



THE CZECH REPUBLIC

acting through the Ministry of Finance

€3,000,000,000

PROGRAMME FOR THE ISSUANCE OF DEBT INSTRUMENTS

Application has been made to the Luxembourg Stock Exchange for debt instruments (the “Instruments”) issued under the programme (the “Programme”) described in this Information Memorandum (as defined herein) to be listed on the Luxembourg Stock Exchange during the period of twelve months after the date hereof. However, Instruments may also be issued under the Programme which are not listed on any stock exchange. The Programme also permits Instruments to be issued on an unlisted basis or to be admitted to listing, trading and/or quotation by such other or further listing authorities, stock exchanges and/or quotation systems as may be agreed with the Issuer (as defined herein).

Arrangers for the Programme

Deutsche Bank

Morgan Stanley

Dealers

Deutsche Bank

Morgan Stanley

3 June 2004

The Czech Republic (the “**Issuer**”) acting through the Ministry of Finance accepts responsibility for the information contained in this document. To the best of the knowledge and belief of the Issuer (which has taken all reasonable care to ensure that such is the case), the information contained in this document is in accordance with the facts and does not omit anything likely to affect the import of such information.

This document should be read and construed with any amendment or supplement thereto (this document, as amended or supplemented, the “**Information Memorandum**”) and with any other documents incorporated by reference and, in relation to any Series (as defined herein) of Instruments, should be read and construed together with the relevant Pricing Supplements) (as defined herein). This Information Memorandum may only be used for the purposes for which it has been published.

The Issuer has confirmed to the dealers (the “**Dealers**”) named under “Subscription and Sale” below that this Information Memorandum is true, accurate and complete in all material respects and is not misleading; that the opinions and intentions expressed therein are honestly held and based on reasonable assumptions; that there are no other facts in relation to the information contained or incorporated by reference in this Information Memorandum the omission of which would, in the context of the Programme or the issue of the Instruments, make any statement therein or opinions or intentions expressed therein misleading in any material respect; and that all reasonable enquiries have been made to verify the foregoing. The Issuer has further confirmed to the Dealers that this Information Memorandum (together with the relevant Pricing Supplement) contains all such information as may be required by all applicable laws, rules and regulations.

No person has been authorised by the Issuer to give any information or to make any representation not contained in or not consistent with this Information Memorandum or any other document entered into in relation to the Programme or any information supplied by the Issuer or such other information as is in the public domain and, if given or made, such information or representation should not be relied upon as having been authorised by the Issuer or any Dealer.

No representation or warranty is made or implied by the Dealers or any of their respective affiliates, and neither the Dealers nor any of their respective affiliates makes any representation or warranty or accepts any responsibility, as to the accuracy or completeness of the information contained in this Information Memorandum. Neither the delivery of this Information Memorandum or any Pricing Supplement nor the offering, sale or delivery of any Instrument shall, in any circumstances, create any implication that the information contained in this Information Memorandum is true subsequent to the date thereof or the date upon which this Information Memorandum has been most recently amended or supplemented or that there has been no adverse change in the financial situation of the Issuer since the date thereof or, if later, the date upon which this Information Memorandum has been most recently amended or supplemented or that any other information supplied in connection with the Programme is correct at any time subsequent to the date on which it is supplied or, if different, the date indicated in the document containing the same. Each potential purchaser of Notes should determine for itself the relevance of the information contained in this Information Memorandum and its purchase of Notes should be based upon any such investigation as it deems necessary.

The distribution of this Information Memorandum and any Pricing Supplement and the offering, sale and delivery of the Instruments in certain jurisdictions may be restricted by law. Persons into whose possession this Information Memorandum or any Pricing Supplement comes are required by the Issuer and the Dealers to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Instruments and on the distribution of this Information Memorandum or any Pricing Supplement and other offering material relating to the Instruments, see “Subscription and Sale”. In particular, Instruments have not been and will not be registered under the United States Securities Act of 1933 (as amended) and may include Instruments in bearer form which are subject to U.S. tax law requirements. Subject to certain exceptions, Instruments may not be offered, sold or delivered within the United States or to U.S. persons.

Neither this Information Memorandum nor any Pricing Supplement constitutes an offer or an invitation to subscribe for or purchase any Instruments and should not be considered as a recommendation by the Issuer, the Dealers or any of them that any recipient of this Information Memorandum or any Pricing Supplement should subscribe for or purchase any Instruments. Each recipient of this Information Memorandum or any Pricing Supplement shall be taken to have made its own investigation and appraisal of the condition (financial or otherwise) of the Issuer.

