Magyar Telekom Plc.
Form 20-F
June 27, 2007
As filed with the Securities and Exchange Commission on June 27, 2007

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

Form 20-F

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2006

Commission file number 1-14720

MAGYAR TELEKOM TÁVKÖZLÉSI NYILVÁNOSAN MŰKÖDŐ RÉSZVÉNYTÁRSASÁG

(Exact Name of Registrant as Specified in Its Charter)

MAGYAR TELEKOM TELECOMMUNICATIONS PUBLIC LIMITED COMPANY

(Translation of Registrant s Name Into English)

Hungary

(Jurisdiction of Incorporation or Organization)

Budapest, 1013, Krisztina krt. 55, Hungary

(Address of Principal Executive Offices)

Securities registered or to be registered pursuant to Section 12(b) of the Act

Title of each class	**Name of each exchange on which registered**
American Depositary Shares, each representing five Ordinary Shares	New York Stock Exchange
Ordinary Shares	New York Stock Exchange*
	Budapest Stock Exchange

Securities registered or to be registered pursuant to Section 12(g) of the Act: **N/A**

Securities for which there is a reporting obligation pursuant to Section 15(d) of the Act: **N/A**

Indicate the number of outstanding shares of each of the issuer s classes of capital or common stock as of the close of the period covered by the annual report:

Ordinary Shares 1,042,768,215
nominal value HUF 100 per share

(as of December 31, 2006)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

YES x NO o

If this report is an annual or transition report, indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934.

YES o NO x

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15 (d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES x NO o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of accelerated filer and large accelerated filer in Rule 12b-2 of the Exchange Act.

Large accelerated filer x Accelerated filer o Non-accelerated filer o

Indicate by check mark which financial statement item the registrant has elected to follow.

Item 17 x Item 18 o

If this is an annual report, indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES o NO x

* Not for trading, but only in connection with the registration of American Depositary Shares.

TABLE OF CONTENTS

Certain Defined Terms and Conventions

In this annual report the terms Magyar Telekom , the Group , the Company , we , us and our refer to Magyar Telekom Plc. and, if applicable direct and indirect subsidiaries as a group; the term Magyar Telekom Plc. refers to Magyar Telekom Plc. without its subsidiaries; the term DT refers to Deutsche Telekom AG. The term TMH refers to the mobile line of business of Magyar Telekom. T-Mobile Magyarország Távközlési Rt., our fully owned subsidiary, merged with Magyar Telekom Plc. on February 28, 2006. From March 1, 2006, Magyar Telekom is the legal successor of TMH.

In this annual report, the term Minister refers to the Minister heading the Ministry of Economy and Transport.

Totals in tables may be affected by rounding. Segment revenue and operating expense figures included in this annual report do not give effect to intersegment eliminations.

Forward-looking Statements

The Company may from time to time make written or oral forward-looking statements. Written forward-looking statements appear in documents the Company files with the Securities and Exchange Commission, including this annual report, reports to shareholders and other communications. The U.S. Private Securities Litigation Reform Act of 1995 contains a safe harbor for forward-looking statements. Actual results may differ materially from a forward-looking statement made by Magyar Telekom or on its behalf. Readers should also consider the information contained in Item 3, Key Information Risk Factors and Item 5, Operating and Financial Review and Prospects , as well as the information contained in the Company s periodic filings with the Securities and Exchange Commission for further discussion of the risks and uncertainties that may cause such differences to occur. The Company s forward-looking statements speak only as of the date they are made, and the Company does not have an obligation to update or revise them, whether as a result of new information, future events or otherwise.

PART I

ITEM 1 IDENTITY OF DIRECTORS, SENIOR MANAGEMENT AND ADVISERS

Not applicable.

ITEM 2 OFFER STATISTICS AND EXPECTED TIMETABLE

Not applicable.

ITEM 3 KEY INFORMATION

SELECTED FINANCIAL DATA

This selected consolidated financial and statistical information should be read together with the consolidated financial statements, including the accompanying notes, included in this annual report. We derived these financial data from our consolidated financial statements as of and for the years ended December 31, 2002, 2003, 2004, 2005 and 2006 and the accompanying notes, which have been audited by PricewaterhouseCoopers Könyvvizsgáló és Gazdasági Tanácsadó Kft. (PwC). These consolidated financial data are qualified by reference to our consolidated financial statements and accompanying notes, which we have prepared in accordance with International Financial Reporting Standards (IFRS). IFRS differs from U.S. Generally Accepted Accounting Principles (GAAP). For a discussion of the principal differences between IFRS and U.S. GAAP as they relate to us, see Note 37 to the consolidated financial statements.

	Year ended December 31,					
	2002	**2003**	**2004**	**2005**	**2006**	**2006**
	HUF	**HUF**	**HUF**	**HUF**	**HUF**	**U.S.$**(1)
	(in millions, except per share amounts)					
Consolidated Income Statement Data:						
Amounts in accordance with IFRS						
Revenues(2)	590,585	607,252	596,792	615,054	671,196	3,503
Operating profit(3)	122,240	122,064	93,719	141,754	136,391	712
Net income	68,128	57,475	34,641	78,415	75,453	394
Operating profit per share(3)	117.76	117.60	90.30	136.46	131.10	0.68
Basic earnings per share(4)	65.66	55.38	33.38	75.49	72.53	0.38
Diluted earnings per share(4)	65.66	55.37	33.37	75.46	72.51	0.38
Amounts in accordance with U.S. GAAP						
Revenues(2)	592,294	610,946	602,953	620,208	675,564	3,526
Operating profit(3)	132,585	132,715	100,294	131,018	132,431	691
Net income	78,619	66,404	39,684	69,260	71,481	373
Operating profit per share(3)	127.73	127.86	96.63	126.12	127.30	0.66
Basic earnings per share(4)	75.77	63.98	38.23	66.67	68.71	0.36
Diluted earnings per share(4)	75.77	63.97	38.22	66.65	68.69	0.36
Consolidated Balance Sheet Data:						
Amounts in accordance with IFRS						
Total assets	1,077,451	1,058,837	1,029,568	1,082,948	1,131,595	5,905
Net assets as reported	575,580	630,384	576,664	597,694	593,167	3,095
Common stock	104,281	104,281	104,281	104,281	104,277	544
Total shareholders equity as reported	516,144	560,110	516,567	527,567	526,039	2,745
Amounts in accordance with U.S. GAAP						
Total assets	1,099,634	1,090,308	1,070,601	1,115,991	1,160,629	6,057
Net assets	570,541	633,783	592,872	610,035	604,400	3,154
Total shareholders equity	514,664	567,452	534,907	542,098	538,190	2,809

	Year ended December 31,				
	2002	2003	2004	2005	2006
	(in millions)				
Other data:					
Weighted average number of shares					
Basic	1,038	1,038	1,038	1,039	1,040
Diluted	1,038	1,038	1,038	1,039	1,041

(1) Translated into U.S. dollars at the official exchange rate of the National Bank of Hungary on December 31, 2006 of U.S. dollar 1.00 = HUF 191.62. These translations are unaudited and presented for convenience purposes only.

(2) In 2006, we reassessed our status in the provision of a number of value added services, where so far we accounted for revenue on a gross basis implying a principal status rather than an agent status in the provision of the service. A gross basis means that revenues included the full amount of fees collected from customers, and outpayments to related service providers were included in operating expenses. After analyzing the relationships with our subcontractors one by one, we have changed our judgment of the situation in some cases, and now we assess that in these cases we are more the selling agent of these products than the principal provider of the service, from an IFRS accounting point of view. This had a decreasing impact on the fixed line Value added, cable voice and other services revenues and the mobile Enhanced services revenues as well as on subcontractor payments in Other operating expenses - net . The change only meant netting between revenues and expenses; it had no impact on either operating profit or net income. We also restated 2004 and 2005 figures accordingly.

(3) In 2006, we changed our accounting policy to disclose Hungarian local business tax and innovation fee as income taxes since we have determined that these taxes have the characteristics of income taxes rather than operating expenses. In previous years, these taxes were included among operating expenses. This change in the disclosure of these taxes decreased our operating expenses and resulted in an equivalent increase in income taxes. The change had no impact on net income or equity. We also restated 2004 and 2005 figures accordingly.

(4) Basic earnings per share under IFRS and basic earnings per share under U.S. GAAP are calculated by dividing net income by the weighted average number of shares outstanding during each period.

Dividends

The following table sets forth the dividend per Magyar Telekom ordinary share for the years 2002, 2003, 2004, 2005 and 2006. The table shows the dividend amounts in Hungarian forints, together with U.S. dollar equivalents, for each of the years indicated.

	Dividend Paid Per Ordinary Share	
	HUF	U.S.$(1)
Year		
2002	18	0.0799
2003	70	0.3367
2004	70	0.3883
2005	73	0.3418
2006	70	0.3653

(1) Translated into U.S. dollars at the official exchange rate of the National Bank of Hungary on December 31, 2006 of U.S. dollar 1.00 = 191.62; December 31, 2005 of U.S. dollar 1.00 = HUF 213.58; December 31, 2004 of U.S. dollar 1.00 = HUF 180.29; December 31, 2003 of U.S. dollar 1.00 = HUF 207.92 and on December 31, 2002 of U.S. dollar 1.00 = HUF 225.16.

2

EXCHANGE RATE INFORMATION

As used in this document, Hungarian forint or HUF mean the lawful currency of Hungary. EUR , euro or mean the single unified currency of the European Union. U.S. dollar, USD or $ mean the lawful currency of the United States.

The National Bank of Hungary (NBH) quotes and publishes official exchange rates of the Hungarian forint for all major currencies based on prevailing market rates. Unless otherwise stated, conversion of Hungarian forint into U.S. dollars have been made at the rate of USD 1.00 to HUF 191.62, which was the official rate quoted and published on December 31, 2006.

The NBH as a policy intervenes in the foreign exchange market to stabilize the exchange rate of the Hungarian forint for the euro. On any given day, the market exchange rate of the Hungarian forint against euro may vary from the official rate of the NBH. Prior to May 4, 2001, the NBH had a policy of intervening in the foreign exchange market, if the market rate deviated more than 2.25 percent above or below the official rate. On May 4, 2001, the NBH announced that it had widened this intervention band to 15 percent above and below the official rate. The central parity is set at 282.36 HUF/EUR rate. This decision was taken as a step toward convergence with the European Union exchange rate regime and as a measure against inflation.

The following tables set forth, for the periods and dates indicated, the period-end, average, high and low official rates quoted and published by the NBH for Hungarian forint per U.S.$1.00 and EUR1.00.

	Exchange Rates			
	Period-End	**Average**(1)	**High**	**Low**
	(amounts in HUF/U.S.$)			
Year				
2002	225.16	258.00	283.98	225.16
2003	207.92	224.44	237.63	206.61
2004	180.29	202.63	217.24	180.19
2005	213.58	199.66	217.54	180.58
2006	191.62	210.51	225.01	191.02
2006				
December	191.62	192.26	194.21	191.02
2007				
January	199.52	195.22	199.52	189.25
February	193.21	193.87	196.88	191.34
March	186.13	188.74	194.91	184.08
April	181.03	182.13	185.02	180.10
May	186.23	183.84	186.79	181.04

(1) The average of the exchange rates on each business day during the relevant period.

3

	Exchange Rates			
	Period-End	Average(1)	High	Low
	(amounts in HUF/EUR)			
Year				
2002	235.90	242.97	252.38	235.17
2003	262.23	253.51	272.03	234.69
2004	245.93	251.68	270.00	243.42
2005	252.73	248.05	255.93	241.42
2006	252.30	264.27	282.69	249.55
2006				
December	252.30	254.08	256.90	252.30
2007				
January	258.04	253.83	258.46	251.15
February	254.79	253.40	255.70	251.65
March	247.83	249.81	256.05	245.67
April	246.42	245.96	247.35	244.96
May	250.35	248.47	251.05	245.78

(1) The average of the exchange rates on each business day during the relevant period.

We will pay any cash dividends in Hungarian forints, and if you are a holder of American Depository Shares (ADSs) exchange rate fluctuations will affect the U.S. dollar amounts you will receive upon conversion of cash dividends on the shares represented by ADSs. Fluctuations in the exchange rate between the Hungarian forint and the U.S. dollar will also affect the prices of shares and ADSs.

RISK FACTORS

Prior to making any investment decision, you should carefully consider the risks set forth below in addition to other information contained in this annual report. The risks described below are not the only risks we face. Additional risks not currently known to us or risks that we currently regard as immaterial also could have a material adverse effect on our financial condition or results of operations or the trading prices of our securities.

Our operations are subject to substantial government regulation, which can result in adverse consequences for our business and results of operations.

The Electronic Communications Act of 2003 (Electronic Communications Act), which came into force in January 2004, was enacted by the Parliament to achieve harmonization of the telecommunications regulatory regime in Hungary with the New Regulatory Framework (NRF) of the European Union (EU) for electronic communications adopted in 2002, and to encourage further competition in the market. The NRF is currently under review in the EU; however, according to our expectations, the amended regulation will not affect business activities earlier than 2010.

Under the Electronic Communications Act, the National Communications Authority (NCA) was established to regulate the telecommunications industry. The primary responsibility of the NCA is to perform market analysis procedures, under which it defines relevant markets, or markets subject to the regulatory framework. The NCA analyzes such markets for the level of competition and, if it finds a lack of sufficient competition in such markets, identifies service providers with significant market power (SMP), and imposes appropriate regulatory obligations on such providers to encourage competition.

The NCA initiated the market analysis procedure on 17 out of 18 relevant markets identified in an applicable decree in 2004 and has reached its final findings on 16 of these markets. Under these findings, Magyar Telekom was found to have SMP on 12 of the 16 markets (i.e., markets 1-9 and 11-13) and TMH was found to have SMP on one market (i.e., market 16). As a result, the NCA imposed various obligations on Magyar Telekom and TMH with respect to these markets. See Item 4 Regulation and Pricing .

The Recommendation of the European Commission on relevant product and service markets within the electronic communications sector susceptible to *ex ante* regulation in accordance with Directive 2002/21/EC of the European Parliament and of the Council on a common regulatory framework for electronic communication networks and services (2003/311/EC) (Recommendation), the regulation on which the market analysis procedure of the NCA is based, is also under review by the EU. The new recommendation is expected to enter into force in 2007.

The new Communications Act which is affecting our Bulgarian subsidiary s, Orbitel s core business is on the agenda of the Bulgarian Parliament. The majority of changes proposed by Orbitel have been accepted by the relevant committee of the Parliament, but the changes are still to be approved by the Parliament. Any further changes proposed in the Communications Act by the members of the Parliament and any delay in the bylaws may negatively influence the business results of Orbitel.

In addition, our businesses in Macedonia and Montenegro are also subject to various regulatory developments.

We cannot fully anticipate the combined impact of these regulatory developments on our business and results of operations. Our business and results of operations may be adversely affected by these changes.

Recent EU initiative on roaming charges in the mobile telecommunications sector could adversely affect our results of operation.

On July 12, 2006 the European Commission proposed an EU regulation to reduce international roaming charges within the EU. The proposal for a regulation of the European Parliament and of the Council is dealing with the roaming on public mobile networks within the EU. The objective of this proposal is to amend the existing regulatory framework for electronic communications to provide the necessary legal basis for effective and timely action to bring about substantial reductions in the level of mobile roaming charges across the EU in a harmonized manner. The EU roaming regulation, as approved on May 23, 2007 by the European Parliament, will set a limit on the international wholesale mobile roaming charges among mobile operators and on international mobile roaming retail charges (Eurotariff). The maximum inter-operator tariff shall not exceed EUR 0.30 per minute, which will be further reduced in 2008 and 2009 to EUR 0.28 and EUR 0.26. The maximum retail charges of the Eurotariff, which a home provider may levy from its roaming customers, for calls made abroad shall not exceed EUR 0.49 per minute (to be further reduced to EUR 0.46 and EUR 0.43 in 2008 and 2009) and for calls received abroad shall not exceed EUR 0.24 per minute (to be further reduced to EUR 0.22 and EUR 0.19 in 2008 and 2009). The Council of the EU telecommunications ministers endorsed the EU roaming regulation on June 7, 2007. The EU roaming regulation will then become directly applicable in EU member states (and therefore not require further transposition into national law) following its publication, expected in June 2007. The EU roaming regulation will have significant consequences for TMH s revenues.

We are subject to more intense competition due to the liberalization of the telecommunications sector.

The Electronic Communications Act was enacted to facilitate further competition and encourage new entrants to the market. Although identities of such entrants are already known to some degrees, the scope of competition and any adverse effect on our results will depend on a variety of factors that we currently cannot assess with precision and are for the most part not within our control. Among such factors are business strategies and capabilities of new competitors, prevailing market conditions, as well as the

effectiveness of our efforts to prepare for new market conditions. Specific risks include loss of customers as a result of unbundled access to the local loop, loss of fixed line customers as a result of introducing naked ADSL and migration to lower priced Internet price plans as a result of speed upgrades.

In the mobile communications business, we already face intense competition. As all telecommunications markets have become increasingly saturated, the focus of competition is starting to shift from customer acquisition to retention. Significant customer defections could have an adverse effect on results of operations, and customer acquisition and retention expenses are substantial. Due to the increased level of competition, prices for mobile telephone services have been declining over the past several years and may continue to decline. An eventual entry of Mobile Virtual Network Operators (MVNOs) into the mobile telecommunications market would intensify the competition in Hungary. MVNOs are mobile operators that do not own their own spectrum or often network infrastructure, buy the use of the spectrum and network infrastructure from traditional mobile operators and provide mobile telecommunications services to consumers based on such purchased capacity. MVNOs will likely target the lower segment of the market and such development will likely increase price-based competition.

We also face intense competition in the market for Internet services, as well as in the data communications markets from other fixed line, mobile and cable television service providers.

In Macedonia, the exclusive rights of Makedonski Telekommunikacii AD (Maktel) to provide fixed line telecommunications services expired at the end of 2004 as a result of the market liberalization. Competition posed by new entrants may result in a downward pressure on Maktel s pricing, sales volume and profitability, which would have an adverse effect on our financial condition and results of operations. The Macedonian telecommunications regulator issued a third mobile license to Austrian Mobilkom in the first quarter of 2007, which is expected to intensify the competition in the Macedonian mobile market.

In Montenegro, the de facto exclusivity of Crnogorski Telekom in international voice traffic has come to an end as Promonte, the Montenegrin market leader in mobile telephony has acquired a license for international voice traffic valid from January 1, 2007. There are several public tenders ongoing in Montenegro that will have a significant long term effect on the telecommunications market. The Montenegrin Telecommunications Agency has announced a public tender for cable television services, and new cable television service providers may enter traditional telecommunications markets in 2007. The Montenegrin Telecommunications Agency has also announced a public tender for providing telecommunications services using World Interoperability for Microwave Access (WiMAX) technology. The outcome of this tender might further increase competition in Montenegro. Furthermore, in November 2006, the Montenegrin telecommunications regulator has issued a tender for two Third Generation (3G) licenses as well as a tender for a mixed 2G-3G license for a third mobile operator. In the first quarter of 2007, T-Mobile Crna Gora and Promonte were awarded with one 3G licenses each and Telekom Serbia won the combined 2G-3G license. It is most likely, that the mobile operation of Crnogorski Telekom could face a significant decrease in its market share over the medium term.

Competition posed by potential new entrants may result in a downward pressure on Crnogorski Telekom s and T-Mobile Crna Gora s pricing, sales volume and profitability, which would have an adverse effect on our financial condition and results of operations.

Our ability to sustain revenue growth will depend in part on our ability to increase traffic and offer value added and data services to our customers.

We expect the number of our fixed access lines and rates for fixed and mobile telephone services to decrease as competition increases. Our ability to sustain revenue growth will therefore depend on our ability to increase the amount of traffic over existing fixed lines and to increase revenues from value added and data services. We also plan to grow our mobile subscriber base and our related lines of business, such as Internet and cable television, and expand our coverage area. We may not be able to sustain revenue

growth, if we are not able to offer attractive and affordable value added services in the future or if our customers do not purchase our services.

We may be unable to adapt to technological changes in the telecommunications market.

The telecommunications industry is characterized by rapidly changing technology with related changes in customer demands for new products and services at competitive prices. Technological developments are also shortening product life cycles and facilitating convergence of various segments of the increasingly global industry. Our future success will largely depend on our ability to anticipate, invest in and implement new technologies with the levels of service and prices that customers demand. Technological advances may also affect our level of earnings and financial condition by shortening the useful life of some of our assets.

The operation of our businesses depends in part upon the successful deployment of continually evolving mobile communications technologies, which requires significant capital expenditures. There can be no assurance that such technologies will be developed according to anticipated schedules, that they will perform according to expectations, or that they will achieve commercial acceptance. We may be required to make more capital expenditures than we currently expect if suppliers fail to meet anticipated schedules, performance of such technologies fall short of expectations, or commercial success is not achieved.

The effects of technological changes on our businesses cannot be predicted. In addition, it is impossible to predict with any certainty whether the technology selected by us will be the most economic, efficient or capable of attracting customer usage. There can be no assurance that we will be able to develop new products and services that will enable us to compete effectively.

TMH launched 3G-based services in Hungary in 2005 before any of its competitors. TMH is currently upgrading the network infrastructure to better provide the new generation of services. However, new alternative technologies and standards, e.g., Wireless Fidelity (WiFi), WiMAX, or Voice over Internet Protocol (VoIP), may keep consumers from choosing 3G-based services. We are not able to predict at the moment which of these competing technologies will be the most widely accepted platform, however we think that High Speed Downlink Packet Access (HSDPA) and High Speed Uplink Packet Access (HSUPA) enabled 3G network is the most likely candidate.

Developments in the technology and telecommunications sectors have resulted and may result in impairments in the carrying value of certain of our assets.

Developments in the technology and telecommunications sectors, including significant declines in stock prices, market capitalization and credit ratings of market participants may result in impairments of our tangible, intangible and financial assets. Future changes in these areas could lead to further impairments at any time. Recognition of impairment of tangible, intangible and financial assets could adversely affect our financial condition and results of operations and might lead to a drop in the trading price of our shares. We review on a regular basis the value of each of our subsidiaries and their assets. The value of goodwill is reviewed annually. In addition to our regular valuations, whenever we identify any indication (due to changes in the economic, regulatory, business or political environments) that goodwill, intangible assets or fixed assets may have been impaired, we consider the necessity of performing certain valuation tests which may result in an impairment charge.

We depend on a limited number of suppliers for equipment and maintenance services.

In each of our operating divisions, there are a limited number of suppliers for necessary equipment and maintenance services. The failure of these suppliers to meet our equipment and maintenance needs in a timely manner could have a significant effect on our revenues and market position. The construction and operation of our networks and the provision of our services and network infrastructure, especially mobile telecommunications services, are dependent on our ability to obtain adequate supplies of a number of key

items on a timely and cost-efficient basis. These include handsets and transmission, switching and other network equipment. Significant delays in obtaining such equipment and maintenance services could have a material adverse effect on our business and results of operations.

Our business may be adversely affected by actual or perceived health risks associated with mobile communications technologies.

Media reports have suggested that radio frequency emissions from mobile telephones are linked to medical conditions such as cancer. In addition, a number of consumer interest groups has requested investigations into claims that digital transmissions from handsets used in connection with digital mobile technologies pose health risks and cause interference with hearing aids and other medical devices. There can be no assurance that the findings of such studies will not have a material effect on our mobile business or will not lead to additional government regulations. Our ability to install new mobile telecommunications base stations and other infrastructure may also be adversely affected, and related costs may increase, due to regulations or consumer action in response to concerns over health risks and adverse effect on the value of properties adjacent to such facilities. The actual or perceived health risks of mobile communications devices could adversely affect mobile communications service providers, including us, through increased barriers to network development, reduced subscriber growth, reduced network usage per subscriber, threat of product liability lawsuits or reduced availability of external financing to the mobile communications industry.

System failures could result in reduced user traffic and revenue and could harm our reputation.

Our technology infrastructure (including our network infrastructure for fixed network services and mobile telecommunications services) is vulnerable to damage and interruption from information technology failures, power loss, floods, windstorms, fires, intentional wrongdoing and similar events. Unanticipated problems at our facilities, system failures, hardware or software failures or computer viruses could affect the quality of our services and cause service interruptions. Any of these occurrences could result in reduced user traffic and revenue and could harm our reputation.

Loss of key personnel could weaken our business.

Our operations are managed by a small number of directors and key executive officers. The loss of directors or key executive officers could significantly impede our financial, marketing and other plans. We believe that the growth and future success of our business will depend in large part on our continuing ability to attract and retain highly skilled and qualified personnel at all levels; however, the competition for qualified personnel in the telecommunications industry is intense. We can give no assurances that we will be able to hire or retain necessary personnel.

Our independent registered public accounting firm identified two contracts for which it was unable to identify a proper business purpose. A subsequent independent investigation into these and other contracts revealed weaknesses in our internal controls, and we may not be able to remedy these weaknesses or prevent future weaknesses.

In connection with their audit of our consolidated financial statements for the year ended December 31, 2005, PwC, our independent auditor, identified two consulting contracts entered into by two of our subsidiaries for which it was unable to identify a proper business purpose. A subsequent independent investigation, carried out by the law firm of White & Case under the supervision of our Audit Committee, and which is still ongoing, concluded that four consulting contracts were entered into by us and our subsidiaries without there being adequate documentation of a proper business purpose for them. The investigation was also impeded by the destruction by certain employees of documents relevant to these four contracts.

The independent investigators Initial Report of Investigation further identified several contracts at our Macedonian subsidiary that could warrant further review. In February 2007, our Board of Directors determined that those contracts should be reviewed and expanded the scope of the independent investigation to cover these additional contracts and related transactions.

The independent investigation revealed certain weaknesses in our internal controls and procedures. Management has failed to sufficiently communicate the importance of integrity and ethical values. There were deficiencies in controls related to the validity and authorization of transactions in the mergers and acquisitions process and deficiencies in the design and effectiveness of controls related to the validity and authorization of expenditures in procurement process. Specifically, senior level managers entered into expenditures by circumventing existing controls and the independent investigation has been unable to determine definitely the purpose of the contracts, and it is possible that they may have been improper.

The investigation delayed the finalization of our 2005 financial statements and Maktel has still not filed its 2005 annual report. We have to date been fined HUF 13 million as a consequence of these delays and additional fines could be imposed in the future. At this juncture, the Company is unable to estimate either the amount of such additional fines or the costs, in general, it could incur in relation to the investigation. For further discussion of the independent legal investigation, its conclusions and the steps that we are taking to remedy our control deficiencies, see Item 15 Controls and Procedures.

Notwithstanding the steps we are taking to address these issues, we may not be successful in remedying these weaknesses or preventing future weaknesses. If we are unable to remedy these weaknesses, there is a risk that we may not be able to prevent or detect improper third-party contracts that could cause a material misstatement of our annual or interim consolidated financial statements. In addition any failure to implement new or improved internal controls, or resolve difficulties encountered with their implementation, could harm our operating results or cause us to fail to meet our reporting obligations and consequently subject us to regulatory fines. Inferior internal controls could also cause investors to lose confidence in our reported financial information, which could have a negative effect on the trading price of our shares and ADSs.

Our share price may be volatile, and your ability to sell our shares may be adversely affected due to the relatively illiquid market for our shares and ADSs.

The Hungarian equity market is relatively small and illiquid compared to major global markets. As a result of the limitations of the Hungarian equity market and the volatility of the telecommunications sector in general, the price of our shares and ADSs may be relatively volatile and you may have difficulty selling your shares in the event of unfavorable market conditions.

The value of our investments, results of operations and financial condition could be adversely affected by economic developments in Hungary and other countries.

Our business depends on general economic conditions in Hungary and abroad. There are many factors, which are outside of our control that influence global and regional economies. A cautious or negative business outlook may cause our customers to delay or cancel investment in information technology and telecommunications systems and services, which would adversely affect our revenues directly and, in turn, slow the development of new services and applications that could become future revenue sources.

Due to the substantial state budget deficit, the Hungarian government passed a stabilization package in June 2006. The stabilization program provides for significant tax hikes for both corporations and individuals, including the introduction of an additional income tax on high-income individuals, increases in corporate taxes and Value-Added Tax (VAT), and a new tax on healthcare contributions and other benefits. The stabilization program also introduces material energy price increases. We expect this

stabilization program could have the effect of increasing the Consumer Price Index (CPI) and decreasing GDP in 2007 and 2008 from the levels that might otherwise be attained without it. As an effect of any relative CPI increase and/or GDP decrease, disposable income may decrease accordingly in both the corporate and the residential segments. Any such decrease in disposable income could negatively affect spending on telecommunications, which could result in decreased revenues for Magyar Telekom. In addition, the measures introduced and to be introduced by the government negatively affect our employees remuneration and may cause difficulties in the negotiations conducted with the trade unions. In order to meet our efficiency improvement targets, we will not be in the position to fully compensate the negative effects of the government measures suffered by our employees.

Fluctuations in the currency exchange rate could have an adverse effect on our results of operations.

We are subject to currency translation risks, mainly relating to the results of our Macedonian and Montenegrin operations. Devaluation of the Macedonian denar or appreciation of the Hungarian forint may exert a negative influence on Maktel s results that are converted into HUF. The conversion of Crnogorski Telekom s results into HUF depends on the value of the HUF against the EUR. This is mainly a reporting risk, but through the dividend payments it has direct financial (cashflow) effects on us as well.

ITEM 4 INFORMATION ON THE COMPANY

ORGANIZATION

Until May 6, 2005, the legal name of the Company was Magyar Távközlési Rt. and it operated under its commercial name, Matáv . On May 6, 2005, Magyar Távközlési Rt. was rebranded as Magyar Telekom Távközlési Rt. (Magyar Telekom Telecommunications Co. Ltd.) and its commercial name became Magyar Telekom Ltd. On March 1, 2006, Magyar Telekom changed its name to Magyar Telekom Távközlési Nyilvánosan Működő Rt. (Magyar Telekom Telecommunications Plc.).

Magyar Telekom is a limited liability stock corporation incorporated and operating under the laws of Hungary. Our shares are listed on the Budapest Stock Exchange, and our ADSs are listed on the New York Stock Exchange. Our headquarters are located at 55 Krisztina krt., 1013 Budapest, Hungary. Our telephone numbers are +36-1-458-0000 and +36-1-458-7000. Our agent for service of process in the United States is CT Corporation, 111 Eighth Avenue, New York, New York 10011, USA.

HISTORY AND DEVELOPMENT

Prior to 1990, the Hungarian national postal, telephone and telegraph authority, Magyar Posta, provided all public telephone services in Hungary. On January 1, 1990, the Hungarian government split Magyar Posta into three distinct entities based on the nature of their operations: postal services, telecommunications and broadcasting. The Hungarian government made Magyar Távközlési Vállalat, the predecessor to Matáv, responsible for telecommunications operations. This entity was transformed on December 31, 1991 into a stock corporation, Magyar Távközlési Rt., or Matáv, then wholly owned by the predecessor of Állami Privatizációs és Vagyonkezelő Rt. (State Privatization and Holding Company or ÁPV).

MagyarCom GmbH (MagyarCom), a holding company in which Deutsche Telekom and Ameritech Corporation (Ameritech) each held a 50 percent interest, was selected by the Minister in an international tender and subsequently purchased a 30.1 percent stake in Matáv for approximately U.S.$ 875 million on December 22, 1993. ÁPV contributed U.S.$ 400 million of the purchase price paid by MagyarCom to Matáv to provide it with capital to expand the telephone network.

MagyarCom entered into a concession agreement with the Hungarian government on December 19, 1993. MagyarCom then assigned certain of its rights under the concession agreement to Matáv. On December 22, 1993, Matáv entered into a concession contract (the Concession Contract) with the Hungarian government, which gave us the exclusive right to provide domestic long distance and international public telephone services throughout Hungary and local public fixed line voice telephone services in 31 of 54 Local Primary Areas for a term of eight years ending on December 22, 2001. On May 24, 1994, we obtained the right to provide telephone services in an additional five Local Primary Areas for a term of eight years ending in May 2002.

On December 22, 1995, MagyarCom acquired from ÁPV an additional 37.2 percent interest for approximately U.S.$ 852 million, raising its stake to 67.3 percent.

In connection with the Company s initial public offering in November 1997, both MagyarCom and ÁPV collectively sold 272,861,367 shares or 26.31 percent of then outstanding shares. In June 1999, ÁPV sold its remaining 5.75 percent stake in Matáv in a secondary offering.

On October 8, 1999, SBC Communications Inc. (SBC) completed its acquisition of Ameritech and thus gained control over Ameritech s 50 percent interest in MagyarCom.

On July 3, 2000, SBC sold its 50 percent ownership in MagyarCom to Deutsche Telekom, making Deutsche Telekom a 100 percent owner of MagyarCom.

On December 20, 2005, Magyar Telekom s Extraordinary General Meeting approved the decision on the merger of Magyar Telekom Plc. and TMH. The court registration of the merger took place on February 28, 2006. From March 1, 2006, Magyar Telekom is the legal successor of TMH. TMH continues its operations within Magyar Telekom under an independent brand and as an independent line of business.

On March 1, 2006, Magyar Telekom changed its name to Magyar Telekom Távközlési Nyilvánosan Működő Rt. (Magyar Telekom Telecommunications Public Limited Company) and its abbreviated name became Magyar Telekom Plc.

For the details on our principal acquisitions during the last three years, see Item 10 Material contracts .

In line with the Group s strategy of increasing its focus on service quality and operational efficiency, and taking into account the positive results from the merger of Magyar Telekom Plc. and T-Mobile Hungary, the Board of Directors proposed further integration steps within the Hungarian operations of the T-Com segment on May 25, 2007.

Emitel is a fully owned subsidiary of Magyar Telekom, offering telecommunication services in three regional service areas of South-Hungary. The company operated 72,000 lines at the end of March 2007. The increasing competition generates the need for further efficiency improvements which can be ensured through integrating the legal entity into Magyar Telekom. Following the integration, we aim to achieve increased efficiency through joint marketing, communication activities and customer relationship management, as well as simplifying the operating structure through eliminating overlaps in activities.

The activities of T-Online Hungary, also a fully owned subsidiary of Magyar Telekom, will be divided between the access business area and the content and portal area. The access business area includes internet access products such as ADSL, dial-up, cable Internet, as well as IPTV and VoIP services. Driven by the need to increase the focus on broadband services and the spread of integrated services, the Board of Directors proposed to integrate the Internet access area into the T-Com segment. The merger will allow service quality to be improved and facilitate broadband development thanks to the integrated customer service and customer relationship management, as well as ensuring increased organizational efficiency. The remaining business entity of T-Online will focus on media, content and other new business areas.

The Board proposal is subject to approval by the Extraordinary General Meeting of Magyar Telekom to be held on June 29, 2007, and the consent of the supreme bodies of the two subsidiaries. The merger process will be completed with registration by the Court of Registry. Following that, Magyar Telekom will be the legal successor of Emitel and the merged area of T-Online. As both companies are fully owned subsidiaries of Magyar Telekom, the planned steps do not require approval from the Hungarian Competition Authority.

Following the expansion of the T-Systems segment s service portfolio, particularly through the recent acquisitions of KFKI Group and T-Systems Hungary, the Company has reviewed the organizational structure of the segment. Since January 1, 2007 the T-Systems segment has consisted of three divisions Infocom, IT Infrastructure and IT Applications. The latter two encompass the activities of the current six subsidiaries, divided according to their profiles and competencies. In order to increase the segment s transparency and improve sales efficiency, the number of subsidiaries will be reduced via legal integration into the two respective divisions, thus forming two individual legal entities. The legal procedures are expected to be completed by January 1, 2008. This move will enable us to focus more efficiently on strengthening our market leadership in the info-communications service market as well as repositioning our corporate market approach as a true IT/TC provider. Operational efficiency will also be improved through the elimination of overlapping activities.

