takes precedence over the English version.

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

	Note	At December 31, 2017	At December 31, 2018
		(in HUF millions)	
ASSETS			
Current assets			
Cash and cash equivalents	4.2.1	5,399	7,204
Trade receivables and other assets	4.2.2, 12.1, 18	157,745	195,220
Other current financial assets	4.2.3.1	8,162	11,631
Current income tax receivable	6.1	384	254
Inventories	7	17,175	19,118
		188,865	233,427
Assets held for sale	8	162	-
Total current assets		189,027	233,427
Non current assets			
Property, plant and equipment	9	458,343	443,147
Intangible assets	10	441,458	447,952
Investments in associates and joint ventures	11	1,324	1,393
Deferred tax assets	6.3	59	77
Other non current financial assets	4.2.3.2, 18	19,323	24,985
Other non current assets	12.2	127	5,015
Total non current assets		920,634	922,569
Total assets		1,109,661	1,155,996
LIABILITIES			
Current liabilities			
Financial liabilities to related parties	4.4.1	35,191	111,144
Other financial liabilities	4.4.2	8,757	9,228
Trade payables	4.4.3	135,446	175,312
Current income tax payable	6.1	324	343
Provisions	13	3,267	3,418
Other current liabilities	14	43,596	41,395
		226,581	340,840
Liabilities associated with assets held for sale	8	-	-
Total current liabilities		226,581	340,840
Non current liabilities			
Financial liabilities to related parties	4.4.1	231,646	123,349
Other financial liabilities	4.4.2	47,608	47,919
Deferred tax liabilities	6.3	13,743	17,246
Provisions	13	9,231	11,265
Other non current liabilities	15	779	445
Total non current liabilities		303,007	200,224
Total liabilities		529,588	541,064
EQUITY			
Equity of the owners of the parent			
Common stock		104,275	104,275
Capital reserves		27,282	27,263
Treasury stock		(2,187)	(3,991)
Retained earnings		396,320	429,294
Accumulated other comprehensive income		21,505	23,650
Total Equity of the owners of the parent		547,195	580,491
Non-controlling interests	16	32,878	34,441
Total equity		580,073	614,932
Total liabilities and equity		1,109,661	1,155,996

Budapest, February 20, 2019

Tibor Rékasi
Chief Executive Officer, Board member

János Szabó
Chief Financial Officer

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

	Note	2017	2018
		For the year ended December 31, (in HUF millions, except per share amounts)	
Revenues	18	610,851	657,104
Direct costs	19	(245,777)	(286,931)
Employee related expenses	20	(80,240)	(82,968)
Depreciation and amortization	9, 10	(108,174)	(115,529)
Other operating expenses	21	(105,918)	(103,915)
Operating expenses		(540,109)	(589,343)
Other operating income	22	6,746	9,217
Operating profit		77,488	76,978
Interest income	23	543	363
Interest expense	24	(13,525)	(13,423)
Other finance expense - net	25	(8,645)	(4,724)
Net financial result		(21,627)	(17,784)
Share of associates' and joint ventures' net profit	11	343	588
Profit before income tax		56,204	59,782
Income tax	6.2	(15,958)	(13,333)
Profit for the year from continuing operations		40,246	46,449
Profit for the year from discontinued operations	26.2.1	9,526	-
Profit for the year		49,772	46,449
Other comprehensive income			
(Items that are or may be reclassified subsequently to profit or loss):			
Exchange differences on translating foreign operations		(439)	3,169
Revaluation of available-for-sale financial assets		19	219
Other comprehensive income from continuing operations, net of tax		(420)	3,388
Other comprehensive income from discontinued operations, net of tax	26.2.1	(12,512)	-
Other comprehensive income for the year, net of tax		(12,932)	3,388
Total comprehensive income from continuing operations		39,826	49,837
Total comprehensive income from discontinued operations	26.2.1	(2,986)	-
Total comprehensive income for the year		36,840	49,837
Profit attributable to:			
Owners of the parent		46,727	43,318
From continuing operations		37,239	43,318
From discontinued operations		9,488	-
Non-controlling interests		3,045	3,131
From continuing operations		3,007	3,131
From discontinued operations		38	-
		49,772	46,449

	Note	2017	2018
		For the year ended December 31, (in HUF millions, except per share amounts)	
Total comprehensive income attributable to:			
Owners of the parent		36,742	45,463
From continuing operations		36,948	45,463
From discontinued operations		(206)	-
Non-controlling interests		98	4,374
From continuing operations		2,878	4,374
From discontinued operations		(2,780)	-
		36,840	49,837
Earnings per share (EPS) information:			
Profit attributable to the owners of the Company		46,727	43,318
From continuing operations		37,239	43,318
From discontinued operations		9,488	-
Weighted average number of common stock outstanding (thousands) used for basic EPS		1,040,073	1,035,394
Average number of dilutive share options		4,585	6,074
Weighted average number of common stock outstanding (thousands) used for diluted EPS		1,044,658	1,041,468
Basic earnings per share (HUF)		44.93	41.84
From continuing operations		35.82	41.84
From discontinued operations		9.11	-
Diluted earnings per share (HUF)		44.93	41.59
From continuing operations		35.82	41.59
From discontinued operations		9.11	-

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Note	2017	2018
		For the year ended December 31, (in HUF millions)	
Cashflows from operating activities			
Profit for the year		40,246	46,449
Depreciation and amortization		108,174	115,529
Income tax expense		15,958	13,333
Net financial result		21,627	17,784
Share of associates' and joint ventures' result		(343)	(588)
Change in assets carried as working capital		(17,959)	(30,237)
Change in provisions		(1,581)	1,385
Change in liabilities carried as working capital		21,817	29,857
Income tax paid		(10,425)	(11,953)
Dividend received		111	535
Interest and other financial charges paid		(19,949)	(18,810)
Interest received		382	312
Other non-cash items		(647)	(4,498)
Net cash generated from operating activities from continuing operations		157,411	159,098
Net cash generated from operating activities from discontinued operations		(23)	-
Net cash generated from operating activities		157,388	159,098
Cashflows from investing activities			
Purchase of property plant and equipment (PPE) and intangible assets	28	(90,800)	(93,688)
Purchase of subsidiaries and business units	29	(3,791)	(2,045)
Cash acquired through business combinations		475	137
Proceeds from other financial assets		3,030	7,033
Payments for other financial assets		(5,897)	(4,978)
Proceeds from disposal of PPE and intangible assets		2,629	10,449
Proceeds from disposal of subsidiaries and business units		1	-
Payments for interests in associates and joint ventures		-	-
Net cash used in investing activities from continuing operations		(94,353)	(83,092)
Net cash inflow from investing activities from discontinued operations		36,292	-
Net cash used in investing activities		(58,061)	(83,092)
Cashflows from financing activities			
Dividends paid to Owners of the parent and Non-controlling interest		(29,403)	(29,547)
Proceeds from loans and other borrowings	4.4.2.2	101,310	59,793
Repayment of loans and other borrowings	4.4.2.2	(169,042)	(96,767)
Repayment of other financial liabilities	4.4.2.3	(7,485)	(5,988)
Treasury share purchase		(2,139)	(1,822)
Net cash used in financing activities from continuing operations		(106,759)	(74,331)
Net cash inflow from financing activities from discontinued operations		2,041	-
Net cash used in financing activities		(104,718)	(74,331)
Exchange differences on cash and cash equivalents from continuing operations		(15)	130
Exchange differences on cash and cash equivalents from discontinued operations		-	-
Change in cash and cash equivalents		(5,406)	1,805
Cash and cash equivalents, beginning of year		10,805	5,399
Cash and cash equivalents, end of year	4.2.1	5,399	7,204

The accompanying notes form an integral part of these consolidated financial statements.

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

	pieces	In HUF millions									
			Capital reserves				Accumulated Other Comprehensive Income				
	Shares of common stock (a)	Common stock (a)	Additional paid in capital (b)	Reserve for equity settled share based transactions (c)	Treasury stock (d)	Retained earnings (e)	Cumulative translation adjustment (f)	Revaluation reserve for AFS financial assets – net of tax (g)	Equity of the owners of the parent	Non-controlling interests (h)	Total Equity
Balance at December 31, 2016	1,042,742,543	104,275	27,379	511	(825)	375,660	31,521	(31)	538,490	42,843	581,333
Dividend declared to Owners of the parent (i)						(26,067)			(26,067)	–	(26,067)
Dividend declared to Non-controlling interests (j)									–	(3,320)	(3,320)
Equity settled share based transactions (c)				(608)	777				169	–	169
Treasury share purchase (k)					(2,139)				(2,139)	–	(2,139)
Disposal of subsidiaries (l)									–	(6,743)	(6,743)
Transactions with owners in their capacity as owners		–	–	(608)	(1,362)	(26,067)	–	–	(28,037)	(10,063)	(38,100)
Other Comprehensive income							(9,995)	10	(9,985)	(2,947)	(12,932)
Profit or loss						46,727			46,727	3,045	49,772
Total Comprehensive Income		–	–	–	–	46,727	(9,995)	10	36,742	98	36,840
Balance at December 31, 2017	1,042,742,543	104,275	27,379	(97)	(2,187)	396,320	21,526	(21)	547,195	32,878	580,073
Adoption of new standards (IFRS 9, IFRS 15) (m)						15,724			15,724	671	16,395
Revised balance at January 1, 2018	1,042,742,543	104,275	27,379	(97)	(2,187)	412,044	21,526	(21)	562,919	33,549	596,468
Dividend declared to Owners of the parent (i)						(26,068)			(26,068)	–	(26,068)
Dividend declared to Non-controlling interests (j)									–	(3,482)	(3,482)
Equity settled share based transactions (c)				(19)	18				(1)	–	(1)
Treasury share purchase (k)					(1,822)				(1,822)	–	(1,822)
Transactions with owners in their capacity as owners		–	–	(19)	(1,804)	(26,068)	–	–	(27,891)	(3,482)	(31,373)
Other Comprehensive income							2,021	124	2,145	1,243	3,388
Profit or loss						43,318			43,318	3,131	46,449
Total Comprehensive Income		–	–	–	–	43,318	2,021	124	45,463	4,374	49,837
Balance at December 31, 2018	1,042,742,543	104,275	27,379	(116)	(3,991)	429,294	23,547	103	580,491	34,441	614,932
Of which treasury stock	(8,836,348)										
Shares of common stock outstanding at December 31, 2018	1,033,906,195										

The accompanying notes form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(a) The total amount of issued shares of common stock of 1,042,742,543 (each with a nominal value of HUF 100) is fully paid as at December 31, 2018. The number of authorized ordinary shares on December 31, 2018 is 1,042,742,543.

Voting Rights and Voting

The holder of each Series "A" ordinary share shall be entitled to one vote at the General Meeting of the Company. The names of shareholders and nominees who intend to participate at the General Meeting shall be registered in the Share Register on the second working day prior to the starting date of the General Meeting. The General Meeting shall adopt its resolutions by a simple majority vote except for resolutions on issues listed in the Articles of Associations, which shall require at least a three-quarters majority of the votes cast. There is no limitation on the rights of non-resident or foreign shareholders to hold or exercise voting rights on the ordinary shares. There is no limitation of voting rights for ordinary shares in the Articles of Association. The Company has no shares assigned with special management rights.

Transfer of Shares

For the transfer of dematerialized share a contract for transfer or other legal title is required and, in that context, the transferor's securities account shall be debited and the new holder's securities account shall be credited with the transferred dematerialized shares. The holder of dematerialized share shall be considered the holder of the securities account on which the dematerialized shares are recorded.

The transfer of any Series "A" ordinary shares is not bound to any restriction or attainment of agreement.

(b) Additional paid in capital represents the amount above the nominal value of the shares that was received by the Company during capital increases.

(c) Reserve for equity settled share based transactions includes the compensation expenses accrued in this reserve related to share settled compensation programs. See also Note 20.1.2.

(d) Treasury stock represents the cost of the Company's own shares repurchased. When the Company or its subsidiaries purchase the Company's equity shares, the consideration transferred including any attributable incremental external costs are deducted from the Equity of the owners of the parent as Treasury stock until they are re-sold or cancelled. When such shares are subsequently sold, the treasury share balance decreases by the original cost of the shares, thereby increasing equity, while any gains or losses are also recognized in equity (Retained earnings). Treasury stock transactions are recorded on the transaction date.

(e) Retained earnings include the accumulated and undistributed profit of the Group. The distributable reserves of the Company under Hungarian law (Section 5 (b) 114/B of Act C of 2000 on Accounting relating to untied retained earnings available for the payment of dividends) at December 31, 2018 amounted to approximately HUF 450 billion (HUF 424 billion at December 31, 2017).

(f) Cumulative translation adjustment represents the foreign exchange differences arising on the consolidation of foreign subsidiaries.

(g) Revaluation reserve for available-for-sale (AFS) financial assets includes the unrealized gains and losses net of tax on available-for-sale financial assets. Magyar Telekom reclassified all equity instruments previously recognized as available-for-sale financial assets to the IFRS 9 category at fair value through other comprehensive income as at January 1, 2018. (See also Note 4.5.1.)

(h) Non-controlling interests represent the Non-controlling shareholders' share of the net assets of subsidiaries in which the Group has less than 100% ownership (Note 16).

(i) Dividends payable to the Company's shareholders and to Non-controlling shareholders of the Group's subsidiaries are recorded as a liability and debited against equity (Retained earnings or Non-controlling interests) in the Group's financial statements in the period in which the dividends are approved by the shareholders.

(j) The amount of dividends declared to Non-controlling interests includes predominantly the dividends declared to the Non-controlling owners of Makedonski Telekom (MKT) and the Group's subsidiaries.

(k) In 2018 Magyar Telekom Plc. purchased 4,251,418 ordinary shares for the purpose of the new employee incentive program (Note 20.1.2.5). In 2017 Magyar Telekom Plc. purchased 4,534,758 ordinary shares for the purpose of the new employee incentive program (Note 20.1.2.5). In 2016 Magyar Telekom Plc. purchased 1,252,616 ordinary shares for the purpose of the Employee Share Ownership Program (ESOP) (Note 20.1.2.4), of which the ESOP sold 25,764 shares due to the revision of the number of the participants in the program. These share transactions were carried out on the Budapest Stock Exchange through UniCredit Bank Hungary Zrt., as investment service provider.

(l) In January 2017, the Company signed a share purchase agreement with Hrvatski Telekom d.d. for the sale of the total of its 76.53% shareholding in Crnogorski Telekom A.D.. Details of the disposal are disclosed in Note 26.2.1.

(m) As of January 1, 2018, the Group adopted IFRS9 and IFRS15. Details of the adoption are disclosed in Notes 1.3 and 2.1.1.

Together with the approval of these financial statements for issue, the Board of Directors of the Company proposes a dividend distribution in total HUF 26,068 million to be approved by the Annual General Meeting of the Company in April 2019. In 2018 Magyar Telekom Plc. paid in total HUF 26,068 million dividend.

The accompanying notes form an integral part of these consolidated financial statements.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

1 GENERAL INFORMATION

1.1 About the Company

Magyar Telekom Telecommunications Public Limited Company (the Company or Magyar Telekom Plc.) with its subsidiaries form Magyar Telekom Group (Magyar Telekom or the Group). Magyar Telekom is the principal provider of telecommunications services in Hungary and Macedonia and alternative service provider in Bulgaria and Romania. These services are subject to various telecommunications regulations depending on the countries of operations (Note 34).

The Company was incorporated in Hungary on December 31, 1991 and commenced business on January 1, 1992. The Company's registered seat is Könyves Kálmán krt. 36., 1097 Budapest, Hungary since November 1, 2018. Name of the Court of Registration and the registration number of the Company: Metropolitan Court as Court of Registration, Cg. 01-10-041928.

Magyar Telekom Plc. is listed on the Budapest Stock Exchange and its shares are traded on the Budapest Stock Exchange. Magyar Telekom's American Depository Shares (ADSs) each representing five ordinary shares were also traded on the New York Stock Exchange until November 12, 2010, when the ADSs were delisted. Magyar Telekom terminated the registration of its shares and ADSs in the US in February 2012. The Company maintains its American Depositary Receipt program on a Level I basis.

The ultimate controlling parent of Magyar Telekom is Deutsche Telekom AG (DT or DTAG) who fully consolidates Magyar Telekom Group. Deutsche Telekom Europe B.V. (Stationsplein 8, 6221 BT Maastricht, the Netherlands), a member of the Deutsche Telekom Group, is the direct owner of 59.21% of the Company's issued shares and voting rights. The consolidated financial statements of DT AG are available at DT AG's website (www.telekom.com/en), while those of Magyar Telekom Group are available at its registered office and on its corporate website.

The consolidated financial statements are prepared and presented in millions of Hungarian Forints (HUF), unless stated otherwise.

The Company's Board of Directors (the Board) accepted the submission of these consolidated financial statements of the Company on February 20, 2019 to the Annual General Meeting (AGM) of the owners, which is authorized to approve these financial statements, but also has the right to require amendments before approval. As the controlling shareholders are represented in the Board of the Company that accepted the submission of these financial statements, the probability of any potential change required by the AGM is extremely remote, and has never happened in the past.

Magyar Telekom Plc.'s corporate website is: www.telekom.hu

1.2 Composition of the Group

At December 31, 2017 and 2018 the principal operating subsidiaries of the Group were as follows:

Subsidiaries	Group interest in capital as at December 31,		Activity
	2017	2018	
Incorporated in Hungary:			
T-Systems Magyarország Zrt., Budapest........................	100.00%	100.00%	System integration and IT services
KalászNet Kft., Budapest..	100.00%	100.00%	Telecom service provider
Telekom New Media Zrt., Budapest	100.00%	100.00%	Interactive service provider of telecommunications applications
Incorporated in Macedonia:			
Makedonski Telekom A.D., Skopje (MKT)	56.67%	56.67%	Telecom service provider
Stonebridge A.D., Skopje	100.00%	100.00%	Holding company
Incorporated in Romania:			
Combridge S.R.L., Bucharest	100.00%	100.00%	Wholesale telecom service provider
Incorporated in Bulgaria:			
Novatel EOOD, Sofia..	100.00%	100.00%	Wholesale telecom service provider

At December 31, 2017 and 2018 the joint ventures of the Group were as follows:

Joint ventures	Group interest in capital as at December 31,		Activity
	2017	2018	
Incorporated in Hungary:			
E2 Hungary Zrt., Budapest	50.00%	50.00%	Energy services to business customers

The Group's interest in the capital of the above subsidiaries equals the voting rights therein. There is no significant entity in the Group that is not controlled even though more than half of the voting rights are held. There is one structured entity in the Group that is fully consolidated, see Note 20.1.2.5.

All subsidiary undertakings are included in the consolidation.

1.3 Financial information – impact of the adoption of IFRS 9 and IFRS 15

As a major change compared to 2017, the Group adopted IFRS 9 and IFRS 15 as of January 1, 2018. The following tables show the amounts by which each financial statement line item is affected in 2018 due to the application of the new standards. We show the impact of IFRS 9 and IFRS 15 accounting standards together since that of IFRS 9 accounting standard is not significant. For further details please see Note 2.1.1. 2018 figures are presented in accordance with the new standards in the Notes to the Consolidated Financial statements, while the 2017 comparatives are presented as in the previous year in accordance with IFRS 9 and IFRS 15 transition requirements.

The tables below show the impacts of these on the 2018 Consolidated Statement of financial position and Consolidated Statement of profit or loss and other comprehensive income for the year ended December 31, 2018. As the impacts appear in a separate line in the Consolidated Statement of Changes in Equity, this is not presented here. As these changes had no impact on the Consolidated Statement of cash flows, this is not presented here either.

The column Catch-up & reclass of IFRS 9 & IFRS 15 includes the accumulated effect of the first-time application of IFRS 9 and IFRS 15 together with the related reclassifications that were required by these standards at the adoption date, i.e. as of January 1, 2018. The column IFRS 9 & IFRS 15 effects includes the impact resulting from the application of IFRS 9 and IFRS 15 throughout 2018. Other changes include the changes resulting from the usual business operations of the Group.

(in HUF millions)	At December 31, 2017	Catch-up & reclass of IFRS 9 & IFRS 15	At January 1, 2018	IFRS 9 & IFRS 15 effects	Other changes	At December 31, 2018
ASSETS						
Current assets						
Cash and cash equivalents	5,399	-	5,399	-	1,805	7,204
Trade receivables and other assets	157,745	9,467	167,212	508	27,500	195,220
Thereof: Contract assets	-	14,286	14,286	508	3,026	17,820
Other current financial assets	8,162	-	8,162	-	3,469	11,631
Current income tax receivable	384	(339)	45	-	209	254
Inventories	17,175	-	17,175	-	1,943	19,118
	188,865	9,128	197,993	508	34,926	233,427
Assets held for sale	162	-	162	-	(162)	-
Total current assets	189,027	9,128	198,155	508	34,764	233,427
Non current assets						
Property, plant and equipment	458,343	-	458,343	-	(15,196)	443,147
Intangible assets	441,458	-	441,458	-	6,494	447,952
Investments in associates and joint ventures	1,324	-	1,324	-	69	1,393
Deferred tax assets	59	(43)	16	-	61	77
Other non current financial assets	19,323	3,365	22,688	195	2,102	24,985
Thereof: Contract assets	-	3,365	3,365	195	-	3,560
Other non current assets	127	5,507	5,634	(975)	356	5,015
Thereof: Contract costs	-	5,507	5,507	(975)	-	4,532
Total non current assets	920,634	8,829	929,463	(780)	(6,114)	922,569
Total assets	1,109,661	17,957	1,127,618	(272)	28,650	1,155,996

(in HUF millions)	At December 31, 2017	Catch-up & reclass of IFRS 9 & IFRS 15	At January 1, 2018	IFRS 9 & IFRS 15 effects	Other changes	At December 31, 2018
LIABILITIES						
Current liabilities						
Financial liabilities to related parties	35,191	-	35,191	-	75,953	111,144
Other financial liabilities	8,757	(64)	8,693	-	535	9,228
Trade payables	135,446	-	135,446	-	39,866	175,312
Current income tax payable	324	356	680	-	(337)	343
Provisions	3,267	-	3,267	-	151	3,418
Other current liabilities	43,596	(178)	43,418	(74)	(1,949)	41,395
Thereof: Contract liabilities	-	11,265	11,265	(74)	1,181	12,372
	226,581	114	226,695	(74)	114,219	340,840
Liabilities associated with assets held for sale	-	-	-	-	-	-
Total current liabilities	226,581	114	226,695	(74)	114,219	340,840
Non current liabilities						
Financial liabilities to related parties	231,646	-	231,646	-	(108,297)	123,349
Other financial liabilities	47,608	-	47,608	-	311	47,919
Deferred tax liabilities	13,743	1,393	15,136	-	2,110	17,246
Provisions	9,231	-	9,231	-	2,034	11,265
Other non current liabilities	779	55	834	(54)	(335)	445
Thereof: Contract liabilities	-	520	520	(54)	(38)	428
Total non current liabilities	303,007	1,448	304,455	(54)	(104,177)	200,224
Total liabilities	529,588	1,562	531,150	(128)	10,042	541,064
EQUITY						
Equity of the owners of the parent						
Common stock	104,275	-	104,275	-	-	104,275
Capital reserves	27,282	-	27,282	-	(19)	27,263
Treasury stock	(2,187)	-	(2,187)	-	(1,804)	(3,991)
Retained earnings	396,320	15,724	412,044	(256)	17,506	429,294
Accumulated other comprehensive income	21,505	-	21,505	128	2,017	23,650
Total Equity of the owners of the parent	547,195	15,724	562,919	(128)	17,700	580,491
Non-controlling interests	32,878	671	33,549	(16)	908	34,441
Total equity	580,073	16,395	596,468	(144)	18,608	614,932
Total liabilities and equity	1,109,661	16,736	1,126,397	(272)	29,871	1,155,996

The table below shows the above impact on the 2018 Consolidated Statement of profit or loss and other comprehensive income. In order to present comparable data of the Consolidated Statement of profit or loss, 2018 figures are also shown under IAS 18 and IAS 11 in the table below.

(in HUF millions, except per share amounts)	2017 IAS 18 / IAS 11	2018 IAS 18 / IAS 11	2018 Effects of IFRS9 & IFRS15	2018 IFRS9 & IFRS15
Revenues	610,851	655,104	2,000	657,104
Direct costs	(245,777)	(284,912)	(2,019)	(286,931)
Employee related expenses	(80,240)	(82,789)	(179)	(82,968)
Depreciation and amortization	(108,174)	(115,529)	-	(115,529)
Other operating expenses	(105,918)	(103,842)	(73)	(103,915)
Operating expenses	(540,109)	(587,072)	(2,271)	(589,343)
Other operating income	6,746	9,217	-	9,217
Operating profit	77,488	77,249	(271)	76,978
Interest income	543	363	-	363
Interest expense	(13,525)	(13,423)	-	(13,423)
Other finance expense - net	(8,645)	(4,724)	-	(4,724)
Net financial result	(21,627)	(17,784)	-	(17,784)
Share of associates' and joint ventures' loss	343	588	-	588
Profit before income tax	56,204	60,053	(271)	59,782
Income tax	(15,958)	(13,333)	-	(13,333)
Profit for the year from continuing operations	40,246	46,720	(271)	46,449
Profit for the year from discontinued operations	9,526	-	-	-
Profit for the year	49,772	46,720	(271)	46,449
Other comprehensive income (Items that are or may be reclassified subsequently to profit or loss):				
Exchange differences on translating foreign operations	(439)	3,041	128	3,169
Revaluation of available-for-sale financial assets	19	219	-	219
Other comprehensive income for the year from continuing operations	(420)	3,260	128	3,388
Other comprehensive income for the year from discontinued operations	(12,512)	-	-	-
Other comprehensive income for the year	(12,932)	3,260	128	3,388
Total comprehensive income for the year from continuing operations	39,826	49,980	(143)	49,837
Total comprehensive income for the year from discontinued operations	(2,986)	-	-	-
Total comprehensive income for the year	36,840	49,980	(143)	49,837

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(in HUF millions, except per share amounts)	2017 IAS 18 / IAS 11	2018 IAS 18 / IAS 11	2018 Effects of IFRS9 & IFRS15	2018 IFRS9 & IFRS15
Profit attributable to:				
Owners of the parent	46,727	43,574	(256)	43,318
From continuing operations	37,239	43, 574	(256)	43,318
From discontinued operations	9,488	-	-	-
Non-controlling interests	3,045	3,146	(15)	3,131
From continuing operations	3,007	3,146	(15)	3,131
From discontinued operations	38	-	-	-
	49,772	46,720	(271)	46,449
Total comprehensive income attributable to:				
Owners of the parent	36,742	45,590	(127)	45,463
From continuing operations	36,948	45, 590	(127)	45,463
From discontinued operations	(206)	-	-	-
Non-controlling interests	98	4,390	(16)	4,374
From continuing operations	2,878	4,390	(16)	4,374
From discontinued operations	(2,780)	-	-	-
	36,840	49,980	(143)	49,837
Earnings per share (EPS) information:				
Profit attributable to the owners of the Company	46,727	43,574	(256)	43,318
From continuing operations	37,239	43,574	(256)	43,318
From discontinued operations	9,488	-	-	-
Weighted average number of common stock outstanding (thousands) used for basic EPS	1,040,073	1,035,394	-	1,035,394
Average number of dilutive share options	4,585	6,074	-	6,074
Weighted average number of common stock outstanding (thousands) used for diluted EPS	1,044,658	1,041,468	-	1,041,468
Basic earnings per share (HUF)	44.93	42.09	(0.25)	41.84
From continuing operations	35.82	42.09	(0.25)	41.84
From discontinued operations	9.11	-	-	-
Diluted earnings per share (HUF)	44.93	41.84	(0.25)	41.59
From continuing operations	35.82	41.84	(0.25)	41.59
From discontinued operations	9.11	-	-	-

2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

2.1 Basis of preparation

The consolidated financial statements of Magyar Telekom have been prepared in accordance with International Financial Reporting Standards (IFRS) as endorsed by the European Union (EU). All standards and interpretations endorsed by the EU effective as at December 31, 2018 and applicable to Magyar Telekom had been adopted. These consolidated financial statements also comply with the Hungarian Accounting Act on consolidated financial statements, which refers to the IFRS as endorsed by the EU.

The consolidated financial statements are presented in millions of HUF unless stated otherwise.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Group's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the consolidated financial statements, are disclosed in Note 3.

2.1.1 Standards, significant amendments and interpretations effective and adopted by the Group in 2018

Title of standard	Nature of change	Impact on consolidated financial statements
IFRS 9 Financial Instruments	IFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities and introduces new rules for hedge accounting. In December 2011, in November 2013 and in July 2014, the IASB amended the standard in order to make further changes to the classification and measurement rules and also introduced a new impairment model. These latest amendments completed the new financial instruments standard.	The adoption of the new standard and its amendments did not result in material changes in the consolidated financial statements of the Group. The new provisions on the classification of financial assets gave rise to changes in measurement and presentation of certain debt instruments failing to meet the" solely payments of principal and interest" (SPPI) criterion. On January 1, 2018 (the date of initial application of IFRS 9), Magyar Telekom Group's management assessed which business models apply to the financial assets held by the group and classified its financial instruments into the appropriate IFRS 9 categories. The effects resulting from this reclassification are disclosed in Note 4. From 1 January 2018, the Group classifies its financial assets in the following measurement categories: ▪ those to be measured subsequently at fair value (either through OCI, or through profit or loss), and ▪ those to be measured at amortised cost. The classification depends on the entity's business model for managing the financial assets and the contractual terms of the cash flows. For assets measured at fair value, gains and losses will either be recorded in profit or loss or OCI. At initial recognition, the Group measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVTPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVTPL are expensed in profit or loss. The new provisions on the accounting for impairment losses led to expected losses having to be expensed earlier in case of trade receivables. Application of the simplified approach for financial assets with a significant financing component also led to a minor increase in impairment losses (HUF 0.8 billion). The impairment

		losses on contract assets recognized for the first time as of January 1, 2018 in accordance with IFRS 15 is disclosed within the effects of IFRS 15. The cumulative effect arising from the transition is recognized as adjustment to the opening balance of equity in the year of initial application. Prior-year comparatives are not adjusted.
Title of standard	**Nature of change**	**Impact on consolidated financial statements**

IFRS 15 Revenue from Contracts with Customers	The core principle of the new standard is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration (that is, payment) to which the company expects to be entitled in exchange for those goods or services. The new standard also resulted in enhanced disclosures about revenue, provides guidance for transactions that were not previously addressed comprehensively (for example, service revenue and contract modifications) and new guidance for multiple-element arrangements.	The adoption of the new standard resulted in significant changes to the financial statements of the Group, primarily in respect of the timing of revenue recognition and in respect of capitalization of costs of obtaining a contract with a customer and contract fulfilment costs.
		
		▪ Magyar Telekom applied the modified retrospective method, i.e., contracts that were not completed by January 1, 2018 were accounted for as if they had been recognized in accordance with IFRS 15 from the very beginning. The cumulative effect arising from the transition (catch-up) was recognized as an adjustment to the opening balance of Retained earnings in 2018. Prior-year comparatives were not adjusted; however, an explanation of the reasons for the changes in items in the consolidated statement of financial position and the consolidated statement of profit or loss and other comprehensive income for the current period are provided as a result of applying IFRS 15 for the first time. The effects were analyzed in a Group-wide project on implementation of the new standard. The changeover to the new standard resulted in a cumulative increase in retained earnings of HUF 19 billion before taxes. As a consequence, HUF 2 billion income tax arose. This effect was mainly attributable to the first-time recognition of
		    ▪ Contract assets (HUF 18 billion including also reclassifications of HUF 5 billion that resulted mainly from construction contract receivables under IAS 11 and the discount given to customers of unbilled receivables under IAS 18) that, under IFRS 15, led to the earlier recognition of revenue from the sale of goods and merchandise, and
		    ▪ Deferred customer acquisition costs (HUF 6 billion) that, under IFRS 15, resulted in the later recognition of selling expenses.
		▪ As regards to the new standard's impact on the Consolidated Statement of profit or loss and other comprehensive income, Magyar Telekom's share of overall revenue from the provision of services decreased, whilst the overall share of revenue from the sale of goods and merchandise increased . As described, IFRS 15 means revenue is recognized earlier and expenses are recognized later for contracts not yet completed by January 1, 2018. However, as the accounting effects of the changeover to the new standard were recognized directly in equity, the only effects on the Consolidated Profit or Loss and Other Comprehensive Income in 2018 were related to changes in the point in time at which revenue and expenses are realized. On the assumption that business development remains unchanged, this means for a mass market characterized by a large number of

		customer contracts that are being concluded at different points in time the following: ▪ For existing contracts, lower service revenues and higher selling expenses from the amortization of capitalized contract assets and customer acquisition costs are largely compensated for by higher revenue, on the conclusion of new contracts, from the sale of goods and lower selling expenses from the capitalization of contract assets and customer acquisition costs. Compared with the previous accounting method, major effects on earnings thus arise only if business development changes, for example, if volumes or prices change or if there are changes to business models or products offered. ▪ In the case of multiple-element arrangements (e.g., mobile contract plus handset) with subsidized products delivered in advance, a larger portion of the total consideration is attributable to the component delivered in advance (mobile handset), requiring earlier recognition of revenue. This lead to the recognition of what is known as a contract asset – a receivable arising from the customer contract that has not yet legally come into existence – in the Consolidated Statement of Financial Position. ▪ On first-time application of the standard, both total assets and shareholders' equity increased due to the capitalization of contract assets and customer acquisition costs. ▪ Later recognition of revenue is required in cases where "material rights" are granted, such as offering additional discounts for future purchases of further products. ▪ Contract liabilities (which, as deferred revenue, were already recognized as liabilities in the past and with the transition reclassified) are now netted off against the contract assets for each customer contract. ▪ For the purposes of determining whether Magyar Telekom sells products for its own account (principal = gross revenue) or for the account of others (agent = net revenue), there was no material change. ▪ A significant financing component is not considered for the amount and timing of revenue recognition if the period between when a promised good or service is transferred to the customer and when the customer pays for that good or service will be one year or less. Accounting policies of subsidiaries have been adjusted to ensure consistency with the policies adopted by the Group.

2.1.2 Standards, amendments and interpretations that are not yet effective and have not been early adopted by the Group

Certain new accounting standards, interpretations and their amendments have been published that are not mandatory for reporting periods ending December 31, 2018 and have not been early adopted by the Group. The Group's assessment of the impact of these new standards and interpretations is set out below.

Title of standard	Nature of change	Impact on consolidated financial statements	Application date and EU endorsement
IFRS 16 Leases	IFRS 16 requires entities when they are a lessee, to ▪ recognize a right-of-use asset representing its right to use the underlying leased asset and a lease liability representing its obligation to make lease payments on the statement of financial position, initially measured at the present value of non-cancellable lease payments (including inflation-linked payments), and payments to be made in optional periods if the lessee is reasonably certain to exercise an option to extend the lease; ▪ recognize amortization of right-of-use assets and interest on lease liabilities over the lease term; and ▪ separate the total amount of cash paid into a principal portion (presented within financing activities) and interest (presented within operating activities) in the statement of cash flows.	Magyar Telekom applied the modified retrospective approach. The Group mainly leases cell sites, rooftops, office buildings and retail shops, network assets, space on masts or towers and cars that will be affected by the new standard. IFRS 16 standard will have a significant effect on the consolidated financial statements and introduces a single lease accounting model by taking right-of-use assets and lease liabilities on the balance sheet. The transitional effect on both right-of-use assets and lease liabilities will be in the range of HUF 92.7 and 114.3 billion (excluding the finance leases recognized as at December 31, 2018 under IAS 17, prior to the transition). As a result of adopting IFRS 16, the 2018 operating lease expenses will be presented as depreciation and interest expense from January 1, 2019. For the agreements already concluded by the end of 2018, the transition effect on profit or loss is expected to be between HUF 17.1 and 20.9 billion in 2019 that includes the depreciation and interest expense excluding the leases which were previously accounted for as finance leases under IAS 17. Details of the Group's leases (including lease commitments) are disclosed in Note 17. On the lessor side, MT Group mainly analyzes the revised definition of leases including the head and sublease constructions. Other than that, MT Group does not expect a considerable impact on the financial statements of the Group at this time, as lessor accounting itself is not changing significantly through the introduction of IFRS 16. Regarding the transition to IFRS 16, MT Group decided: ▪ not to apply the practical expedient in IFRS 16.C3 ("Grandfathering approach"). As a result, a re-assessment was performed whether existing contracts are or contain a lease at the date of initial application, i.e. as of January 1, 2019. ▪ not to use the low value exemption, ▪ to apply a single discount rate to a portfolio of leases with reasonably similar characteristics (such as leases with a similar remaining lease term for a similar class of underlying asset in a similar economic environment) as a lessee, ▪ not to apply the practical expedient regarding short-term leases except for some minor and insignificant lease arrangements with a lease term of one month or less, ▪ to use hindsight such as in determining the lease term if the contract contains options to extend or terminate the lease.	An entity is required to apply IFRS 16 for annual periods beginning on or after 1 January 2019 and permits to apply the new Leases Standard early, if the entity also applies IFRS 15 Revenue from Contracts with Customers at or before the date of early application. The European Union has endorsed this standard.

There are no other standards or amendments that are not yet effective and that would be expected to have a material impact on the Group in the current or future reporting periods and on foreseeable future transactions.

2.2 Consolidation

2.2.1 Subsidiaries

Subsidiaries are entities controlled by the Group. The Group controls an entity when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The financial statements of subsidiaries are included in the consolidated financial statements from the date on which control commences until the date on which control ceases.

The existence and effect of potential voting rights that are presently exercisable or presently convertible are also considered when assessing whether the Group controls another entity.

Subsidiaries are consolidated from the date on which control is transferred to the Group, and are no longer consolidated from the date control ceases. The acquisition method of accounting is used to account for business combinations. The cost of an acquisition is measured as the fair value of the assets given up, shares issued or liabilities undertaken at the date of acquisition whereby costs directly attributable to the acquisition are expensed. The excess of the cost of acquisition over the fair value of the net assets and contingent liabilities of the subsidiary acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognized in the Profit for the year (Other operating income).

If applicable, the Group recognizes at the acquisition date a liability for any contingent purchase consideration. If the amount of contingent consideration accounted for as a liability changes as a result of a post-acquisition event (such as meeting an earnings target), it is recognized in accordance with other applicable IFRSs as appropriate rather than as an adjustment of goodwill.

As for the measurement of non-controlling interest, the Group may recognize 100% of the goodwill of the acquired entity, not only the Group's portion of the goodwill. This is elected on a transaction-by-transaction basis. The Group attributes their share of losses to the non-controlling interests even if this results in the non-controlling interests having a deficit balance.

In a step acquisition, the fair values of the acquired entity's assets and liabilities, including goodwill, are measured on the date when control is obtained. Accordingly, goodwill is measured as the difference at the acquisition date between the fair value of any investment the business held before the acquisition, the consideration transferred and the fair value of the net asset acquired and non-controlling interest is recorded at fair value when the Group elects the fair value option.

In case of acquisitions where the transaction takes place between companies under common control (i.e. with other Deutsche Telekom Group companies), the transaction is recorded at the carrying amounts as recorded in the selling owner's accounts, and any gains, losses or differences between the carrying amount and the sale-purchase price are recognized in Retained earnings. The consolidated financial statements include the results of subsidiaries acquired from parties under common control from the date of the closing of the transaction.

A partial disposal of an investment in a subsidiary while control is retained is accounted for as an equity transaction with owners, therefore gain or loss is not recognized in profit or loss for such disposals.

A partial disposal of an investment in a subsidiary that results in loss of control triggers re-measurement of the residual interest to fair value. Any difference between fair value and carrying amount is a gain or loss on the disposal, recognized in profit or loss (Other income).

Inter-company transactions, balances and unrealized gains or losses on transactions between the Magyar Telekom Group companies are eliminated. Accounting policies of subsidiaries have been adjusted to ensure consistency with the policies adopted by the Group.

There is one structured entity in the Group that is fully consolidated, see Note 20.1.2.5.

2.3 Foreign currency translation

2.3.1 Functional and presentation currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment in which the entity operates (the functional currency).

The consolidated financial statements are presented in millions of HUF, as the Group's presentation currency is the Hungarian Forint.

2.3.2 Transactions and balances

Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognized in the Profit for the year (Other finance expense – net).

2.3.3 Group companies

The income and financial position of all of the Group's entities (none of which has the currency of a hyperinflationary economy) that have a functional currency different from the presentation currency are translated into the presentation currency as follows:

- For the initial consolidation of foreign subsidiaries acquired, their assets and liabilities at the acquisition date are incorporated into the consolidated financial statements after translating the balances into HUF using the exchange rate prevailing at the date of acquisition. The fair value adjustments resulting from the purchase price allocation and goodwill are accounted for in HUF for acquisitions before March 31, 2004, after which date these adjustments arising on consolidation are accounted for in the functional currency of the subsidiary.
- Assets and liabilities for each Statement of financial position presented are translated at the closing rate at the date of that Statement of financial position.
- Items of Profit or loss and other comprehensive income are translated at annual cumulated average exchange rates.
- All resulting exchange differences are recognized in the consolidated equity (Cumulative translation adjustment). When a foreign operation is fully or partially disposed of so that control is given up, exchange differences that were recorded in equity until the date of the sale are recognized in the Profit for the year as part of the gain or loss on sale (Other operating income).

2.4 Comparative information

In order to maintain consistency with the current year presentation in the Financial statements and the Notes thereto, certain items have been reclassified for comparative purposes. Material changes in disclosures, if any, are described in detail in the relevant notes.

3 CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the prevailing circumstances. The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, rarely equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities are outlined below.

3.1 Useful lives of assets

The determination of the useful lives of assets is based on historical experience with similar assets as well as any anticipated technological development and changes in broad economic or industry factors. The appropriateness of the estimated useful lives is reviewed annually, or whenever there is an indication of significant changes in the underlying assumptions. We believe that this is a critical accounting estimate since it involves assumptions about technological development in an innovative industry and heavily dependent on the investment plans of the Group. Further, due to the significant weight of depreciable assets in our total assets, the impact of any changes in these assumptions can be material to our financial position, and results of operations. As an example, if Magyar Telekom was to shorten the average useful life of its assets by 10%, this would result in additional annual depreciation and amortization expense of approximately HUF 13 billion (2017: HUF 12 billion). See Notes 9 and 10 for the changes made to useful lives in 2018.

The Group constantly introduces a number of new services or platforms including, but not limited to, the 3G and 4G based broadband services in the mobile communications and the fiber-to-the-home rollout in the fixed line operations. In case of the introduction of such new services, the Group conducts a revision of useful lives of the already existing platforms, but in the vast majority of the cases these new services or assets are designed to co-exist with the existing platforms, resulting in no change-over to the new technology. Consequently, the useful lives of the existing platforms usually do not require shortening.

3.2 Estimated impairment of goodwill

Goodwill is not amortized, but tested for impairment annually or more frequently. The recoverable amounts of the operating segments are calculated based on fair value less cost to sell determined by the discounted projected cash flows of the operating segments over the next ten years with a terminal value. This is highly judgmental, which carries the inherent risk of arriving at materially different recoverable amounts if estimates used in the calculations proved to be inappropriate. The Group has an implemented policy to make the impairment test based on a 10-year cash flow projection on reasonable and supportable assumptions that present the management's best estimate on market participants' assumptions and expectations. We use 10 year cash flow projections as the payback period of our investments in the telecommunications operations often exceeds 5 years.

In order to determine the recoverable amounts of the operating segments, the Group calculates the operating segments' fair values less cost to sell. In the calculations, Magyar Telekom uses a range of weighted average cost of capital (WACC) and estimated perpetual growth rate (PGR) depending on the country of operations and the characteristics of the markets the Group's segments operate in. The WACCs are determined based on CAPM (capital asset pricing model) using the average betas of the peer group, 10 year zero coupon yields and a debt ratio in line with the usual indebtedness of listed peer telecommunications companies, while the PGRs used are in line with the long-term average growth rate for the particular segment.

Costs of certain central functions that are not cross charged are also considered in the fair value calculations, when conducting the goodwill impairment tests. The costs of these central functions are allocated to the operating segments based on the segments' revenue share of the Group's total revenue.

Goodwill is allocated to the operating segments of the Group: MT-Hungary and Macedonia.

In 2018 and 2017, no goodwill had to be impaired. Details of the carrying amounts of goodwill allocated to the segments are in Note 10.4.

The tables below show the WACCs and PGRs used in the fair value calculations of the Group's operating segments for the goodwill impairment test conducted in 2018 and 2017. The tables below also include sensitivity analyses that show how much impairment would have been recognized as at December 31, 2018 or 2017 for the goodwill allocated to the operating segments if we changed the sensitive parameters in the calculations.

In 2018 we disclose what impact a 4 percentage point increase of the WACC would have on the goodwill. In case of the PGRs we disclose what impact a 9 percentage point decrease of the PGR would have on the goodwill. In case of the cash flow projections we disclose what impact a 20% or a 40% lower than projected cash flow stream would have on the goodwill.