All references in this Information Memorandum to “Euro”, “EUR” or “€” are to the single currency introduced at the start of the third stage of European Economic and Monetary Union pursuant to the Treaty establishing the European Community, as amended and all references to “Czech Koruna” or

“CZK” are to the lawful currency of the Czech Republic. For the convenience of the reader, this Information Memorandum contains translations of information in Czech koruna amounts into EUR at the specified rates. Unless otherwise indicated, the EUR equivalent for information in Czech koruna is based on the average mid-rate reported by the Česká národní banka (the “Czech National Bank” or “CNB”) for 2003, which was CZK 31.844 = EUR 1. On 27 May 2004, the exchange rate (mid-rate) between Czech koruna and EUR reported by the CNB was CZK 31.865 = 1 EUR. No representation is made that the Czech koruna or EUR amounts referred to herein could have been or could be converted into EUR or Czech koruna, as the case may be, at any particular rate or at all.

Certain figures included in this Information Memorandum have been subject to rounding adjustments; accordingly, figures shown for the same category presented in different tables may vary slightly and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

In connection with the issue of any Tranche of Instruments under the Programme, the Dealer (if any) which is specified in the relevant Pricing Supplement as the Stabilising Manager (or any person acting for the Stabilising Manager) may over-allot or effect transactions with a view to supporting the market price of the Instruments at a level higher than that which might otherwise prevail for a limited period. However, there may be no obligation on the Stabilising Manager (or any agent of the Stabilising Manager) to do this. Such stabilising, if commenced, may be discontinued at any time and must be brought to an end after a limited period. Such stabilising shall be in compliance with all applicable laws, regulations and rules.

DOCUMENTS INCORPORATED BY REFERENCE

This Information Memorandum should be read and construed in conjunction with each relevant Pricing Supplement. All amendments and supplements to this Information Memorandum and any Pricing Supplements prepared by the Issuer from time to time shall be deemed to be incorporated in, and to form part of, this Information Memorandum, save that any statement contained in this Information Memorandum or in any of the documents incorporated by reference in, and forming part of, this Information Memorandum shall be deemed to be modified or superseded for the purpose of this Information Memorandum to the extent that a statement contained in any document subsequently incorporated by reference modifies or supersedes such statement.

The Issuer has undertaken, in connection with the listing of the Instruments on the Luxembourg Stock Exchange, that if there shall occur any adverse change in the financial position of the Issuer or any change in the information set out under “**Terms and Conditions of the Instruments**”, that is material in the context of issuance under the Programme the Issuer will prepare or procure the preparation of an amendment or supplement to this Information Memorandum or, as the case may be, publish a new Information Memorandum, for use in connection with any subsequent issue by the Issuer of Instruments to be listed on the Luxembourg Stock Exchange.

The Issuer will, at the specified offices of the Paying Agents, provide, free of charge, upon request therefor, a copy of this Information Memorandum (or any document incorporated by reference in this Information Memorandum). Written or telephone requests for such documents should be directed to the specified office of any Paying Agent or the specified office of the Listing Agent in Luxembourg.

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SUMMARY OF THE PROGRAMME

The following is a brief summary only and should be read in conjunction with the rest of this document and, in relation to any Instruments, in conjunction with the relevant Pricing Supplement and, to the extent applicable, the Terms and Conditions of the Instruments set out herein.