DESCRIPTION OF BUSINESS AND ITS SEGMENTS

We are the principal provider of fixed line telecommunications services in Hungary, with approximately 2.6 million fixed access lines as of December 31, 2006. We are also Hungary s largest mobile telecommunications services provider, with more than 4.4 million mobile subscribers (including users of prepaid cards) as of December 31, 2006. We hold a 100 percent interest in Stonebridge Communications AD, which controls Maktel, the sole fixed line telecommunications services provider and, through its subsidiary T-Mobile Macedonia, the leading mobile telecommunications operator in Macedonia. We also hold a 76.53 percent ownership in Crnogorski Telekom, the principal fixed line telecommunications services provider and, through its subsidiary T-Mobile Crna Gora, the second largest mobile telecommunications operator in Montenegro.

Our consolidated revenues were HUF 671,196 million (U.S.$ 3,503 million), and our consolidated net income was HUF 75,453 million (U.S.$ 394 million) in 2006.

We are a full-service telecommunications provider operating in two business segments:

Fixed Line Telecommunications Services. Our fixed line telecommunications services consist of local, long distance and international telephone as well as other telecommunications services, including leased line, data transmission, cable television and Internet services. We also provide corporate network services, system integration (SI) and information technology (IT) services, sell telecommunications equipment and offer network construction and maintenance services. We are the market leader for most of these services in Hungary.

The fixed line telecommunications service segment also includes three Macedonian companies. Stonebridge is a holding company through which Magyar Telekom controls Maktel. Telemacedonia is a management company through which Magyar Telekom provides management and consulting services to Maktel, T-Mobile Macedonia and Stonebridge. Maktel is Macedonia s leading fixed line telecommunications company. In addition, the fixed line telecommunications service segment also includes our Montenegrin subsidiary, Crnogorski Telekom. Crnogorski Telekom is the principal fixed line telecommunications service provider in Montenegro.

Mobile Telecommunications Services. Our mobile telecommunications business, TMH, is a leading provider of mobile telecommunications services in Hungary. TMH is one of three digital mobile services providers in Hungary. Since December 7, 2004, TMH also has rights to operate 3G, or Universal Mobile Telecommunications System (UMTS), mobile telecommunications services. Mobile telecommunications services have contributed significantly to our revenues.

The mobile telecommunications service segment also includes T-Mobile Macedonia, a leading mobile telecommunications services provider in Macedonia. T-Mobile Macedonia is a fully owned subsidiary of Maktel. In addition, the segment also includes T-Mobile Crna Gora, the second largest mobile telecommunications services provider in Montenegro, a fully owned subsidiary of Crnogorski Telekom.

STRATEGY

Since becoming a listed company in 1997, we have maintained our leading positions in the domestic fixed line, mobile, Internet and data businesses. We have successfully expanded into international operations through selective acquisitions, and continuously produced solid results.

The telecommunications industry is undergoing a major change globally. We have observed several long-term trends which are changing the structure of the Hungarian telecommunications market. Key drivers of the long-term trends include changes in technology (i.e., IP-based broadband products and solutions, emerging wireless broadband technologies), customer requirements (i.e., mobility and ease of use, triple-play solutions), competition and regulation (i.e., low entry barriers, new business models).

To adapt to these changes in the market, we are now moving from the traditional traffic-based revenue structure to an access-based revenue structure, which will allow us to substitute declining traffic revenues with content, entertainment and bundled access revenues. In addition, we are seeking new revenue sources by entering into non-traditional converged telecommunications markets.

Accordingly, we have redefined the focus areas of our corporate strategies to better exploit our position as the only integrated telecommunications operator with a full range of services in Hungary and the region, as well as to ensure our long-term competitiveness. Our strategies are designed to enable us to exploit and develop our extended customer base, significantly improve efficiency and capture growth opportunities.

To ensure our continuing success, we have been operating under our Value Creation Program since mid-2004. We believe that the successful implementation of this Program is critical to capturing new growth opportunities as the telecommunications market rapidly develops in new directions.

In order to continue our transformation to become a cost-efficient integrated service company in an extended market of telecommunications and converged industries we have set our strategic priorities as follows:

1. Excellence

- *Service excellence* Provide best-in-class customer care, service delivery and provisioning to our customers in order to maintain our leadership on the market

- *Broadband push* Aggressively expand broadband relations, exploit multi-access cost-efficient broadband rollout and content service

2. Efficiency

- *Operational efficiency* Exploit efficiency improvement potential in current operations and processes to improve our competitiveness

- *Integrated operations* Capture maximum revenue and cost potential in integrated operations and leverage economies of scale and synergies in a converging market

3. Expansion & Acquisition

- *Content and media* Move towards content and media businesses to support traditional access services and build new revenue streams/exploit new revenue sources

- *System integration* Focus on complex service offering via managed services, system integration and outsourcing through consultancy-based sales to corporate customers

- *New services expansion* Capture potential growth opportunities on new converged market areas by extending our service portfolio

- *International acquisitions* Seek value-creating core acquisition targets in the South-East European region with appropriate scale and leverage our regional presence

We have developed a comprehensive market-oriented program designed to improve operational performance on Group-level and in every division. Our primary focus is on the following areas of business operations:

1. Excellence

- *Service Excellence* As a service company operating on a competitive market, one of our major strategic focuses has been to maximize customer satisfaction in all areas of operation. In order to achieve further improvement in customer service, we are now developing a Group-level customer value-based Customer Relationships Management (CRM) system. Throughout the past years of servicing our mobile division, TMH has used a state-of-the-art customer value management system to track and monitor the value of each customer. We are now in the process of extending this system to Group level. This will enable us to retain and target customer segments and sub-segments even more accurately. In addition, we aim to radically improve service delivery/provisioning capabilities as it is a vital component in increasing our competitiveness.

- *Broadband Push* In 2004, we nearly doubled Hungary s Asymmetrical Digital Subscriber Line (ADSL) access base to 200,000. In 2005 and 2006, we extended our ADSL customer base further to over 500,000. As the leading broadband provider in Hungary, we are committed to accelerating growth in country-wide broadband penetration. Ongoing promotions, a new differentiated product range and innovative broadband-specific content services are being developed to generate a strong increase in demand, while strategic pricing should allow optimal subscriber and profit growth. In November 2006, we launched Internet Protocol-based TV (IPTV) services; in early 2007, we doubled bandwidths on our network by utilizing ADSL2 technology and to further boost market development by introducing naked DSL services. Also, we believe different wireless broadband technologies will play an increasingly important role in the coming years. Applying the so-called multi-access (i.e., optimal combination of different wired and wireless broadband access technologies) approach provides the most cost-efficient means to expand broadband access base countrywide. Accordingly, leveraging first mover advantage on our newly built HSDPA capacities is one of TMH s primary strategic focuses on the fast growing wireless broadband market.

2. Efficiency

- *Operational Efficiency* We plan to improve our internal efficiency by prolonging the aggressive internal cost reduction program, which has been underway for several years. A set of specific operational efficiency targets has been set in place. Our initial 2006 goal to improve the

14

efficiency of our workforce by increasing the fixed lines (B-channel equivalent) per employee ratio to over 500 (a ratio that corresponds to the best practice in Western Europe) was already reached by the end of February 2006. We are committed to further simplification and improvement of processes and connected systems, accelerating decision making and therefore speeding up time-to-market. In addition to organizational measures and process improvement, we seek cost savings by leveraging our group-wide synergies in procurement.

- *Integrated Operations* Fixed-mobile convergence is fast developing in the telecommunications industry, particularly with respect to technology, customer needs, products/services and organizational structures. Telecommunications companies are heading towards further integration of fixed and mobile businesses driven primarily by the technological developments and the increasing customer demand for integrated services. We are expecting significant value generation through the gradual implementation of the integration by seizing additional revenues and optimizing operating and capital expenses. To ensure our competitiveness and our ability to create shareholder value in the long run, we decided to merge our mobile and fixed divisions effective March 2006.

The integration of our fixed and mobile businesses will particularly enhance our competitiveness in the following areas:

- Customer care and customer service (e.g., common chain of retail stores, one-stop shopping for corporate customers and marketing); unified T-Shop retail network was successfully set up in 2006;

- Back-office and supporting systems (e.g., common use of functional services, procurement synergies, unified supporting systems);

- Network infrastructure (e.g., unified IP-based backbone network, joint platform planning and development); and

- Products and value propositions (e.g., fixed-mobile bundled products, value added services based on broadband access and content).

Customers directly experience and benefit from the expansion of the service portfolio, easier access to products, and more competitive value propositions. Exploitation of the operational synergies, streamlined organizational structures and simplified processes will improve our corporate efficiency.

3. Expansion & Acquisition

Traditional telecommunications markets of our core operations imply limited top line growth potential, whereas surrounding convergent market areas such as mass media, transactional services, commerce and info-communications (ICT) services imply stable growth over long term. Leveraging our relationship advantage, extended distribution network and strong brand awareness, we are in a strong position to enter these new markets and increase our market share in the extended marketplace. We also see significant growth potential in expanding our core operations further in the South-East European region, where we have gained hands-on experience with a good track record.

- *Content and Media* content and innovative broadband-based services play a crucial role in further enhancing broadband market development. We aim to further advance and extend our presence in this market segment. Accordingly, in April 2006, we gained control of iWiW Kft., the leading Hungarian online social network currently registering over 2.1 million users. In May 2006, we acquired Adnetwork Kft., the leading domestic online advertisement network, to leverage the online advertisement potential of T-Online and partner web pages.

- *Systems Integration* the growth potential of traditional telecommunications services in the Hungarian corporate market is limited. IT services such as systems integration, managed network services, custom application development, IT outsourcing and consultancy services are becoming the new growth drivers in the corporate market. In line with changing customer demands we believe IT services will become the new gateway to sell integrated telecommunications services, and the winning telecommunications firms in the future Hungarian corporate market will be those that establish their credentials as trusted IT/telecommunications service partners. Therefore, to maintain sustainable competitiveness in the corporate sector, we have committed to further developing our IT competencies. Acquisitions are an important part of this program, as they offer the fastest means to build our position and improve our competency mix in the corporate IT/telecommunications market. As a major provider of SI/IT services in Hungary, the acquisition of KFKI Group in June 2006 was a major step towards this initiative. In April 2006, we acquired Dataplex, a major provider of ICT infrastructure outsourcing. Also, by acquiring additional two percent of T-Systems Hungary in January 2007, we are now the majority stakeholders of the company.

- *New Services Expansion* to further leverage our core assets we are continuously exploring emerging business possibilities on new converging markets through expanding our service portfolio. We are considering entering new market segments such as transactional services and commerce to generate new revenue streams in case a potential business opportunity is arising.

- *International Acquisitions* We acquired a 51.12 percent stake in Crnogorski Telekom from the government of Montenegro in March 2005. At the same time, we acquired an additional 21.92 percent of Crnogorski Telekom s shares from minority shareholders. As a result of a public offer, we acquired an additional 3.49 percent stake in Crnogorski Telekom, increasing our stake to 76.53 percent by May 24, 2005. In February 2006, we acquired a 100 percent stake in a Bulgarian alternative fixed line telecommunications and Internet services provider, Orbitel. Leveraging our hands-on experience and good track record in the region, we are committed to further strengthen and leverage our presence in the South-East European region. Accordingly, we are continuously seeking further value-creating acquisition and investment targets with even larger scale.

OVERVIEW OF MAGYAR TELEKOM S REVENUES AND PRINCIPAL ACTIVITIES

For the years ended December 31, 2004, 2005 and 2006, our total revenues by business segments were as follows:

	Year ended December 31, 2004 (in HUF millions)	2005	2006	Year ended December 31, 2006/2005 (% change)
Revenues				
Fixed line Hungary	298,707	284,985	292,193	2.5
Fixed line Foreign operations	45,693	57,983	68,953	18.9
Total	344,400	342,968	361,146	5.3
Less: intra-segment revenue	(1,271)	(2,284)	(3,569)	56.3
Total revenue of Fixed line segment	343,129	340,684	357,577	5.0
Less: revenue from Mobile segment	(11,146)	(11,478)	(13,711)	19.5
Fixed line revenue from external customers	331,983	329,206	343,866	4.5
Mobile Hungary	260,568	266,217	297,209	11.6
Mobile Foreign operations	33,734	42,693	52,399	22.7
Total	294,302	308,910	349,608	13.2
Less: intra-segment revenue	(58)	(27)	(42)	55.6
Total revenue of Mobile segment	294,244	308,883	349,566	13.2
Less: revenue from Fixed line segment	(29,435)	(23,035)	(22,236)	(3.5)
Mobile revenue from external customers	264,809	285,848	327,330	14.5
Total revenue of the Group	596,792	615,054	671,196	9.1

Most of our revenues in 2004, 2005 and 2006 were derived from services provided within Hungary, except for the international fixed line and international mobile revenues, which were mainly derived from services provided in Macedonia in 2004, and in Macedonia and Montenegro in 2005 and 2006.

Our business is not materially affected by seasonal variations.

FIXED LINE TELECOMMUNICATIONS SERVICES SEGMENT

In 2006, our fixed line telecommunications services generated revenues of HUF 357,577 million before inter-segment eliminations. Fixed line telecommunications services consist of domestic and international services, Internet services, data transmission, SI/IT services, cable television, multimedia and telecommunications equipment sales, as well as construction, maintenance and other services.

The Hungarian fixed line operations include activities of Magyar Telekom in Hungary and South-Eastern Europe. Magyar Telekom provides international network and carrier services in South-Eastern Europe through Points of Presence (PoPs). Magyar Telekom entered the Romanian market in July 2004, the Bulgarian market in September 2004, and the Ukrainian market in August 2005 to offer various wholesale services. Capitalizing on our experience in these markets, we have entered into the retail market segment in Romania with a full service portfolio and intend to do so in Bulgaria and Ukraine as soon as the regulatory environment becomes favorable.

Hungarian Fixed Line Operations

Domestic Services

Revenues from domestic fixed line telephone services consist of:

- subscriptions, connections and other charges;
- outgoing domestic traffic revenues; and
- incoming domestic traffic revenues.

Products and Services

Local and Long Distance Telephone Services. We provide local, domestic and international long distance telephone services to our fixed line subscribers and to fixed line subscribers in other Local Telecommunications Operator (LTO) areas.

Public Switched Telephone Network (PSTN). Due to the fierce competition and mobile substitution, the number of our PSTN lines decreased from 2,252,943 as of December 31, 2005 to 2,158,547 as of December 31, 2006.

Integrated Services Digital Network (ISDN). ISDN allows a single access line to be used simultaneously for a number of purposes, including voice, data, facsimile and video transmission. We offer both basic ISDN access lines with two channels and multiplex ISDN access lines with 30 channels. As of December 31, 2006, we had installed 171,995 ISDN access lines with two channels and 4,710 ISDN access lines with 30 channels, for a total of 485,290 ISDN channels. We intend to extend the life cycle of the ISDN product in the business segment by offering various discounts to our customers.

Digifon Services. At the end of 2005, our network was 100 percent digitalized, which enable us to provide value added services in our entire service area. We provide a number of value added services, such as call forwarding, call waiting, call conference and caller number identity to a significant number of our fixed line subscribers. These services help increase fixed line usage as they make busy signals and unanswered calls less common. We also offer bundled packages of digifon services, including Digifon Home, Digifon Business, Összhang and Visszhang. The most popular of these packages is the Összhang, which contains five services at a discount price. Összhang package had approximately 265,000 customers by the end of 2006.

Shared Cost/Toll Free Numbers. The reverse charged numbers (blue and green) are primarily used by business customers leveraging the service benefits in the course of their business operations. The customer base and the usage volume of this service are stable. In line with international regulations, we ensure the international availability of reverse charged numbers both from fixed line and mobile networks.

Voice-mail. We offer a voice-mail service including call return and call capture. We also offer voice-mail Short Message Service (SMS), which provides an SMS alert to the mobile handset of the customer each time he or she receives a voice-mail message. These services allow better usage of the network, provide convenience to our customers and decrease the ratio of uncompleted calls.

Fixed SMS. From a fixed line terminal, short text messages can be sent with an SMS-capable telephone and SMS termination is available for every subscriber. If the addressee does not have an SMS-capable telephone, the text message is converted and sent as a voice message. In December 2005, we launched a new platform for the fixed SMS service, resulting in higher service quality. From 2006, our clients are able to send fixed SMS to all domestic fixed and mobile operators network. In addition, the increasing number of SMS-capable telephone sets also contributed to

our revenue growth in 2006.

Private Branch Exchange (PBX) Services. We offer PBX services through one of our subsidiaries, BCN Rendszerház Kft. (BCN Kft.). The vast majority of the leased equipment is digital and meets the demands of developing technologies such as ISDN and digitally enhanced cordless telecommunications.

Directory Assistance. We offer directory inquiry services. The domestic directory assistance database includes all fixed line and postpaid mobile subscribers data in Hungary. We offer a call completion option to subscribers, whereby calls may be connected automatically. We also offer increasingly popular Directory Assistance-Plus (DA-Plus) service. DA-Plus offers a wide range of information including Yellow Pages, residential classified advertisements, encyclopedia- and dictionary-based information, recipes, poems, as well as telephone numbers, postal, e-mail and website addresses without any quantity restrictions. The requested information may be provided verbally, by SMS, by e-mail or by fax. The fees for the service are based on per minute usage. We also offer a call completion option to the subscribers of DA-Plus.

Subscribers

The following table sets forth information regarding total fixed access lines and penetration rates in the service areas of Magyar Telekom Plc. and Emitel:

	At December 31, 2004	**2005**	**2006**
Number of fixed lines			
Residential lines	2,080,408	1,981,876	1,902,011
Business lines	263,889	248,955	236,019
Public payphones	27,818	22,112	20,517
Total	2,372,115	2,252,943	2,158,547
ISDN channels	530,250	500,696	485,290
Total	2,902,365	2,753,639	2,643,837
Lines installed per 100 residents in the service areas of Magyar Telekom Plc.	37.5	35.6	34.2
Digital exchange capacity as% of Magyar Telekom Plc. s total exchange capacity	92.9	100	100

Our domestic fixed line subscribers can be classified into two categories: residential customers and business customers, which include our customers in the public sector. As of December 31, 2006, 74 percent of our access lines was utilized by our residential customers and 25 percent by our business customers. The remaining one percent of access lines was used for public payphones.

The Hungarian government, through its various institutions and departments, constitutes our largest customer group. We develop separate service packages for each of these institutions and departments, as each of them generally has its own annual budget, particular telecommunications needs and responsibilities. From a strategic perspective, however, we consider the Hungarian government a single customer. We offer most of our largest customers, including the government, discounts for services we provide.

Fees and Charges

We charge fixed line subscribers a one-time connection fee, monthly subscription charges and call charges based on usage. A call charge contains two elements: a call set-up charge and a traffic charge measured in seconds based on the call s duration. In accordance with the Act LXXXVII of 1990 on Pricing (the Pricing Act), as modified by the Electronic Communications Act, the Minister, together with the Minister of Finance, is responsible for establishing the maximum rates for universal services. We may, however, offer services at prices lower than those established by the Minister.

Our one-time connection fee and monthly subscription charges are different for residential and business customers. We do not, however, charge our business and residential customers different traffic charges if they use the same price plan.

In 2006, we increased the number of price plans to allow customers in different market segments to choose plans that best suit their calling patterns. These price plans also serve as a tool to maintain our customer base in the fully liberalized market as those customers who select us as the operator for every traffic direction (local, long distance and international) receive the highest discounts. In 2005, we introduced flat rate price plans that offer free unlimited calls to customers during a certain period of the day for an additional monthly fee.

As a result of the VAT reduction in January 2006, the consumer prices decreased. At the same time, we decreased the minute fees of the Felező price plan, thus we managed to create an even more attractive product. In May 2006, within the framework of our flat rate program, we introduced offers containing no time limitation on usage. During 2006, the fixed-mobile bundled offers proved to be successful customer retention tools. In November 2006, we developed a price plan with a monthly fee that can be fully offset by call charges. This product (Total price plan) proved to be very successful and generated more than 80,000 subscribers by December 31, 2006. By the end of 2006, Favorit and Felező price plans attracted the highest customer base, with 550,000 and 539,000 subscribers, respectively.

We target business customers attacked by the mobile substitution (especially fleet offers) with our business flat rate price plans, which are transparent and easy to budget. It is designed to retain fixed line traffic, to stop the increasing erosion, and to provide an opportunity for the reacquisition of traffic that we lost due to pre-selection. Customers of flat rate price plans can use our network for local, domestic, and long distance calls for a fixed monthly fee. We also offer flat rate price plans with options for mobile, international or LTO calls.

We introduced two products in our new business flat rate portfolio (Grátisz 100, Grátisz 500) as well as optional supplementary price plans for mobile and international flat rate calls. These plans proved to be successful tools for traffic retention in the business segment. At the end of 2006, we had 25,000 subscribers for the Grátisz 500 and 12,000 subscribers for the Grátisz 100 price plans.

Public Telephones

As of December 31, 2006, Magyar Telekom operated 20,517 public payphones. The call charges for calls from public payphones are at a premium to those charged to fixed line subscribers.

International Telephone Services

International telephone services consist of outgoing and incoming international calls, including voice and switched transit traffic through Hungary.

Products and Services

We provide international calling access to our fixed line subscribers and to subscribers of other local telephone operators and mobile service providers. Our Hungary Direct and Country Direct services permit customers to charge calls made from 50 foreign countries to their home phone numbers in Hungary.

International toll free service was launched in 1998. This service enables the caller to make international calls free of charge to and from 38 countries, while the subscriber of the toll free number is billed for these calls. Universal international toll free service was launched in 2003. This service enables the subscriber to be called free of charge from 22 foreign countries with the same telephone number.

In June 2000, we introduced the international prepaid calling card, Barangoló, which allows customers to make phone calls, including IP-based calls, in 40 countries. This service enables customers to make international calls from touch-tone payphones in Hungary and abroad.

Fees and Charges

The call charge for an international call consists of two elements: a call set-up charge and a traffic charge measured in seconds based on the call s duration. Although the published prices of our international rates did not change in 2006, the average per minute rates decreased as a result of discounts given in various optional price plans.

Settlement Arrangements. Under bilateral settlement arrangements, we pay other carriers for the use of their networks for outgoing international calls and receive payments from other carriers for the use of our network for incoming international calls. In Europe, such settlement arrangements fall under the general auspices of the International Telecommunications Union. Settlement payments are generally denominated in Special Drawing Rights (SDR), based on a currency basket in which U.S. dollars have the greatest weight. Due to the large exchange rate fluctuations of the SDR caused by the recent volatility of the U.S. dollars, we started to shift our accounting rate agreements to euro-based arrangements. Most new international carrier partners prefer to use the euro as a settlement currency.

International Telecommunications Hub

We believe that Hungary is geographically well positioned to serve as a telecommunications gateway between Eastern and Western Europe. We have two state-of-the-art international gateways as well as fiber optic cable connections serving 25 border crossings. These fiber optic cable connections use synchronous digital hierarchy transmission facilities and we have launched our own Dense Wavelength-Division Multiplexing (DWDM) backbone network. To increase the utilization of our transmission network, we offer attractive price schedules for dedicated transit services through Hungary. We are DT s partner in Delivery of Advanced Network Technology to Europe (DANTE), which provides transmission paths interconnecting Bucharest (2x622 Mbit/s) and Sofia (2x155 Mbit/s) to the European research and educational network, GEANT through their Budapest node.

We have X.25 links, which are used for packet switched data transmission with 83 international networks. We also have ISDN connections with 50 international networks.

To seize the opportunities presented by the liberalization of the telecommunications market in Romania, we established interconnection arrangements with major Romanian alternative service operators and network service providers to offer transit services to Western Europe. In addition, we use our own point of presence in Austria, which enables us to engage in telephone and Internet business with alternative telecommunications carriers located in Vienna. We provide Internet transit service to several Romanian and Bulgarian ISPs on our two IP PoPs in Romania and high-capacity international Internet transit service on our IP PoPs in Hungary to ISPs in Ukraine and Macedonia.

Internet Services

T-Online Hungary, our fully-owned ISP subsidiary, offers Internet services based on dial-up, ADSL technology as well as access through cable television, Wireless Local Area Network (WLAN) and leased lines to provide residential and business customers with narrowband or broadband Internet services at affordable prices.

In 2006, T-Online Hungary increased its subscriber base by 30 percent to 427,000. T-Online Hungary is the largest Internet service provider in Hungary with an estimated 39 percent market share based on the number of dial-up subscribers. The number of T-Online Hungary s broadband (ADSL, cable television,

WLAN and leased line) customers reached 395,599 as of December 31, 2006 compared to 247,597 a year earlier.

In 2006, the number of Internet users increased significantly. By the end of 2006, approximately 23 percent of Hungarian households were connected to the Internet compared to 19 percent at the end of 2005. T-Online Hungary is committed to accelerating Internet penetration growth and has invested a significant amount of resources to develop attractive and innovative content, such as T-Home TV.

In 2006, T-Online Hungary and Magyar Telekom Plc. introduced an IPTV service. IPTV allows broadcasts to be seen on a television set with a set-top-box over ADSL connection. The new product line offers various interactive contents, such as time-shift function, program-magazine on screen, recording onto the hard disc built in the set-top-box, video library and picture in picture. T-Home TV is available in six large cities in Hungary.

The joint product of T-Com (the residential Line of Business of Magyar Telekom) and T-Online Hungary, Klip offers VoIP services via broadband access. Users of Klip can initiate and receive calls for free via the Internet, to both fixed line and mobile networks. Klip users can also be called from T-Com s fixed network. The product, launched at the end of 2005, already had more than 58,000 registered users at the end of 2006.

Magyar Telekom ADSL. ADSL is a continuous, high-speed Internet access service based on the Asymmetric DSL technology. The service offers cost-efficient broadband Internet access together with telephone service over existing copper wires. We sell these services mainly on a wholesale basis to ISPs, which in turn resell the services to residential and small business customers. At the end of 2006, we had contractual relationships with 22 ISPs. In 2006, this service saw a significant growth with the number of ADSL connections reaching 512,810 by December 31, 2006 from 329,314 at December 31, 2005.

In 2006, we implemented an infrastructure expansion project. A large amount of investment was used for the roll-out of broadband Internet. As a result of these steps, over 150 additional settlements were connected to the service in 2006, exceeding 1,000 connected settlements by December 31, 2006.

T-Com ADSL (T-DSL). We offer voice and Internet bundles (T-DSL) for both residential and business costumers. Residential T-DSL price plans contain telephone line with flat voice and a flat Internet access. Our objective is to expand the broadband Internet market aggressively. To support this goal, we launched a free service trial period (Try&Buy ADSL campaign) in 2006. After the free trial period, 49 percent of the customers subscribed for commercial ADSL.

ADSL2+. On June 1, 2006, we introduced a number of new commercial products based on ADSL2+ technology, providing two broadband packages to the ISP partners with a maximum download bit rate of 12 Mbit/s and 18 Mbit/s, a bit rate much higher than before. ADSL2+ packages were available in 791 settlements by December 31, 2006.

T-Com HotSpot. T-Com HotSpot is a wireless broadband Internet solution, based on the WiFi technology for public sites (i.e., hotels, conference centers and restaurants). The HotSpot payment methods include T-Com HotSpot prepaid card and subscription packages (HotSpot 180). The T-Com HotSpot service is also available for T-Online Hungary s Internet access subscribers, for whom the usage fee is paid through T-Online Hungary s Internet access monthly bill. Customers with a valid T-Mobile HotSpot access identification may also use the T-Com HotSpot service. The HotSpot service is also available online by bank card payment. At the end of 2006, there were 354 public HotSpot sites in operation (113 hotels, 17 T-Ponts and 224 others).

T-Com Open Internet. T-Com Open Internet is our dial-up Internet service. To use the service, customers do not need to sign a contract or register and no monthly fees need to be paid. The minute fee of the usage is paid on the telephone bill. The low fees, the ease of use and setup make this service an optimal choice for inexperienced Internet users. This dial-up service also provides for us a potential base for broadband migration. At the end of 2006, there were more than 60,000 customers using Open Internet.

Data Transmission and Related Services

We are the principal provider of leased lines in Hungary.

Leased line service establishes a permanent connection for transmission of voice and data traffic between two geographically separate points (point-to-point connection) or between a point and several other points (point-to-multipoint connection). These points can be either all within Hungary or some in Hungary and others abroad.

We lease lines to other local telephone operators and mobile service providers, who use such lines as part of their networks. We also lease lines to providers of data services. In addition, we lease lines to multi-site business customers who use leased lines to transmit internal voice and data traffic.

We offer a broad variety of standard analog and digital lines for lease, including two-wire and four-wire analog lines and digital lines with capacities from 64 Kbit/s to 155 Mbit/s. We also offer high capacity customized digital lines to other telecommunications providers.

Flex-Com. We offer Flex-Com, domestic and international digital leased lines with managed back-up systems that are dedicated to data transmission. The number of Flex-Com connections decreased from 10,289 as of December 31, 2005 to 9,165 lines as of December 31, 2006. However, during the same period the aggregate sum of the bandwidths of the connections has increased by 11.3 percent from 3.46 Gbit/s to 3.85 Gbit/s, which led to higher revenues.

High Speed Leased Line (HSLL). The HSLL service provides permanent, digital, transparent, point-to-point leased line service between service access points (SAPs). The connections are established by a service provider according to the needs of its customers. Transmission rates provided by the HSLL service are 2, 34, 45, 140 and 155 Mbit/s. We increased our HSLL connections from 1,355 at December 31, 2005 to 2,493 by December 31, 2006.

As an addition to the HSLL portfolio, we offer a WDM technology-based premium service, Gigalink, which provides leased line service at a higher speed (622 Mbit/s) to business customers and to other service providers. For the Campus backbone network (a link between universities and academic institutions) we offer Gigalink service up to 10 Gbit/s speed.

Datex-P. We offer Datex-P, a packet-switched data transmission service based on the X.25 protocol. The service provides low to medium speed domestic switched data communications services with international connectivity to business customers. As a result of the proliferation of new technologies, growth in the number of subscribers has stopped. Between 2003 and 2005, our major objectives were to extend the lifecycle of the product, maintain profitability, optimize the network and reduce costs. In 2005, we assessed and commenced migration of customers to other data transmission services. In 2006, we introduced a flat rate price plan and widened the access option by Ethernet interface.

Our leased line customers pay a one-time connection fee based on the type of line leased. Monthly subscription charges vary with the type and length of lines leased and, in some cases, with the term of the lease. With the exception of leased lines required for connection with other networks, leased line charges are not subject to regulation. As part of the overall rebalancing of our rates, we have reduced our leased line charges in real terms over the last few years in response to competition, which partly offset the revenue increase generated by volume and bandwidth increases of the leased line services.

Data transmission and related services consist primarily of data transmission and network services for business customers, such as financial institutions and insurance companies, and, to a lesser extent, residential customers. The market for data transmission and related services in Hungary is highly competitive. We are the leading supplier of data transmission and related services in Hungary.

Our revenues from data transmission have grown significantly as a result of both the development of the Hungarian economy and our increasingly sophisticated services. We expect the market for these services to grow with the proliferation of personal computers and increasing consumer demand. We believe that the ability to offer new data products and services will be critical to competing effectively in the future, particularly with respect to business customers.

Magyar Telekom DataLink. In 2004, we launched a new data transmission product that offers technology independent data transmission between business customers locations. The customer only needs to define three main parameters, bandwidth, Service Level Agreement (SLA) and interface. This service provides data connection below 2 Mbit/s, with X.21 or Ethernet interfaces. With the introduction of this service, we can better utilize our spare data transmission capacity.

IP Connect. IP Connect service, a complete solution for ISPs providing transport and access facilities to IP traffic, includes the provision of ports in the service area, required for the subscribers of ISPs to dial-in from analog or ISDN lines. The service also enables leased line access, and ensures that traffic will be forwarded to both domestic and international switches as well as to the domestic switch of a particular ISP. The domestic switch of the ISP is connected to our IP network via a leased line. To maintain our market share and competitive position, a new product offering, called Symmetrical Internet was introduced in 2003, which includes access and IP/Internet service. After the introduction of this new service, many of our customers switched from IP Connect to Symmetrical Internet.

IP Complex Plus. IP Complex Plus is an IP-based Virtual Private Network (IP-VPN) service. IP Complex Plus service is offered to retail and wholesale customers having multiple remote sites. This service enables them to establish secure data traffic between sites without the need of setting up point-to-point connections between two sites. The development of supplementary services, such as ISDN back-up, integrated voice/data, ADSL/Single-Pair High-Speed Digital Subscriber Line (SHDSL) access and dial-up access to IP-VPNs make this product more attractive to a growing number of business customers. In addition to the current function of integrated voice/data service, we provide number portability for our IP Complex Plus customers. Using this new service, customers can use their existing phone numbers within their private network as well. In 2007, we intend to extend our portfolio with new access technologies, which enable our customers to connect to the IP network with a speed up to 1 Gbit/s.

International data products. We provide signaling links for mobile operators to facilitate international roaming. We also sell international leased lines, including international managed leased lines, international ISDN, X.400, X.25 and telegraph services. The sales of international leased lines are steadily growing, partly due to the introduction of one-stop-shopping agreements, whereby customers can order from and pay for the service at one end-point of the connection, which eliminate the need to deal with multiple service providers. International Internet connectivity was enhanced in 2004 to provide services for Internet service providers. By the end of 2004, the capacity of international Internet connections reached 3 Gbit/s.

System Integration and Information Technology

In June 2006, we acquired one of the leading Hungarian IT companies, KFKI Group with the aim of becoming the leading system integrator in Hungary and we increased our share in T-Systems Hungary to 51 percent on January 1, 2007. As a result of these acquisitions, IT equipment and IT services revenues will represent a significant part of our revenues in the coming years.

We were able to achieve significant increase in the sales of complex ICT solutions, outsourcing and managed services. In cooperation with business partners, we also sell the products and services of our subsidiaries (e.g., BCN, Integris, KFKI) and external market partners (e.g., Cisco) to our customers.

The most successful product was our Outsourcing Business Model. In 2006, we concluded several contracts to provide outsourcing services to our strategic customers (e.g., Budapest Bank, Inter-Európa Bank, Allianz, E.ON). In addition, we experienced high customer demand in the sales of IP telephony, complex solutions, flat rate price plans and bandwidth expansion. The set-up of low current systems and the sales of IT solutions also showed a significant increase. The most important project in this field related to the Electronic Government Backbone Network (EKG).

E-Learning. We provide e-learning solutions for employees or private individuals via Internet and private networks (LAN, Intranet, etc.). This service proved to be a cost efficient solution for both the training organization and the user.

E-Municipality. Our aim is to establish electronic governments that support information access, provide Internet-based public administration, create an open and transparent public sphere and support competitiveness through efficient village marketing. This solution includes both IT hardware and software elements as well as ICT applications combined with project management.

Távszámla (Electronic Bill Presentment and Payment). This service replaces the use of paper-based invoices, as it connects the invoice issuer and the invoice payer via Internet. The system includes the presentment and the payment solution for invoices. For all these functions, the users need only a PC with Internet access. After a successful registration, the invoices can be viewed and paid immediately. In addition to telephone, Internet, mobile and cable TV invoices issued by Magyar Telekom, Távszámla became available for E.ON customers in 2006.

Public Administration e-Signature. The Public Administration Procedure Act, which came into effect on November 1, 2005, provides the facility to use e-Signature (tax return submission, passport requests, etc.) and stipulates extra demand for the authentication services. In 2006, we improved our certified e-Signature service and introduced it to the government authority. NHH audited and assessed us as a certified authentication service provider from March 20, 2007.

rEDInet. This service allows editing of business documents electronically, quickly, accurately, remotely and with full security. The technology behind the Electronic Data Interchange (EDI) service is used worldwide. We also provide professional training and consultation services to the users of our rEDInet service. The rEDInet offers EDI service for the Hungarian Fast Moving Consumer Goods (FMCG) sector and for suppliers of European car factories. In recent years, the growth of the traditional EDI market has slowed down in terms of new participants, but the number and type of transferred messages are growing. Further growth will be realized with the introduction of e-invoice solutions and Internet-based services with lower costs. E-invoicing is supported by the approved regulation of EDI-based invoices. The Internet-based solution allows customers of the Small Office/Home Office (SOHO) and Small and Medium size Enterprises (SME) segment without IT background to become a member of the electronic trading community. For our customers and other service providers we introduced Virtual Private Network (VPN) access via Internet.