2018	**MT-Hungary**	**Macedonia**
WACC		
Used in the calculation	7.85%	7.10%
If changed to	11.85%	11.10%
Potential impairment (HUF million)	69,029	5,739
PGR		
Used in the calculation	1.0%	1.0%
If changed to	-8.0%	-8.0%
Potential impairment (HUF million)	17,211	1,785
Cash-flow		
If changed by	-20%	-20%
Potential impairment (HUF million)	-	-
If changed by	-40%	-40%
Potential impairment (HUF million)	63,911	4,887

In 2017 we disclosed what impact a 4 percentage point increase of the WACC would have had on the goodwill. In case of the PGRs we disclosed what impact a 8 percentage point decrease of the PGR would have had on the goodwill. In case of the cash flow projections we disclosed what impact a 20% or a 40% lower than projected cash flow stream would have had on the goodwill.

2017	**MT-Hungary**	**Macedonia**
WACC		
Used in the calculation	6.39%	6.77%
If changed to	10.39%	10.77%
Potential impairment (HUF million)	-	7,095
PGR		
Used in the calculation	1.0%	1.0%
If changed to	-7.0%	-7.0%
Potential impairment (HUF million)	-	2,063
Cash-flow		
If changed by	-20%	-20%
Potential impairment (HUF million)	-	-
If changed by	-40%	-40%
Potential impairment (HUF million)	-	2,297

The table below shows what changes can be observed in the 10 year plans prepared in 2017 compared to those prepared in 2018.

	MT-Hungary	**Macedonia**
Cumulative average growth rate of revenues during the 10 years compared to 2018	0.4%	0.5%
Cumulative average growth rate of revenues during the 10 years compared to 2017	0.9%	0.3%
Cumulative average growth rate of EBITDA during the 10 years compared to 2018	1.3%	0.9%
Cumulative average growth rate of EBITDA during the 10 years compared to 2017	1.2%	1.3%
Cumulative average growth rate of Capex during the 10 years compared to 2018	(1.4%)	(1.4%)
Cumulative average growth rate of Capex during the 10 years compared to 2017	3.2%	(3.3%)

Magyar Telekom's management believes that preparing the value in use (VIU) calculation was unnecessary, since it would have resulted in a lower value than the FVLCS. The VIU method is assuming a model without future investments, meaning that additional capex and related revenues and gains to be recognized in the future cannot be considered in the calculations. Assuring the revenues on long term in a telecom business very much depends on future investments. In Magyar Telekom on average only approximately 20% of the capex spent in a year is related to maintenance. Others are new investments, also related to providing new connections to the network. It is obvious, that without this the revenue generation would start to decline sharply on a long term. Consequently, we did not prepare the value in use calculations for any of the segments.

3.3 Estimated impairment of trade and other receivables

We calculate impairment for accounts receivable based on estimated losses resulting from the inability of our customers to make required payments. The loss allowance is recognized in respect of not only losses already incurred as of the reporting date (incurred losses) but also losses which have not yet incurred as of the reporting date but which are expected to be incurred in the future (expected losses). For the largest customers and other telecommunications service providers, impairment is calculated on an individual basis, while for other customers it is estimated on a portfolio basis, for which we base our estimate on the aging of our accounts receivable balance and our historical write-off experience, customer credit-worthiness and recent and expected changes in our customer payment terms. These factors are reviewed annually, and changes are made to the calculations when necessary. In addition, we consider also the nature of the business (residential, business, fixed line, mobile, internet, cable TV, etc.) and the environment in which the Group's entities operate in the various markets. If the financial condition of our customers were to deteriorate, actual write-offs of currently existing receivables may be higher than expected and may exceed the level of the impairment losses recognized so far. The Group applied IFRS 9 from 2018. See also Notes 4 and 5.1.2.

3.4 Contracts with customers

From 2018 with the adoption of IFRS 15 the Group applies the guidance to a group of contracts with similar characteristics instead of to a single contract with a customer. The characteristics considered include mainly the business segment of the customer, business model of the contract, and whether the contract is committed or not.

Contract assets are recognized for unbilled amounts typically resulting from sales under long-term contracts when revenue recognized exceeds the amount billed to the customer in that period. This is a temporary difference so that revenue recognized and revenue billed are the same by the end of the commitment term. The amount of the contract assets is determined considering the estimated churn rate of the relevant group of contracts. The time frame for reclassification of contract assets to a receivable is the minimum contract term of the relevant group of contracts.

Furthermore, the Group recognizes assets for costs incurred in connection with the signing of customer contracts which would not have been incurred if the customer contract had not been concluded (contract costs). Capitalization is subject to the expectation that those costs will be recovered by future revenues resulting from the contract.

Costs of obtaining a contract with a customer generally include sales commissions both direct and indirect distribution channels. Capitalizing incremental costs of obtaining a contract does not only refer to contracts concluded with a new customer but also to contract renewals. Accounting treatment of acquisition and retention related contract costs is the same.

Costs of obtaining a contract with a customer are amortised on a portfolio basis over the period that the related goods or services are transferred to the customer which is

- based on historical customer retention data and past experiences in that business segment in case of uncommitted contracts (e. g. prepaid) and
- in case of committed contracts the commitment period is considered as amortisation period.

The Group decided not to use the practical expedient to expense incremental costs of obtaining a contract immediately which are amortized over a period of one year or less.

See Note 18.4 for the amount of contract assets, contract liabilities and contract costs as at December 31, 2018.

Under IAS 18 and IAS 11 until 2017 subscriber acquisition and retention costs primarily included the loss on the equipment sales and fees paid to subcontractors that acted as agents to acquire new customers or retain the existing subscribers. The Group's agents also spend a portion of their agent fees for marketing the Group's products, while a certain part of the Group's marketing costs could also be considered as part of the subscriber acquisition and retention costs. The up-front fees collected from customers for activation or connection were marginal compared to the incremental acquisition and retention costs. These revenues and costs were recognized when the customer was connected to the Group's fixed or mobile networks. No such costs or revenues were capitalized or deferred. These acquisition and retention costs (losses) were recognized immediately as they were not accurately separable from other marketing costs.

3.5 Annual fees of mobile licenses

Magyar Telekom's primary activities are the fixed line and mobile operations in Hungary and Macedonia. These services are in most cases regulated by these countries' laws or other legislations. These services in most cases require the acquisition of a license or concession, which usually requires a one-off fee and annual payments. It is judgmental whether we consider the annual fees to be reliably estimable or not. If we consider that we can reliably estimate these annual fees, the present value of those are capitalized as part of the cost of the license, otherwise these are recognized as costs in the period they relate to.

As the conditions of the new license contract concluded in Hungary in 2014 and 2013 (see Note 34.1) substantially changed compared to the old ones, in addition to the initial cost of the new frequencies in 2014 (HUF 59 billion) and the renewal of the old ones in 2013 (HUF 38 billion) we also recognized the discounted present value of the future annual license fees (HUF 39 billion in 2014 and HUF 17 billion in 2013).

In 2013 Magyar Telekom concluded an Authority Contract with the National Media and Infocommunications Authority (NMIAH) on the prolongation of the then existing 900 MHz and 1800 MHz frequencies until April, 2022. The Contract included provisions on lowering the annual fee of these and the 2100 MHz bands in the form of a legislation. The reduction of the annual fees was a result of the Hungarian mobile operators' years of interest enforcement efforts as former fees were far higher than the European average. The probability of the modification of these Authority Contract based fees prior to the expiry of the term has become very low as the parties agreed in all terms and provisions of the contract, including the reduced fees of the bands, until 2022. It would be unprecedented that the annual fees change prior to the expiry of the term of the contract. While the mobile operators took significant efforts prior to the recent amendment to reduce the fees, the lowered fees in the newly concluded contract are more favorable for MT than the fee in the authority decree. Based on the same consideration, the mobile operators also initiated the reduction of the fees of those bands that were outside the scope of the modification of the Authority Contract. The fee of the 2100 MHz band, which can be used until 2019, was reduced by 50% pursuant to the relevant National Media and Infocommunications Authority decree and this was such an extensive reduction that it makes the revision of the fees until the expiry of the contracts in 2019 very unlikely. The mobile operators had reached their objectives as the annual fee obligation was significantly reduced and it is now aligned to the EU trends.

The Authority Contract concluded between the Company and the NMIAH in October 2014 on the use of the new 800MHz, 900 MHz and 1800 MHz frequency bands also includes annual fees that are in line with the ones achieved in 2013, i.e. we considered them reliably estimable to capitalize their discounted present value as part of the cost of the license.

The Authority Contract concluded between the Company and the NMIAH in August 2018 on the prolongation of the 26 GHz frequency until May, 2024 also includes annual fees that are in line with the ones achieved in 2013, i.e. we considered them reliably estimable to capitalize their discounted present value as part of the cost of the license.

The Authority Contract concluded between the Company and the NMIAH in December 2018 on the prolongation of the 2100 MHz frequency until June, 2027 also includes annual fees that are in line with the ones achieved in 2013, i.e. we considered them reliably estimable to capitalize their discounted present value as part of the cost of the license.

In case of the other frequency license fees of the Group, we did not consider the annual fees to be reliably estimable at the time of acquisition, therefore, those were not capitalized.

4 FINANCIAL INSTRUMENTS

A financial instrument is any contract that gives rise to a financial asset of one entity and a financial liability or equity instrument of another entity.

Financial assets of the Group include cash and cash equivalents, equity instruments of another entity and contractual rights to receive cash (trade receivables) or another financial asset from another entity or to exchange financial assets or financial liabilities with another entity under conditions that are potentially favorable to the entity (derivatives) a contract that will or may be settled in the entity's own equity instruments and is a non-derivative for which the entity is or may be obliged to receive a variable number of the entity's own equity instruments; or a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose, the entity's own equity instruments do not include puttable financial instruments classified as equity instruments, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.

Financial liabilities of the Group include liabilities that originate from contractual obligations to deliver cash or another financial asset to another entity (non-derivatives); or to exchange financial assets or financial liabilities with another entity under conditions that are potentially unfavorable to the entity (derivatives) or a contract that will or may be settled in the entity's own equity instruments and is a non-derivative for which the entity is or may be obliged to deliver a variable number of the entity's own equity instruments; or a derivative that will or may be settled other than by the exchange of a fixed amount of cash or another financial asset for a fixed number of the entity's own equity instruments. For this purpose, the entity's own equity instruments do not include puttable financial instruments that are classified as equity instruments, instruments that impose on the entity an obligation to deliver to another party a pro rata share of the net assets of the entity only on liquidation and are classified as equity instruments, or instruments that are contracts for the future receipt or delivery of the entity's own equity instruments.

Financial liabilities, in particular, include liabilities to banks and related parties, finance lease payables, trade payables and derivative financial liabilities and other financial liabilities.

4.1 Financial assets – accounting policies

4.1.1 Financial assets – accounting policies relevant from 2018

From January 1, 2018 with the application of IFRS 9, the Group classifies its financial assets on the basis of both:

- the entity's business model for managing the financial assets and
- the contractual cash flow characteristics of the financial asset

in the following categories:

- at amortised cost if both of the following conditions are met:
  - the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows and
  - the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.
- at fair value through other comprehensive income (FVOCI) if both of the following conditions are met:
  - the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and
  - the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.
- at fair value through profit or loss (FVTPL) unless it is classified in the previous categories.

For the purpose of the above classification:

- principal is the fair value of the financial asset at initial recognition
- interest consists of consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs, as well as a profit margin.

Standard purchases and sales of financial assets are recognized on the trade-date, the date on which the Group commits to purchase or sell the asset. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the Profit for the year.

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred. Financial assets have been transferred when the contractual rights to receive cash flows of the financial assets have been transferred or the contractual rights to receive cash flows of the financial assets have been retained but there is a contractual obligation to pay the cash flows to one or more recipients in an arrangement compliant with the conditions set out by IFRS 9. Any gains or losses on derecognition are recognized in Profit for the year and are calculated as the difference between (a) the sum of the consideration received and any cumulative gain or loss that had been recognised in other comprehensive income and (b) the carrying amount derecognized.

4.1.1.1 Impairment of financial assets

Depending on the business model of the Group and the characteristics of the contractual cash flows of the financial assets, financial assets are subsequently measured at amortized cost, at fair value through other comprehensive income or at fair value through profit or loss.

A loss allowance must be recognized for financial assets measured at amortised cost and at fair value through other comprehensive income. The loss allowance must be recognized through profit or loss and reduces the carrying amount of the relevant financial asset; in the case of financial assets measured at fair value through other comprehensive income, the corresponding offsetting entry is recognized in other comprehensive income and does not reduce the carrying amount of the financial asset.

Loss allowances must also be recognized for lease receivables as defined in IAS 17 and IFRS 16, contract assets as defined in IFRS 15, financial guarantee contracts and loan commitments relating to loans bearing an off-market interest rate.

From January 1, 2018 with the transition to IFRS 9, loss allowance is recognized in respect of not only losses already incurred as of the reporting date (incurred losses) but also losses which have not yet incurred as of the reporting date but which are expected to be incurred in the future (expected losses).

Based on the changes in credit risk, it must be assessed at each reporting date whether the current loss allowance must be measured at an amount equal to the lifetime expected credit losses or at an amount equal to the 12-month expected credit losses. If it is not possible to assess whether the credit risk has increased significantly based on the individual financial asset, it must be assessed at the portfolio level.

The simplified and the general approaches are to be applied to assess and account for credit losses.

- Simplified approach

All financial instruments underlying simplified approach are measured with lifetime expected credit loss. Therefore, except for insolvency, neither any indicators for increase in credit risk nor any default events are relevant within simplified approach.

The simplified approach is applicable for trade receivables, contract assets and lease receivables without a significant financial component. MT Group has chosen the right to use the simplified approach for these receivables with a significant financial component as well.

- General approach

According to the expected credit loss model the financial instruments are classified into three buckets. The classification into the three buckets is based upon the changes of the credit risk for the financial asset. A relative credit risk model is used for the evaluation of an increased credit risk. The increase of credit risk in comparison to the initial recognition is reflected in the transfer of the financial instrument between the buckets.

According to the expected credit risk model the impairment is determined differently for the three buckets. The impairment for financial instruments in bucket 1 is calculated based upon the 12 months expected credit loss. The impairment for financial instruments in bucket 2 and 3 is calculated based upon the lifetime expected credit losses. Once a long term asset moved to bucket 3 effective interest method has to be applied to reach net value after impairment.

The general approach is applied for bank accounts, factoring receivables, other financial receivables and employee loans.

4.1.1.2 Financial assets measured at amortised cost

The following items are assigned to this category:

- cash and cash equivalents;
- deposits over 3 months;
- trade receivables;
- other receivables.

Financial assets at amortised cost are initially recognized at fair value and subsequently carried at amortized cost using the effective interest method (relevant only for the receivables with long-term maturity).

Cash and cash equivalents

Cash and cash equivalents include cash on hand and in banks, and all highly liquid deposits and securities with original maturities of three months or less, and exclude all overdrafts.

Bank deposits with original maturities over 3 months

Bank deposits with original maturities over 3 months include bank deposits and other liquid deposits and securities with original maturities over three months.

Trade and other receivables

If there is significant increase in the credit risk of trade receivables carried at amortized cost, the amount of the impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the receivable's original effective interest rate (i.e. the effective interest rate computed at initial recognition). In case of short-term trade receivables estimation is made on the amount of expected future cash inflows and compared to the carrying amount, the difference is accounted for as allowance for trade receivables. The carrying amount of the asset is reduced through use of an allowance account. The amount of the loss is recognized as Bad debt expense.

When it is determined that there is no significant increase in the credit risk for an individually assessed accounts receivable, the item should be included in a group of accounts receivables with similar credit risk characteristics and assessed collectively for impairment. Receivables that are individually assessed for impairment and for which an impairment loss is or continues to be recognized are not included in a collective assessment of impairment.

There are three categories of calculating impairment loss for trade receivables:

- for invoices which are overdue
- for invoices which are not yet due ('zero day impairment calculation')
- for unbilled revenue.

In case of collective assessment there is significant increase in the credit risk if there are overdue items in a group of receivables. An ageing list is prepared on overdue receivables and the amount of impairment is calculated by multiplying impairment rates based on historical loss experience with the amount of receivables.

Impairment rates are calculated based on historical loss experience, however it is adjusted on the basis of current observable data to reflect the effects of current conditions that did not affect the period on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently. During the impairment calculation forward looking information is also considered. Such kind of information can be for example internal changes in the billing and dunning processes and external extreme changes e.g. in unemployment rates, credit crisis etc.

When a trade receivable is established to be uncollectible, it is written off against Trade receivables and other assets. Impairment and subsequent recoveries of amounts previously written off are accounted for against the period's Direct costs.

4.1.1.3 Financial assets at fair value through other comprehensive income (FVOCI)

The "financial assets at fair value through other comprehensive income" measurement category includes the following financial assets:

- listed and unlisted equity instruments that are neither fully consolidated nor included using the equity method in the consolidated financial statements, not held for trading and OCI option has been applied;
- debt instruments within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets.

Financial assets at fair value through other comprehensive income are initially recognized at fair value and are also subsequently carried at fair value. The unrealized changes in the fair value of financial assets at fair value through other comprehensive income are recognized in equity, in the Revaluation reserve for FVOCI financial assets for both equity instruments and debt instruments.

When securities classified as financial assets at fair value through other comprehensive income are sold, the accumulated fair value adjustments recognized in equity before are recognized in the profit or loss except for equity instruments, where it will be reversed to equity.

The Group assesses at each balance sheet date whether there is significant increase in the credit risk . There is significant increase in the credit risk of a financial asset as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be estimated reliably.

If any such evidence exists for FVOCI financial assets, the cumulative loss – measured as the difference between the acquisition cost and the current fair value, less any impairment loss on that financial asset previously recognized in the profit or loss – is removed from equity and recognized in the income statement. Impairment losses recognized in the profit or loss on equity instruments are not reversed through the profit or loss.

4.1.1.4 Financial assets at fair value through profit or loss (FVTPL)

Debt instruments which do not meet the conditions set out to be initially classified either at amortised cost or at fair value through other comprehensive income must be measured at fair value through profit or loss.

The "financial assets at fair value through profit or loss" measurement category includes the following financial assets:

- Debt instruments that are designated as "at fair value through profit or loss" using the fair value option.
- Equity instruments acquired for the purpose of selling immediately or in the near term and thus classified as "held for trading" and equity instruments not held for trading where the OCI option has not been applied.
- Derivative financial assets.
- Debt instruments not fulfilling conditions of either financial assets at amortized cost or financial assets at fair value through other comprehensive income.

Financial assets at fair value through profit or loss are subsequently carried at fair value. Gains or losses arising from changes in the fair value of the financial assets at fair value through profit or loss category are recognized in the profit or loss in the period in which they arise.

Housing loans to employees

Employee loans generally do not meet the SPPI criteria, hence are classified in fair value through profit or loss category.

4.1.2 Financial assets – accounting policies relevant in 2017

In 2017 and before the transition to IFRS 9, the Group classified its financial assets in the following categories:

- at fair value through profit or loss (FVTPL)
- loans and receivables
- available-for-sale (AFS)

The classification depends on the purpose for which the financial asset was acquired. Management determines the classification of financial assets at their initial recognition and the characteristics of the asset itself.

Standard purchases and sales of financial assets are recognized on the trade-date, the date on which the Group commits to purchase or sell the asset. Investments are initially recognized at fair value plus transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets carried at fair value through profit or loss are initially recognized at fair value, and transaction costs are expensed in the Profit for the year.

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Group has transferred substantially all risks and rewards of ownership. Any gains or losses on derecognition are recognized in Profit for the year and are calculated as the difference between (a) the sum of the consideration received and any cumulative gain or loss that had been recognised in other comprehensive income and (b) the carrying amount derecognized.

4.1.2.1 Impairment of financial assets

The Group assesses at each financial statement date whether there is objective evidence that a financial asset is impaired. There is objective evidence of impairment if as a result of loss events that occurred after the initial recognition of the asset have an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Impairment losses of financial assets are recognized in the Profit for the year against allowance accounts to reduce the carrying amount until the derecognition of the financial asset.

(a) Financial assets measured at amortised cost

The Group first assesses whether objective evidence of impairment exists individually for financial assets that are individually significant, and collectively for financial assets that are not individually significant. If no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it is assessed collectively for impairment. Assets that are individually assessed for impairment and for which an impairment loss is recognized are not included in a collective assessment of impairment. Collective assessment is carried out by grouping together assets with similar risk characteristics.

Individual assessment of impairment is carried out for debtors under litigation; bankruptcy proceedings and for the total receivables of customers with more than 1 year overdue receivables. Individual assessment is also performed in special circumstances, if there is an overdue receivable from any designated customer with different credit risk attributes.The carrying amount of loans and receivables, which would otherwise be past due, whose terms have been renegotiated is not impaired if the collectability of the renegotiated cash flows are considered ensured.

In assessing collective impairment, the Group uses historical information on the timing of recoveries and the amount of loss incurred, and makes an adjustment if current economic and credit conditions are such that the actual losses are likely to be greater or lesser than suggested by historical trends. The Group's benchmark policy for collective assessment of impairment of trade and other receivables is based on the aging of the receivables due to the large number of relatively similar type of customers.

An impairment loss is calculated as the difference between an asset's carrying amount and the present value of the estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the loss is recognized in the Profit for the year.

Impairment loss on cash and cash equivalents and bank deposits with original maturities over 3 months and its reversal are recognized in the Profit for the year (Other finance expense – net). Impairment loss on trade and other receivables and its reversal are recognized in Direct costs in the Profit for the year (Bad debt expense). Impairment losses on Employee loans and any reversal is recognized in the Profit for the year (Employee related expenses).

If the amount of impairment loss subsequently decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), then the previously recognised impairment loss is reversed through the Profit for the year by adjusting the allowance account. The reversal shall not result in a carrying amount of the financial asset that exceeds what the amortized cost would have been had the impairment not been recognized at the date the impairment is reversed. The amount of the reversal shall be recognized in the Profit for the year as a reduction to Direct costs (Bad debt expense).

When the Group considers that there are no realistic prospects of recovery of the asset (i.e. uncollectible), the relevant amounts are written off. The amounts written off and subsequent recoveries of amounts previously written off are recognised in the same line item of the Statement of profit or loss as the impairment losses.

(b) Available-for-sale (AFS) financial assets

Impairment losses on available-for-sale financial assets are recognised by reclassifying the losses accumulated in the Revaluation reserve for AFS financial assets to the Profit for the year (Other finance expense – net). The amount reclassified is the difference between the acquisition cost (net of any principal repayment and amortisation) and the current fair value, less any impairment loss previously recognised in the Profit for the year. If the fair value of an impaired available-for-sale debt security subsequently increases and the increase can be related objectively to an event occurring after the impairment loss was recognised, then the impairment loss is reversed through the Profit for the year (Other finance expense – net).

Impairment losses recognised in Profit for the year for an investment in an equity instrument classified as available-for-sale are not reversed through the Profit for the year.

4.1.2.2 Financial assets at fair value through profit or loss

The “financial assets at fair value through profit or loss” measurement category includes the following financial assets:

- Financial assets incurred for the purpose of selling immediately or in the near term and thus classified as “held for trading”
- Derivative financial assets not involved in an effective hedge relationship are classified as “held for trading”

Assets in this category are normally classified as current assets (Other current financial assets). Derivatives aimed to hedge the cash flow risk of non current financial instruments are classified as non current assets (Non current financial assets).

No reclassification between categories has been made in the past and no reclassifications are expected in the future.

Assets in this category are initially recognized and subsequently carried at fair value. Gains or losses arising from changes in the fair value are recognized in the Profit for the year (Other finance expense – net) in the period in which they arise. The Group only classifies derivative financial instruments in this category.

Derivatives are initially recognized at fair value on the date a derivative contract is entered into and their fair values are re-measured at subsequent financial statement dates. Magyar Telekom does not apply hedge accounting for its financial instruments, therefore all gains and losses are recognized in the Profit for the year (Other finance expense – net).

4.1.2.3 Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Receivables are included in current assets, except those with maturities over 12 months after the financial statement date. These are classified as Non-current financial assets.

The following items are assigned to the “loans and receivables” measurement category:

- cash and cash equivalents
- bank deposits with original maturities over 3 months
- trade receivables
- employee loans
- other receivables

Loans and receivables are initially recognized at fair value plus any directly attributable transaction costs and subsequently carried at amortized cost using the effective interest method, less any impairment.

(a) Cash and cash equivalents

Cash and cash equivalents include cash on hand and in banks, and all highly liquid deposits and securities with original maturities of three months or less, and exclude all overdrafts.

(b) Bank deposits with original maturities over 3 months

Bank deposits with original maturities over 3 months include bank deposits and other liquid deposits and securities with original maturities over three months.

(c) Trade and other receivables

Trade receivables include the receivables for the services rendered and goods sold from the customers of the Group while other receivables mainly include advances and prepayments.

(d) Employee loans

Employee loans are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method, less any impairment loss.

The difference between the nominal value of the loan granted and the initial fair value of the employee loan is recognized as prepaid employee benefits (Other non current assets). Interest income on the loan granted calculated by using the effective interest method is recognized as Interest income, while the prepaid employee benefits are amortized to Employee related expenses evenly over the term of the loan.

4.1.2.4 Available-for-sale (AFS) financial assets

AFS financial assets are non-derivative financial assets that are either designated in this category or not classified in any of the other categories. They are included in Non current financial assets unless management intends to dispose of the investment within 12 months of the financial statement date. In this latter case they are included in Other current financial assets.

The AFS measurement category includes:

- equity instruments that are neither consolidated nor included using the equity method in the consolidated financial statements
- debt instruments

AFS financial assets are initially recognized and also subsequently carried at fair value. The unrealized changes in the fair value of AFS financial assets are recognized in Accumulated other comprehensive income (Revaluation reserve for AFS financial assets).

Interest on AFS debt securities calculated using the effective interest method is recognized in the Profit for the year (Interest income). Dividends on AFS equity instruments are recognized in the Profit for the year (Interest income) when the Group's right to receive payments is established.

4.2 Financial assets in the statement of financial position

4.2.1 Cash and cash equivalents

Cash and cash equivalents include cash on hand and in banks, and all highly liquid deposits and securities with original maturities of three months or less, and exclude all overdrafts. These financial assets are exposed to credit risks, for which see more details in Note 5.1.2. No impairment had to be recognized for any of these balances in the reported years.

In HUF millions	At December 31,	
	2017	2018
Cash on hand	175	151
Cash in bank (demand deposits)	3,807	4,515
Bank deposits with original maturities less than 3 months	1,417	2,538
	5,399	7,204

Average interest rates	At December 31,	
	2017	2018
Cash on hand	0.00%	0.00%
Cash in bank (demand deposits)	0.09%	0.10%
Bank deposits with original maturities less than 3 months	0.35%	0.24%
Average interest rate	0.16%	0.15%

Cash and cash equivalents by currency	At December 31,	
In HUF millions	2017	2018
HUF	1,865	2,522
EUR	784	2,471
MKD	1,703	1,536
RON	594	521
USD	411	95
Other	42	59
	5,399	7,204

Cash and cash equivalents by country of location	At December 31,	
In HUF millions	2017	2018
Macedonia	2,643	3,960
Hungary	2,064	2,627
Other countries	692	617
	5,399	7,204

4.2.2 Trade receivables and contract assets

Trade receivables and other assets in the Consolidated statement of financial position includes both trade receivables, contract assets and other assets (Note 12).

4.2.2.1 Trade receivables and contract assets – carrying amounts

		At December 31,	
In HUF millions		2017	2018
Trade receivables from third parties		135,082	154,579
Trade receivables from Deutsche Telekom Group companies		9,029	10,143
Trade receivables from associates and joint ventures		326	549
Trade receivables	(a)	144,437	165,271
Contract assets - current (Notes 1.3 and 18.4)		-	17,820
Total trade receivables and contract assets		144,437	183,091

The change of Trade receivables from third parties from 2017 to 2018 includes also the effect of the reclassification due to the transition to IFRS 15 (i.e. partial recognition of contract assets). See also Notes 1.3 and 2.1.1.

(a) Age profile of Trade receivables

The following tables show the age profile of the Group's trade receivables by country of operation by days outstanding (past due). The carrying amounts of past due receivables are shown net of impairment losses charged as of the financial statement dates.

In HUF millions	Carrying amount as of Dec 31, 2018	of which not past due	of which past due by					
			less than 30 days	30–60 days	61–90 days	91–180 days	181–360 days	over 360 days
Hungary	150,647	128,891	15,904	2,518	741	1,254	696	643
Macedonia	13,806	10,467	1,560	327	130	229	324	769
Other countries	818	697	74	14	14	13	5	1
Total	165,271	140,055	17,538	2,859	885	1,496	1,025	1,413

In HUF millions	Carrying amount as of Dec 31, 2017	of which not past due	of which past due by					
			less than 30 days	30–60 days	61–90 days	91–180 days	181–360 days	over 360 days
Hungary	130,277	113,727	10,208	2,261	1,143	961	529	1,448
Macedonia	13,365	9,853	1,570	482	278	352	444	386
Other countries	795	634	76	24	11	30	14	6
Total	144,437	124,214	11,854	2,767	1,432	1,343	987	1,840

The vast majority of trade receivables is impaired on a portfolio basis using the simplified approach. The vast majority of past due trade receivables is partly or fully impaired depending mainly on the period of delay of payments. Only insignificant amounts of past due trade receivables are not impaired based on past experience of payment behavior of certain business and governmental customers. As these amounts are not significant, these are not disclosed separately.

4.2.2.2 Impairment losses of trade receivables and contract assets

The table below shows the impairment losses and changes therein related to trade receivables for 2017 and 2018.

In HUF millions	At December 31,	
	2017	2018
Impairment loss, beginning of period	37,590	30,036
First-time adoption of IFRS 9&15 (Notes 1.3 and 2.2)	-	771
Charged to expense – net (included in Direct costs)	5,575	8,271
Translation difference	(41)	384
Decrease of impairment losses due to sale of subsidiary	(6,301)	-
Utilized	(6,787)	(7,358)
Impairment loss, end of period	30,036	32,104

The table below shows the impairment losses and changes therein related to contract assets for 2017 and 2018.

In HUF millions	At December 31,	
	2017	2018
Impairment loss, beginning of period	-	-
First-time adoption of IFRS 9&15 (Notes 1.3 and 2.2)	-	893
Charged to expense – net (included in Direct costs)	-	1,225
Translation difference	-	16
Utilized	-	(665)
Impairment loss, end of period	-	1,469

In 2018, the line First-time adoption of IFRS 9&15 includes the increase in impairment losses as a result of the first-time adoption of IFRS 9 (HUF 771 million), as the expected credit loss model was applied and the increase in impairment losses as a result of the first-time adoption of IFRS 15 (HUF 893 million), as the newly recognized contract assets had to be impaired as at the application date (see also notes 1.3 and 2.2).
The line Charged to expense - net included in 2017 also this type of change in impairment related to Crnogorski Telekom AD which was considered as discontinued operation (see also note 26.2.1).
The table below includes the impairment losses and the changes therein in 2017 and 2018 for the countries of operation of the Group.

In HUF millions	At December 31, 2016	Charged to expense	Translation difference (and rounding)	Decrease of impairment losses due to sale of subsidiary	Utilized (1)	At December 31, 2017
Hungary	21,801	4,742	1	-	(6,472)	20,072
Macedonia	9,370	774	(36)	-	(293)	9,815
Montenegro	6,248	55	-	(6,301)	(2)	-
Other countries	171	4	(6)	-	(20)	149
Group	37,590	5,575	(41)	(6,301)	(6,787)	30,036

(1) Utilized means reversed on derecognition (settlement, write-off or factoring).

In HUF millions	At December 31, 2017	First-time adoption of IFRS 9&15	Charged to expense	Translation difference (and rounding)	Utilized (1)	At December 31, 2018
Hungary	20,072	1,108	8,662	(1)	(7,174)	22,667
Macedonia	9,815	556	831	391	(849)	10,744
Other countries	149	-	3	10	-	162
Group	30,036	1,664	9,496	400	(8,023)	33,573

(1) Utilized means reversed on derecognition (settlement, write-off or factoring).

See also Note 5.1.2 for further analysis of credit risks related to Trade receivables.

4.2.3 Other financial assets

Other financial assets include receivables due within 12 months (current) and due after 12 months (non current) from the end of the reporting period (financial statement date). These financial assets are exposed to credit risks, for which see more details in Note 5.1.2. The impairment loss recognised or reversed for other current and non current financial assets is not material.

4.2.3.1 Other current financial assets

In HUF millions		At December 31, 2017	At December 31, 2018
Bank deposits with original maturities over 3 months	(a)	3,523	3,915
Finance lease receivable	(b)	246	50
Loans and receivables from employees	(c)	325	355
Derivative financial instruments contracted with related parties	(d)	2,978	-
Cashpool receivables	(e)	-	6,580
Other		1,090	731
		8,162	11,631

(a) Bank deposits with original maturities over 3 months were deposited in Macedonia predominantly in euro. They amounted to HUF 3,915 million as at December 31, 2018 (2017: HUF 3,523 million).

4.2.3.2 Other non current financial assets

In HUF millions		At December 31, 2017	At December 31, 2018
Finance lease receivable	(b)	346	308
Employee loans and receivables from employees	(c)	1,429	1,099
Trade receivables over one year	(f)	16,690	18,056
Derivative financial instruments contracted with related parties	(d)	-	1,026
Equity instruments	(g)	325	544
Contract assets	(h)	-	3,560
Other		533	392
		19,323	24,985

(b) See Note 17.2.1 for more information on Finance lease receivable.

(c) Employee loans and receivables from employees primarily represent the housing loans provided to the employees of the Group. There are no significant past due employee receivables, and the loans are pledged with mortgage. See also 4.1.1.4 and 4.1.2.3 d).

(d) Derivative financial instruments contracted with related parties include the fair value of open currency forwards and cross-currency interest rate swaps (see more details in Note 5.1.1.1 and 5.1.1.3).

(e) The aggregate balance of the cashpool is a receivable (HUF 6,580 million) as at December 31, 2018 which also included cashpool liabilities (HUF 592 million). (The aggregate balance of the cashpool was a liability as at December 31, 2017 which also included cashpool receivables (HUF 97 million). See also Note 4.2.3.1.)

December 31, 2018	Carrying amount in HUF millions	Lender	Currency	Effective Interest rate (%)	Fixed / floating
	6,249	DT AG	HUF	0.00	floating
	923	DT AG	EUR	0.00	floating
	(592)	DT AG	USD	2.46	floating
Due within 1 year	6,580				

(f) Trade receivables over one year include receivables from customers paying over 1-2 years in installments for telecommunications equipment sold. The impairment losses of trade receivables over one year amounted to HUF 1,243 million as at December 31, 2018 (2017: HUF 1,358 million).

(g) Equity instruments include insignificant investments in equity securities.

(h) Contract assets are disclosed together with revenues from contracts with customers in Note 18.4.

4.3 Financial liabilities – accounting policies

The accounting policies of the Group did not change significantly regarding the financial liabilities with the transition to IFRS 9 and they are disclosed below.

There are two measurement categories for financial liabilities used by the Group:

- Financial liabilities carried at amortized cost
- Financial liabilities at fair value through profit or loss

No reclassification between categories has been made in the past and no reclassifications are expected in the future. Both types of financial liabilities are initially recognized at fair value, while subsequent measurements are different (see below). We derecognize a financial liability (or a part of a financial liability) from the Statement of financial position when, and only when, it is extinguished – i.e. when the obligation specified in the contract is discharged, cancelled or expired.

4.3.1 Financial liabilities carried at amortized cost

The measurement category for “financial liabilities measured at amortized cost” includes all financial liabilities not classified as “at fair value through profit or loss”.

(a) Loans and other financial liabilities

Loans and other financial liabilities are recognized initially at fair value less transaction costs, and subsequently measured at amortized costs using the effective interest rate method. The effective interest is recognized in the Profit for the year (Interest expense) over the period of the liabilities.

(b) Trade and other payables

Trade and other payables (including accruals) are recognized initially at fair value and subsequently measured at amortized cost using the effective interest method.

4.3.2 Financial liabilities at fair value through profit or loss

The Group currently has no intention of measuring non-derivative financial liabilities at fair value, therefore, only derivative financial instruments are assigned to this category. However, contingent consideration recognised by the Group as acquirer in a business combination to which IFRS 3 applies will subsequently be measured at fair value through profit or loss.

The Group does not apply hedge accounting, therefore, all derivatives are measured at fair value through profit or loss.

Derivatives are initially recognized at fair value at the date a derivative contract is entered into and their fair values are re-measured at subsequent balance sheet dates. Magyar Telekom does not apply hedge accounting for its financial instruments, therefore all gains and losses are recognized in the Profit for the year (Other finance expense – net).

4.4 Financial liabilities in the statement of financial position

4.4.1 Financial liabilities to related parties

Financial liabilities to related parties include HUF and EUR denominated loans taken from DT Group. In addition, for the whole nominal amount and interest payment of loans denominated in EUR granted by DTIF we have cross-currency interest rate swap agreements in place (with DT AG) so that Magyar Telekom's exposure in fact remains in HUF. The loans and the related swap agreements are accounted for and disclosed on a gross basis. These loans were primarily taken for significant acquisitions in the past and for dividend payments. These loans, when expiring, are also refinanced by DT, depending on the actual financing need of Magyar Telekom.

The tables below show the details of the financial liabilities towards Deutsche Telekom Group members as at December 31, 2018 and 2017.

December 31, 2018	Carrying amount in HUF millions	Lender	Currency	Effective Interest rate (%)	Fixed / floating	Maturity	Original Term
	35,000	DT AG	HUF	5.89	fixed	Mar 2019	5 years
	20,000	DT AG	HUF	4.98	fixed	Jun 2019	5 years
	50,000	DT AG	HUF	4.33	fixed	Oct 2019	5 years
Due within 1 year	105,000						
Accrued interest	5,872						
Other financial liabilities	185						
Derivatives	87						
Total current	111,144						
	35,000	DT AG	HUF	3.83	fixed	Jun 2020	5 years
	42,013	DTIF	EUR	1.99	fixed	Jan 2021	6 years
	45,811	DTIF	EUR	1.60	fixed	Jul 2021	5 years
Non current	122,824						
Derivatives	525						
Total non current	123,349						

December 31, 2017	Carrying amount in HUF millions	Lender	Currency	Effective Interest rate (%)	Fixed / floating	Maturity	Original Term
	15,555	DTIF	EUR	4.08	fixed	Nov 2018	7 years
	12,982	DT AG	HUF	0.30	floating	Cashpool	N/A
	(97)	DT AG	EUR	0.00	floating	Cashpool	N/A
	468	DT AG	USD	1.48	floating	Cashpool	N/A
Due within 1 year	28,908						
Accrued interest	6,034						
Derivatives	249						
Total current	35,191						
	35,000	DT AG	HUF	5.89	fixed	Mar 2019	5 years
	20,000	DT AG	HUF	4.98	fixed	Jun 2019	5 years
	50,000	DT AG	HUF	4.33	fixed	Oct 2019	5 years
	35,000	DT AG	HUF	3.83	fixed	Jun 2020	5 years
	40,626	DTIF	EUR	1.99	fixed	Jan 2021	6 years
	45,657	DTIF	EUR	1.60	fixed	Jul 2021	5 years
Non current	226,283						
Derivatives	5,363						
Total non current	231,646						

The table below shows the carrying amounts and fair values of the related party loans.

In HUF millions	At December 31, 2017		2018	
	Book value	Fair value	Book value	Fair value
HUF denominated loans				
At fixed rate	140,000	154,475	140,000	147,860
At floating rate	12,982	12,981	-	-
	152,982	167,456	140,000	147,860
EUR denominated loans				
At fixed rate	101,838	109,122	87,824	93,552
At floating rate	(97)	(97)	-	-
	101,741	109,025	87,824	93,552
USD denominated loans				
At fixed rate	-	-	-	-
At floating rate	468	468	-	-
	468	468	-	-
Accrued interest	6,034	6,034	5,872	5,872
Other financial liabilities	-	-	185	185
Derivatives	5,612	5,612	612	612
Total related party financial liabilities	266,837	288,595	234,493	247,896

The weighted average interest rate on related party loans was 3.57% in 2018 (3.44% in 2017). Any decrease of market interest rates will result in an increase of the fair value of the fixed interest rate liabilities.

The aggregate balance of the cashpool is a receivable (HUF 6,580 million, see also Note 4.2.3.1) as at December 31, 2018. (The aggregate balance of the cashpool was a liability as at December 31, 2017 which also included cashpool receivables (HUF 97 million).

Derivatives contracted with related parties include cross-currency interest rate swaps and FX forwards concluded with DT AG to change the Group's exposure to HUF in case of the EUR denominated loans and to cover FX needs of expected future foreign currency outflows.

There were no defaults or breaches in connection with the financial liabilities to related parties.

4.4.2 Other financial liabilities

4.4.2.1 Other financial liabilities - Balances

The table below shows the current balances of Other financial liabilities.

In HUF millions		At December 31, 2017	2018
Annual frequency fee payable	(a)	3,492	3,722
Debtor overpayment		1,110	1,327
Finance lease payable	(b)	882	694
Contingent consideration liabilities	(c)	-	178
Other		3,273	3,307
Total other financial liabilities – current		8,757	9,228

The table below shows the non current balances of Other financial liabilities.

In HUF millions		At December 31, 2017	2018
Annual frequency fee payable	(a)	41,722	42,392
Finance lease payable	(b)	3,291	3,132
Contingent consideration liabilities	(c)	-	530
Other		2,595	1,865
Total other financial liabilities – non current		47,608	47,919

There were no defaults or breaches in connection with other financial liabilities.

(a) Annual frequency fee payable

On October 15, 2014 Magyar Telekom and the NMIAH signed the Authority Contract for the use of the 800 MHz, 900 MHz and 1800 MHz frequency bands that came into force on that day. Magyar Telekom acquired the frequency usage rights in the above listed spectrums till June 15, 2034. See Note 34.1 for more details of the agreement. This agreement provides sufficient basis for a reliable estimate of the future annual fees payable related to these Hungarian frequency licenses, as a result of which the present value of the annual fees payable (HUF 39,038 million) was recognized as part of the carrying amount of the licenses as intangible assets, with corresponding current and non current financial liabilities falling due from 2015 to 2034.

On September 6, 2013 Magyar Telekom and the NMIAH signed the modification of the Authority Contract for the use of the 900 MHz and 1800 MHz frequency bands. See Note 34.1 for more details of the agreement. This agreement provides sufficient basis for a reliable estimate of the future annual fees payable related to these Hungarian frequency licenses, as a result of which the present value of the annual fees payable (HUF 17,332 million) was recognized as part of the carrying amount of the licenses as intangible assets, with corresponding current and non current financial liabilities falling due from 2014 to 2022.

In December 2018 based on the resolution of the NMIAH Magyar Telekom's frequency usage rights in the 2100 MHz frequency band otherwise expiring on December 27, 2019 were prolonged until June 27, 2027. For the three duplex 5 MHz frequency blocks Magyar Telekom is required to pay a price of HUF 11 billion, due in the first quarter of 2019. As this agreement provides sufficient basis for a reliable estimate of the future annual fees payable related to these Hungarian frequency licenses, the present value of the annual fees payable (HUF 4.2 billion) were recognized as part of the carrying amount of the licenses as intangible assets with corresponding current and non current financial liabilities falling due from 2018 to 2027.

(b) Finance lease payable

See Note 17.2.2 for the details of finance leases.

(c) Contingent consideration liabilities

Contingent consideration liabilities are recognised by Magyar Telekom as acquirer in a business combination to which IFRS 3 applies. They are measured at fair value through profit or loss.

4.4.2.2 Proceeds/repayments of loans and other borrowings

Cash payments for regular bank loans and related party loans are included in the Repayment of loans and other borrowings line of the Statements of cash flows.

4.4.2.3 Additional disclosure about changes in liabilities arising from financing activities

The following table includes changes in net debt reconciled with their effects on the Consolidated statement of cash flows in order to enable users of financial statements to evaluate changes in liabilities arising from financing activities.

Changes in financial liabilities without cash movement are mainly due to FX effects of financial liabilities denominated in EUR and transactions where future cash flows are recognized at the present value of the annual fees payable (e.g.: frequency fees and finance leases).

