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.

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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

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	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.

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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.

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	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

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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

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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 ou