Managed Services. In 2006, we introduced the Managed Services portfolio with three pillars. Depending on the success of the current portfolio, we intend to develop the Managed Desktop as the fourth pillar.

- Managed Voice. The Managed Voice service provides a solution for turn-key VPN development and operation as well as voice traffic based on the data infrastructure of our partners. The service is based on the operation of a full infrastructure specifically created for this purpose, including integrated data and voice transmission via MultiProtocol Label Switching (MPLS) network to

25

forward IP-packet information and connections with public networks. In addition to using the Managed LAN service, this solution enables the comprehensive management of all network elements.

- Managed LAN. The Managed LAN service is a provisioning and support solution that manages data lines and the connected local networks. Within the framework of the solution we also provide local network infrastructure development and operation as well as continuous supervision with national coverage and proactive fault repair in order to help our customers in their network management related tasks.

- Managed Security. The Managed Security service includes the development and operation of the protection of IT infrastructure through local or centralized supervision. This service covers the Internet access and the related local networks comprehensive protection systems. It is able to guarantee continuous and undisturbed data communication, uninterrupted and authorized access and the enforcement of the corporate security policy and rules of operation.

Multimedia

Our cable television (CATV) group consists of two entities providing various cable television services in Hungary. The larger entity is T-Kábel Hungary, which began providing cable television services on January 1, 1999.

Through network development and acquisitions, our CATV group significantly increased its number of cable television customers during the past years. We are the second largest cable television provider in Hungary with a market share of about 19 percent. The growth of subscribers has slowed down in the past two years. The CATV group had approximately 414,000 subscribers as of December 31, 2006 compared to approximately 404,000 a year earlier.

T-Kábel Hungary offers 45 analog television channels in three program packages and 17 radio stations in most of its networks. Premium digital television services are available in the product portfolio since December 2005. As of December 31, 2006 more than 13,000 packages were subscribed to from the 31 digital channels offered in 11 mini program packages. At the end of 2006, T-Kábel Hungary also launched digital simulcast of television channels of two of its three analog program packages in Budapest and in its vicinity.

Our CATV firms in cooperation with ISPs offer broadband Internet services. Partly due to the enlargement of the area with bidirectional data transmission network capability, the number of broadband Internet subscribers through our cable television networks substantially increased to approximately 63,000 on December 31, 2006 compared to 29,000 a year earlier. During 2006, T-Kábel Hungary more than doubled the number of its VoIP service (Kábeltel) customers to over 28,000 subscribers as of December 31, 2006.

T-Kábel Hungary s cable television activities benefit from our long-term relationship with the customers, our thorough market knowledge as well as our strong brand name, and further synergies have been mutually utilized. Our main goals in this area are to increase market share through acquisitions, to connect new customers in the existing service areas, to broaden the product portfolio, to improve the quality of and further extend the enhanced technical capabilities of the networks, to enlarge the coverage of triple-play offering capabilities and to increase Average Revenue per User (ARPU).

Fixed Line Telecommunications Equipment Sales

We distribute an extensive range of telecommunications equipment, from individual telephone sets to facsimile terminals, PBXs and complete network systems, through a network of customer service centers. In addition to stand-alone telephone-set sales, we offer various packages combining telephone sets with telephone lines and price plans.

We do not manufacture telecommunications equipment but resell and lease equipment manufactured by other companies.

The telecommunications equipment sector is highly competitive and characterized by rapid technological innovation. We believe that the supply and service of telecommunications equipment are integral element of a full service telecommunications provider and are necessary for the expansion of our customer base. In addition, these activities allow to ensure that technologically advanced equipment required for new services is available in Hungary.

Other Revenues

Other revenues include construction, maintenance, rental, wholesale infrastructure services and other miscellaneous revenues.

We construct fixed line telecommunications networks and offer network maintenance services to other telecommunications operators in Hungary. These construction and maintenance services are ancillary to the construction and maintenance of our networks.

Magyar RTL Televízió ZRt. (M-RTL) is a Hungarian television broadcast company, in which Magyar Telekom has a 25 percent effective share through a holding company, IKO-Telekom Média Holding ZRt. M-RTL is entitled to provide commercial television programs but not to engage in broadcast diffusion or distribution activities. M-RTL has a concession for a period of ten years with an option for a five-year extension. The Program Provision Agreement was signed on July 9, 1997, being the starting date of the license. On July 20, 2005, M-RTL has extended the license for an additional five years which will be effective from July 10, 2007. M-RTL operates a channel under a brand name, RTL KLUB.

Since its launch in 1997, RTL KLUB has rapidly established a strong position in Hungary s television market, being the market leader for the last six years. Market share among the targeted age 18-49 audience remained stable, 29 percent in 2006 compared to 31 percent in 2005 for the whole day and 34 percent in 2006 compared to 37 percent in 2005 for the prime-time (between 7 and 11 p.m.). M-RTL has successfully converted its leading audience result into television advertising market share.

RTL KLUB seeks to maintain and increase audience share through investing in local productions, as well as successful internationally licensed programs, and through its continued long-term relationships with major film distributors, including Warner Brothers, Fox, Buena Vista and Columbia. M-RTL is strategically concentrating on sport events, such as Formula One races, Paris-Dakar rally and boxing.

International Fixed Line Operations

Macedonian Fixed Line Operations

We fully own a Macedonian holding company, Stonebridge, which owns a 51 percent interest in Maktel. Magyar Telekom has commenced a liquidation procedure of Stonebridge in accordance with the relevant Macedonian laws. Once the process is complete, Magyar Telekom will directly own its shares in Maktel, thus simplifying the ownership structure.

Maktel is the primary fixed line service provider in Macedonia. Its exclusive rights in fixed line telecommunications services expired in December 2004. These exclusive rights included local, national and international long distance public telephone services, VoIP services, leased line services and building and operating public telephone network services.

Subscribers

The following table sets forth information regarding the total fixed access lines and penetration rates of Maktel:

	At December 31,		
	2004	2005	2006
Number of fixed lines			
Residential lines	524,722	467,559	430,082
Business lines	56,329	48,252	42,780
Public payphones	2,725	2,063	2,087
Total	583,776	517,874	474,979
ISDN channels	42,082	41,262	42,200
Total	625,858	559,136	517,149
Lines installed per 100 residents in the service areas of Maktel	29.0	26.0	23.9
Digital exchange capacity as% of Maktel s total exchange capacity	100	100	100

Maktel has a 94 percent market share in the Macedonian Internet market. The number of Internet subscribers is gradually increasing. Maktel provides Internet access via the public switched telephone network, leased lines and ADSL. By the end of 2006, Maktel had 125,699 Internet customers, including 16,462 ADSL connections compared to 91,865 Internet customers, including 7,798 ADSL connections at the end of 2005.

Historically Maktel, like government-owned operators in other countries, maintained relatively low domestic charges and high rates for international calls. Since November 1999, however, Maktel has been gradually rebalancing its rates. International rates are expected to decrease further, bringing them in line with the EU standards. Local rates and basic access charges are expected to increase.

Montenegrin Fixed Line Operations

Following a successful privatization tender, between March and May 2005, Magyar Telekom obtained a 76.53 percent interest in Crnogorski Telekom.

For details on the Crnogorski Telekom acquisition, see Item 10 Material contracts .

Crnogorski Telekom is the principal fixed line service provider in Montenegro. Its exclusive rights in fixed line telecommunications services expired in December 2003. Crnogorski Telekom provides local, national and international services, in addition to a wide range of telecommunications services involving leased line circuits, data networks, telex and telegraph services.

For the past three years, Crnogorski Telekom s major operational goals were to digitalize the fixed line network and to increase the number of subscribers and access to broadband services. The digitalization rate reached nearly 100 percent by the end of 2006.

On June 26, 2006 the Shareholders Assembly of Telekom Montenegro approved the proposal of the Board of Directors to adopt the T brand in the Montenegrin market. On September 26, 2006, the fixed line operations became T-Com Crna Gora (T-Com CG) and the mobile business changed its name to T-Mobile Crna Gora (T-Mobile CG), while the fixed line parent company and the group was renamed to Crnogorski Telekom.

Subscribers

The following table summarizes key operational information of Crnogorski Telekom:

	At December 31, 2004	2005	2006
Number of fixed lines			
Analog lines	n.a.	175,122	173,248
ISDN channels	n.a.	18,750	21,288
Total	n.a.	193,872	194,536
Lines installed per 100 residents in the service areas of Crnogorski Telekom	n.a.	31.2	31.4
Digital exchange capacity as% of Crnogorski Telekom s total exchange capacity	n.a.	99.9	99.9

Through its wholly-owned subsidiary, Internet Crna Gora, Crnogorski Telekom has a 98 percent market share in the Montenegrin Internet market. Internet Crna Gora, in cooperation with Crnogorski Telekom, is the sole provider of ADSL in Montenegro. The time spent on dial-up Internet shows erosion, due to ADSL substitution and increase in dial-up tariffs in January 2006, while the number of active customers is stable. Internet access is provided via the public switched telephone network, leased lines and ADSL. Crnogorski Telekom group had 25,669 active dial-up Internet customers by the end of 2006. Crnogorski Telekom increased the number of ADSL customers from 1,085 at the end of 2005 to 6,639 at the end of 2006.

Similarly to other fixed line service providers before privatization, Crnogorski Telekom maintained relatively low domestic charges and high charges for international calls. In December 2004, Crnogorski Telekom made the first rebalancing step according to the rebalancing roadmap adopted by the Montenegrin Agency of Telecommunications. International charges are expected to decrease further while local charges and basic access charges are expected to increase.

In order to improve efficiency, in June 2005, Crnogorski Telekom offered severance packages for employees leaving voluntarily with the goal of reducing Crnogorski Telekom work force by approximately 250. This program was successfully completed by the year-end significantly reducing Crnogorski Telekom s labor costs. By the end of 2006, Crnogorski Telekom set up a technological surplus program which identified approximately further 270 employees to be made redundant in 2007. The program was agreed upon with the trade unions of Crnogorski Telekom.

MOBILE TELECOMMUNICATIONS SERVICES SEGMENT

Our mobile telecommunications services generated revenues of HUF 349,566 million in 2006 before inter-segment eliminations.

Hungarian Mobile Operations

We provided mobile telecommunications services in Hungary through our wholly-owned subsidiary, TMH (previously: Westel Mobil Távközlési Rt., Westel) prior to the merger of Magyar Telekom and TMH, which is described below.

As of December 31, 2006, TMH accounted for an estimated 44.5 percent of the total Hungarian mobile market in terms of subscribers based on the number of active Subscriber Identity Module (SIM) cards. The penetration rate of mobile telephone services in Hungary increased from 86.4 percent at December 31, 2004 to 99.0 percent at December 31, 2006.

On October 6, 2005, in line with Magyar Telekom s medium-term strategy announced in 2004, Magyar Telekom s Board of Directors made a proposal for the merger of Magyar Telekom and TMH. On December 20, 2005, Magyar Telekom s Extraordinary General Meeting approved the decision on the merger of the two companies.

The court registration of the merger took place on February 28, 2006. From March 1, 2006, Magyar Telekom is the legal successor of TMH. TMH continues its operations within Magyar Telekom under an independent brand and as an independent business segment.

In 2006, TMH was the first mobile operator in Hungary to launch HSDPA service. TMH also launched new data products, like web n walk and mobile Internet-based on HSDPA. TMH reached 30.3 percent HSDPA coverage based on population, which is a quite significant achievement in this short period.

In October 2005, the Hungarian government selected the consortium of Magyar Telekom Plc. and TMH to build and operate the nation-wide EDR (Hungarian abbreviation for Unified Digital Radio Network) system in Hungary. For this purpose, Magyar Telekom established a new subsidiary, Professzionális Mobilrádió Zrt. (Pro-M Zrt.) in December 2005.

EDR is a 380-400 MHz band nation-wide Professional Mobile Radio (PMR) network used by public safety and security agencies in Hungary. The main users of EDR are police and fire departments and ambulance agencies. The high-quality EDR network replaces the analog radios currently used by these agencies.

The consortium was able to offer favorable terms mainly due to its existing radio and fixed line infrastructure, on which the EDR network is based. The EDR service utilizes the Terrestrial Trunked Radio (TETRA) technology, which is a global standard for Public Safety and Security mobile radio communication, defined and approved by the European Telecommunications Standards Institute (ETSI) as the official European Standard for digital Professional Mobile Radio.

The roll-out of EDR has started in 2006. Under the terms of the agreement the government will pay us annual payments of HUF 9.3 billion starting in 2007 for nine years.

In 2006, TMH continued to enhance its non-voice service portfolio, introduced several new products, increased the penetration and usage of the existing products and extended the access of some of its domestic products abroad:

- International roaming service was available for TMH subscribers on 373 networks in 173 countries as of December 31, 2006, of which 164 networks in 89 countries were available for prepaid customers. At the end of 2006, customers could use 161 General Packet Radio Service (GPRS) networks in 86 countries.

- In line with the increase in the number of MMS-capable handsets in the market, TMH experienced a boost in MMS penetration and traffic. The number of mobile-originated MMSs in 2006 was 20.2 percent higher than in 2005.

- TMH started to sell laptops with data cards in the second half of 2006, which boosted data revenue and traffic. TMH reached 20.8 percent of its postpaid customer base with data service and expects further increase in data penetration and traffic. Packet switched traffic was four times larger than in 2005.

- In 2006, TMH launched WLAN service (Internet Fix) in 120 small settlements where there s no or not sufficient broadband coverage. The international WLAN roaming service became available in seven European countries and additionally in T-Mobile US mobile network for TMH s subscribers in 2006.

- TMH widened its digital contents on t-zones WAP, web and 3G portal. TMH s t-zones WAP portal offers news, chat and downloadable content (e.g., logos, ring-tones, Java games). The popularity of this portal grew continuously during 2006 and the daily average number of visitors reached 45,000 to 50,000. TMH s special t-zones portal for 3G customers contains mainly multimedia contents, such as on-line streaming, music and traffic monitors. News, sports, weather and other contents are available via InfoSMS and InfoMMS as well.

- Premium-rate SMS and premium voice traffic were substantial in 2006. TMH is able to provide premium-rate services voice and SMS on the same number, which is a competitive advantage in this field.

- The web n walk service ensures the access to the Internet on mobile phones for TMH postpaid customers from June 1, 2006. In addition to Internet browsing, customers have the opportunity to download wide range of contents, such as Java games, ring tones, videos and to enjoy Mobile TV service.

- In 2006, TMH significantly widened the range of products that can be purchased by WAP or SMS. Using mobile purchase service, customers can buy various products and services offered by TMH and third-party vendors. We experienced a strong growth in sales of products such as parking tickets, lottery and highway fees. We believe that mobile purchasing has a great potential for further growth.

- For corporate customers TMH offers a full range of telecommunications solutions. In 2006, the total corporate non-voice revenue was 25 percent higher than in 2005. The most successful services are Corporate LAN Access and Bulk SMS in the corporate segment.

- Electronic top-up services are available at many Automatic Teller Machines (ATMs), petrol stations, Internet-banks, Telebanks and Mobilbank. In 2006, the number of electronic top-up outlets increased significantly. The share of electronic top-up increased, reaching 60 percent by the end of 2006.

Subscribers. The number of TMH subscribers has been growing over the past three years. The table below sets forth information concerning the number of TMH subscribers at the dates indicated:

	At December 31, 2004	2005	2006
Number of subscribers			
Postpaid subscribers	1,163,483	1,323,814	1,545,115
Prepaid subscribers	2,868,562	2,870,041	2,886,021
Total subscribers	4,032,045	4,193,855	4,431,136
Average monthly Minutes of Use (MOU) per subscriber	115	127	142
Churn ratio (%)			
Postpaid subscribers	11.9	10.4	9.9
Prepaid subscribers	17.4	22.0	21.9
Total subscribers	15.9	18.5	17.9
Average monthly Revenue per User in HUF			
Postpaid subscribers	11,712	10,838	9,849
Prepaid subscribers	2,352	2,239	2,300
Total subscribers	4,892	4,832	4,800
Mobile penetration in Hungary (%)	86.4	92.4	99.0
TMH s market share (%)	46.2	45.0	44.5

The increase in the number of TMH subscribers since December 31, 2004 is attributable to a number of factors, including the expansion of mobile broadband services. Though the market is slowly reaching a saturation level, in 2006 total growth rate exceeded previous year s results due to significant growth in the postpaid segment.

According to NCA, as of December 31, 2006, TMH had a 44.5 percent market share of the mobile services market in Hungary in terms of subscriber base.

Traffic. TMH s average traffic per subscriber is comparable to other European countries and was at a blended level of 142 minutes in 2006. Average traffic per subscriber has increased over 2005 as a result of successful tariff plans targeting both postpaid and prepaid segment.

Rates. Since January 1998, mobile subscriber rates have been deregulated, and carriers have had the freedom to set the level of fee components (i.e., connection fee, subscription charge and traffic charges).

TMH charges subscribers a one-time connection fee, monthly subscription charges, event charges and time-based traffic charges. Customers using prepaid cards do not pay monthly subscription charges (but in case of some price plans monthly recurring fees do exist). TMH does not charge subscribers for incoming calls, other than calls received while roaming. TMH receives payments from other telecommunications service providers for terminating calls on its network. TMH maintained the widest range of price plans and successfully introduced additional plans in 2006 to acquire new subscribers and develop loyalty.

TMH faced intense price-based competition in 2006. Competitors waged various campaigns, including introduction of new price plans and products, to win over TMH s subscribers. TMH responded to the competitors with its own new tariff initiatives across all of the subscriber segments.

International Mobile Operations

Macedonian Mobile Operations

On February 28, 2006 the Shareholders Assembly of Mobimak approved the rebranding of Mobimak to T-Mobile Macedonia AD Skopje. The rebranding was completed in September 2006.

Our Macedonian mobile services provider, T-Mobile Macedonia, experienced significant growth in 2006.

T-Mobile Macedonia is the leading mobile operator in Macedonia, dedicated to providing up-to-date technologies and advanced service offerings, commensurate to the highest technological and service standard of the T-Mobile group.

By the end of 2006, T-Mobile Macedonia had expanded its customer base from 877,142 at the end of 2005 to 944,530, despite the competitive market environment. The principal activities of T-Mobile Macedonia s operations are digital mobile telephone services based on the GSM technology and non-voice services such as SMS, MMS and GPRS. T-Mobile Macedonia also provides GSM phase2+ data and facsimile transmission services, mobile Internet and a number of other content services. The Macedonian market is very price sensitive. We offer various promotions and incentives to encourage use of our services.

The number of T-Mobile Macedonia customers has grown significantly over the past three years. The table below sets forth information concerning the number of T-Mobile Macedonia subscribers at the dates indicated:

	At December 31,		
	2004	2005	2006
Number of subscribers			
Postpaid subscribers	118,862	139,367	177,311
Prepaid subscribers	633,600	737,775	767,219
Total subscribers	752,462	877,142	944,530
Average monthly Minutes of Use per subscriber	66	63	72
Average monthly Revenue per User in HUF	3,804	3,065	3,206
Mobile penetration in Macedonia (%)	48.1	61.3	68.2
T-Mobile Macedonia s market share (%)	76.3	69.2	66.7

The increase in the number of T-Mobile Macedonia subscribers in the last three years is attributable to a number of factors, including reductions in handset prices and call charges in real terms, successful marketing campaigns and the introduction of installment purchase plans.

As of December 31, 2006, T-Mobile Macedonia had a 66.7 percent market share in the Macedonian mobile telecommunications market in terms of subscribers. The mobile penetration rate is still growing, though at a smaller extent than in 2005.

T-Mobile Macedonia s business is affected by seasonal factors, with a general increase in roaming revenues during the third calendar quarter of each year due to the summer holidays and increased sales of products and services during the fourth quarter due to Christmas purchases.

Montenegrin Mobile Operations

Following the shareholders decision on introducing the T-brands in Montenegro, on September 26, 2006, Monet changed its name to T-Mobile Crna Gora and markets its services under the brand T-Mobile .

Our Montenegrin mobile services provider, T-Mobile Crna Gora, experienced significant growth in 2006.

T-Mobile Crna Gora is the second largest mobile operator in Montenegro in terms of number of subscribers. Since its inception in 2000, it has dedicated itself to offering innovative and advanced services to the Montenegrin market and has been experiencing dynamic growth.

The main activities of T-Mobile Crna Gora s operations are digital mobile telephone services based on the GSM technology and non-voice services, such as SMS, MMS and GPRS. T-Mobile Crna Gora actively employs various promotions and incentives to encourage use of its services. In 2006, T-Mobile Crna Gora made significant investments in its network and core systems to ensure sufficient capacity, maintain competitive service level, as well as to extend its service portfolio. In addition to a variety of service packages, T-Mobile Crna Gora offers WAP, MMS, content SMS and premium-rate SMS services. After the commercial introduction of GPRS in 2004, T-Mobile Crna Gora continued the expansion of its services by launching EDGE in 2005.

The table below summarizes the key operational statistical figures of T-Mobile Crna Gora:

	At December 31, 2004	2005	2006
Number of subscribers			
Postpaid subscribers	n.a.	31,212	48,252
Prepaid subscribers	n.a.	176,882	283,364
Total subscribers	n.a.	208,094	331,616
Average monthly Minutes of Use per subscriber	n.a.	127	127
Average monthly Revenue per User in HUF	n.a.	3,745	3,858
Mobile penetration in Montenegro (%)	n.a.	78.6	129.8
T-Mobile Crna Gora s market share (%)	n.a.	42.7	41.2

T-Mobile Crna Gora s operations, customer base and revenues are significantly affected by seasonal factors. In summer, there is a significant subscriber and revenue growth attributable to tourists who visit the Montenegrin seaside. In 2006, the penetration level in the summer season reached almost 110 percent, as many tourists purchased prepaid cards, and these seasonal subscribers churned out in the fourth quarter. In 2006, this drop in customer base in the last quarter was mitigated by the change of prepaid offer by T-Mobile Crna Gora in October 2006. In order to meet the competitor s offer, prepaid voucher lifecycles (i.e. access to the service) were extended from the earlier three months to 11 months.

In November 2006, the Agency of Telecommunications launched a 3G tender for the Montenegrin mobile market for service licenses to be distributed in the first quarter of 2007. T-Mobile Crna Gora won one of the licenses.

MARKETING AND DISTRIBUTION

Hungarian Fixed Line Operations

One year after the rebranding, our main strategic objectives focused on the development of customer relationship, the enhancement of the customer experience, the revenue maximization, the expansion of the number of broadband accesses as well as the start of mobile integration.

In the Hungarian fixed line segment competition became fiercer and the range of services became significantly wider in 2006. The CATV providers expanded their operations, for example by introducing triple-play services. In addition, fixed line competitors offered local loop unbundling and number porting

services. Due to these factors and mobile substitution, the number of Magyar Telekom s fixed access lines decreased by 4.0 percent by December 31, 2006, compared to a year earlier.

We consider the retention of the fixed line user base and the decrease of the customer churn to be one of our key objectives. We intend to prevent line churn with active and preventive measures, including favorable offers and targeted customer contact. In addition, we further intensify our access line sales activities. In 2006, we significantly increased our broadband customer base.

In 2006, the MOU of our residential customers increased by 15.6 percent, driven primarily by our price plans offering unlimited calls for a fixed monthly fee. The number of our flat rate customers grew significantly in 2006 and reached 630,000 by the end of the year.

In 2006, we continued to expand the selection of price plans available with pre-selection on the service areas of other fixed line service providers. In line with our strategic objectives, the portfolio of our pre-selection price plans was broadened and customers were gradually migrated from the call-by-call price plans to pre-selection schemes. As a result of the new offers and our intensive sales activity, almost 134,000 users on the service area of our competitors registered to use our services by the end of 2006.

In 2006, we continuously worked on integrating our services with TMH products to make them available from one place, in one package and at the lowest possible rates.

In 2006, our retail stores were gradually converted into integrated T-Ponts, where both fixed line and mobile services are available. The development of a unified T-Pont shop network started in January 2006 and was finished at the end of 2006.

TOP 3600 key accounts are served by qualified personal account managers. In 2006, we implemented joint account management with TMH and from 2007 we plan to assign single contact customer relationship managers with KFKI and T-Systems Hungary as well.

In the area of improving customer satisfaction one of the key programs of 2006 was the Quality for our customers! initiative. This is a comprehensive, service quality assurance program that aims at the improvement of the customer relations, the continuous development of our services and the maintenance of our competitiveness. As part of the program, public commitments and customer service standards were formulated by the subsidiaries of Magyar Telekom. As a result of these efforts, customer satisfaction significantly improved in 2006.

International Fixed Line Operations

Macedonian Fixed Line Operations

After the market liberalization in 2006, the new fixed line service providers (26 in total) started their operation by offering international outgoing calls via prepaid cards. Maktel responded with fee adjustments for international calls, special price plans (Partner Country , Favorite Country) and launched co-branded prepaid cards. As a result, Maktel lost only a small market share in the international outgoing voice traffic.

Several sales campaigns launched in 2006 increased the number of ADSL connections. Maktel also launched several new ADSL products to cover different customer segments and to compete with low priced CATV offers. In addition, in the last quarter of 2006, the PC+ADSL campaign was launched to extend PC penetration and broadband Internet usage in Macedonia.

Aggressive marketing and sales approach combined with wide territory coverage, fast provisioning time and high service reliability, supported by strong image campaign, allowed Maktel to retain the dominant position on the Internet market and strengthen the position of ADSL as premium quality service

for broadband access to Internet. In 2006, Maktel doubled the number of broadband ADSL users compared to the end of 2005.

In 2006, Maktel continued to develop business solutions for the corporate market including video surveillance and bundled equipment and services offers.

Montenegrin Fixed Line Operations

In 2006, the main focus of our marketing activities in our Montenegrin fixed line operations was to increase ADSL sales. In order to profit from the market dominance of Crnogorski Telekom and to stimulate growth of non-voice revenues, several promotions have been implemented. The ADSL subscriber base has grown more than sixfold. Substantial growth could be still achieved in the dial-up Internet segment by adapting the tariff portfolio and introducing postpaid dial-up Internet access.

On September 26, 2006 the old brand Telekom Crna Gora has been replaced by T-Com . This gives a new appeal to the fixed line operations of being more modern, international, quality-focused and customer-oriented. The first product introductions under the new brand have been a new ADSL entry-level price plan and a voice weekend price plan, the latter with the goal of improving price perception and stimulating fixed voice usage. To prevent erosion of fixed line connections, the weekend price plan offers segment specific conditions for second home owners.

Montenegrin fixed voice tariffs are still unbalanced by international standards, i.e. access and local call fees are relatively low, whereas international call rates are rather high, opening the door for alternative providers like international VoIP carriers. For historical reasons, business customers are paying higher fees than residential customers. There is a general rebalancing roadmap agreed upon with the regulatory agency.

Hungarian Mobile Operations

In 2006, the Hungarian mobile market reached a 99.0 percent penetration rate, which is comparable to the average level in Western European countries. The growth in mobile market increased as compared to previous years. The Hungarian mobile market is highly competitive and dominated by three mobile network operators: TMH, Pannon and Vodafone. Due to the very high penetration level, our focus has moved from acquisition to retention. In case of our new service, EDR, we are already working on introducing new services for the EDR users (e.g. Automatic Vehicle Location).

At T-Mobile International Group, focus areas and corresponding key performance indicators have been defined for the key pillars of our strategy:

- Customer centricity;
- Superior network experience; and
- Operational excellence.

This provides the strategic framework for the local organizations. Each local company has translated these focus areas into concrete BIG X programs which outline the direction and define the strategic goals for 2006, taking local priorities into account.

At TMH the Big7 program consisted of the following items:

- Build T-Mobile brand and be an advocate for it;
- Launch fixed-mobile products and stabilize mobile market share;
- Best-in-class service culture;

- Grow service revenue focusing on high value customers;
- Exploit mobile data/Internet;
- Network leadership; and
- Number one in HSDPA going commercial.

2006 was a very successful year for TMH in all of our strategic areas:

Build T-Mobile brand and be an advocate for it

We work continuously to strengthen our brand and build our brand values reliability, simplicity, inspiration; adding value for money in Hungary. Our efforts have maintained the aided brand awareness at nearly 100 percent, whereas the spontaneous brand awareness was higher than 80 percent during the whole year.

Launch fixed-mobile products and stabilize mobile market share

After the announcement of the merger, TMH has developed fixed-mobile bundled offers as one of the first tangible benefits of the integration. The first offer, Vica-Versa price plan was re-launched at the end of 2006 offering free calls between maximum four mobile and a fixed number for a monthly fee of HUF 890 per subscription. In addition to this offer, other trial bundled products were also offered. These and the mobile-only services and price plans helped TMH to stabilize its market share. Domino Aktív, Kameleon and the Relax price plans were especially successful.

Best-in-class service culture

According to measurement developed by T-Mobile International Group, TMH has succeeded in reaching a higher than market average promoter score.

Grow service revenue focusing on high value customers

The active customer portfolio management facilitated the increase in value of our customer base. Our main targets were the followings:

- Develop services based on value and needs of customers;
- Differentiate service levels based on the value of customers; and
- Enhance effectiveness of communication via CRM and campaign management tools.

Exploit mobile data/Internet

Non-voice and content services are playing an increasingly important role in the mobile market. All providers strengthened their non-voice services in 2006. TMH is the first mobile operator in Hungary to launch HSDPA. By the end of 2006, TMH subscribers equipped with the latest net-card could already use the Internet with a download speed of 3.6 Mbit/s in 23 cities. In 2007, this speed is expected to increase up to 7.2 Mbit/s in Budapest.

Network leadership

Not only the objective Key Performance Indicators showed excellence in regards to the network, but our customers judged TMH s network to be of very high quality during the whole year.

Number one in HSDPA going commercial

In 2006, TMH launched its fast commercial mobile Internet service, HSDPA, in the internal districts of Budapest. The network allows 3.6 Mbit/s downlink speed, however most of the currently available mobile phonesets support only 1.8 Mbit/s. HSDPA may contribute to the fast diffusion of broadband mobile Internet access.

Distribution

As a consequence of the merger of Magyar Telekom and TMH, the direct shop networks of T-Mobile and T-Com have been integrated during 2006. As a result of the functional and organizational integration, by September 2006, Magyar Telekom had a shop network offering the entire product and service portfolio (T-Com, T-Mobile, T-Online and T-Kábel products and services). The main objective of the integrated T-Pont network is to leverage group level potentials for cross-selling, retention, and customer satisfaction.

Before the integration, TMH s strong direct distribution network consisted of 36 stores, whereas T-Com had 18 direct shops (T-Ponts). The integration process resulted in an optimized direct shop network consisting of 47 integrated T-Pont shops by the end of 2006. All 47 shops provide full-scale sales and customer service in case of all related lines of business. Full-scale mobile handset repair service is provided in 27 shops. 12 T-Ponts are located in Budapest and the other 35 in regional centers. During 2006, 20 shops have been fully and 13 have been partially refurbished according to the T-Pont design. The full refurbishments of the remaining shops continue in 2007.

TMH also has a department dedicated to major accounts. This department consists of 86 sales representatives and serves major accounts on the segment basis. Our customers can also purchase TMH products on our on-line shop.

TMH also distributes its products and services through indirect sales partners. At the end of 2006, TMH had 211 full-scale T-Mobile indirect shops nationwide that provide the full product portfolio for the customers. From January 1, 2006 all T-Mobile Partners (211 full-scale shops) have access to the CRM system. 91 of the T-Mobile shops also provide customer care with access to the central customer database.

From April 1, 2006 within the frames of the shop integration project, TMH took over the management control of the T-Com partner shop network as well. At the end of 2006, this network consisted of 77 T-Com partners, of which 49 are T-Mobile partners, too. There are three contracted partners selling mobile data products. TMH also sells its prepaid products (e.g., prepaid SIM packages, plastic top-up cards, on-line top-up) through major Hungarian retail channels. Prepaid products are available in 10,542 sales points nationwide (including 7,967 shops where on-line top-up is available).

International Mobile Operations

Macedonian Mobile Operations

In September 2006, Mobimak changed its name to T-Mobile Macedonia and became a member of the T-Mobile family. To sustain its primary position in the country, T-Mobile Macedonia has developed a wide range of services and price plans for prepaid, postpaid and business customers. With the rebranding, T-Mobile Macedonia introduced new tariff models for all segments, launched a prepaid loyalty program and carried out a number of innovative promotions.

Marketing based on customer data is widely used to build strong customer relationships. Loyalty schemes and handset upgrade programs are also used to improve customer satisfaction and reduce customer churn rate.

Montenegrin Mobile Operations

In Montenegro, the brands of Monet and later T-Mobile Crna Gora are generally perceived as customer-oriented, with strong sense of customers communications needs. Under the new T-Mobile brand, the brand values include higher international competence and higher quality standards.

In order to have a successful brand introduction and to increase market share, new offers have been quickly introduced to the market. At first, a whole portfolio of new postpaid price plans (Smart) targeted at the residential segment has been introduced in October 2006, accompanied by a strong handset campaign. Minimum contract durations and handset subsidies differentiated by contract value have been introduced. Secondly, a strong promotion followed in November 2006 for the prepaid segment.

In line with the introduction of the new brand, nine shops (T-Centars) have been opened in major towns, setting a new benchmark in shop design for Montenegro. These are accompanied by a network of 16 exclusive Partner Shops which use a similar design to the own shops. Both types of outlets provide a permanent portfolio of handsets and the full range of services for new and existing customers. In addition, there are 1,600 contracted Points of Sale for prepaid vouchers and SIM cards.

COMPETITION

Hungarian Fixed Line Operations

In 2006, despite the increased competition, we managed to retain our leading position in the voice services market with 80 percent market share at the end of the year. Similarly to the prior years, mobile carriers still remain our largest competitors. In addition to the fierce competition triggered by mobile carriers, new market entrants provide public fixed voice telephony services by unbundling local loops. Competitors include mobile telecommunications providers, other LTOs, alternative service providers (e.g., Tele2, PanTel) and cable television service providers.

Mobile penetration reached 99.0 percent by the end of 2006, which not only led to intense competition on the mobile telecommunications market, but also affected the fixed line telephone market. This near-saturation level has led mobile carriers to offer residential and business customers more and more competitive packages and lower prices in an effort to win fixed line customers. In 2006, the main reason for fixed line churn was mobile substitution.

New alternative service providers were able to enter the voice and broadband services market in 2006 due to the unbundling of local loops. As the obstacles imposed by technology disappeared, every major competitor (alternative service provider, ISP, CATV) is able to become a triple-play provider. This trend is expected to largely influence the telecommunications trends and competition on the Hungarian market in the following years.

In our service areas, a number of carriers (Tele2, GTS Datanet, eTel, Invitel, PanTel, British Telecom and Monortel) offer pre-selection and call-by-call services and were able to attract some of our customers. Our competitors voice minute tariffs are decreasing, and they also provide significant discounts from the monthly fee of their services. We also offer similar price plans and are successful in attracting new customers from LTO areas. In the government and public administration sector, we could successfully attack our competitors low prices with the discounts we provide due to the high volume of the EKG frame contracts.

In 2006, Tele2 expanded its service portfolio (flat rate price plans and dial-up Internet access), and introduced various promotions. Tele2 mainly focuses on the residential market. It competes on the basis of simple and low pricing structure, aggressive marketing and innovative sales channels. However, we responded to the challenge posed by Tele2 with attractive price plans, and we believe that we have successfully limited Tele2 s expansion.

In 2004, cable television providers also entered the voice market with triple-play offers, consisting of voice telephone services, Internet access and cable television. The main advantages of the triple-play offers are free calls within the network, low monthly fee and one-stop shopping. Our largest cable television competitor is UPC. In 2006, triple-play offers had significant impact on the fixed line telephone competition.