In HUF millions	Opening					Changes affecting cash flows from financing activities					Closing
	Balance at January 1, 2017	Changes in cash and cash equivalents	Changes affecting cash flows from operating activities	Changes in financial liabilities without cash movement	Changes affecting cash flows from investing activities	Proceeds from loans and borrowings (continuing operation)	Proceeds from loans and borrowings (discontinued operation)	Repayment of loans and other borrowings	Repayment of other financial liabilities	Other	Balance at December 31, 2017
Related party loans	316,316		(1,665)	(2,438)		97,516	2,041	(150,545)			261,225
Derivatives from related parties	3,452			5,512	(3,352)						5,612
Bank loans	11,501		(1)	3,203		3,794		(18,497)			-
Payable for building exchange transaction	952								(937)		15
Frequency fee payable	48,490		(88)						(3,188)		45,214
Finance lease liabilities	5,822			229					(1,878)		4,173
Debtors overpayment	1,180		(70)								1,110
Other financial liabilities	4,753		(135)	2,717					(1,482)		5,853
-Less cash and cash equivalents	(10,805)	5,406									(5,399)
-Less other current financial assets	(5,104)		564	(3,421)	(201)						(8,162)
Net debt	**376,557**	**5,406**	**(1,395)**	**5,802**	**(3,553)**	**101,310**	**2,041**	**(169,042)**	**(7,485)**	**-**	**309,641**
Treasury share purchase										(2,139)	
Dividends paid to Owners of the parent and Non-controlling interest										(29,403)	
Net cash used in financing activities										**(104,718)**	

In HUF millions	Opening					Changes affecting cash flows from financing activities					Closing
	Balance at January 1, 2018	Changes in cash and cash equivalents	Changes affecting cash flows from operating activities	Changes in financial liabilities without cash movement	Changes affecting cash flows from investing activities	Proceeds from loans and borrowings (continuing operation)	Proceeds from loans and borrowings (discontinued operation)	Repayment of loans and other borrowings	Repayment of other financial liabilities	Other	Balance at December 31, 2018
Related party loans	261,225		(12,113)	15,163		72,953		(103,347)			233,881
Derivatives from related parties	5,612			(3,651)	(1,349)						612
Frequency fee payable	45,214		(2,604)	6,924					(3,419)		46,115
Finance lease liabilities	4,173			430					(777)		3,826
Debtors overpayment	1,110		217								1,327
Contingent consideration	-			708							708
Other financial liabilities	5,868		(572)	1,667					(1,792)		5,171
-Less cash and cash equivalents	(5,399)	(1,805)									(7,204)
-Less other current financial assets	(8,162)		602	(1,304)	3,813	(6,580)					(11,631)
Net debt	**309,641**	**(1,805)**	**(14,470)**	**19,937**	**2,464**	**66,373**	**-**	**(103,347)**	**(5,988)**	**-**	**272,805**
Treasury share purchase										(1,822)	
Dividends paid to Owners of the parent and Non-controlling interest										(29,547)	
Net cash used in financing activities										**(74,331)**	

4.4.3 Trade payables

In HUF millions	At December 31, 2017	2018
Payable to DT Group companies	12,026	11,119
Payable to associates and joint ventures	23	451
Other trade payables	123,397	163,742
	135,446	175,312

4.5 Additional disclosures on financial instruments

4.5.1 Financial assets and liabilities

The Group classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1)
- inputs other than quoted prices included within Level 1 observable for the asset or liability, either directly or indirectly (Level 2)
- inputs for the asset or liability that are not based on observable market data (Level 3)

The level in the fair value hierarchy within which the fair value measurement is categorized in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety. The significance of an input is assessed against the fair value measurement in its entirety. As at the date of initial application there were no changes in the carrying amounts arising from the change in measurement attribute on transition to IFRS 9. No fair value gain or loss was recognised in profit or loss or other comprehensive income during the reporting period at the reclassification.

There was no transfer between Level 1 and Level 2 financial instruments except for employee loans with repayment option before the due date, as these were designated in the fair value through profit and loss category.

Most of the financial assets and financial liabilities are measured at amortized cost, but fair value information is also provided for these. The fair values of these assets and liabilities were determined using level 3 type information. The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques, mainly by applying the discounted cash flow method. The cash flow estimations are based on the relevant underlying contracts and the discount rates are calculated based on the interest rate benchmarks applicable for the relevant maturities and currencies (BUBOR, BIRS, EURIBOR, EUR swap yields). Foreign exchange conversion is made based on central bank FX fixings (preferably that of the Central Bank of Hungary). There are no assets or liabilities carried at fair value where the fair value was determined using level 3 type information except for the contingent consideration liabilities.

Level 2 information are available to determine derivatives assets and liabilities as well as for calculating the fair values of employee loans designated at FVTPL. Level 1 information is used for determining Fair Value of equity instruments designated as financial assets at fair value through other comprehensive income.

In addition, Magyar Telekom reclassified all equity instruments previously recognized as available-for-sale financial assets to the IFRS 9 category at fair value through other comprehensive income.

The tables below include the carrying amounts and fair values of the Group's financial assets and liabilities as at December 31, 2018 and 2017.

4.5.1.1 Financial assets – Carrying amounts and fair values

December 31, 2018 In HUF millions	Carrying amount Amortized cost	FVOCI (Level 1)	FVTPL (Level 2)	FVTPL (Level 3)	Total	Fair value
Cash and cash equivalents	7,204	-	-	-	7,204	7,204
Bank deposits with original maturities over 3 months	3,915	-	-	-	3,915	3,915
Cashpool	6,580	-	-	-	6,580	6,580
Trade receivables within one year	165,271	-	-	-	165,271	165,271
Trade receivables over one year	18,056	-	-	-	18,056	19,133
Contract assets	21,380	-	-	-	21,380	21,380
Loans and receivables from employees	706	-	748	-	1,454	1,524
Derivative financial instruments contracted with related parties	-	-	1,026	-	1,026	1,026
Finance lease receivable	358	-	-	-	358	467
Equity instruments	-	544	-	-	544	544
Other current	731	-	-	-	731	731
Other non current	392	-	-	-	392	325
Total	224,593	544	1,774	-	226,911	228,100

December 31, 2017 In HUF millions	Carrying amount Loans and receivables	Held-to-maturity	Available-for-sale (Level 1)	FVTPL (Level 2)	Total	Fair value
Cash and cash equivalents	5,399	-	-	-	5,399	5,399
Bank deposits with original maturities over 3 months	3,523	-	-	-	3,523	3,523
Trade receivables within one year	144,437	-	-	-	144,437	144,437
Trade receivables over one year	16,690	-	-	-	16,690	17,814
Loans and receivables from employees	1,754	-	-	-	1,754	1,897
Derivative financial instruments contracted with related parties	-	-	-	2,978	2,978	2,978
Finance lease receivable	592	-	-	-	592	629
Financial assets AFS	-	-	325	-	325	325
Other current	1,090	-	-	-	1,090	1,090
Other non current	533	-	-	-	533	765
Total	174,018	-	325	2,978	177,321	178,857

As a result of the first-time application of IFRS 9, financial assets were categorized in the new measurement categories. All of the financial assets from the 2017 loans and receivables category were classified as financial assets measured at amortized cost in 2018 except for employee loans with repayment option before the due date, as these generally do not meet the SPPI criteria. Therefore they were designated in the fair value through profit or loss category. Fair Values of these financial assets are determined using level 3 type information, where the fair value is determined taking into account the probability of reaching the earnings target and discounting the amounts payable to their present value.

Fair value through profit or loss assets include derivative financial instruments, the fair values of which are based on a discounted cash flow method. The calculation is prepared by Magyar Telekom based on money market interest rate curves, basis swap points and spot FX rates from Reuters database published at the last working day of the reporting period. The present value of the expected future cash flows is discounted to the reporting date using money market interest rates and basis swap points in the specific currency from Reuters and exchanged to HUF using spot FX rate. The difference between the HUF present value of the payable and receivable is accounted for as assets or liabilities.

The carrying values of assets measured at amortized cost with short times to maturity approximate their fair values.

Equity instruments designated as financial assets at fair value through other comprehensive income (Financial assets available for sale in 2017) include insignificant investments in equity instruments, all measured at fair value, which is the Macedonian stock exchange price of the equity instruments.

4.5.1.2 Financial liabilities – Carrying amounts and fair values

December 31, 2018	Carrying amount			Total	Fair value
In HUF millions	Measured at amortized cost	FVTPL (Level 2)	FVTPL (Level 3)		
Financial liabilities to related parties	233,881	612	-	234,493	247,896
Trade payables	175,312	-	-	175,312	175,312
Frequency fee payable	46,114	-	-	46,114	52,845
Finance lease liabilities	3,826	-	-	3,826	7,119
Debtors' overpayment	1,327	-	-	1,327	1,327
Contingent consideration liabilities	-	-	708	708	708
Other current	3,307	-	-	3,307	3,307
Other non current	1,865	-	-	1,865	1,865
Total	465,632	612	708	466,952	490,399

December 31, 2017	Carrying amount		Total	Fair value
In HUF millions	Measured at amortized cost	FVTPL (Level 2)		
Financial liabilities to related parties	261,225	5,612	266,837	288,595
Trade payables..	135,446	-	135,446	135,446
Frequency fee payable.......................................	45,214	-	45,214	55,130
Finance lease liabilities......................................	4,173	-	4,173	9,009
Debtors' overpayment..	1,110	-	1,110	1,110
Other current...	3,273	-	3, 273	3, 273
Other non current..	2,595	-	2,595	2,590
Total	453,036	5,612	458,648	495,153

Derivatives and liabilities from contingent consideration of a business combination are measured at fair value, while all other financial liabilities are measured at amortized cost.

Additional fair value information on the loans and other borrowings is provided in Notes 4.4.1 and 4.4.2.

The carrying values of the current financial liabilities measured at amortized cost approximate their fair values.

FVTPL liabilities include both of derivative financial instruments, where the fair values of which are calculated the same way as FVTPL assets disclosed above in Note 4.5.1.1., and liabilities from contingent consideration of a business combination where the fair value of such liability is determined applying the discounted cash flow method.

4.5.1.3 Financial liabilities carried at fair value determined using level 3 type information

The only financial instrument which is carried at fair value where the fair value was determined using level 3 type information is the contingent consideration liability. The table below includes the movements of these liabilities.

In HUF millions	2017	2018
Opening balance at January 1	-	-
Increase arising on business combinations	-	450
Increase arising on asset deals	-	250
(Gains) or losses for the period on remeasurement		
- recognised in profit or loss (net financial result)	-	8
- recognised in other comprehensive income	-	-
Closing balance at December 31	-	708

4.5.2 Items of income, expense, gains and losses arising on financial instruments

The tables below include income, expense, gains and losses arising on financial instruments in 2018 and 2017.

2018 In HUF millions	From interest	From subsequent measurement			From derecog-nition	From fee expense	Total net gain / (loss)
		Change in fair value	Currency translation	Impair-ment loss			
Equity instruments (Level 1)	-	219	-	-	-	-	219
Debt instruments (Level 2)	-	38	-	-	-	-	38
Financial assets measured at amortized cost	276	-	79	(9,496)	-	(4,375)	(13,516)
Financial liabilities measured at amortized cost	(12,062)	-	(6,042)	-	-	(33)	(18,137)
FVTPL financial instruments (Level 2)	-	3,048	-	-	2,236	-	5,284
FVTPL financial instruments (Level 3)	-	(8)	-	-	-	-	(8)
Net gain/(loss) on financial instruments	(11,786)	3,297	(5,963)	(9,496)	2,236	(4,408)	(26,120)

2017 In HUF millions	From interest	From subsequent measurement			From derecognition	From fee expense	Total net gain / (loss)
		Change in fair value	Currency translation	Impairment loss			
Available-for-sale financial assets (Level 1)	-	19	-	-	-	-	19
FVTPL financial instruments (Level 2)	-	(4,448)	-	-	(325)	-	(4,773)
Loans and receivables	327	-	(161)	(5,520)	-	(4,813)	(10,167)
Financial liabilities measured at amortized cost	(12,091)	-	1,268	-	-	(42)	(10,865)
Net gain/(loss) on financial instruments	(11,764)	(4,429)	1,107	(5,520)	(325)	(4,855)	(25,786)

The tables above include the amounts before capitalization of borrowing costs (See Note 24).

Impairment losses on Financial assets measured at amortized cost (2017: Loans and receivables) includes all expenses incurred or expected to be incurred in relation to the default of our customers. Before writing off or factoring, we impair the receivables to their recoverable amounts through the use of an impairment allowance account, as a result of which the actual write-off or factoring of these receivables results in no derecognition gains or losses.

4.5.3 Offsetting financial assets and financial liabilities

For the financial assets and liabilities subject to enforceable netting arrangements, each agreement between the Group and the counterparty (typically roaming and interconnect partners) allows for net settlement of the relevant trade receivable and payable.

The following trade receivables and trade payables are subject to offsetting agreements, and are presented after netting in the Consolidated statements of financial position.

In HUF millions	At December 31, 2017		At December 31, 2018	
	Trade receivables and other assets	Trade payables	Trade receivables and other assets	Trade payables
Gross amounts of recognized financial instruments.............	160,750	138,451	197,216	177,308
Gross amounts of financial instruments set off.....................	(3,005)	(3,005)	(1,996)	(1,996)
Net amounts of recognized financial instruments presented in the statement of financial position......................................	157,745	135,446	195,220	175,312

4.5.4 Other disclosures about financial instruments

Magyar Telekom is also exposed to risks that arise from the possible drawdown of guarantees in a nominal amount of HUF 14.1 billion as at December 31, 2018 (2017: HUF 10.7 billion). These guarantees were issued by banks on behalf of Magyar Telekom as collateral to secure the fulfillment of the Group's certain contractual obligations. The Group has been delivering on its contractual obligations and expects to continue doing so in the future, consequently no significant drawdown of the guarantees happened in 2018 or 2017, and is not expected to happen in the future.

Magyar Telekom does not hold any material collateral of its financial assets.

No financial assets were transferred in such a way that part or all of the financial assets did not qualify for derecognition.

The Group does not have compound financial instruments with multiple embedded derivatives.

5 FINANCIAL RISK MANAGEMENT

5.1 Financial risk factors

Magyar Telekom is primarily exposed to credit risks related to its financial assets. In addition, the Group is also exposed to risks from movements in exchange rates, interest rates that affect the fair value and/or the cash flows arising from financial assets and liabilities.

Financial risk management aims to limit these risks through ongoing operational and finance activities. Selected derivative and non-derivative hedging instruments are also used for this purpose, depending on the risk assessment. Magyar Telekom only hedges the risks that affect the Group's cash flows, no hedges are concluded to hedge fair values. Derivatives are exclusively used as hedging instruments, i.e., not for trading or other speculative purposes. To reduce the counterparty risk, hedging transactions are generally only concluded with leading Hungarian or international financial institutions or Deutsche Telekom. Nevertheless, hedge accounting is not applied to such transactions, considering that not all the criteria in IFRS 9 are met.

The detailed descriptions of risks, the management thereof as well as sensitivity analyses are provided below. These sensitivity analyses calculate with reasonably possible changes in the relevant risk variables and their impact on profit before tax. The impacts disclosed below for the reported periods are subject to an average effective income tax rate of approximately 25%, i.e. the impact on Profit for the year would be approximately 75% of the pre tax amount in a year that is free from significant one-off non-deductible pre-tax impacts and significant changes in the tax legislations. The potential impacts disclosed (less tax) would be the same on the Group's Equity.

There were no major changes in these risks compared to the previous reporting period.

5.1.1 Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk:

- foreign currency risk;
- interest rate risk;
- price risk.

The fundamentals of Magyar Telekom's financing strategy are established each year by the Board of Directors. The Group's policy is to borrow centrally using a balanced combination of medium term and short term loans, and fixed and floating interest rates on those loans. The Board of Directors has approved two debt protection ratio KPIs, and monitors their fulfillment annually. At the end of 2018 Magyar Telekom fulfilled both criteria; Total Debt to EBITDA ratio of 1.52 in 2018 (2017: 1.74), the allowed maximum of which would be 2.8 and EBITDA to Net financial result ratio of 10.81 in 2018, (2017: 8.58), the allowed minimum of which would be 3.0. The Group's Treasury is responsible for implementing the finance policy and for ongoing risk management. The details of foreign exchange, liquidity and counterparty risk management guidelines are determined and monitored by the Group's Treasury continuously.

Magyar Telekom is exposed to interest and foreign exchange (FX) rate risk associated with its interest bearing assets and liabilities and anticipated transactions. As the vast majority of the revenues and expenses of the Hungarian entities arise in HUF, the functional currency of the Hungarian entities of Magyar Telekom is HUF. Consequently, Magyar Telekom's objective is to minimize the level of its financial risk in HUF terms.

For the presentation of market risks, we also provided sensitivity analyses that show the effects of hypothetical changes of relevant risk variables on Profit before tax. These hypothetical changes were modeled to present a reasonably possible change in the relevant risk variables. The periodic effects are determined by relating the hypothetical changes in the risk variables to the balance of financial instruments at the end of the latest reporting period (2018) and the preceding reporting period (2017). The balances at the end of the reporting period are usually representative for the year as a whole; therefore the impacts are calculated using the year end balances. The methods and assumptions used in the sensitivity calculations did not change significantly compared to the previous period. As a result of the still rather volatile international capital and securities markets, higher fluctuations of the FX and interest rates are also possible.

5.1.1.1 Foreign currency risk

Foreign currency risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in FX rates. Currency risks primarily arise on financial instruments denominated in a currency that is not the functional currency of the given operating segment of the Group. Differences resulting from the translation of the foreign subsidiaries' financial statements into the Group's presentation currency are not taken into consideration. Relevant risk variables are generally all non-functional currencies in which Magyar Telekom has financial instruments.

In order to mitigate FX risk in case of FX denominated financial instruments, Magyar Telekom minimized its foreign currency borrowings in the past years, or covered them with derivative instruments to substantially reduce FX risk.

(a) FX risks arising on loans from DTIF and related swaps with DT AG

Several related party loans taken to finance general needs of the Group from Deutsche Telekom or its financing vehicle, Deutsche Telekom International Finance B.V. (DTIF) are denominated in EUR, while, at the same time, cross-currency interest rate swaps or FX swaps are concluded with Deutsche Telekom AG (DT AG) to fix the actual cash flows of Magyar Telekom in HUF for the whole nominal amount and interest payments of these loans. Even though the Group does not apply hedge accounting, the change in the HUF/EUR exchange rate has limited (net) impact on Profit before tax related to the hedged loans and the hedging transactions together.

Sensitivity analysis

A reasonably possible strengthening or weakening of the EUR in the table below against HUF as at the end of the reporting period would have affected the measurement of financial instruments denominated in a foreign currency and increased (+)/ decreased (-) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant and ignores any impact of forecast sales and purchases. As the profit or loss effect would be the same as the equity effect, only the former is disclosed.

In HUF millions	Profit or loss	
	Strengthening	Weakening
At December 31, 2018		
EUR/HUF (10% movement)		
Loan	(8,782)	8,782
Swap agreements	9,364	(9,364)
Net effect	582	(582)
At December 31, 2017		
EUR/HUF (10% movement)		
Loan	(10,184)	10,184
Swap agreements	10,924	(10,924)
Net effect	740	(740)

(b) Other FX exposure

The remaining FX exposure of Magyar Telekom is mostly related to (i) holding foreign currency cash balances in its subsidiaries in the Southern and Eastern Europe region, and (ii) operating activities through revenues from, and payments to, international telecommunications operators as well as capital and operating expenditure contracted with vendors in foreign currency. In line with currency hedging policy, the Company holds sufficient amounts of foreign currencies on its bank accounts or buys foreign currencies through FX forward transactions, the amounts of which are determined considering the balance of short term FX denominated trade and leases payables and trade receivables in order to hedge the currency risk arising in connection with those assets and liabilities. The Group's foreign currency denominated liabilities (other than the above described loans) exceed the Group's foreign currency denominated assets, therefore changes of the functional currencies' exchange rates would have the following impact on the profit of the Group.

In order to reduce the above exposure, Magyar Telekom occasionally enters into derivative contracts. The negative fair value of the related open short term forward positions was HUF 0.1 billion as of December 31, 2018 (2017: HUF 0.2 billion liability). These positions were opened to hedge the FX risks of future FX payments exceeding FX income.

Sensitivity analysis

A reasonably possible strengthening or weakening of the currencies in the table below against HUF and MKD as at the end of the reporting period would have affected the measurement of financial instruments denominated in a foreign currency and increased (+)/ decreased (-) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular interest rates, remain constant and ignores any impact of forecast sales and purchases. As the profit or loss effect would be the same as the equity effect, only the former is disclosed.

In HUF millions	**Profit or loss**	
	Strengthening	**Weakening**
At December 31, 2018		
EUR/HUF (10% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank balances	(3,683)	3,683
Related forward agreements	1,637	(1,637)
Net effect	(2,046)	2,046
USD/HUF (15% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank balances	(621)	621
Related forward agreements	76	(76)
Net effect	(545)	545
EUR/MKD (10% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank balances	166	(166)
Related forward agreements	0	0
Net effect	166	(166)
USD/MKD (10% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank balances	11	(11)
Related forward agreements	0	0
Net effect	11	(11)

In HUF millions	Profit or loss	
	Strengthening	Weakening
At December 31, 2017		
EUR/HUF (10% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank	(1,764)	1,764
Related forward agreements	1,992	(1,992)
Net effect	228	(228)
USD/HUF (15% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank	(463)	463
Related forward agreements	430	(430)
Net effect	(33)	33
EUR/MKD (10% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank	(95)	95
Related forward agreements	0	0
Net effect	(95)	95
USD/MKD (10% movement)		
Net balance of FX denominated trade payables and trade receivables plus bank	32	(32)
Related forward agreements	0	0
Net effect	32	(32)

As a result of the volatile international capital and securities markets, even a more than 10% fluctuation of the functional currency HUF against EUR, a more than 15% fluctuation of the functional currency HUF against USD and a more than 10% fluctuation of the functional currency MKD against the EUR and USD is possible as extraordinary market conditions may cause extreme volatility on FX markets.

5.1.1.2 Interest rate risk

Magyar Telekom is also exposed to interest rate fluctuations. This is due to the fact that changing interest rates affect the fair value of the fixed rate instruments and also affect the cash flows through the floating rate instruments.

Changes in the market interest rates of non-derivative financial instruments with fixed interest rates only affect income if these are measured at their fair value. On the other hand, all financial instruments with fixed interest rates (which are carried at amortized cost) are not subject to cash flow interest rate risk.

Changes in the market interest rate of interest rate derivatives (interest rate swaps, cross-currency swaps) that are not part of a hedging relationship as set out in IFRS 9 affect Other finance expense - net (net gain/loss from re-measurement of the financial assets to fair value).

Changes in market interest rates affect the interest income or expense of non-derivative floating-interest financial instruments for which no cash flow hedges are in place.

(a) Financial assets

Excess cash of the Group's Hungarian operations is primarily used to repay loans, however, significant amount of cash of the Group's Macedonian subsidiary is mostly held in local banks. These amounts are deposited primarily on fixed interest rate terms in order to minimize exposure to market changes that would potentially adversely affect the cash flows from these instruments.

Due to the extremely low interest rates, even a reasonably possible change in the interest rates would not have a significant impact on the Group's interest income.

(b) Financial liabilities

Financial liabilities exposed to interest rate risk are primarily the related party (DTIF, DT AG) and third party loans and the related swap agreements in place. These loans are almost exclusively taken by the Company as the financing of the Group is managed centrally. The analysis below describes the Group's net exposure to the net interest rate risks related to the loans and the related swap agreements.

As the vast majority of debt portfolio is denominated in HUF, or swap agreements are in place so that the loans payable are exposed to changes in HUF interest rates, the Group is mostly exposed to the HUF interest rate fluctuations for its financial liabilities. To control this interest rate risk, a combination of fixed and floating rate debt is used. Fixed interest-bearing debts (including loans swapped to fixed interest and excluding loans swapped to floating interest) made up 100% of the Group's total debt as of December 31, 2018 (2017: 89%).

Cash-flow sensitivity analysis for variable rate instruments

The Group had no floating interest-bearing debts as of December 31, 2018. Floating interest-bearing debts (including loans swapped to floating interest and excluding loans swapped to fixed interest) made up 11% of the Group's total debt as of December 31, 2017.

A reasonably possible change of 100 basis points in interest rates during the reporting period (assuming the year-end balance throughout the reporting period) would have increased (decreased) equity and profit or loss by the amounts shown below. This analysis assumes that all other variables, in particular foreign currency exchange rates, remain constant. As the profit or loss effect would be the same as the equity effect, only the former is disclosed.

In HUF millions	Profit or loss	
	100bp increase	100bp decrease
At December 31, 2018		
Floating rate instrument	-	-
IR swap	-	-
Cash-flow sensitivity (net)	-	-
At December 31, 2017		
Floating rate instrument	(134)	134
IR swap	(155)	155
Cash-flow sensitivity (net)	(289)	289

5.1.2 Credit risk

Credit risk is the risk that one party to a financial instrument will cause a financial loss for the other party by failing to discharge an obligation.

The maximum exposure to credit risk as at the end of the reporting period are represented by the carrying amounts of the financial assets in the Statement of financial position. Guarantee agreements reducing the maximum exposure to credit risk as at the end of the reporting period are described later in this section.

The vast majority of credit risks may arise in respect of Cash and cash equivalents, Bank deposits with original maturities over 3 months and Trade receivables, most of which have short term maturities.

In line with the Group's risk management policy Magyar Telekom Group companies deposit the vast majority of excess cash in banks rated at least BBB+ (or equivalent), or make efforts to get guarantees for these fixed term deposits from banks rated at least BBB+. We, however, also have current accounts in banks with lower rating than this.

Cash and cash equivalents and Bank deposits with maturities over 3 months held in Macedonia are primarily denominated in MKD and EUR. Cash and cash equivalents and Bank deposits with maturities over 3 months deposited in Macedonia run higher counterparty risk, due to the small amount of internationally substantial financial institutions in that countries. The deposits in Macedonia of HUF 6.4 billion as of December 31, 2018 (2017: HUF 4.9 billion) are fully covered with bank guarantees issued by international financial institutions rated at BBB.

Concentrations of credit risk relating to trade receivables are limited due to the large number of customers comprising the Group's customer base and their dispersion across many different geographic areas and industries.

No financial assets other than trade and other receivables had to be impaired in the reported years, as they are neither past due nor are there any signs of impairment.

The following table contains the carrying amount of trade receivables broken down by country of operation. The vast majority of these balances are denominated in the functional currency of the countries of operations (HUF in Hungary and MKD in Macedonia).

In HUF millions	**At December 31,**	
	2017	**2018**
Hungary	130,277	150,647
Macedonia	13,365	13,806
Other	795	818
	144,437	165,271

The amounts in the table above are shown net of provisions for impairment losses. The annual bad debt expense of the Group in 2018 was 1.4% (2017: 0.9%) of the consolidated revenues. Adverse changes in customer payment behavior in the future, however, may result in higher impairment losses. Each additional 1 percentage point of uncollectible revenue would result in additional impairment charges of HUF 6.6 billion in 2018 (in 2017: HUF 6.1 billion, considering only the continuing operations).

There are varying credit checking practices applied across the members of the Group as described below.

Hungary

Credit checking at the time of the service request is carried out automatically by the credit checking application. A variety of checks including checking the bankruptcy list, the internal database of risky installation locations, the collection history of the past 6 months, the outstanding debt and the joint database of debtors of the Hungarian mobile operators are performed depending on the service to be used. The Fraud Detecting System monitors extreme usage and fraudulent behavior of customers for mobile, fixed-line and Internet services. In case of business customers, account managers check if the customer has outstanding debts.

Dunning procedures are run automatically by the billing systems and include various reminder tools like SMS, reminder message via Telekom APP, telephone calls, reminder letters, reminder emails, restricted service, termination letters and disconnections. In case of medium and large enterprises dunning process starts manually (first reminder letter). After the first step, this process is also automated. Based on the effective laws and regulations and over a minimum overdue amount we apply varying and customized reminder procedures with specific deadlines to the different customer groups. After the termination of the contract and depending on the expected success of the process, we combine the different collection steps of involving external partners, selling the outstanding debt or initiating legal proceedings. All parts of the process are regulated by internal directives.

Macedonia

The process of managing the credit risk from operating activities includes preventive measures such as creditability checking and prevention barring, corrective measures during legal relationship for example reminding and disconnection activities, collaboration with collection agencies and collection after legal relationship as litigation process and court proceedings. The overdue payments are monitored based on customer type, amount of debt, average invoiced amount and number of disconnections. The credit risk is controlled through credibility checking – which determines that the customer is not indebted and the customers' credit worthiness and through preventive barring – which determines the credit limit based on the usual level of the customer's previous traffic revenues. There is no concentration of risk in Macedonia either with any single customer or group of customers with similar characteristics. The procedures in Macedonia ensure on a permanent basis that sales are made to customers with an appropriate credit history and that an acceptable level of credit exposure is not exceeded.

5.1.3 Liquidity risk

Liquidity risk is the risk that an entity may encounter difficulty in meeting obligations associated with financial liabilities.

Prudent liquidity risk management implies maintaining sufficient Cash and cash equivalents and Bank deposits as well as available funding through adequate amount of committed credit lines. The Group's Treasury management aims at maintaining flexibility in funding by keeping committed credit lines available. The undrawn credit lines amounted to HUF 43.5 billion as at December 31, 2018 (2017: HUF 41.0 billion). In addition to the above, Deutsche Telekom confirmed its readiness to finance Magyar Telekom Group's budgeted financing needs until the end of June 2020.

The following two tables summarize the maturity structure of Magyar Telekom's financial liabilities including the interest payable on those liabilities as of December 31, 2018 and 2017. As the majority of the financial liabilities are paid from the cash generated from the ongoing operations, the maturity analysis of the financial assets as at the end of the reporting periods (in comparison with the financial liabilities) would not be useful, therefore, is not included in the tables below.

December 31, 2018 (in HUF millions)	Total	within 1 year	1 to 5 years	after 5 years
Trade payables	175,312	175,312	-	-
Financial liabilities to related parties	246,003	114,808	131,195	-
Bank loans	-	-	-	-
Finance lease liabilities	9,551	1,827	5,053	2,671
Other financial liabilities	53,321	8,534	16,728	28,059
Total other financial liabilities	62,872	10,361	21,781	30,730
Total cash flows	484,187	300,481	152,976	30,730
Open swap positions' cash flows				
Gross cash inflow in EUR million	290	10	280	-
Gross cash inflow in HUF million (at spot rate)	93,238	3,215	90,023	-
Gross cash outflow in HUF million	95,291	4,844	90,447	-
Net cash inflow in HUF million	(2,053)	(1,629)	(424)	-
Open forward positions' cash flows				
Gross cash inflow in EUR million	93	93	-	-
Gross cash inflow in USD million	2	2	-	-
Total gross cash inflow in HUF million (at spot rate)	30,462	30,462	-	-
Gross cash outflow in HUF million	30,521	30,521	-	-
Net cash inflow in HUF million	(59)	(59)	-	-

December 31, 2017 (in HUF millions)	Total	within 1 year	1 to 5 years	after 5 years
Trade payables	135,446	135,446	-	-
Financial liabilities to related parties	227,101	18,562	208,539	-
Bank loans	-	-	-	-
Finance lease liabilities	10,925	2,079	5,076	3,770
Other financial liabilities	52,192	7,875	16,298	28,019
Total other financial liabilities	63,117	9,954	21,374	31,789
Total cash flows	425,664	163,962	229,913	31,789
Open swap positions' cash flows				
Gross cash inflow in EUR million	352	62	290	-
Gross cash inflow in HUF million (at spot rate)	109,170	19,229	89,941	-
Gross cash outflow in HUF million	113,396	18,106	95,290	-
Net cash inflow in HUF million	(4,226)	1,123	(5,349)	-
Open forward positions' cash flows				
Gross cash inflow in EUR million	64	64	-	-
Gross cash inflow in USD million	11	11	-	-
Total gross cash inflow in HUF million (at spot rate)	22,696	22,696	-	-
Gross cash outflow in HUF million	23,037	23,037	-	-
Net cash inflow in HUF million	(341)	(341)	-	-

The average maturity of Magyar Telekom's debt portfolio was 1.36 years as at December 31, 2018 (2017: 2.19 years). The floating interest payments arising from the financial instruments were calculated using the last interest rates fixed before December 31, 2018 and 2017.

5.2 Capital risk management

The Group's objectives when managing capital are to safeguard the Group's ability to continue as a going concern in order to provide returns for shareholders and benefits for other stakeholders and to maintain an optimum capital structure to reduce the cost of capital.

The Company's management proposes to the owners (through the Board) of the Company to approve dividend payments or adopt other changes in the Company's equity capital in order to optimize the capital structure of the Group. This can be achieved primarily by adjusting the amount of dividends paid to shareholders, or alternatively, by returning capital to shareholders by capital reductions, selling or buying own shares. Consistent with others in the industry, the Group monitors capital on the basis of the gearing ratio.

This ratio is calculated as Net debt divided by Equity (including Non-controlling interest) and Net debt. Net debt is calculated as follows:

- Current and non current financial liabilities to related parties – Note 4.4.1
- plus Other current and non current financial liabilities – Note 4.4.2
- less Cash and cash equivalents – Note 4.2.1
- less Other current financial assets – Note 4.2.3.1

During 2017 and 2018, the Group's mid and long term target as approved by the Board was to maintain a gearing ratio within 30% to 40%. The gearing ratio at December 31, 2018 was 30.8% (2017: 34.8). The Company paid HUF 26,068 million dividend in 2018 (HUF

26,067 million dividend in 2017), and the Company's Board recommends to declare a HUF 26,068 million dividend at the April 2019 Annual General Meeting.

In addition to the above, according to the Hungarian Civil Code, Magyar Telekom Plc. has to ensure that the Company's Equity in the standalone financial statements does not fall below two thirds of its Common stock. The Company is in compliance with this regulation, and no such statutory regulation exists for consolidated equity.

The equity capital, which the Group manages, amounted to HUF 615 billion on December 31, 2018 (2017: HUF 580 billion).

6 INCOME TAX

6.1 Income taxes – accounting policies

Income tax expense comprises current and deferred tax. It is recognised in profit or loss except to the extent that it relates to a business combination, or items recognised directly in equity or in other comprehensive income.

6.1.1 Current taxes

Current tax comprises the expected tax payable or receivable on the taxable income or loss for the year and any adjustment to the tax payable or receivable in respect of previous years. The amount of current tax payable or receivable is the best estimate of the tax amount expected to be paid or received that reflects uncertainty related to income taxes, if any. It is measured using tax rates enacted or substantively enacted at the reporting date. Current tax also includes any tax arising from dividends. Current tax assets and liabilities are offset only if certain criteria are met.

Income taxes comprises of corporate income taxes and other income taxes.

6.1.1.1 Corporate income taxes

Corporate income taxes are payable to the central tax authorities of the countries in which the Group's consolidated entities operate. The basis of the tax is the taxable entities' accounting profit adjusted for non-deductible and non-taxable items. The nominal tax rates and the determination of the tax bases vary among the countries in which the Group operates.

As Magyar Telekom Plc. is listed on the Budapest Stock Exchange, it was obliged to adopt IFRSs in its statutory financial statements from 2017 in accordance with the Act C of 2000 on Accounting. In the first and in the second year following the IFRS transition, taxpayers, who adopt IFRS in their statutory financial statements, are obliged to pay the total sum of their current taxes (i.e. corporate income tax and local business tax) calculated for the tax year preceding the year of the IFRS transition, if in these two years their current tax liabilities are lower than in the tax year preceding the IFRS transition (minimum tax). Magyar Telekom Plc. does not have this minimum tax payment obligation in 2017 and in 2018 either.

6.1.1.2 Other income taxes

Other income taxes include certain local and central taxes levied in Hungary on the companies' net margins, usually determined at a substantially higher level than the corporate tax base, but applying a significantly lower tax rate.

6.1.2 Deferred taxes

Deferred tax is recognized applying the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Consolidated financial statements.

Deferred tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction (other than a business combination) that at the time of the transaction affects neither accounting nor taxable profit.

Deferred tax is determined using income tax rates that have been enacted or substantially enacted by the financial statement date and are expected to apply when the related deferred tax asset is realized or the deferred tax liability is settled.

Deferred tax assets are recognized to the extent that it is probable that future taxable profit (or reversing deferred tax liabilities) will be available against which the temporary differences can be utilized.

Deferred tax is measured at the tax rates that are expected to apply to temporary differences when they reverse using income tax rates enacted or substantially enacted at the reporting date.

6.2 Income taxes in the Consolidated Statement of profit or loss and other comprehensive income

The table below shows the income tax expenses charged in the Profit for the year.

	For the year ended December 31,	
In HUF millions	**2017**	**2018**
Corporate income tax	1,553	2,434
Other income taxes	8,850	8,991
Deferred income taxes	5,555	1,908
Total income tax expense	15,958	13,333

6.2.1 Tax expense reconciliation

The reconciliation between the reported income tax expense and the theoretical amount arising by applying the statutory income tax rates is as follows:

		For the year ended December 31,	
In HUF millions		**2017**	**2018**
Consolidated IFRS profit before income tax		56,204	59,782
Tax at 9%		(5,058)	(5,380)
Impact of different tax rates	(a)	(140)	(124)
Tax shield of items not subject to income tax	(b)	56	1,010
Tax impact of non deductible items	(c)	(2,557)	(742)
Other income taxes	(d)	(8,850)	(8,991)
Impact of tax deductibility of other income taxes	(e)	797	809
Energy suppliers' tax	(f)	(180)	-
(De)/recognized deferred tax on tax losses	(g)	(272)	(19)
Investment tax credit accretion	(h)	246	104
Income tax expense		(15,958)	(13,333)
Effective tax rate		28.39%	22.30%

(a) Impact of different tax rates

From January 1, 2017 a flat tax rate of 9% is effective in Hungary.

This line of the reconciliation includes the tax impacts of the different tax rates of the foreign countries where the Group is also present through its subsidiaries. The corporate tax rate is 10% in Macedonia, 16% in Romania and 10% in Bulgaria in the reported years. This line of the reconciliation includes the tax impacts of the above differences compared to the 9% general tax rate of Hungary applied to the profit before tax of the Group.

(b) Tax shield of items not subject to income tax

This line of the reconciliation primarily includes the tax shield impact of expenses, which are not included in the consolidated profit before tax, but deductible when determining the standalone corporate income tax base. These items include the depreciation of assets (or additional values of assets) which are not included in the assets of the consolidated statements of financial position, and which are not considered in the deferred tax calculation.

(c) Tax impact of non deductible items

This line of the reconciliation includes the negative tax impact of the expenses included in the consolidated profit and loss, but non deductible when determining the standalone corporate income tax base. These items primarily include the non deductible receivable impairment and write-downs and penalties.

(d) Other income taxes

Other income taxes include certain local and central taxes levied in Hungary on the companies' net margins, determined usually at a substantially higher level than the corporate tax base, but with substantially lower tax rates (max 2%). As the first line of the reconciliation calculates theoretical tax expense calculated using the general corporate tax rate, the Hungarian local business tax and the innovation fee impose additional income tax expenses for the Hungarian entities of the Group, included in this line of the reconciliation.

(e) Deductibility of other income taxes from the corporate tax base

The Hungarian local business tax and innovation fee are deductible expenses for corporate tax purposes, the positive tax impact of which is included in this line of the reconciliation.

(f) Energy suppliers' tax

This line of reconciliation includes the Energy suppliers' additional tax levied on energy supplier companies' profits in Hungary. The tax base is the profit before tax adjusted by certain items that increase or decrease the tax base. Magyar Telekom Plc. is also considered as an energy supplier company subject to the energy suppliers' additional tax, in proportion to its energy revenues. As tax credit can be utilized for the energy supplier's tax to the extent that the tax liability can be decreased by a half, this effect is also included in this line of the reconciliation. As Magyar Telekom Plc. has completely ended its energy supplier's activity, this tax would no longer be applicable from 2018.

(g) (De)/recognized deferred tax on tax losses

Deferred tax asset is recognized on tax losses only to the extent that the realization of the related tax benefit is probable in the foreseeable future. Deferred tax assets on tax losses that will probably not be recovered are un-recognized in the period of the loss or de-recognized in subsequent periods. On the other hand, when the recoverability of the previously un/derecognized tax losses becomes probable, these deferred tax assets are recognized.

(h) Investment tax credit accretion

Investment tax credit accretion includes the increase of the net present value of the investment tax credit deriving from the utilization of the tax credits in periods subsequent to the year of recognition. See also Note 6.3.2.1.

6.3 Income taxes in the Statement of financial position

6.3.1 Current taxes in the Statement of financial position

Current income tax receivable and payable balances in the Statements of financial position represent the amount of corporate and other income taxes receivable from, and payable to, the tax authorities of the countries in which the Group operates.

6.3.2 Deferred taxes in the Statement of financial position

The Group's deferred tax balances and the movements therein are as follows:

In HUF millions	Balance at Dec. 31, 2016	Effect on profit	Other movements	Change due to sale of subsidiary	Balance at Dec. 31, 2017	Effect on profit	Other movements	Balance at Dec. 31, 2018
Deferred tax assets and (liabilities)								
Investment tax credits (Note 6.3.2.1)	10,907	(3,169)			7,738	(3,582)		4,156
Net operating loss carry-forward (Note 6.4.)	622	(272)			350	(202)		148
Withholding tax	(119)	119			-	-		-
Other financial assets	(325)	397	(119)		(47)	4	(102)	(145)
Impairment of receivables and inventory	1,782	(371)			1,411	183		1,594
Property, plant and equipment and intangible assets	(9,627)	(907)	(57)	714	(9,877)	914	(39)	(9,002)
Goodwill	(11,977)	(866)			(12,843)	(1,638)		(14,481)
Trade and other payables	2	67			69	(69)		-
Loans and other borrowings	(1,481)	1,481			-	1		1
IFRS transition	-	(1 362)			(1,362)	708		(654)
Deferred revenue	(45)	(97)			(142)	99		(43)
First-time application of IFRS 15	-	-			-	1,436	(1,436)	-
Provisions for liabilities and charges	1,594	(575)			1,019	238		1,257
Total net deferred tax liability	(8,667)	(5,555)	(176)	714	(13,684)	(1,908)	(1,577)	(17,169)
Of which deferred tax liabilities	(8,740)				(13,743)			(17,246)
Of which deferred tax assets	73				59			77
<u>Items included in other movements:</u>								
First-time application of IFRS 15							(1,436)	
Relating to the merger of subsidiary			(119)				(102)	
Investment tax credit adjusted against P&L			(57)				(39)	
Relating to the sale of subsidiary				714				

Items included in the Other movements column in 2018 indicate the investment tax credit decrease (HUF 39 million), which was adjusted against the P&L in deferred taxes, as well as the tax effect of the fair value or foreign exchange adjustments relating to the subsidiaries (HUF 73 million for ITgen merger and HUF 29 million for Maktel). Items in the line First-time application of IFRS 15 in 2018 include the effect of the transition to IFRS15, the standard on Revenue from contracts with customers.

Items included in the Other movements column in 2017 indicated the investment tax credit decrease (HUF 57 million) which was adjusted against the P&L in deferred taxes, as well as the tax effect of the fair value adjustment relating to the merger of Serverinfo Kft (HUF 119 million). The deferred tax balances as at December 31, 2017 did not include the tax effects of the Montenegrin subsidiary (HUF 714 million), as Crnogorski Telekom constituted a discontinued operation. The column of Change due to sale of subsidiary indicates this difference in 2017.

The Group consists of a number of legal entities, most of which have deferred tax assets and liabilities. The assets and liabilities are netted by legal entity so that one legal entity has either a deferred tax asset or a liability and the consolidated Statement of financial position includes these balances accordingly.

The Group's net deferred tax liability balance as at December 31, 2018 is HUF 17,169 million which includes a high amount of individual deferred tax asset and liability items (see in the above table). Of these items, approximately HUF 2,829 million net deferred tax asset is expected to reverse in 2019 (deferred tax asset of HUF 3,356 million and deferred tax liability of HUF 527 million).

The Group's net deferred tax liability balance as at December 31, 2017 is HUF 13,684 million which includes a high amount of individual deferred tax asset and liability items (see in the above table). Of these items, approximately HUF 2,342 million net deferred tax asset is expected to reverse in 2018 (deferred tax asset of HUF 2,572 million and deferred tax liability of HUF 230 million).

Deferred tax assets arising on investment tax credits are recognized against the capitalized cost of the related investment.

Temporary differences associated with investments in subsidiaries for which deferred tax liabilities or assets have not been recognized amounted to a net liability of HUF 14,916 million at December 31, 2018 (HUF 11,016 million at December 31, 2017).

Deferred tax liability on goodwill is related to the goodwill arising from the acquisition of subsidiaries (Emitel and T-Mobile) in the Company's financial statements, which had merged into Magyar Telekom Plc. The amortization of goodwill is a tax deductible expense in corporate income tax, while under IFRSs there is no amortization accounted in the books. The difference deriving from the two types of accounting is represented by the deferred tax liability.

6.3.2.1 Investment tax credits

In order to increase broadband internet penetration in Hungary, companies investing over HUF 100 million in a year in broadband assets (e.g. DSL lines, UMTS assets) from 2003 could apply for a corporate tax reduction. MT accomplished such tax credit programs between 2003 and 2008. The tax credit programs commenced in 2012 and 2013 are "large investment" programs, which enable companies to invest not only in broadband related assets, if the investment value exceeds HUF 3 billion and certain special criteria (i.e. headcount increase) are met. In case of both types of tax credit programs, the potential reduction of the corporate tax charge is defined as a percentage of the companies' capital investment in qualifying assets. As both of these investment tax credits are of a government grant nature, Magyar Telekom recognized the deferred tax asset against the cost of the related investment. There are no unrecognized tax credits. If the tax credits are not utilized in the year when earned, the amount of tax credits carried forward can be utilized at a higher amount as outstanding amounts are accreted. This accretion is recognized as an increase in the investment tax credit balance against a reduction in the current year deferred tax expense.