Issuer:	The Czech Republic acting through the Ministry of Finance
Arrangers:	Deutsche Bank AG London and Morgan Stanley & Co. International Limited.
Dealers:	Deutsche Bank AG London and Morgan Stanley & Co. International Limited and any other dealer appointed from time to time by the Issuer either generally in respect of the Programme or in relation to a particular Tranche (as defined below) of Instruments.
Issue and Paying Agent:	Citibank, N.A.
Registrar:	Citigroup Global Markets Deutschland AG & Co. KGaA
Luxembourg Listing Agent:	Kredietbank S.A. Luxembourgeoise
Initial Programme Amount:	€3,000,000,000 (and, for this purpose, any Instruments denominated in another currency shall be translated into €3,000,000,000 at the date of the agreement to issue such Instruments using the spot rate of exchange for the purchase of such currency against payment of U.S. dollars being quoted by the Issue and Paying Agent on the date on which the relevant agreement in respect of the relevant Tranche (as defined below) was made or such other rate as the Issuer and the relevant Dealer may agree) in aggregate principal amount of Instruments outstanding at any one time. The maximum aggregate principal amount of Instruments permitted to be outstanding at any one time under the Programme may be increased from time to time, subject to compliance with the relevant provisions of the Dealership Agreement as defined under “ Subscription and Sale ”.
Issuance in Series:	Instruments will be issued in series (each, a “ Series ”). Each Series may comprise one or more tranches (“ Tranches ” and each, a “ Tranche ”) issued on different issue dates. The Instruments of each Series will all be subject to identical terms, except that the issue date and the amount of the first payment of interest may be different in respect of different Tranches. The Instruments of each Tranche will all be subject to identical terms in all respects save that a Tranche may comprise Instruments of different denominations.
Form of Instruments:	Instruments may be issued in bearer form or in registered form. In respect of each Tranche of Instruments issued in bearer form, the Issuer will deliver a temporary global Instrument (a “ Temporary Global Instrument ”) or (if so specified in the relevant Pricing Supplement in respect of Instruments to which U.S. Treasury Regulation §1.163-5(c)(2)(i)(C) (the “ TEFRA C Rules ”) applies (as so specified in such Pricing Supplement)) a permanent global instrument (a “ Permanent Global Instrument ”). Such global Instrument will be deposited on or before the relevant issue date therefor with a depositary or a common depositary for Euroclear Bank S.A./N.V., as operator of the Euroclear System (“ Euroclear ”) and/or Clearstream Banking, société anonyme, Luxembourg (“ Clearstream, Luxembourg ”) and/or any other relevant clearing system. Each Temporary Global Instrument will be exchangeable for a Permanent Global Instrument or, if so specified in the relevant Pricing Supplement, for Instruments in definitive bearer form (“ Definitive Instruments ”) and/or (if so specified in the relevant Pricing Supplement) registered form in accordance with its terms (“ Registered Instruments ”). Each Permanent Global Instrument will be exchangeable for Definitive Instruments and/or (if so specified in

the relevant Pricing Supplement) Registered Instruments in accordance with its terms. (See further under “**Provisions Relating to the Instruments whilst in Global Form**” below). Definitive Instruments will, if interest-bearing, either have interest coupons (“**Coupons**”) attached and, if appropriate, a talon (“**Talon**”) for further Coupons and will, if the principal thereof is repayable by instalments, have payment receipts (“**Receipts**”) attached. Each Instrument issued in registered form shall represent the entire holding of Registered Instruments by the same holder. A Registered Instrument may be registered in the name of a nominee for one or more clearing system and such an Instrument is referred to herein as a “**Global Registered Instrument**”. Instruments in registered form may not be exchanged for Instruments in bearer form.

Currencies:

Instruments may be denominated in any currency or currencies, subject to compliance with all applicable legal and/or regulatory and/or central bank requirements.

Issues of Instruments with a maturity of more than one year denominated in Swiss Francs or carrying a Swiss Franc-related element will be effected in compliance with the relevant regulations of the Swiss National Bank based on article 7 of the Federal Law on Banks and Savings Banks of 8 November 1934 (as amended) and article 15 of the Federal Law on Stock Exchanges and Securities Trading of 24 March 1995 (as amended) in connection with article 2, paragraph 2 of the Ordinance of the Federal Banking Commission on Stock Exchanges and Securities Trading of 25 June 1997. Under these regulations, the relevant Dealer or, in the case of a syndicated issue, the lead manager (the “**Swiss Dealer**”), must be a bank domiciled in Switzerland (which includes branches or subsidiaries of a foreign bank located in Switzerland) or a securities dealer duly licensed by the Swiss Federal Banking Commission pursuant to the Federal Law on Stock Exchanges and Securities Trading of 24 March 1995 (as amended). The Swiss Dealer must report certain details of the relevant transaction to the Swiss National Bank no later than the date of issue of the relevant Instruments.

Status and Ranking of Instruments:

Instruments issued will constitute direct, general and unconditional obligations of the Issuer which will at all times rank *pari passu* among themselves and at least *pari passu* with all other present and future unsecured obligations of the Issuer save for such obligations as may be preferred by provisions of law that are mandatory and of general application to creditor rights.

Issue Price:

Instruments may be issued at any price and either on a fully or partly paid basis, as specified in the relevant Pricing Supplement.

Maturities:

Any maturity, subject, in relation to specific currencies, to compliance with all applicable legal and/or regulatory and/or central bank requirements.