On the Internet market, we could keep our leading position with the continuous, intense increase of the number of ADSL lines.

We have several competitors in the IT market as well, including Siemens, Synergon and Humansoft. Smaller, but very efficient and flexible service providers also proved to be strong competitors in system and network integration market. In 2007, together with KFKI Group and T-Systems Hungary, we expect to be able to react more efficiently to the challenge posed by our competitors.

International Fixed Line Operations

Macedonian Fixed Line Operations

On January 1, 2005, Maktel s exclusive rights to provide fixed line telephone services expired, but as a result of the delay in implementation of the new regulatory framework, competition from other fixed line service providers started only in February 2007. Maktel, however, faced indirect competition earlier from mobile service providers and, to a limited extent, from VoIP providers.

Starting from the second quarter of 2006, Maktel opened its network for alternative VoIP service providers of international outgoing calls. By the end of 2006, Maktel has concluded 26 ISDN-based commercial Network Access Agreements with alternative VoIP service providers.

On November 15, 2006, Maktel signed its first Reference Interconnection Offer (RIO)-based interconnection agreement with OnNet, an alternative fixed line network operator. OnNet launched its long distance, fix to mobile and international services in February 2007. The second interconnection agreement was concluded with Akton in December 2006. In March 2007, Akton started to provide international termination services. As a result, Maktel will face direct competition in its fixed line business from the first quarter of 2007. OnNet has already requested Local Loop Unbundling services from Maktel based on the approved unbundling reference offer (MATERUO). OnNet has requested only fully unbundled access to the local loop.

Maktel is the leading provider of leased line services and data transmission services. CATV and other wireless operators have built their own networks and are also capable to offer data transmission services, transmission capacity and various broadband services.

In the Internet market, there are three major ISPs in addition to Maktel: OnNet, MOL and UNet. Maktel is the market leader based on the number of Internet dial-up minutes. On the broadband market, Maktel has approximately 50 percent market share and it faces competition mainly from OnNet s wireless broadband and CATV operators cable broadband Internet, offered to the CATV customers through their own networks.

Montenegrin Fixed Line Operations

Crnogorski Telekom is the sole provider of fixed line telecommunications in Montenegro. However, it faces fixed-mobile service substitution, which is expected to become increasingly significant. The high mobile penetration and the introduction of a third mobile operator in 2007 will intensify this trend. Crnogorski Telekom, however, owns a 100 percent interest in T-Mobile Crna Gora, the second largest mobile service provider in Montenegro.

Several Multichannel Multipoint Distribution Service (MMDS) and CATV licenses were awarded at the beginning of 2007. Some of the cable operators have declared their intention to provide Internet and telephony services, too. Three fixed wireless access licenses have also been awarded, to Telekom Serbia (the third mobile operator), to Broadband Montenegro (an MMDS operator with nationwide coverage) and to T-Mobile Crna Gora.

Hungarian Mobile Operations

In 2006, the Hungarian mobile telecommunications market was characterized by intense competition, driven by new services, lower prices and aggressive marketing. The mobile penetration rate further increased to 99.0 percent by the end of 2006. At TMH, the focus on acquisition was clearly replaced by the focus on retention. Despite the intense competition, TMH retained its market leading position with a 44.5 percent market share based on the number of active SIM cards.

The direct competitors of TMH are Pannon and Vodafone. Vodafone, the smallest mobile service provider in terms of the number of subscribers in Hungary, continued its intensive and aggressive marketing campaigns and captured a 21.4 percent market share by the end of 2006. Pannon has refreshed its brand, started to build a new image in line with the global renewal of the Telenor companies. Pannon has reached a market share of 34.1 percent by the end of 2006.

Non-voice and content services are playing an increasingly important role in the mobile market. All providers strengthened their non-voice services in 2006. TMH was the first mobile operator in Hungary to launch HSDPA and provide high-speed mobile Internet services and new data services, like web n walk.

To draw attention and boost the number of active users, notebooks with HSPDA enabled data cards are sold in the T-Pont network and at selected dealers from September 2006. Several 3G handsets and data cards were offered as a promotion.

International Mobile Operations

Macedonian Mobile Operations

There are at present two mobile operators operating in the Macedonian mobile market. Competition is generally intense and conducted on the basis of price, subscription options, subsidized handsets, range of services offered, innovation and quality of service. The second largest mobile telecommunications services provider in the country, Cosmofon, began commercial operation in June 2003. Its marketing and advertising efforts are aggressive with low and competitive handset pricing, attractive price plans, broad array of advertising and indirect channels of sales. In June 2005, Cosmofon launched 2.5G services (MMS, GPRS). The Macedonian telecommunications regulator issued a third mobile license to Austrian Mobilkom in the first quarter of 2007, which is expected to intensify the competition in the Macedonian mobile market.

In 2006, the competition between the two mobile operators has become stronger especially during the large rebranding campaign launched by T-Mobile Macedonia. Both T-Mobile Macedonia and Cosmofon launched several price plans during this period. Special price plans (closed user groups, special business offers) combined with additional services (SMS, MMS, GPRS) and large advertising campaigns were introduced to capture various parts of the telecommunications market and to provide higher value compared to fixed line offerings.

According to T-Mobile Macedonia s estimates, Cosmofon had approximately 33.3 percent market share at the end of 2006. Cosmofon s subscriber base is mainly prepaid. Cosmofon has been increasingly targeting T-Mobile Macedonia s residential and business postpaid (contract) customers.

In this intensive competitive environment, T-Mobile Macedonia plans to maintain its market share through improved productivity, efficiency measures and maintenance of existing customer relations to avoid the escalation of price-based competition.

Montenegrin Mobile Operations

T-Mobile Crna Gora started its commercial operation as a second mobile telecommunications services provider in Montenegro in 2000, four years after the first mobile provider, Promonte, started its operations. According to T-Mobile Crna Gora s estimate, T-Mobile Crna Gora had 41.2 percent market share in terms of number of subscribers at the end of 2006.

As in other countries, competition in mobile services is intense and driven by pricing, subscription options, subsidized handsets, coverage, as well as quality and portfolio of services offered. Our competitor s marketing and advertising activities are aggressive.

T-Mobile Crna Gora s goal is to increase its market share by introducing segment-oriented price plans, continuously offering new attractive handsets, exploiting synergies of the DT group, and maintaining existing customer relations and community involvement as a sponsor of important social, cultural, sports and educational events.

In November 2006, the Montenegrin telecommunications regulator has issued a tender for two 3G licenses as well as a tender for a mixed 2G-3G license for a third mobile operator. In the first quarter of 2007, T-Mobile Crna Gora and Promonte were awarded with one 3G licenses each and Telekom Serbia won the combined 2G-3G license. It is most likely, that the mobile operation of Crnogorski Telekom could face a significant decrease in its market share over the medium term.

DEPENDENCE ON PATENTS, LICENSES, CUSTOMERS, INDUSTRIAL, COMMERCIAL AND FINANCIAL CONTRACTS

We do not believe that we are dependent on any patent or other intellectual property right, on any individual third party customer or on any industrial, commercial or financial contract. Similar to other fixed line and mobile operators, we require telecommunications licenses from the governments of Hungary, Macedonia, Montenegro, Romania and Bulgaria, the countries in which we provide telecommunications services.

REGULATION

Development of the Telecommunications Regulatory Regime in Hungary

Prior to 2001, Act LXXII of 1992 on Telecommunications, as amended (the Telecommunications Act), provided the general regulatory framework for the telecommunications industry in Hungary. The telecommunications industry has been also governed by other general legislation, including, among others, Act XVI of 1991 on Concessions, as amended (the Concessions Act), the Pricing Act and Act LVII of 1996 on the Prohibition of Unfair and Restrictive Market Practice (the Competition Act).

The regulatory framework of the telecommunications industry was fundamentally altered in December 2001, when the Communications Act came into effect. The Communications Act provided the main regulatory framework for the liberalized market until the end of 2003.

The limited level of competition that resulted from the Communications Act and harmonization of the Hungarian law to EU standards required by the accession of Hungary to EU led to the further modification of the regulatory regime. Act C of 2003 on Electronic Communications came into effect on January 1, 2004 and the Communications Act was superseded at that time.

The Electronic Communications Act and the Contract on Universal Service Provision

The Electronic Communications Act was approved by the Parliament on November 24, 2003 and came into effect on January 1, 2004. Under the Act, the NCA, the supreme supervisory body, and Permanent Court of Arbitration for Communications (CAC) were established.

Set forth below is a brief summary of certain provisions of the Electronic Communications Act.

Universal Service. The Electronic Communications Act provides that universal services are basic communications services that should be available to all at an affordable price. Universal services include access to fixed line voice telephone services of certain quality enabling access to Internet services, a regulated density of public payphones, a public directory of telephone users, national domestic inquiry service as well as free call-blocks and emergency calls. Access to voice services at an affordable price is effected by designation of universal service providers (the Minister shall appoint the most efficient service provider) and state subsidies to disabled or low-income users.

We were designated a universal service provider and entered into a universal service contract with the Minister. The current contract is valid until December 31, 2008 and can be extended for an additional four years.

Subscriber Contracts. Service providers must establish general terms and conditions of subscriber contracts. The Electronic Communications Act provides general rules of agreements between subscribers and telecommunications services providers for telecommunications services. The ministerial Decree 16/2003 (XII.27.) on Telecommunications Subscriber Contract contains other important rules relating to subscriber contracts. In subscriber contracts, parties can modify the provisions of the Electronic Communications Act only if they are more favorable to the subscribers.

The general terms and conditions of subscriber contracts must contain, among other things, the procedure for terminating and amending subscriber contracts, the quality of the telecommunications service, conditions for restriction of the service, the fault-repair service and the method for handling subscriber complaints. The individual subscriber contract must contain personal data of the subscriber.

Significant Market Power Regulation. On February 11, 2003, the European Commission identified in its recommendation (2003/311/EC) the following 18 relevant product and service markets within the electronic communications sector susceptible to ex ante regulation in accordance with Directive 2002/21/EC on a common regulatory framework for electronic communication networks and services:

Retail level:

1. Access to the public telephone network at a fixed location for residential customers.

2. Access to the public telephone network at a fixed location for non-residential customers.

3. Publicly available local and/or national telephone services provided at a fixed location for residential customers.

4. Publicly available international telephone services provided at a fixed location for residential customers.

5. Publicly available local and/or national telephone services provided at a fixed location for non-residential customers.

6. Publicly available international telephone services provided at a fixed location for non-residential customers.

7. The minimum set of leased lines.

Wholesale level:

8. Call origination on the public telephone network provided at a fixed location.

9. Call termination on individual public telephone networks provided at a fixed location.

10. Transit services in the fixed public telephone network.

11. Wholesale unbundled access (including shared access) to metallic loops and sub-loops for the purpose of providing broadband and voice services.

12. Wholesale broadband access.

13. Wholesale terminating segments of leased lines.

14. Wholesale trunk segments of leased lines.

15. Access and call origination on public mobile telephone networks.

16. Voice call termination on individual mobile networks.

17. The wholesale national market for international roaming on public mobile networks.

18. Broadcasting transmission services, to deliver broadcast content to end users.

In 2004, analysis of 17 out of 18 markets was initiated by the NCA. Analysis on 16 of these markets has been completed so far. The results of the analysis on fixed line retail markets have identified Magyar Telekom as having SMP and imposed a price cap on retail access market services (market 1 and 2) for residential and non-residential customers. In addition, it required Magyar Telekom to allow fixed line residential and non-residential customers to select other service providers for local and/or national and international calls (markets 3-6) and obliged Magyar Telekom to provide the minimum set of leased lines (market 7). On the wholesale markets, the NCA imposed the obligations of transparency (markets 8-9, 11-13), accounting separation (markets 8-9, 11-13), access and interconnection obligations (markets 8-9, 11-13), various obligations regarding cost-based prices and price control (markets 8-9, 11-13) and non-discrimination (markets 12-13). The market analysis procedure also identified TMH as having SMP in the mobile termination market (market 16) and imposed the obligations of transparency, accounting separation, access/interconnection and cost-based prices and price control.

The aforementioned list of relevant markets taken into account in the market analysis of the NCA is currently under review in the EU. The amended Recommendation of the EU that contains the relevant markets is expected to enter into force in 2007. As a result, retail call markets and the minimum set of leased lines are expected to be deregulated. Consultation papers of the review raised the possibility that SMS termination could become part of market 16, which would mean the extension of regulation to SMS termination in addition to mobile voice call termination.

The new round of analysis of the 18 relevant product and service markets started in the second half of 2006. The new resolution on market 16 was published on October 2, 2006. The rest of the resolutions are expected to be published in 2007.

Local Loop and Bit-stream Unbundling. According to the Electronic Communications Act and Government Decree 277/2003, (XII.24.) on The detailed rules of procedures related to the reference offers and networking contracts , operators with SMP providing unbundled access or broadband access are obliged to unbundle local loops and prepare reference offers for unbundled local loops (whether fully or partially unbundled) and bit-stream access and to provide these services when there is a request for them by other telecommunications service providers.

Providers with SMP may refuse the request for unbundling only if:

- there are technical barriers; and
- providing access to the local loop or bit-stream access would endanger the unity of the provider s network.

Interconnection. According to the Electronic Communications Act and Government Decree 277/2003 (XII. 24.), providers with SMP are obliged to prepare reference offers for interconnection and to provide these services upon the reference offer when there is a request for them by other telecommunications service providers.

According to the Government Decree 277/2003 (XII. 24.), providers with SMP are obliged to enter into agreements for access to their networks when requested by another service provider. If the provider is obliged to prepare a reference interconnection offer, this offer must be in line with the legal regulations about the reference offer. The NCA has authority to arbitrate in disputed cases and may establish provisional arrangements. The reference offer of the providers with SMP must be approved by the NCA.

Carrier Selection. According to the Electronic Communications Act, voice telephone customers have the right to select different service providers for each call directions. The implementing regulation was released in Government Decree 73/2004 (IV.15.) in April 2004.

Number Portability. Fixed line telecommunications service providers are required to provide number portability on their networks, and to allow subscribers to change service providers without changing their telephone numbers in the same geographic location. In May 2004, non-geographic and mobile number portability were also implemented.

Licensing and Allocation of Frequencies. With the exception of a program receiver device, radio equipment, radio stations and radio communication networks may be operated with a radio license. A radio license may be issued exclusively on the basis of a valid frequency assignment license, with certain exceptions. Radio equipment, radio stations, radio networks and radio communications systems may be installed with a frequency assignment license, with certain exceptions. Payment of fees is required for reservation and authorized use of frequencies assigned for civil purposes, reservation of identifiers and use of the assigned identifiers.

Magyar Telekom Plc. pays a frequency license fee on the basis of Decree 6/1997 (IV.22.) KHVM on Frequency Reservation and Usage Fee and Government Decree 120/1998 (VI.17.) on Rules of Payment of Frequency Reservation and Usage Fee . Additional rules related to frequency usage include Government Decree 346/2004 (XII. 22.) on Specification of the National Frequency Allocation Table and Government Decree 78/2006 (IV. 4.) on Rules of the Auction and Tender to Obtain the Frequency Usage Right .

Magyar Telekom Plc. pays a number usage fee for call numbers used by the Company, according to Decree 11/2005 (IX. 28.) IHM on Fees of Engaging the Identification Numbers Necessary for the Provision of Public Telephone Services .

Frequency assignments must conform to the National Frequency Range Distribution Chart, which lays out the entire spectrum and the purpose and availability of frequency bands. Our frequencies are generally valid for periods of one to five years.

Rights of Way. According to the Electronic Communications Act, communications service providers are entitled with prior notice to enter private property where communications facilities (equipment, cables, antennas) are located for maintenance and repair. The public telecommunications service provider must enter into a contract with the property owner setting forth conditions for the common use of the property. The property owners are also obliged to remove obstructions to public telecommunications networks.

Mobile Concession Contracts

Hungary was the first country in Central and Eastern Europe to introduce public mobile telecommunications services. Westel 0660 began providing analog mobile radiotelephone service in October 1990 with an exclusive license. In 1993, the Minister awarded two concessions to provide nationwide mobile telephone services using the digital GSM 900 standard: one to TMH and the other to Pannon.

Under the Concession Contract, dated November 4, 1993, as amended (the 900 Concession Contract), between the Minister and TMH, TMH was granted the right to provide public GSM mobile telephone services for 15 years. The parties may agree to extend the TMH concession for an additional period of seven and half years for an additional fee. In May 2007, the government indicated that it would require a HUF 10 billion concession fee to extend the 900 Concession Contract.

On February 25, 1999, the Ministry issued an invitation to tender for concessions for the DCS 1800 services in Hungary, a mobile telecommunications service in the 1800 MHz frequency band. The tender was closed on May 7, 1999. On October 7, 1999, an amended 900 Concession Contract was signed, allowing TMH and its competitor, Pannon, to start commercial service in the 1800 MHz band for 15 years beginning November 26, 2000. At that time, the Minister also signed a concession contract with V.R.A.M. Rt., which operates the Vodafone brand name.

TMH, simultaneously with Pannon, started commercial operation of the 1800 MHz band on November 16, 2000. Upon the request of Vodafone, the national roaming agreement between TMH and Vodafone was terminated effective November 30, 2000, whereby TMH was released from the obligation to provide Vodafone with domestic roaming services on a nationwide basis. Effective December 6, 2002 Pannon terminated its national roaming agreement with Vodafone. As Vodafone had no remedy available for such a unilateral decision, it was forced to speed up its network roll-out to close the coverage gap vis-à-vis its competitors.

By virtue of the amendment to the Concession Contract in 1999, by the end of 2003, the three digital mobile telecommunications service providers had the same spectrum resources allocated to them both on the 900 and the 1800 MHz bands.

TMH was required to pay a HUF 11 billion concession fee, adjusted for changes in the HUF/USD exchange rate. The first installment of the concession fee, HUF 2,750 million was paid eight days after the modification of the 900 Concession Contract in November 1999. The second installment of HUF 2,750 million, adjusted for changes in the HUF/USD exchange rate, was paid eight days after the commencement of 1800 MHz service in November 2000. The third installment of HUF 1,830 million, adjusted for changes in the HUF/USD exchange rate, was paid in November 2002. The last installment of HUF 3,670 million, adjusted for changes in the HUF/USD exchange rate, was paid on December 2003. TMH also pays an annual concession fee of USD 1 million.

Frequency Fees. TMH had frequency fee payment obligations for channels allocated in the 1800 MHz band. In 2006, TMH paid HUF 3,530 million for frequency usage in the 900 MHz band, and paid HUF 150 million for the right to use the 15 MHz frequency band, and HUF 271 million for the actual use of channels within 1800 MHz band.

TMH also paid frequency fees for the IMT-2000/UMTS band. In 2006, TMH paid HUF 151 million for the right to use the 2x15 MHz frequency band and HUF 487 million for the actual use of channels within the band. In addition, TMH paid HUF 871 million in 2006 for the right to use microwave frequencies.

Fees and Charges. TMH s subscriber charges are not subject to regulation under the Pricing Act or any ministerial decree.

Roaming Agreements. TMH may sign roaming agreements with other public mobile telecommunications service operators outside of Hungary in accordance with the rules of the GSM Association, an association of GSM operators and associated members.

Market Assessment, SMP Designation Process and Interconnection. See Item 4 Pricing .

Termination. TMH met all of its concession obligations in 2006. If an event of default occurs under the 900 Concession Contract, the NCA may issue a cure notice to TMH. TMH would then have 90 days to agree with the NCA on a plan of action for curing the default. If TMH does not reach an agreement with the NCA or if TMH does not cure any such default within an agreed period of between three to six months, the NCA may issue a notice terminating the 900 Concession Contract. Upon termination of the 900 Concession Contract, TMH would be dissolved under the Concessions Act.

UMTS. On December 7, 2004, the NCA awarded TMH the exclusive right to use the frequency blocks of 1920-1935 / 2110-2125 MHz Frequency Division Duplex (FDD) and 1915-1920 MHz Time Division Duplex (TDD) for deployment and operation of International Mobile Telecommunications (IMT) 2000/UMTS mobile telecommunications system (3G system). The duration of the frequency usage right is 15 years (until 2019) with an option to extend for another seven and a half years.

The right was awarded after a tender process that started on September 1, 2004 and concluded on December 7, 2004. TMH applied for all three frequency blocks (A , B and C) separately and won the usage right of frequency block A . The right to use the frequencies vested upon payment of the first installment of the license fee on December 27, 2004.

TMH was obliged by the term of the license decree to start commercial IMT-2000/UMTS service in the inner city of Budapest within 12 months of the grant of the license. This obligation was met. It is also obliged to expand the coverage to 30 percent of the Hungarian population within 36 months of the license.

The license fee for IMT-2000/UMTS was HUF 17,000 million plus reclaimable VAT, payable by the end of 2005. In addition to the license fee, TMH capitalized expenses incurred in connection with the acquisition process of the license. The total amount capitalized was HUF 17,073 million. The IMT-2000/UMTS license right is amortized on a straight-line basis over 15 years from the time of the commencement of the commercial service on August 26, 2005 to the end of the initial license period.

Mobile radiotelephone license s terms are extendable; however, they expire in the following years:

- GSM 900: 2008
- DCS 1800: 2014
- IMT-2000/UMTS: 2019

Competition Law Restrictions

The Electronic Communications Act and the Contract on Universal Service Provision in line with the Competition Act prohibit us from the abuse of our dominant position in the public voice telephone services market.

Under the Competition Act, a market participant is considered to be in a dominant position if, among other things, it is able to pursue economic activities substantially independent of other market participants, i.e., without the need to consider the market behavior of its competitors, suppliers, customers and other business partners.

Under the Electronic Communications Act and the Competition Act, service providers with SMP are required to provide services to other telecommunications service providers on the same commercial terms, and these terms may not be less favorable than those offered to other service providers controlled by it or controlling it.

According to the Contract on Universal Service Provision, we are obliged to treat similar subscribers in a reasonably similar manner and to refrain from effecting discrimination and/or unjustified advantage with respect to conditions and fees of universal service provision.

Hungary and the European Union

Hungary joined the European Union on May 1, 2004 and became a member state without transitional provisions.

In connection with the accession, Hungarian regulations relating to electronic communications were harmonized with the EU NRF, which required all member states of the European Union to adopt it through national legislation. The NRF consists of various directives relating to the following:

- access to and interconnection of electronic communications networks;
- mandatory minimum service standards for all users (universal service) and users rights;
- authorization and licensing regimes;
- data protection and privacy; and
- decision on a regulatory framework for radio spectrum policy in the EU.

The NRF, in particular:

- sets out the rights, responsibilities, decision-making powers and procedures of the National Regulatory Authorities (NRAs) and the European Commission. This includes the NRAs obligation to submit to the Commission and the NRAs of other EU member states the draft regulatory measures that they intend to implement with respect to market definition and SMP and the European Commission s power to require NRAs to withdraw such drafts, if the European Commission considers that such measures may create a barrier to the single European market or are incompatible with EU law;
- identifies specific policy objectives that NRAs must achieve in carrying out their responsibilities (namely, to promote an open and competitive European market for communications services, to promote the interests of European citizens and to consolidate the EU s internal market in a converging technological environment); and
- provides that operators with SMP in relevant communications markets will be subject to obligations set out in the directives on universal service and access.

The European Commission started to carry out a review of the NRF in November 2005 and the review is currently ongoing (consultations, publication of Commission communications, etc.). Proposals for the European Parliament and the Council directives modifying the NRF can be expected in the first half of 2007, which will be followed by the community legislation procedure. The amended regulation is expected to be implemented in 2010.

The European Commission issued a Recommendation on relevant product and services markets in February 2003. The Recommendation identifies markets with certain characteristics that may justify imposition of ex ante regulatory obligations. See Regulation Significant Market Power Regulation .

The European Commission will regularly carry out a review of the Recommendation on relevant markets. The first review of this Recommendation started in line with the NRF review in November 2005 and the amended new recommendation is expected to enter into force in 2007.

On July 12, 2006 the European Commission proposed an EU regulation to reduce international roaming charges within the EU. The proposal for a regulation of the European Parliament and of the Council is dealing with the roaming on public mobile networks within the EU. The objective of this proposal is to amend the existing regulatory framework for electronic communications to provide the necessary legal basis for effective and timely action to bring about substantial reductions in the level of mobile roaming charges across the EU in a harmonized manner. The EU roaming regulation, as approved on May 23, 2007 by the European Parliament, will set a limit on the international wholesale mobile roaming charges among mobile operators and on international mobile roaming retail charges (Eurotariff). The maximum inter-operator tariff shall not exceed EUR 0.30 per minute, which will be further reduced in 2008 and 2009 to EUR 0.28 and EUR 0.26. The maximum retail charges of the Eurotariff, which a home provider may levy from its roaming customers, for calls made abroad shall not exceed EUR 0.49 per minute (to be further reduced to EUR 0.46 and EUR 0.43 in 2008 and 2009) and for calls received abroad shall not exceed EUR 0.24 per minute (to be further reduced to EUR 0.22 and EUR 0.19 in 2008 and 2009). The Council of the EU telecommunications ministers endorsed the EU roaming regulation on June 7, 2007. The EU roaming regulation will then become directly applicable in EU member states (and therefore not require further transposition into national law) following its publication, expected in June 2007. The EU roaming regulation will have significant consequences for TMH s revenues.

Implementation of NRF in the member states is overseen by the European Commission and the European Regulators Group (ERG), which issues reports and common statements. The ERG is a body composed of representatives of NRAs and the European Commission, which plays an important role in advising and assisting the Commission in consolidating the internal market for electronic communication networks and services.

Hungary fully implemented the NRF with the enactment of the Electronic Communications Act and fully implemented decrees in 2004.

Broadcasting and Transmission

Broadcasting and transmission in Hungary are governed by Act I of 1996 on Radio and Television Broadcasting (Media Act), Act LXII of 1993 on Frequency Management (Frequency Act), the Electronic Communications Act and the Concessions Act. Under the Media Act, the National Radio and Television Board (NRTB) has the primary authority for issuing tenders for broadcasting contracts and registering broadcasters and transmitters.

National and regional television and radio broadcasting or broadcast distribution to local operators generally require concessions under the Electronic Communications Act and may be carried out on the basis of a program distribution contract in accordance with the Media Act between the NRTB and the distributor. Frequencies are assigned under the terms of the Frequency Act. Entities registered as program distributors are permitted to transmit broadcasts of third parties to subscribers through a cable transmission network.

The restriction under the Media Act on our further expansion in the program distribution sector was lifted on January 1, 2004. Accordingly, we are now free to increase our ownership interest in any program distributor, including cable television companies, despite our existing controlling interest in one cable television company.

Development of the Telecommunications Regulatory Regime in Macedonia

A new Macedonian law concerning electronic communications (Law on Electronic Communications, ECL), which was enacted on March 5, 2005, brings the country s telecommunications regulations closer to the EU regulatory framework, with some transitional provisions. It also provides a number of strict obligations for the existing operators.

Since the parliamentary elections in July 2006, the Government of the Republic of Macedonia has enacted a number of bylaws and rulebooks regulating different communication areas. As a result of the intensified implementation, there is a possibility that certain ECL provisions and bylaws will be soon amended.

Regulation of Fixed Line Business

On December 31, 2004, Maktel s monopoly rights in the Macedonian telecommunications market expired, thus making it possible for other network and service providers to enter the Macedonian telecommunications markets, upon the submission of notification to the Macedonian telecommunications regulator (and the registration thereof). By December 2006, the Macedonian telecommunications regulator had registered 45 network operators and 55 providers of public fixed telephony services. Maktel published Network Access Agreement for the VoIP service providers for international calls. In February 2007, the Government of the Republic of Macedonia determined that the concession contracts of three telecommunications operators (Maktel, T-Mobile Macedonia and Cosmofon) do not exist any more according to the ECL, and that these companies should therefore continue their operations according to the provisions of the ECL. After several meetings held between the representatives of the telecommunications operators with valid concession contracts and the Macedonian government, the parties agreed that the current concession contracts should be harmonized with the provisions of the ECL.

In July 2005, the Macedonian telecommunications regulator issued regulations governing the conditions of interconnection. Rules for access to, and the use of, specific network facilities were issued in August 2005, and regulations governing the opening of the local loop to competitors, and carrier selection, were adopted in December 2005.

On August 8, 2005, Maktel submitted its first RIO to the Macedonian telecommunications regulator. The interconnection prices contained in this offer were approved on January 23, 2006. In November 2006, the first interconnection contract was signed according to the conditions determined in the RIO. Maktel s first Reference Offer for the Unbundling of the Local Loop (RUO) was submitted to the Macedonian telecommunications regulator on September 5, 2005 and approved on July 19, 2006.

To prepare for competition in its fixed line business, Maktel carried out several changes to its retail pricing structure. For example, Maktel continued to align the prices it charged for network access products and calling services with the underlying costs, and changed its pulse-based charging system to a more customer-oriented time-based charging system with shorter time units. In addition, on the basis of the ECL, the Macedonian telecommunications regulator imposed obligation for cost-based prices for wholesale services of Maktel. Because Maktel s monthly fees for network access and the prices it charges for local calls amount to approximately half of the respective EU averages and are below Maktel s approved cost-based wholesale prices, further cost-based realignment of retail prices might become necessary. To the extent that any of its subscriber line prices do not yet fully reflect the cost of service, a negative impact on Maktel s competitiveness in the wholesale and retail markets can be expected.

According to the obligations imposed by the ECL, a new number portability bylaw has been published by the Agency for Electronic Communications on December 27, 2006. Maktel and T-Mobile Macedonia, as operators of publicly available telephone services, must enable their subscribers to retain their geographic and non-geographic numbers when changing telecommunications operators. The number

portability is scheduled to be fully implemented by July 1, 2007. Due to the short notice, the implementation of number portability will be technically hardly feasible within the given timeframe, therefore Maktel will use the appropriate legal steps to respond to this.

Since the end of 2004, when Maktel s obligation for providing universal services according to its concession contract expired, there has been no operator dedicated as universal service provider. In May 2006, the Government of the Republic of Macedonia enacted a decision for implementation of temporary strategy for universal services, which set the basic strategic decisions. The relevant bylaws regulating the technical parameters, quality requirements and pricing of providing universal services in Macedonia were enacted in the second half of 2006.

The Agency for Electronic Communications announced its willingness to implement a public tender procedure for granting authorizations for radio frequency utilization in the 3.4-3.6 GHz band for realization of a fixed wireless access, WiMAX. The tender will be implemented due to efficient and effective utilization of the scarce radio frequency resources.

Regulation of Mobile Business

The services provided by the mobile network operators in Macedonia are currently not subject to price regulation. However, the Macedonian telecommunications regulator is collecting market data on the fixed-to-mobile market. It is expected that this market analysis will be completed by the end of the first half of 2007 and a probable outcome is that T-Mobile Macedonia will be designated with SMP status. Depending on the outcome and findings of this market analysis, regulatory obligations, including those relating to wholesale pricing, carrier selection and pre-selection and national roaming cannot be excluded.

A public tender for a third mobile operator license was published on October 30, 2006. The tender envisages granting of an authorization for radio frequencies utilization to a third mobile operator on the entire territory of the Republic of Macedonia in the GSM 900 and DCS 1800 radio frequency bands. The authorization will be granted for an initial period of 10 years, with a possibility of subsequent extension of another 10 years. The public opening of the bid was held on January 31, 2007. The Commission granted the license to the only bidder, Austrian Mobilkom.

The Agency for Electronic Communications announced a call for expressions of interest for a fourth mobile operator on April 2, 2007.

Macedonia and the European Union

The Republic of Macedonia signed the Stabilization and Association Agreement with the European Union and its Member States on April 9, 2001. The Macedonian Parliament ratified the Agreement on April 12, 2001, reaffirming the strategic interest and the political commitment for integration with the European Union. The Stabilization and Association Agreement has been ratified and in force since April 1, 2004.

On December 17, 2005, the EU decided to grant Macedonia EU candidate status. Following candidate status, the EU must set a date to begin the negotiations about full access encompassing all aspects of EU membership, including trade, environment, competition and health. Macedonia, as candidate country, should harmonize its legislation with the EU.

Development of the Telecommunications Regulatory Regime in Montenegro

Following the privatization of Crnogorski Telekom, the gradual liberalization of the telecommunications markets in Montenegro can be expected in the coming years. The 2000 Montenegrin telecommunications law (the 2000 Law) conferred broad authority upon the Montenegrin telecommunications regulator. The 2000 Law established a licensing regime whereby all

telecommunications activity must be licensed by the Montenegrin telecommunications regulator. In addition, a new competition law came into force on January 1, 2006. However, no Montenegrin competition agency has yet been set up, and to date there is no consumer protection law or agency in Montenegro.

We expect that the 2000 Law will be significantly amended in the third quarter of 2007. The major goal of these amendments will be to bring the legislation closer to EU directives, to stimulate competition, to stimulate Internet usage and to encourage investment in the telecommunications sector. We also expect that the current licensing-based regulatory regime will be replaced with an authorization-based regime. Furthermore, the introduction of cost-based pricing and accounting separation obligations, and of the provision of binding reference interconnection offers by operators with significant market power, can also be expected. All of these obligations would significantly lower the market entry barriers for new providers in the telecommunications markets, thus leading to market share losses for Crnogorski Telekom in the medium and long term.

Furthermore, in November 2006, the Montenegrin telecommunications regulator has issued a tender for two 3G licenses as well as a tender for a mixed 2G-3G license for a third mobile operator. In the first quarter of 2007, T-Mobile Crna Gora and Promonte were awarded with one 3G licenses each and Telekom Serbia won the combined 2G-3G license. It is most likely, that the mobile operation of Crnogorski Telekom could face a significant decrease in its market share over the medium term.

Local governments in Montenegro have the authority to levy municipal taxes on telecommunications equipment placed on municipal land and under roads, resulting in a high degree of uncertainty for Crnogorski Telekom with respect to the overall tax liabilities. The parliament adopted legislation that established a cap on taxes that can be charged by local governments for objects above the ground and abolishes this tax from January 1, 2008. The local governments still have the freedom to levy any tax on cables placed under the ground.

Montenegro and the European Union

Montenegro became an independent state in 2006 and is in the process of conducting negotiations about a Stabilization and Association Agreement with the European Union.

PRICING

Hungarian Fixed Line Operations

Connection Fees

Decree 3/2002 (I.21.) MeHVM on Charges for Voice Telephone Services Provided by Companies with Significant Market Power and Price Plans Related to Universal Services (the 2002 Fixed Line Tariff Decree) gives service providers the right to collect an additional fee of up to 50 percent of the costs incurred for providing connections in rural areas, if the connection fee does not cover the direct costs of the service provider. Connection fees and subscription charges, but not usage charges, are different for our business and residential customers. We may apply discounts to the published charges but are not allowed to exceed any published charge.

Subscription Fees and Usage Charges

Under the Pricing Act, as modified by the Electronic Communications Act, the Minister is responsible for establishing the maximum rates for universal services. Tariff regulation in Hungary is currently based on a price cap method for universal services. Since February 1, 2002, fixed line rates and connection fees have been regulated by the 2002 Fixed Line Tariff Decree. This decree has been modified to limit its scope of price regulation to universal services. The 2002 Fixed Line Tariff Decree established the price cap

formula, under which our annual price increase cap was set as the forward-looking CPI less a three percent productivity factor.

According to the SMP resolutions concerning residential and business access markets, a price cap should apply to subscription fees of various price plans. These SMP resolutions were only effective for 2005, although a resolution with similar price cap regulation is expected for 2007 as well. The SMP resolutions concerning residential and business access markets extend the applicability of price caps to all subscription fees. The resolutions provide that the maximum aggregate price increase of the subscription fees business and residential separately cannot be higher than the actual CPI for the current year.

This implies that a price check can only be carried out after the year the price cap relates to has ended.