The following table shows the details of the tax credits in HUF millions:

Earned in year	Amount of qualifying investment	Amount of tax credit earned	Accretion recognized in tax expense to date	Tax credit utilized	Tax credit carried forward at December 31, 2018	Tax credit carried forward at December 31, 2017	Expires in year
2012	11,074	3,375	517	(3,892)	-	2,564	2021
2013	13,782	4,452	490	(,954)	3,988	5,004	2023
2014	490	156	12	-	168	170	2023
Total	25,346	7,983	1,019	(4,846)	4,156	7,738	

In order to utilize the tax credits and certain tax deductibility opportunities earned by the Group's entities, they have to comply with strict requirements as set out in the relevant tax regulations. The most important requirement for all investment tax credits is that the relevant assets have to be operated for at least 5 years, which criteria was sufficiently fulfilled by the Company. However, for those earned in 2012 and in 2013 certain increase in headcount and/or salary has to be maintained for at least 4 subsequent years following the first year of tax credit utilization. The headcount of the Company has to be increased by 150 and maintained in the subsequent 4 years from the first utilization of the investment tax credit (which is 2012 and 2014). The Company fulfilled the headcount criterion by the end of 2018.
The 2013 tax credit program was finished in January 2014, so the first utilization of 2013 tax credit is in 2014. The base year for both programs is 2011.

6.4 Tax loss carry forwards

Deferred tax assets are recognized for tax loss carry forwards only to the extent that realization of the related tax benefit is probable.

The table below shows the tax losses carried forward of the Group.

Expires in year	Tax loss carry forwards at December 31, 2017	Tax loss carry forwards at December 31, 2018
2017	125	-
2018	22,442	55
2019	88	90
2020	129	133
2021	2	-
2022	2	2
2025	3,915	1,563
Total	26,703	1,843
Tax losses for which deferred tax is recognized	3,884	1,633
Tax losses for which deferred tax is not recognized	22,819	210
Total	26,703	1,843

The Hungarian corporate tax law was amended as of January 1, 2015 including that all tax loss carry forwards incurred up to December 31, 2014 may be used to reduce the pre-tax profit until no later than December 31, 2025.

6.5 Tax reviews

The tax authorities have commenced a comprehensive tax audit at Magyar Telekom Plc. in 2018 December in relation to the tax years of 2016 and 2017. As a result, additional tax assessments with penalties and penalty interest may be imposed in 2019. Management is not aware of any circumstances which may give rise to a potential material liability in this respect.

6.6 Dividends paid by Magyar Telekom Plc.

The dividends paid and payable by Magyar Telekom Plc. to its owners may be subject to withholding or income taxes of the owners, which do not have an impact on the amount of the dividend declared or on the Company's tax expense as these taxes – if any – are levied on the owners.

6.7 IFRS Transition of Magyar Telekom Plc.

As Magyar Telekom Plc. is listed on the Budapest Stock Exchange, it was obliged to adopt IFRS in its statutory financial statements from 2017 in accordance with the Act C of 2000 on Accounting. As a result of the IFRS transition, Magyar Telekom Plc. has an IFRS transition difference of HUF 21.8 billion, which qualifies as a corporate income tax increasing item. The corporate income tax incurred in relation to this transition difference will be paid in 3 equal instalments in 2017-2019.

Other companies of the Group did not elect to adopt IFRS for their local financial statements.

7 INVENTORIES

7.1 Inventories – accounting policies

Inventories are stated at the lower of cost or net realizable value using the historical cost method of accounting, and are valued on a weighted average basis. The cost of inventories comprises all costs of purchase, cost of construction and other costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale.

Phone sets are often sold for less than cost in connection with promotions to obtain new subscribers with minimum commitment periods (Note 3.4). Such loss on the sale of equipment is only recorded when the sale occurs if the normal resale value is higher than the cost of the phone set. If the normal resale value is lower than costs, the difference is recognized as impairment.

Impairment losses on Inventories are recognized in Other operating expenses.

7.2 Inventories in the statement of financial position

	At December 31,	
In HUF millions	**2017**	**2018**
Inventory for resale	16,247	17,286
Other inventory	1,111	2,069
Subtotal	17,358	19,355
Less allowances	(183)	(237)
	17,175	19,118

The impairment loss accounted or released for inventories is not material therefore no separate table of movements is disclosed.

The Group has no inventory pledged as security as at December 31, 2017 or December 31, 2018.

8 ASSETS HELD FOR SALE AND LIABILITIES ASSOCIATED WITH ASSETS HELD FOR SALE

8.1 Non current assets held for sale – accounting policies

An asset (typically real estate) is classified as held for sale if it is no longer needed for the future operations of the Group, and has been identified for sale, which is highly probable to take place within 12 months. These assets are accounted for at the lower of carrying value or fair value less cost to sell. Depreciation is discontinued from the date of designation to the held for sale status. When an item of PPE or intangible assets is designated for sale, and the fair value is determined to be lower than the carrying amount, the difference is recognized in the Profit for the year (Depreciation and amortization) as an impairment loss.

8.2 Assets held for sale in the statement of financial position

	At December 31,	
In HUF millions	**2017**	**2018**
Property, plant and equipment	162	-
Total assets held for sale	162	-

Assets held for sale include primarily land and buildings identified for sale, which is expected within 12 months, as a result of the continuing improvement of utilization of properties. These assets are presented at carrying amount as no impairment had to be recognized when reclassified as held for sale.

9 PROPERTY, PLANT AND EQUIPMENT

9.1 Property, plant and equipment (PPE) – accounting policies

Property, plant and equipment are stated at historical cost less accumulated depreciation and impairment losses.

The cost of an item of PPE comprises its purchase price, including import duties and non-refundable purchase taxes, after deducting trade discounts and rebates, any costs directly attributable to bringing the asset to the location and condition necessary for it to be capable of operating in the manner intended by management. The initial estimate of the costs of dismantling and removing the item and restoring the site on which it is located is also included in the costs if the obligation incurred has to be recognized as a provision according to IAS 37 – Provisions, Contingent Liabilities and Contingent Assets.

Government grants relating to the purchase of PPE are deducted from the original cost of the items and are recognized in the Profit for the year through the reduced amount of depreciation of the related assets over their useful lives. Investment tax credits relating to qualifying investment projects (Note 6.3.2.1) are also recognized in this manner.

Cost in the case of telecommunications equipment comprises of all expenditures including the cabling within customers' premises and borrowing costs of related loans.

Subsequent expenditure on an asset that meets the recognition criteria to be recognized as an asset or an addition to an asset is capitalized, while maintenance and repairs are charged to expense when incurred.

When assets are scrapped, the cost and accumulated depreciation are removed from the accounts and the loss is recognized in the Profit for the year (Depreciation and amortization).

When assets are sold, the cost and accumulated depreciation are removed from the accounts and any related gain or loss is recognized in the Profit for the year (Other operating income).

Depreciation is calculated on a straight-line basis from the time the assets are deployed and charged over their economic useful lives. On an annual basis, Magyar Telekom reviews the useful lives and residual values for consistency with current development plans and advances in technology. For further details on the groups of assets impacted by the most recent useful life revisions refer to Note 9.3. The annual revisions are conducted in the second quarter of the year and the resulting changes are applied from the third quarter of the year. In addition to the regular revisions, any investment decisions made throughout the year may also result in a change of useful life of a group of assets in any period of the year.

The useful lives assigned to different types of property, plant and equipment are as follows:

	Years
Buildings	5–50
Duct, cable and other outside plant	3–38
Other telecommunications equipment	2–25
Other equipment	2–12

Assets that are subject to amortization or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the assets' fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units – CGUs).

The fair values of the individual tangible and intangible assets of the Group in most cases cannot be determined as individual assets do not generate cash flows. Instead, the Group determines CGUs to which the individual assets are allocated and the fair values can only be determined at CGU level, primarily by using discounted cash flow analyses. See also Note 3.2. Corporate assets which have the distinctive characteristics of not generating cash inflows independently of other assets or groups of assets are allocated to CGUs when conducting impairment tests.

Goodwill is tested for impairment annually or more frequently if circumstances indicate that impairment may have occurred. When conducting the impairment tests, Magyar Telekom allocates goodwill to its cash generating units determined at operating segment level. See also Note 3.2. Operating segments may include one clearly identifiable company or a group of companies, or certain components of one company and other companies as well.

The Group establishes the segments' recoverable amounts by determining their fair value less cost to sell by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analyses and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs. The fair values determined as described above are used as a basis when establishing the need for an impairment of any goodwill allocated to the operating segments. See also Note 3.2. If the calculated fair value less cost to sell is lower than the carrying amount of the operating segment, goodwill is impaired.

The impairment losses of PPE and intangible assets are accounted for in the Depreciation and amortization line of the Statement of profit or loss.

9.2 Property, plant and equipment in the statement of financial position

In HUF millions	Land and equivalent rights	Buildings	Telecom. equipment	Other equipment	Total
At January 1, 2017					
Cost	8,194	154,876	1,079,697	104,073	1,346,840
Accumulated depreciation	(2,451)	(60,528)	(714,575)	(84,556)	(862,110)
Carrying amount	5,743	94,348	365,122	19,517	484,730
Of which held for sale					(1,556)
					483,174
Carrying amount – January 1, 2017	5,743	94,348	365,122	19,517	484,730
Exchange differences	-	(74)	(204)	(18)	(296)
Additions due to business combinations	432	3,644	66	1,951	6,093
Changes due to revisions of asset retirement obligations	-	297	(30)	-	267
Investments	1	2,125	44,986	10,256	57,368
Disposals	(20)	(995)	(48)	(289)	(1,352)
Depreciation charge	(74)	(5,003)	(51,721)	(7,428)	(64,226)
Decrease due to sale of subsidiary	(811)	(5,478)	(16,972)	(818)	(24,079)
Reclassifications	185	539	212	(936)	-
Carrying amount – December 31, 2017	5,456	89,403	341,411	22,235	458,505
At December 31, 2017					
Cost	7,873	151,129	1,014,408	104,535	1,277,945
Accumulated depreciation	(2,417)	(61,726)	(672,997)	(82,300)	(819,440)
Carrying amount	5,456	89,403	341,411	22,235	458,505
Of which held for sale					(162)
					458,343
Carrying amount – January 1, 2018	5,456	89,403	341,411	22,235	458,505
Exchange differences	3	692	1,562	165	2,422
Additions due to business combinations	-	-	779	(1,924)	(1,145)
Changes due to revisions of asset retirement obligations	-	-	140	(1)	139
Investments	34	2,061	52,692	7,386	62,173
Disposals	(665)	(4,708)	(538)	(278)	(6,189)
Depreciation charge	(77)	(5,106)	(59,791)	(7,784)	(72,758)
Reclassifications	22	1,226	(1,952)	704	-
Carrying amount – December 31, 2018	4,773	83,568	334,303	20,503	443,147
At December 31, 2018					
Cost	7,267	147,112	1,035,352	103,904	1,293,635
Accumulated depreciation	(2,494)	(63,544)	(701,049)	(83,401)	(850,488)
Carrying amount	4,773	83,568	334,303	20,503	443,147
Of which held for sale					-
					443,147

The closing balance of Property, plant and equipment (PPE) includes assets in the course of construction in an amount of HUF 59,250 million as at December 31, 2018 (2017: HUF 61,452 million). In the table above the assets in course of construction are shown in the categories where the asset is expected to be classified when placed into service.

Exchange differences include the translation impact arising on the consolidation of foreign subsidiaries of the Group.

Additions due to business combinations include the fair value or carrying value of the assets acquired by Magyar Telekom through business combinations at the time of the acquisition. Differences between the preliminary and the final purchase price allocations are also included in this line.

Changes due to revisions of asset retirement obligations represent the adjustments of the carrying amounts of the assets against a provision for asset retirement obligation (see also Note 13.2.4).

Investments represent the regular investing activity in PPE assets. The below table includes the Investments by type of operation.

In HUF millions	2017	2018
Investments in continuing operations	57,278	62,173
Investments in discontinued operations	90	-
	57,368	**62,173**

The below table includes the Depreciation charge by type of operation.

In HUF millions	2017	2018
Depreciation charge in continuing operations	(63,950)	(72,758)
Depreciation charge in discontinued operations	(276)	-
	(64,226)	**(72,758)**

The reclassifications between asset categories or their impact on depreciation expense was not material.

No impairment was identified in 2018 and 2017.

Included in buildings are assets sold and leased back under finance lease conditions. At December 31, 2018 the gross book value of the assets leased back is HUF 4,048 million (2017: HUF 4,048 million) and the net book value is HUF 1,249 million (2017: HUF 1,529 million).

Included mainly in buildings and telecom equipment are also assets leased under finance lease conditions other than sale and lease back. At December 31, 2018 the gross book value of the finance leased assets is HUF 1,157 million (2017: HUF 3,826 million) and the net book value is HUF 682 million (2017: HUF 1,060 million).

Included in telecommunications equipment at December 31, 2018 are assets leased under operating lease contracts to customers with a gross book value of HUF 55 million (2017: HUF 127 million) and 0 net book value (2017: HUF 0 million).

The Group has no PPE with restricted titles or pledged as security as at December 31, 2018 or December 31, 2017.

9.3 Review of useful lives

The reviews of the useful lives (and residual values) of property, plant and equipment during 2018 affected the lives of a large number of assets primarily inhouse network. The revisions resulted in the following change in the original trend of depreciation in the current and future years.

In HUF millions	2018	2019	2020	2021	After 2021
Increase / (decrease) in depreciation expense	10,282	3,010	1,622	115	(15,029)

10 INTANGIBLE ASSETS

10.1 Intangible assets – accounting policies

Intangible assets are stated at historical cost less accumulated amortization and impairment losses.

Acquired computer software licenses are capitalized on the basis of the costs incurred to acquire and bring to use. These costs are amortized over the estimated useful life of the software. Costs associated with developing or maintaining computer software programs are generally recognized as an expense as incurred. Costs directly associated with the production of identifiable and unique software products controlled by the Group, and that will probably generate economic benefits exceeding costs beyond one year, are recognized as intangible assets. Direct costs include the software development employee related costs and an appropriate portion of relevant overhead and borrowing costs. Computer software development costs recognized as assets are amortized over their estimated useful lives. Most computer software capitalized include acquired elements representing the majority of the cost and own costs incurred to a lesser extent. These are considered as non self developed software. Computer software fully developed by own resources represent an immaterial portion of all software, therefore these are not disclosed separately.

Costs associated with the acquisition of long term frequency licenses are capitalized. The present value of the future annual payments for the use of the frequencies are also capitalized if these payments can be estimated reliably, or otherwise recognized as Other operating expenses in the year the payment obligation refers to. The useful lives of concessions and licenses are determined based on the underlying agreements and are amortized on a straight line basis over the period from availability of the frequency for commercial use until the end of the initial concession or license term. Renewal periods are considered in the determination of useful life only if we are sure that it will be realized without further consideration to be transferred.

Amortization is calculated on a straight-line basis from the time the assets are deployed and charged over their economic useful lives. Other than goodwill, the Group has no intangible assets with indefinite useful life. The amortization expense is presented in the depreciation and amortization line of the Statement of profit or loss.

On an annual basis, Magyar Telekom reviews the useful lives for consistency with current development and replacement plans and advances in technology. For further details on the groups of assets impacted by the most recent useful life revisions refer to Note 10.3. The annual revisions are conducted in the second quarter of the year and the resulting changes are applied from the third quarter of the year. In addition to the regular revisions, any investment decisions made throughout the year may also result in a change of useful life of a group of assets in any period of the year.

The estimated useful lives of intangible assets other than goodwill are are as follows:

	Years
Software	2–24
Concessions and licenses	3–25
Other intangible assets	3–10

Goodwill represents the excess of the cost of an acquisition over the fair value of the Group's share of the net assets and contingent liabilities of the acquired subsidiary or business at the date of acquisition. Goodwill is carried at cost less accumulated impairment losses. Impairment testing is carried out on an annual basis for all goodwill in the last quarter of the year based on the carrying values as at September 30 of the year. Impairment losses on goodwill are not reversed. Gains and losses on the disposal of an entity or business include the carrying amount of goodwill allocated to the entity or business sold.

In determining whether an asset that incorporates both intangible and tangible elements should be treated under IAS 16 – Property, Plant and Equipment or as an intangible asset under IAS 38 – Intangible Assets, management uses judgment to assess which element is more significant and recognizes the assets accordingly.

Assets that are subject to amortization or depreciation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of the assets' fair value less costs to sell and its value in use. For the purposes of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units – CGUs).

The fair values of the individual tangible and intangible assets of the Group in most cases cannot be determined as individual assets do not generate cash flows. Instead, the Group determines CGUs to which the individual assets are allocated and the fair values can only be determined at CGU level, primarily by using discounted cash flow analyses. See also Note 3.2. Corporate assets which have the distinctive characteristics of not generating cash inflows independently of other assets or groups of assets are allocated to CGUs when conducting impairment tests.

Goodwill is tested for impairment annually or more frequently if circumstances indicate that impairment may have occurred. When conducting the impairment tests, Magyar Telekom allocates goodwill to its cash generating units determined at operating segment level. See also Note 3.2. Operating segments may include one clearly identifiable company or a group of companies, or certain components of one company and other companies as well.

The Group establishes the segments' recoverable amounts by determining their fair value less cost to sell by using valuation techniques. These include the use of recent arm's length transactions, reference to other instruments that are substantially the same, discounted cash flow analyses and option pricing models, making maximum use of market inputs and relying as little as possible on entity-specific inputs. The fair values determined as described above are used as a basis when establishing the need for an impairment of any goodwill allocated to the operating segments. See also Note 3.2. If the calculated fair value less cost to sell is lower than the carrying amount of the operating segment, goodwill is impaired.

The impairment losses of PPE and intangible assets are accounted for in the Depreciation and amortization line of the Statement of profit or loss.

10.2 Intangible assets in the statement of financial position

In HUF millions	Goodwill	Concessions and licenses	Software	Other	Total
At January 1, 2017					
Cost	218,098	198,322	296,027	20,444	732,891
Accumulated amortization	-	(51,245)	(194,250)	(9,133)	(254,628)
Carrying amount	218,098	147,077	101,777	11,311	478,263
Carrying amount – January 1, 2017	218,098	147,077	101,777	11,311	478,263
Exchange differences	-	(21)	(31)	6	(46)
Additions due to business combinations	631	-	-	117	748
Investments	-	-	24,827	4,180	29,007
Disposals	-	-	(72)	-	(72)
Decrease due to sale of subsidiary	(6,445)	(10,393)	(4,342)	(797)	(21,977)
Amortization charge	-	(15,151)	(26,278)	(3,036)	(44,465)
Reclassifications	-	-	-	-	-
Carrying amount – December 31, 2017	212,284	121,512	95,881	11,781	441,458
At December 31, 2017					
Cost	212,284	184,071	305,563	22,904	724,822
Accumulated amortization	-	(62,559)	(209,682)	(11,123)	(283,364)
Carrying amount	212,284	121,512	95,881	11,781	441,458
Of which held for sale					-
					441,458
Carrying amount – January 1, 2018	212,284	121,512	95,881	11,781	441,458
Exchange differences	-	112	241	205	558
Additions due to business combinations	820	-	-	2,618	3,438
Investments	-	15,713	27,564	2,095	45,372
Disposals	-	-	(102)	(1)	(103)
Amortization charge	-	(14,756)	(24,739)	(3,276)	(42,771)
Reclassifications	-	-	-	-	-
Carrying amount – December 31, 2018	213,104	122,581	98,845	13,422	447,952
At December 31, 2018					
Cost	213,104	200,075	333,289	26,934	773,402
Accumulated amortization	-	(77,494)	(234,444)	(13,512)	(325,450)
Carrying amount	213,104	122,581	98,845	13,422	447,952
Of which held for sale					-
					447,952

Exchange differences include the translation impact arising on the consolidation of foreign subsidiaries of the Group.

Additions due to business combinations include the fair value of assets acquired by Magyar Telekom through business combinations in the reported years and the goodwill arising on these business combinations. Differences between the preliminary and the final purchase price allocations are also included in this line.

Investments represent the regular investing activity in intangible assets. Additions to Concessions and licenses in 2018 include the cost of the right of use of the new frequency bands prolonged by the NMIAH for the Company in 2018 and the present value of the annual fees payable for the use of these frequencies until 2027. (See also Notes 4.4.2 and 34.)

The below table includes the Investments by type of operation.

In HUF millions	**2017**	**2018**
Investments in continuing operations	28,920	45,372
Investments in discontinued operations	87	-
	29,007	**45,372**

The amortization expense as well as the impairment losses of intangible assets including also goodwill is accounted for in the depreciation and amortization line of the Statement of profit or loss. The below table includes the Amortization charge by type of operation.

In HUF millions	**2017**	**2018**
Amortization charge in continuing operations	(44,224)	(42,771)
Amortization charge in discontinued operations	(241)	-
	(44,465)	**(42,771)**

The reclassifications between asset categories or their impact on amortization expense was not material.

The Group has no intangible assets with restricted title or pledged as security as at December 31, 2018 or December 31, 2017.

10.3 Useful lives

The reviews of the useful lives of intangible assets during 2018 affected the lives of a large number of assets primarily software. The revisions resulted in the following change in the original trend of amortization in the current and future years.

In HUF millions	**2018**	**2019**	**2020**	**2021**	**After 2021**
Increase / (decrease) in depreciation expense	(273)	(590)	289	148	425

10.4 Goodwill

For the goodwill impairment tests, the total amount of goodwill was allocated to the operating segments of the Group and the recoverable amounts of the operating segments were determined based on fair values less costs of disposal based on Level 3 inputs in the fair value calculations (Note 4.5.1). The recoverable amounts of the segments disclosed in the table below exclude net debts (Note 5.2), which are not allocated to the segments. For further information, please also see Note 3.2.

In HUF millions	As at December 31, 2017			As at December 31, 2018		
	Carrying amount of goodwill allocated	Carrying amount of operating segment (incl. goodwill)	Recoverable amount of operating segment	Carrying amount of goodwill allocated	Carrying amount of operating segment (incl. goodwill)	Recoverable amount of operating segment
MT-Hungary	192,085	791,806	1,703,753	192,905	785,911	1,250,068
Macedonia	20,199	63,265	180,004	20,199	65,160	181,057
Total	212,284	855,071	1,883,757	213,104	851,071	1,431,125

The Group regularly carries out an impairment test on goodwill in the last quarter of the financial years. During the annual impairment test conducted in the last quarter of 2017 and 2018 no goodwill impairment was established for any goodwill of the Group.

10.5 Significant individual other intangible assets

The Group's most significant individual other intangible assets are the mobile licenses. The carrying values and remaining amortization periods of the significant licenses are listed in the table below. For further information on these assets, please see Note 34.

In HUF millions	As at December 31, 2017 Carrying amount	As at December 31, 2017 Remaining amortization period (years)	As at December 31, 2018 Carrying amount	As at December 31, 2018 Remaining amortization period (years)
Hungarian mobile licenses acquired in 2014	82,192	17	77,211	16
Hungarian mobile licenses prolonged in 2018	31,717	4	39,509	11
Hungarian 3G license	3,581	2	1,788	1
Macedonian 4G license	2,534	16	2,473	15
Macedonian 2G/3G license	417	1	339	1
Other	1,071		1,261	
Total concessions and licenses	121,512		122,581	

11 INVESTMENTS IN ASSOCIATES AND JOINT ARRANGEMENTS

11.1 Associates and joint arrangements – accounting policies

Associates are entities over which the Group has significant influence but not control, generally reflecting a voting right between 20% and 50%.

Joint arrangements are arrangements where the parties are bound by a contractual arrangement of which two or more parties have joint control and which exist only when decisions about the relevant activities require the unanimous consent of the parties sharing the control.

If the parties that have joint control of the arrangement have rights to the net assets of the arrangement, it is a joint venture.

If the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement, it is a joint operation.

Investments in associates and joint ventures are accounted for using the equity method of accounting and are initially recognized at cost. The Group's investment in associates and joint ventures includes goodwill arising on acquisitions, and net of any accumulated impairment loss.

The Group's share of its associates' and joint ventures' post-acquisition profits or losses is recognized in the Profit for the year (Share of associates' and joint ventures' profits). The cumulative post-acquisition movements are adjusted against the carrying amount of the investment. When the Group's share of losses in an associate or joint venture equals or exceeds its interest in the company, the Group does not recognize further losses, unless it has incurred legal or constructive obligations or made payments on behalf of the associate or joint venture.

Unrealized gains on transactions between the Group and its associates and joint ventures are eliminated to the extent of the Group's interest in the company. Accounting policies of associates and joint ventures are adjusted where necessary to ensure consistency with the policies adopted by the Group.

In case of a joint operation, the assets, liabilities, revenues and expenses relating to the joint operation are recognized to the extent of the Group's interest in the joint operation.

11.2 Associates

The Group had no significant associates at December 31, 2017 and 2018. The Group had no contingent liabilities or commitments related to its associates at December 31, 2017 and 2018.

11.3 Joint ventures

The only joint venture of the Group at December 31, 2017 and 2018 was E2 Hungary Zrt. established in 2015 by Magyar Telekom Plc. and MET Holding AG. E2 Hungary provides energy services for business customers from 2016. The company's issued capital is HUF 200 million, and additional HUF 1,800 million was contributed as additional paid-in capital which were fully paid by both parties. The joint venture is set up by the parties on a 50:50 ownership basis with balanced rights in the management structure. The investment was recognized at cost in 2015 and E2 Hungary Zrt. is accounted for using the equity method. The operations of the company resulted in HUF 999 million profit in 2017 and HUF 721 million profit in 2018. Current year profit is preliminary at the date of the approval of these financial statements. HUF 1,038 million was declared as dividend in 2018 (HUF 193 million in 2017).

The Group had no contingent liabilities or commitments relating to its joint ventures at December 31, 2017 and 2018.

The following table shows the total assets and liabilities as at December 31, 2017 and 2018, and revenues and profit for the year ended December 31, 2017 and 2018 of E2, the single significant joint venture of the Group.

In HUF millions	2017	2018
Current assets	14,246	16,816
Non current assets	108	329
Current liabilities	11,356	14,423
Non current liabilities	-	-
Revenues	53,878	57,260
Profit/ (Loss) for the year	999	721

11.4 Joint operations

Magyar Telekom and Telenor Hungary agreed in 2015 to jointly operate and develop their 800MHz 4G mobile networks in all parts of Hungary except Budapest. The primary goal of the agreement was to accelerate 4G mobile broadband coverage rollout in the countryside and to offer higher bandwidth to the 4G customers, in line with the coverage obligations of the 800 MHz spectrum contract signed in 2014 with the NMIAH. Based on the agreement, Telenor Hungary maintains sites in West Hungary and Magyar Telekom operates sites in the eastern region of the country.

The Company assessed the agreement as joint operation as strategic decisions are made jointly by Magyar Telekom and Telenor, and there is no separate vehicle to control the operation of the arrangement. The Company does not share the obligations for liabilities and any returns or expenses beyond the assets included in the agreement.

Therefore only the assets owned by the Company are recognized while there is no need to present the partner's assets, liabilities, or revenues and expenses. The charges from MT to Telenor and from Telenor to MT are almost equal and settled on a net basis and accounted for in the statement of profit or loss and the effect of this settlement is not significant.

In case any of the parties initiates the termination of this contract, in order to ensure the continuous service for the customers the Company might be exposed to additional capital expenditure. The probability is estimated remote by the Management currently.

12 OTHER ASSETS

12.1 Other current assets

	At December 31,	
In HUF millions	2017	2018
Prepayments and advance payments	8,756	9,784
Other taxes receivable	1,659	2,130
Other	2,893	215
Total other receivables	13,308	12,129

12.2 Other non current assets

Other non current assets mainly include assets recognized from the costs to obtain contracts with customers (amounting to HUF 4,532 million, see also note 18.4) as at December 31, 2018, while the 2017 year-end balance mainly included long-term prepaid employee benefits relating to housing loans provided by the Group to employees at lower than market interest rates (see Notes 4.1.1.4 and 4.1.2.3).

13 PROVISIONS

13.1 Provisions – accounting policies

Provisions are recognized when Magyar Telekom has a present legal or constructive obligation (excluding executory contracts) as a result of past events and it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate of the amount of the obligation can be made.

Provisions are measured and recorded as the best estimate of the economic outflow required to settle the present obligation at the financial statement date. The estimate can be calculated as the weighted average of estimated potential outcomes or can also be the single most likely outcome. Expenses for provisions are recognized in the statement of profit or loss line where the actual expense is expected to be incurred. When a provision is released unused, it is released to the same line of the statement of profit or loss where it was originally provided for.

Provisions for obligations expected to fall due after 12 months are generally recognized at their present value and are accreted (against Interest expense) until utilization or reversal.

13.2 Provisions in the statement of financial position

In HUF millions	Severance	Share-based payments	Other employee related	Total Employee related	Legal cases	ARO	Other	Total
January 1, 2017	2,081	589	1,325	3,995	1,916	7,100	1,010	14,021
Amounts reversed	(633)	(44)	(37)	(714)	(156)	(73)	(846)	(1,789)
Additions	2,851	431	216	3,498	25	340	605	4,468
Decrease due to sale of subsidiary	-	(4)	(177)	(181)	(34)	-	-	(215)
Interest	-	4	-	4	(112)	157	-	49
Exchange rate difference	-	-	(3)	(3)	(3)	-	-	(6)
Amounts utilized (incl. interest component)	(2,694)	(128)	(534)	(3,356)	(624)	(36)	(14)	(4,030)
December 31, 2017	1,605	848	790	3,243	1,012	7,488	755	12,498
Of which current	1,356	0	528	1,884	871	19	493	3,267
Of which non current	249	848	262	1,359	141	7,469	262	9,231
January 1, 2018	1,605	848	790	3,243	1,012	7,488	755	12,498
Amounts reversed	(284)	(74)	(37)	(395)	(149)	(35)	(141)	(720)
Additions	2,999	731	5	3,735	1,173	174	1094	6,176
Interest	-	1	-	1	28	190	-	219
Exchange rate difference	-	1	10	11	32	(2)	(1)	40
Amounts utilized (incl. interest component)	(2,723)	(56)	(633)	(3,412)	-	(43)	(75)	(3,530)
December 31, 2018	1,597	1,451	135	3,183	2,096	7,772	1,632	14,683
Of which current	1,316	725	-	2,041	884	23	470	3,418
Of which non current	281	726	135	1,142	1,212	7,749	1,162	11,265

The Interest lines in the table above include the subsequent unwinding of the discount applied at initial recognition and the interest element of any provision recognized, as well as the release of the interest / accretion element in case of reversal of provisions.

Magyar Telekom does not expect any reimbursement with regards to the provisions recognized, therefore, no related assets have been recognized in the financial statements.

13.2.1 Severance

The majority of the provision for severance as at December 31, 2018 relates to the stand-by-pool and the employee terminations payable in 2019 in relation to the further efficiency improvement in Magyar Telekom Plc. The stand-by-pool of employees includes people whose legal status is an employee, however, these people do not provide services to the Company any more, but the Company provides a reduced amount of compensation and pays social security expenses for them. This is a way of severance that is not paid in one lump sum but in monthly installments following the discontinuation of services. The majority of the provision for severance as at December 31, 2017 also related to the stand-by-pool and the employee terminations paid in 2018 in relation to the efficiency improvement in Magyar Telekom Plc.

1,181 employees left the Group in 2018 (2017: 1,044), related to which termination payments were made. The balance of provision as at December 31, 2018 relates to 164 employees and former employees in the stand-by-pool (2017: 406).

The total payments made in relation to employee termination in 2018 amounted to HUF 4,486 million (2017: HUF 4,066 million).

13.2.2 Share-based payments

The bases of the provisions for share-based payments are described in Note 20.1.

13.2.3 Legal cases

Provisions for legal cases mainly include amounts expected to be paid to regulatory and competition authorities as well as to ex-employees and trading partners as a result of legal disputes. There are numerous legal cases for which provisions were recognized, which are individually not material.

13.2.4 Asset retirement obligations (ARO)

Asset retirement obligations primarily exist in case of the telecommunications structures constructed on third parties' properties. The Group carries out a revision of the necessary provisions every year. The revisions did not result in material changes in 2018 or 2017.

13.2.5 Other provisions

Other provisions include guarantee obligations, onerous contracts and further other individually small items.

14 OTHER CURRENT LIABILITIES

		At December 31,	
In HUF millions		**2017**	**2018**
Other taxes and social security		14,520	12,708
Salaries and wages	(a)	10,466	12,412
Contract liabilities (Note 18.4)		-	12,372
Deferred revenue and advances received		13,891	2,003
Advances received for asset-related grants	(b)	4,648	1,851
Dividend payable to non-controlling interests		22	24
Other liabilities		49	25
		43,596	41,395

(a) Salaries and wages

This line of the table includes also the liability arising from the bonus payment via the ESOP Organization (HUF 3,391 million in 2018). See also Note 20.1.2.5.

(b) Advances received for asset-related grants

In 2016 HUF 12.2 billion of EU funds were granted to Magyar Telekom Plc. as a result of the first and second rounds of a tender aimed at developing digital networks nationwide to cover households in Western and Eastern parts of Hungary with a fixed network capable of reaching speed of at least 30 Mbps. The Company used up HUF 3,318 million of this advance in 2018 (HUF 1,416 million in 2017). See also Note 9 for government grants relating to the purchase of PPE and Note 28 for details of Purchase of PPE and intangible assets.

15 OTHER NON CURRENT LIABILITIES

Other non current liabilities primarily include deferred revenues related to long term projects resulting from the non current contract liabilities. See also Note 18.4.

16 NON-CONTROLLING INTERESTS

Non controlling interests included the minority shareholders in Makedonski Telekom (MKT) and Crnogorski Telekom (CT) until 2016. As a result of the sale of Crnogorski Telekom, the 2017 and 2018 year-end balances include only the minority shareholders in MKT. See also Note 26.2.1.

In HUF millions	MKT	CT (discontinued)	Other	Total
Balance at January 1, 2017	33,319	9,524	-	42,843
Dividend declared	(2,728)	-	(592)	(3,320)
Total comprehensive income	2,879	(2,781)	-	98
Decrease due to sale of subsidiary	-	(6,743)	-	(6,743)
Balance at December 31, 2017	33,470	-	(592)	32,878
Transition to IFRS 9 and 15 (Note 1.3)	671	-	-	671
Dividend declared	(3,482)	-	-	(3,482)
Total comprehensive income	4,374	-	-	4,374
Balance at December 31, 2018	35,033	-	(592)	34,441

16.1 Summarized financial information on subsidiaries with material non-controlling interests

The information below includes the amounts as included in the consolidation, before inter-company eliminations.

a) Summarized balance sheets

In HUF millions	MKT		CT (discontinued)	
	2017	2018	2017	2018
Current assets	22,425	24,520	-	-
Current liabilities	(18,607)	(18,777)	-	-
Non-current assets	97,872	98,786	-	-
Non-current liabilities	(3,660)	(2,875)	-	-
Net assets	98,030	101,654	-	-

b) Summarized income statements

In HUF millions	MKT		CT (discontinued)	
	2017	2018	2017	2018
Revenues	51,795	54,680	2,023	-
Profit before income tax	7,930	8,035	184	-
Profit for the period	6,890	6,986	161	-

c) Summarized cash flows

In HUF millions	MKT		CT (discontinued)	
	2017	2018	2017	2018
Net cash generated from operating activities	19,227	19,453	3,691	-
Net cash from investing activities	(12,630)	(9,656)	(6,073)	-
				-
Dividends/capital reduction paid to Controlling interests	(3,566)	(4,550)	-	-
Dividends/capital reduction paid to Non-controlling interests	(2,728)	(3,482)	-	-
Other cash flows from financing activities	(2,417)	(1,792)	(4)	-
Net cash used in financing activities	(8,711)	(9,824)	(4)	-

16.2 Transactions with non-controlling interests

There were no material transactions with non-controlling interests in 2018 or 2017 other than the dividend payments.

The only significant non-controlling interest of the Group is the Macedonian Republic, holding shares in MKT. MKT and Magyar Telekom did not execute as part of its normal business activities any transactions that were individually material in the 2018 or 2017 financial year with companies controlled by the Macedonian Republic or companies over which the Macedonian Republic can exercise a significant influence.

17 LEASES

17.1 Leases – accounting policies

A lease is an agreement whereby the lessor conveys to the lessee in return for a payment or series of payments the right to use an asset for a period of time set out in the contract. A lease can be either an operating lease or a finance lease.

According to the accounting principle of substance over (legal) form, in practice not only those arrangements can accounting-wise qualify for leases that are denominated as leases.

In the Group's practice, the following can be in particular arrangements that are not legally leases but might contain leases:

- arrangements assigning network capacity rights to others
- outsourcing-type arrangements (i.e. whereby the Group outsources its own resources/assets/some of its activities/certain employees to another company).

An arrangement contains a lease, if the fulfilment of the arrangement is dependent on the use of a specific asset or assets or if the arrangement conveys a right to use the asset(s). The arrangement conveys the right to use the asset(s) when the arrangement conveys the control over the use of the underlying asset(s) for the lessee. If an arrangement contains a lease, then the lease element of the arrangement should be classified and accounted for as either operating or finance lease. The element of the arrangement other than the lease element should be accounted for in accordance with the applicable standards.

For the purpose of applying the classification and accounting rules payments and other consideration required by the arrangement shall be separated at the inception of the arrangement or upon a reassessment of the arrangement into those for the lease and those for other elements on the basis of their relative fair values. In doing such separation, a significant degree of estimation might be necessary.

It is the task of the contracting organizations of the Company and supporting controlling departments to inform the relevant accounting experts related to each new lease transaction who then have the responsibility of deciding whether the agreements in question contain a lease element and determining their booking.

a) Finance lease – Group as lessor

Leases of assets where Magyar Telekom transfers substantially all the benefits and risks of ownership are recognized and disclosed as revenue against a finance lease receivable. The revenue equals the estimated present value of the future minimum lease payments receivable and any unguaranteed residual value (net investment in the lease). The cost of the asset sold in a finance lease transaction is recognized at the inception of the lease. Each lease receipt is then allocated between the receivable and interest income so as to achieve a constant rate of return on the finance receivable balance outstanding. The interest element of the lease receipt is recognized in Interest income.

Finance leases mainly include equipment provided to business customers as part of our outsourcing contracts where the Company is the service provider.

b) Finance lease – Group as lessee

Leases of property, plant and equipment where Magyar Telekom assumes substantially all the benefits and risks of ownership are classified as finance leases. Finance leases are capitalized at the fair value of the asset or if lower, at the estimated present value of the future minimum lease payments against a finance lease payable. Each lease payment is allocated between the finance lease liability and interest expense so as to achieve a constant rate of interest on the outstanding balance payable. The finance lease obligations, net of finance charges, are included in the Statement of financial position (Other financial liabilities). The interest element of the lease payments is charged to the Profit for the year (Interest expense) over the lease period. Property, plant and equipment acquired under finance lease contracts are depreciated over the shorter of the lease term or the useful life of the asset.

c) Operating lease – Group as lessor

Assets leased to customers under operating leases are included in Property, plant and equipment in the Statement of financial position. They are depreciated over their expected useful lives on a basis consistent with similar assets. Rental revenue is recognized as revenue on a straight-line basis over the lease term.

d) Operating lease – Group as lessee

Costs in respect of operating leases are charged to the Profit for the year (Other operating expenses) on a straight-line basis over the lease term.

e) Sale and leaseback transactions

Sale and leaseback transactions involve the sale of an asset by Magyar Telekom and the leasing of the same asset or part of it back to Magyar Telekom. When sale and leaseback transactions qualify as finance leases any gain on the sale is deferred and recognized in the Profit for the year over the lease term through lower depreciation expense. If the leaseback qualifies as an operating lease, any gains or losses on the sale are recognized in the Profit for the year (Other operating income) at the time of the sale as the sales price reflects the fair value of the asset, while the lease payments are recognized in the Profit for the year (Other operating expenses) on a straight line basis over the period of the lease.

17.2 Finance leases

17.2.1 Finance lease – Group as lessor

Finance leases mainly include equipment provided to business customers as part of our outsourcing contracts where the Group is the service provider.

Future lease receivables under finance leases at December 31, 2017 and 2018 are as follows:

In HUF millions	At December 31, 2017			At December 31, 2018		
	Present value	Interest component	Minimum lease receipt	Present value	Interest component	Minimum lease receipt
Within 1 year	246	19	265	50	14	64
1–5 years	163	46	209	161	42	203
After 5 years	183	31	214	147	70	217
Total	592	96	688	358	126	484

The interest component represents the unearned finance income. The present value due within one year is included in Other current financial assets, while the present value after one year is included in Non current financial assets. The finance income accruing to the Group over the lease term is recognized in the Profit for the year (Interest income).

The unguaranteed residual values accruing to the benefit of the Group are insignificant.

17.2.2 Finance lease – Group as lessee

Finance leases in 2017 and 2018 mainly relate to the sale and lease back of spaces in buildings accommodating telephone exchanges. In most cases the contracts are denominated in EUR, the term of the leases is 5–15 years, and the contracts include renewal options but no purchase options.

Future lease payments under finance leases related to sale and lease back transactions at December 31, 2017 and 2018 are as follows:

In HUF millions	At December 31, 2017			At December 31, 2018		
	Present value	Interest component	Minimum lease payment	Present value	Interest component	Minimum lease payment
Within 1 year	438	810	1,248	235	764	999
1–5 years	649	2,577	3,226	850	2,344	3,194
After 5 years	1,201	1,213	2,414	881	803	1,684
Total	2,288	4,600	6,888	1,966	3,911	5,877

Finance leases other than sale and lease back in 2017 and 2018 mainly relate to real estate. In most cases the contract term of the leases is 5–10 years mostly with renewal options and without purchase options.

Future lease payments under finance leases other than sale and lease back transactions at December 31, 2017 and 2018 are as follows:

In HUF millions	At December 31, 2017			At December 31, 2018		
	Present value	Interest component	Minimum lease payment	Present value	Interest component	Minimum lease payment
Within 1 year	444	387	831	459	369	828
1–5 years	626	1,224	1,850	751	1,108	1,859
After 5 years	815	541	1,356	650	337	987
Total	1,885	2,152	4,037	1,860	1,814	3,674

The Group has no contingent rents related to its finance leases. The Group does not sub-lease any of the assets leased in a finance lease contract.

17.3 Operating leases

17.3.1 Operating lease – Group as lessor

The following table includes the future minimum lease payments receivable by the Group for the operating leases of mobile tower sections and dark fibre where Magyar Telekom is the lessor.

In HUF millions	At December 31,	
	2017	2018
Within 1 year	411	596
1–5 years	579	1,181
After 5 years	523	1,145
Total	1,513	2,922

17.3.2 Operating lease – Group as lessee

Operating lease commitments are mainly in respect of the rental of the new headquarters and mobile cell sites, and to a lesser extent, related to other buildings, network and other telecommunications facilities and equipment. The following table includes the future minimum lease payments payable of the Group:

In HUF millions	At December 31,	
	2017	2018
Within 1 year	11,501	21,501
1–5 years	24,569	52,837
After 5 years	4,847	71,674
Total	40,917	146,012

In 2018 the Group is exposed to HUF 56 billion rental fee commitment due to the new Magyar Telekom Plc. headquarters. Besides this, the lease commitments represent a high amount of individually immaterial lease agreements, the terms of which vary on a wide range, spanning from 1 to 20 years with renewal options in most cases, but no purchase options.

18 REVENUE

18.1 Revenue – accounting policies

The accounting policies of the Group changed regarding accounting for revenue from 2017 to 2018 with the transition from IAS 18 and IAS 11 to IFRS 15 and they are disclosed below.

18.1.1 Sale of goods and Rendering of services

Under IAS 18

Revenue from sale of goods (equipment) is recognised when risks and rewards of ownership have been transferred to the customer, recovery of the consideration is probable, the associated costs and possible return of goods can be estimated reliably, there is no continuing management involvement with the goods, and the amount of revenue can be measured reliably. The timing of the transfer of risks and rewards varies depending on the individual terms of the agreement. Revenue from sale of goods is measured net of returns, trade discounts and volume rebates.

The Group recognises revenue from rendering of services in proportion to the stage of completion of the service at the reporting date. The method of assessment of the stage of completion depends on the type of the service.

Under IFRS 15

The core principle of IFRS 15 is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration (that is, payment) to which the company expects to be entitled in exchange for those goods or services.

Revenue should be recognised if it is probable that the Group will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. If the Group determines that collectability is no longer ensured (e.g. because subsequently the customer's ability or intent to pay significantly deteriorates), the Group must apply cash accounting for the remainder of the contract, i.e. for the outstanding goods and services to be provided. This reassessment does not affect recorded assets and revenue relating to performance obligations already satisfied.

Revenue is recognized when or as performance obligations are satisfied by transferring control of a promised good or service to a customer. Control either transfers over time or at a point in time, which affects when revenue is recorded.

As a practical expedient, the Group applies the guidance to a group of contracts with similar characteristics instead of to a single contract with a customer. A portfolio approach is acceptable if the Group can reasonably expect that the effect of applying a portfolio approach to a group of contracts or group of performance obligations would not differ materially from considering each contract or performance obligation separately. This implies that a portfolio of contracts with similar characteristics does not necessarily need to refer to homogenous products being included in these contracts.

Transition

Magyar Telekom utilized the option for simplified initial application, i.e., contracts that were not completed by January 1, 2018 were accounted for as if they had been recognized in accordance with IFRS 15 from the very beginning. The cumulative effect arising from the transition (catch-up) was recognized as an adjustment to the opening balance of equity in 2018. Prior-year comparatives were not adjusted. IFRS 15 means revenue is recognized earlier and expenses are recognized later for contracts not yet concluded by January 1, 2018. However, as the accounting effects of the changeover to the new standard were recognized directly in equity, the only effects on the Consolidated Statement of Income in 2018 were related to changes in the point in time at which revenue and expenses are realized.