Where Instruments have a maturity of less than one year and either (a) the issue proceeds are received by the Issuer in the United Kingdom or (b) the activity of issuing the Instruments is carried on from an establishment maintained by the Issuer in the United Kingdom, such Instruments must (i) have a minimum redemption value of £100,000 (or its equivalent in other currencies) and be issued only to persons whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses or who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their business; or (ii) be issued in other circumstances which do not constitute a contravention of section 19

of the Financial Services and Markets Act 2000 (the “FSMA”) by the Issuer.

Redemption:	Instruments may be redeemable at par or at such other Redemption Amount (detailed in a formula or otherwise) as may be specified in the relevant Pricing Supplement.
Early Redemption:	Early redemption will be permitted as mentioned in “ Terms and Conditions of the Instruments – Optional Early Redemption (Call) ” and “ – Optional Early Redemption (Put) ”, only to the extent specified in the relevant Pricing Supplement.
Interest:	Instruments may be interest-bearing or non-interest bearing. Interest (if any) may accrue at a fixed or floating rate and may vary during the lifetime of the relevant Series.
Denominations:	Instruments will be issued in such denominations as may be specified in the relevant Pricing Supplement, subject to compliance with all applicable legal and/or regulatory and/or central bank requirements.
Taxation:	All payments in respect of Instruments will be made free and clear of withholding taxes of the Czech Republic, unless the withholding is required by law. In that event, the Issuer will (subject as provided in Condition 8) pay such additional amounts as will result in the Instrument holders receiving such amounts as they would have received in respect of such Instruments had no such withholding been required.
Redenomination:	In respect of any Tranche of Instruments, if the country of the Specified Currency becomes or, announces its intention to become, a Participating Member State, the Instruments may be redenominated in euro in accordance with Condition 18 if so specified in the relevant Pricing Supplement.
Negative Pledge:	Instruments will have the benefit of a negative pledge in relation to Public External Indebtedness of the Issuer, all as more fully described in Condition 4.
Governing Law:	The Instruments and all related contractual documentation will be governed by, and construed in accordance with, English law.
Listing:	Each Series may be listed on the Luxembourg Stock Exchange and/or any other stock exchange as may be agreed between the Issuer and the relevant Dealer and specified in the relevant Pricing Supplement or may be unlisted.
Terms and Conditions:	A Pricing Supplement will be prepared in respect of each Tranche of Instruments a copy of which will, in the case of Instruments to be listed on the Luxembourg Stock Exchange be delivered to the Luxembourg Stock Exchange on or before the date of issue of such Instruments. The terms and conditions applicable to each Tranche will be those set out herein under “ Terms and Conditions of the Instruments ” as supplemented, modified or replaced by the relevant Pricing Supplement.
Enforcement of Instruments in Global Form:	In the case of Instruments in global form, individual investors rights will be governed by a Deed of Covenant dated 3 June 2004, a copy of which will be available for inspection at the specified office of the Issue and Paying Agent.
Clearing Systems:	Euroclear, Clearstream, Luxembourg and/or, in relation to any Instruments, any other clearing system as may be specified in the relevant Pricing Supplement.

Selling Restrictions:

For a description of certain restrictions on offers, sales and deliveries of Instruments and on the distribution of offering material in the United States of America, the Czech Republic, the United Kingdom, Japan, Switzerland and the Federal Republic of Germany, see under “**Subscription and Sale**”.

TERMS AND CONDITIONS OF THE INSTRUMENTS

The following are the Terms and Conditions of the Instruments which as supplemented, modified or replaced in relation to any Instruments by the relevant Pricing Supplement, will be applicable to each Series of Instruments:

The Instruments are issued pursuant to and in accordance with an issue and paying agency agreement dated 3 June 2004 as amended, supplemented or replaced (the “**Issue and Paying Agency Agreement**”) and made between the Czech Republic acting through the Ministry of Finance (the “**Issuer**”), Citibank, N.A. in its capacity as issue and paying agent (the “**Issue and Paying Agent**”, which expression shall include any successor to Citibank, N.A. in its capacity as such), Citigroup Global Markets Deutschland AG & Co. KGaA as registrar (the “**Registrar**”), which expression shall include any successor to Citigroup Global Markets Deutschland AG & Co. KGaA in its capacity as such) and Kredietbank S.A. Luxembourgeoise and BNP Paribas Luxembourg as paying agents (the “**Paying Agents**”, which expression shall include the Issue and Paying Agent and any substitute or additional paying agents appointed in accordance with the Issue and Paying Agency Agreement, and “**Paying Agents**” shall be construed accordingly) and as transfer agents (“**Transfer Agents**”, which expression shall include any successor or additional transfer agents appointed in accordance with the Issue and Paying Agency Agreement). For the purposes of making determinations or calculations of interest rates, interest amounts, redemption amounts or any other matters requiring determination or calculation in accordance with the Conditions of any Series of Instruments (as defined below), the Issuer may appoint a calculation agent (the “**Calculation Agent**”) for the purposes of such Instruments, in accordance with the provisions of the Issue and Paying Agency Agreement, and such Calculation Agent shall be specified in the applicable Pricing Supplement. The Instruments have the benefit of a deed of covenant (as amended, supplemented or replaced, the “**Deed of Covenant**”) dated 3 June 2004 executed by the Issuer in relation to the Instruments. Copies of the Issue and Paying Agency Agreement and the Deed of Covenant are available for inspection during normal business hours at the specified office of each of the Paying Agents, the Registrar, and the Transfer Agents. All persons from time to time entitled to the benefit of obligations under any Instruments shall be deemed to have notice of, and shall be bound by, all of the provisions of the Issue and Paying Agency Agreement and the Deed of Covenant insofar as they relate to the relevant Instruments.

The Instruments are issued in series (each, a “**Series**”), and each Series may comprise one or more tranches (“**Tranches**” and each, a “**Tranche**”) of Instruments. Each Tranche will be the subject of a pricing supplement (each, a “**Pricing Supplement**”), a copy of which will be available during normal business hours at the specified office of the Issue and Paying Agent and/or, as the case may be, the Registrar. In the case of a Tranche of Instruments in relation to which application has not been made for listing on any stock exchange, copies of the Pricing Supplement will only be available by a Holder of or, as the case may be, a Relevant Account Holder (as defined in the Deed of Covenant) in respect of, such Instruments.

References in these Terms and Conditions to Instruments are to Instruments of the relevant Series and any references to Coupons (as defined in Condition 1.2) and Receipts (as defined in Condition 1.3) are to Coupons and Receipts relating to Instruments of the relevant Series.

References in these Terms and Conditions to the Pricing Supplement are to the Pricing Supplement or Pricing Supplement(s) prepared in relation to the Instruments of the relevant Tranche or Series.

In respect of any Instruments, references herein to these Terms and Conditions are to these terms and conditions as supplemented or modified or (to the extent thereof) replaced by the Pricing Supplement.

1. Form and Denomination

Form of Instruments

- 1.1 Instruments are issued in bearer form (“**Bearer Instruments**”) or in registered form (“**Registered Instruments**”), as specified in the Pricing Supplement and are serially numbered. Registered Instruments are not exchangeable for Bearer Instruments.
- 1.2 Interest-bearing Bearer Instruments have attached thereto at the time of their initial delivery coupons (“**Coupons**”), presentation of which will be a prerequisite to the payment of interest save in certain circumstances specified herein. In addition, if so specified in the Pricing Supplement, such Instruments have attached thereto at the time of their initial delivery, a talon (“**Talon**”) for further coupons and the expression “**Coupons**” shall, where the context so requires, include Talons.

- 1.3 Bearer Instruments, the principal amount of which is repayable by instalments (“**Instalment Instruments**”) have attached thereto at the time of their initial delivery, payment receipts (“**Receipts**”) in respect of the instalments of principal.

Denomination of Bearer Instruments

- 1.4 Bearer Instruments are in the specified Denomination or specified Denominations (each of which denomination is integrally divisible by each smaller denomination) specified in the Pricing Supplement. Bearer Instruments of one denomination may not be exchanged for Bearer Instruments of any other denomination.

Denomination of Registered Instruments

- 1.5 Registered Instruments are in the minimum specified Denomination specified in the Pricing Supplement or integral multiples thereof.

Currency of Instruments

- 1.6 The Instruments are denominated in such currency as may be specified in the Pricing Supplement. Any currency may be so specified, subject to compliance with all applicable legal and/or regulatory and/or central bank requirements.

Partly Paid Instruments

- 1.7 Instruments may be issued on a partly paid basis (“**Partly Paid Instruments**”) if so specified in the Pricing Supplement. The subscription moneys therefor shall be paid in such number of instalments (“**Partly Paid Instalments**”) in such amounts, on such dates and in such manner as may be specified in the Pricing Supplement. The first such instalment shall be due and payable on the date of issue of the Instruments. For the purposes of these Terms and Conditions, in respect of any Partly Paid Instrument, “**Paid Up Amount**” means the aggregate amount of all Partly Paid Instalments in respect thereof as shall have fallen due and been paid up in full in accordance with the Terms and Conditions.