On January 1, 2005, we set new prices for our services. We increased most of our residential subscription fees, resulting in an average subscription fee increase of approximately 3.5 percent for residential PSTN lines. Subscription fees for business PSTN lines changed to a very small extent. In 2005, our traffic charges did not change significantly.

In 2006, we increased the subscription fee of our residential PSTN lines by 2.7 percent, while the prices of the business PSTN lines were raised by slightly more than one percent. Traffic fees were only changed in case of the popular Felező price plan: these were reduced by an average of 7.7 percent. There were no SMP resolutions for 2006.

On January 1, 2007 we increased our subscription fees for the residential market. As a result, the PSTN residential subscription fees rose by 2.8 percent on average. Business subscription fees for analog lines were raised from March 1, 2007 by 2.8 percent. Traffic fees are not expected to be changed in 2007.

In 2006, the NCA initiated a controlling process on price cap compliance in all three areas (universal services, residential and business access). We submitted the data required by the enquiry. We were not certain about the calculation method used by the NCA. As a result, there was a briefing on our request on December 15, 2006, at which the NCA informed us about the method to be used. According to the calculation of the NCA, we have breached the price cap by 5.9 percentage points, however, we have not received an official resolution yet. We dispute the correctness of the method set forth by the NCA. There was another consultation on February 15, 2007, at which the representatives of the NCA seemed to accept two of our propositions, but these were not yet officially accepted by the NCA s committee. The sanctions can include a fine (approximately HUF 250 million) and/or the obligation to reduce our residential subscription fees (a two percent reduction would mean a revenue loss of about HUF 1 billion).

Rates for PSTN Access to the Internet

Since January 1, 2004, retail rates for PSTN access to the Internet are no longer regulated. Since 2002, however, a part of the charge billed to the customer 30 percent in peak time and 10 percent in off-peak time must be transferred to ISPs. In the case of flat rate Internet access, 13 percent of the fee must be shared with ISPs. This type of revenue sharing remains in operation under the Electronic Communications Act. Since January 1, 2004, Internet call origination and Flat Rate Internet Access Call Origination (FRIACO) services are part of the RIO and the prices of these services are also regulated within the scope of the RIO (rates approved by the NCA).

Leased Line Fees

After our concession ended in the area of leased lines required for interconnection, the leased lines market became unregulated in 2002. In 2005, we were identified as an operator with SMP on the retail market of a minimum set of leased lines and on the wholesale market of terminating segments of leased lines. In both cases we have been identified as the only operator with SMP in Hungary.

For the leased line termination market, the SMP resolution has adopted the retail minus pricing rule, requiring us to provide all wholesale leased line access services at prices approximately 33 percent lower than the listed retail prices. We are also required to provide all services identified in the resolution nationwide. On October 11, 2006, the court abolished this resolution of the NCA, and obliged it to carry out a new process for determining SMP obligations for us on the wholesale leased line market. The court s decision is not binding.

Regulated Wholesale Prices

Since December 23, 2001, the interconnection rates are no longer regulated on an itemized basis but as part of the RIO. Since January 1, 2004, local bit-stream access must be offered as part of the RUO, which also regulates pricing for the local bit-stream access. The cost methodologies used in the reference offers are provided in the Ministerial Decree 18/2003 (XII.27.) IHM on cost calculation of electronic telecommunications services. The cost-based unbundling and interconnection rates must be approved by the NCA. The reference offers must contain approved rates.

The NCA has published its SMP resolution with respect to the wholesale broadband market, and identified Magyar Telekom Plc., as well as all other LTOs, as operators with SMP. The SMP resolution adopted a retail-minus pricing rule for the wholesale broadband market. According to the resolution, the NCA intends to transform the local bit-stream access service currently provided by us into a nationwide bit-stream access service. Pricing for the local bit-stream access service is currently regulated on a cost-based rule under the RUO.

We have been identified as an operator with SMP in the voice termination and origination market and the wholesale market on unbundling of copper loops, along with all other LTOs. These SMP resolutions included obligations to submit RIO and RUO to the NCA. The NCA also adopted cost-based pricing rules, based on Long Run Incremental Costs (LRIC) for the RIO and Fully Distributed Costs (FDC) for the RUO. We submitted our first draft RIO in June 2005 and first draft RUO in October 2005. After several rejections and repeated submissions the NCA accepted our RIO on May 3, 2006 and our RUO on September 11, 2006. The RIO took effect from September 15, 2005 retrospectively and the RUO from January 20, 2006 also retrospectively. On December 12, 2006 the court abolished the NCA s decision that the RIO fees would take effect retrospectively from September 15, 2005. The court s decision is not binding.

Other Wholesale Prices

The Electronic Communications Act provides that network access fees be set based on a number of objective criteria, with transparency and without discrimination. The cost of wholesale access services are now required to be calculated based on LRIC and the pricing for these services must be approved by the NCA, even if the service provider is not obliged to make a reference offer for these services.

Network Access and Interconnection Agreements between Magyar Telekom and ISPs

We enter into network access agreements with ISPs to secure access to services provided by ISPs for our subscribers. In addition to the network access agreements, we may enter into interconnection agreements with ISPs. The terms and conditions for the network access agreements must be in line with the terms and conditions of the existing subscriber contracts.

Reverse Charging Agreements between Magyar Telekom and ISPs

We have entered into reverse charging agreements with a number of ISPs. Under these agreements, customers remit payment for Internet services to the ISPs rather than directly to us. This scheme allows ISPs to offer various price plans based on their customers needs.

Price Squeeze (Predatory Pricing) Issues

Under the Electronic Communications Act, service providers with SMP are prohibited from pricing retail network services below their wholesale prices. When service providers reduce their end user prices and it causes a price squeeze , they are obliged to proportionally reduce their prices in their reference offers. This provision only applies if the price reduction affects more than 10 percent of subscribers for the service, or the impact of the price reduction exceeds five percent of net sales of the service.

If the regulatory authority identifies a price squeeze, the NCA examines whether the price of the network service is in line with the incurred costs. If the network prices are cost-based, the NCA refers the case to the Competition Authority. If the network prices are not cost-based, the NCA determines the minimum mandatory margin between the price of the network service and the end user service and/or orders the service provider to modify the reference offer.

Hungarian Mobile Operations

Market Assessment, SMP Designation Process and Interconnection

Upon request for interconnection (to provide either network access or network interconnection) from another telecommunications operator, TMH is required under the Electronic Communications Act and a related decree to provide such services, if such request is reasonable on both technical and economic grounds and provision of such services is not impossible due to the limitation of resources.

See Item 8 Legal proceedings for developments on TMH s SMP designation process and interconnection rates.

Macedonian Fixed Line and Mobile Operations

Pricing for most of the retail services provided by Maktel is regulated by Maktel s Concession Contract. Pricing and maximum change in prices for these services are based on the price cap method.

In addition, according to the ECL, based on market analysis the Agency for Electronic Communications may impose retail price regulations and price controls on operators with SMP in a relevant market. The SMP operator is obliged to keep separate accounting records for its wholesale and retail activities.

Pricing for dial-up and ADSL access to the Internet, however, is currently unregulated.

Regulated Wholesale Prices. During 2006, the Agency for Electronic Communications approved Maktel s interconnection and unbundling fees (MATERIO and MATERUO) based on the fully distributed cost accounting method. However, the current interconnection fees between Maktel and two mobile operators, and between the two mobile operators themselves, are still established based on former interconnection agreements and not yet harmonized with MATERIO. According to the relevant bylaw, Maktel is obliged to implement long run incremental costing methodology for interconnection and unbundling prices by July 2007.

On December 21, 2006, the Agency for Electronic Communications decided to change the interconnection fees. The level of the new fees was determined according to benchmarks and was mainly based on Maktel s retail fees without taking into account the costing model prepared by Maktel as prescribed by the relevant law. On February 14, 2007, the Agency for Electronic Communications decided to change the unbundling fees based on benchmarks.

The level of wholesale regulated prices directly depends on the finalization of the price adjustment of Maktel s retail regulated prices. In case Maktel does not increase its retail prices, that can lead to significant decrease of wholesale regulated prices.

Pricing for mobile telecommunications services is currently unregulated. Under the Law on Electronic Communications, however, the National Regulatory Agency is empowered to regulate the pricing of the retail mobile services, in case concern over competition arises.

ORGANIZATIONAL STRUCTURE

MagyarCom, which is fully owned by Deutsche Telekom, owns 59.21 percent of outstanding ordinary shares of Magyar Telekom.

For a list of principal operating subsidiaries and associates of the Company as of December 31, 2006, see Note 2.2 (b) to the consolidated financial statements.

PROPERTY, PLANTS AND EQUIPMENT

We have one of the largest real estate holdings in Hungary. We use substantially all of these properties for telecommunications installations, computer installations, research centers, service outlets and offices. Our equipment and machinery primarily consist of switches, communication towers and other telecommunications equipment.

Due to the consolidation of various operations, the conversion to digital switches and ongoing staff reductions, we anticipate that a substantial portion of our owned and leased properties will not be necessary for our core business in the future. We intend to sell or rent our surplus properties.

We intend to rely fully on outside providers of facility and real estate management services in the medium-term. We are accordingly developing a new service-based contract structure and intend to terminate all our remaining in-house real estate management functions. Our aim is to secure reliable facility and real estate services at the needed quality level and at prices that allow flexible management of our changing real estate portfolio and reduction of real estate management expenses.

Since February 2005, Magyar Telekom Plc. s real estate development, investment, operations and management activities have been outsourced to DeTe Immobilien-Hungary Zrt. The Company s real estate department, however, continues to handle strategic management and control of its real estate holdings.

Maktel outsourced its real estate management operations to a third party starting from April 1, 2006.

The number of sites used by Magyar Telekom is approximately 7,800, out of which approximately 2,800 sites are owned by the Company and approximately 5,000 sites are leased. The total area of properties used by Magyar Telekom as of December 31, 2006 was approximately 1,200,000 m2.

The majority of sites used in our operations are smaller than 100 m2. Approximately 55 percent of the total area is used to house telecommunications equipment and other technical devices. The largest site is our headquarters building located at Krisztina krt. 55 in Budapest, with floor space of 35,000 m2.

INFRASTRUCTURE AND TECHNOLOGY

Hungarian Fixed Line Operations

The following table provides information on the length of the copper and fiber optic cables contained in Magyar Telekom Plc. s access, backbone and rural area networks in Hungary at December 31, 2006, and each of the two prior years in kilometers:

	At December 31, 2004 (in kilometers)	2005	2006
Copper cable	159,504	158,112	159,951
Fiber optic cable	13,580	14,376	15,026

Expansion of Access Networks. At the end of 2000, we began to offer broadband Internet access services, based on the ADSL and Asynchronous Transfer Mode (ATM) technologies. We selected Ethernet-based Digital Subscriber Line Access Multiplexers (DSLAMs) to provide a more cost effective ADSL solution together with the ATM technology already in use. The ADSL transmission system provides high-speed digital access to any data network over existing copper wires without interruption of Plain Old Telephone Service (POTS) and ISDN2 services with the data speed of 512 Kbit/s and 1, 2, 3 and 6 Mbit/s. In 2006, we continued the roll-out of the ADSL technology nationwide. At the end of 2006, approximately 500,000 customers were using ADSL lines for connection to the Internet. By the end of 2006, our infrastructure allowed up to 2.1 million of our analog and ISDN2 subscribers to have access to the ADSL service. This represents coverage of over 1,000 towns and cities and approximately 87 percent of the population in our service area. In 2007, we plan to introduce the VDSL2 technology to provide high-speed data access with data speed of 25 and 50 Mbit/s.

We used fiber optic cables for our fixed line local loop networks for approximately 120,000 customers at the end of 2006. We installed a substantial amount of local network fiber optic cable in Budapest, where segments of the old cable network were in poor condition and where we believe the demand for high capacity and high quality transmission will be the greatest (e.g., shopping malls, industrial parks). We plan to extend our local fiber optic network both inside and outside Budapest to cover new business demands in existing areas, mainly to provide broadband services through optical access as well.

Wireless Solutions. In 2003, we introduced the WLAN technology in the access network for hot spot applications. By the end of 2006, 440 hot spot sites were in operation. With this technology, we can provide Internet access service in public areas to customers requiring temporary Internet access (e.g., conference centers, exhibitions, airports, hotels). Since the end of 2004, WLAN users of TMH and Magyar Telekom Plc. can use hot spot sites operated by either entity.

We have been selectively applying radio technology in our local loops since 1996. At the end of 2006, approximately 71,444 subscriber lines were based on the radio technology.

Backbone Network. We have a digital fiber optic national long distance network that connects local primary area networks. We have implemented the DWDM technology and Synchronous Digital Hierarchy (SDH) systems in both the national long distance and Budapest networks. The countrywide DWDM backbone network, installed in 2006, provides high capacity (maximum 64 times 10 Gbit/s) in the most important nodes of Hungary, as well as in international directions. In 2006, we carried on an extension of the DWDM network. In addition to cost advantages, SDH systems provide a flexible transmission infrastructure with automatic transmission paths. We introduced a new generation of the SDH system that, besides increasing network availability and transmission capacity, enables new services, such as data transmission (e.g., Ethernet). In 2006, the increase in the capacity of the backbone network served the growing demand of IP core network and HSLL. The HSLL is mainly provided for mobile operators. Since we currently have a robust optical backbone network, we have no immediate plan for expansion.

IP/MPLS. Since 2000, we have provided Internet access and IP-VPN services on the same IP/MPLS platform. The network is built-up of STM-16, Gigabit Ethernet and 10GE connections. The network has several access options (dial-up, leased line, broadband DSL, CATV) with PoPs in each primary area in Hungary. Available services include IP-VPN (scalable interconnection for corporate sites with Integrated Voice and Data option), IPSec and xDSL to Virtual Private Networks, Virtual Private Dial-up Network and wholesale Internet services for ISPs. The connectivity network that concentrates xDSL traffic towards the IP core is based on ATM and Ethernet technology. In 2006, we started to develop carrier-grade IP core network to be able to ensure high availability, demanded quality of service, scalability and security for triple-play, VoIP and broadband data communication services, and also for the common T-Com and T-Mobile IP platform. In 2006, significant capacity, quality and functional upgrades have been performed, including the development of the countrywide 10 Gbit/s core network, installation of new Gigabit Ethernet

(GE) and 10 GE connections, duplications of devices to increase redundancies, change of old devices etc. Further Quality of Service (QoS) and high-availability features are planned in the next three years in order to increase network capacity according to traffic demand, to install new network functions and to develop connectivity and integrity with different communication networks to become an appropriate transport platform for Next Generation Network (NGN) and triple-play services.

We are making preparations for interconnection and convergence of voice and data networks, which are currently separate. The NGN concept has been espoused as a long-term project. We do not plan to develop our traditional (such as PSTN/ISDN) network further except for maintenance and legal compliance purposes. The key focus instead will be on development of technologies and networks compatible with or forming a part of NGN, such as VoIP. In 2005, Voice-over CATV, Integrated Voice and Data service (IP Complex Plus) and Voice-over Internet (KLIP) have been introduced. In 2006, we continued to deploy a carrier-grade multi-service NGN. We also launched the commercial IPTV service at the end of 2006 together with T-Online. An IP Multimedia Subsystem was installed in 2006, which is considered to be the base for feature-rich, IP-based, Publicly Available Telephone Service (PATS). In 2007, we continue to deploy a carrier-grade multi-service NGN and launch new services, such as IP Centrex.

Information Technology. We have dedicated a significant amount of resources to improve our information technology systems. We believe that the continuing development of these systems is essential to improving customer service and the efficiency and productivity of our employees.

Our nationwide operational support system integrates the following elements:

- CRM;
- Billing, e-billing;
- automated call collection;
- network traffic management;
- workforce and workflow management;
- element, network and service management (configuration, alarm management, SLA management); and
- process controlled technical inventories.

This operational support system environment permits us to focus on our customers needs, to offer more personalized services, itemized billing, to bundle products and services in price plans and to generate a single bill for customers with multiple locations. In 2006, a project has been established to develop and implement the Next Generation Support System (NGOSS) concept to support the new triple-play and NGN platform based services.

Hungarian Mobile Operations

GSM Network. TMH operates a nationwide GSM public digital mobile network in the 900 MHz band with 8 MHz duplex spectrum since 1994, in the 1800 MHz band with 6 MHz duplex spectrum since 1999 and in the 1800 MHz band with a total of 15 MHz duplex spectrum since January 2004. To guarantee the best possible service quality for our customers, we are dedicated to the continuing network roll-out to meet traffic and coverage demands.

Coverage. By the end of 2004, coverage of villages with population between 1,000 and 10,000 was 97 percent. This level was further increased up to 99 percent by December 31, 2006. The deep indoor coverage was 97 percent in Budapest and 96 percent in cities over 100,000 inhabitants by the end of 2004.

The deep indoor coverage in cities over 100,000 inhabitants, including Budapest, was increased up to 97 percent as of December 31, 2006.

EDGE Packet Switched Data Service. At the end of 2003, commercial EDGE service was launched in approximately 23 percent of Budapest area. By the end of 2004, EDGE coverage reached 91 percent of Budapest. In 2005 and 2006, the EDGE development project was continued, resulting in 59 and 74 percent population coverage by the end of the year, respectively. The peak data rate was increased to around 200 Kbit/s in 2005.

Universal Mobile Telecommunications System. The 3G network enables besides rapid data transmission and video-telephone more comprehensive and interesting contents than before, including, in addition to image and text, fast transmission of high quality multimedia materials. In December 2004, TMH was awarded a 3G service license and was granted the use of 15 MHz duplex and 5 MHz unpaired 3G spectrums until 2019. In August 2005, TMH launched commercial UMTS service, first in Hungary. By the end of 2005, UMTS coverage increased to 43.6 percent of Budapest. On May 17, 2006, TMH launched commercial HSDPA service in the internal districts of Budapest, first in Hungary. From the last quarter of 2006, each 3G cell is capable of HSDPA, therefore the UMTS/HSDPA population coverage reached 30.3 percent by the end of 2006. The network allows 3.6 Mbit/s downlink speed, however most of the currently available mobile phonesets support only 1.8 Mbit/s.

WLAN project. In the frame of the WLAN program Small settlements , 110 access points have been rolled out during 2006 making Internet Fix service available in 120 settlements.

Special Project TETRA. TMH took part in the exclusive mobile tender of the Hungarian Government. A new entity, Pro-M, was established for providing TETRA services for governmental organizations. The network uses the 380-400 MHz spectrum, applying TETRA technology. By December 2006, TMH completed the development of 225 sites and four switches according to the roll-out program.

Information Technology. TMH s operations are supported extensively by IT solutions. A great number of closely integrated application systems are used in sales, customer service, collection, service provisioning, call data processing (mediation) and charging, fraud management, billing, handset logistics, interconnect billing, general ledger reporting and electronic document archiving.

TMH operates proprietary Data Warehouse (DWH), which provides management and endorsers with business reports and marketing and finance analysts with detailed subscriber, traffic and business information for on-line interactive analysis. DWH is playing a major role in customer segmentation and customer life-cycle value calculation.

Macedonian Fixed Line Operations

Maktel endeavors to maintain its network at a high technological level to offer and provide a wide range of products and services that will satisfy customers demands.

The PSTN/ISDN network in the Republic of Macedonia has been fully digitalized since the end of 2003. The liberalization of the telecommunications market required Maktel to perform a substantial upgrade of the PSTN/ISDN platform. With the upgrade, switching systems are now able to support carrier selection and pre-selection functions.

Maktel s primary area networks are connected to the fiber optic national long distance network. The SDH technology has been implemented in the backbone network, in the transmission networks in Skopje and other cities in the country. For connection of Remote Subscriber Units, Plesiochronous Digital Hierarchy (PDH) equipment is used as well.

The existing copper-wire network is a good basis for introduction of broadband services based on the DSL technologies. At the end of 2003, Maktel introduced broadband Internet access services based on the ADSL technology. Optical cables in the access network are used for connection of key business customers.

The core of the IP backbone network is built on the Gigabit Switch Routers (GSR) platform. The core is connected to the global Internet network through two main internet gateways. Available services include IP-VPN, ADSL, dial-up Internet access, wholesale Internet services for ISPs, web services, content oriented services and video streaming. In 2006, Maktel has installed Intrusion Detection and Prevention System in order to protect its users from Denial of Service (DOS).

In 2006, Airspan-based VoIP platform was installed in the network for the purposes of terminating and originating international VoIP calls as well as for providing business VoIP services.

In 2006, Maktel installed a Service Selection Gateway platform. It is based on Cisco Systems solution and provides bandwidth on demand, walled garden, anti-virus and anti-spam services to its Internet subscribers. The migration from frame relay to IP-VPN solutions was also finalized in 2006.

Macedonian Mobile Operations

T-Mobile Macedonia has built a high quality and high capacity network that meets the requirements and needs of its growing subscriber base. Our rating and billing platforms provide enhanced services for the entire prepaid and postpaid customer base as well as for the interconnection partners. Our comprehensive solutions for promotions, discounts and incentives provide extensive flexibility for tailored offerings and customer satisfaction.

ENVIRONMENT PROTECTION

The management committee of Magyar Telekom adopted the Sustainability Strategy of the Company in January 2005 to strengthen our commitment to sustainable development.

As a part of our commitment to sustainability, we developed a sustainability section for Magyar Telekom s website. This section includes our reports and news relating to sustainability and discusses our philosophy and approach to sustainability.

ITEM 4A UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 5 OPERATING AND FINANCIAL REVIEW AND PROSPECTS

The following discussion should be read together with the consolidated financial statements, including the accompanying notes, included in this annual report. The consolidated financial statements, the accompanying notes as well as the discussion of results presented below have been prepared in accordance with IFRS. IFRS differs in certain respects from U.S. GAAP. For a discussion of the principal differences between IFRS and U.S. GAAP as they relate to us, see Note 37 to the consolidated financial statements. Revenues and operating expenses discussed under Results of Operations By Segment do not reflect intrasegment and intersegment eliminations.

OPERATING RESULTS

Results of Operations Total

Basis of presentation

We determine segments primarily based on products and services that are subject to risks and returns different from those of other businesses. In 2004, we changed our segment disclosure as a result of the change in our management and reporting structure. The primary segments are based on the business lines (fixed line and mobile operations), which include both Hungarian and international activities. Reported segments are consistent with information used by management for internal reporting and monitoring purposes. In addition, our secondary format for reporting segment information is geographical segments.

In 2005, Magyar Telekom acquired a 76.53 percent interest in Crnogorski Telekom. Crnogorski Telekom s balance sheet was consolidated in our accounts as of March 31, 2005, and the results of Crnogorski Telekom are included in our consolidated income statement from the second quarter of 2005.

Magyar Telekom has reassessed its status in the provision of a number of value added services, where revenue was accounted for on a gross basis implying a principal status rather than an agent status in the provision of the service. A gross basis means that revenues included the full amount of fees collected from customers, and payments to related service providers were included in operating expenses. After analyzing the relationships with our subcontractors one by one, we have changed our judgment of the situation in some cases and determined that in these cases the Group is more the selling agent of these products than the principal provider of the service.

This change had a decreasing impact on the Fixed line Voice retail revenues and the Mobile Non voice revenues, with equivalent corresponding effects in operating expenses. The change resulted in netting revenues with expenses, and has no impact on operating profit, net income or equity. Prior year s reported numbers have been restated accordingly. See Note 2.1.7 to the consolidated financial statements.

The Group has changed its accounting policy to disclose the Hungarian local business tax and innovation fee as income taxes as we have established that these taxes have the characteristics of income taxes rather than operating expenses. In previous years, these taxes were disclosed among operating expenses.

This change in the disclosure of these taxes had a decreasing impact on operating expenses and an equivalent increase in income taxes. The change resulted in no impact on net income or equity. Prior year s reported numbers have been restated accordingly. See Note 2.1.7 to the consolidated financial statements.

Total Revenues

Our total revenues grew by 9.1 percent from HUF 615,054 million in 2005 to HUF 671,196 million in 2006. The increase in revenues was mainly due to higher revenues from mobile telecommunications services, which grew by 14.5 percent from 2005 to 2006, driven mainly by Pro-M s EDR activities in the Hungarian mobile operations. The higher system integration and IT revenues as well as higher broadband

Internet revenues also contributed to the growth, and were only partly offset by lower revenues from outgoing domestic and international traffic in the fixed line telecommunications services. The longer consolidation period (12 months in 2006 compared to nine months in 2005) of Crnogorski Telekom also contributed to the revenue growth.

Total Operating Expenses

Our total operating expenses increased by 11.9 percent from 2005 to 2006. Operating expenses amounted to HUF 481,309 million in 2005 and HUF 538,380 million in 2006. Our total operating expenses as a percentage of total revenues increased from 78.3 percent in 2005 to 80.2 percent in 2006.

Depreciation and amortization and employee-related expenses are our most significant operating expenses.

Depreciation and amortization increased by 6.6 percent from HUF 114,686 million in 2005 to HUF 122,249 million in 2006 mainly as a result of the consolidation of Crnogorski Telekom and the impairment of the Monet, TCG and Internet CG brandnames in connection with the rebranding in Montenegro in September 2006. In addition, depreciation increased at TMH due to the capitalized UMTS concession and also due to their higher gross asset base of telecommunications and IT equipment. As a result of the continuous revision of the useful life of our assets, the lives of certain assets were changed as of January 1, 2006. These assets mainly included IT equipments and software, and the change in life resulted in HUF 58 million higher depreciation expense in 2006.

Employee-related expenses increased by 2.7 percent in 2006 as compared to 2005 because of the inclusion of new subsidiaries (such as Pro-M, Dataplex and KFKI). Higher expenses resulted also from the severance provision recognized in connection with the headcount reduction program at Crnogorski Telekom and from higher severance expenses of Magyar Telekom Plc. in 2006. The total payment made in relation to employee termination in 2006 amounted to HUF 6,099 million, of which HUF 2,639 million was charged against the provision for liabilities and charges as at December 31, 2005, while the rest was recognized as employee-related expense in 2006.

Other operating expenses include materials, maintenance, marketing, service fees, fees and levies, outsourcing expenses, energy and consultancy. Other operating expenses increased by 13.5 percent in 2006 compared to 2005 primarily due to higher fees for outsourcing services (e.g., real estate management, transportation, customer service and informatics) as well as higher expenses in connection with various projects. The significant increase in materials and maintenance fees was driven by the consolidation of new subsidiaries such as Dataplex and KFKI. In 2006, higher concession fees were due to the UMTS fee paid by TMH and to increased frequency fees at T-Mobile Macedonia. Non-rebranding related marketing expenses increased significantly as well at Magyar Telekom Plc., due to more intensive advertising activity in 2006.

In the course of conducting their audit of our 2005 financial statements, PwC identified certain contracts the nature and business purposes of which were not readily apparent. PwC notified the Audit Committee and advised them to retain independent counsel to conduct an investigation into these contracts. Our Audit Committee retained White & Case, as its independent legal counsel, to conduct the investigation. See Item 3 Risk Factors and Item 15 Controls and Procedures.

In 2006, Magyar Telekom incurred HUF 4.1 billion expenses relating to the investigation, which are included in other operating expenses in the Hungarian fixed line operations. This amount includes HUF 3.3 billion legal fees, HUF 0.3 billion audit-related fees and HUF 0.5 billion fees paid for legal counsel representing our current and former employees.

In 2005, other expenses include HUF 2,059 million paid under four consulting contracts entered into by Magyar Telekom Plc. and two of its subsidiaries as to which it has not been able to obtain sufficient

evidence that it or its subsidiaries received adequate value. This amount also includes the tax implications of the payments as well.

Total Operating Profit

Our total operating profit decreased by 3.8 percent from HUF 141,754 million in 2005 to HUF 136,391 million in 2006 due to the fact that the increase in expenses was higher than the growth in revenues.

Outlook

The telecommunications industry is undergoing a major change globally. We have observed several long-term trends which are changing the structure of the Hungarian telecommunications market. Key drivers of the long-term trends include changes in technology (i.e., IP-based broadband products and solutions, emerging wireless broadband technologies), customer requirements (i.e., mobility and ease of use, triple-play solutions), competition and regulation (i.e., low entry barriers, new business models).

To adapt to these changes in the market, we are now moving from the traditional traffic-based revenue structure to an access-based revenue structure, which will allow us to substitute declining traffic revenues with content, entertainment and bundled access revenues. In addition, we are seeking new revenue sources by entering into new non-traditional converged telecommunications markets.

We should emphasize that each segment is affected by its unique business environment, and we are subject to circumstances and events that are yet unforeseen or beyond our control. We have identified several risk factors which may affect our business in the future including changes in the regulatory environment, changes in competition, the unforeseeable effects of the announced stabilization package of the Hungarian government and changes in the foreign exchange rates just to mention the most important ones. See the detailed description of these and other risk factors in Item 3 Risk Factors .

Magyar Telekom s current plans and outlook are based on our current best knowledge and expected circumstances. Nevertheless the behavior of our competitors can hardly be completely predicted. Therefore a stronger than assumed impact of alternative operators, new market entrants and new solutions in any country where Magyar Telekom is present could influence our business performance negatively.

We expect that our core business units will be able to continue to generate strong free cash flow. However, there are some significant elements that can have negative effects on the free cash flow, for example, the roll-out of EDR infrastructure and potential acquisitions. Despite these effects we expect to generate solid positive free cash flow in 2007 as well.

Revenues

The following reflects our current expectations with respect to our segmental plans and initiatives:

Fixed line segment

In the fixed line segment, we expect continued gradual decline in fixed line voice revenues due to continued line reduction and fixed line unit price erosion driven by mobile substitution and the increased competition in the fixed line market, including competition from PSTN resellers and VoIP or VoCATV providers. As indicated in our strategy, to mitigate the decrease in fixed line voice revenues we are now moving from the traditional traffic-based revenue structure to an access-based revenue structure, which will allow us to substitute declining traffic revenues with content, entertainment and bundled access revenues.

As the leading broadband provider in Hungary, we are committed to accelerating growth in country-wide broadband penetration by applying a multi-access cost-efficient approach. In November 2006, we launched IPTV services; in early 2007 we doubled bandwidths on our network by utilizing ADSL2 technology and sought to further boost market development by introducing naked DSL services.

We aim to move towards content and media businesses to support traditional access services and build new revenue streams and exploit new revenue sources. Accordingly, in April 2006, we gained control of iWiW Kft., the leading Hungarian online social network, which has currently more than two million users registered. In May 2006, we acquired Adnetwork, the leading domestic online advertisement networks to leverage the online advertisement potential of T-Online and partner web pages.

To maintain sustainable competitiveness in the corporate sector, we have committed to further developing our IT competencies by focusing on complex service offering via managed services, system integration and outsourcing through consultancy-based selling to corporate customers. This strategic initiation is promoted by the acquisition of KFKI Group in June 2006 and Dataplex in April 2006. Expanding our business operation to these new areas with lower EBITDA margins results in a dilutive effect in the EBITDA margin both on fixed segment and Magyar Telekom Group level.

In addition, we are seeking new revenue sources by entering new non-traditional telecommunication markets such as transactional services and commerce to generate new revenue streams in case a potential business opportunity arises to capture potential growth opportunities on new converged market areas.

We also had higher contributions from Crnogorski Telekom in 2006 since the consolidation commenced in April 2005. International PoP and alternative operations are expected to contribute increased revenues as well. Especially in the case of our Bulgarian subsidiary (Orbitel) are we expecting a changing trend because since its EU membership commenced in January 2007, Bulgaria has to apply the EU regulation in the telecommunication sector as well.

In Montenegro, the de facto exclusivity of Crnogorski Telekom in international voice traffic has come to an end as Promonte, the Montenegrin market leader in mobile telephony has acquired a license for international voice traffic valid from January 1, 2007. There are several public tenders ongoing in Montenegro having a significant long term effect on the telecommunication market. The Montenegrin Telecommunication Agency has announced a public tender for cable television services, in which 10 companies got licenses. As a result, new cable television service providers may enter traditional telecommunications markets in 2007. The Montenegrin Telecommunication Agency has also announced public tenders for providing telecommunication services using WiMAX technology. These tenders will influence the level of competition in Montenegro.

Mobile segment

In the mobile segment we expect continuing growth in net revenues at TMH, T-Mobile Macedonia and T-Mobile Crna Gora as well. Market penetration in Hungary is now almost saturated, and we expect lower growth rates due to a smaller number of potential new subscribers. This trend is partly offset by the migration of prepaid customers to postpaid packages and the future growth potential of higher-value services, which is supported by the launch of UMTS and HSDPA services. Accordingly, leveraging first mover advantage on our newly built HSDPA capacities is one of T-Mobile Hungary s primary strategic priorities on the fast growing wireless broadband market.

We won the EDR tender of the Hungarian government and will provide TETRA services for 10 years. Significant revenue contribution was realized from this project already in 2006. The EDR system implementation resulted in significant increase in revenues and also in the cost of equipment sale in 2006. Looking forward to 2007, this significant one-off revenue and cost of telecommunications equipment sale will be eliminated resulting in lower revenues and accordingly also lower cost of equipment sale on this field of operation.

In the Macedonian and Montenegrin market, subscriber growth continued in 2006 and drove the net revenue growth. For 2007, we expect a slowdown of subscriber growth in both countries.

The government of Macedonia has approved Austrian Mobilkom s bid to become the country s third mobile operator at the beginning of 2007. The Austrian firm was the sole company to submit a bid on the tender for the third license. Under the license rules, the new operator must launch services within six months of being granted the license. Therefore the successful bidder is expected to launch its operation by July 2007.

The Montenegrin Telecommunication Agency has announced public tenders for providing 3rd Generation mobile services and a combined new license to provide 2G/3G mobile telephony services in Montenegro. The outcome of this tender will definitely influence the market development in Montenegro.

Expenses

In line with our strategy, we plan to improve our internal operational efficiency in all segments. Our initial 2006 goal to improve the efficiency of our workforce by increasing the fixed lines (B-channel equivalent) per employee ratio to over 500 (a ratio that corresponds to the best practice in Western Europe) was already reached by the end of February 2006. We are targeting further headcount reductions in our Macedonian and Montenegrin fixed line service providers. We are determined to bring their performance in line with industry best practice and our management is committed to further simplification and improvement of processes and connected systems. In addition to organizational measures and process improvement, we seek cost savings by leveraging our group-wide synergies in procurement.

The merger of Magyar Telekom Plc. and TMH enables us to further improve efficiency. We are expecting significant value generation through the gradual implementation of the integration by seizing additional revenues and optimizing operating and capital expenses. In 2006, the first impacts from the fixed-mobile integration in terms of sales and customer retention began to be seen. These were, however, offset by related costs. In the next three years we expect to see a significant positive impact, with net present value of these benefits currently estimated to be around HUF 60 billion in the period of 2007-2009. The integration of our fixed and mobile businesses will particularly enhance our competitiveness in the areas of customer care and customer service, products and value propositions, back-office and supporting systems and joint network infrastructure management.

Gross additions to tangible and intangible assets

We aimed to reduce the gross additions to tangible and intangible assets to sales ratio to below 15 percent in 2006 and succeeded in meeting this target. We are targeting this ratio to fall below 14 percent in 2007 excluding potential acquisitions. We expect an increasing proportion of gross additions to relate to high-growth areas in the fixed line segment, such as Internet, broadband and data transmissions, while our mobile segment will continue the roll-out of the UMTS and HSDPA infrastructure.

According to our strategic directions we are committed to further strengthening and leveraging our presence in the South-East European region. Therefore, we are continuously seeking for further value-creating acquisition and investment targets with even larger scale.

Revenue and EBITDA targets

Based on our former outlook and market and regulatory conditions, we expected to achieve compounded average revenue growth rate of at least three percent for the period of 2006-2007. In terms of EBITDA, we targeted to maintain the 2005 reported EBITDA level in 2006. At the end of 2006, we were fully on track to meet both of these targets. Looking forward to 2007, we are targeting stable revenue and EBITDA in forint terms over 2006 reported figures.