Main principles

- If Group performs by transferring goods or services to a customer before the customer pays consideration or before payment is due, the Group shall present the contract as a Contract asset, excluding any amounts presented as a receivable. A contract asset is the Group's right to consideration in exchange for goods or services that the Group has transferred to a customer.
- In the case of multiple-element arrangements (e.g., mobile contract plus handset) with subsidized products delivered in advance, a larger portion of the total remuneration is attributable to the component delivered in advance (mobile handset), requiring earlier

recognition of revenue. This leads to the recognition of what is known as a contract asset – a receivable arising from the customer contract that has not yet legally come into existence – in the Consolidated Statement of Financial Position.

- At the same time, it resulted in higher revenue from the sale of goods and merchandise and to lower revenue from the provision of services.
- Expenses for sales commissions (customer acquisition costs) must now be capitalized in the Contract costs line of the Consolidated Statement of Financial Position and recognized over the estimated customer retention period.
- Later recognition of revenue in cases where "material rights" are granted, such as offering additional discounts for future purchases of further products.
- Contract liabilities (which, as deferred revenue, were already recognized as liabilities in the past and with the transition reclassified) are now netted off against the contract assets for each customer contract.
- For the purposes of determining whether Magyar Telekom sells products for its own account (principal = gross revenue) or for the account of others (agent = net revenue), there was no material change.
- A significant financing component is not considered for the amount and timing of revenue recognition if the period between when a promised good or service is transferred to the customer and when the customer pays for that good or service will be one year or less.
- If the promise to grant a license is distinct from the other promised goods or services in the contract then the promise to grant the license is a separate performance obligation and the Group shall determine whether the license transfers to a customer either at a point in time or over time.

18.1.2 Revenue from operating leases

Revenues from operating leases are recognized as revenue on a straight line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income, over the term of the lease. Operating lease revenue are primarily recognized as System integration and IT revenue.

18.2 Revenues from major service lines

18.2.1 Mobile and Fixed line telecommunications revenues

Revenue is primarily derived from services provided to Magyar Telekom's customer subscribers and other third parties using Magyar Telekom's telecommunications network, and equipment sales.

Customer subscriber arrangements typically include an equipment sale, subscription fee and charge for the actual voice, internet, data or multimedia services used.

Airtime revenue is recognized based upon minutes of use and contracted fees less credits and adjustments for discounts, while subscription and flat rate revenues are recognized in the period they relate to. In case of IFRS 15 usage-based consideration (e.g. airtime) is generally not part of the transaction price as the Group does not have a right to consideration at contract inception.

The Group provides customers with narrow and broadband access to its fixed, mobile and TV distribution networks.

Advertising revenues are recognized in the period that the advertisements are exhibited.

Revenues from premium rate services are recognized on a gross basis when the delivery of the service over Magyar Telekom's network is the responsibility of the Group, the Group determines the prices of these services and bears substantial risks of these services; otherwise these revenues are presented on a net basis.

Customers may also purchase prepaid mobile, public phone and internet credits (cards) which allow those customers to use Magyar Telekom's telecommunications network for a selected amount of time. Customers must pay for such services at the date when the card is purchased. Revenues from the sale of cards are recognized when used by the customers or when the credits expire with unused traffic.

Third parties using Magyar Telekom's telecommunications network include roaming customers of other service providers and other telecommunications providers which terminate or transit calls on Magyar Telekom's network. These wholesale (incoming) traffic revenues are recognized in the period of related usage. A proportion of the revenue received is often paid to other operators (interconnect) for the use of their networks, where applicable. The revenues and costs of these transit calls are stated gross in the Financial statements as the Group is the principal supplier of these services using its own network freely defining the pricing of the services, and recognized in the period of related usage.

Under IAS 18

The Group considers the various elements of these arrangements to be separate earnings processes and classifies the revenue for each of the deliverables into the categories using the residual method for each of the elements. These units are identified and separated, since they have value on a standalone basis and are sold not only in a bundle, but separately as well. Therefore the Group recognizes revenues for all of these elements using the residual method, i.e. the amount of consideration allocated to the delivered elements of the arrangements equals the total consideration less the fair value of the undelivered elements. The revenue allocable to a delivered item, however, is limited to the amount that is not contingent upon the delivery of additional items (the non contingent amount). The revenue to be recognized is therefore restricted by the amount received that is not contingent upon undelivered elements of the arrangement. Fix and mobile service revenues are recognized when the services are provided in accordance with contractual terms and conditions. Revenues and expenses associated with the sale of telecommunications equipment and accessories are recognized when the products are delivered, provided that there are no unfulfilled obligations that affect the customer's final acceptance of the arrangement. In case the equipment is sold on installments with payment terms exceeding 12 months, the amount of the revenue immediately recognized is the present value of the installments.

Under IFRS 15

Contracts are frequently sold to customers containing a cross subsidy between two or more components. A typical example is where a mobile phone is sold at a price significantly below its market value in a bundle with a service contract for a period of 12 or 24 months. From a commercial point of view, the subsidy on the mobile phone is recompensated via the service fee.

With this adjustment requirement (also termed as "basic adjustment") a cross-subsidy or an overall bundle discount must be allocated to the individual components of the bundle so that revenue generally reflects the fair value of the good and/or service with a bundle discount being appropriately distributed among the affected items.

The revenue is determined for every component by distributing the transaction price to the individual components in proportion to their relevant standalone selling prices.

18.2.2 System integration (SI) and IT revenues

Contracts for network services, which consist of the installation and operation of communication networks for customers, have an average duration of 2-3 years.

Revenue from outsourcing contracts reflects the extent of actual services delivered in the period in accordance with the terms of the contract. The contracts are analyzed based on the requirements of IFRIC 4 – Determining whether an Arrangement contains a Lease, and if they include embedded lease elements, the revenues attributable to these are recognized according to IAS 17 – Leases as described in Note 17.

Revenue from system integration contracts requiring the delivery of customized products and/or services is generally covered by one of the following types of contracts: fixed-price or time and material-based.

Under IAS 18

For fixed-price contracts, revenue is generally recognized based on percentage of completion taking into account the proportion that contract costs incurred for work performed to date bear to the estimated total contract costs. In the case of contracts billed on the basis of time and material, revenue is recognized as the services are rendered.

Revenue from maintenance services (generally fixed fee per month) is recognized over the contractual period or as the services are provided. Revenue from repairs, which are not part of the maintenance contract, billed on the basis of time and material used is recognized as the services are provided.

Revenue from hardware and software sales or sales-type leases is recognized when the risk of ownership is substantially transferred to the customer, provided there are no unfulfilled obligations that affect the customer's final acceptance of the arrangement. Any related costs of these revenues are recognized when the revenue is recognized.

Revenues from construction contracts are accounted for using the percentage-of-completion method. The stage of completion is determined on the basis of the costs incurred to date as a proportion of the estimated total costs. Receivables from construction contracts are classified in the Statement of financial position as Trade receivables. If the total actual and estimated expenses exceed revenues for a particular contract, the total expected loss is recognized immediately (Direct costs) against a provision.

Under IFRS 15

MT transfers control of goods and services over time and, therefore, satisfies a performance obligation and recognizes revenue over time, if one of the following criteria is met:

- a customer simultaneously receives and consumes the benefit provided by MT's performance as MT performs
- MT's performance creates or enhances assets that the customer controls as the asset is created or enhanced
- MT's performance does not create an asset with an alternative use to MT and MT has an enforceable right to payment for performance completed to date.

If the performance obligation is not satisfied over time, MT satisfies the performance obligation at a point in time.

Revenue from maintenance services (generally fixed fee per month) is recognized over time. Revenue from repairs, which are not part of the maintenance contract, billed on the basis of time and material used is recognized at point in time.

Revenue from hardware sales or sales-type leases is recognized when the customer obtains the control over the product.

To determine the progress of performance Magyar Telekom Group is applying the Input method. MT recognize revenue on the basis of the MT's efforts or inputs to the satisfaction of a performance obligation (resources consumed, labour hours expended, cost incurred, time elapsed or machine hours used) relative to the total expected inputs to the satisfaction of the performance obligation.

18.3 Revenue in the Statement of profit or loss and other comprehensive income

18.3.1 Disaggregation of revenue from contracts with customers

The 2018 balances in the below table were determined with regard to IFRS 15 while the 2017 balances are shown based on IAS 18 and IAS 11. The effects of the IFRS 15 transition are disclosed in Note 1.3.

	For the year ended December 31,	
In HUF millions	**2017**	**2018**
Mobile revenues		
Voice retail	141,185	133,512
Voice wholesale	9,987	9,845
Data	73,992	80,881
SMS	17,259	19,175
Equipment	64,210	87,423
Other mobile revenues	16,023	12,309
Total Mobile revenue	322,656	343,145
Fixed line revenues		
Voice retail	45,977	42,695
Broadband retail	49,334	51,449
TV	45,188	47,098
Equipment	9,254	18,132
Data retail	10,690	9,367
Wholesale	19,050	19,879
Other fixed line revenues	16,615	18,281
Total Fixed line revenue	196,108	206,901
System integration and IT revenue	87,485	107,058
Revenue from energy services	4,602	-
	610,851	657,104

In HUF millions	For the year ended December 31, 2017	2018
Total revenue:	610,851	657,104
Of which:		
Revenue from contracts with customers	n.a.	639,605
Other sources	n.a.	17,499

Other sources of revenue include real estate and network rental fees which are presented above in the Fixed line wholesale and Fixed line other revenue lines.

Equipment revenue is recognized at a point in time while service revenue is recognized over time. SI/IT revenue is recognized mostly over time and to a lesser extent at a point in time depending on the project. In 2018 approximately 70% of SI/IT revenue was recognized over time.

None of the Group's customers represent a significant source of revenue. Revenues from transactions with a single external customer (or group of entities that – knowingly to us – are under common control of a third party or government) do not exceed 10 per cent of the Group's revenues.

Regarding geographical segmentation of revenue please see note 33.

18.4 Assets and liabilities related to contracts with customers

Contract assets of the Group consist of unbilled amounts typically resulting from sales under long-term contracts when revenue recognized exceeds the amount billed to the customer. The current portion of contract assets is included in Trade receivables and other assets in the Consolidated statement of financial position. The non current portion of contract assets is included in Other non current financial assets in the Consolidated statement of financial position.

Contract liabilities consist of advance payments and billings in excess of costs incurred and deferred revenue. The current portion of contract liabilities is included in Other current liabilities in the Consolidated statement of financial position. The non current portion of contract liabilities is included in Other non current liabilities in the Consolidated statement of financial position.

In HUF millions	At December 31, 2017	2018
Contract assets – current	-	17,820
Contract assets – non current	-	3,560
Contract liabilities - current	-	(12,372)
Contract liabilities – non current	-	(428)
Net contract assets (liabilities)	-	8,580
Revenue recognized in the reporting period from		
Amounts included in contract liability at the beginning of the period	-	7,700
Asset recognized from the costs to obtain contracts with customers		4,532
Amortisation recognized as cost of obtaining contracts during the period	-	(5,721)

The increase in our net contract assets from December 31, 2017 to December 31, 2018 was primarily due to the first-time application of IFRS 15. Contract assets increased during 2018 as a result of the new 2018 contracts with telecommunication customers of the Group.

Contract liabilities increased during 2018 as a result of new prepaid subscription contracts and construction contracts.

Impairment losses recognized on contract assets are disclosed together with trade receivables in Note 4.2.2.2 and they amounted to HUF 1,469 million as at December 31, 2018.

As of December 31, 2018 the aggregate amount of the transaction price allocated to the remaining performance obligation is HUF 132,042 million and the Group will recognize this revenue as services are rendered, which is expected to occur over the next 13-30 months.

The Group did not account for revenue recognized in the reporting period from performance obligations satisfied (or partially satisfied) in previous periods as IFRS 15 was adopted in 2018.

19 DIRECT COSTS

		For the year ended December 31,	
In HUF millions		**2017**	**2018**
Interconnect costs		18,885	20,641
SI/IT service related costs		60,438	75,849
Telecom tax	(a)	25,085	25,487
Bad debt expense		5,520	9,496
Energy service related costs		4,787	-
Other direct costs	(b)	131,062	155,458
		245,777	286,931

(a) Telecom tax was introduced in Hungary for fixed and mobile voice and mobile SMS/MMS services, effective from July 1, 2012. The tax imposed on fixed and mobile usage amounts to HUF 2 per minute and HUF 2 per SMS/MMS for private individual subscribers' subscriptions and to HUF 3 per minute and HUF 3 per SMS/MMS for non-private individual subscribers' subscriptions. The tax is capped at HUF 700 and HUF 5,000 per month per calling number for private and non-private individuals' subscriptions, respectively.

(b) Other direct costs include costs of mobile and fixed device, accessories and other equipment, agent commissions and non-voice direct costs.

20 EMPLOYEE RELATED EXPENSES

20.1 Employee related expenses – accounting policies

20.1.1 Short term employee benefits

Short term employee benefits are recognized as a current expense in the period when employees render their services. These include wages, social security contributions, bonuses, paid holidays, discounted telephone bills, meal and holiday contributions and other fringe benefits and the tax charges thereon.

Payments to defined contribution pension and other welfare plans are recognized as an expense in the period in which they are earned by the employees.

20.1.2 Share based compensation

Magyar Telekom recognizes the costs of services received from its employees in a share based payment transaction when services are received. Magyar Telekom recognizes a corresponding increase in its equity reserves (Reserve for equity settled share based transactions) if the services are received in an equity-settled share based payment transaction. When the share based compensation program is completed, i.e. the shares are transferred to the employees' ownership or the share options have forfeited, the respective reserve is transferred to Retained earnings. If the services are received in a cash-settled share based payment transaction, the Group recognizes the expense against a liability, re-measured to fair value at each financial statement date.

Fair values are determined using option pricing models (such as Black –Scholes and Monte Carlo simulation) and other relevant techniques. As Magyar Telekom Plc. and DT AG are listed and actively traded on the stock exchanges, the share prices and their history are readily available as a basis for fair value calculations.

Bonuses tied to the long term performance of the Magyar Telekom and Deutsche Telekom shares are recognized in the Profit for the year at their time-proportioned fair value against an accumulating balance in Provisions.

20.1.2.1 Share Matching Plan of Magyar Telekom's CEO

In December 2011 the Board of Directors approved the implementation of the revolving Share Matching Plan of Magyar Telekom. The program was implemented for the CEO of Magyar Telekom starting in 2012. An amount of minimum 10% of the gross annual bonus of the CEO was to be invested in shares of Magyar Telekom. The CEO had the option of voluntary increase to a maximum of 33.3% of his bonus. These shares are to be held for a period of at least 4 years (lock-up period). After the lock-up period of 4 years has passed, one additional share (matching share) will be granted for every share acquired as part of the aforementioned personal investment. The program was planned to be revolving in 5 consecutive years starting in 2012.

Magyar Telekom implemented amendments to the CEO's Share Matching Plan from July 1, 2015 so that the CEO had to invest in DT shares instead of MT shares. The other principles remained the same.

The Share Matching Plan of Magyar Telekom's CEO was ended on December 31, 2017. In 2018 no expenses were recognized for the program (2017: HUF 5 million).

20.1.2.2 Share Matching Plan of Deutsche Telekom

As of July 1, 2015, Magyar Telekom Group implemented Share Matching Plan for all executives (cca. 60). Participation in the program is voluntary, with the exception of the CEO, who is obliged to participate in the program with the conditions above.

The participant is required to invest a minimum of 10% of his/her gross annual bonus in Deutsche Telekom shares, with an option to voluntary increase this amount to a maximum of 33.3% (personal investment). These shares shall be kept for at least 4 years (the lock-up period), the participant is granted matching shares upon expiry of the lock-up period. The share allocation ratio of the program (1:1, 1:2 or 1:3) depends on the evaluation of the participant's performance in the previous year. Deutsche Telekom grants the matching shares to the participant based on the acquired Deutsche Telekom shares by the participant within the framework of the program. The program starts annually if the free cash flow target of Deutsche Telekom Group was met in the previous year.

In 2018 HUF 28 million was recognized as expenses for the program (2017: HUF 27 million).

20.1.2.3 Long-term incentive program (LTI)

As of January 1, 2015 Magyar Telekom Group changed its existing LTI program, turning it into a share-based compensation program. Approximately 60 executives may participate in the program. The CEO's participation is unconditional, while other executives may participate only if the evaluation of the participant's performance in the previous year meets the requirements.

LTI is payable in cash tied to the achievement of four key strategic indicators. In the framework of the program, in each year a new four-year tranche is to be launched. Payment is due after the end of the program term depending on the evaluation of the achievement of the pre-set targets (0 to 150%).

At the beginning of the program, the relevant incentive amount is converted into a number of virtual shares of DTAG and awarded to the plan participant in the form of virtual shares (basic number). The annual level of target achievement is determined at the end of each year. This target achievement level is multiplied on a pro rata basis by the basic number of virtual shares awarded. The number of virtual shares calculated using this method shall then be "fixed" for the plan participant as the binding result for that specific year ("annual result"). At the end of the plan term, the four binding annual results shall be added together. The resulting total number of virtual shares shall be converted into cash applying the then prevailing share price of DTAG, which is paid to the plan participants. For dividend payments during the plan term, the virtual shares shall be treated as real shares. The dividends shall be taken into account as follows: The first/second/third dividend payments shall be "reinvested" into virtual shares when the actual dividends are paid on real shares. The fourth (and last) dividend payment shall not be reinvested but paid in cash together with the plan payment following the DTAG shareholders' meeting at which a decision is made regarding this dividend payment. The plan currency is euro.

In 2018 HUF 620 million was recognized as expenses for the program (2017: HUF 380 million).

20.1.2.4 Share transfer to ESOP Organization

In July 2016 Magyar Telekom launched a Remuneration Policy based employee share ownership program (ESOP) under which Magyar Telekom shares were distributed to the vast majority of the employees of Magyar Telekom Plc. and T-Systems Hungary Ltd.. This program was in addition to the Company's regular remuneration package. The award of shares was contingent on the Company's actual internal operating Free Cash Flow of MT-Hungary segment of the year ending December 31, 2016 exceeding that of the year ended December 31, 2015. Each eligible individual was entitled to receive 226 Magyar Telekom shares (in the value of HUF 100,000 calculated on the unweighted average share price of 20 trading days prior to June 30, 2016), along with any entitlement to the dividends attached to such shares and with no lock-up restrictions. In July 2016, the Company purchased 1,261,204 Magyar Telekom shares in the open market, which was completed by 272,432 treasury shares to finance the program. In order to distribute the shares an employee share ownership organization (ESOP Organization) was established by the Company and registered by the Metropolitan Court in 2016 , which has its supreme body appointed by the founder (i.e. the Company). Upon the confirmation of the improvement of the oFCF of MT-Hungary segment by the Board of Directors in late February 2017, the ESOP Organization was expected to distribute the shares amongst 6,646 employees in April 2017, where each eligible individual was entitled to receive 226 shares.

In accordance with the ESOP Act the ESOP Organization manages the financial instruments provided to the ESOP Organization in accordance with the effective remuneration policies approved by the Company and the Articles of Association of the ESOP Organization.

The ESOP Organization is managed and represented by the managing director. The managing director is vested with powers to solely represent the ESOP Organization. The managing director is nominated and recalled by the supreme body. The managing director shall not be instructed by the Founder or the Participants.

Magyar Telekom transferred 1,533,636 treasury shares in August 2016 to the established ESOP Organization of which 25,764 shares were sold by the ESOP Organization due to the revision of the number of the participants in the program. The ESOP Organization is fully consolidated from its set up as it was established and it is controlled by the Company. As the improvement of the oFCF of MT-Hungary segment was confirmed by the Board of Directors, the ESOP Organization distributed the shares amongst 6,452 employees in April 2017.

In 2017 HUF 164 million was recognized as expenses for the program.

20.1.2.5 Bonus payment via ESOP Organization

By reshaping the current remuneration structure, the Company has launched an incentive program based on the new remuneration policy in 2017, by which the corporate financial targets, approximately half (50%) of the total bonus, will be paid via the ESOP Organization for Magyar Telekom Plc. and T-Systems Magyarország Zrt. eligible employees. Under the new incentive program, the Company purchased 4,534,758 Magyar Telekom shares worth HUF 2,139 million during 2017 and additional 804,236 shares (HUF 364 million) in 2018. The purchased shares were transferred to the ESOP Organization in several installments. The vesting conditions of the new program are (a) that the operating free cash flow for the MT-Hungary segment for the financial year ended December 31, 2017 to exceed that for the previous year ended December 31, 2016 and (b) that the respective employee is employed by Magyar Telekom Plc. or T-Systems Magyarország Zrt. in March 2018 (vesting date). In accordance with the remuneration program those employees of the Company and T-Systems Magyarország Zrt. are rewarded who are under the personal scope of the Remuneration policy approved on February 22, 2017 by the Company's Board of Directors.

As the vesting conditions were met the corporate financial target was paid in cash based on the employees' claims arising from the conversion of the Magyar Telekom ordinary shares transferred into cash which amounted to HUF 2,251 million in March 2018 via the ESOP Organization. The Company considers January 1, 2017 as grant date with respect to the initial assumptions of the newly formed share based program because the parties had a common understanding on the relevant terms defined by historical conditions at that date.

The Company was able to cover the significant proportion of the bonus payments related to the corporate financial target via the ESOP based on the formula in the Remuneration policy and relevant internal regulation. The remaining part of the total bonus was granted to the employees as supplementary benefit when the exchange rate for converting the shares into cash by the ESOP Organization was already known. The Company was liable to repurchase the shares under the Articles of Association of the ESOP Organization.

Employees who fell out of the scope of the Remuneration policy before the management of the ESOP Organization asserted the fulfillment of the vesting conditions, were not entitled for the benefit via the ESOP Organization, such benefits were paid off by the Company under the relevant internal regulations.

In 2017 HUF 2.1 billion was recognized as the total expenses of the program which was recognized in the statement of financial position as Other current liability.

The Company decided on further changes in the remuneration structure for 2018. Based on these changes significant portion of the central bonus for 2018 will be paid via the ESOP Organization for Magyar Telekom Plc. and T-Systems Hungary Ltd. eligible employees. To operate the incentive program, in addition to the treasury shares held by the Company, further Magyar Telekom shares worth HUF 1,458 million was purchased from the stock exchange and 8,845,794 Magyar Telekom shares worth HUF 3,846 million were transferred to the ESOP Organization together with the shares bought back from ESOP at bonus payment for program 2017.

The remuneration condition of the new program is a) the operating free cash flow for the MT-Hungary segment for the financial year ended December 31, 2018 to exceed that for the previous year ended December 31, 2017 and b) that the affected employee is employed by Magyar Telekom Plc. or T-Systems Magyarország Zrt. in March 2019 (vesting date). If the remuneration condition is met, the relevant compensation will be paid in cash by the ESOP Organization through conversion of the Magyar Telekom shares provided, expectedly in March 2019.

The Company considers January 1, 2018 as grant date with respect to the initial assumptions of the share based program because the parties had a common understanding on the relevant terms defined by historical conditions at that date.

The Company is expected to be able to cover the significant proportion of the bonus payments related to the corporate financial target via the ESOP based on the formula in the Remuneration policy and relevant internal regulation. The remaining part of the total bonus will be granted to the employees as supplementary benefit when the exchange rate for converting the shares into cash by the ESOP Organization is already known. The Company is liable to repurchase the shares under the Articles of Association of the ESOP Organization.

As the number of effected employees is uncertain for calculating the starting number of shares, fluctuation rates were considered and the exchange rate is fixed at the 2018 March 20-day-average closing rate of Magyar Telekom shares.

Employees who fall out of the scope of the Remuneration policy before the management of the ESOP Organization asserts the fulfillment of the vesting conditions, are not entitled for the benefit via the ESOP Organization, such benefits will be paid off by the Company under the relevant internal regulations.

In 2018 HUF 3.4 billion was recognized as the total expenses of the program which was recognized in the Consolidated statement of financial position as Other current liability. The ESOP Orgainzation owns 8,732,763 Magyar Telekom shares on December 31, 2018.

20.1.3 Termination benefits

Termination benefits are payable whenever an employee's employment is terminated before the nominal retirement date or whenever an employee accepts voluntary redundancy in exchange for these benefits. The Group recognizes termination benefits when it is demonstrably committed to either terminate the employment of current employees according to a detailed formal plan without the possibility of withdrawal or to provide termination benefits as a result of an offer made to encourage voluntary redundancy.

20.2 Employee related expenses in the Statement of profit or loss and other comprehensive income

In HUF millions	For the year ended December 31, 2017	2018
Short term benefits (Notes 20.1.1)	80,562	81,447
Termination benefits (Note 20.1.3)	3,618	4,495
Equity settled share based compensations (Notes 20.1.2.1 and 20.1.2.2)	32	28
Cash settled share based compensations (Note 20.1.2.3)	380	620
Employee share ownership program (ESOP Note 20.1.2.4)	164	-
Bonus payment via ESOP (Note 20.1.2.5)	2,131	3,391
Total before capitalization	86,887	89,981
Expenses capitalized	(6,647)	(7,013)
	80,240	82,968
Total costs expensed in relation to defined contribution plans (including social security contribution)	16,288	15,417
Average number of employees (full time equivalent)	9,135	9,160
Closing number of employees (full time equivalent)	9,154	8,948

21 OTHER OPERATING EXPENSES

In HUF millions		For the year ended December 31, 2017	2018
Rental and leasing expenses		17,931	19,652
Marketing expenses		11,383	11,491
Utility tax	(a)	7,418	7,159
Energy costs		8,351	7,130
Cost of other purchased services	(b)	52,408	50,204
Other operating expenses		8,427	8,279
		105,918	103,915

Research as well as marketing costs are expensed as incurred. Research costs recognized by the Group were not material in either of the presented years.

(a) Utility tax

In 2012 the Hungarian Parliament adopted an act imposing a new tax on utility networks, effective from January 1, 2013. The act provides that a tax of HUF 125 per meter is levied on the owners of ducts providing for electricity, telecommunication, natural gas, heating, water and wastewater services. For telecommunication networks, the level of tax levied depends on the length of ducts (applicable as of 1 January 2014): for the ducts not exceeding the first 200 000 meter length no taxes have to be paid for. 30% of the HUF 125 per meter is levied on between 200,000 and 350,000 meter length of ducts, 75% is levied between 350,000 and 500,000 meters, while the total HUF 125 per meter has to be paid for all ducts above 500,000 meters.

(b) Audit costs included in Cost of other purchased services

Cost of other purchased services among others include expenses incurred in relation to the audit of the standalone and consolidated financial statements of the members of the Group as well as other services provided by PricewaterhouseCoopers (PwC) as follows.

	For the year ended December 31,	
In HUF millions	**2017**	**2018**
Audit of the financial statements	380	438
Other audit related fees	29	43
Other non audit related fees	-	41
Total expenses payable to PwC	409	522

Audit of the financial statements is the aggregate fees of PwC in connection with the audit of our annual financial statements and services performed in relation to legal obligations and submissions required by regulatory provisions.

Other audit-related fees are the aggregate fees of PwC for review of the second quarterly report and services which are normally performed by the external auditor in connection with the auditing of the annual financial statements, e.g. advice on issues of accounting and reporting, which were not classified as audit services.

Other non audit related fees are fees of PwC primarily related to consulting services and services like participation by Magyar Telekom employees in conferences and training sessions organized by PwC.

22 OTHER OPERATING INCOME

	For the year ended December 31,	
In HUF millions	**2017**	**2018**
Gain on the sale of PPE, Intangible assets and assets held for sale - net	1,290	4,604
Income received for the relocation and reconstruction of our own network	939	1,127
Brand license fee	500	300
Income from insurance compensation	163	123
Income from intra-DT group support services	104	49
Other	3,750	3,014
	6,746	9,217

The increase of Other operating income reflects the one-off gain realized on the sale of the old headquarters.

23 INTEREST INCOME

In HUF millions	For the year ended December 31, 2017	2018
Interest income on financial assets	327	276
Finance lease interest income	27	19
Reversal of interest element of provisions	175	52
Dividend income	14	16
	543	363

24 INTEREST EXPENSE

In HUF millions	For the year ended December 31, 2017	2018
Interest expense payable to DT	9,094	8,818
Other interest expense	3,212	3,303
Finance lease interest expense	1,209	1,214
Accretion / interest on provisions	49	219
less: borrowing costs capitalized	(39)	(131)
	13,525	13,423

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognized as an expense. Borrowing costs include interest and other costs that the Group incurs in connection with the borrowing of funds. The borrowing costs eligible for capitalization are capitalized applying the weighted average of the borrowing costs applicable to the general borrowings of the Group that are outstanding during the period. A qualifying asset is an asset that necessarily takes a substantial period of time, in general over 12 months, to get ready for its intended use.

Total Interest expense is shown net of borrowing costs capitalized using average borrowing rates of 3.04%-3.40% in 2018 (2017: 2.92%-3.46%). When calculating the borrowing rates, Other finance expenses (included in Note 25) are also considered.

25 OTHER FINANCE EXPENSE – NET

In HUF millions	For the year ended December 31, 2017	2018
Fee expense	4,856	4,416
Net foreign exchange losses / (gains) on financial instruments	(1,107)	5,963
Other net foreign exchange losses / (gains)	123	(325)
Losses / (gains) on the subsequent measurement of derivatives contracted with related parties	4,448	(3,048)
Losses / (gains) on the subsequent measurement of derivatives contracted with third parties	-	-
Losses / (gains) on the subsequent measurement of financial assets at fair value through profit or loss (other than derivatives)	-	(38)
Losses / (gains) on the subsequent measurement of financial liabilities at fair value through profit or loss (other than derivatives)	-	(8)
Losses / (gains) on the derecognition of derivatives contracted with related parties	337	(2,236)
Losses / (gains) on the derecognition of derivatives contracted with third parties	(12)	-
Losses / (gains) on the derecognition of equity instruments (Reclassifications from Other comprehensive income)	-	-
	8,645	4,724

26 CHANGES IN THE GROUP

26.1 Business combinations

26.1.1 Acquisition of ITgen Kft.

In November 2017 T-Systems Magyarország Zrt. signed a Share Purchase Agreement to acquire a 100% stake in ITgen Kft., an SAP technology and security specialist, for a purchase price plus a potential earnout payment totalling to a maximum of HUF 1.2 billion, dependent on 2018, 2019 and 2020 financial performance. The closing of the transaction took place in January 2018.

The carrying values of assets and liabilities acquired as well as the consideration transferred are disclosed in the table below.

In HUF millions	**Carrying values**
Consideration transferred	1,249
Less: Fair value of the net assets acquired	(873)
Goodwill	376
Net assets acquired:	
Cash and cash equivalents	137
Trade and other receivables	155
Brand	123
Property, plant and equipment	6
Customer value	688
Trade and other payables	(163)
Deferred tax liability	(73)
	873

From the total purchase price HUF 799 million was paid in cash in 2018 while the earnout payment of HUF 450 million depending on the 2018, 2019 and 2020 performance of the company will be paid in the relevant years.

26.1.2 Acquisition of SERVERINFO

In October 2016 T-Systems Magyarország Zrt. signed an agreement with WING Group to buy 100% of SERVERINFO-INGATLAN Kft. (Serverinfo). As a result of the transaction Magyar Telekom Group gained ownership of the property where its highly secure data center with state of the art technical infrastructure is located. The value of the transaction was EUR 14.4 million (approximately HUF 4.4 billion) including loans of HUF 3.2 billion of Serverinfo, which were repaid subsequent to the closing of the transaction. Serverinfo manages the rentals and the maintenance of the property where the data center of T-Systems Magyarország Zrt. is located. The majority of the consideration relates to the fair value of the property. The closing of the transaction took place in January 2017.

The carrying values of assets and liabilities acquired as well as the consideration transferred are disclosed in the table below.

In HUF millions	**Carrying values**
Consideration transferred	1,485
Less: Fair value of the net assets acquired	(1,150)
Goodwill	335
Net assets acquired:	
Cash and cash equivalents	475
Trade and other receivables	55
Income tax receivables	1
Property, plant and equipment	4,079
Loans	(3,203)
Trade and other payables	(138)
Deferred tax liability	(119)
	1,150

The total purchase price was paid in cash in 2017.

Serverinfo and GTS Hungary Kft. merged into TSM Hungary Zrt. as of September 30, 2017. Magyar Telekom made its decision on the merger in line with its portfolio simplification strategy.

26.1.3 Cable TV network and operations

In 2018 and 2017, the Group acquired a number of cable TV businesses in individually insignificant transactions. All these acquisitions qualified as business combinations of the MT-Hungary operating segment. The vast majority of the total purchase price was paid in cash in 2018 and 2017.

The table below shows the summary of the individually insignificant transactions.

In HUF millions	2017	2018
Consideration transferred	2,428	1,092
Less: Fair value of the net assets acquired	(2,132)	(648)
Goodwill	296	444

26.2 Disposals of subsidiaries

26.2.1 Sale of Crnogorski Telekom A.D.

In January 2017, the Company signed a share purchase agreement with Hrvatski Telekom d.d. for the sale of the total of its 76.53% shareholding in Crnogorski Telekom A.D. for a total consideration of EUR 123.5 million (HUF 38.5 billion). The closing of the transaction took place in January 2017.

This subsidiary was previously not classified as held for sale but it was considered as a separate cash generating unit and reportable segment as well, therefore the sale constituted a discontinued operation. Impact on the segment disclosures is in Note 33.2.1. The comparative consolidated statement of profit or loss and other comprehensive income has been restated to show the discontinued operation separately from continuing operations of the Group. In the Consolidated Statements of cash flows the proceeds from the sale of subsidiaries and business units are disclosed net of the Cash and cash equivalents of the subsidiaries sold.

26.2.1.1 Results of the discontinued operation

In HUF millions	For the year ended December 31,	
	2017	2018
Revenues	2,027	-
Direct costs	(533)	-
Employee related expenses	(332)	-
Depreciation and amortization	(517)	-
Other operating expenses	(525)	-
Operating expenses	(1,907)	-
Other operating income	73	-
Operating profit	193	-
Net financial result	7	-
Income tax from discontinued operations	(23)	-
Profit after tax from discontinued operations	177	-
Gain on sale of discontinued operation	10,504	-
Income tax on gain on sale of discontinued operation	(1,155)	-
Profit for the year from discontinued operations	9,526	-
Other comprehensive income from discontinued operations	(12,512)	-
Total comprehensive income from discontinued operations	(2,986)	-

26.2.1.2 Effect of the disposal on the financial position of the Group

In HUF millions	At disposal in 2017
Cash and cash equivalents	2,062
Trade and other receivables	8,860
Other current financial assets	452
Other current assets	736
Inventories	558
Property, plant and equipment	24,079
Intangible assets (including goodwill)	21,977
Deferred tax assets	718
Other non current financial assets	3,060
Other non current assets	540
Current financial liabilities	(2,826)
Other current liabilities	(1,099)
Trade payables	(9,260)
Current income tax payable	(408)
Provisions	(215)
Non current financial liabilities	(590)
Deferred tax liabilities	(1,439)
Net assets and liabilities	47,205
Consideration received	38,458
Cash and cash equivalents disposed of	2,062
Net cash inflows	36,396

26.3 Pro forma information

The pro forma information shows the most important financial data of the Group, as if the business combinations that took place in that year had been consolidated from the beginning of the year of acquisition, and also how much the business combination contributed to the reported figures since the acquisition date. Cable TV acquisitions were insignificant in 2017 and 2018 therefore their contribution to the Group's operations was also insignificant. The 2017 sale of Crnogorski Telekom A.D. is considered as a discontinued operation, which resulted in re-presented 2016 figures. As Serverinfo and ITgen Kft. were acquired in January 2017 and January 2018, respectively, and their inclusion in the Group's operations was not significant, they do not affect the pro forma information.

27 EARNINGS PER SHARE

Basic earnings per share is calculated by dividing profit attributable to the owners of the Company for the period by the weighted average number of common stocks outstanding. Diluted earnings per share is calculated considering the weighted average number of diluting share options (if any) in addition to the number of common stocks outstanding.

28 PURCHASE OF PROPERTY, PLANT AND EQUIPMENT AND INTANGIBLE ASSETS

The table below shows the reconciliation of investments in property, plant and equipment and intangible assets and the cash payments made for these investments from continuing operations. The investments in both property, plant and equipment and intangible assets of discontinued operations are included in the Net cash used in investing activities from discontinued operations line of the Consolidated Statement of cash flows. Capitalized borrowing costs are included in the Investments in PPE and intangible assets, where applicable.

In HUF millions		For the year ended December 31, 2017	2018
Investments in property, plant and equipment (Note 9.2)		57,278	62,173
Investments in intangible assets (Note 10.2)		28,920	45,372
Total investments in PPE and intangible assets		86,198	107,545
Capitalized annual frequency fee payable	(a)	-	(4,391)
Net change of advances received for asset-related grants	(b)	456	2,797
Capitalized leases	(c)	(272)	(343)
Change in trade payables relating to capital expenditures	(d)	4,418	(11,920)
Cash payments for purchases of PPE and intangible assets		90,800	93,688

(a) Capitalized annual frequency fee payable

The present value of the annual frequency fees is capitalized as part of the intangible asset (Licenses) if the future payments can be reliably estimated, however, these fees are paid in cash in subsequent periods. The cash payments on the discounted liability are included in the Repayment of other financial liabilities line of the Financing cash flow, while the interest payments accruing on the discounted liability are included in the Interest and other financial charges paid line of the Operating cash flow. The significant license acquisition in 2018 is described in Note 10.

(b) Advances received for asset-related grants

In 2016 HUF 12.2 billion of EU funds have been granted to Magyar Telekom Plc. (Details in Note 14 (a).) HUF 5.1 billion were received by the Company as advance for this grant, and none of this was used up in 2016. In 2017, additional HUF 1.0 billion were received by the Company as advance for this grant, and HUF 1.4 billion of this was used up. In 2018, additional HUF 1.8 billion was used up from the grant. As such grants are deducted from the original cost of the items (Note 10.1), the amount reduces cash payments for purchases of PPE and intangible assets.

(c) Capitalized leases

Investments in PPE as a result of finance lease transactions do not usually result in immediate cash payments. The cash payments throughout the lease term appear as Repayment of other financial liabilities (Financing cash flow) and Interest and other financial charges paid (Operating cash flow).

(d) Change in trade payables relating to capital expenditures

Change in payables relating to capital expenditures includes the effect that the actual cash settlement of the vendor invoices is made subsequent to the recognition of the investment.

29 PURCHASE OF SUBSIDIARIES AND BUSINESS UNITS

In HUF millions	For the year ended December 31, 2017	2018
Acquisition of ITgen Kft. (Note 26.1.1)	-	920
Acquisition of Serverinfo (Note 26.1.2)	1,485	-
Cable TV businesses (Note 26.1.3)	2,306	1,125
Cash payments for purchases of subsidiaries and business units	3,791	2,045

Cash payments related to the purchases of subsidiaries and business units include advance payments made before the closing of the transaction, the initial purchase price paid on the closing of the transaction as well as amounts paid as additional contingent purchase prices disbursed in years following the year of the business combination.

30 CONTINGENT ASSETS AND LIABILITIES

30.1 Contingent assets

A contingent asset is a possible asset that arises from past events and whose existence will be confirmed only by the occurrence of uncertain future events not within the control of the Group. These assets are not recognized in the statement of financial position.

The Group has no contingencies where the inflow of economic benefits would be probable and material.

30.2 Contingent liabilities

No provision is recognized for contingent liabilities. A contingent liability is a possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events (excluding executory contracts) not wholly within the control of the entity; or a present obligation that arises from past events but is not recognized because it is not probable that an outflow of resources embodying economic benefits will be required to settle the obligation or the amount of the obligation cannot be measured with sufficient reliability.

The most significant contingent liabilities of the Group are described below. No provisions have been recognized for these cases as management estimates that it is unlikely that these claims originating from past events would result in any material economic outflows from the Group, or the amount of the obligation cannot be measured with sufficient reliability.

30.2.1 Hungary

30.2.1.1 Guarantees

Magyar Telekom Plc. is exposed to risks that arise from the possible drawdown of guarantees for which see more details in Note 4.5.4.

31 PURCHASE COMMITMENTS

31.1 Purchase commitments for tangible and intangible assets

The table below summarizes Magyar Telekom's contractual purchase commitments for tangible and intangible assets with the majority falling due within two years.

In HUF millions	At December 31, 2017	At December 31, 2018
Property, plant and equipment	9,813	5,433
Intangible assets	5,310	6,499
Total	15,123	11,932

31.2 Purchase commitments for businesses

As at December 31, 2018 and 2017 the Group had no significant committed business combinations.

32 RELATED PARTY TRANSACTIONS

No impairment was recognized for receivables from related parties in the reported years.

32.1 Deutsche Telekom Group and the Federal Republic of Germany

32.1.1 Deutsche Telekom Group

Deutsche Telekom AG is the ultimate (indirect) controlling owner of Magyar Telekom Plc. holding 59.21% of the voting rights attached to the Company's shares. Deutsche Telekom Group has a number of fixed line, mobile and IT service provider subsidiaries worldwide, with whom Magyar Telekom Group has regular transactions.

Deutsche Telekom International Finance (DTIF) is the treasury center of DT Group, which typically provides loan financing across the DT Group including Magyar Telekom.

The table below summarizes the above related party transactions and balances with DT Group.

In HUF millions	2017	2018
Revenues from services provided to DT Group companies	18,370	19,854
Costs of services provided by DT Group companies	(13,151)	(15,921)
Income from support services provided to DT Group companies	104	49
Interest expense to DTIF	(2,297)	(2,172)
Interest expense to DTAG	(6,797)	(6,646)
Dividend paid to parent company	15,436	15,516
Accounts receivable from DT Group companies	9,029	10,143
Accounts payable to DT Group companies	(12,026)	(11,119)
Loans payable to DTIF	(101,838)	(87,824)
Loans payable to DTAG	(153,353)	(140,000)
Fair value of swap agreements with DTAG – asset	2,978	1,026
Fair value of swap agreements with DTAG – liability	(5,612)	(612)

Deutsche Telekom has pledged its support for Magyar Telekom's budgeted financing needs through to June 30, 2020.

32.1.2 The Federal Republic of Germany

The Federal Republic of Germany is both a direct and an indirect shareholder and holds approximately 32 percent of the share capital of DTAG. Due to the average attendance at the shareholders' meetings, the Federal Republic of Germany represents a solid majority at the shareholders' meetings of DTAG, although it only has a minority shareholding, making DTAG a dependant company of the Federal Republic. Therefore, the Federal Republic and the companies controlled by the Federal Republic or companies over which the Federal Republic can exercise a significant influence are classified as related parties of DTAG, and consequently of Magyar Telekom as well.

DTAG and Magyar Telekom did not execute as part of its normal business activities any transactions that were individually material in the 2018 or 2017 financial year with companies controlled by the Federal Republic or companies over which the Federal Republic can exercise a significant influence.

32.2 Associates and joint ventures

The Group has no significant associates and the transactions with them are not material.

E2 Hungary Zrt. is a joint venture of the Magyar Telekom Group since July 9, 2015 and provides energy services for business customers. See also note 11.3. The Group did not have material transactions with its joint venture in either 2017 or 2018.

32.3 Board and Supervisory Board members

	For the year ended December 31,	
In HUF millions	**2017**	**2018**
Remuneration of the members of the Board of Directors	16	16
Remuneration of the members of the Supervisory Board	63	63
Loans granted to the members of the Board of Directors	-	-
Loans granted to the members of the Supervisory Board	2	1

Loans granted to the members of the Supervisory Board are limited to the employee delegates and had been granted to them in their capacity as employees.

32.4 Key management

Key management has been identified as the members of the Company's Management Committee, which is the chief operating decision making body of Magyar Telekom.

The table below shows in total the compensation expenses (including social security and other payroll related taxes) incurred by the Group in relation to the key management.

	For the year ended December 31,	
In HUF millions	**2017**	**2018**
Salaries and other short-term employee benefits	1,168	969
Contractual termination expense	-	-
Share based compensation (Note 20.1)	25	8
	1,193	977
Of which costs expensed in relation to defined contribution plans (including social security contribution)	295	147

The Group does not provide loans to its key management.

33 REPORTABLE SEGMENTS AND INFORMATION ABOUT GEOGRAPHICAL AREAS

33.1 Segment information

The Group's segments are reported in a manner consistent with the internal reporting provided to the chief operating decision makers, the members of the Management Committee (MC) of Magyar Telekom Plc. The MC is responsible for allocating resources to, and assessing the performance of, the operating segments on a monthly basis. The accounting policies and measurement principles of the operating segments are very similar to those applied for the Group described in the previous sub-notes of the Summary of significant accounting policies. The differences primarily originate from the fact that the operating segments' annual results are determined and closed at an earlier stage, around January 8–10 each year, than these Financial statements. Any items discovered and requiring adjustment between the closing date of the segment results and the approval date of the Financial statements are reflected in the next year's segment results.

The operating segments' revenues include revenues from external customers as well as the internal revenues generated from inter-segment support services.

The operating segments' results are monitored by the MC down to EBITDA (Earnings before interest, tax, depreciation and amortization) level, which is defined by the Group as Operating profit without Depreciation and amortization expense.

The MC does not monitor the assets and liabilities at segment level.

Another important KPI monitored at segment level is capital expenditure (Capex), which is determined as the annual investments in PPE and Intangible assets.