Not less than 14 days nor more than 30 days prior to the due date for payment of any Partly Paid Instalment (other than the first such instalment) the Issuer shall publish a notice in accordance with Condition 15 stating the due date for payment thereof and stating that failure to pay any such Partly Paid Instalment on or prior to such date will entitle the Issuer to forfeit the Instruments with effect from such date (“**Forfeiture Date**”) as may be specified in such notice (not being less than 14 days after the due date for payment of such Partly Paid Instalment), unless payment of the relevant Partly Paid Instalment together with any interest accrued thereon is paid prior to the Forfeiture Date. The Issuer shall procure that any Partly Paid Instalments paid in respect of any Instruments subsequent to the Forfeiture Date in respect thereof shall be returned promptly to the persons entitled thereto. The Issuer shall not be liable for any interest on any Partly Paid Instalment so returned.

Interest shall accrue on any Partly Paid Instalment which is not paid on or prior to the due date for payment thereof at the Interest Rate (in the case of non-interest bearing Instruments, at the rate applicable to overdue payments) and shall be calculated in the same manner and on the same basis as if it were interest accruing on the Instruments for the period from and including the due date for payment of the relevant Partly Paid Instalment up to but excluding the Forfeiture Date. For the purpose of the accrual of interest, any payment of any Partly Paid Instalment made after the due date for payment shall be treated as having been made on the day preceding the Forfeiture Date (whether or not a Business Day as defined in Condition 5.9).

Unless an Event of Default (or an event which with the giving of notice, the lapse of time or the making or giving of any determination or certification would constitute an Event of Default) shall have occurred and be continuing, on the Forfeiture Date, the Issuer shall forfeit all of the Instruments in respect of which any Partly Paid Instalment shall not have been duly paid, whereupon the Issuer shall be entitled to retain all Partly Paid Instalments previously paid in respect of such Instruments and shall be discharged from any obligation to repay such amount or to pay interest thereon.

2. Title and Transfer

- 2.1 Title to Bearer Instruments, Receipts and Coupons passes by delivery. References herein to the “**Holders**” of Bearer Instruments or of Receipts or Coupons are to the bearers of such Bearer Instruments or such Receipts or Coupons.
- 2.2 Title to Registered Instruments passes by registration in the register which the Issuer shall procure to be kept by the Registrar. For the purposes of these Terms and Conditions, “**Registrar**” means, in relation to any Series comprising Registered Instruments, the Principal Registrar, the First Alternative Registrar or, as the case may be, the Second Alternative Registrar, as specified in the Pricing Supplement, provided always that where such Series is listed on the Luxembourg Stock Exchange, “**Registrar**” shall mean the Second Alternative Registrar. References herein to the “**Holders**” of Registered Instruments are to the persons in whose names such Registered Instruments are so registered in the relevant register.
- 2.3 The Holder of any Bearer Instrument, Coupon or Registered Instrument will (except as otherwise required by applicable law or regulatory requirement) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest thereof or therein, any writing thereon, or any theft or loss thereof) and no person shall be liable for so treating such Holder. No person shall have any right to enforce any term or condition of any Instrument under the Contracts (Rights of Third Parties) Act 1999.

Transfer of Registered Instruments and exchange of Bearer Instruments for Registered Instruments