Results of Operations By Segment

The following table sets forth revenues, operating expenses and operating profit by segment:

	Year ended December 31,		
	2004	2005	2006
	(in HUF millions)		
Revenues			
Hungarian Fixed line	298,707	284,985	292,193
International Fixed line	45,693	57,983	68,953
Total	344,400	342,968	361,146
Less: intra-segment revenues	(1,271)	(2,284)	(3,569)
Total revenue of Fixed line segment	343,129	340,684	357,577
Less: inter-segment revenues(1)	(11,146)	(11,478)	(13,711)
Fixed line revenue from external customers	331,983	329,206	343,866
Hungarian Mobile	260,568	266,217	297,209
International Mobile	33,734	42,693	52,399
Total	294,302	308,910	349,608
Less: Intra-segment revenues	(58)	(27)	(42)
Total revenue of Mobile segment	294,244	308,883	349,566
Less: inter-segment revenues(1)	(29,435)	(23,035)	(22,236)
Mobile revenue from external customers	264,809	285,848	327,330
Total revenue of the Group	596,792	615,054	671,196
Operating expenses net			
Hungarian Fixed line	280,766	239,716	260,065
International Fixed Line	38,669	49,022	57,461
Total	319,435	288,738	317,526
Less: intra-segment expenses	(1,271)	(2,284)	(3,569)
Total operating expenses net of Fixed line segment	318,164	286,454	313,957
Hungarian Mobile	200,861	190,998	221,532
International Mobile	24,687	30,388	35,304
Total	225,548	221,386	256,836
Less: intra-segment expenses	(58)	(27)	(42)
Total operating expenses net of Mobile segment	225,490	221,359	256,794
Less: inter-segment expenses(1)	(40,581)	(34,513)	(35,946)
Total operating expenses net of the Group	503,073	473,300	534,805

(1) Inter-segment eliminations include primarily interconnection fees between the fixed line and mobile networks.

	Year ended December 31,		
	2004	2005	2006
	(in HUF millions)		
Segment results (Operating profit)			
Fixed line Hungary	17,941	45,269	32,128
Share of associates profits (Hungary)	1,896	330	703
Fixed line Foreign operations	7,024	8,961	11,492
Fixed line segment	26,861	54,560	44,323
Mobile Hungary	59,707	75,219	75,677
Mobile Foreign operations	9,047	12,305	17,095
Mobile segment	68,754	87,524	92,772
Less: Share of associates profits	(1,896)	(330)	(703)
Total operating profit of the Group	93,719	141,754	136,391

(1) Inter-segment eliminations include primarily interconnection fees between the fixed line and mobile networks.

Fixed Line Telecommunications Segment

The fixed line segment includes Magyar Telekom Plc. and its consolidated subsidiaries, other than T-Mobile Macedonia, T-Mobile Crna Gora, TMH and Pro-M.

Revenues

Our fixed line telecommunications segment includes local, domestic and international long distance telephone services as well as value added digifon services such as call waiting, itemized billing and telephone and private branch exchange equipment rental. This segment also consists of revenues from related services, such as leased lines, data transmission, Internet, SI/IT, equipment sales and cable television.

Hungarian Fixed Line Operations

Hungarian fixed line operations include Magyar Telekom Plc. and its consolidated subsidiaries, other than TMH, Pro-M and our foreign subsidiaries.

The following table sets forth information regarding Hungarian fixed line revenues:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Subscriptions	79,577	80,261	81,897	0.9	2.0
Domestic outgoing traffic revenues	91,452	67,717	49,034	(26.0)	(27.6)
International outgoing traffic revenues	8,528	6,835	5,524	(19.9)	(19.2)
Value added, cable voice and other services	8,780	7,342	6,895	(16.4)	(6.1)
Voice-retail revenues	188,337	162,155	143,350	(13.9)	(11.6)
Domestic incoming traffic revenues	8,120	9,429	8,256	16.1	(12.4)
International incoming traffic revenues	9,969	9,050	9,905	(9.2)	9.4
Voice-wholesale revenues	18,089	18,479	18,161	2.2	(1.7)
Voice revenues total	206,426	180,634	161,511	(12.5)	(10.6)
Internet broadband	17,441	28,295	39,548	62.2	39.8
Internet narrowband, content and other	11,192	8,939	6,253	(20.1)	(30.0)
Internet revenues total	28,633	37,234	45,801	30.0	23.0
Data	27,642	27,508	27,087	(0.5)	(1.5)
System integration/Information technology	9,154	8,790	24,359	(4.0)	177.1
Multimedia	13,364	15,017	17,481	12.4	16.4
Equipment sales	5,104	5,530	4,444	8.3	(19.6)
Other revenues	8,384	10,272	11,510	22.5	12.1
Total fixed segment revenues	298,707	284,985	292,193	(4.6)	2.5

Subscriptions. Revenues from subscriptions consist of revenues from monthly subscription fees for price plans. Revenues from subscriptions are principally a function of the number and mix of residential, business and ISDN access lines and corresponding charges.

Revenues from subscription fees slightly increased both in 2005 and 2006 due to higher revenues from customized and supplementary price plans at Magyar Telekom Plc. resulting from increased number of customers choosing these plans. This increase was partly offset by decreased ISDN subscription fee revenues at Magyar Telekom Plc. as a result of the lower number of average ISDN connections and lower tariffs.

The table below sets forth information regarding average access lines in our service areas:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
				(% change)	
Average access lines in the service areas of Magyar Telekom Plc. and Emitel					
Residential	2,078,089	2,033,397	1,942,260	(2.2)	(4.5)
Business	264,858	255,207	242,192	(3.6)	(5.1)
Public payphones	28,966	23,822	21,706	(17.8)	(8.9)
Total	2,371,913	2,312,426	2,206,158	(2.5)	(4.6)
ISDN channels	530,622	515,900	493,766	(2.8)	(4.3)
Total	2,902,535	2,828,326	2,699,924	(2.6)	(4.5)

The number of lines decreased both in 2005 and 2006, as a result of migration of customers to mobile services and due to increased competition in the fixed line market.

Domestic outgoing traffic revenues. Domestic outgoing traffic revenues consist of traffic charges for local and domestic long distance calls placed by our subscribers. Domestic outgoing traffic revenues are a function of rates, the total number of telephone calls, the distribution of call duration, the time of day and the mix between more costly domestic long distance calls and less expensive local calls.

The following table sets forth the total minutes of domestic telephone traffic that our Hungarian fixed line subscribers generated, including calls from the fixed line network to mobile subscribers:

	Year ended December 31,			December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in thousands of minutes)			(% change)	
Domestic voice traffic at Magyar Telekom Plc. and Emitel	5,859,967	5,126,455	5,037,235	(12.5)	(1.7)

Domestic outgoing traffic revenues decreased in 2005 as compared to 2004 mainly as a result of decreased fixed line usage due to mobile substitution as well as intensive competition from other fixed line operators. The proportion of calls changed unfavorably as well, as the higher priced long distance and fixed-to-mobile traffic decreased to a greater extent than local traffic. The decrease in revenue is higher than the decrease in traffic, due to lower average per minute fees. In line with the decision of the National Regulatory Authority to reduce fixed-to-mobile termination rates, we recorded a reduction in the fixed-to-mobile revenues. The price discounts included in different price plans also contributed to lower outgoing domestic traffic revenues. At the end of December 2005, approximately 66 percent of Magyar Telekom Plc. s customers had chosen customized price plans, the most popular of which were the Felező plan with over 530,000 subscribers and the Favorit plan with approximately 325,000 customers.

Domestic outgoing traffic revenues decreased in 2006 as compared to 2005 mainly as a result of lower average per minute fees and loss of fixed line customers mainly owing to competition from other fixed line service providers and mobile substitution. Both Magyar Telekom Plc. and Emitel offered several price discounts to customers choosing different price plans. Customized price plans represented 83.4% of the lines at Magyar Telekom Plc. at December 31, 2006. The most popular of these plans were the Favorit plans with almost 550,000 subscribers, but our Felező plan also gained approximately 539,000 subscribers by the end of 2006.

International outgoing traffic revenues. International outgoing traffic revenues are a function of rates and the number, duration and mix of calls to destinations outside Hungary placed by our fixed line subscribers.

The following table sets forth information concerning outgoing international traffic:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in thousands of minutes)			(% change)	
International outgoing traffic at Magyar Telekom Plc. and Emitel(1)	133,773	113,315	98,723	(15.3)	(12.9)

(1) Excludes minutes from calls placed by subscribers of other local telephone operators and mobile service providers. Our revenues relating to these calls are included in revenues from domestic incoming traffic.

In 2005 and 2006, international outgoing traffic revenues decreased primarily as a result of lower usage due to the relatively high number of international calls placed by mobile subscribers and the rapid growth of private leased lines. The decrease also resulted from rate decreases due to various discounts provided to subscribers of optional price plans.

Value added, cable voice and other services. Revenues from value added, cable voice and other services consist of revenues from connection fees, fees for digifon services, rental charges for telephones and private branch exchanges as well as cable TV voice subscription fees.

Value added, cable voice and other services revenues showed a decrease both in 2005 and 2006 principally due to lower amortization of deferred revenues as amortization of connection fees collected ten years ago started to run out. In 2005, lower value-added services relating to Sulinet together with decreased PBX revenues at BCN Rendszerház Kft. also reduced revenues from other services.

These decreases were partly compensated by higher revenues from cable TV voice subscription fees reflecting strong increase in the number of VoCATV subscribers in 2006 as compared to 2005.

Domestic incoming traffic revenues. Domestic incoming traffic revenues include amounts related to domestic and international long distance services that we provide to other LTO or mobile customers. Incoming domestic traffic revenues increased in 2005 as compared to 2004 primarily as a result of higher LTO call origination and call termination traffic in line with the increased customer base of other fixed line service providers, partly offset by lower LRIC-based interconnection rates introduced on June 15, 2004. These increases were partly offset by decreased incoming domestic traffic revenues from mobile operators at Magyar Telekom Plc. resulting from lower traffic as well as lower interconnection rates mainly in mobile to international calls.

Domestic incoming traffic revenues decreased in 2006 as compared to 2005 due to lower traffic revenues from LTOs at Magyar Telekom Plc. due to the application of the new RIO prices based on NCA decision from June 2006 and applied retrospectively since September 2005. Revenues from call origination and call termination also declined as a result of lower RIO fees, partly offset by higher volume of traffic.

International incoming traffic revenues. International incoming traffic revenues consist of amounts paid by foreign carriers for the use of our network to carry calls placed by their customers.

The following table sets forth information concerning international incoming traffic:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in thousands of minutes)			(% change)	
International incoming traffic(1)	288,564	295,405	316,183	2.4	7.0

(1) Includes minutes from calls transited by Magyar Telekom Plc. and terminating with subscribers of Magyar Telekom Plc, other local telephone operators and mobile service providers. Does not include transit traffic and other international services via Hungary.

International incoming traffic revenues decreased in 2005 as compared to 2004 principally driven by the lower HUF/SDR average exchange rates. The volume of incoming international traffic somewhat increased as higher traffic terminated in Magyar Telekom Plc. and LTO areas was only partly offset by lower mobile terminated international traffic transited by Magyar Telekom Plc. (due to the migration of international calls to mobile networks).

International incoming traffic revenues increased in 2006 as compared to 2005 due to higher revenues at Magyar Telekom Plc. resulting from the increased volume of international incoming traffic and higher HUF/EUR average exchange rate, partly offset by lower average EUR settlement rates.

Internet broadband. Revenues from Internet broadband services increased in both 2005 and 2006 as a result of significant growth in the number of Internet subscribers, ADSL and cable TV customers. The proportion of higher revenue generating broadband Internet customers significantly grew within the customer base, which also contributed to the revenue growth. By the end of 2006, the total number of our broadband connections exceeded 572,000 in the Hungarian fixed line operations.

Internet narrowband. Revenues from Internet narrowband services decreased in both 2005 and 2006 reflecting the decrease in the volume of Internet dial-up traffic and lower number of Internet dial-up subscribers.

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
ADSL connections	205,886	329,314	512,810	59.9	55.7
Number of Internet subscribers					
Dial-up	111,638	80,938	31,401	(27.5)	(61.2)
Leased line	907	751	656	(17.2)	(12.6)
DSL	137,910	218,954	336,181	58.8	53.5
W-LAN	1,153	1,467	1,175	27.2	(19.9)
CATV	14,412	26,425	57,587	83.4	117.9
Total	266,020	328,535	427,000	23.5	30.0

Data. Revenues from data transmission services slightly decreased both in 2005 and 2006 mainly driven by lower narrowband retail revenues, partly offset by higher broadband data retail revenues (mainly HSLL) and higher broadband IP revenue at Magyar Telekom Plc.

System integration/Information technology. System integration (SI) and Information technology (IT) revenues decreased in 2005 as compared to 2004 primarily driven by lower revenues at X-Byte. In 2006, the strong increase in SI and IT revenues resulted mainly from the consolidation of KFKI and Dataplex revenues since their acquisitions in 2006. The increased number of SI/IT service projects at Magyar Telekom Plc. and BCN also had positive effects on revenues. The most significant projects were the outsourcing services provided to E.ON and Erste Bank, set-up of low current systems as well as SI and IT solutions provided to the Hungarian government (E-Közmű).

Multimedia. Multimedia revenues increased both in 2005 and 2006 mainly due to the growth in cable TV revenues resulting from the increase in the average number of cable TV subscribers and price increases.

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
Cable television customers	383,904	403,631	414,286	5.1	2.6

Equipment sales. Revenues from telecommunications equipment sales increased in 2005 as compared to 2004 due to the higher amount of equipment sold at Magyar Telekom Plc. during marketing campaigns and also due to increased sales of BCN Rendszerház Kft. In 2006, equipment sales revenue showed a decrease due to lower rental fees of telecommunications equipment and decreased PBX charges at Magyar Telekom Plc.

Other revenues. Other revenues include construction, maintenance, rental, wholesale infrastructure service and miscellaneous revenues.

Other revenues increased in both 2005 and 2006 mainly as a result higher amount of fees paid for real estate rental and IT services by DeTeImmobilien to Magyar Telekom Plc.

International Fixed Line Operations

The results of the international fixed line operations include our foreign subsidiaries, other than T-Mobile Macedonia and T-Mobile Crna Gora.

The following table sets forth information regarding international fixed line revenues:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
Subscriptions	9,359	10,317	11,611	10.2	12.5
Domestic outgoing traffic revenues	16,076	19,794	20,696	23.1	4.6
International outgoing traffic revenues	3,768	4,322	4,744	14.7	9.8
Value added, cable voice and other services	1,464	1,489	1,782	1.7	19.7
Voice-retail revenues	30,667	35,922	38,833	17.1	8.1
Domestic incoming traffic revenues	2,042	4,414	5,749	116.2	30.2
International incoming traffic revenues	6,437	7,885	11,335	22.5	43.8
Voice-wholesale revenues	8,479	12,299	17,084	45.1	38.9
Voice revenues total	39,146	48,221	55,917	23.2	16.0
Internet broadband	730	1,536	2,529	110.4	64.6
Internet narrowband, content and other	1,001	1,167	1,516	16.6	29.9
Internet revenues total	1,731	2,703	4,045	56.2	49.6
Data	3,046	5,224	6,633	71.5	27.0
System integration/Information technology	296	257	385	(13.2)	49.8
Multimedia	0	20	52	n.a.	160.0
Equipment sales	181	178	349	(1.7)	96.1
Other revenues	1,293	1,380	1,572	6.7	13.9
Total fixed segment revenues	45,693	57,983	68,953	26.9	18.9

Total revenues of the international fixed line operations were strongly affected by the inclusion of T-Com Crna Gora s revenues from the second quarter of 2005. In 2005, total revenues from international fixed line operations decreased by 2.6 percent without the consolidation of T-Com Crna Gora. In 2006, the depreciation of HUF against MKD and EUR had significant effect on the revenue increase of Maktel and T-Com Crna Gora.

Subscriptions. Revenues from subscriptions increased both in 2005 and 2006, mainly as a result of the additional revenues due to the consolidation of T-Com Crna Gora. In 2005, this increase was partly offset by lower PSTN subscription fees at Maktel, reflecting the lower average number of customers and higher number of disconnected lines. In 2006, higher subscription revenues at Maktel resulted from increased tariffs as rates rebalancing occurred in August 2005, partly compensated by lower average number of customers.

Domestic outgoing traffic revenues. Domestic outgoing traffic revenues showed an increase both in 2005 and 2006 due to the consolidation of T-Com Crna Gora s revenues. The increase was partly offset by lower revenues at Maktel as a result of decreased usage, partly compensated by price increases in August 2005.

International outgoing traffic revenues. International outgoing traffic revenue increased in 2005 and 2006 due to the inclusion of T-Com Crna Gora s revenues, partly offset by lower revenues at Maktel, reflecting decreased volume of traffic and lower prices.

Value added, cable voice and other services. Value added, cable voice and other services revenues showed an increase both in 2005 and 2006. In 2006, the strong increase was due to higher premium rate revenues relating to TV quiz shows at T-Com Crna Gora.

Domestic incoming traffic revenues. Domestic incoming traffic revenue increased significantly both in 2005 and 2006 mainly due to the consolidation of T-Com Crna Gora s revenues. In 2005, this increase was partly compensated by decreased domestic incoming traffic revenue at Maktel as a result of lower traffic from T-Mobile Macedonia and lower interconnection fees. In 2006, lower domestic incoming revenue at Maktel was principally due to lower interconnection fees of international calls, partly compensated by increased traffic from Cosmofon in line with its increased subscriber base.

International incoming traffic revenues. International incoming traffic revenue increased in 2005 as compared to 2004 reflecting the consolidation of T-Com Crna Gora s revenues. This increase was mitigated by decreased incoming international revenues at Maktel as a result of lower average settlement rates and stronger MKD against the SDR. Higher international incoming traffic revenue in 2006 was primarily attributable to increased amount of international incoming minutes resulting from the restricted illegal VoIP traffic at Maktel. The revenue increase was also due to the inclusion of T-Com Crna Gora s full year revenues.

Internet. Revenues from Internet services increased in both 2005 and 2006 because of significantly higher number of ADSL subscribers as well as increased average number of Internet customers at Maktel. In 2006, the increase in Internet revenues was also helped by the strong increase in the number of ADSL subscribers at T-Com Crna Gora.

	Year ended December 31,			**Year ended December 31,**	
	2004	**2005**	**2006**	**2005/2004 (% change)**	**2006/2005**
ADSL connections					
Maktel	2,447	7,798	16,462	218.7	111.1
T-Com Crna Gora	n.a.	1,085	6,639	n.a.	511.9
Number of Internet subscribers					
Maktel	67,391	91,865	125,699	36.3	36.8
T-Com Crna Gora	n.a.	26,796	32,429	n.a.	21.0

Data. Data transmission revenues grew both in 2005 and in 2006 primarily resulting from the consolidation of T-Com Crna Gora s revenues.

Equipment sales. Revenues from telecommunications equipment sales decreased in 2005 due to fewer phonesets sold and the lower average price of phonesets at Maktel. In 2006, higher equipment sales revenues resulted from the higher amount of equipment sold at Maktel during marketing campaigns.

Other revenues. Other revenues increased in both 2005 and 2006 mainly as a result of the inclusion of T-Com Crna Gora s revenues.

Operating Expenses

Hungarian Fixed Line Operations

The following table sets forth information regarding operating expenses of Hungarian fixed line operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Operating expenses:					
Employee-related expenses	78,744	58,108	59,801	(26.2)	2.9
Depreciation and amortization	72,547	61,290	62,397	(15.5)	1.8
Payments to other network operators	50,375	38,185	32,276	(24.2)	(15.5)
Cost of telecomm. equipment	3,723	3,990	6,332	7.2	58.7
Other operating expenses net	75,377	78,143	99,259	3.7	27.0
Total	280,766	239,716	260,065	(14.6)	8.5

Employee-related expenses. Employee-related expenses consist of wages and salaries, social security and other expenses. Employee-related expenses decreased in 2005 as a result of significantly lower severance provisions and expenses at Magyar Telekom Plc. as well as a decrease in average headcount. This decrease was partly offset by a 5.6 percent average wage increase for employees of Magyar Telekom Plc. in April 2005.

In 2006, employee-related expenses increased mainly due to the inclusion of new subsidiaries (e.g., Dataplex, KFKI). Higher severance expenses of Magyar Telekom Plc. also contributed to the increase.

Depreciation and amortization. Depreciation and amortization decreased in 2005 as compared to 2004 due to the HUF 5,355 million impairment losses recorded on our tangible fixed assets and scrapping of certain fixed assets in the Hungarian fixed line operations. In 2006, the small increase in depreciation and amortization expenses was driven by the inclusion of newly acquired subsidiaries (e.g., Dataplex, KFKI) and higher depreciation of intangible assets due to the capitalization of service rights relating to the Electronic Governmental Backbone Network at Magyar Telekom Plc.

Payments to other network operators. Payments to other network operators include amounts paid to mobile operators, other local fixed line telephone operators and to foreign telephone operators for calls terminated on their network. In 2005 and 2006, payments to domestic network operators decreased because of lower traffic transited through Magyar Telekom Plc. and lower fixed-to-mobile termination rates. In 2005, interconnection traffic between Magyar Telekom Plc. and the LTOs increased significantly, but the traffic increase was offset by lower LRIC-based rates. In 2006, Magyar Telekom Plc. s outpayments to LTOs decreased driven by lower RIO fees based on NCA decision from June 2006 and applied retrospectively since September 2005, partly compensated by higher interconnection traffic. Payments to foreign network operators decreased in 2005 mainly due to lower international traffic. Payments to foreign network operators increased in 2006 primarily due to higher HUF/EUR exchange rates, partly offset by lower international settlement rates and decreased international traffic.

Cost of telecommunications equipment. Cost of telecommunications equipment increased both in 2005 and 2006. In 2005, the growth mainly resulted from the increased sales of phonesets as part of the Favorit campaigns at Magyar Telekom Plc. In 2006, the significantly higher cost of equipment resulted from various network construction and system integration tenders at Magyar Telekom Plc. Higher sales at BCN Rendszerház Kft. as well as the inclusion of KFKI also contributed to the increase.

Other operating expenses net. In 2005, other net operating expenses increased due to higher subcontractor s fees at Magyar Telekom Plc. as a result of increased commissions related to price plans

74

sold both in LTOs and Magyar Telekom Plc. s service areas. In 2005, other expenses included HUF 1,344 million paid under two consulting contracts entered into by Magyar Telekom Plc., as to which it had not been able to obtain sufficient evidence that it or its subsidiaries received adequate value. This amount also included the tax implications of the payments as well. See Item 15 Controls and Procedures .

In 2006, the significant growth in other net operating expenses was due to higher fees for outsourcing services (e.g., real estate management, transportation, customer service and informatics) as well as higher expenses in connection with various projects. The increase in materials and maintenance fees was driven by the consolidation of new subsidiaries such as Dataplex and KFKI. Non-rebranding related marketing expenses increased significantly as well at Magyar Telekom Plc., due to more intensive advertising activity in 2006. Other operating expenses net included a HUF 4.1 billion one-off item, which included the expenses Magyar Telekom incurred relating to the ongoing investigation.

International Fixed Line Operations

The following table sets forth information regarding operating expenses of international fixed line operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Operating expenses:					
Employee-related expenses	10,502	11,657	13,239	11.0	13.6
Depreciation and amortization	9,114	10,604	12,677	16.3	19.5
Payments to other network operators	10,628	13,932	17,943	31.1	28.8
Cost of telecomm. equipment	344	377	621	9.6	64.7
Other operating expenses net	8,081	12,452	12,981	54.1	4.2
Total	38,669	49,022	57,461	26.8	17.2

In 2005, total operating expenses from international fixed line operations decreased by 6.9 percent without the consolidation of T-Com Crna Gora. In 2006, the weaker HUF against MKD and EUR had significant effect on the expenses of Maktel and T-Com Crna Gora.

Employee-related expenses. Employee-related expenses increased both in 2005 and in 2006, mainly as a result of the consolidation of T-Com Crna Gora s expenses. The increase was partly offset by decreased severance provisions and expenses at Maktel relating to the headcount rationalization. In 2006, higher employee-related expenses at T-Com Crna Gora resulted primarily from the severance provision recognized in connection with the headcount reduction program.

Depreciation and amortization. Depreciation and amortization expense increased both in 2005 and 2006 reflecting the consolidation of T-Com Crna Gora s expenses. In 2005, this increase was partly compensated by lower expenses at Maktel because of the cessation of goodwill amortization from January 1, 2005. In 2006, the impairment of TCG and Internet CG brandnames in connection with the rebranding in Montenegro in September 2006 also contributed to higher expenses, partly offset by the decrease at Maktel in line with lower gross additions to tangible and intangible assets and higher number of fully amortized assets.

Payments to other network operators. Payments to other network operators increased in 2005 as compared to 2004 due to the inclusion of T-Com Crna Gora s expenses. This increase was partly offset by decreased payments at Maktel to T-Mobile Macedonia due to lower volume of traffic, which was partly compensated by increased outpayments to the second mobile telecommunications service provider, Cosmofon, as a result of its increased mobile subscriber base. Lower international outpayments at Maktel were due to decreased traffic and the stronger MKD against the SDR.

Payments to other network operators increased in 2006 as compared to 2005 primarily due to the inclusion of Orbitel s expenses and higher outpayments by Combridge. The longer consolidation period of T-Com Crna Gora (12 months in 2006 as opposed to nine months in 2005) also increased the outpayments. The increase was also attributable to Maktel s increased mobile outpayments to Cosmofon, partly offset by lower international outpayments due to decreased outgoing minutes, lower international average settlement rates as well as the lower MKD/SDR exchange rate.

Cost of telecommunications equipment. Cost of telecommunications equipment increased both in 2005 and 2006. In 2005, the growth mainly resulted from the consolidation of T-Com Crna Gora, while in 2006, the significantly higher cost of equipment was due to the inclusion of Orbitel.

Other operating expenses net. Other operating expenses showed a considerable increase in 2005 due to the consolidation of T-Com Crna Gora s expenses. In 2005, other expenses include HUF 144 million paid under a consulting contract entered into by T-Com Crna Gora, as to which the Company has not been able to obtain sufficient evidence that it or its subsidiaries received adequate value. This amount also includes the tax implications of the payments as well. See Item 15 Controls and Procedures .

In 2006, higher other net operating expenses resulted from increased expenses at Combridge and Novatel as well as the inclusion of Orbitel.

Operating Profit

Hungarian Fixed Line Operations

The following table sets forth information concerning operating profit and operating margin for the Hungarian fixed line operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
Operating profit (in HUF millions)	17,941	45,269	32,128	152.3	(29.0)
Operating margin (%)(1)	6.0	15.9	11.0	n.a.	n.a.

(1) Operating margin is the ratio of operating profit to revenue, expressed as a percentage.

In 2005, operating profit significantly increased by 152.3 percent mainly as a result of decreased severance provisions and expenses, lower payments to other network operators, lower amount of depreciation and amortization and higher Internet revenues. These favorable movements were partly offset by lower traffic revenues and increased other net operating expenses. In 2006, operating profit declined by 29.0 percent, mainly as a result of significantly higher other net operating expenses, higher cost of equipment and decrease in traffic revenues. These negative effects on operating profit were partly compensated by the strong increase in SI and IT revenues as well as higher Internet revenues.

International Fixed Line Operations

The following table sets forth information concerning operating profit and operating margin for the International fixed line operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
Operating profit (in HUF millions)	7,024	8,961	11,492	27.6	28.2
Operating margin (%)(1)	15.4	15.5	16.7	n.a.	n.a.

(1) Operating margin is the ratio of operating profit to revenue, expressed as a percentage.

Operating profit increased by 27.6 percent in 2005 as the increase in total revenues was higher than the increase in total operating expenses. Total revenues mainly increased due to higher domestic incoming revenues and higher Internet and data revenues. Operating profit increased by 28.2 percent in 2006 due to higher increase in revenues compared to the increase in total operating expenses. Total revenues mainly increased due to higher international incoming traffic revenues and higher internet and data revenues.

Mobile Telecommunications Segment

Mobile telecommunications segment includes TMH, Pro-M, T-Mobile Macedonia and T-Mobile Crna Gora.

Revenues

Revenues from the mobile telecommunications segment consist of one-time connection fees, monthly subscription fees (only payable by postpaid customers), traffic charges, including fees for enhanced services, and equipment sales.

Hungarian Mobile Operations

The results of the Hungarian mobile operations include TMH and Pro-M.

The following table sets forth information regarding revenues from Hungarian mobile operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Network usage and access	208,361	211,360	216,658	1.4	2.5
Enhanced services	26,779	31,876	35,110	19.0	10.1
Equipment sales	22,965	21,021	22,286	(8.5)	6.0
Activation fees	676	697	741	3.1	6.3
Other revenues	1,787	1,263	22,414	(29.3)	1,674.7
Total	260,568	266,217	297,209	2.2	11.6

The following table provides information concerning subscribers of mobile telecommunications services and monthly usage of the network at TMH:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
				(% change)	
Average number of subscribers					
TMH	3,906,319	4,077,521	4,270,324	4.4	4.7
Average monthly usage per					
TMH subscriber (minutes).	115	127	142	10.4	11.8
ARPU in HUF					
TMH subscriber	4,892	4,832	4,800	(1.2)	(0.7)
Postpaid TMH subscriber	11,712	10,838	9,849	(7.5)	(9.1)
Prepaid TMH subscriber	2,352	2,239	2,300	(4.8)	2.7
Enhanced services within ARPU in HUF	559	621	667	11.1	7.4
Average subscriber acquisition cost (SAC) per customer in HUF	10,275	7,062	6,234	(31.3)	(11.7)

Network usage and access. Revenues from network usage and access increased both in 2005 and 2006 principally as a result of the growth in the average monthly usage per subscriber, and, to a lesser extent, due to the higher number of subscribers. The average number of TMH subscribers grew by 4.4 percent in 2005 and 4.7 percent in 2006. TMH continuously monitors its churn rates and proactively offers tailor-made discounts to retain valuable customers. While the penetration growth of mobile customers has slowed down in Hungary, TMH maintained its leading position with a 44.5 percent market share at December 31, 2006.

Prepaid customers represented 65.1 percent of total TMH customers at December 31, 2006 as compared to 68.4 percent at the end of 2005. The proportion of prepaid customers decreased as many of them migrated to more favorable, for example flat rate, postpaid price plans.

TMH s average usage per customer per month measured in MOU increased by 11.8 percent from 127 minutes in 2005 to 142 minutes in 2006. The ARPU slightly decreased from HUF 4,832 in 2005 to HUF 4,800 in 2006 as the proportion of calls within the TMH network with lower per minute fees increased.

The increase in revenue was partly offset by the decrease in fixed-to-mobile termination fees. Pursuant to the relevant provisions of Decree 9/2003 and Decree 10/2003, issued by the Ministry of Informatics and Communications at the end of June 2003 and also in accordance with the decision of the Telecommunications Arbitration Council published on July 8, 2003 with regards to the regulation of interconnect charges applicable by TMH for fixed-to-mobile calls terminating on its network, the relevant interconnect charges were required to be reduced by 10 percent from September 1, 2003. In May 2004, the NCA ordered TMH to further reduce its interconnection fees by an average of 8.8 percent from June 15, 2004. In August 2005, a further NCA decree was released, which resulted in additional decrease in fixed-to-mobile termination rates with a retroactive effect from May 25, 2005.

Enhanced services. Within the mobile telecommunications services, enhanced services show 19 percent growth in 2005 and 10.1 percent growth in 2006 at TMH. Enhanced services represented approximately 12 percent of TMH s total revenues in 2006. This revenue is primarily from fees charged for short message services and multimedia messaging services. The strong revenue growth in 2005 is due to the increasing proportion of content messages with higher rates, and also due to higher access (data, Internet, GPRS, etc.) revenues. In 2006, higher enhanced services revenue resulted partly from the increased number of SMS and MMS and partly from higher access revenues.

Equipment sales. Equipment sales decreased in 2005 in the Hungarian mobile operations due to lower average price of phonesets, which was partly compensated by higher gross additions to customers as well as a higher number of phoneset upgrades. In 2006, the increase in equipment sales revenue reflects higher average handset prices and higher gross additions.

Average acquisition cost per customer fell by 11.7 percent to HUF 6,234 in 2006 from HUF 7,062 a year earlier at TMH. When calculating subscriber acquisition cost, TMH includes the connection margin (activation fee less the SIM card cost), the sales related equipment subsidy and agent fee.

Other revenues. In 2006, the significant increase in other revenues reflects Pro-M s operations. Pro-M s EDR activities contributed HUF 18.0 billion to total Hungarian mobile revenues and a similar amount to cost of equipment sales.

International Mobile Operations

The results of the international mobile operations include T-Mobile Macedonia and T-Mobile Crna Gora.

The following table sets forth information regarding international mobile revenues:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Network usage and access	27,421	35,548	43,871	29.6	23.4
Enhanced services	3,309	4,736	5,882	43.1	24.2
Equipment sales	2,062	1,843	2,131	(10.6)	15.6
Activation fees	200	149	63	(25.5)	(57.7)
Other revenues	742	417	452	(43.8)	8.4
Total	33,734	42,693	52,399	26.6	22.7

The following table provides information concerning subscribers of mobile telecommunications services and monthly usage of the network at T-Mobile Macedonia:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
				(% change)	
Average number of subscribers	629,844	809,691	901,485	28.6	11.3
Average monthly usage per T-Mobile Macedonia subscriber (minutes).	66	63	72	(4.5)	14.3
ARPU in HUF	3,804	3,065	3,206	(19.4)	4.6

In 2005, total revenues from international mobile operations increased by 1.6 percent without the consolidation of T-Mobile Crna Gora, partly offset by a 1.0 percent decrease due to the HUF/MKD foreign exchange movements. In 2006, the depreciation of HUF against MKD and EUR strongly contributed to the revenue increase both in the Macedonian and Montenegrin mobile operations.

Network usage and access. Revenues of the international mobile operations increased both in 2005 and 2006. In 2005, the increase was mainly as a result of the inclusion of T-Mobile Crna Gora s revenue. In 2006, the strong increase at T-Mobile Macedonia was owing to the higher average number of subscribers and higher MOU, partly offset by lower per minute rates.

Within T-Mobile Macedonia s subscriber base, prepaid subscribers represented 81.2 percent of total mobile customers at the end of 2006. T-Mobile Macedonia s MOU increased by 14.3 percent from 63 minutes in 2005 to 72 minutes in 2006. The ARPU also increased from HUF 3,065 in 2005 to HUF 3,206 in 2006 as a result of the weakening of HUF against MKD.

T-Mobile Crna Gora had 331,616 subscribers and a 41.2 percent market share in the Montenegrin mobile market at the end of December 2006.

Enhanced services. Enhanced services increased over the period mainly due to the consolidation of T-Mobile Crna Gora and in 2006, also as a result of increased number of SMSs at T-Mobile Macedonia.

Equipment sales. Equipment sales revenue decreased in 2005 due to the lower average price of mobile handsets, partly offset by higher gross additions in the Macedonian mobile operations. In 2006, higher equipment sales revenue was owing to the longer consolidation period and increased sales during campaigns at T-Mobile Crna Gora.

Operating Expenses

Hungarian Mobile Operations

The following table sets forth information regarding operating expenses for the Hungarian mobile operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Operating expenses:					
Employee-related expenses	18,708	20,540	19,185	9.8	(6.6)
Depreciation and amortization	47,571	33,897	36,359	(28.7)	7.3
Payments to other network operators	56,564	59,799	64,734	5.7	8.3
Cost of telecomm. equipment	34,172	29,548	48,822	(13.5)	65.2
Other operating expenses net	43,846	47,214	52,432	7.7	11.1
Total	200,861	190,998	221,532	(4.9)	16.0

Employee-related expenses. Employee-related expenses increased in 2005 principally as a result of increased wages and welfare expenses. In 2006, lower employee-related expenses were primarily attributable to higher personnel expenses capitalized.