33.2 Reportable segments

As of Q1 2017, Magyar Telekom's operating segments are MT-Hungary and Macedonia. Magyar Telekom disposed of its majority stake in Crnogorski Telekom A.D. in January, 2017, and as such, the Montenegrin segment is no longer part of the Group's consolidated results. Further information about this discontinued operation is provided in Note 26.2.1.

The MT-Hungary segment operates in Hungary, providing mobile and fixed line telecommunications, TV distribution, information communication and system integration services to millions of residential and business customers under the Telekom and T-Systems brands. Residential and SMB customers are served by the Telekom brand and key business customers (large corporate and public sector customers) are served by the T-Systems brand. The MT-Hungary segment is also responsible for the wholesale of mobile and fixed line services within Hungary, and performs strategic and cross-divisional management, as well as support functions on behalf of the Group including Procurement, Treasury, Real Estate, Accounting, Tax, Legal and Internal Audit. This segment is also responsible for the Group's points of presence in Bulgaria and Romania, which mainly provide wholesale services to local companies and operators. The Macedonian segment is responsible for the Group's full-scale mobile and fixed line telecommunications operations in Macedonia.

33.2.1 Information regularly provided to the Management Committee (MC)

The following tables present the segment information by reportable segment regularly provided to the MC of the Company, reconciled to the corresponding Group numbers. The information regularly provided to the MC includes several measures of profit which are considered for the purposes of assessing performance and allocating resources, including EBITDA adjusted for the impact of certain items considered as "special influence". These items vary year-over-year in nature and magnitude. Management believes that Revenue, EBITDA and Capex are the segment measures that are most consistent with the measurement principles used in measuring the corresponding amounts in these financial statements.

Revenues	**For the year ended December 31,**	
In HUF millions	**2017**	**2018**
Total MT-Hungary revenues	559,248	602,609
Less: MT-Hungary revenues from other segments	(127)	(117)
MT-Hungary revenues from external customers	559,121	602,492
Total Macedonia revenues	51,795	54,680
Less: Macedonia revenues from other segments	(65)	(68)
Macedonia revenues from external customers	51,730	54,612
Total consolidated revenue of the segments	610,851	657,104
Measurement differences / rounding between segment and Group revenue	-	-
Total revenue of the Group from continuing operations	**610,851**	**657,104**
Total Montenegro revenues (discontinued)	2,023	-
Less: Montenegro revenues from other segments (discontinued)	4	-
Montenegro revenues from external customers (discontinued)	2,027	-
Total revenue of the Group	**612,878**	**657,104**

MT-Hungary revenues	**For the year ended December 31,**	
In HUF millions	**2017**	**2018**
Voice	134,060	127,195
Non-voice	83,381	91,642
Equipment	59,751	79,886
Other	14,321	11,047
Total mobile revenue	291,513	309,770
Voice retail	40,858	37,685
Broadband - retail	43,995	46,134
TV	41,798	43,212
Equipment	8,854	17,722
Other	41,216	42,601
Total fixed-line revenue	176,721	187,354
SI/IT revenue	86,412	105,485
Revenue from energy services	4,602	-
Total revenue of the MT-Hungary segment	**559,248**	**602,609**

Macedonia revenues	**For the year ended December 31,**	
In HUF millions	**2017**	**2018**
Voice	17,112	16,162
Non-voice	7,870	8,414
Equipment	4,459	7,537
Other	1,709	1,266
Total mobile revenue	31,150	33,379
Voice retail	5,119	5,008
Broadband - retail	5,339	5,315
TV	3,390	3,886
Equipment	400	412
Other	5,324	5,107
Total fixed-line revenue	19,572	19,728
SI/IT revenue	1,073	1,573
Total revenue of the Macedonia segment	**51,795**	**54,680**

As other sources of revenue represent an insignificant part of total revenue, we assumed regarding segment revenue that total revenue is revenue from contracts with customers.

Segment results (EBITDA)	**For the year ended December 31,**	
In HUF millions	**2017**	**2018**
MT-Hungary	164,968	170,776
Macedonia	20,225	21,365
Total EBITDA of the segments from continuing operations	185,193	192,141
Measurement differences / rounding between segment and Group EBITDA	469	366
Total EBITDA of the Group from continuing operations	**185,662**	**192,507**
Montenegro (discontinued)	702	-
Income from sale of Crnogorski Telekom (segment Montenegro)	10,504	-
Measurement differences / rounding between segment and Group EBITDA	8	-
Total EBITDA of the Group from discontinued operations	**11,214**	**-**
Total EBITDA of the Group	**196,876**	**192,507**

Capital expenditure (Capex) on PPE and Intangible assets	As at December 31,	
In HUF millions	2017	2018
MT-Hungary	73,936	81,403
Macedonia	12,529	10,566
Montenegro (discontinued)	177	-
Total capital expenditure of the segments	86,642	91,969
Acquisition of mobile licenses (Note 10)	-	15,713
Other measurement differences between segment and Group Capex	(267)	(137)
Total investments of the Group in PPE and Intangible assets	**86,375**	**107,545**

The acquisition of mobile licenses is not considered part of the Capex measure of the segments. Total investments of the Group in PPE and Intangible assets correspond to the "Investments" lines disclosed in Notes 9, 10 and 28.

33.3 Information about geographical areas

The table below shows the revenues generated from external customers in the countries where the Group operates, using the same measurement principles as for the corresponding Group numbers. As other sources of revenue represent an insignificant part of total revenue, we assumed regarding geographical areas of revenue that total revenue is revenue from contracts with customers.

Revenues	For the year ended December 31,	
In HUF millions	2017	2018
Hungary	554,831	596,603
Macedonia	51,730	54,612
Romania	2,307	3,579
Bulgaria	1,983	2,310
Total revenue of the Group from continuing operations	**610,851**	**657,104**
Montenegro (discontinued)	2,027	-
Total revenue of the Group	**612,878**	**657,104**

The table below shows the Non current assets of the Group located in the countries of operations (including goodwill allocated to operating segments operating in these countries) and the reconciliation to the total Non current assets of the Group, using the same measurement principles as for the corresponding Group numbers.

Non current assets	**As at December 31,**	
In HUF millions	**2017**	**2018**
Hungary	799,616	794,822
Macedonia	95,845	96,324
Montenegro (discontinued)	-	-
Bulgaria	3,038	3,361
Romania	1,429	1,607
Total excluding Other non current financial assets, Investments in associates and joint ventures and Deferred tax assets	899,928	896,114
Other non current financial assets (Note 4.2.3.2)	19,323	24,985
Investments in associates and joint ventures (Note 11)	1,324	1,393
Deferred tax assets (Note 6.3.2)	59	77
Total Non current assets of the Group	920,634	922,569

34 REGULATED MARKETS AND PROCEDURES

Magyar Telekom's primary activities are the fixed line and mobile operations in Hungary and Macedonia. These services are partially regulated by these countries' laws or other legislations. These services in most cases require request for service provision or acquisition of requested rights, which usually requires a one-off fee and annual payments.

The most important features of the regulations of these services are described below.

34.1 Hungarian Mobile

Magyar Telekom Plc. is the market leading mobile service provider in Hungary. The Implementation of the EU New Regulatory Framework (NRF) Review package had been completed by the amendment of the Act C of 2003 on Electronic Communications (hereinafter: Communications Act). The National Media and Infocommunications Authority of Hungary (NMIAH) is the supreme supervisory body and is responsible for secondary legislation making and the preparation of relevant decrees.

In June 2012, the Hungarian Parliament adopted the modification of the Electronic Communications Law extending the scope of competence and tasks of the NMIAH. Pursuant to the amendment, all spectrum related issues are dealt with by the NMIAH.

On December 7, 2004, the Company obtained the spectrum usage right of certain frequency blocks in the 2100 MHz band for the deployment and operation of an IMT2000/UMTS mobile telecommunications system (3G system). The duration of the spectrum license was 15 years (until December 7, 2019) that was extended for another 7.5 years in December 2018 for a one-time fee of HUF 11 billion.

The Company won a tender for a spectrum usage right for a 26 GHz block on April 30, 2009. On May 14, 2012 the NMIAH granted spectrum license to Magyar Telekom for 4 pieces of basic spectrum blocks (2 x 28 MHz each) in the 26 GHz band. Furthermore Telekom acquired GTS Hungary Ltd's 2 blocks in the 26 GHz band for HUF 114.6 million HUF net, and has a usage right for it from November 1, 2016. Blocks purchased in 2009 were prolonged in 2018.

The Company filed an auction bid in December 2011 with the NMIAH for the right of use of unused spectrum in the 900 MHz frequency band, related to the provision of mobile telecommunications services. The spectrum can be utilized in a technology-neutral manner. The NMIAH announced its first-instance decision on the result of the 900 MHz auction (Auction) on January 30, 2012. Magyar Telekom won the right of use of two duplex frequency blocks of 1 MHz each for a period of 15 years.

On September 6, 2013 Magyar Telekom and the NMIAH signed the modification of the Authority Contract on the use of the 900 MHz and 1800 MHz frequency bands. The main stipulations of the modification are the following:

- Magyar Telekom's spectrum usage rights in the 1800 MHz frequency band otherwise expiring on October 7, 2014 and in the 900 MHz frequency band otherwise expiring on May 4, 2016 were prolonged and harmonized until April 2022.
- Magyar Telekom will retain spectrum usage right also until April 2022 on the two duplex 1 MHz frequency blocks in the 900 MHz frequency band won in the 900 MHz auction in 2012. Accordingly, Magyar Telekom currently has frequency usage rights of 10 MHz duplex frequency blocks in the 900 MHz frequency bands and of 15 MHz duplex blocks in the 1800 MHz frequency band.
- The initial fee of the prolongation and harmonization of 900 MHz/1800 MHz spectrum licenses was HUF 38 billion. However, Magyar Telekom was required to pay HUF 34 billion out of the aforementioned amount, considering the expiry of the frequency blocks won in 2012 being changed from the original 2027 date to 2022.

On May 22, 2014, the NMIAH published the "Documentation for the tender announced in the subject of spectrum licenses for broadband services". Blocks in 800 MHz / 900 MHz / 1800 MHz / 2600 MHz and 26 GHz frequency bands were auctioned.

On September 29, 2014 the NMIAH published the tender results so that Magyar Telekom acquired the following frequencies for an aggregate amount of HUF 58,650 million:

- 2 x 10 MHz in 800 MHz
- 2 x 2 MHz in 900 MHz
- 2 x 30 MHz in 2600 MHz
- 2 x 10 MHz in 1800 MHz.

On October 15, 2014 Magyar Telekom and the NMIAH signed the Authority Contract on the use of the 800MHz, 900 MHz and 1800 MHz frequency bands that came into force right on that day. For the new bands the frequency license and radio permission were issued on October 17, 2014 to Magyar Telekom.

As a result of the last tender Magyar Telekom acquired frequency usage rights in the above listed spectrums till June 15, 2029. The Authority Contract can be prolonged with further 5 years if all requirements defined in the contract are met.

The Company is subject to number portability regulation since 2004, applicable only in case of other mobile operators. The Company is designated as an SMP operator (a service provider with significant market power) in the mobile wholesale call termination market (new M2, old M7 market) and subject to regulatory obligations regarding the termination charge of calls into its network, mobile termination rate (MTR). The last mobile market resolution was published on March 18, 2015 with a newly defined pure Bottom-Up Long Run Incremental Costing model (pure BU-LRIC) resulting in an MTR of 1.71 HUF/min net cost based fee.

Since June 30, 2007, an EU regulation has been regulating international roaming tariffs for wholesale and retail customers on the basis of a price cap system. The first EU roaming regulation prescribed a glide-path that mandated annual reductions of wholesale and retail prices. (EU Roaming Regulation I.)

As of July 2009 the EU also introduced regulated tariffs for SMS and data roaming similarly to the regulation of voice roaming. (EU Roaming Regulation II.)

As of July 1, 2012 the EU further broadened the European roaming regulation with a new regulatory measure: separate sales of regulated roaming services. As a result Magyar Telekom had to implement the technical possibility to host an Alternative Roaming Provider in its network and also it allows its own customers to use Local Break-out solutions within the EU offered by a foreign EU member country's mobile operator from July 1, 2014. (EU Roaming Regulation III.)

The actual EU roaming regulation - "Full Roam Like At Home With Fair Use Policy Possibility" - is applied from June 15, 2017. (EU Roaming Regulation IV.). As a result, European retail roaming price levels for voice, SMS and data are equal to domestic prices since summer 2017. The Commission implementing regulation (EU) 2016/2286 of 15 December 2016 laid down detailed rules on the application of fair use policy and on the methodology for assessing the sustainability of the abolition of retail roaming surcharges and on the application to be submitted by a roaming provider for the purposes of that assessment.

On December 11, 2018, the European Union published its European Electronic Communication Code ("Code") Directive (EU) 2018/1972 that defines price caps for intra-EU calls and texts that is to be applied by May 15, 2019. MT will fullfil the price cap regulation on time.

34.2 Hungarian Fixed line

Universal services are basic communications services (including access to communication services at a fixed location, public payphones, directory and directory enquiry services) that should be available to all customers at an affordable price. The NMIAH published its request for voluntary universal service provisioning on January 19, 2018. MT did not bid to any parts of the universal services, so the NMIAH designated MT to offer the following universal services from January 1, 2019: public payphones, access on fixed location and for national directory enquiry service. As a result of the procedure MT lost 2 primary areas to serve (Szekszárd – nr74 and Paks – nr75) and received a new one (Szeged - nr62).

In the electronic communications field Magyar Telekom was designated as an SMP operator (a service provider with significant market power) on the regulated markets:

- 1. Wholesale fixed call termination
- 2. Wholesale mobile call termination
- 3.a) Wholesale local access at a fixed location - WLA
- 3.b) Wholesale central access for mass-market products - WCA
- 4. Wholesale high-quality access at a fixed location

Magyar Telekom is Hungary's leading fixed line broadband service provider in the wholesale market and one of the leading ones in the retail market. In accordance with the effective resolution, all retail fixed products shall be 'reproducible' by competitors based on the wholesale service. Consequently, the full retail portfolio shall have a wholesale equivalent. Previous regulation defined a retail minus price setting. The NMIAH published the latest resolutions with regards to markets 3a and 3b on December 15, 2017. SMP operators are obliged to prepare reference unbundling offer for access to (physical) passive network infrastructure (RUO) and to provide these services when there is a request for them by other telecommunications service providers. The reference offer of each SMP operator must be approved by the NMIAH. As a novelty the resolutions contained geographical segmentation in the access regulation, as a start of a deregulation path, in a limited number of settlements and as a new service the virtual unbundling obligation (L2-WAP).

Magyar Telekom was designated as an SMP in both 3a and 3b markets. Service fee calculation for all relevant regulated services – both markets 3a (resolution PC/17915-66/2017.) and 3b (resolution PC/17920-66/2017.) - are with a BU-LRIC+ model. The latest reference unbundling offer (MARUO) accordingly was approved on December 4, 2018. The new fees are applied from January 1, 2019. The new L2-WAP regulated product and its implementation in the reference unbundling offer is ongoing, and assumed to be finished in Q3 2019, also resulting modifications in the MARUO. With regards the fix networks' regulated interconnection the NMIAH published its fifth round market analysis procedure's resolution on May 15, 2018. The resolution's FTR (fix termination rate) proposal - that is based on a pure BU-LRIC model - is 0.26 HUF/min. The new fee had to be applied symmetrically with an effect from end of Q2 2018 altogether for 144 operators.

The latest MARIO and supplementary interconnection service fees are assumed to come into force by end of Q1 2019.

34.3 Energy services in Hungary

Magyar Telekom decided to exit from the residential segment of the gas market with effect from July 31, 2015 and also from the residential segment of the electricity market with effect from November 1, 2017.

From October 1, 2016 Magyar Telekom seized its operation in the public procurement gas market as the natural gas services segment of the energy business was outsourced to E2 Hungary Zrt., a joint venture owned by Magyar Telekom Plc. and MET Holding AG to operate in the business and public procurement segment of the Hungarian gas and energy market. In accordance with the agreement of the owners, Magyar Telekom transferred its business energy operations to E2.

34.4 Macedonian Mobile

The Group is also present in the Macedonian mobile market through its subsidiary, Makedonski Telekom AD Skopje (MKT, previously T-Mobile). The Macedonian telecommunications sector is regulated by the Electronic Communications Law (ECL) enacted in March 2014 as primary legislation and rulebooks as secondary legislation.

On September 5, 2008 the Agency for Electronic Communications (AEC, the Agency), ex officio, issued a notification to T-Mobile for those public electronic communication networks and/or services which have been allocated thereto under the Concession Contracts. The license for radiofrequencies used by T-Mobile with a bandwidth of 25 MHz in the GSM 900 band, was also issued in a form regulated in the ECL with a validity period until September 5, 2018, which was renewed in 2018 for additional 10 years until 2028 in accordance with the ECL. Due to changes in the bylaws the 900 MHz band was opened for UMTS technology and based on MKT's request the radiofrequency license was changed so that these frequencies are now available for both GSM and UMTS technology.

In 2008 a decision for granting three licenses were published. The validity of the license is 10 years i.e. December 17, 2018, License was renewed in 2018 with for 10 years, until 2028 in accordance with the ECL.

On December 19, 2014, amendments of the ECL were enacted. Many significant changes were made on the ECL, with the Balkan Roaming Regulation being one of the most important changes made in line with EU Roaming III regulation. The glide path for roaming prices reduction finished on July 1, 2017. Additional roaming regulation was proposed, with final goal roaming prices among the Western Balkan countries to be on the same level as domestic ones, starting from July 2021 (RLAH – Roam Like At Home – model).

Both mobile operators on the market, T-Mobile and One.VIP are designated as operators with SMP status on relevant wholesale market "Access and call origination on public mobile networks". The Agency imposed same regulatory remedies for both operators:

- mobile access obligation for all MVNO hybrid types (including Reseller),
- cost based price for Full MVNO
- retail minus (-35%) for the Reseller,
- obligation for access to MMS services and mobile data based on technology neutrality

An MVNO, Lyca Mobile hosted on One.VIP network entered the Macedonian market and started retail operations in July 2016 under regulated wholesale conditions.

Telekabel offering fixed services, in January 2019 started operating as MVNO hosted on Telekom mobile network under regulated wholesale conditions.

Both operators, Telekom and One.VIP are designated as operators with SMP status on relevant wholesale market "Wholesale call termination on public mobile networks". The current termination rates are symmetrical for Telekom and One.VIP, but Lyca Mobile has high assymmetry starting from May 2018. .

The Agency made new market analysis in the middle of 2018 for „Wholesale SMS termination in public mobile networks" and deregulated Telekom and One.VIP, which were SMP operators on this market, and removed all obligations to both operators.

An auction procedure concluded in August 2013 awarded the whole 790 – 862 MHz band together with the unassigned spectrum in the 1740–1880 MHz band for Long Term Evolution (LTE) technology in a public tender. Each of the 3 Macedonian mobile operators, at that time, obtained an LTE radiofrequency license of 1x10 MHz in the 800 MHz band and 2x15 MHz in the 1800 MHz band. Each license was acquired for a one-off fee of EUR 10.3 million (approximately HUF 3.2 billion). The license is for 20 years, until December 1, 2033, with an extension option for 20 years, in accordance with the ECL.

After the merger of One and VIP, One.VIP submitted a request on November 18, 2016 to the Agency for change of the licenses for using radio frequencies in land mobile service with record numbers 108269/1, 108271/1, 104068, 104069, 104711, 108269/2 and 108267/2. The Agency brought resolution not to approve the reshuffling request of One.VIP.

Based on public debate at the beginning of 2017 the Agency adopted changes in the Rulebook on Radiofrequencies fees:

- Decrease of RF fees from 2.3 GHz to 3 GHz for 43% (from 16,800 EUR/MHz to 9,600 EUR/MHz)
- Decrease of RF fees above 3 GHz for 76 % (from 16,800 EUR/MHz to 4,000 EUR/MHz)
- Decrease of RF fees above 55 GHz (E band RF links) for 50% (from 8,000 EUR/250 MHz to 4,000 EUR/250 MHz)

The change is favorable for the existing operators and for new entrants, especially for 2.6 GHz (not occupied).

Licence duration of two licences previously owned by VIP was until 2017, 10 MHz from 900 MHz band and 10 MHz from 1800 MHz band expired on March 23, 2017, positioned in the lower parts of the bands. Based on request from One.VIP for licence prolongation, the Agency brought resolution No. 0804-974 from November 2, 2016 not to prolong these two licences. At the moment these radiofrequencies are not allocated and not available for sale.

On May 26, 2017 One.VIP submitted a request to the Agency for change of the licence for using radio frequencies in land mobile service with registered number 108267/2, whereby the following radiofrequency block is allocated: 1770-1785/1865-1880 MHz. On October 9, 2017, the Agency issued resolution for refusal of one.VIP's request for reshuffling on 1800 MHz.

The Agency announced in their 2019 working program preparation of tender for 700 MHz band. Also they announced release of Digital dividend 2 radiofrequencies and repositioning of the broadcasters in the lower part of the UHF band. Also, public debate on high of onetime fees and annual fees for 5G spectrum is expected in 2019 with possibility 3.xGHz to be announced on public tender.

34.5 Macedonian Fixed line

Makedonski Telekom has SMP obligations in several regulated markets for fixed services.

At the beginning of 2015, the regulation for access to fiber was implemented, with Local Bitstream Access over NGA on level 3 and 4 and VULA (Virtual Unbundled Local Access) regulation on level 2. The introduction of new technologies (VDSL Vectoring technology in 2017) announced by MKT for the retail customers led to the introduction on new wholesale access products and reshaping the regulatory obligations.

Final document for wholesale central access for mass-market products provided at a fixed location market analyses (Market 6) was published in April 2017. For the first time the Agency imposed regulation of access to Hybrid Fiber Coaxial Access (HFC). All existing obligations for the copper and fiber network remain unchanged. All obligations apply for MKT and for One.VIP operator as SMP on the broadband market.

According to the Rulebook for technical conditions and building infrastructure (from July15, 2014), Makedonski Telekom AD is obliged to build its infrastructure underground in urban areas with over 15,000 citizens for buildings for collective living with more than eight apartments. MKT has a Digital Agenda obligation for coverage of 100% and 50% of all Macedonian households with 30 Mbps and 100 Mbps broadband speed respectively, with a technology neutral basis until the end of 2020.

The amendments in September 2016 with a new obligation to register on the new & existing electronic networks (ATLAS), refer to the joint building and use of networks and a new obligation for the Agency to publish the received reports on the optic backbone segment measurements by all operators.

The tender for USO provider has been published at the end of 2016, and one of the main criteria is the required amount for a refund.

According to the results from the last tender, the Company is universal service provider until 2021 for the following services:

- Fixed access and access to disabled users (voice and internet of minimum 2Mbit/s download)
- Public payphones

The tender for USO provider was completed at the end of 2016 and also R3 Infomedia signed contract with the Agency for the Telephone Directory and Directory Inquiry universal services.

Following the market trends and EU regulation, the Agency made decisions for deregulation on several markets: trunk segment of leased lines and avoiding regulation of the Ethernet leased line services; minimal set of leased lines (retail); WLR (Wholesale Line Rental) market; traditional retail fixed voice services (access and traffic). MKT has a cost based price obligation for the regulated wholesale services, using Long Run Incremental Costs methodology (LRIC).

The Agency developed process and model for economical replica of retail and wholesale NGN (Next Generation Network) products.

Ministry for information society and administration formed working groups for mapping the telecommunication networks and developing National Broadband Plan and 5G strategy for fulfillment of the Digital Agenda, which should be finalized in Q1 2019.

35 EVENTS AFTER THE REPORTING PERIOD

35.1 Cable TV network and operations

In December 2018, the Group signed a Share Purchase Agreement to acquire a cable TV business for a purchase price of HUF 789 million. The closing of the transaction took place in February 2019.

35.2 Sale of Szerémi-Kaposvár buildings

In January 2019, the sale of Szerémi-Kaposvár buildings was completed, representing the last remaining transaction of the comprehensive real estate agreement signed with WING Group on May 19, 2015. The sales price amounted to EUR 11.3 million.

Budapest, February 20, 2019.

Tibor Rékasi
Chief Executive Officer, Board member

János Szabó
Chief Financial Officer

CONSOLIDATED BUSINESS REPORT

MAGYAR TELEKOM TELECOMMUNICATIONS

PUBLIC LIMITED COMPANY

FOR THE YEAR ENDED DECEMBER 31, 2018

INTRODUCTION

The Company's activities are described in Note 1 of the Consolidated Financial Statements, while the business report provides additional information on the following topics:

- SUMMARY ON 2018 OPERATIONS
- THE COMPANY'S SHARE CAPITAL, VOTING RIGHTS AND TRANSFER OF SHARES
- CORPORATE GOVERNANCE
- SOCIAL COMMITMENTS, LABOUR STANDARDS, HUMAN RIGHTS
- COMPENSATION OF MEMBERS OF THE BOARD OF DIRECTORS, SUPERVISORY BOARD, AND MANAGEMENT COMMITTEE
- RESEARCH AND DEVELOPMENT
- REAL ESTATE, SITES OF OPERATION
- SUSTAINABILITY
- ENVIRONMENT PROTECTION
- CORPORATE COMPLIANCE
- ECONOMIC ENVIRONMENT
- TARGETS AND STRATEGY
- INTERNAL CONTROLS, RISKS AND UNCERTAINTIES
- ANALYSIS OF FINANCIAL RESULTS FOR 2018
- SUBSEQUENT EVENTS BETWEEN THE END OF THE YEAR AND THE RELEASE OF THE REPORT

SUMMARY ON 2018 OPERATIONS

Tibor Rékasi, CEO commented:

"The Group has maintained strong earnings momentum throughout 2018, delivering revenue growth of 7.6% for the year. We outperformed our guidance, for both revenues, which reached HUF 657.1 billion, and EBITDA, which amounted to HUF 192.5 billion. The factors behind the EBITDA growth were the higher gross profit and one-off profit realized by the sale of real estates. We also exceeded our free cash flow target, which reached HUF 68 billion in 2018 thanks to a higher EBITDA, declining acquisition costs and the one-off income from the real-estate sales, while CAPEX stood at HUF 91.8 billion. Furthermore, through our continuous focus on our core business and meeting customer needs, and by constantly refreshing our product offering, we regained or maintained our leading position in all key market segments, including post-paid mobile, TV and fixed broadband.

In Hungary, positive business trends continued throughout the year, with revenue growth across all three major business lines. In the mobile segment, demand for mobile data continued to grow as more customers used our state-of-the-art 4G network, significantly supporting revenue generation. This was reinforced by our ongoing strategy for equipment sales and the migration of pre-paid customers into post-paid packages. We delivered moderate growth in our customer base, while also increasing mobile ARPU in Q4, with growth of 6.8% achieved in the full year.

In the fixed market, we maintained our strong focus on growing our fixed network, providing nearly 300,000 new households with 100+ MBs internet connectivity, and bringing us closer to our goal of providing gigabit internet connectivity across the whole country. We continued to see the positive results of this strategy in the growth of fixed line revenue, where – despite the industry-wide trend of declining voice revenues – we grew revenues by 5.5% year-on-year and by 4.9% in the final quarter. Furthermore, broadband and TV revenues and fixed line equipment revenues maintained strong growth, reaching 95.9% year-on-year, thanks to a strong fourth quarter performance helped by Black Friday and Christmas promotions.

With the strong performance of both our fixed and mobile business lines, we were able to focus on the third pillar of our core business strategy, the FMC customer base. In 2018 we remained the only truly integrated player in Hungary and we took action to reinforce our leading position in this market. While in the second quarter we doubled the mobile data allowance, in the third quarter we unified our offering, giving our Magenta1 customers the ability to secure a 30% discount on all related services. Building on this we were able to continuously grow our Magenta1 customer base, by offering a simpler and more attractive package. We also looked for new ways to reach our customers and strengthened our online channels. Over 40% of our customers now use our Telekom app and over 20% of all sales occur via our online channels.

In the System Integration and IT segment we had a strong year, achieving 22.4% growth versus 2017. Once again, the growth was attributable to a high volume of software and hardware projects with lower profit margins. Our strategy is to continue focusing on these deals, to build long-term relationships with our business partners, and over time convert these relationships to higher margin service contracts.

Group performance during the year was further supported by the continued turnaround in Macedonia. Both revenues and EBITDA improved, thanks to a solid performance across all business lines, positive trends in service revenues, and outstanding growth in System Integration and IT revenues."

1 THE COMPANY'S SHARE CAPITAL, VOTING RIGHTS AND TRANSFER OF SHARES

As of December 31, 2018, the share capital of Magyar Telekom Plc. was HUF 104,274,254,300, consisting of 1,042,742,543 Series "A" dematerialized ordinary shares. All Series "A" ordinary shares have a nominal value of HUF 100. Rights and obligations related to Series "A" ordinary shares are described in detail in Section 2 of the Articles of Association (http://www.telekom.hu/about_us/investor_relations/corporate_governance/corporate_governance_documents). Information concerning our ownership structure as of December 31, 2018 is described in the following table:

Shareholder	Number of shares	Percentage of share capital
Deutsche Telekom Europe B.V.	617,436,759	59.21
Publicly traded	416,469,436	39.94
Treasury shares	8,836,348	0.85
	1,042,742,543	100.00

Deutsche Telekom Europe B.V. owning 59.21% of the Company's voting rights is member of the Deutsche Telekom Group. The ultimate controlling parent of Magyar Telekom is Deutsche Telekom AG (DT or DTAG).

Deutsche Telekom Europe B.V. does not have different voting rights than our other shareholders and, as with our other shareholders, Deutsche Telekom Europe B.V. is entitled to one vote per each ordinary share that it owns.

1.1 Voting Rights and Voting

The holder of each Series "A" ordinary share shall be entitled to one vote at the General Meeting of the Company. The names of shareholders and nominees who intend to participate at the General Meeting shall be registered in the Share Register on the second working day prior to the starting date of the General Meeting. The General Meeting shall adopt its resolutions by a simple majority vote except for resolutions on issues listed in the Articles of Associations, which shall require at least a three-quarters majority of the votes cast. There is no limitation on the rights of non-resident or foreign shareholders to hold or exercise voting rights on the ordinary shares. There is no limitation of voting rights for ordinary shares in the Articles of Association. The Company has no shares assigned with special management rights.

1.2 Transfer of Shares

For the transfer of dematerialized share a contract for transfer or other legal title is required and, in that context, the transferor's securities account shall be debited and the new holder's securities account shall be credited with the transferred dematerialized shares. The holder of dematerialized share shall be considered the holder of the securities account on which the dematerialized shares are recorded.

The transfer of any Series "A" ordinary shares is not bound to any restriction or attainment of agreement.

2 CORPORATE GOVERNANCE

2.1 Annual General Meeting

The General Meeting has the exclusive right to approve and amend the Articles of Association (section 5.2.(a)) unless otherwise provided by law or the Articles of Association. According to the Articles of Association, the Board of Directors is entitled to make decisions regarding any change in the registered seat, sites, branch offices and – except for the main activity – the scope of activities of the Company and in relation to this, to modify the Articles of Association (section 6.4.(p)).

2.2 Board of Directors

The detailed rules on the scope of authorities and operation of the Board of Directors are detailed in 6.4 of the Articles of Association and in the Rules of Procedure of the Board of Directors (https://www.telekom.hu/about_us/investor_relations/corporate_governance/board_of_directors).

The rules of competence regarding the capital increase and purchase of treasury shares are detailed in Sections 5.2 (b) and (p) as well as 6.4. (l) and (m) of the Articles of Association. The General Meeting by its Resolution No. 8/2018 (IV.10.) authorized the Board of Directors to purchase Magyar Telekom ordinary shares for 18 months starting from the date of approval of the resolution. See the detailed description of the authorization on the General Meetings section of our website.

The Board of Directors is responsible for all matters relating to the Company's management and course of business not otherwise reserved to the General Meeting or to other corporate bodies by the Articles of Association or by the laws. The Board of Directors draws up, at the end of each business year, a report for the General Meeting and quarterly to the Supervisory Board on the management of the Company, the assets of the Company, the financial situation of the Company and the business policy of the Company.

Pursuant to the Articles of Association, the Board of Directors consists of a minimum of six and a maximum of eleven members elected by the General Meeting for a term of three years, unless otherwise provided by the General Meeting. On December 31, 2018, there were seven members of the Board of Directors.

Meetings of the Board of Directors are held at least four times a year. Meetings of the Board of Directors require the presence of at least the majority of the members for a quorum. Each member of the Board of Directors has one vote. The Board of Directors passes resolutions by a simple majority vote.

On December 31, 2018, members of the Board of Directors, their principal occupation and the years of their original election were as follows:

Name	Born	Principal Occupation	Member since
Tibor Rékasi................................	1973	Chief Executive Officer of Magyar Telekom Plc.	2018
Dr. Mihály Patai............................	1953	Chairman-CEO of Unicredit Bank Hungary Ltd.	2012
Ralf Nejedl..................................	1970	Senior Vice President B2B Europe, Deutsche Telekom AG	2016
Frank Odzuck..............................	1959	Chief Executive Officer of Zwack Unicum Plc.	2006
Dr. Robert Hauber........................	1971	Senior Vice President Finance & Performance Management Europe, DT AG, Chairman of the Board of Directors of Magyar Telekom Plc.	2017
Guido Menzel..............................	1961	Senior Vice President Technology Europe, Deutsche Telekom AG	2017
Mardia Niehaus...........................	1963	Lead of Innovation Hub at Technology & Innovation, Deutsche Telekom AG[i]	2017

The members' assignment lasts until May 31, 2019.

[i] As of January 1, 2019 Senior Vice President HR BP Technology&Innovation.

2.3 Management Committee

Pursuant to the Rules of Procedure of the Board of Directors, the Board of Directors established a Management Committee in 2000. The Management Committee carries out its activities based on its Rules of Procedure approved by the Board of Directors, which is available on the Company's website:

(http://www.telekom.hu/about_us/investor_relations/corporate_governance/management_committee).

Management Committee membership shall last from the date of the assignment or from the date set forth therein as the date of the assignment, to the termination of the assignment, due to any reasons.

On December 31, 2018, the members of the Management Committee and the years of their original election were as follows:

Name	Born	Current position	Member since
Tibor Rékasi................................	1973	Chief Executive Officer of Magyar Telekom Plc.	2013
János Szabó................................	1961	Chief Financial Officer	2013
Dr. Balázs Máthé[i].........................	1968	Chief Legal and Corporate Affairs Officer	2010
Melinda Szabó.............................	1971	Chief Commercial Officer Residential	2018
Zsuzsanna Friedl	1977	Chief Human Resources Officer	2017
Zoltán Kaszás.............................	1968	Chief Commercial Officer Enterprise, Chief Executive Officer of T-Systems Hungary Ltd.	2017

[i] MC membership terminated on December 31, 2018

2.4 Supervisory Board

The Supervisory Board carries out its activities based on Section 7 of the Articles of Association and its Rules of Procedure approved by the General Meeting (https://www.telekom.hu/about_us/investor_relations/corporate_governance/supervisory_board). The Supervisory Board shall examine all submissions to be submitted to the General Meeting and present its opinion thereof at the General Meeting. The General Meeting may pass a resolution on a report pursuant to the Accounting Act and the use of the profit after income tax only upon receipt of the written report of the Supervisory Board. The Supervisory Board makes a proposal directly to the General Meeting regarding the election, remuneration and removal of the Statutory Auditor.

Pursuant to the Company's Articles of Association, the Supervisory Board consists of a minimum of three and a maximum of fifteen members elected by the General Meeting for a term of three years, unless otherwise provided by the General Meeting. The Central Workers' Council of Magyar Telekom nominates one-third of the Supervisory Board members (employee representatives). Meetings of the Supervisory Board have a quorum if two-thirds of its elected members but at least three members are present.

On December 31, 2018, the members of the Supervisory Board, their principal occupation and the years of their original election were as follows:

Name	Born	Principal Occupation	Member since
Dr. László Pap	1943	Professor emeritus, Budapest University of Technology and Economics	1997
Dr. János Bitó	1936	Chairman of the Thesis and Final Examination Board at Pázmány Péter Catholic University, Information Technology Faculty	2010
Attila Bujdosó	1967	President of the Telecommunications Trade Union	2018
Sándor Hartai	1966	Expert of Wholesale Directorate, Magyar Telekom	2016
Dr. János Illéssy	1962	Managing Director of Lebona Kft.	2006
Dr. Sándor Kerekes	1948	Director of Institute of Environmental Sciences, Corvinus University Budapest	2006
Konrad Kreuzer	1948	Managing Director of EUTOP Vienna, Budapest and Prague	2006
Tamás Lichnovszky	1962	Chairman of the Central Workers' Council, Magyar Telekom	2010
Martin Meffert	1960	Project Manager Asset Development Europe, Deutsche Telekom AG	2009
Dr. Károly Salamon	1954	Managing Director of MIS Kft.	2010
Zsoltné Varga	1969	Quality Manager, Magyar Telekom	2008
Dr. Konrad Wetzker	1950	Chairman of the School of Management of Corvinus University Budapest	2011

The members' assignment lasts until May 31, 2019.

2.5 Audit Committee

The Audit Committee executes its duties pursuant to the Articles of Association Section 7.8, and its own Rules of Procedure (https://www.telekom.hu/about_us/investor_relations/corporate_governance/audit_committee). The members of the Audit Committee have been elected by the General Meeting from the independent members of the Supervisory Board for the same period as their membership in the Supervisory Board.

On December 31, 2018, the members of the Audit Committee were as follows:

- Dr. János Illéssy
- Dr. János Bitó
- Dr. Sándor Kerekes
- Dr. László Pap
- Dr. Károly Salamon

2.6 Remuneration and Nomination Committee

As of September 20, 2013, certain nomination related tasks were also assigned to the Remuneration Committee and its name was changed to Remuneration and Nomination Committee.

The Remuneration and Nomination Committee is established by the Board of Directors of the Company to function as supporting body of the Board of Directors of the Company regarding the remuneration and certain nomination related issues of the members of the corporate bodies and the top executives of the Company in accordance with its Rules of Procedure. (https://www.telekom.hu/about_us/investor_relations/corporate_governance/compensation).

The Remuneration and Nomination Committee, among others, makes recommendations to the Board of Directors on the establishment and/or termination of employment, and the modification of the employment contract of the chief executive officer and the chief officers, as well as the remuneration package of the chief executive officer and the chief officers, including setting and evaluating annual individual targets. The Remuneration and Nomination Committee holds at least two meetings each year.

The Remuneration and Nomination Committee consists of three members. The members are elected by the Board of Directors from among its members.

On December 31, 2018, the members of the Remuneration and Nomination Committee were as follows:

- Frank Odzuck
- Dr. Robert Hauber
- Ralf Nejedl

2.7 Corporate Governance and Management Report

Magyar Telekom Plc. is a public limited company listed on the Budapest Stock Exchange. In 2004, the Budapest Stock Exchange issued its Corporate Governance Recommendations (the Recommendations) containing recommendations related to the corporate governance practice of companies listed on the Budapest Stock Exchange, taking account of the most commonly used international principles, of experiences gathered in Hungary, and of the characteristics of the Hungarian market as well as the Companies Act. The Recommendations were updated in 2007, 2008, 2012 and in 2018. The Recommendations effective from time to time is available at the website of the Budapest Stock Exchange: https://www.bse.hu/Products-and-Services/Rules-and-Regulations/BSE-Rules

In line with the current regulations, the Board of Directors of Magyar Telekom Plc. approved the Corporate Governance and Management Report of the Company (report) prepared in accordance with the Corporate Governance Recommendations and submitted it to the General Meeting. The report – along with other corporate governance related documents- is published at the Corporate Governance section of the website of the Company:

http://www.telekom.hu/about_us/investor_relations/corporate_governance/corporate_governance_documents

Companies listed on the stock exchange are required to express their views on their corporate governance practices in two ways. In the first part of the report they have to give account of the corporate governance practices applied by their company in the given business year, including their corporate governance policy, and a description of any unusual circumstances. In the second part of the report, the issuers should give an account on their compliance with each point of the Recommendations in accordance with the "comply or explain" principle, including any reasons for derogating from a specific recommendation and/or proposal. When an issuer does not apply a recommendation or applies it in a different way, they should explain where the differences are and offer a reason for such derogation ('comply or explain' principle). This method allows issuers to consider their unique, industry-specific etc. idiosyncrasies and to inform shareholders and market players about their derogations from general corporate governance principles and to provide an explanation. Operating on the same principle, issuers can also explain any derogations from the proposals.

The Corporate Governance Declaration on the Compliance with the Corporate Governance Recommendations, and regarding certain questions the possible alterations and their explanations are included in the report. Sections 1 to 5 of the above report include the description and operation of the Board of Directors, the Supervisory Board, the relevant committees and executive management. Section 6 of the report includes a description of the internal controls and risk management procedures, while Section 8 of the report describes the disclosure policies and insider trading guidelines. In Sections 9 to 10 the method of excercising shareholders' right and the rules on conducting the General Meeting is summarized, while Section 11 contains the Remuneration Statement. The Company complies with the vast majority of the 85 recommendations and proposals, however in the business year of 2018 in case of 4 recommendations and 2 proposals it has not or not completely complied with due to the organizational structure or processes of the Company.

The Board of Directors, through the internal audit area, carried out an evaluation of the Company's disclosure processes in 2018 again. Based on the evaluation, the disclosure controls and procedures of the Company were effective and designed to ensure a proper basis for the timely and accurate disclosures to the market participants required under the respective accounting, capital markets and company law regulations.

3 SOCIAL COMMITMENTS, LABOUR STANDARDS, HUMAN RIGHTS

Some of the key challenges of the sustainability strategy come from the area of human resources management. This is why human resources management has a crucial part in the achievement of our sustainability targets. Our vision is to operate in a corporate environment that is livable, likeable and successful. This set of values strengthens the commitment and satisfaction of our employees and is also attractive on the job market.

3.1 People strategy

3.1.1 People strategy from the perspective of the company

The priorities of Magyar Telekom's people strategy in 2018 were:

- Improvement of employer branding
- Culture development – growth mindset – development based corporate culture
- Increased digitalization

3.1.2 People strategy from the perspective of our employees

The business strategy of Magyar Telekom is centered around the realization of a digital business model that is based on utilizing new technologies in service of consumer relationship management in order to build trust and drive value creation. In support of reaching this goal the operating model and the organization of HR has been transformed to an even more efficient and client oriented body backing up the corporate business strategy goals.

Key focus areas of HR in 2018:

- Efficient support of transforming workforce
- Development of adaptive corporate structure and culture
- Diverse and attractive workplace
- Resilient and impactful HR organization

Employer brand building – we create a livable and likeable workplace, which is satisfactory for our employees and offers an attractive perspective in the labor market through its future oriented methods of work. We put greater emphasis on using social media solutions in building the brand.

Recruitment-selection – We use segment-based online recruitment channels and means to select the best candidate for the specific positions. During the selection process, we seek the attitude and personal traits defined as requirements for future Telekom employees.

Remuneration –We make our company attractive for employees by means of our wide range of benefits. We have a transparent, simpler and consistent job grading model, which reflects primarily the respective values of jobs, and provides for market comparison, as a basis for a competitive remuneration policy.

Training development– We owe our competitive advantage to our qualified workforce. We are building a digital Telekom, thus put an increasing emphasis on collaborative digital tools and solutions that enable and inspire self-development. Online training catalogue, online training materials, online coachbank and mentoring, online knowledge sharing (Share).

Wellbeing – Energetic employees We take action for each other and ourselves in order to maintain our physical, mental and social wellbeing. Energized employees make us successful. We draw employees' attention to conscious preventive health efforts, volunteer work, sustainability and work-life balance.

3.1.3 Headcount

The following table provides information on the number of full-time employees, including full-time equivalents, of Magyar Telekom Plc. and its consolidated subsidiaries:

	2017	2018
Magyar Telekom Plc.	6,241	6,134
A Magyar Telekom Plc. and its consolidated subsidiaries	9,154	8,948

	2017	2018
MT-Hungary / Telekom Hungary	7,977	7,865
Macedonia	1,177	1,083
Total	9,154	8,948

From 2017 the operating segments of the Group: MT-Hungary and Macedonia. Please refer to the Note 33. to Consolidated financial statement for further details.

3.2 Policies

3.2.1 Policies and agreements

Code of Conduct: https://www.telekom.hu/static-tr/sw/file/mt-code-of-conduct.pdf

The Code of Conduct provides the framework of orientation for all employees of Deutsche Telekom Group and Magyar Telekom Group. Additionally, it applies to people to who are viewed as equivalent to employees in functional terms, e. g. to temporary agency employees. It combines the joint requirement of compliance with legal obligations and acting with integrity and thus ensures that Deutsche Telekom and Magyar Telekom remain transparent and traceable enterprises for everybody. Deutsche Telekom and Magyar Telekom expect their suppliers and consultants to comply with the rules of behavior manifested in this Code of Conduct and to endeavor them to ensure that they are also obliged to abide to its regulation by contract.

Code of Human Rights and Social Principles:

https://www.telekom.hu/static-tr/sw/file/code-of-human-rights-social-principles-eng.pdf

Equal Opportunities Plan: https://www.telekom.hu/static-tr/sw/file/Magyar_Telekom_Eselyegyenlosegi_Terv_2016_2020_en.pdf

The Code of Human Rights and Social Principles and the Equal Opportunities Plan of Magyar Telekom set the general human rights principles of the group and guidance to their group-wide implementation. Magyar Telekom Group recognizes and respects the fact that the cultural, social and legal diversity of its employees provide the foundations of operations based on equal opportunities. It is also a competitive advantage that leads to business success.