- 2.4 A Registered Instrument may, upon the terms and subject to the conditions set forth in the Issue and Paying Agency Agreement, be transferred in whole or in part only (provided that such part is, or is an integral multiple of, the minimum denomination specified in the Pricing Supplement) upon the surrender of the Registered Instrument to be transferred, together with the form of transfer endorsed on it duly completed and executed, at the specified office of the Registrar or any Transfer Agent. A new Registered Instrument will be issued to the transferee and, in the case of a transfer of part only of a Registered Instrument, a new Registered Instrument in respect of the balance not transferred will be issued to the transferor.
- 2.5 If so specified in the Pricing Supplement, the Holder of Bearer Instruments may exchange the same for the same aggregate principal amount of Registered Instruments upon the terms and subject to the conditions set forth in the Issue and Paying Agency Agreement. In order to exchange a Bearer Instrument for a Registered Instrument, the Holder thereof shall surrender such Bearer Instrument at the specified office outside the United States of the Issue and Paying Agent, the Registrar or of any Transfer Agent together with a written request for the exchange. Each Bearer Instrument so surrendered must be accompanied by all unmatured Receipts and Coupons appertaining thereto other than the Coupon in respect of the next payment of interest falling due after the exchange date (as defined in Condition 2.6) where the exchange date would, but for the provisions of Condition 2.6, occur between the Record Date (as defined in Condition 9B.3) for such payment of interest and the date on which such payment of interest falls due.
- 2.6 Each new Registered Instrument to be issued upon the transfer of a Registered Instrument or the exchange of a Bearer Instrument for a Registered Instrument will, within three Relevant Banking Days of the transfer date or, as the case may be, the exchange date be available for collection by each relevant Holder at the specified office of the Registrar or any Transfer Agent or, at the option of the Holder requesting such exchange or transfer be mailed (by uninsured post at the risk of the Holder(s) entitled thereto) to such address(es) as may be specified by such Holder. For these purposes, a form of transfer or request for exchange received by the Registrar, the Issue and Paying Agent or any Transfer Agent after the Record Date in respect of any payment due in respect of Registered Instruments shall be deemed not to be effectively received by the Registrar, Issue and Paying Agent or any Transfer Agent until the day following the due date for such payment. For the purposes of these Terms and Conditions,
- (i) “**Relevant Banking Day**” means a day on which commercial banks are open for business (including dealings in foreign exchange and foreign currency deposits) in the place where the specified office of the Registrar is located and, in the case only of an exchange of a Bearer Instrument for a Registered Instrument where such request for exchange is made to the Issue and Paying Agent, in the place where the specified office of the Issue and Paying Agent or the Transfer Agent is located;

- (ii) the “**exchange date**” shall be the Relevant Banking Day following the day on which the relevant Bearer Instrument shall have been surrendered for exchange in accordance with Condition 2.5; and
 - (iii) the “**transfer date**” shall be the Relevant Banking Day following the day on which the relevant Registered Instrument shall have been surrendered for transfer in accordance with Condition 2.4.
- 2.7 The issue of new Registered Instruments on transfer or on the exchange of Bearer Instruments for Registered Instruments will be effected without charge by or on behalf of the Issuer, the Issue and Paying Agent, the Registrar or the Transfer Agent, but upon payment by the applicant of (or the giving by the applicant of such indemnity as the Issuer, the Issue and Paying Agent, the Registrar or the Transfer Agent may require in respect of) any tax, duty or other governmental charges which may be imposed in relation thereto.
- 2.8 Upon the transfer, exchange or replacement of Registered Instruments bearing the private placement legend (the “**Private Placement Legend**”) set forth in the form of Registered Instrument scheduled to the Issue and Paying Agency Agreement, the Registrar or any Transfer Agent shall deliver only Registered Instruments that also bear such legend unless either (i) such transfer, exchange or replacement occurs three or more years after the later of (1) the original issue date of such Instruments or (2) the last date on which the Issuer or any affiliates (as defined below) of the Issuer as notified to the Registrar or such Transfer Agent by the Issuer as provided in the following sentence, was the beneficial owner of such Instrument (or any predecessor of such Instrument) or (ii) there is delivered to the Registrar or such Transfer Agent an opinion reasonably satisfactory to the Issuer of counsel experienced in giving opinions with respect to questions arising under the securities laws of the United States to the effect that neither such legend nor the restrictions on transfer set forth therein are required in order to maintain compliance with the provisions of such laws. The Issuer covenants and agrees that it will not acquire any beneficial interest, and will cause its “**affiliates**” (as defined in paragraph (a)(1) of Rule 144 under the Securities Act of 1933, as amended (the “**Securities Act**”)) not to acquire any beneficial interest, in any Registered Instrument bearing the Private Placement Legend unless it notifies the Registrar and Transfer Agent of such acquisition. The Registrar, the Transfer Agents and all Holders shall be entitled to rely without further investigation on any such notification (or lack thereof).
- 2.9 For so long as any of the Registered Instruments bearing the Private Placement Legend remain outstanding and are “**restricted securities**” within the meaning of Rule 144(a)(3) under the Securities Act, the Issuer covenants and agrees that it shall, during any period in which it is not subject to Section 13 or 15(d) under the United States Securities Exchange Act of 1934 nor exempt from reporting pursuant to Rule 12g3-2(b) under such Act, make available to any Holder in connection with any sale thereof and any prospective purchaser of such Instruments from such Holder, in each case upon request, the information specified in, and meeting the requirements of, Rule 144(d)(4) under the Securities Act.