Depreciation and amortization. Depreciation and amortization expenses decreased in 2005 as in accordance with the IFRS 3 standard, goodwill relating to acquisitions after March 31, 2004 was not amortized and the amortization of the existing goodwill was discontinued from January 1, 2005 which caused a HUF 9,540 million decrease in 2005. The decrease was also due to the impairment on the Westel brand name booked in 2004.

Depreciation and amortization expenses increased in 2006 at TMH mainly due to the capitalized UMTS concession and also due to their higher gross asset base of telecommunications and IT equipments.

Payments to other network operators. Payments to other network operators include amounts paid by TMH to other mobile telephone operators and to the fixed line telephone operators as well as to the foreign mobile telephone operators for terminating their calls. Payments to other network operators increased in both 2005 and 2006 as a result of the higher mobile penetration and increased traffic. The increase in 2005 was partly offset by lower international roaming outpayments as a result of favorable agreements concluded with other mobile operators, mainly with other T-Mobile companies.

Cost of telecommunications equipment. Cost of telecommunications equipment decreased in 2005 as a result of lower average cost of phonesets at TMH, reflecting the development of a central procurement process within the DT Group. The significant growth in the cost of equipment in 2006 was due to the EDR activities of Pro-M. Higher cost at TMH was driven by higher gross additions and higher average cost of phonesets, partly compensated by lower equipment sales ratio.

Other operating expenses net. Other net operating expenses increased both in 2005 and 2006. In 2005, the increase mainly resulted from higher agency fees due to higher commissions paid for new subscribers in line with higher gross additions to subscribers. In 2006, higher other net operating expenses were mainly driven by increased concession fees due to the UMTS fee paid by TMH.

International Mobile Operations

The following table sets forth information regarding operating expenses for the international mobile operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Operating expenses:					
Employee-related expenses.	1,657	2,582	3,138	55.8	21.5
Depreciation and amortization	8,434	8,894	10,816	5.5	21.6
Payments to other network operators	3,403	5,029	7,852	47.8	56.1
Cost of telecomm. equipment	3,227	3,522	3,985	9.1	13.1
Other operating expenses net	7,966	10,361	9,513	30.1	(8.2)
Total	24,687	30,388	35,304	23.1	16.2

In 2005, total operating expenses from international mobile operations decreased by 6.5 percent without the consolidation of T-Mobile Crna Gora, including 1.0 percent decrease due to foreign exchange movements. In 2006, the weaker HUF against MKD and EUR had significant effect on the increase in the expenses of T-Mobile Macedonia and T-Mobile Crna Gora.

Employee-related expenses. Employee-related expenses increased both in 2005 and 2006 reflecting the impact of the inclusion of T-Mobile Crna Gora s expenses.

Depreciation and amortization. Depreciation and amortization expenses increased significantly both in 2005 and 2006 mainly as a result of the consolidation effect of T-Mobile Crna Gora s expenses. In 2005, this growth was largely compensated by lower depreciation and amortization expenses at T-Mobile Macedonia due to the cessation of goodwill amortization from January 1, 2005. Higher expenses in 2006 also resulted from the impairment of the Monet brandname in connection with the rebranding in Montenegro in September 2006.

Payments to other network operators. Payments to other network operators increased considerably both in 2005 and 2006. Higher outpayments over the period primarily resulted from the consolidation of T-Mobile Crna Gora s expenses. The increase was also due to T-Mobile Macedonia s higher outpayments to Cosmofon in line with its larger subscriber base.

Cost of telecommunications equipment. In 2005 and in 2006, cost of telecommunications equipment increased as a result of the inclusion of T-Mobile Crna Gora s expenses. In 2005, this increase was partly offset by lower average cost of phonesets at T-Mobile Macedonia, while in 2006, the growth was partly compensated by the lower equipment sales ratio at T-Mobile Macedonia despite higher gross additions and higher average cost of phonesets.

Other operating expense net. Other net operating expenses increased in 2005 principally due to the consolidation of T-Mobile Crna Gora s expenses. In 2005, other expenses include HUF 571 million paid under a consulting contract entered into by T-Mobile Crna Gora, as to which the Company has not been able to obtain sufficient evidence that it or its subsidiaries received adequate value. This amount also includes the tax implications of the payments as well. See Item 15 Controls and Procedures .

Other net operating expenses showed a decrease in 2006 as compared to 2005 resulting from the general cost cutting at T-Mobile Macedonia.

Operating Profit

Hungarian Mobile Operations

The following table sets forth information concerning operating profit and operating margin for the Hungarian mobile operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
Operating profit (in HUF millions)	59,707	75,219	75,677	26.0	0.6
Operating margin (%)(1)	22.9	28.3	25.5	n.a.	n.a

(1) Operating margin is the ratio of operating profit to revenue, expressed as a percentage.

Operating profit increased by 26.0 percent in 2005 mainly due to the significant decrease in depreciation charges resulting from the discontinuation of the goodwill amortization (HUF 9,540 million) and the impairment on the Westel brand name (HUF 4,426 million) in 2004. Cost of equipment also decreased in 2005 due to the central procurement process within Deutsche Telekom Group. In addition, revenues from Hungarian mobile operations increased by HUF 5,649 million in 2005. Operating profit remained broadly stable in 2006 as compared to 2005 as total revenues increased by HUF 30,992 million, while operating expenses increased by HUF 30,534 million year over year. Operating expenses increased due to the combined effect of significantly higher cost of equipment (primarily due to Pro-M s EDR services), increased payments to other mobile operators, higher depreciation (resulting from higher gross asset base of telecommunications and informatics equipment as well as capitalized UMTS concession), increased other operating expenses net and lower employee-related expenses.

International Mobile Operations

The following table sets forth information concerning operating profit and operating margin for the international mobile operations:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004 (% change)	2006/2005
Operating profit (in HUF millions)	9,047	12,305	17,095	36.0	38.9
Operating margin (%)(1)	26.8	28.8	32.6	n.a.	n.a.

(1) Operating margin is the ratio of operating profit to revenue, expressed as a percentage.

Operating profit increased by 36 percent in 2005 and by 38.9 percent in 2006 because total revenues increased at a higher rate than total operating expenses. The main driver in the increase of total revenues was the higher network usage and enhanced revenues. The consolidation of T-Mobile Crna Gora also contributed to the increase in operating profit over the period.

Finance Expenses

The following table sets forth information concerning finance expenses:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Interest expense	34,731	31,340	27,325	(9.8)	(12.8)
Other finance expenses	3,183	3,157	2,831	(0.8)	(10.3)
Less: Interest capitalized			(54)	n.a.	n.a.
	37,914	34,497	30,102	(9.0)	(12.7)

Finance expenses decreased both in 2005 and 2006 primarily as a result of the decrease in HUF interest expenses due to lower average HUF interest rates. In 2006, Magyar Telekom did not have to take loans for dividends, as no dividends were paid due to the delayed acceptance of the 2005 financial statements. The proportion of loan portfolio with variable interest rates was higher than in 2005.

Finance Income

The following table sets forth information concerning finance income:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Gain on sale of financial instruments			1,190	n.a.	n.a.
Gain on sale of subsidiary	191		121	n.a.	n.a.
Gains / (losses) on the valuation of derivative financial instruments)	647		377	n.a.	n.a.
Net foreign exchange gains /(losses)	(523)	1,014	(659)	n.m.	n.m.
Finance lease interest income			480	n.a.	n.a.
Interest and other financial income	1,453	1,982	3,183	36.4	60.6
	1,768	2,996	4,692	69.5	56.6

Finance income showed a significant increase both in 2005 and 2006. In 2005, higher income was driven by the higher foreign exchange gain at Maktel as a result of the weakening of the MKD against the USD, in which the majority of its foreign currency cash and receivables are denominated. Interest income increased at Maktel as it held higher amounts of cash and deposits in banks at longer maturities.

In 2006, increase in finance income was attributable primarily to Crnogorski Telekom as a result of the sale of CKB s shares in December 2006. The increase in Magyar Telekom Plc. s foreign exchange gains was due to the strengthening of the HUF in 2006. These increases were somewhat offset by higher foreign exchange losses at Maktel resulting from the unfavorable movements of the MKD against the USD.

See Notes 3, 16 and 17 to the consolidated financial statements for certain quantitative and qualitative information about financial instruments.

Income Tax Total

The following table sets forth information concerning our income tax expense:

	Year ended December 31,			Year ended December 31,	
	2004	2005	2006	2005/2004	2006/2005
	(in HUF millions)			(% change)	
Income tax expense(1)	16,142	21,858	24,220	35.4	10.8

(1) Due to a change in IFRS rules, we report income tax without the taxation charge on the share of associate s results from 2005 (the 2004 comparative figure was revised accordingly).

Deferred taxes have been recognized for temporary differences arising on the valuation of investments (mainly currency differences) in subsidiaries and associates in the parent companies books as required by IAS 12. For more details on the tax credits, see Note 9 to the consolidated financial statements.

Income tax expense increased in 2005 as a result of the significantly higher profit before tax at almost all members of the Group. The lower effective tax rate in 2005 (19.8 percent compared to 27.1 percent in 2004) was mostly due to the compounding of the tax credit carried forward related to the Hungarian broadband investments, which resulted in tax credits with no impact on profit before tax. In addition, the

higher amount of other income related to the rebranding, which is not taxable, also contributed to the lower effective tax rate.

Income tax expense increased in 2006 as compared to 2005, mainly because of the deferred tax recognized in relation to withholding tax on future dividends based on the undistributed reserves of Maktel and Crnogorski Telekom. In addition, the higher profit before tax at our Macedonian and Montenegrin subsidiaries also increased income tax expenses. These increases were partly offset by lower income tax at Magyar Telekom Plc. in line with its lower pre-tax profit.

CRITICAL ACCOUNTING POLICIES

The discussion and analysis of our financial condition and results of operations are based on our consolidated financial statements, which have been prepared in accordance with IFRS. Reported financial conditions and results of our operations are sensitive to accounting methods, assumptions and estimates that underlie the preparation of the financial statements. We base our estimates on historical experience and on various other assumptions, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources.

The selection of critical accounting policies, the judgments and other uncertainties affecting application of those policies and the sensitivity of reported results to changes in conditions and assumptions are factors to be considered when reviewing our financial statements.

For a list of our critical accounting policies and assumptions, see Note 4 to the consolidated financial statements. For a discussion about the differences between our IFRS and U.S. GAAP accounting policies, see Note 37 to the consolidated financial statements.

LIQUIDITY AND CAPITAL RESOURCES

Cash flow analysis

The following table sets forth information concerning our cashflows:

	Year ended December 31,		
	2004	2005	2006
	(in HUF millions)		
Net cashflows:			
From operating activities	189,751	201,336	187,624
From investing activities	(100,787)	(131,566)	(122,259)
From financing activities	(72,095)	(61,848)	(35,154)
Effect of foreign exchange rate changes on cash and cash equivalents	(2,122)	1,259	1,569
Change in cash and cash equivalents	14,747	9,181	31,780
Cash and cash equivalents, beginning of year	22,132	36,879	46,060
Cash and cash equivalents, end of year	36,879	46,060	77,840

Net Cashflows from Operating Activities. Our primary source of liquidity is cashflows from operating activities.

Net cashflows from operating activities increased by HUF 11,585 million in 2005 as compared to 2004. Income tax paid decreased by HUF 10,513 million, the amount of interest paid decreased by HUF 2,952 million and cash generated from operations decreased by HUF 1,880 million.

Net cashflows from operating activities decreased by HUF 13,712 million in 2006 as compared to 2005. The HUF 7,909 million increase in income tax paid and the HUF 7,005 million decrease in cash generated from operations was partly offset by HUF 1,202 million decrease in interest paid.

Net Cashflows from Investing Activities. Net cashflows from investing activities are primarily driven by capital expenditures and acquisitions of businesses. In 2005, cash spent on purchase of subsidiaries increased significantly as compared to 2004 due to the acquisition of a 76.53 percent stake in Crnogorski Telekom. In 2006, the HUF 9,307 million decrease in cash outflow is predominantly due to the combined effect of the lower cash outflow for capital expenditures, the higher amounts of proceeds from disposal of real estate and from the sale of financial assets, partly offset by lower amount of dividends received. Purchase of tangible and intangible assets were HUF 91,748 million in 2004, HUF 103,587 million in 2005 and HUF 96,790 million in 2006.

Net Cashflows from Financing Activities. Net cashflows from financing activities primarily relate to our borrowing activities and dividend payment.

In 2005, we received net proceeds from loans in an amount of HUF 20,734 million. The increase in borrowings is mainly due to financing the acquisition of Crnogorski Telekom. In 2005, we paid dividends to shareholders in an amount of HUF 84,551 million. The increase in dividends paid as compared to 2004 is primarily due to the higher amount of dividends paid to minority shareholders of Maktel in 2005. In 2006, we had a net repayment of loans of HUF 35,568 million as Magyar Telekom Plc. and Maktel did not pay dividends in 2006. Maktel used part of its cash-flow to buy back shares from the minority shareholders in 2006.

We carry indebtedness at a level we consider appropriate based on a number of factors, including cash flow expectations (i.e., cash requirements for ongoing operation, investment plans), expectations of investors, analysts, rating agencies and the overall cost of capital. We announced a definite dividend policy in 2003, according to which the net debt ratio is to be kept between 30 to 40 percent. Under the new dividend policy, based on the results of 2004, we paid an amount of HUF 70 dividend per share in 2005 and based on the results of 2005, we paid HUF 73 dividend per share in 2007, by which we maintained the net debt ratio in the target range. Our net debt ratio was 27.9 percent at December 31, 2006. Future dividend payment will be determined by the new dividend policy and will depend on our cashflow generation and potential acquisition opportunities.

For a discussion of our financial instruments, loans and other borrowings, see Notes 3, 16 and 17 to our consolidated financial statements.

By the end of May 2007, long term indebtedness increased by HUF 115 billion at Magyar Telekom Plc. from December 31, 2006, mainly due to long term loans taken to finance the dividend payments for 2005 and 2006 and to refinance some expiring short term loans.

In our Hungarian fixed line and mobile operations, our operating revenues and expenses are denominated almost entirely in Hungarian forints. Amounts payable to and receivable from other international carriers, which are denominated in a basket of currencies known as SDRs, are netted against one another and settled primarily in U.S. dollars and euros. Capital expenditures are denominated partly in foreign currencies, principally U.S. dollars and euros.

In 2005, the HUF interest rates started to decline gradually from a very high basis, but from the second half of 2006 they increased again to approximately eight percent. At December 31, 2006, the loans were almost 100 percent denominated in HUF, thus the foreign exchange risk of the loan portfolio is naturally hedged by the HUF-denominated revenues.

At December 31, 2006, 61.1 percent of the loan portfolio bore fixed interest rates - these are mainly the medium and long-term elements of the portfolio - while 38.9 percent of the loan portfolio was subject to variable interest rates. Short-term loans are partially taken to manage liquidity peaks and their variable rates are based on Budapest Interbank Offered Rate (BUBOR). Taking into consideration HUF interest rate volatility, we follow the approach of balancing the fixed and variable interest rate elements in our loan portfolio.

We do not have any legal or economic restrictions on the ability of our subsidiaries to transfer funds to the Company in forms of cash dividends, loans or advances.

Our liquidity needs are primarily covered by our free cash flows. Liquidity peaks are financed from current account overdrafts and bilateral shelf facilities. The total available current account overdrafts at the end of 2006 amounted HUF 10,549 million. The total committed shelf facilities from the Hungarian market amount to HUF 82,349 million, out of which HUF 68,700 million was available at the end of 2006. We also have a EUR 50 million shelf facility with Deutsche Telekom, which functions as a safety net for potential liquidity peaks and has not been drawn since its signing on April 16, 2004.

We have uncommitted lines at Hungarian banks in the amount of around HUF 15 billion, which can be drawn for a maximum period of 90 days. Since these are non-committed lines, we do not rely on them when managing liquidity, however they are used when the liquidity need is only short-term. At the end of 2006, HUF 2 billion was drawn from these facilities.

	Amount of the facility (in HUF millions)	**Drawn at the end of 2006**	**Available at the end of 2006**
Current account overdrafts	14,608	4,059	10,549
Bilateral loans	82,349	13,649	68,700
DT shelf facility	12,615		12,615
Total credit lines	109,572	17,708	91,864
Total uncommitted lines	15,150	2,000	13,150
Total lines for liquidity purposes	124,722	19,708	105,014

The current amount and structure of the shelf facilities described above is sufficient, and for the purposes of liquidity management, we believe that there is no need to establish new facilities.

	Maturity structure		
	2007	**2008**	**2009**
	(in HUF millions)		
Current account overdrafts	14,608		
Bilateral loans	59,349	2,000	21,000
DT shelf facility	12,615		
Total credit lines	86,572	2,000	21,000

Deutsche Telekom is ready to finance our major financing needs (such as refinancing or financing acquisitions) through the international capital markets and it passes the conditions of the loans on an arms length basis to Magyar Telekom. Should this financing source cease to become available in the future, we plan to raise funds from the Hungarian syndicated loan market and from the Hungarian capital markets. Our financial position is quite strong in the Hungarian markets therefore we expect to be able to obtain financing at favourable terms from these markets. In addition, we have access to the international bank and capital markets.

Our ordinary shares are listed on the Budapest Stock Exchange (BSE) and the American Depositary Shares, each representing five of our ordinary shares, are listed on the New York Stock Exchange (NYSE). We had 2,456,659 treasury shares at December 31, 2006. These shares are maintained to hedge and finance exercises of share options under the management share option plan launched in 2002. No issuance is likely in the foreseeable future.

For additional information about market risk sensitive instruments, see Notes 3, 16 and 17 to the consolidated financial statements.

Credit rating

In 2000, we requested both Moody s Investors Services (Moody s) and Standard & Poor s Ratings Services (S&P) to initiate rating coverage.

In 2004, Moody s upgraded DT s credit rating, therefore at the end of 2004, our ratings became same as that of DT: Baa1 (Moody s) and BBB+ (S&P).

In March 2005, S&P upgraded our rating from BBB+ to A- with a stable outlook following a similar upgrade of DT and in June 2005, Moody s upgraded DT s credit rating by one notch to A3, while confirming our Baa1 credit rating.

On September 11, 2006 S&P revised our outlook from stable to negative, while affirming the A- rating. The move followed the outlook revision of DT. On August 31, 2006 Moody s placed the Baa1 issuer rating in both local and foreign currencies of Magyar Telekom on review for possible downgrade, prompted by prolonged delay of the publication of our 2005 audited financial statements. After the publication of these figures, Moody s confirmed the Baa1 issuer rating on January 31, 2007.

Off-balance sheet arrangements

We do not have any off-balance sheet arrangements (including contingent liabilities, guarantees, etc.) that have or are reasonably likely to have a material current or future effect on our financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources. We do not participate in, nor secure, financings for any unconsolidated, limited purpose entities.

Tabular disclosure of contractual obligations

Our contractual obligations, including commitments for future payments under non-cancelable lease arrangements and short- and long-term debt arrangements, are summarized below and are disclosed in more details in Notes 16, 17 and 33 to our consolidated financial statements. Amounts disclosed as purchase obligations represent long-term commitments under outsourcing contracts, commitments towards international telecommunications carriers and other purchase commitments. Commitments under outsourced activities include a long-term contract for IT services, where payment obligations depend on a number of factors, such as the number of PCs, exchange rates and annual inflation rates, therefore the related amounts included in the table below are estimates.

This table excludes other obligations we may have, such as payroll and related human resource services (including bonuses and payments under our mid-term incentive plan). Payments under these contracts are based on the level of service required and are excluded from this table due to the uncertainty of the amounts to be paid, if any, as well as the timing of such amounts.

	Payments Due by Period				
	Total (in HUF millions)	Less than 1 year	1-3 years	3-5 years	More than 5 years
Loans and borrowings including finance lease commitments	309,734	103,605	122,873	23,575	59,681
Interest on loans and borrowings	62,774	22,789	26,473	11,564	1,948
Operating leases.	43,349	6,869	10,943	7,870	17,667
Contractual commitments for capital expenditures	6,022	3,878	2,144		
Purchase obligations	70,172	22,580	31,522	13,278	2,792
Trade and other payables	200,589	200,589			
Total contractual cash obligations	692,640	360,310	193,955	56,287	82,088

In addition to the above, in October 2005, we won the government tender and signed a contract with the Prime Minister s Office to build and operate the nationwide EDR system in Hungary. The rollout of EDR has begun in 2006 and the contract lasts until the end of 2015. Magyar Telekom invested HUF 18.0 billion in 2006 in the assets required to build out the EDR service and expect to invest HUF 2.9 billion in 2007.

On November 29, 2005, we entered into an agreement to acquire a 100 percent stake in Orbitel for a consideration consisting of EUR 7.35 million at the closing of the transaction, an additional EUR 500 thousand to be paid in 2008 depending on whether the two top managers stay at the company until the end of 2007, an additional EUR one million to be paid in 2008 if certain financial targets are met between 2005 and 2007. The closing of the transaction took place in February 2006.

In December 2006, Magyar Telekom agreed to acquire a 100 percent stake in MobilPress. The transaction was closed on January 25, 2007. See Note 5.1.6 to the consolidated financial statements for more details.

As agreed in December 2006, the Company signed a sale-purchase agreement to acquire an additional two percent ownership in TSH effective from January 1, 2007 for a purchase price of HUF 60 million. TSH has been an associate of the Group since September 2004.

According to the Share Purchase Agreement signed on June 16, 2006, the previous owners of KFKI were entitled to an earn-out payment of HUF 1.5 billion depending on the 2006 financial performance. As reported in the company s full year 2006 consolidated financial statements, KFKI delivered HUF 19.8 billion revenues and HUF 2.0 billion EBITDA, reaching the predefined thresholds. As a result, on May 14, 2007, Magyar Telekom has paid the HUF 1.5 billion earn-out payment to the previous owners of KFKI.

On March 28, 2007, the Agency of Telecommunications and Postal Services of the Republic of Montenegro awarded a 3G license to T-Mobile Crna Gora. In April 2007, T-Mobile Crna Gora paid EUR 2.4 million for the license.

In addition to the above, Magyar Telekom assumes the legal expenses of its current and former employees involved in the internal investigation (see Item 3 Risk Factors and Item 15 Controls and Procedures); in connection with this we incurred HUF 458 million expenses in 2006. We are not able to estimate the expenses we will incur in 2007 and future years for legal counsel advising these individuals.

CAPITAL EXPENDITURES

Our capital expenditures on tangible and intangible assets totaled HUF 91,748 million in 2004, HUF 103,587 million in 2005 and HUF 96,790 million in 2006, including in each year changes in the balance of capital expenditure trade creditors and the recognition of investment tax credit. Capital expenditures include expenditures for (1) the fixed line network, including network operations systems, (2) mobile telecommunications and (3) new products, corporate infrastructure and other assets.

Purchases of tangible and intangible assets for the fixed line segment accounted for 40 percent in 2004, 53 percent in 2005 and 55 percent in 2006. Purchases of tangible and intangible assets for the mobile segment totaled 60 percent in 2004, 47 percent in 2005 and 45 percent in 2006.

We expect to be able to finance capital expenditures over the next several years from net cashflows from operations and from borrowings. Our actual future capital expenditures will depend on a variety of factors, such as development of our business and of the Hungarian economy and whether we enter into any new line of business. As a result, our actual future capital expenditures may be significantly different.

RECONCILIATION TO U.S. GAAP

The following table shows net income and shareholders equity under IFRS and U.S. GAAP for the periods indicated:

	Year ended December 31,		
	2004	**2005**	**2006**
	(in HUF millions)		
Profit attributable to the equity holders of the Company (Net income):			
IFRS	34,641	78,415	75,453
U.S. GAAP	39,684	69,260	71,481
Shareholders equity:			
IFRS as reported	516,567	527,567	526,039
U.S. GAAP	534,907	542,098	538,190

The U.S. GAAP reconciliation adjustments (See Note 37 to the consolidated financial statements) can be grouped in two major categories as below:

1. Adjustments arising from differences that existed in the past and still amortizing or remaining in equity

These include revenue recognition differences originating from SAB 101, before the adoption of EITF 00-21 related to connection and activation fees; recognition of intangible assets acquired through business combinations and the corresponding impact on goodwill and the earlier discontinuation of goodwill amortization in U.S. GAAP than in IFRS.

2. New adjustments arising

These include the significantly higher amount of interest capitalization and the consequent impacts on tangible asset depreciation; recognition and consequent amortization and accretion of asset retirement obligations; compensation received from the parent company for the re-branding of the Group s entities and products that is recognized as income in IFRS, while it is recognized as capital contribution in U.S. GAAP; and the recognition of derivatives embedded in contracts denominated in other currencies than the functional currency of the contracting Group company.

Related to the above adjustments, we also have income tax and minority adjustments where applicable.

The net impact of the recurring U.S. GAAP adjustments on the IFRS Net income is rather stable and insignificant. The apparent fluctuation is caused by the non-recurring adjustments including the re-branding compensation in 2004, 2005 and 2006, and the last year of goodwill amortization in IFRS in 2004.

Recent Accounting Pronouncements

We have reviewed the new standards, amendments and interpretations to existing standards that have been published that are mandatory for our accounting periods after January 1, 2007. For a list of recent IFRSs accounting pronouncements, see Note 2.1.3 to the consolidated financial statements. For a list of recent U.S. GAAP accounting pronouncements, see Note 37 to the consolidated financial statements.

RESEARCH AND DEVELOPMENT

Hungarian Fixed Line Operations

Magyar Telekom Plc. has a department dedicated to performance of research and development (R&D) projects to meet the demands of the rapidly changing market, such as development of our telecommunications networks and service platforms. The R&D department works in close cooperation with educational institutions (including the Budapest University of Technical and Economic Sciences and the Technical College of Budapest), strategic investors, suppliers and domestic and international development organizations. Following our accession to the European Union, several funds aimed encouraging research and development activities became available to us as well; this encouraged us to deepen our involvement in national and international consortiums engaged in R&D.

The harmonization projects among DT Group members (Maktel, Slovak Telekom, Croatian Telekom and T-Systems International) play an important role. The joint development themes enable us to utilize group-level synergies, pursue efficient financial and human resource management and use the same third party contractors for our R&D projects.

In the last few years, to maintain or expand the competitive positions of Magyar Telekom we developed the technical platform through the R&D activities for the introduction of new VoIP and multimedia-based services, based on the next generation (NGN) IP/Ethernet-based core and broadband fixed (ADSL, xDSL) and wireless (WLAN, WiFi) accesses.

Significant resources are devoted to the upgrading of our digital backbone network. The DWDM technology was introduced to satisfy the additional demands on the backbone network that arose in connection with broadband services, such as fast Internet access and broadband IP-VPN.

We are continuously developing our data communications and IP network and services to meet demands for broadband services. We developed the concept of a national, high-speed IP network built on DWDM and Gigabit Ethernet. Under this program, the components of our IPv6 protocol pilot network were identified.

In the last few years, we rolled out a wide range of broadband access technologies (e.g., ADSL, cable television, optical access network and managed leased line technologies) to satisfy demands for higher bandwidth. To widen the choice of broadband services, we considered the possibilities of implementing triple-play solutions. In 2006, multimedia services, including IPTV development, were tested in the Ethernet and DSLAM environment. Based upon this work, by the end of 2006, we introduced IPTV services. The possibility of introduction and application of IP High Definition TV (HDTV) and Three Dimension (3D) TV technologies are being investigated.

In 2006, we studied the usability of World Interoperability for Microwave Access (WiMAX) technology. WiMAX can provide wireless broadband access with effective radius of up to several kilometers with up to 70 Mbit/s radio throughput. WiMAX is in a standardization phase. We also plan to implement the new generation of xDSL technologies (VDSL2, Gigabit capable Passive Optic Network) in the access network to extend the broadband access coverage and provide higher bit rate.

The Global Resource Information Database (GRID) mass-computing platform prototype has been further developed providing quota management to enhance its security and to ensure resilience against data flooding attacks.

In the last two years, we laid down the basis for product developments toward the convergence of fixed and mobile networks (FMC) together with TMH. A Bluetooth and WiFi-based intelligent solution has been tested in our laboratory. Our next step in this field will be a study on the FMC possibilities in IP Multimedia Subsystem (IMS) environment, and WiFi/UMTS handsets. A study has been launched on the potential interconnection of the Next Generation fixed and mobile networks, based on the ETSI Telecoms and Internet converged Services and Protocols for Advanced Networks (TISPAN) IMS architecture.

When we aim to provide voice service over IP networks, Name Addressing and Routing (NAR) issues essentially differ from those that we experienced in the PSTN network. Electronic Telephone Number Mapping (ENUM) is one of the most promising technologies to provide information for IP based call routing including information for number portability, freephone and other number or address translation capabilities, SMS and MMS. This routing is available both internally and for interconnection of networks (peering). In 2006, we set up an experimental network and interconnected it with the ENUM trial system of Deutsche Telekom to examine the possibilities of the ENUM infrastructure. In 2007, we aim to build an ENUM network that will be used for dynamic call routing based on Bluetooth sensors.

We have developed a test system for hearing-impaired users, which transforms the speech signals into moving images, so users can recognize the speech by lip-reading.

Macedonian Fixed Line Operations

In the last three years, significant efforts have been made to upgrade the network to extend the range of services offered and improve their quality. This, together with the rationalization of network switching architecture, resulted in improvement in the operational efficiency and network consolidation. New telephone services were introduced through the IN and Voice-mail Platforms and provision of broadband services became available with the implementation of ADSL technology.

In the next phase, the main focus will be on extension of ADSL capacities nationwide and development of new services. To expand broadband offerings, Maktel will evaluate video services in terms of its technical feasibility, impact on access and transport network.

Maktel will continue to dedicate necessary resources for implementation of new technologies to develop the capacity to offer broadband services that will satisfy customers demands. For connection of business customers Metro Ethernet equipment will be used.

Maktel is making preparations for interconnection and convergence of separate voice and data networks. The NGN concept has been seen as a long-term project. Maktel does not plan significant development of traditional PSTN/ISDN network except for purposes of maintenance and compliance with the regulatory requirements. The key focus will be on provisioning of broadband access, upgrade of transport network and network migration towards NGN.

Hungarian Mobile Operations

TMH works in close cooperation on R&D projects with educational institutions such as the Budapest University of Technical and Economic Sciences, strategic investors and suppliers to meet the demand of the rapidly changing market.

TMH has worked successfully on various R&D projects with universities since 1997 in five different areas: Mobile Telecommunications Laboratory deployment, Inter-University Centre for Telecommunications and Informatics, Mobile Innovation Centre, research and development activities as well as joint mobile services development for TMH. Through these areas TMH continuously monitors the forthcoming new generation technologies, hardware-software solutions and mobile services. One of the largest challenges of the new mobile and wireless systems is the integration and interoperability of different technologies. TMH is committed to analyzing and adopting new solutions on a continual basis. University departments actively participate in R&D projects initiated by TMH.

Digital Home is a new field in home automation. These systems aim to make life at home easier. An already common tool in home automation is the remote controlling of lighting, heating, security, garage doors and entertainment devices as TV, Hi-Fi, video, etc. The research focuses on the evolution and the present of digital home systems. Current systems are aimed at integration, the possibility to control multiple household and entertainment devices with non-dedicated controllers, such as a cellular phone or multi-purpose displays scattered around the flat.

The Mobile Communications and Computing Laboratory (MCL) supported by TMH is located at the Department of Telecommunications of BME. Currently there are six staff members, 17 PhD students and approximately 80 undergraduates working on various projects. MCL has strong and successful cooperation since its foundation with TMH. In 2006, the projects focused on 3G radio access planning, application of mobile technology in interactive TV broadcasting and mobile security.

ENUM is an Internet Engineering Task Force (IETF) standard. ENUM allows telephone operators to map telephone numbers to various Internet services. ENUM uses the standard domain name system (DNS) to store the mapping information about different types of services and its mappings. ENUM facilitates the convergence of telecommunications technologies. There were two studies prepared for TMH which describe the technology, the relevant standards and the recent developments in the standardization. Both studies concentrate on the implementation and the use of ENUM by TMH to introduce new services in the Hungarian market.

One of the new technologies in mobile communications is the Radio Frequency Identification (RFID). RFID offers a means of identification, where reader devices are capable of sensing and reading data from RFID tags in their active radius without physical contact. The goal of the current project is to provide TMH with up-to-date information, educational material, expert consultations, testing environment and experimental pilot projects in the area of RFID technology. As a result of this project, TMH will be better prepared for developing and using commercial RFID applications once RFID enabled mobile phones become widely available.

Macedonian Mobile Operations

Research and development projects at T-Mobile Macedonia are performed in close cooperation with suppliers and state educational institutions. The aim of these projects is to prepare T-Mobile Macedonia to meet the needs of the rapidly developing market and to optimize the maintenance of current activities.

The software developed for Optimization, Measurement, Analyses and Presentation with visualization (OMAP) represents a modular and flexible solution based on existing informatics infrastructure at T-Mobile Macedonia, in accordance with international software engineering standards. The software

provides traffic analyses based on information from switches in real time and monitoring of congestion of each traffic route.

The Base Station Alarm Monitoring Performance (BAMP) is a modular software application, which provides alarm monitoring of T-Mobile Macedonia s radio network and inventory management of base stations. The application identifies and reports causes for malfunction of base stations and facilitates prompt corrective actions.

Our R&D teams have developed an e-recharge gateway function that is offered and used by T-Mobile Macedonia dealers for sales of electronic recharges of prepaid vouchers. The system is experiencing intense capacity growth as more and more dealers are utilizing this cost effective process for voucher sales.

Mass market SMS, Interactive Voice Response (IVR), SMS2TV based games and quizzes are also developed to support our market presence and leadership.

In cooperation with other T-Mobile International companies, we are in an early stage of developing a system for Automated Device Management that should enable easier VAS service adoption on the local market.

T-Mobile Macedonia started an IT infrastructure consolidation project aimed at transforming it to a better operating and more efficient system. Together with our suppliers, we are building a component based, service oriented architecture that should enable leaner operation and faster time-to-market service development.

RISK MANAGEMENT POLICIES

It is our policy that all disclosures made by us to our security holders and the investment community be 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, including by-laws of the Budapest Stock Exchange and rules adopted by the U.S. Securities and Exchange Commission (SEC). To achieve these objectives, we formed the Disclosure Committee and developed and have continuously enhanced our risk management policies.

Risk Management Policies

Our risk management includes identification, assessment and evaluation of risks, development of necessary action plans, and monitoring of performance and results. For risk management to be effective, we must ensure that management take business decisions with full understanding of all relevant risks.

In 1999, we established a formal risk management system. In 2000, we established a department to co-ordinate all risk management tasks. This system was integrated into the risk management system of DT in 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 a Chief Executive Officer (CEO) directive on risk management were published in 2003. 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 Group. All of our subsidiaries, business units, divisions and entities are obliged to identify and report their operational risks on a quarterly basis. After evaluation of these risks, results are reported to our management, to the Audit Committee and to DT.

Following the enactment of the Sarbanes-Oxley Act, we decided to enhance our risk management procedures. As this new law requires prompt disclosure of all risk items influencing investors decisions, 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 daily by the risk management department, and the Chief Financial Officer (CFO) is notified when a new material risk or information is identified.

A CEO directive has been issued to define responsibilities of each employee in risk monitoring and management. In addition, an e-learning course was created to train our employees on requirements of the Sarbanes-Oxley Act, our enhanced reporting and corporate governance obligations and the enhanced risk reporting procedures. Completion of this course has been made compulsory for all of our employees.

For further discussion of the steps that we are taking to remedy our control deficiencies, see Item 15 Controls and Procedures.

Disclosure Committee

We established the Disclosure Committee on July 31, 2003. The Disclosure Committee acts both in plenary meetings and through its members acting individually. It supports CEO and CFO in fulfilling their responsibility to oversee processes designed to ensure accuracy and timeliness of our disclosures.