Diversity Policy - https://www.telekom.hu/static-tr/sw/file/Diversity_Policy.pdf

The Diversity Policy of Magyar Telekom Group underscores our commitment to consistently identify and utilize potential for improvement.

Group Policy on Employee Relations - https://www.telekom.hu/static-tr/sw/file/Employee-relations-policy.pdf

The policy is present as an internal corporate directive since 2011 and was being published as a public corporate policy in 2018. Based on our shared values and Guiding Principles, this policy offers a framework that enables the entire workforce to strengthen business performance, contribute individually to business objectives and increase shareholder value. Employee relations cover all aspects of the work life cycle that are relevant to the employment relationship.

Suppliers' Compliance: Magyar Telekom Group is committed to respect and protect human rights and it expects its suppliers to comply with these rules of behavior. Prior to becoming authorized suppliers of Magyar Telekom and T-Systems our suppliers must register their enterprises at our vendors' registration site.

https://beszerzes.telekom.hu/beszerzes/portal_en?appid=beszerzes&page=english/registration_vendor.vm

As an obligatory part of the registration process vendors are obliged to understand and accept our Suppliers Code of Conduct that among other policies, entails our Code of Conduct, Social Charter and Diversity Policy. Our suppliers must understand and accept these policies and obligatory frameworks for their behaviors as well.

Equal Opportunities Plan: https://www.telekom.hu/static-tr/sw/file/Magyar_Telekom_Eselyegyenlosegi_Terv_2016_2020_en.pdf

Anti-discrimination and the safeguarding of equal opportunities is a key priority to Magyar Telekom Group. According to the act CXXV of 2003 on Equal Treatment and Promotion of Equal Opportunities, and the corporate protocol in place since 2010 Magyar Telekom Group has accepted its 4th Equal Opportunities Plan in order to secure the practices of equal treatment, the advancement of equal opportunities and the monitoring an improvement of the labor positions of particular disadvantaged employee groups. The Equal Opportunities plan currently in force is valid between 2016 and 2020 and has been developed in close cooperation with the employee representative bodies.

The Diversity Charter of the European Union – Hungary has joined the Diversity Charter of the European Union in 2016 and, among 50 signatory companies Magyar Telekom has also underscored its dedication to safeguard diversity as a fundamental value. Magyar Telekom has been among the signatory companies in 2017 and 2018 as well.

UN Guiding Principles on Business and Human Rights – According to the dedication of Magyar Telekom Group to safeguard and protect human rights along its operations as stated in the UN Guiding Principles of Business and Human Rights, the company considers the rights and guidelines stated in the Universal Declaration of Human Rights and in the ILO's Declaration on Fundamental Principles and Rights at Work to be mandatory in its own practices.

UN Human Rights Treaties ratified by Hungary – Magyar Telekom Group as a corporation legally registered in Hungary is carrying out its entire operations and business practices in full accordance with the nationally ratified UN Human Rights Treaties.

http://tbinternet.ohchr.org/_layouts/TreatyBodyExternal/Treaty.aspx?CountryID=77&Lang=EN

3.2.2 Monitoring and auditing practices

The group-level coordination of corporate sustainability operations that also incorporate labor standards, social issues and the protection of human rights is being coordinated by the Group Sustainability Coordination Council (GSCC). The levels of development and management of the corporate sustainability strategy are separated from the operative implementation level within the operation of the GSCC, thus the process of implementing sustainability activities is divided to the level of strategy development and management, and the level of operative implementation.

According to the relevant group directive the strategic tasks are allocated to the respective Chief Officers. 50% of the bonuses of Chief Officers depend on the performance of collective objectives. More detailed information about the actual operation of the GSCC and its reporting obligations towards the Management Committee could be found in the Sustainability chapter of this document and in the annual Sustainability Report.

Magyar Telekom Group's Code of Conduct covers the requirements of corporate compliance and states our collective set of values, and thus stands as an affirmation of Magyar Telekom's strong reputation, solid position and future success. The Code of Conduct applies to all board members of Magyar Telekom Group from employees to managing directors, executives and board members. Furthermore, Magyar Telekom Group expects its suppliers and consultants to comply with the rules of behavior manifested in this Code of Conduct and to endeavor them to ensure that they are also obliged to abide to its regulation by contract.

Magyar Telekom Group's Corporate Compliance Program has been elaborated with the aim to ensure that Magyar Telekom Group conducts its business with maximum consciousness and commitment, in accordance with relevant laws and regulations, in harmony with the strictest possible business ethics standards. The Compliance Program involves the Group Compliance Manager and compliance representatives of particular functional areas of operation, who are working together as members of the Group Compliance Committee. The Compliance Program has been designed to ensure that the Group conducts its business to the highest standards of awareness, transparency, accountability, commitment, and adherence to applicable laws and regulations.

External audits could be conducted as part of the control process carried out by the Hungarian Labor Inspectorate. The Inspectorate has the right to issue such an auditing process in case of public complaints or issued requests. The Inspectorate also provides counseling to the corporations in support of legal compliance.

3.3 Results of Policies

3.3.1 Diversity and Equal Opportunities

As one of the largest employers in the Hungarian ICT sector we believe that diversity contributes to the success of businesses and all kinds of organizations to a large extent. This value is also at the core when it comes to the increase of creativity and innovation, to the involvement of new partners, experts and clients, to the quick adaptation to changes and most of all, to the compliance with the legal obligations of non-discrimination in all corporate operations.

The corporate Equal Opportunities Plan of 2016-2020 addresses actions and procedures to improve the labor conditions and career perspectives of particular vulnerable employee target groups such as women, employees with families, employees on child-care leave, employees living with disabilities, recent graduates and 50+ employees. In order to maintain this focus Magyar Telekom has developed and accepted Equal Opportunities plans since 2008 in close cooperation with the employee representative bodies. The current is the 4^{th} Equal Opportunities Plan of the company, the guidelines, policies and actions of which cover the 2016-2020 period.

The principles of justice and equal treatment of Magyar Telekom are being defined by our Code of Conduct. Ways of non-typical employment such as Telework, flexible working hours, part-time work, employment of people living with disabilities allow the company to realize the principle of equal treatment in practice. These measures are further assisted by several measures implemented in corporate day-to-day operations, such as the large office spaces that are designed to support Teleworking in the new headquarters of Magyar Telekom.

In accordance with Hungarian labor legislations we provide our employees with extra days off after their children, and after blood donation. In case of more than 40% health damage we provide our employees with extra five days off annually for rehabilitation. On top of these we also credit the voluntary work of our employees by providing days off, the proportion of which is strictly regulated in internal directives.

One of the targets of our 2016-2020 Sustainability strategy was to measure and improve the diversity culture of Magyar Telekom. We have measured the state of corporate diversity culture through an internal survey in January 2018. After the evaluation of the results we have defined the strategic steps, targets and result indicators of the effective improvement of our corporate diversity and equal opportunities culture that is going to be advanced through the complex implementation of operative measures.

3.3.2 Anti-discrimination and labor-market integration actions

As an employer, Magyar Telekom has issued the following actions in 2018 to improve the conditions of the employee groups marked in the 2016–2020 Equal Opportunities plan.

The company continued to support the HRom and Integrom labormarket integration programs aiming to support and enable young roma talents to connect with large corporations and help them in their job application processes. In 2018 the corporate recruitment team received a professional training on labor market inclusion practices of vulnerable social groups. As a member of the Hungarian Employers Forum on Equal Opportunities we have contributed our experiences and best practices to the paper (HU-only) 'Diverse and inclusive workplaces for roma and others' http://mef.forum.hu/ckfinder/userfiles/files/sokszinu_befogado_munkahelyek.pdf

In order to secure the equal opportunities of our current and future colleagues living with disabilities, we are using a special module on our online job-application site (http://www.telekom.hu/rolunk/ karrier) since 2010, where our applicants are encouraged to state any accessibility requests they might have in order to attend the selection process.

3.3.3 Respect of Human Rights, actions against child labor and all kinds of forced labor

As disclosed in the Code of Human Rights and Social Principles the company rejects child labor and all kinds of forced or compulsory labor and fights against all kinds of human trafficking and modern day slavery by all means at its disposal. As the parent company of Magyar Telekom Deutsche Telekom Group is responsible for supply chain compliance auditing and management on a global level. More detailed information about the methodology and results of the global supply chain management at https://www.telekom.com/en/corporate-responsibility/assume-responsibility/assume-responsibility/supply-chain-management-355304

New employees of Magyar Telekom Group as part of their orientation process in their first two months receive compulsory education about the company principles, guidelines and practices concerning social issues, labor standards and human rights. All employees must understand and accept these guidelines as the fundaments of their own professional behavior and operations.

In line with the Code of Human Rights and Social Principles, all Magyar Telekom Group employees and all partners closely related to our brand representation attended compulsory trainings regarding human rights. From the end of 2018 the training is part of the compulsory trainings of Magyar Telekom.

Moreover, the company is aware of the fact that there could be situations in which it is harder to tell appropriate from inappropriate. In order to assist employees in making the right choices in these situations, the company offers secure internal whistleblower channels, operated by the Corporate Compliance Department. “Kérdezz!” (“Ask me!”) advice portal has been set up to help resolve uncertainties as far as compliance relevant behavior is concerned. Serious misconduct must be announced for prevention purposes and for appropriate sanctions. For this reason, the “Tell me!” whistleblower portal has been established. The main principles and the detailed description of the internal inspection process is detailed in employee directives available on all employees on the shared intranet platform. Throughout the inspection process the whistleblowers’ anonymity, personal and data privacy are guaranteed and handled with utmost discretion.

3.3.4 Relationship of management and employees

At present two unions and workers’ council operate at Magyar Telekom, communication with them runs on two levels. Central decisions concerning the whole Company, when the employee representation bodies need to be consulted, are deliberated with the Central Workers Council and the representatives delegated by the trade unions, either in the frame of joint consultation (Interest Reconciliation Council), or separately, depending on the nature of the matter discussed. Central communication is managed both verbally (negotiation) and in writing. The Chief HR Officer and the HR Strategic Director are responsible for central level communication with the employee representation bodies. Interest enforcement issues concerning a given governance area are also discussed locally with the representatives of the trade unions and the local workers’ council. The HR Business Partners of the governance area are responsible for communication with the local employee representation bodies.

Trade union and the workers’ council (Central Workers Council) must be consulted and their opinion solicited on significant decisions resulting in organizational changes or changes affecting a large group of employees. In organization restructuring decisions the collective bargaining bodies have 7 days to submit their comments, in other cases 15 days. The measure in question may not be implemented during this 15-day period. Trade unions and workers’ councils (Central Workers Council) must be consulted with regard to draft resolutions, aiming at organizational changes without regard to the number of employees concerned.

Under the Act V of 2013 on the Civil Code one third of the Supervisory Board shall consist of employee representatives. The employee representatives in the Supervisory Board are nominated by the Central Workers’ Council considering the opinion of the trade unions operating at the Company. Persons nominated by the Central Workers’ Council shall be elected by the General Meeting to the member of the Supervisory Board, except if disqualifications exist in respect of the nominated persons. On December 31, 2018, four members of the Supervisory Board were employee representatives. These members were Tamás Lichnovszky, Zsoltné Varga, Attila Bujdosó and Sándor Hartai.

3.3.5 Freedom of organization and collective bargaining

Magyar Telekom Group acknowledges the basic rights to freedom of organization and collective agreement in its Social Charter. In line with an openness and trust that relies on a constructive social dialogue, Magyar Telekom Group declares its support to cooperation with the legitimate representatives of the employees in order to establish a balance of interests.

The Social Charter together with the long history of mutual respect and cooperation of the management and employee representative councils are the guarantees that these rights are being fully and thoroughly respected. 100% of the employment contracts of Magyar Telekom Group employees operating in Hungary fall under collective bargaining agreements developed with the Hungarian Telecommunications Trade Unions (Távközlési Szakszervezet, TÁVSZAK and Magyar Távközlési Ágazati Szakszevezet, MATÁSZ). The agreement, which can be terminated by either party with three months' notice, applies to all Magyar Telekom Plc. employees except the CEO, regardless of their union membership status. Wage terms in the collective bargaining agreement must be renegotiated annually. If the employment is terminated due to reasons related to the employer’s operation, employees are entitled to a specific amount of severance pay surplus, which depends on the tenure of the employee.

In addition to the collective bargaining agreement, employees of our Hungarian operations are generally covered by the Act I of 2012 on the Labor Code, which imposes various restrictions on the involuntary termination of employment. The Labor Code protects employee interests through two different labor organizations: the Trade Union and the Workers' Council.

The Trade Union, as the official representative of employee interests in negotiations relating to the terms of employment, has the right to be informed of all corporate measures that may significantly affect the interests of employees and to commence legal action against the Company for employment-related conduct that infringes an employment rule. In addition, the Workers' Council directly represents employee interests in dealings with management and decides jointly with management on matters involving employee welfare funds and institutions. The Workers' Council must be informed semi-annually on issues affecting our economic performance and changes in wages, employment conditions and working hours. The Workers' Council must also be consulted on corporate measures affecting employees.

We believe that our relations with our employees are good. We have not experienced any labor strikes or disruptions since our formation.

3.3.6 Workforce Reduction and Redeployment

Magyar Telekom – in order to ensure the resources related to the Company's strategic objectives - has reached an agreement with the trade unions in 2018 on headcount reduction and wage increase measures for 2019.

According to the terms of the agreement, the Company plans to make ca. 400 parent company employees redundant. The majority of the employees to be made redundant are expected to have left the Company by the end of 2018 or by March 1, 2019. The company shall provide active job search, labor market training and one-on-one counselling to the colleagues laid off, in the framework of Program Chance, which has proven its success in the past years, and trusts that the above support these highly-trained employees of up-to-date professional expertise in finding employment elsewhere as soon as possible.

It is planned to reinvest a significant proportion of the expected employee cost savings in resources related to the Company's strategic objectives.

As from April 1, 2019, employee salaries at the Company will rise by an average of 5%.

3.3.7 Pensions and Benefit Programs

Magyar Telekom's welfare and social benefits constitute an exceedingly wide-ranging pool. A part of them is granted to every employee, while others are available on certain conditions or are of an insurance nature. In case of certain benefits, employee's individual contribution is a prerequisite of the employer's contribution. The way social benefits and discretionary benefits are granted is set out in the Collective Agreement and related regulations.

We provide employees with telecommunication allowances, subsidized meals, interest-free housing loans (such loans are not offered or extended to the Company's Board of Directors), discount holiday facilities and other fringe benefits. In addition to our statutory contributions to governmental health, retirement and unemployment schemes, we contribute to the employees' pension, health and self-aid savings, provided he is member of the voluntary fund, which provides private pension and health insurance as well as social benefits supplementing government pension and health benefits. We do not, however, guarantee payment by the fund to its members. In December 31, 2018, approximately 55% of employees of Magyar Telekom Plc. participated in the pension-, 36% in the self-aid-, and 43.8% in the health fund.

3.4 Risk management

3.4.1 Providing educational and professional background

The educational pillar of Magyar Telekom's Sustainability Strategy aims to improve the digital competencies of the clients and the wider public. It also aims to contribute to the development of industrial succession knowing that a potential throwback in the amount of available highly qualified professionals in the industry could mean a serious risk to maintaining, improvement and development of the quality of our services. In order to secure the highest quality service to our clients we need work with the best professionals. To be able to have them a competitive industrial educational background is necessary.

Upon the initiative and by funding of T-Labs (Telekom Innovation Laboratories, Berlin) the faculty Data Science and Engineering began to operate at Eötvös Loránd University from September 2016 as the first pillar of the EU Labs researcher network.

Magyar Telekom also provides practice opportunities for secondary school pupils from the relevant technological industries. In 2018 45 students have spent their obligatory practices at our company.

We supported the work of the Environment Protection Committee of the Hungarian Academy of Sciences as well as the scientific work of the National Adaptation Center. Our colleagues are in close relationship with several higher education institutes and we help the universities with consultancy for writing theses, expert education and giving lectures.

3.4.2 Employee expectations and equal opportunities

The pillars of our People Strategy are based on the aim to meet the needs of our employees, and to live up to the challenges of maintaining our company status as a highly competitive and future oriented employer. Our employees require security, stability, opportunities for advancement and competitive compensations. Magyar Telekom, as a company committed to provide equal opportunities to its employees, finds it especially important to harmonize wages and to terminate unjust wage gaps. Our tiered wage system, built on the Hay methodology, serves the above purpose. Our remuneration system is fully transparent thus our base wage tables and the relevant policies are available for all employees. We pay extraordinary attention not to differ unreasonably the wages of the employees performing the same tasks and that the wage differences between the employees reflect real work differences.

As an employer dedicated to diversity as a core value, Magyar Telekom finds it important to raise the amount of women in leadership positions. As a member of Deutsche Telekom Group the objective in 2010 was to increase the proportion of female managers to 30% by 2020. Along the aim to contribute to reaching the defined target, the company strives to utilize the actual business benefits inherent to the advancement of corporate diversity culture.

Magyar Telekom considers stress, overload and burnout related risk-reduction as its priority duty in relation to its employees. In order to take charge of these risks by securing an empowering environment to develop and maintain a healthy lifestyle, employees are also provided with coaching and training opportunities that help in the advancement of their task management skills. Efficient work-life balance of employees with families is further supported by our child-friendly offices and the available, tax-free nursery and/or kindergarten support that could be selected from our cafeteria benefit scheme, thus contributing to the reduction of expenses. Taking notice of the special conditions of employees (ex. illness or the longer term domestic care of a relative) a longer period of unpaid leave is also available.

3.5 Performance indicators

Education results of the 2016-2020 Sustainability Strategy:
- 48 051 smarter brains since 2016 with the help of digital inclusion programs eg. Digital Bridge, LTI

Non-typical employment at Magyar Telekom Group
- No. of Part-time employees in 2018: 585
- No. of Flexi-time employees in 2018: 1395
- No. of Teleworking employees in 2018: 3046

More women in leadership positions at Magyar Telekom Plc.
- Percentage of women in overall workforce: 35.5%
- Percentage of women in senior management: 23.5%
- Percentage of women in executive board: 40%

Volunteer work benefits at Magyar Telekom Group
- No. of volunteer working hours: 11 991
- No. of supported people by the projects: 22 581

3.6 ESOP organization

In 2018 the Company continued its incentive program based on the reshaped renumeration policy launched in 2017. According to the 2018 program the central bonus element of employees of Magyar Telekom Plc. and T-Systems Magyarország Zrt. will be paid through the ESOP organization. In order to maintain the program, the company has transferred 8 845 794 Magyar Telekom shares to the ESOP organization in two steps. The vesting condition of the 2018 year program is that is the operating free cash flow for the MT-Hungary segment for the financial year ending December 31, 2018 to exceed that for the previous year ending December 31, 2017. In accordance with the remuneration program those employees of the Company and T-Systems Magyarország Zrt. are rewarded who are under the personal scope of the Remuneration policy approved on March 26, 2018 by the Company's Board of Directors. For further information see Note 20.1.2.5 of the Consolidated Financial Statements.

4 COMPENSATION OF MEMBERS OF THE BOARD OF DIRECTORS, SUPERVISORY BOARD, AND MANAGEMENT COMMITTEE

The aggregate compensation of the members of the Board of Directors in their capacity as Board members was HUF 13 million in 2018.

The aggregate compensation of the members of the Supervisory Board in their capacity as Supervisory Board members was HUF 63 million in 2018.

The total compensation expenses (including social security and other payroll-related taxes as well as contractual termination expenses) of the members of the Management Committee (MC) was HUF 1,116 million in 2018.

On December 31, 2018, five MC members have an employment contract with indefinite duration. The notice period is two months for all five of the indefinite contracts. Pursuant to Hungarian legislation, if an employment contract is terminated before the end of its term, the absence fee received for the remaining period is up to 12 months. In case of one contract the severance payment is in accordance with the Labour Code and the Collective Agreement, for the rest of the contracts the severance payment is between 3 and 16 months. The employment status of the sixth member of the MC got terminated as of December 31, 2018.

In addition to the above, the affected persons are bound by the non-compete clause, under which the employee is barred from entering into employment with any Hungarian or international competitor of Magyar Telekom and is required to refrain from providing direct or indirect services or activities of any kind to such companies for a definite period (not longer than one year) upon termination of his/her employment. Furthermore, such employee is barred from any action aimed to recruit employees of Magyar Telekom for any other company. This limitation entails certain compensation which is proportional with the above obligation. If the employee is in breach of the agreement, he/she will reimburse the net amount of compensation to the employer. In addition, the employee will be liable for a payment of compensation to the employer.

MC members from foreign countries may be entitled to housing subsidies. There are no current members affected by this entitlement.

In line with the Company's remuneration guidelines, the Company provides contribution-based personal pension scheme and personal insurance scheme on behalf of the MC members. In addition, the MC members are entitled to the use of company cars.

For information about the Share Based Compensation programs, see Note 20.1.2 of the Consolidated Financial Statements.

5 RESEARCH AND DEVELOPMENT

Hungary

In 2018, within the scope of tender obligations, the research and development activities of Magyar Telekom were comprised of maintaining the R&D tender project funded and awarded by the National Research, Development, and Innovation Fund.

During 2017, in addition to the tender obligation, we have continued the development of several project related products and services that were based on the R&D activities of previous years.

In addition to the above, in 2018 we have continued our common R&D projects with the Hungarian Academy of Sciences in the fields Big Data. We have investigated the opportunities of modelling and forecasting mobility trends in city regions using mobile data.

In addition to innovative domestic SMEs, the research and development tasks are performed by the internal researchers as well as the product and services development staff of Magyar Telekom. In addition, the Company leverages the synergistic effect of an internal and external knowledge base, and strives for partnership with well-known innovation centers and institutes of higher education. Our main partners are renowned Hungarian universities and research institutes, such as the Budapest University of Technology and Economics, the Eötvös Loránd University, the Budapest Corvinus University, the Óbuda University, and the Hungarian Academy of Sciences.

Within the framework of cooperation launched in 2016, we have continued our work with the Technische Universität Berlin, the Department of Data Science and Data Technology operating at the Faculty of Informatics at the Eötvös Loránd University, the research and development department of Magyar Telekom and Deutsche Telekom, and the Telekom Innovation Laboratories (T-Labs) in Berlin.

As the partner of EIT Digital, Magyar Telekom promotes and supports even closer cooperation between higher education institutions and their industrial partners. Within this framework, the Budapest University of Technology and Economics and the Eötvös Loránd University provides professional support to students within the EIT Digital post gradual training system.

In 2018, we have launched the 2nd season of our internal idea incubation initiative the Mission T Program. All the applicants were from the employees of the Magyar Telekom group. Within the framework of this program applications are received and after several rounds of selection, the best five ideas are realized to prototype level. This will be followed by the go-live and business utilization of stand-alone prototypes.

In addition to the above, Magyar Telekom also believes it important to support R&D type knowledge transfer projects. As a result, it has been an active participant of the EIT ICT Labs knowledge transfer program as a professional cooperating partner since 2012, and cooperates several international R&D tender initiatives.

Macedonia

Makedonski Telekom (MKT) continues with its determination and its work to be innovation and technology leader on the market. Among the main focuses, as a continuation to the previous years, are the projects in the area of the Smart City. Further to our successful Smart Bus Transport Project implemented for the City of Skopje in 2015 and 2016 and realized demo operation solutions for a Smart Light, Smart Waste, Smart Parking, Smart Bench and Electrical Vehicle Charging in 2017, during this year we have demonstrated the advantages from the implementation of such smart systems and our competences in this area to municipalities and key accounts.

Apart of the Smart City business area, we drive full force exploring of other business possibilities for growth and development, in the field of finance, health, education etc, especially considering their business prospects and potentials in terms of top line growth of our ICT and B2B business in overall. MKT as firm supporter of the new era of smart connected way of life and working, in 2018 we realized successfully our pilot project in the area of Smart school - Hybrid Classroom, that is about implementation of ICT assisted solution for interactive learning at classes and at distance, in two secondary schools in the City of Skopje. Implementation of this project aims at creating positive change of way of education, providing advanced, self-driven, collaborative and interactive classroom experience for youngsters. As well its aim is to demonstrate how use of technology could support the quality and efficiency of the education, thus impacting the long-term development of the educational system as well as the society and economy.

Moreover we investigated potential market and we made cost analysis for implementation of Narrowband for Internet of Things (NB-IoT).

Also, utilizing the potential coming out from the EU funded projects in the smart Digitalization, IoT solutions, e-government, etc., was under close loop as well.

In addition to the business development activities given above, in 2018 we put focus to the development of the projects and products for digitalization and smart working for the business segment, which we believe that are growing market potentials in the forthcoming years, expected to be driven by the advantages of the efficiency of ICT in daily workflows systems and networks, as well as by the transparency and accountability of such solutions.

Under the motto - INNOVATION SYNERGIES – WIN WITH PARTNER, we keep further on our strategic technology partnerships-Cisco Gold, EMC Cloud solution provider and Microsoft Silver Data Center. Furthermore, in 2018 we got recertification of our Oracle Platinum and HP Business partnership, and have finished the process of getting a status of Microsoft Cloud Solution provider and we lunched Office 365 as a first Microsoft Cloud product. These partnerships are confirmations of MKT's competences in the areas of enterprise networks, cloud, collaborations, network securities, and Data Center technologies. Such competences are deemed to be crucial assets on which we can leverage further in our ICT business development activities.

Competitive pressure in conjunction with saturated Telco market, complexity of business environment with multiple and more sophisticated customer segments, multiple vendors and complex service offerings, fast changes in the technology with new technology paradigm targeting for one universal IP network and cloud based service delivery platform, as well as changes in the regulations, are only part of the challenges that MKT will face in the next few years.

In order to keep sustainable business and major revenue streams in very complex telecommunication environment, as well as proactively influence to market trends with new business opportunities, MKT is aiming to keep technology leadership position and ensure growth through service improvement and innovation by continuous development of its infrastructure.

Development of infrastructure and investment in Technology should encompass the following objectives/trends: broadband performance, integrated service delivery platforms, efficiency and quality leadership, self-service enablers, cloud concept and "virtual" infrastructure, cost efficiency, flexibility and responsiveness – reduced time-to-market, as well as competence development.

During 2018, we have made significant steps towards achievement of our goals with development of telecommunication network, service platforms and supporting systems.

In order to ensure high quality Broad Band (BB) performance, BB market and technology leadership, MKT is continuously investing in fix and mobile access development. At the end of 2018, more than 172,500 homes passed installed capacity or 30,5% MKT network households' coverage with FTTH was reached. Regarding VDSL rollout, total numbers of VDSL CO was more than 154k and more than 13k VDSL FTTC homes passed.

Hybrid Access Solution was further developed which aggregates the bandwidth of both DSL and LTE transmission links and create a single, powerful broadband pipe between the network service node and customer's Broadband CPE. At the end of 2018, there were more than 4,8K users and more than 2,8K FMS users.

Significant improvement was also done in LTE rollout, reaching 92% territory coverage and 99,67% population coverage outdoor. More than 95% of total sites provide LTE services. At the end of 2018, 62% of BTSs were connected via optic.

Alongside extensive mobile BB access rollout, during 2018, high focus was set on the network quality and performance, which is confirmed by P3 "Best in Test" certificate in November 2018 which represents an internationally recognized acknowledgement for quality of mobile network, as well as by the National Report for Network Quality Parameters prepared by the Agency. Makedonski Telekom is the best in class for voice and data services and leads the overall ranking with 907 points.

During 2018, the emphasis was placed on fix voice network modernization. The scope of the project included HW/SW upgrade of IMS network nodes, OSS migration and consolidation, MMDec HW/SW upgrade, as well as LI HW/SW upgrade. Project for Consolidation of subscriber databases finished with migration of fixed customers at the end of November 2018. It was in a way to unify the existing monolithic 2G/3G and LTE UDM mobile networks with the existing monolithic UDM for IMS fixed network. It provides consolidation of user data for all network functions like user authentication, service authorization, mobility management and fraud protection on a single SDM system, thus enabling convergence of CS, PS, EPC, WLAN, M2M and IMS user profile services.

MKT continuously follow the newest technology trends in the world thus providing their customers with the latest innovative services which constantly keep them as leading operators on the market in Macedonia and wider as part of DT Group. In that line, start of VoLTE project in MKT was announced at the end of 2018. It is one of the more important projects planned for 2019 with commercial start planned for the end of 2019. The introduction of VoLTE will guarantee for long-term competitiveness of mobile services in Makedonski Telekom by securing leading position on Macedonian market, at the same time following DT PAN NET strategy and fulfilling the given directions and requirements.

Technical implementation of Mobile Virtual Network Operator was finished with internal resources and Managed Services help at the end of 2018. Planned commercial launch is at the beginning of 2019. Modernization of voice network will continue in direction of MSS HW and SW modernization for MKT mobile users. The 2019 project is driven by the HW/SW EoS (End of Support) dates and they will cover both MSS sites, Skopje and Veles and it is aimed for MSS SW/HW upgrade to SW version 18B and replacement of existing MGWs with new MRS network elements.

The growth of BB access and continuous traffic increase are supported with further development of IP Core and transport network as cornerstone of all services. During the last two years, IP Core & Transport Network Modernization project which includes modernization, reorganization and extension of all IP Core Network elements, Transport and Aggregation systems was successfully completed. MKT managed to install full DWDM network and finalized IP Core implementation and integration, as well as IP Core services migration. Plans are to continue with HA Aggregation Network modernization and to finish 100% of the Aggregation sites and to continue with activities for modernization of SPNI & BRAS segment of the network.

Video and high-speed data services are expected to be the main driver and main potential for further market differentiation as well as main opportunity for business growth. In order to improve the quality of IPTV service and to achieve the ambition for number 1 TV provider on the Macedonian market, it is very important to follow the new technologies and new market trends. In that line, expectation from the platform besides ensuring high quality of the existing services is new functionality that should increase interactivity and service personalization for the customers. Implementation of the new IPTV client was completed at Q2 2018. It provides introducing new marketing demands and features on new DT harmonized design of IPTV client user interface. Replacement of solution for IPTV Network Time Protocol Infrastructure was performed as well. Following the Corporate Strategy and the EU IT strategy in the DT group, MKT IT has developed IT Strategy and Business Plan that is focusing on:

1. Supporting new products development
2. Digitalization
3. Future proof and transformation
4. Cloudification.

There are several projects that are aimed to provide efficient IT systems and solutions which will fulfill the plan and realization of strategic focuses. In order to support new products development, functional improvements of several systems like CRM system, Billing, OSS, as well as SAP system were done during 2018.

Charging System Upgrade project to version CS18 was successfully finished at the end of 2018. SugarCRM Mobile Consolidation project, as well as SugarCRM Sales Force Automation project are ongoing and planed go live is Q1 2019. Change Request in CRM for improved automated provisioning of Hybrid technology and 4G devices, as well as for Complains handling improvements went live in December 2018. Version upgrade of BPMS system- (Appian) was successfully done as well.

The One App project started in Q3 2018 with first delivery planned Q1 2019. Implementation of this project will provide usage of new generation of Telekom MK self-servicing application that enables MKT customers to easy and online manage their telecommunication services. MKT customers using OneApp will have improved online access to all their mobile and fix telecommunication services, be able to online manage their services, view and pay their bills, top-up voucher, activate add-on services, chat to MKT Customer Service, view history of their spending, get access to MKT shop map, access to MKT HGW, use SDK modules such as VITO, push notification, analytics, and many more. The application presents central online communications channel for the entire business that will be available to both residential (PostPaid and PrePaid) and business segments.

In terms of IT infrastructure solutions, during 2018, SAN Infrastructure Renovation Project and Project for Corporate Network Renovation were completed according plan.

6 REAL ESTATE, SITES OF OPERATION

We have one of the largest real estate holdings in Hungary and we are also a major real estate owner in Macedonia. We use substantially all of these properties for telecommunications installations, offices, warehouses, garages and shops. Our equipment and machinery primarily consist of switches, communication towers and other telecommunications equipment. In order to increase the utilization of real estates and increase efficiency, we make efforts to sell our surplus properties.

Headquarters of major member companies of the Group

- Magyar Telekom Plc.: Hungary, 1097 Budapest, Könyves Kálmán körút 36.
- T-Systems Magyarország Zrt.: Hungary, 1097 Budapest, Könyves Kálmán körút 36.
- Makedonski Telekom A.D.: Macedonia, 1000 Skopje, Kej 13 Noemvri, No. 6.
- Combridge S.R.L.: Romania, Municipiul Sfantu-Gheorghe, Strada 1 DECEMBRIE 1918, parter comercial, nr. VI, Bloc 6, Judet Covasna
- Novatel EOOD: Bulgaria, Sofia Oblast, Stolichna Municipality, Sofia 1404, Triaditza District, 45A Bulgária Blvd.

Hungary

Out of the number of 1,702 buildings that take place on the 1,490 sites of Magyar Telekom Plc, 48% is owned by the company, 5 % is jointly owned and the rest 47% is leased. These figures do not contain the technology sites, from these types of sites we have 6,128.

The total area of properties used by Magyar Telekom Plc. as of December 31, 2018 was 669,081 m^2. The majority of sites used in our operations are smaller than 100 m^2. The largest site is our headquarters building (leased) located at Könyves Kálmán krt. 36 in Budapest, with floor space of over 55,000 m^2

Macedonia

At the end of December 2018, MKT radio access network consisted of 810 physical sites on which there are 694 2G base stations, 798 3G base stations and 771 4G base stations. 91% of the site infrastructure (towers) is in possession of MKT and 9% is leased.

The total area that is used by MKT is around 109,490 m2 as of December 2018, out of which around 44, 981 m2 are in sole possession of MKT and in great part (55 %) is attributable to 2 major buildings, the headquarters and the main technical building. The remaining 64,509 m2 are in joint possession with Macedonian Post.

7 SUSTAINABILITY

Magyar Telekom has been addressing the sustainability implications of its operations for close to twenty years, and in 2000, it was one of the first Hungarian companies to establish a sustainability unit that managed environmental issues in the beginning and coordinates sustainability processes now. Its sustainability activities are characterized by comprehensive, long-term plans, and the Company is currently implementing its fourth five-year sustainability strategy.

Being a leading ICT provider of the region, we set an example and provide opportunities by our forward-looking thinking, innovative, sustainable products and services and responsible conduct, we contribute to the establishment of a renewable society and environment.

Magyar Telekom committed to support the ten principles set forth by the UN Global Compact since 2009 in the areas of human rights, environment and anti-corruption, the results of which are also addressed by our Sustainability Reports.

Magyar Telekom's sustainability activities and achievements are comprehensively discussed in the annual Sustainability Reports, which aims to make the Group's environmental, social and economic activities transparent to everyone.

The present report includes reference only to certain key topics of our sustainability approach, namely human rights, employees, environment protection and compliance.

Charters and initiatives of cooperation accepted and signed by Magyar Telekom Group

Besides professional challenges, the Group also seeks cooperation opportunities for the solution of social and environmental problems.

The Group has been an active member of ETNO's (European Telecommunications Network Operators Association) Sustainability Workgroup for years. The members work closely towards solving all kinds of sustainability-related programs. In addition to the three meetings held each year, an internet portal also helps our joint work and contributes to the sharing of best practices.

In respect of the hello holnap! fee package we held various forums with the involved organizations of people living with disabilities (AOSZ, ÉFOÉSZ, MEOSZ, MVGYOSZ). Our cooperation with these bodies is continuous, active and based on the proposals we continuously improve our relationship with disabled people and develop our relevant services. The latest version of the fee package that provides several services at the cheap price for disabled people. Thus one living with disability customer can have all together three subscriptions on their own name.

We supported the work of the Environment Protection Committee of the Hungarian Academy of Sciences. Our colleagues are in close relationship with several higher education institutes and we help the universities with consultancy for writing theses, expert education and giving lectures.

OECD-Guidelines – Magyar Telekom has been the first among the Hungarian companies to accept OECD Guidelines for Multinational Enterprises and set them up as mandatory guidelines for its operations.
European Union's Diversity Charter – has been signed by the company and considered as a mandatory guideline inherent in the corporate Human strategy.
UN Global Compact has been signed by the company and the current report also stands to report our achievements in the 10 principles.
UN Sustainable Development Goals – Magyar Telekom has acknowledged the SDG and through incorporating them as guidelines in its Sustainability strategy 2016-2020 the company finds the contribution to the goals a mandatory element of its operations.
Carbon Disclosure Project (CDP) – Magyar Telekom has signed the global initiative and fulfills its annual reporting obligations
The Group is a member of several working groups of the Hungarian Business Leaders Forum (HBLF).

https://www.telekom.hu/about_us/society_and_environment/cooperation

Quality guarantees in the Magyar Telekom Group can be found:

https://www.telekom.hu/about_us/about_magyar_telekom/principles/quality_guarantees

7.1 Sustainability strategy

In 2016, Magyar Telekom Group started its new five-year sustainability strategic cycle, 2016-2020.

In addition to the results of our Sustainability Strategy 2011-2015, the goals and tasks defined for the period through the end of 2020 have been determined by the goals and directions applied internationally in terms of sustainable development (SDG, CDP, GeSI SMARTer2030, EU2020 climate package), which we, as a Group, adhere to. When identifying our priorities, we have focused on the expectations of the responsible investors monitoring our company and the current corporate trends. Of course, local market conditions, as well as consumer behavior and demand have also been taken into account, so that we be able to proactively meet our customers' needs.

When identifying our strategic goals, we kept in mind that our sustainable operation has a significant impact on the society, the economy and the environment. In addition to being responsible for the livable future of our several million customers and nearly 10 000 employees, as a market leader ICT provider and a large enterprise of regional proportions, we are aware that our business and operational decisions influence the economy and the society of the future, too. It is our firm belief that we, as a company, are responsible for all the groups of people whom we can enable by ICT solutions, and that we have to make social, economic and environmental responsibility a part of our corporate genetic code to thus promote sustainable development and opportunities for future generations.

The main objective set forth by the fouth Sustainability strategy strategy covering the period through the end of 2020 is to make sustainability part of Magyar Telekom's business. This can be ensured, if considering all three pillars of sustainability, we are comprehensive, credible and innovative.

Until 2020, climate protection, education and awareness, and digitally enabled sustainability are the major foci of the strategy.

Climate protection

Our goal is to make our customers climate-conscious, too, and to be an authentic and responsible company that helps them along that journey. It is our ambitious objective to generate revenue from our climate protection activities, as the ICT world offers especially great potential for that, at the same time to push Magyar Telekom Group's actual CO_2 emission below 100,000 tons. In order to achieve the above, in addition to the emission decreasing initiatives, we also need to work on elaborating "green" services specifically.

KPI: push Magyar Telekom Group's actual CO_2 emission below 100,000 tons

KPI: generate revenue from climate protection

Education

We want to assume a role in educating the public and our customers. Our goal is to directly or indirectly reach 100,000 people in Hungary with our trainings by the end of the period covered by the strategy. We shall primarily focus these trainings on two areas: programs aimed at eliminating the digital gap and the succession pool of the industry.

KPI: 1 000,000 digitally educated people in Hungary

Digitally enabled sustainability

Being a sustainable digital company, it is our clear expectation that our customers should also use sustainable digital services. To that end, we strive to pursue responsible marketing and activities that enable and inspire others, as well as are based on sharing. In this context, our goal is that awareness about Magyar Telekom, as a sustainable company should reach 50%.

KPI: awareness about Magyar Telekom, as a sustainable company should reach 50%

Awards and recognitions achieved in 2018:

- Oekom – B Prime category, rank number 1 in Telecommunication sector
- FTSE4Good Index membership
- CEERIUS sustainability index membership
- MSCI ESG rating AA
- Most Appealing Workplace Award

7.2 Initiatives concerning stakeholders

In order to successfully operate the company it is essential to have strong relations with stakeholders.
Below you will find a list of our key activities with our stakeholders the details of which are elaborated in the respective chapters of the Sustainability Report:

- Investors – Investor (and responsible investor) assessment
- Customers – Sustainable products and services, hello holnap! mobile app
- Employees – community solar pilot, diversity culture survey, hello holnap! points
- Regulators – conformity, regulatory relations
- Local communities –Telekom Voluntary Day, Autistic Art Strategic Partnership (donations, voluntary, tablets, awareness videos), Telekom Community Gardens
- Non-profit organizations – Sustainability Roundtable Discussion, 11th Sustainability Day
- Suppliers – sustainable supplier chain, TOP3 sustainable supplier of Magyar Telekom
- Media – Sustainability Media Club, Press Award on the Sustainability Day
- Future generations – Become an IT expert! sustainable innovation, sustainable innovations

For the year of 2018 we started the community solar program pilot. Most of the electricity consumption of the educational building in Kékvirág street is given by solar panels located on the roof of the building. During the program employees had the opportunity to adopt a solar panel and get extra benefit in exchange. 113 solar panels had been adopted in 2 workdays.

In 2018, we organized the Sustainability Roundtable Discussion for the 19th time, the objective of which is to have an open dialogue with our stakeholders for the sake of understanding the demands towards Magyar Telekom Group, discussing the arising problems, and to provide a suitable background for thinking together and co-operating in building a sustainable future.

In 2008, our Company founded the DELFIN (the word for dolphin in Hungarian) award, which in Hungarian stands for “Award for a Committed, Sustainable, and Innovative Generation”. With the DELFIN award Magyar Telekom wants to promote the idea of a sustainable development and recognize efforts made towards this goal. The award is given to suppliers offering outstanding performance in the field of sustainability, in four categories:

- Sustainable innovation;
- Diversity;
- Climate protection;
- Raising sustainability awareness.

A jury of experts decides which submitted project should receive the award. The eleventh award ceremony took place on June 15, 2018, as part of the Sustainability Roundtable. In 2018, we recognized organizations and businesses promoting climate protection and awareness raising.

The 11th Sustainability Day event took place on September 29, 2018. The topic of the day was liveliness. More than six thousand visitors attended the event where they participated in panel discussions on the three pillars of sustainability and examined pieces of works submitted to the creative design exhibition as well as exhibitors.

The event presented an opportunity to hand over the Sustainability Media Award for the eighth time by the members of the Sustainability Media Club - established by Magyar Telekom. Awards were distributed in three categories: tv/radio/video content, written newspaper (print, online); blog, vlog. The award amounted to HUF 300 000 for each category.

In 2018, we continued to sensitize our employees to social issues by organizing volunteer work events. The strategic target of the corporate volunteering is 50,000 hours of voluntary work by Magyar Telekom employees. To achieve that they had the possibility to grow the amount of the theoretical contribution to society by educational (eg. Be an IT expert!,) and charity (eg. It is good to give! cookie campaign) voluntary events and the Telekom Voluntary Day. The philanthropic voluntary programs are very popular among our employees eg. the seasonal blood donation or helping in caring homes operated by associations for youth living with disabilities. During the year 1059 colleagues worked 11,991 hours of volunteer work, by means of which a theoretical amount of HUF 42.1 million was thus donated to the society.

In 2018, the "hello holnap!" employee point collection was transformed. In the fifth year of the initiative (between 1 April 2017 and 31 March 2018). The first three employees who collected the most points and the TOP1 employee who collected the most points in the five-year period were given a Feldobox voucher. Near than 30,000 points were collected by 11,000 colleagues between 2013 and 2018. After that employees collect points in "hello holnap!" mobile application.

The children's protection website of Magyar Telekom dedicated to threats caused by children's media consumption. The website provides information to parents not only about ICT technologies, devices and content, but also about threats caused by their usage and consumption, as well as possible preventive measures. More details are available on:

http://www.telekom.hu/about_us/society_and_environment/society/protection_of_our_children.

We launched the "hello holnap!" mobile app on September 27, 2014, by which we drew attention to Telekom's sustainability efforts in particular and sustainable lifestyles in general. By using the app, users can collect "hello holnap!" points and donate them, converted into real money by Telekom, to non-governmental organizations of their choice. The success of the mobile application in 2018 is best represented by the fact that it has more than 17,000 downloads and HUF M 2.4 have been donated to the organizations connected to the application.

One pillar of atypical staffing is telework, which is one of the most important sustainability aspects of the Future Work project. Working from home in the framework of the project launched in July 2014 enabled the Company's employees to save time and mileage. Thus, drivers can relieve the environment of as much as 4 million kilometers and twenty years of travel in 2018.

7.3 Annual Sustainability Report

Magyar Telekom Group has committed, among other things, to publish reports about its sustainability performance annually. When the reports are compiled the GRI (Global Reporting Initiative) guidelines are applied, thus ensuring compliance with the principle that the reports have to be the cornerstones ensuring transparency and international comparability. Since 2007 Magyar Telekom has prepared reports adhering to the highest level of compliance with international standards each year, thus the 2013 Sustainability Report was the seventh to meet the requirements of the GRI A+ application level.

The 2014 and 2015 Sustainability Report was compiled along the Fourth-Generation Principles set forth by the Global Reporting Initiative (GRI G4), while the 2016 and 2017 Sustainability report was compiled along the newest requirement, the GRI Standard It was applied on comprehensive level and includes more information about the Group's sustainability performance. The independent assurance and certification of compliance with the GRI Standard criteria was conducted by PricewaterhouseCoopers along the ISAE 3000 international standard. Further details on the sustainability performance of the Company can be found in the annual reports available on:

https://www.telekom.hu/about_us/society_and_environment/sustainability_reports

The 2018 Sustainability Report is going to be published in 2019 spring.

8 ENVIRONMENT PROTECTION

8.1 Policies

Magyar Telekom Group upholds its commitment to sustainable development and the environment protection in the environmental policy. The policy contains obligations for the members of the Magyar Telekom Group both individually and as a Group: https://www.telekom.hu/static-tr/sw/file/Magyar_Telekom_environmental_policy.pdf

The Group-level coordination is continued to be implemented under the auspices of the Group Sustainability Coordination Council (GSCC). The levels of development and management of the corporate sustainability strategy are separated from the operative implementation level within the operation of the GSCC, thus the process of implementing sustainability activities is divided to the following levels:

1. Strategy development and strategy management level operating under the auspices of the GSCC: development of strategic concepts, implementation of the strategy, relevant communication with national and international organizations

2. Operative implementation level managed by relevant organisations of the governance areas and business units, actual operative activities, task management, data provision etc.

The GSCC's operation is regulated by a group level directive: on the regulation of Magyar Telekom Group's sustainability operation and the responsibilities and competence of stakeholders.

The operative management of Magyar Telekom Group, the Management Committee receives at least once a year a report on the implementation of the tasks of the Group Sustainability Strategy and other ongoing significant sustainability activities, results, potential exposures and opportunities.

The MC is informed on the latest sustainability trends and may respond to the feedback from stakeholders through the annual report and based on the report may decide on the amendment of the strategy. The MC keeps contact with the stakeholders through the GSCC. Incoming inquiries are received by the respective professional areas and critical comments regarding sustainability are transferred to the responsible staff members by the GSCC members. According to the relevant group directive the strategic tasks are allocated to the respective Chief Officers.

8.2 Results of the policies

As a leading provider of info-communications services in the region, Magyar Telekom's commitment to sustainable development with a focus on preserving the environment lies in the centre of its mission. In our new Sustainability Strategy 2016-2020 we set the ambitious goal to reduce the level of our carbon dioxide emission below 100 000 tons.

In 2018 we continued our carbon offset project. We spent half of the income of our company car policy regulated bonus-malus system to carbon offset. Our aim was to become carbon neutral again in 2018 too. We have reached our goal by using 100% renewable energy for our electricity and we offset the rest of our emissions, by purchasing and retiring 30,000 CER (Certified Emission Reduction) units. The reduction came from a Chinese project. In 2018 Magyar Telekom Plc. has purchased 180 GWh of renewable energy that is equal with 100% of the total amount of electricity used by the Company.

Our highlighted environmental and operational ecoefficiency goals are:

- Reducing our CO2 emissions (target set below 100 000 tons of CO2 by 2020)
- Energy consumption: saving energy (reduce consumption), increase of energy efficiency levels, using green energy
- Increase the energy efficiency of our buildings
- Decrease our fleet consumption, promotion travel replacement solutions, and dematerialization solutions
- Introduction of sustainable and climate friendly products and services
- Waste management: reduction of waste (increased recycling-rate)
- Measure the climate footprint of our customers and suppliers

8.3 Risks

Based on the Business Continuity Management System (BCM) we have identified the critical climate risks (floods, heat waves) that might affect our operations and we have prepared action plans for possible risk management. According to our annual assessment the rate of climate damage in the network did not reach the level of intervention (HUF 50 million damage/ month). In 2018 we have identified 228 climate related cases (storm damage) with the costs of 23.3 million HUF. During heatwaves we allow our colleagues to work remotely in order to reduce the energy consumption of our offices, and we increase the core temperature of our datacenters and base stations.

8.4 Performance indicators

Cumulated CO_2 emission – 96,842 tons CO_2

Group CO_2 emission by categories – Scope1: 21,783 tons CO_2, Scope2: 75,059 tons CO_2

Energy efficiency – bits transmitted / energy consumption – 115.47 Gbit/kWh

The average CO2 emission of the fleet – 114.9 g/km CO2

9 CORPORATE COMPLIANCE

When shaping the compliance program of the Magyar Telekom Group, the goal was to ensure that the Magyar Telekom Group pursues its business activity with maximum awareness of and commitment to the compliance with the applicable laws and legal provisions, in accordance with the strictest norms of ethical business conduct. To this end, we issued decrees addressing the potentially arising compliance-related risks, and we apply the procedures set out in these decrees and arrange continuous training courses for our employees related to these procedures. We established clear concise processes to report, examine, follow up and correct suspected cases of non-compliance.

The Corporate compliance program is supervised by the Group compliance officer. The Group compliance officer reports directly to the Audit Committee, and cooperates with the Board of Directors, the Supervisory Board and the management. The Corporate compliance program focuses on the Code of Conduct.

Code of Conduct of the Magyar Telekom Group contains the summary of the compliance requirement within the company, sets common values of the Group and is a key to the strong position, reputation and successful future of Telekom. The Code of Conduct applies to everyone within the Magyar Telekom Group from the employees to the members of the Board. In addition, contracted partners of the Magyar Telekom Group also have to know and accept these values, when registering to the procurement website.

In the year 2010 an external independent party audited the implementation of the Compliance program, and we were awarded a certificate of compliance with the external expectations and of the implementation of the system. The program was revised in 2013, including other related areas as well – such as procurement, internal audit, HR, sales. The audit was not aimed only at the implementation and control of the system in the different areas, but it measured the operational efficiency of the control system. We met the expectations and were awarded by a certificate issued by Ernst&Young as independent external party. In 2017 again an external auditor (KPMG) evaluated the effectiveness of the compliance management system of Magyar Telekom, and issued a certification that the program complies with the requirements of the new anti-corruption ISO standard.

The first distance learning course addressing compliance was started in 2008 in the topic of “Conscious recognition of fraud and corruption”. Since then we have been providing a general eLearning course for our new employees, mandatory for all colleagues joining to the company. The course is completed with the acceptance of the Code of Conduct. Since the start of the program, 67 955 distance learning courses were completed by the employees on group level, related to topics, such as compliance awareness, supplier due diligence, anti-corruption measures, incompatibility or insider trading.

On the top of that, our company has arranged personal training sessions for employees working in professional areas exposed to compliance and abuse related risks – both within the parent company and Hungarian and international subsidiaries – in the topics of organized anti-corruption behavior, screening of contracted partners and rules of giving and accepting gifts.

In 2018 – similarly to the practice of the previous years – risk analyses were conducted with the participation of organizations and subsidiaries of Magyar Telekom Nyrt. Based on the results of the survey, a comprehensive audit was prepared for the potential compliance and abuse risks, the result of which was submitted to the Audit Committee of the Company.

During the year we check the soundness of the reports submitted to our company in connection with unethical behavior, and if necessary, we act on these reports. In case we identify actual abuses, we take care of the necessary and adequate countermeasures. Magyar Telekom published all cases of corruption and the related countermeasures in accordance with the related applicable laws and legal provisions.

9.1 Fight against bribery and corruption

9.1.1 Policies

Magyar Telekom des not tolerate any attempts of corruption, so numerous procedures and policies were introduced to prevent and fight corruption. Magyar Telekom complies with the anti-corruption rules the Group, and expects its business partners not engage in unlawful activities (including breaching the anti-corruption laws) such as utilize any money or other services provided by Magyar Telekom for unlawful purposes. This also includes direct or indirect payments to individual(s) to improve the perception of Magyar Telekom (or any parties acting for Magyar Telekom) or to influence any business decision. Magyar Telekom strictly prohibits any form of corruption including (but not only), receiving personal advantages or monetary gains, accepting or providing bribes or promising facilitating payments. The Group also prohibits employees to make beneficial decisions towards family, friends or close or distant acquaintances. It is not allowed to provide any gift or invitation to an event to third parties if it could potentially influence any business transaction. Magyar Telekom Group does not support morally or financially any political parties, organizations or representatives of these. Magyar Telekom will not start business relations with third parties that violate the anti-corruption clauses of the Compliance Program or the basic principles of the Code of Conduct.

Due Diligence procedures: There are no fixed procedures on how thorough due diligence should be to avoid legal responsibility or any investigation as per the anti-corruption laws. The aim of these procedures is to identify high-risk areas, and to provide indication when further due diligence or review is required.

9.1.2 Result of the policies

During the year, we have verified the plausibility of any complaints we have received about unethical behaviour and initiated internal investigations if necessary. If we have identified any misconduct we initiated the necessary measures and actions. Any complaints regarding breaches of internal or external rules can be sent to the Tell Me! portal of Magyar Telekom. Any questions regarding corporate compliance can be asked on the Ask Me! intranet portal.

9.1.3 Risk

The basis and prerequisite of the efficient defense against breaches of laws and policies is the register and analysis of compliance risks and identified other compliance relevant cases at Magyar Telekom. The yearly Compliance Risk Assessment (CRA) handles active and passive corruption separately. The risk assessment always includes Magyar Telekom, T-Systems and Makedonski Telekom. Other subsidiaries can be included on a case-by-case basis, based on information originating from internal investigations. The CRA fully covers the abovementioned companies. The Group Compliance Officer informs the Audit Committee, the Board of Directors, and the management about the result of the risk assessment and gives an update about the status of the measures in every quarter.

10 ECONOMIC ENVIRONMENTS

The telecommunications industry is undergoing a major change globally. Worldwide trends are driving towards an integrated telecommunications, information, media and entertainment market. The increasing need for mobility and interactivity together with local specifics create a new set-up in our economic environment in terms of infrastructure, servicing and new types of business models.

Hungary

Traditional telco markets are shrinking on midterm. Market for voice services (both mobile and fixed) is saturated and voice services becoming a utility wth flat tariffs and simple offers. There is an increasing demand for data services driven by content consumption but strong competition puts pressure on prices. The centre of offering is data service both on fixed and mobile focusing on speed in fixed and unlimited on mobile. The fixed market is characterized by fixed-mobile integrated bundles, with broadband becoming a core element of service offerings. After finalization of Vodafone – UPC merge we still expect Digi – still struggling to launch its own mobile service - to enter the market as a third FMC operator.

Mobile market is characterised by great quality and coverage from network perspective. The mobile broadband uptake still fuels the overall mobile market. However, the increasing regulation, in particular the abolishment of roaming fees and the decrease in mobile termination rates, is putting further pressure on market players. 2019 is the year of introduction for 5G networks as well. 5G networks is no longer the network with residential segment focus, but rather the industrial usage.

The growing economic environment had a positive effect on the households' budget in recent years. The growing budgets however are hard to translate into growing telco spending.

Macedonia

Positive impact to overall economy expected, upon initiation of accession talks with the EU in June 2019 and NATO full membership by mid-2020 (After changing the country's constitutional name to North Macedonia, thus fulfilling its part of the mutual agreement with Greece to unlock Macedonia's NATO and EU integration).

Based on the above, main economy drivers expected to rebound, resulting telco market stabilization and return to growth.

Telekom with very good financial performance YoY, showing growth of +2,1% on revenues and +4,5% EBITDA excl. SI. achieving positive turnaround in revenue development in 2018.

Integrated telco market overview shows stable position of Telekom with 55,0% Q3'18 revenue market share, VIP with 37,7% Q3'18 and 7,3% Q3'18 to other operators.

Mobile market is still remaining limited to current (2) players, although an open door is still kept further for new entrant (after several announcements by the regulator on expressed interests by 3rd parties). Lycamobile, currently single mobile MVNO in the country with insignificant revenue share and focused only on prepaid segment. New MVNO entrant announced with start of operations at beginning of 2019. The new entrant, Telekabel (major cable operator), with expected impact on postpaid segment and FMC market.

Fix market, from 2019, with 3 integrated players focused on convergent offers on the Market and other smaller operators. Telekom with further focus on fiber roll-out and providing high speed and high quality internet to its customers.

11 TARGETS AND STRATEGY

11.1 Outlook

The telecommunications industry is undergoing significant changes globally. We have observed several long-term trends which are changing the structure of the telecommunications market. These long-term trends include changes in technology (Digitalization, AR & VR, AI, autonomous driving, IoT), customer requirements (e.g., media consumption everywhere, wearables, eHealth solutions) and competition and regulation (e.g. low entry barriers, new business models, convergence in the telecommunications and media broadcast industry).

Each of our business segments is affected by their own unique business environment, and we are subject to circumstances and events that are unforeseen or are beyond our control. The global economy recovered from the crisis and passed the first shock of Brexit and the uncertainty of Trump's appearance. Our business environment largely depends on the monetary policy of the FED, the growth of the Chinese and European economy and the movements of EU funds. The last 3 years have brought significant prosperity in the world economy and that pulled the Hungarian economy too.

Hungary

The biggest challenges for Magyar Telekom are the intense optical rollout in fixed and the data traffic increase of the mobile market while competition is ready to to challenge Magyar Telekom on the FMC market on midterm . We aim to keep the leading position on our key markets with the continuously growing number of customers with Magenta 1 offers which connect the mobile and fixed services, and with the improvement & utilization of the HSI (high speed internet) network. In addition, the SI/IT market is expected to grow further thanks to the development of digital economy; our intention is to increase our market share through a greater focus on high margin system integration projects. On midterm there is a focus on increasing the income of service based solutions for the business segment.

Macedonia

One of the main challenges on the market is new MVNO entry by Telekabel (Major CaTV operator), becoming new convergent player , besides Makedonski Telekom and VIP (rebranding expected in A1 Telekom Austria's brand in 2019).

Despite new challenges, Makedonski Telekom keeps growth and market share perspectives, confirmed by number 1 position in Technology (by P3 international benchmarking), scoring historic highest result in Macedonia's history, also supported by very high results of TRIM indexes, confirming the strive for number 1 position in superior network and technology, thus having highest customer satisfaction on the market, securing firmly number1 market position in the years to come as well.

With regards to regulatory strategy in alignment with DT EU strategy, Makedonski Telekom is focused at:

- Announced NRA's plan for reduction of roaming and international termination prices between West Balkan countries until 2021
- Introduction of National NGN Broadband Plan

- Latest amendments of Law on audio and audio visual media services, process for testing economical replicability for retail and wholesale NGN products
- Draft Consumer protection law
- Radiofrequencies allocation

11.2 Revenue, EBITDA and Capex targets

Magyar Telekom continued to deliver strong performance in 2018. Our continued commitment to satisfy our customers' needs and constantly refresh our product offering strengthened our position in the market in several key areas including post-paid mobile, TV and fixed broadband.

The strong revenue growth recorded by the Group in the first nine months of 2018 continued into Q4 2018, resulting in a 7.6% revenue rise for the full year. Despite the growth of low margin revenue lines such as equipment sales and SI/IT hardware and software deals we have also managed to grow on EBITDA, thanks to higher gross profit and one-off profit realized by the sale of real estates, leaving us well positioned for the year ahead.

The Hungarian operation continued on the positive trajectory set earlier this year as revenue increased across all three major services lines.

Looking ahead to 2019, we continue our push in the FMC segment leveraging our position of being the only truly integrated service provider in the Hungarian market. We strongly believe that the key to long-term success lies in the ability to offer truly integrated solutions to our customers. In Macedonia, we are confident that, in spite of challenging market conditions, the EBITDA turnaround is sustainable with upsides thanks to a still growing SI/IT business line.

Looking forward we expect revenues to moderately decline in 2019, whilst EBITDA is expected to increase by 1%-2% on a comparable basis thanks to a reduction in indirect costs. Capital expenditures are expected to remain stable (excluding the increase driven by IFRS 16 implementation and any possible spectrum costs) as spending on the fixed network will continue to reflect the acceleration of the fiber-rollout program. Continuing the successful turnaround in profitability, we expect free cash flow (excluding spectrum license fees) to continue increase by around 5%.

Based on the current operating and regulatory environment and outlook, we expect the Company to pay HUF 27 dividend per share in relation to 2019 earnings. This is subject to the Board of Directors' future proposal to the General Meeting which will be submitted in due course, once all necessary information is available and all prerequisites to making such a proposal are met.

Public guidance:

	2018 Actual	Public guidance for 2019[2]
Revenue	HUF 657 billion	slight decline
EBITDA	HUF 193 billion	increasing at 1%-2%
Capex[1]	HUF 92 billion	broadly stable
FCF[1]	HUF 68 billion	increasing at ca 5%
Dividend	HUF 25 per share[3]	HUF 27 per share

[1] *excluding spectrum license fees*
[2] *on a comparable basis*
[3] *subject to approval by the General Meeting*

11.3 Strategy

Hungary

As a result of our focused strategic efforts, Magyar Telekom maintained its leading position in its Hungarian fixed voice, broadband, pay TV, mobile and ICT businesses in 2018, we successfully improved customer retention and delivered strong volume figures. We built a word class 4G mobile network and preparing to roll out 5g while massively improving our fixed line optical coverage in the coming years.

Based on our improved network capabilities we aim to provide services to all segment and customer on voice, TV broadband and IT markets. The strategic objective in the mid-term is to become more agile, enhance efficiency, simplify the product and services portfolio, increase process automation and online customer servicing. As an integrated provider, we continue to deliver a unique customer experience supported by our leading brand and best technology.

While anticipating new competencies required by the changing customer behaviour, technological advances, and new business models, we aim to exploit our abilities to become a leader in all digital services around the home for both customers and third parties.

Following our strategy enables us to exploit and develop our extended customer base, improve efficiency and capture growth opportunities in an extended market of information and communications technology and related industries, which secures stable cash generation in the long run.

Macedonia

Telekom executed successfully the "Mission Turnaround" and achieved turnaround and growth in several segments. With further focus on continuous and sustainable growth and transformation to Telco of Tomorrow, a growth strategy was developed with clear growth areas and transformation initiatives.

Following the DT strategy of transformation to Telco of Tomorrow with full focus on the following initiatives:

- Brand and Customer Engagement – position as Premium and most preferred brand
- Fiber – Further FTTH rollout and clear monetization plan
- Simplification – simple and easy to understand from customers perspective
- New It Model –Critical enabler of Digitization
- Common Operation NT/ IT across – Data Center consolidation and cloudification
- Efficient Central Business Functions – Agile and Digital Transformation

12 INTERNAL CONTROLS, RISKS AND UNCERTAINTIES

12.1 The presentation of the systems of internal controls and the evaluation of the activity in the relevant period

Magyar Telekom's management is committed to establish and maintain an adequate internal control system to ensure the reliability of the financial reports, and minimize operating and compliance risks. Our internal control system is designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in conformity with International Financial Reporting Standards (IFRS) as adopted by the European Union.

For the business year 2018 we accomplished control documentation and evaluation in the IT supported ICS[i] system. Transaction Level Controls describe the controls built into our business processes that have been designed and operated to ensure that material misstatements in each significant financial account and disclosure within the financial statements are prevented or detected in a timely manner.

Complete evaluation of our internal control system is based on the method established in "Internal Control —Integrated Framework" issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). The operation of the internal control system is supported also by the independent internal audit function. Beyond tasks regarding the risk based internal audit work plan, contributes to the enhancement of the internal control processes and to the reduction of existing risks through ad-hoc audits. The Internal Audit area follows up the implementation of the measures defined on the basis of the audits. The Supervisory Board and the Audit Committee receive regular reports on the findings of the audits; measures, based on the findings and fulfilment of tasks.

In line with the criteria of the adopted internal control framework, management evaluates the effectiveness of internal control system within each financial year. Management's assessment for 2018 is finished, and based on the collected information internal control system has been operating effectively to prevent potential material misstatements in the financial statements, and minimize operating

[i] Internal Control System

and compliance risks.

The Company's shareholders are being informed about the operation of our internal control system through our public reports.

The management and Board of Directors of Magyar Telekom are committed to conduct all business activities of Magyar Telekom Group according to the highest legal and ethical standards. Based on this commitment the Board of Directors established the Corporate compliance program of Magyar Telekom.

The Corporate compliance program is applicable to all bodies, organizations, employees of Magyar Telekom Group, and advisors, agents, representatives as well as to all persons and organizations that work on behalf of the Company or its subsidiary.

The Corporate compliance program of Magyar Telekom ensures that the business activities of the Group are conducted with observing and in compliance with the relevant laws to the outmost extent, according to the highest standards of training and commitment. It requires the realization of guidelines and processes that manage potential compliance risks and implement specific processes in order to report, investigate, monitor and correct suspected or actual lack of compliance.

12.2 The utilization of financial instruments, risk management and hedging policies

It is our policy that all disclosures made by us to our security holders and the investment community, are accurate and complete, and fairly present our financial condition and results of operations in all material respects. Such disclosures should be made on a timely basis as required by applicable laws, rules and regulations. To achieve these objectives we developed and have continuously enhanced our risk management policies.

Our risk management includes the identification, assessment and evaluation of risks, the development of necessary action plans, as well as the monitoring of performance and results. For the risk management to be effective, we must ensure that the management takes business decisions with full understanding of all relevant risks.

In 1999, we established a formal risk management system. This system has been operating in an integrated way with the risk management system of Deutsche Telekom since 2002.

All risks related to material internal and external operations, financial and legal compliance and certain other risks are evaluated and managed by a well-defined internal mechanism. A risk management handbook and an internal regulation on risk management were issued. A risk management course was developed for employees responsible for risk management in all organizational areas. Risk items affecting our operations are reviewed quarterly throughout the Company. All of our subsidiaries, business units, divisions and entities are obliged to identify and report their operational risks on a quarterly basis. After the evaluation of these risks, results are reported to our management, to the Board of Directors and to the Audit Committee.

For the sake of prompt disclosure of all risk items influencing investors' decisions, we enhanced our risk management procedures by adding a new element. We complemented our quarterly risk reporting system with a continuous reporting procedure which requires all of our departments and subsidiaries to report on a real-time basis any new material fact, information or risk that comes to their knowledge. Information thus submitted is monitored and evaluated by the risk management area and the CFO is notified when a new material risk or information is identified.

An internal regulation has been issued to define responsibilities of each employee in risk monitoring and management.

12.3 Risk factors

Our financial condition, results of operations or the trading prices of our shares could be materially adversely affected by any of the risks described below. These risks are not the only risks we face. Additional risks not currently known to us, or risks that we currently regard as immaterial, could also have a material adverse effect on our financial condition, results of operations or the trading prices of our shares.

- Our operations are subject to substantial government regulations, further restrictions related to consumer protection were published; the change of the price setting methodology of already regulated wholesale products and new type of regulated access services are probable, which can result in adverse consequences for our business and results of operations;
- Net neutrality regulation has no defined framework in Hungary yet. Case-by-case decisions of the Regulatory Authority may hinder innovation;
- We are subject to more intense competition in the fixed business due to meeting our competitors on more and more area as a result of the network roll-outs;

- Hungarian telecommunication market realignes, so we may be subject of more intense competition in the mobile and fixed business (Digi-Invitel acquisition, Vodafone-UPC acquisition, ownership change of Telenor);
- Beyond current market players in Hungary, DIGI also acquired 2x5 MHz spectrum block in the 1800 MHz band and 1x20 MHz spectrum block in the 3400-3600 MHz band, and will most probably enter the mobile market as a new player ;
- We may be unable to adapt to new trends and technological changes in the telecommunications market (IoT, Big Data, AI, 5G);
- The future of our current operational model is subject to currently unforeseeable changes in the future business environment;
- Developments in the technology and telecommunications sectors may result in impairment of the carrying value of certain of our assets;
- Our business may be adversely affected by actual or perceived health risks associated with mobile communications technologies;
- System failures could result in reduced user traffic and revenue and could harm our reputation;
- Loss of key personnel could weaken our business;
- The regulatory environment in Macedonia is expected to remain strict, since the Regulatory Body's aim is at widening the scope of wholesale regulation (bitstream and cost based pricing);
- More intense competition in Macedonia driven by VIP being an integrated player as well, furthermore MVNOs may also enter the market;
- Our share price may be volatile, and the ability to sell our shares may be adversely affected due to the relatively illiquid market for our shares and ADSs;
- The value of our investments, results of operations and financial condition could be adversely affected by economic developments in Hungary and other countries;
- Unpredictable changes in the Hungarian tax regulations may have an adverse effect on our results;
- Fluctuations in the currency exchange rate could have an adverse effect on our results of operations;
- Disputes and litigation with regulators, competitors and other parties could have an adverse effect on our results of operations.
- The number of cyber attacks have been evolving at an exponential rate recently worldwide. Although Magyar Telekom provides services with highest security-standards and constantly tests and updates its cyber security countermeasures, it cannot be fully excluded that the Company will be subject of a cyber attack.

12.4 Financial risk management

The classification of the group's financial instruments is described in detail in Note 4 and the financial risk management of the Group is described in detail in Note 5 of the Consolidated Financial Statements.

13 ANALYSIS OF FINANCIAL RESULTS FOR 2018

Key Performance Indicators (continuing operatios)	At December 31, 2017	2018
Revenue (HUF million)	610,851	657,104
Mobile revenues	322,656	343,145
Fixed line revenues	196,108	206,901
System Integration/Information Technology revenues	87,485	107,058
Energy service revenues	4,602	
EBITDA (HUF million)	185,662	192,507
EBITDA margin	30.4%	29.3%
Operating margin	12.7%	11.7%
Capex to sales ratio	14.1%	16.4%
Net debt (HUF million)	309,641	272,805
Net debt ratio (net debt to total capital)	34.8%	30.7%

13.1 Revenues

Total revenues increased from HUF 610.9 billion in 2017 to HUF 657.1 billion in 2018 (HUF 655.1 billion excluding the impact of IFRS

15 adoption), driven primarily by the significant growth in SI/IT, equipment and mobile data revenues. Both the Hungarian and Macedonian operations recorded revenue growth in the period.

Mobile revenues increased to HUF 343.1 billion in 2018, compared to HUF 322.7 billion in 2017, thanks to the continued dynamic increase in mobile data revenues and strong demand for smart devices in both countries of operation.

- **Voice retail** revenues declined 5.4% to HUF 133.5 billion in 2018, reflecting the adoption of IFRS 15. Excluding its impact, voice retail revenues rose by 1.1% driven by a higher post-paid ratio in both Hungary and Macedonia which counterbalanced tariff pressure across both operations.
- **Voice wholesale** revenues declined by 1.4% to HUF 9.8 billion in 2018 as a slight increase in Hungary was offset by a fall recorded in Macedonia. In Hungary, higher voice wholesale revenues reflected increased traffic driven by a growing portion of flat rate packages. In Macedonia, the decline was due to a further decrease in international incoming traffic.
- **Data** revenues grew by 9.3% to HUF 80.9 billion in 2018 or HUF 85.2 billion excluding the impact of IFRS 15 adoption. This trend was driven by continued growth in subscriber numbers and data usage in both countries.
- **SMS** revenues increased by 11.1% to HUF 19.2 billion in 2018 primarily as a result of further growth in mass messaging revenues in Hungary and a marginal improvement in Macedonia driven by higher SMS usage thanks to the success of promotional offers.
- **Mobile equipment** revenues increased by 36.2% to HUF 87.4 billion in 2018, or 13.5% to HUF 72.8 billion excluding the impact of IFRS 15 adoption driven primarily by higher average handset prices in both Hungary and Macedonia.

Fixed line revenues increased to HUF 206.9 billion in 2018, up from HUF 196.1 billion in the previous year. The continued decline in voice revenues was fully offset by improvements in TV, broadband and equipment revenues.

- **Voice retail** revenues decreased by 7.1% to HUF 42.7 billion in 2018, primarily due to a further reduction in average tariff levels in both countries, combined with the impact of lower customer base in Hungary.
- **Broadband retail** revenues increased by 4.3% to HUF 51.4 billion in 2018 (up 6.5% to HUF 52.6 billion excluding the impact of the IFRS 15 adoption) thanks to growth in both Hungary and Macedonia. In Hungary, customer base expansion was coupled with some increase in the broadband ARPU level; whereas in Macedonia, customer number increase offset the decline in the broadband ARPU.
- **TV** revenues increased by 4.2% to HUF 47.1 billion in 2018 (up 6.0% to HUF 47.9 billion excluding the impact of the IFRS 15 adoption), thanks to higher revenues in both Hungary and Macedonia. In Hungary the dynamic growth of the customer base and stable ARPUs, whereas in Macedonia the positive impact of the enlarged customer base was amplified by higher ARPU levels.
- **Fixed equipment** revenues rose in both countries, from HUF 9.3 billion in 2017 to HUF 18.1 billion in 2018 (HUF 15.0 billion excluding the impact of IFRS 15 adoption). The significant increase was largely attributable to a strong performance in Hungary, where sales of smart devices to retail customers rose substantially.
- **Data retail** revenues declined by 12.4% to HUF 9.4 billion in 2018. This was primarily due to the absence of one-off revenue recorded in 2017 at the Hungarian operation, delivered by a major project related to the 2017 Swimming Word Championship (FINA).
- **Wholesale** revenues increased by 4.4% to HUF 19.9 billion in 2018. Lower fixed incoming domestic and international traffic in Macedonia resulted in lower wholesale revenues, but was offset by increased wholesale revenues in Hungary driven by higher wholesale voice transit revenues.

System Integration (SI) and IT revenues amounted to HUF 107.1 billion in 2018, compared to HUF 87.5 billion in 2017, thanks to significant growth in both countries of operations. In Hungary, this was attributable to a high volume of hardware and software sales and the implementation of projects, primarily within the public segment. In Macedonia, SI/IT revenues recovered from a temporary decline in 2017, when major public sector projects suffered some delays due to a period of political uncertainty.

Energy Services were discontinued following the exit from the residential segment of the electricity market, as of November 1, 2017.

13.2 Direct costs

Direct costs increased from HUF 245.8 billion in 2017 to HUF 286.9 billion in 2018 (HUF 284.9 billion excluding the impact of IFRS 15 adoption), mainly due to higher SI/IT related costs, in addition to an increase in other direct costs.

- **Interconnect costs** grew 9.3% to HUF 20.6 billion in 2018, driven by a higher volume of off-net mobile traffic that led to higher payments to other mobile operators in both Hungary and Macedonia.
- **SI/IT service related costs** increased by 25.5% to HUF 75.8 billion in 2018, in line with higher SI/IT revenues in both countries, and the increasing portion of hardware and software sales in the sales mix in Hungary.
- **Energy services** were discontinued following the exit from the residential segment of the electricity market, as of November 1, 2017.
- **Bad debt expenses** increased from HUF 5.5 billion in 2017 to HUF 9.5 billion in 2018 (HUF 8.3 billion excluding the impact of IFRS 15 adoption). This was driven by a higher bad debt expense in Hungary resulting from the strong growth in revenues as well as the absence of the positive one-off impact recorded in 2017 which stemmed from the application of lower impairment rates. In Macedonia, bad debt expense (excluding the impact of IFRS 9 and 15 adoption) declined thanks to lower impairment levels related to mobile sales.
- **Telecom tax** increased by 1.6% to HUF 25.5 billion in 2018, driven by higher mobile voice traffic in both residential and business segments attributable to the growing share of flat rate packages.
- **Other direct costs** increased by 18.6% to HUF 155.5 billion in 2018 primarily due to the higher cost of equipment sales, in line with higher sales volumes in both Hungary and Macedonia. TV and other content related costs and roaming payments also grew in Hungary.

13.3 Gross profit

Gross profit improved to HUF 370.2 billion in 2018, from HUF 365.1 billion in 2017, thanks to a strong increase in revenues.

13.4 Employee-related expenses

Employee-related expenses grew 3.4% year-on-year to HUF 83.0 billion, as a combined result of changed trainee employment form in Hungary, a 5% average wage increase at the Parent Company and higher severance-related expenses in both Hungary and Macedonia.

13.5 Other operating expenses

Other operating expenses declined from HUF 105.9 billion in 2017 to HUF 103.9 billion. In Hungary, cost saving measures implemented during the year resulted in lower HR-related, IT maintenance and energy costs which more than offset increased rental fees and maintenance costs. Hungarian utility tax was also 3.5% lower in 2018. This reflected the positive effects of Magyar Telekom's tax credit relating to new network investments and upgrades, to enable internet access at speeds of at least 100 Mbps. Other operating expenses in Macedonia improved moderately thanks to lower marketing and maintenance expenses.

13.6 Other operating income

Other operating income increased to HUF 9.2 billion in 2018 from HUF 6.7 billion 2017, reflecting the one-off profits realized from the sale of the old headquarters in Hungary.

13.7 EBITDA

EBITDA grew 3.7% to HUF 192.5 billion in 2018, thanks to the improvements in gross profit and other operating expenses in both countries of operation and the higher other operating income in Hungary.

13.8 Depreciation and amortization

Depreciation and amortization (D&A) expenses increased by 6.8% to HUF 115.5 billion in 2018. In Hungary, higher D&A expenses resulted from the shortened useful lives of customer connections related network equipments, while in Macedonia, the increase reflected higher D&A related to intangible assets and TV content fees, capitalized at the end of 2017.

13.9 Operating profit

Operating profit decreased moderately from HUF 77.5 billion in 2017 to HUF 77.0 billion in 2018 as increases in EBITDA were offset by the higher D&A expenses.

13.10 Net financial result

Net financial loss narrowed from HUF 21.6 billion in 2017 to HUF 17.8 billion in 2018, thanks to the lower average debt level, as well as a reduction in losses on the fair valuation of derivatives versus 2017. This occurred due to different EUR-HUF exchange rate and yield developments between the two periods.

13.11 Income tax

The income tax expense decreased from HUF 16.0 billion in 2017 to HUF 13.3 billion in 2018. The decline reflects one-off corrections made in 2017, which resulted in the increase of the 2017 income tax expense.

13.12 Profit attributable to non-controlling interests

Profit attributable to non-controlling interests increased by 4.1% to HUF 3.1 billion in 2018, due to higher profit generation at the Macedonian subsidiary during the period.

13.13 Cash flows

HUF millions	1-12 months 2017	1-12 months 2018	Change
Operating cash flow	157,411	159,098	1,687
Investing cash flow	(94,353)	(83,092)	11,261
Less: Payments for / Proceeds from other financial assets - net	2,867	(2,055)	(4,922)
Investing cash flow excluding Proceeds from other financial assets – net	(91,486)	(85,147)	6,339
Repayment of other financial liabilities	(7,485)	(5,988)	1,497
Free cash flow from continuing operation	**58,440**	**67,963**	**9,523**
Net cash used in operating activities from discontinued operation	(23)	0	23
Net cash generated from investing activities from discontinued operation*	36,292	0	(36,292)
Free cash flow from discontinued operation	**36,269**	**0**	**(36,269)**
Total free cash flow	**94,709**	**67,963**	**(26,746)**
Payments for /Proceeds from other financial assets - net	(2,867)	2,055	4,922
Repayment of loans and other borrowings - net	(67,732)	(36,974)	30,758
Dividend paid to shareholders and Non-controlling interests	(29,403)	(29,547)	(144)
Repurchase of treasury shares	(2,139)	(1,822)	317
Net cash generated in financing activities from discontinued operation	2,041	0	(2,041)
Exchange differences on cash and cash equivalents	(15)	130	145
Change in cash and cash equivalents	**(5,406)**	**1,805**	**7,211**

* Less: Payments for / Proceeds from other financial assets - net from discontinued operation

Free cash flow from continuing operations (FCF) increased from HUF 58.4 billion in 2017 to HUF 68.0 billion in 2018 due to the reasons described below.

Operating cash flow from continuing operations

Net cash generated from operating activities amounted to HUF 159.1 billion in 2018, compared to HUF 157.4 billion in 2017, as a result of the following trends:

- HUF 6.8 billion **positive impact of** higher **EBITDA** recorded in 2018 compared to 2017
- HUF 12.3 billion **negative change in active working capital,** mainly as a result of the following factors:
  - higher increase in instalment receivables compared to the corresponding period in 2017 in line with the increased corresponding sales volumes (negative impact: ca. HUF 5.8 billion)
  - higher increase in SI/IT receivables in 2018 compared to 2017 (negative impact: ca. HUF 2.6 billion)
  - lower SI/IT related advance payment as well as higher advance payment settlement in 2018 compared to 2017 due to different project seasonality (positive impact: ca. HUF 1.7 billion)
  - no decrease in energy receivables in 2018 as the energy services were discontinued following the exit from the residential segment of the electricity market, as of November 1, 2017 (negative impact: ca. HUF 1.2 billion)
  - higher increase in SI/IT related inventory balances in 2018 against a sharp decrease in 2017 due to different project timings, combined with a decrease in equipment inventories during 2018 due to higher sales (negative impact: ca. HUF 0.8 billion)
  - decrease in the total balance of contract assets and contract costs (excl. the effect of cumulative catch-up adjustments and reclassifications) following the implementation of IFRS 9 and IFRS 15 accounting standards, with effect from 1 January 2018 (positive net impact: ca. HUF 0.3 billion)

- HUF 3.0 billion **positive change in provisions,** due to lower payments of legal provisions and a higher net addition to severance provision in 2018 versus 2017

- HUF 8.0 billion **positive change in passive working capital,** primarily driven by the following factors:

  - lower payment related to SI/IT services in 2018 than in 2017 (positive impact: HUF 6.9 billion)
  - higher HR-related personnel expense payments in 2018 than in 2017 due to different timing of salary payments (negative impact: HUF 3.0 billion)
  - the slower growth in the balance of equipment creditors resulting from changes in payment terms agreed with handset suppliers was more than offset by the higher increase in the balances of invoiced and non-invoiced other creditors due to improved vendor management in 2018 compared to 2017(positive impact: HUF 2.7 billion)
  - the customer loyalty programme in Hungary was terminated in 2017, and there was no movement in the relating balances of deferred income in 2018 (positive impact: HUF 2.1 billion)
  - lower SI/IT related advance payment received during 2018 compared to 2017 (negative impact: HUF 1.1 billion)
  - no decrease in the volume of energy suppliers in 2018 compared to 2017 as the energy services were discontinued following the exit from the residential segment of the electricity market, as of November 1, 2017 (positive impact: HUF 0.4 billion)
  - decrease in contract liabilities (excl. the effect of cumulative catch-up adjustments and reclassification) due to the implementation of the IFRS 15 accounting standard with effect from 1 January 2018 (negative impact: ca. HUF 0.1 billion)

- HUF 1.5 billion **negative change** due to overpayment of **local business and innovation tax paid** in 2017, as well as higher payment in 2018 than in 2017 due to the transition impact of IFRS 15
- HUF 0.4 billion **positive change** due to the **higher dividend received** from the E2 energy joint venture in 2018 versus 2017
- HUF 1.1 billion **positive change** due to lower levels of **interest expense paid** as well as lower levels of postal and bank charges paid in 2018 than in 2017
- HUF 3.9 billion **negative change** mainly due to the **one-off non-cash gains** resulting from the sale of the old headquarters recorded in 2018 which was partly offset by a real estate sale in 2017

Investing cash flow from continuing operations excluding proceeds from other financial assets – net

Net cash used in regular investing activities amounted to HUF 85.1 billion in 2018, compared to HUF 91.5 billion in 2017, with the lower cash outflow driven by the following:

- HUF 21.3 billion **negative effect** due to higher **CAPEX** in 2018 than in 2017 mainly due to the HUF 15.7 billion higher spectrum licence purchase in 2018

- HUF 18.5 billion **positive change** due to lower payments to **CAPEX creditors** in 2018 compared to 2017
- HUF 1.7 billion **positive impact** from lower cash outflows for business combinations in 2018 versus 2017 (**ITGen Kft.** in 2018 **and** ServerInfo**-Ingatlan Kft.** in 2017, and the lower volume **of cable TV operation acquisitions** in 2018)
- HUF 0.4 billion **negative impact** due to the lower amount of **cash acquired** through acquisitions
- HUF 7.8 billion **positive change** related to the **disposal of PPE,** mainly reflecting the sale of the old headquarters in 2018 which was partly offset by a real estate sale in 2017

Repayment of other financial liabilities

Repayment of other financial liabilities decreased from HUF 7.5 billion in 2017 to HUF 6.0 billion in 2018, mainly due to the following:
- HUF 1.1 billion **positive change** caused by the termination of certain finance lease contracts, resulting in lower lease payments in 2018 compared to 2017
- HUF 0.9 billion **positive impact** of the absence of a repayment instalment relating to the financing of the Macedonian headquarters building in 2017
- HUF 0.3 billion **negative change** due to higher content right payments in 2018 compared to 2017

Free cash flow from discontinued operations (FCF) decreased by HUF 36.3 billion mainly due to the sale of Crnogorski Telekom A.D. (disclosed within discontinued operations) in Q1 2017.

Proceeds from other financial assets - net improved by HUF 4.9 billion, primarily due to a lower amount of 3-month bank deposits at Maktel in net terms compared to 2017 as well as higher cash inflows from derivatives in 2018 than in 2017.

Repayment of loans and other borrowings – net improved by HUF 30.8 billion, due to lower reimbursement of parent company (DT AG) loans in 2018 mainly due to the reimbursement from the sale proceeds of the Crnogorski Telekom A.D disposal in 2017.

Dividends paid to owners of the parent and non-controlling interests increased by HUF 0.1 billion mainly due to the higher dividend payment from MT Group to its non-controlling interests in 2018 compared to 2017.

Repurchase of treasury shares decreased by HUF 0.3 billion due to lower repurchase of treasury shares for ESOP (Employee Stock Ownership Program) in 2018 than in 2017.

Net cash generated from financing activities from discontinued operations declined by HUF 2.0 billion due to the positive impact in 2017 of a loan repayment by Crnogorski Telekom A.D. to Magyar Telekom in 2017 following its disposal.

Exchange differences on cash and cash equivalents from continuing operations improved by HUF 0.1 billion due to more favourable foreign exchange rate movements in 2018 compared to 2017.

The financial and operating statistics are available on the following website:

http://www.telekom.hu/about_us/investor_relations/financial

13.14 Statements of Financial Position

The most significant changes in the balances of the Statements of Financial Position from December 31, 2017 to December 31, 2018 can be observed in the following lines:

- Trade receivables and other assets
- Property plant and equipment and intangible assets (including Goodwill)
- Other non-current financial assets
- Other non-current assets
- Financial liabilities to related parties (current and non-current combined)
- Trade payables
- Other current liabilities

Trade receivables and other assets increased by HUF 37.5 billion from December 31, 2017 to December 31, 2018, driven by the increase in current installment receivables (ca. HUF 18.5 billion) and the adoption of IFRS 9 and IFRS 15 accounting standards. The total impact of the opening adjustment comes to HUF 9.5 billion related to the catch-up adjustment and ca. HUF 4.0 billion resulting from the reclassification of construction contract receivables under IAS 11 and the discount given to customers of unbilled receivables under IAS 18 to contract assets within the same line. The closing balance of current contract assets amounted to HUF 17.8 billion.

Property plant and equipment (PPE) and intangible assets (including Goodwill) together decreased by HUF 8.7 billion from December 31, 2017 to December 31, 2018, as depreciation and scrapping of assets exceeded capital expenditure for the period.

Other non-current financial assets increased by HUF 5.7 billion from December 31, 2017 to December 31, 2018, mainly due to the adoption of IFRS 9 and IFRS 15 accounting standards. The closing balance of non-current contract assets amounted to HUF 3.6 billion.

Other non-current assets increased by HUF 4.9 billion from December 31, 2017 to December 31, 2018 as a result of the adoption of IFRS 9 and IFRS 15 accounting standards. The closing balance of contract costs amounted to HUF 4.5 billion.

Financial liabilities to related parties (current and non-current combined) decreased by HUF 32.3. billion from December 31, 2017 to December 31, 2018 mainly due to the repayment of DT group loans in 2018.

Trade payables increased by HUF 39.9 billion from December 31, 2017 to December 31, 2018, largely a reflection of the increase in the balances outstanding to handset, SI/IT and CAPEX suppliers.

Other current liabilities decreased by HUF 2.2 billion from December 31, 2017 to December 31, 2018. The closing balance of Other current liabilities includes HUF 12.4 billion of contract liabilities mainly due to the reclassification of advance payments received from customers and of deferred revenue within the same line.

There have not been any other material changes in the items of the Consolidated Statement of Financial Position from December 31, 2017 to December 31, 2018; other less significant changes can largely be attributable to the impacts of the implementation of IFRS 9 and IFRS 15 accounting standard as presented in Section 3.9. In terms of the Consolidated Statement of Cash Flows for 2018, the related explanations can be found above in Section 13.14.

14 SUBSEQUENT EVENTS BETWEEN THE END OF THE YEAR AND THE RELEASE OF THE REPORT

14.1 Cable TV network and operations

In December 2018, the Group signed a Share Purchase Agreement to acquire a cable TV business for a purchase price of HUF 789 million. The closing of the transaction took place in February 2019.

14.2 Sale of Szerémi-Kaposvár buildings

In January 2019, the sale of Szerémi-Kaposvár buildings was completed, representing the last remaining transaction of the comprehensive real estate agreement signed with WING Group on May 19, 2015. The sales price amounted to EUR 11.3 million.

Budapest, February 20, 2019.

Tibor Rékasi
Chief Executive Officer, Board member

János Szabó
Chief Financial Officer

Declaration

We the undersigned declare that

- the attached annual financial statements which have been prepared in accordance with the applicable set of accounting standards and to the best of our knowledge, gives a true and fair view of the assets, liabilities, financial position and profit or loss of Magyar Telekom Plc. and the undertakings included in the consolidation as a whole, and
- the business report gives a fair view of the position, development and performance of Magyar Telekom Plc. and the undertakings included in the consolidation as a whole, together with a description of the principal risks and uncertainties of its business.

Budapest, April 9, 2019

Tibor Rékasi
Chief Executive Officer,
Member of the Board

János Szabó
Chief Financial Officer