The Disclosure Committee consists of individuals knowledgeable in significant and diverse aspects of our business, finances and risks. The members of the Disclosure Committee are:

- Group Compliance Director;
- Director of Group Accounting Branch;
- Director of Group Legal Services Branch;
- Director of Group Human Resources Branch;
- Head of Secretariat of the Chairman-CEO;
- Head of External Reporting Department;
- Head of the Business Development and Acquisitions Branch;
- Head of Group Investor Relations Department; and
- Head of Group Risk Management Department.

Director of Internal Audit Branch is a permanent invitee.

Principal responsibilities of the Disclosure Committee are as follows:

- preparation of all SEC and Budapest Stock Exchange filings of the Company (e.g., Form 20-F and Registration Statements) and local annual/interim reports that are subsequently submitted on Form 6-K;
- monitoring and recommendation of all disclosure controls and procedures;
- determination of the content of general rules and instructions issued to preparers of all SEC filings of the Company; and
- recommendations as to materiality of information and procedures relating to the CEO and CFO certifications required by the Sarbanes-Oxley Act.

94

ITEM 6 DIRECTORS, SENIOR MANAGEMENT AND EMPLOYEES

Board of Directors

Under Hungarian laws, the Board of Directors is responsible for the Company s management and decides on matters other than those that must be determined by shareholders. The Board of Directors is required to report annually to the shareholders at the general meeting of the shareholders and quarterly to the Supervisory Board on our business administration, state of assets and business policy.

Pursuant to our Articles of Association, the Board of Directors consists of a minimum of six and a maximum of eleven members elected at the annual general meeting of the shareholders for a term of three years. One of the current directors was nominated by the holder of the Series B Share pursuant to the Articles of Association, seven of the current directors were nominated by MagyarCom and two of the current directors are independent; MagyarCom therefore controls Magyar Telekom.

Meetings of the Board of Directors are held at least four times a year. Meetings of the Board of Directors require the presence of six members for a quorum. Each member has one vote. The Board of Directors passes resolutions by a simple majority vote.

On December 31, 2006, members of the Board of Directors, their principal occupations and the years of their original election were as follows:

Name	Age	Principal Occupation	Member since
Christopher Mattheisen	45	Chairman and Chief Executive Officer of Magyar Telekom Plc.	2006
Dr. István Földesi(1)	58	International business advisor	2003
Dr. Mihály Gálik	60	Director of the Marketing and Media Institute of the Corvinus University	2006
Michael Günther	62	Member of the Management Board of T-Mobile International	2002
Dr. Klaus Hartmann(2)	46	Chairman and Chief Executive Officer of Polska Telefonia Cyfrowa Sp. Z o.o	2000
Horst Hermann	52	Senior Executive Vice President of DT, responsible for Affiliate Management in Central and Eastern Europe	2003
Thilo Kusch	42	Chief Financial Officer of Magyar Telekom Plc.	2006
Gerhard Mischke	48	Senior Executive Vice President, Treasury and International Investment, DT	2005
Frank Odzuck	47	Chief Executive Officer of Zwack Unicum Plc.	2006
Dr. Ralph Rentschler	46	Member of the Management Board of T-Com	2003

(1) Representative of the holder of the Series B Share

(2) Resigned from his position on June 19, 2007.

Other Principal Directorships of Members of the Board of Directors

Name	Position held	Company
Christopher Mattheisen	None	
Dr. István Földesi	President	Inter-Access, Inc. (US)
	Member of the Board of Directors	Sláger Rádió
	Managing Director	Hungarian Technology Center
Dr. Mihály Gálik	None	
Michael Günther	Chairman of the Board of Directors	T-Mobile Slovensko a.s., Slovakia
	Member of the Board of Management	T-Mobile Worldwide Holding GmbH
	Chairman of the Supervisory Board	T-Mobile Macedonia
	Chairman of the Supervisory Board	Polska Telefonia Cyfrowa Sp. Z. o.o., Poland
	Member of the Supervisory Board	T-Hrvatski Telekom, Croatia
	Vice-Chairman of the Supervisory Board	T-Mobile Hrvatski d.o.o., Croatia
Dr. Klaus Hartmann	Chairman of the Management Board	Polska Telefonia Cyfrowa
Horst Hermann	Member of the Supervisory Board	T-Hrvatski Telekom, Croatia
	Member of the Board of Directors	Slovak Telecom
Thilo Kusch	None	
Gerhard Mischke	Member of the Supervisory Board	Deutsche Telekom, Inc., New York
	Member of the Supervisory Board	DeTe Asia Holding GmbH
	Chairman of the Supervisory Board	T-Hrvatski Telekom, Croatia
	Member of the Supervisory Board	T-Systems International GmbH
Frank Odzuck	Member of the Board of Directors	Zwack Unicum Plc.
Dr. Ralph Rentschler	Member of the Board of Directors	Slovak Telecom
	Member of the Supervisory Board	T-Hrvatski Telekom, Croatia
	Member of the Supervisory Board	CAP Customer Advantage Program GmbH
	Member of the Supervisory Board	DeTe Fleet Services GmbH

Biographies of Members of the Board of Directors

Christopher Mattheisen. Mr. Mattheisen studied economics and finance at Indiana University of Bloomington and at Columbia University. He first came to Hungary in 1990 to start a strategic planning and business consulting company. In 1993, in his capacity as a marketing manager of U.S. West International, Mr. Mattheisen helped launch various Hungarian, Polish and Czech mobile service operators. He worked as a marketing and sales director of TMH between 1993 and 1996. Between 1997 and 1999, he ran sales and marketing activities of MediaOne in London and later worked in Britain as a business, sales and marketing director of BT s Cellnet. In September 2002, Mr. Mattheisen became Chief Officer of Residential Services of Magyar Telekom and in January 2005 Chief Officer of the Wireline Lines of Business (T-Com , including Residential Services, Internet and Network divisions). From December 6, 2006, Mr. Mattheisen is the Chief Executive Officer of Magyar Telekom, from December 21, 2006 he is the Chairman of the Company s Board of Directors.

Dr. István Földesi. Dr. Földesi received a degree in economics in 1972 and graduated with a Ph.D. in 1974. He spent twenty years as a diplomat in London, Madrid and Washington D.C. At the end of the 1980 s, he served as an advisor to the Prime Minister and participated in round table negotiations resulting in political and economic changes. In 1991, he became an advisor to the OECD. He has been working as an international business advisor since 1992. From 1994 to 1999, Mr. Földesi was a member of the Board of Directors of Magyar Telekom and until 1996 he acted as Chairman of the Board. In 2003, he was reappointed as a member of the Board of Directors of Magyar Telekom.

Dr. Mihály Gálik. Dr. Gálik is a senior university lecturer with a Ph.D in economics. He spent nearly two decades in the media, working for Hungarian Radio, where he held several positions involving high responsibility, including that of Managing Director. Afterwards, his professional career has been linked to the Budapest University of Economics (currently called Corvinus University), one of the most prestigious institutions in Hungarian academic education. For three years, he was a senior lecturer, while in the last seven years he headed several departments at the university. He is a key figure of the university s cultural life, author of some 70 scientific publications including four textbooks. He is also a recipient of the Széchenyi Professor Scholarship. He is the Director of the Marketing and Media Institute of the Corvinus University and the Head of the Media, Marketing Communications and Telecommunications Department.

Michael Günther. Mr. Günther studied business administration at universities in Berlin and Hamburg. In 1971, he started his career at Philips-Konzern where he was a financial executive. From 1987 to 1993, Mr. Günther was a member of the Board of Directors of Philips Kommunikations Industrie AG in Nuremberg and was responsible for controlling, finance and accounting, as well as information technology. In 1994, he joined DeTeSystems, a DT subsidiary, as Financial Director. In 1996, Mr. Günther joined DT as Head of Financial and Controlling Division. From September 1997 to August 2000, Mr. Günther served as Financial and Controlling Director at T-Mobile International AG. In February 2000, Mr. Günther became Chief Financial Officer, then since June 2001, he has served as Chief Executive Officer of the Joint Venture Management for T-Mobile International AG.

Dr. Klaus Hartmann. Dr. Hartmann received a Ph.D. in economics from the Institute for Company Management in Germany in 1987. He also holds an MBA from the University of Birmingham. Prior to his employment with DT, he worked for Arthur Andersen in Germany and as a treasurer and operational controller for a subsidiary of the BICC Group. He joined DT in 1995 as Manager of International Capital Markets and became Corporate Treasurer of Global One, a joint venture of DT, France Telekom and Sprint in 1997. He returned to DT s Bonn headquarters as Senior Advisor to CFO in April 2000. He was appointed as CFO of Magyar Telekom and Vice-Chairman of our Management Committee in November 2000. On September 15, 2006, he became CEO of Polska Telefonia Cyfrowa.

Horst Hermann. After graduating with an engineering degree, Mr. Hermann joined DT as an operations manager in the Telecommunications Office in Bonn in 1978. In 1990, he began to work for Corporate Strategy and Regulatory Policy at the DT headquarters. From 1994 until 1996, he was Assistant Managing Director in Business Development and Finance at DT s regional headquarters in Singapore covering branch offices in Hongkong and New Delhi. From 1996 until 1998, Mr. Hermann returned to DT headquarters for a strategic planning position. In April 1998, he joined Magyar Telekom to head Strategy, Business Development and M&A. On January 1, 2002, he became Chief Strategy and International Officer and was also put in charge of our Business Portfolio, Maktel and our group policy for Media. In June 2003, Mr. Hermann became responsible for Affiliate Management for DT s Central and Eastern European telecommunications operations, such as Magyar Telekom, T-Hrvatski Telekom, Croatia and Slovak Telecom.

Thilo Kusch. Mr. Kusch studied communication engineering and business administration at Technische Universität Berlin. From 1989 to 1992 he successfully established his own company selling PCs and PC network to residential and small business customers. From 1992 to 1998 he worked in a leading position in Arthur D. Little s Telecoms, IT, media and entertainment practice as a management consultant and from 1998 to 2001 he was telecommunications equity analyst with Dresdner Kleinwort Wasserstein. He joined Deutsche Telekom Group in 2001 as Senior Director in charge of IPO preparations and investor relations for T-Mobile International. Since April 2002 he was a Senior Executive Vice president of Deutsche Telekom, in charge of investor relations. He was appointed Chief Financial Officer of Magyar Telekom in September 2006.

Gerhard Mischke. Mr. Mischke received a degree in business management at Justus-Liebig University in Gießen in 1984. Between 1985 and 1990, he worked at the Finance Department of Franz Haniel & Cie GmbH in Duisburg. From 1990 until 1991, he worked at the Finance Department of Scrivner Inc., Oklahoma City and concurrently studied as a correspondence student at Cornell University. From 1991 until 1998 he acted as Head of Finance and M&A at GEHE AG, Stuttgart, then he worked as Group Finance Director of GEHE UK, Coventry until 2000. In September 2000, he was appointed Senior Executive Vice President Finance and Treasurer of Deutsche Telekom AG. Since October 2004, he has served as Senior Executive Vice President, Treasury and International Investment.

Frank Odzuck. Mr. Odzuck obtained an economist degree in 1983 in Budapest. He has been working in Hungary for over 15 years. He was the managing director of the Hungarian operations of Eduscho and Eduscho-Tchibo for 8 years and later the managing director of Nestlé-Schöller Hungary Ltd. Since 2003, he has been the CEO of Zwack Unicum Rt, listed on the Budapest Stock Exchange. The company, producing and marketing a genuine Hungaricum , is one of the best-known international companies in Hungary (Underberg, Diageo).

Dr. Ralph Rentschler. Dr. Rentschler has been CFO of T-Com since 2001. After receiving a doctorate degree in economics, he worked for four years for Robert Bosch GmbH as an expert advisor on business principles and methods. His areas of responsibility included investment analysis and cost accounting. Later he became Commercial Manager of Brand Optics Division at Carl Zeiss, where he managed Accounting, Controlling, Data Processing and Purchasing. Mr. Rentschler was Head of Group Controlling and Planning and Reporting Departments at Carl Zeiss from 1992 to 1997. His areas of responsibility included production and investment controlling, controlling of affiliated companies, M&A and strategic planning.

Management Committee

Pursuant to our amended Articles of Association and the amended Rules of Procedure of the Board of Directors, the Board of Directors established a Management Committee in 2000, which is empowered to carry out the day-to-day operations in accordance with the annual business plan. On December 31, 2006, the Management Committee consisted of six chief officers of Magyar Telekom. The members were as follows:

Name	Age	Position	Member since
Christopher Mattheisen	45	Chairman and Chief Executive Officer	2006
Thilo Kusch	42	Chief Financial Officer	2006
Dr. Tamás Pásztory(1)	55	Chief Human Resources and Legal Officer	2000
György Simó	40	Chief Operating Officer, Wireline Services LoB and Chief Executive Officer of T-Online	2006
Zoltán Tankó.	49	Chief Operating Officer, Business Services LoB	2000
János Winkler	52	Chief Operating Officer, Mobile Services LoB	2006

(1) Resigned from his position as of March 30, 2007. Effective April 1, 2007, Éva Somorjai was appointed as Chief Human Resources Officer. At the same time, a Chief Information Officer position was established and István Maradi was appointed to fill this position. Both new officers are members of the Management Committee.

Other Principal Directorships of Members of Management Committee

Name	Position held	Company
Christopher Mattheisen	See above	
Thilo Kusch	See above	
Dr. Tamás Pásztory	Member of the Board of Directors	Investel Zrt.
	Member of the Board of Directors	T-Online Hungary Zrt.
György Simó	Member of the Board of Directors	T-Online Hungary Zrt.
	Member of the Board of Directors	Maktel
	Trustee	Magyar Mozgókép Közalapítvány
	Member of the Advisory Board	Dataplex Kft.
Zoltán Tankó	Chairman of the Supervisory Board	Linum Foundation
János Winkler	None	

Biographies of Chief Officers

Christopher Mattheisen. See Biographies of Members of the Board of Directors above.

Thilo Kusch. See Biographies of Members of the Board of Directors above.

Dr. Tamás Pásztory. Dr. Pásztory graduated with degrees in law and organization engineering. He was appointed Deputy Chief Officer of Magyar Telekom in July 1995 and Chief Human Resources and Legal Officer in February 1996. He joined our predecessor in 1969 and has been in various positions in the human resources area since 1980. His professional expertise includes top-level corporate governance, change management, transformation of companies and corporate groups, as well as business operations. He resigned from his position as of March 30, 2007.

György Simó. Mr. Simó graduated in 1997 at ELTE Sociology Department. During his studies received a scholarship to the Sociology Department of the New School for Social Research (New York). In 1991 he founded Tilos Radio, where he acted as host, later as Chairman of the Board of Trustees. From 1996 to 1998 Vice-Chairman of AMARC-EUROPE, the European Association of Community Radio Broadcasters. From 1999 he was Program Director at MATÁVnet, then in 2000 one of the leaders of the

99

project elaborating Magyar Telekom s Internet strategy. From April 1, 2000 Chief Officer and Executive Director of MATÁVnet Kft., from September 1, 2000 Senior Chief Officer of the company (renamed on May 2, 2001 to Axelero Internet Rt.) responsible for media, strategy and communication, from July 2002 member of Axelero Internet Rt. s Board of Directors. From November 1, 2003 CEO of Axelero Internet, from May 6, 2005 CEO of T-Online, Deputy to Head of T-Com and Head of T-Com s Internet Services Division. As of September 20, 2006, György Simó was appointed Chief Operating Officer of the Wireline LoB of Magyar Telekom. He also retains his position as CEO of T-Online Hungary.

Zoltán Tankó. Mr. Tankó graduated from Budapest Technical University with a degree in electrical engineering. He started as an IT development engineer for Budapest Radio Technology Enterprise in 1980 and for Kőbánya Pharmaceuticals in 1982. He had several positions at Műszertechnika (Instrument technology) starting in 1984, including Chief Telecommunications Officer starting in 1990. He became Director of our Business Communications Branch in February 1996, Chief Sales Officer in January 2000 and Chief Operating Officer of Business Services Lines of Business (T-Systems) in January 2002.

János Winkler. Mr. Winkler earned an economics degree at the Budapest University of Economic Sciences, and in 2000 an MBA degree at Purdue University (USA). He started his career as trade manager with Nikex Foreign Trade Company, then from 1986 to 1991 he served in Beijing at the Commercial Section of the Republic of Hungary, first as commercial secretary, later deputy counselor. From 1992 he was National Sales Manager, later Deputy Director of Marketing at TMH and in 1994 he was appointed Deputy CEO. From February 1996 he has been Chief Marketing and Sales Officer of TMH. As of January 20, 2006, he was appointed TMH s CEO and became member of the Management Committee of Magyar Telekom. From March 1, 2006 he has been Chief Operating Officer of Magyar Telekom s Mobile Services LoB.

Supervisory Board

The Supervisory Board is responsible for supervising our administration and control and for assuring our compliance with Hungarian legal requirements and provisions set out in our governing instruments. The Supervisory Board reviews every significant report delivered to the general meeting of the shareholders, proposals by the Board of Directors, financial statements and proposals regarding profit distribution. The Supervisory Board also prepares a report on these subjects for the annual general meeting of shareholders.

Pursuant to the Articles of Association, the Supervisory Board consists of a minimum of three and a maximum of fifteen members elected by the shareholders for a term of three years. The Works Council nominates one third of the Supervisory Board members. The holder of the Series B Share has the right to nominate one member of the Supervisory Board. Meetings of the Supervisory Board require a quorum of eight members.

On December 31, 2006, the members of the Supervisory Board, their principal occupation and the years of their original election were as follows:

Name	Age	Principal Occupation	Member since
Géza Böhm	54	Chairman of Hungarian Telecommunications Trade Union	2002
Attila Csizmadia(1)	57	Ministry of Finance, Chief Counsellor	2003
Dr. Ádám Farkas	39	CEO of Allianz Bank Zrt.	2005
Dr. János Illéssy	44	Chief Financial Officer of Borsodchem	2006
Gellért Kadlót	58	Member of the Workers Council of the sales field	2002
Dr. Sándor Kerekes	58	Director of Institute of Environmental Sciences Corvinus University Budapest	2006
Dr. Thomas Knoll	40	Senior Executive Vice President, Corporate Audit	2005
Konrad Kreuzer	58	Chairman of the Board of Directors of E.ON Hungária Zrt.	2006
Dr. László Pap	63	Budapest University of Technology, Professor and Head of Telecommunication Department	1998
György Varju	60	Chairman of the Workers Council at Technical Services	2005
Péter Vermes	60	Chairman of Magyar Telekom s Central Workers Council	1995

(1) Representative of the holder of the Series B Share

On March 1, 2007, Dr. György Szapáry joined the Supervisory Board.

Other Principal Directorships of Members of the Supervisory Board

Name	Position held	Company
Géza Böhm	Member of the Supervisory Board	DIMENZIÓ Biztosító és Önsegélyező Egyesület
Attila Csizmadia	Member of the Supervisory Board	Postaautó Tisza ZRt.
	Member of the Supervisory Board	Puskás Tivadar Közalapítvány
	Member of the Supervisory Board	Neumann János Digitális Könyvtár és Multimédiás Központ Kht.
	Member of the Board of Directors	MÁV Cargo ZRt.
Dr. Ádám Farkas	Member of the Board of Directors	Thomson Financial Services Ltd., Hungary
	Member of the Board of Directors	Allianz Bank Zrt.
	Member of the Board of Directors	Budapest Airport Ltd.
	Member of the Supervisory Board	Central European Broker Training Foundation
Dr. János Illéssy	Member of the Supervisory Board	Béres Gyógyszergyár Zrt.
	Member of the Board of Directors	Borsodchem Plc.
Gellért Kadlót	None	
Dr. Sándor Kerekes	Member of the Supervisory Board	Tomori Pál Főiskola
	Chairman of the Advisory Board	Zöld Irányító Alapítvány
	Chairman of the Advisory Board	Partners Hungary Alapítvány
Dr. Thomas Knoll	None	
Konrad Kreuzer	Chairman of the Board of Directors	ZSE
	Chairman of the Supervisory Board	E.ON Tiszántúli Zrt.
	Chairman of the Supervisory Board	E.ON Észak-Dunántúli Zrt.
	Chairman of the Supervisory Board	E.ON Dél-Dunántúli Zrt.
	Chairman of the Supervisory Board	KÖGÁZ Zrt.
	Chairman of the Supervisory Board	DDGÁZ Zrt.
Dr. László Pap	None	
György Varju	None	
Péter Vermes	None	

Biographies of Members of the Supervisory Board

Géza Böhm. Mr. Böhm has been working with Magyar Telekom and its predecessor since 1970. He has worked as a foreman, an administrator in charge of transmission investment and an SDH project leader. He has been an officer of the Workers Council since 1993. Since March 2002, he has been Chairman of the Hungarian Telecommunications Trade Union.

Attila Csizmadia. Mr. Csizmadia holds an engineering degree in telecommunications. From 1968 to 1983, he worked at the Budapest Telephone Directorate as an engineer, then held various management positions. In 1983, he became a senior staff member at the General Directorate of Hungarian Post. From 1986 to 1990, he was a senior staff member and Head of Telecommunications Department at the National Planning Office. From 1990, he worked as Head of Department and chief counsellor in the Ministry of Finance. He also took part in work of various inter-departmental committees and consulting bodies dealing with IT and communications issues.

Dr. Ádám Farkas. Dr. Farkas graduated from the Budapest University of Economics in 1990 and he obtained a Ph.D. from the same institution in 1995. He studied and worked on various research projects at several universities outside Hungary. He started his career as a full-time lecturer at the university and as a finance advisor to EBRD (London). At present, he is a lecturer at the Budapest University of Economics as well as at International Training Centre for Bankers. Between 1997 and 2001 he was Managing Director of the National Bank of Hungary and member of its Board of Directors. From 1999 until 2001, he acted as Deputy Chairman of Keler Rt. s Board of Directors and was a member of the Stock Exchange Council. From 2001, he was Managing Director of CIB Central European International Bank, and then he was Chief Executive Officer between 2002 and 2005. He is a member of executive committees of several Hungarian professional associations as well as of the Supervisory Board of the Central European Training Foundation for Brokers. In March 2006, he became CEO of Allianz Bank Zrt.

Dr. János Illéssy. Dr. Illéssy is an electrical engineer graduated from the Budapest Technical University and acquired MBA and PhD degrees at the Pittsburgh University. For over one and a half decades he worked for Pannonplast, a plastics manufacturer company listed at the Budapest Stock Exchange, in various positions of advisor, controller, Chief Financial Officer and Chief Executive Officer. From 2001 to 2003 he has been the managing director of the Hungarian branch bank office of BNP Paribas. Since 2004 he has been the Chief Financial Officer and member of the Board of Directors of BorsodChem.

Gellért Kadlót. Mr. Kadlót has been working with Magyar Telekom since 1970, initially in operations, and later in development. Currently, he coordinates cooperation between local telecommunications operators and Magyar Telekom within the Domestic Carriers Division. From 1996 to 2005, he was Chairman of the Workers Council of the Domestic Carriers Division. Since 2005, he has been serving as Member of the Workers Council of the sales field.

Dr. Sándor Kerekes. Professor Kerekes has a PhD in Chemistry and a Degree in Economics as well as an advanced Management Program in Harvard Business School. He served as Chairman in various Boards of mid sized companies in Hungary for 15 years. The last 8 years he served as the Head of Business Administration Faculty of the Corvinus University of Budapest. He is the Director of the Institute of Environmental Sciences of Corvinus University.

Dr. Thomas Knoll. Dr. Knoll received a degree in economics in 1992 and a Ph.D. in 1999. During his studies, he acquired job experience at Hypo-Bank and Lufthansa Informationstechnik und Software GmbH where he started his career in 1992. Since December 1992, he has been working at Deutsche Telekom AG in various executive positions. From 1998 until 2000 he acted as Head of the Finance and Controlling Department of Deutsche Telekom AG, Branch of the Network Division, Cologne. In 2000 he became Head of the Board of Management Office and Chief of Staff at the Headquarters in Bonn. At present, he is Senior Executive Vice President, Corporate Audit.

Konrad Kreuzer. Mr. Kreuzer is a lawyer with a degree in Business Administration. After serving in various positions at the Universities of Munich and Konstanz and in the Ministry of Domestic Affairs of the State of Bavaria, he joint Bayernwerke utilities as a Head of the Law and Property Department. Since 1997, he has been serving EON in Hungary as the Chairman of the Board of Directors. His current responsibilities are Legal Affairs, Gas Business and International Affairs. He is also a Chairman of the Board of Directors of Západoslovenska energetika, Slovakia.

Dr. László Pap. Dr. Pap graduated from the Budapest Technical University with a degree in telecommunications. He received a Ph.D. in 1980 and Doctor of Sciences (the highest degree awarded by the Hungarian Academy of Sciences) in 1992. He has been a professor in the Electrical Engineering Department and Head of the Department of Telecommunications at Budapest Technical University since 1967. He has obtained numerous patents for his inventions. He is Vice President of the Scientific Society of Telecommunications, a member of the editorial board of the periodical World of Nature, a member of the Hungarian Society of Inventors, and an expert of the Hungarian Space Research Governmental Committee.

György Varju. Mr. Varju has been working with Magyar Telekom and its legal predecessor since 1977. Until 1998, he acted as an on-site construction manager. In 1993, he was elected to the Workers Council, and he is now Chairman of the Workers Council at Technical Services and a member of the Central Workers Council. Between 1999 and 2002, he was a member of Magyar Telekom s Supervisory Board as a representative of the employees.

Péter Vermes. Mr. Vermes became a qualified engineer in 1972, graduated with a degree in telecommunications in 1975 and became a teacher of technical sciences in 1978. Between 1972 and 1986, he worked for the Budapest Regional Directorate and between 1986 and 1997 for the Long-Distance Telecommunications Directorate. He currently works for the Operations and Maintenance Directorate. He has been Chairman of our Central Workers Council since 1993. He was elected as the employees representative on the Supervisory Board in 1995 for the first time.

The mandate of the members of the Board, Supervisory Board and Audit Committee expired on April 26, 2007, on the date of the annual general meeting closing business year 2006. On the same day, the annual general meeting elected the following people to these bodies:

Board of Directors: Dr. István Földesi, Dr. Mihály Gálik, Michael Günther, Dr. Klaus Hartmann, Horst Hermann, Rudolf Kemler, Thilo Kusch, Christopher Mattheisen, Frank Odzuck and Dr. Ralph Rentschler.

Supervisory Board: Jutta Burke, Attila Csizmadia, Dr. Ádám Farkas, Dr. János Illéssy, Gellért Kadlót, Dr. Sándor Kerekes, István Koszorú, Konrad Kreuzer, Dr. László Pap, Dr. György Szapáry, Péter Vermes and György Varju.

Audit Committee: Dr. Ádám Farkas, Dr. János Illéssy, Dr. Sándor Kerekes, Dr. László Pap and Dr. György Szapáry.

The mandate of the members of the Board, Supervisory Board and Audit Committee lasts until the day of the Annual General Meeting that closes fiscal year 2009, but no later than May 31, 2010.

Indemnification of the Board of Directors and the Supervisory Board

Pursuant to our Articles of Association, to the extent permitted by law, we are required to indemnify each current and former member of the Board of Directors and the Supervisory Board under certain circumstances. Generally, if such individual is liable for certain costs or damages in connection with his or her board position and has acted in good faith, we must indemnify him or her. We may maintain insurance on behalf of any member of the Board of Directors or the Supervisory Board against any liability asserted against him or her and incurred by him or her in any such capacity, whether or not we have the obligation to indemnify him or her against such liability.

Statement of the Board of Directors

The role of the Board of Directors is to act on behalf of the shareholders to ensure that Magyar Telekom operates in a manner that serves the interests of shareholders all over the world. As members of Magyar Telekom s governing body we will always act in accordance with our fiduciary responsibilities and the following values:

- accountability to our shareholders;
- openness to scrutiny;
- transparency of all decisions taken; and
- deliberation that will be fair and open but also efficient, timely and orderly.

By accepting to serve on Magyar Telekom s Board, we have committed ourselves not to spare neither time nor effort to earn the trust of those who have invested in the future of this Company.

Compensation of Directors and Officers

For the year ended December 31, 2006, the aggregate compensation of the members of the Board of Directors was HUF 8.5 million.

For the year ended December 31, 2006, the aggregate compensation of the members of the Supervisory Board was HUF 17.5 million.

For the year ended December 31, 2006, the aggregate compensation of the members of the Management Committee (MC) was HUF 817.3 million.

Half of the MC members have an employment contract for a fixed duration. Pursuant to Hungarian legislation, if an employment contract is terminated before the end of its term, the average compensation received by the employee prior to such termination is payable for the remaining period up to 12 months. In the case of an employment contract for a fixed duration the notice period is normally six months, and severance is between 16 and 21 months.

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 Group and is required to refrain from provision of 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 Group 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.

The MC members from foreign countries may be entitled to housing subsidies.

In line with the Company s allowance scheme, the company contributes to the personal pension scheme and the personal insurance scheme on behalf of the MC members. In addition, the MC members are entitled to the use of company cars.

Board Practices

Members of the Board of Directors and the Supervisory Board are elected for a term of three years. Members of the Management Committee are elected for the duration of their employment in the respective chief officer position.

Employment contracts with our management employees contain special provisions providing for entitlements after termination of employment; therefore, the amount of severance is higher than the amount required by the applicable provisions of the Labor Code.

In compliance with the relevant provisions of the new Company Act and the amendments to the Company s Articles of Association approved on October 9, 2006 the EGM held on November 6, 2006 elected an Audit Committee from the independent members of the Supervisory Board. Since November 6, 2006, the members of the Audit Committee of Magyar Telekom are Dr. Ádám Farkas (Chairman), Dr. László Pap, Dr. János Illéssy, Dr. György Szapáry and Dr. Sándor Kerekes. The mandate of Dr. György Szapáry has begun as of March 1, 2007.

The Audit Committee assists in appointment of independent auditors to be elected by the annual general meeting and reviews the scope of external audit services. It advises the Supervisory Board with respect to approval of all audit and non-audit services to be performed by the external auditor. The Audit Committee also reviews our annual financial statements, taking into account results of audits and reviews performed by the independent auditors. The Audit Committee also reviews financial reports submitted to the stock exchanges, banks and regulatory bodies as well as reports prepared by our internal auditors. The Audit Committee meets at least four times a year.

The Remuneration Committee makes proposals to the Board of Directors with respect to appointment and dismissal, as well as remuneration of chief officers, including establishment and assessment of bonus targets. Members of the Remuneration Committee are Michael Günther, Frank Odzuck and Dr. Ralph Rentschler. The Remuneration Committee meets at least three times a year.

Employees

We had 12,341 employees as of December 31, 2006. The following table provides information concerning the number of full-time employees, including full-time equivalents, of Magyar Telekom Plc. and its consolidated subsidiaries:

	2004	2005	2006
Magyar Telekom Plc.	7,740	5,478	6,980
Magyar Telekom Plc. and its consolidated subsidiaries:	13,724	11,919	12,341

The following table provides information on the breakdown of Magyar Telekom s employees by operations:

	Number of employees		
	2004	2005	2006
Hungarian fixed line operations	9,141	6,852	6,963
International fixed line operations	2,386	2,760	2,901
Hungarian mobile operations	1,780	1,708	1,880
International mobile operations	417	599	597
Total	13,724	11,919	12,341

Workforce Reduction and Redeployment. Centralization, technological improvements and attrition have allowed us to reduce the size of our workforce. While overall personnel levels are falling, the number of highly skilled employees is increasing. We plan to further reduce the number of our employees.

In 2005 and 2006, we carried out a restructuring program, which included a significant headcount reduction. The objective of the restructuring program was to redefine the focus of our operation and consumption patterns. We reallocated substantial human and financial resources to the mobile, data and Internet operations.

Employee Representation and Labor Relations. Magyar Telekom Plc. has entered into a collective bargaining agreement 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 Chief Executive Officer, regardless of their union membership status. Wage terms in the agreement must be renegotiated annually. Under the agreement, employees are generally entitled to prior notice before termination. Furthermore, employees are entitled to a specific amount of severance pay, which depends on the tenure of the employee. Employees are also entitled to welfare benefits as discussed below.

In addition to the collective bargaining agreement, employees of our Hungarian operations are generally covered by the Hungarian Labor Code, Law XXII of 1992, as amended, which imposes various restrictions on the involuntary termination of employment. The Hungarian 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 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 us 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.

Under the Hungarian Companies Act, employee representatives on the Supervisory Board are nominated by the Workers Council in cooperation with the Trade Union. The composition of the Supervisory Board is approved by the annual general meeting. At least one third of the members of the Supervisory Board must be employee representatives. Currently, four members of the Supervisory Board are employee representatives. These members are Géza Böhm, Gellért Kadlót, György Varju and Péter Vermes.

We believe that our relations with our employees are good. We have not experienced any labor strikes or disruptions since our formation.

Pensions and Benefit Programs. We provide employees with discounted telephone services, subsidized meals, interest-free loans to purchase real estate, 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 voluntary pension fund and supplementary benefits fund, which provide private pension and health insurance benefits supplementing government pension and health benefits. We do not, however, guarantee payment by the benefits fund to its members. At the end of 2006, approximately 85 percent of all employees participated in the pension plan, 78 percent in the self-help plans and 71 percent in the health fund.

Share Ownership of Management

The following table sets out information relating to holdings of ordinary shares by our directors and executive officers at December 31, 2006:

Name	Position	No. of Options Owned	No. of Shares Owned
Christopher Mattheisen	Chairman-CEO, Board Member		
Dr. Klaus Hartmann	Board Member	103,600	8,000
Dr. Mihály Gálik	Board Member		1,000
Horst Hermann	Board Member, Remuneration Committee Member		400
Attila Csizmadia	Supervisory Board Member		6,272
György Varju	Supervisory Board Member		417
Péter Vermes	Supervisory Board Member	3,600	8,800
Dr. Tamás Pásztory	Chief Human Resources and Legal Officer	70,000	
Zoltán Tankó	Chief Operating Officer, Business Services LoB		1,100
Total		177,200	25,989

For information about share options, see Note 28 to the consolidated financial statements.

ITEM 7 MAJOR SHAREHOLDERS AND RELATED PARTY TRANSACTIONS

Major Shareholders

The share capital of Magyar Telekom Plc. is HUF 104,276,831,500, consisting of 1,042,768,215 Series A ordinary shares and one Series B voting preference share. All Series A ordinary shares have a nominal value of HUF 100 each and the Series B Share has a nominal value of HUF 10,000. The holder of the Series B Share enjoys certain preferential voting and other rights. See Item 10 Additional Information Voting Rights and Voting Series B Share and Transfer of Shares .

Ordinary shares outstanding as of December 31, 1999 amounted to 1,037,281,600 shares. In June 2000, 630,000 ordinary shares of the Company were registered, which increased Magyar Telekom Plc. s number of registered ordinary shares to 1,037,911,600. Of the newly issued shares, 77,270 ordinary shares were traded outside Magyar Telekom. Consequently, the number of shares outstanding increased to 1,037,358,870 shares.

In 2002, the remaining 552,730 shares from the June 2000 transaction issue were traded outside Magyar Telekom. In addition, as a result of the new management stock ownership program launched in 2002, we issued 4,900,000 shares of common stock, which were repurchased immediately. As a result, the number of registered shares increased to 1,042,811,600.

At the end of February 2006, TMH was merged into Magyar Telekom Plc. According to the Hungarian Act on Business Associations it is not mandatory for the shareholders to remain shareholders of the merged company and the company s share capital should be reduced by the nominal value of the shares held by departing shareholders. When departing shareholders stated to leave the merged Company, MagyarCom, as controlling stakeholder, also had to divest some of the interest in Magyar Telekom to avoid a public offering procedure. As 43,385 shares were divested by departing shareholders, the number of ordinary shares outstanding decreased to 1,042,768,215 as of February 28, 2006, when the Court of Registry registered the merger.

Information concerning our ownership structure as of December 31, 2006 is set out in the following table:

	Percentage of