3. Status of the Instruments

The Instruments constitute direct, general and unconditional, unsubordinated and (subject to the provisions of Condition 4) unsecured obligations of the Issuer and rank *par passu* without any preference among themselves and at least *par passu* with all other unsubordinated and unsecured obligations of the Issuer, present and future, save for such obligations as may be preferred by provisions of law that are mandatory and of general application to creditor rights.

4. Negative Pledge

The Issuer undertakes that so long as any of the Instruments remain outstanding (as defined in the Issue and Paying Agency Agreement), the Issuer shall not create nor permit to subsist any Security Interest upon the whole or any part of its present or future assets or revenues to secure any Public External Indebtedness or any Guarantee of any Public External Indebtedness without (a) at the same time or prior thereto securing the Instruments equally and rateably therewith or (b) providing such other security for the Instruments as may be approved by an Extraordinary Resolution of Holders.

For the purposes of this Condition 4:

“**Guarantee**” means any guarantee of, or indemnity in respect of, indebtedness or other like obligation.

“**Public External Indebtedness**” means any present or future indebtedness for borrowed money which is in the form of, or represented by, bonds, notes, debentures or loan stock or other securities and which is, or is capable of being, quoted, listed or ordinarily dealt in on any stock exchange, over-the-counter or other securities market and which is denominated or payable (or at the option of the relevant creditor or holder thereof may be payable), in a currency other than the lawful currency of the Czech Republic provided that, if at any time the lawful currency of the Czech Republic is the Euro, then any indebtedness for borrowed money as described herein, expressed in or payable or optionally payable in Euro, more than 50 per cent. of the aggregate principal amount of which is initially placed outside the Czech Republic and issued after the date on which the Euro becomes the lawful currency of the Czech Republic, shall be included.

“**Security Interest**” means any mortgage, charge, pledge, lien or other security interest.

5. Interest

Interest

- 5.1 Instruments may be interest-bearing or non interest-bearing, as specified in the Pricing Supplement. Words and expressions appearing in this Condition 5 and not otherwise defined herein or in the Pricing Supplement shall have the meanings given to them in Condition 5.9.

Interest-bearing Instruments

- 5.2 Instruments which are specified in the Pricing Supplement as being interest-bearing shall bear interest from their Interest Commencement Date at the Interest Rate payable in arrear on each Interest Payment Date.

Floating Rate Instruments

- 5.3 If the Pricing Supplement specifies the Interest Rate applicable to the Instruments as being Floating Rate, the Interest Rate applicable to the Instruments for each Interest Accrual Period will be determined by the Calculation Agent on the following basis:
- (i) if the Reference Rate is a composite quotation or customarily supplied by one entity, the Calculation Agent will determine the Reference Rate which appears on the Relevant Screen Page as of the Relevant Time on the relevant Interest Determination Date;
 - (ii) in any other case, the Calculation Agent will determine the arithmetic mean of the Reference Rates which appear on the Relevant Screen Page as of the Relevant Time on the relevant Interest Determination Date;
 - (iii) if, in the case of (i) above, such rate does not appear on that page or, in the case of (ii) above, fewer than two such rates appear on that page or if, in either case, the Relevant Screen Page is unavailable, the Calculation Agent will:
 - (A) request the principal Relevant Financial Centre office of each the Reference Banks to provide a quotation of the Reference Rate at approximately the Relevant Time on the Interest Determination Date to prime banks in the Relevant Financial Centre interbank market in an amount that is representative for a single transaction in that market at that time; and
 - (B) determine the arithmetic mean of such quotations; and
 - (iv) if fewer than two such quotations are provided as requested, the Calculation Agent will determine the arithmetic mean of the rates (being the nearest to the Reference Rate, as determined by the Calculation Agent) quoted by major banks in the Principal Financial Centre of the Specified Currency, selected by the Calculation Agent, at approximately 11.00 a.m. (local time in the Principal Financial Centre of the Specified Currency) on the first day of the relevant Interest Accrual Period for loans in the Specified Currency to leading European banks for a period equal to the relevant Interest Accrual Period and in an amount that is representative for a single transaction in that market at that time,

and the Interest Rate applicable to such Instruments during each Interest Accrual Period will be the sum of the relevant margin (the “**Relevant Margin**”) specified in the Pricing Supplement and the rate (or, as the case may be, the arithmetic mean (rounded as aforesaid) of the rates) so determined provided, however, that, if the Calculation Agent is unable to determine a rate (or, as the case may be, an arithmetic mean of rates) in accordance with the above provisions in relation to any Interest

Accrual Period, the Interest Rate applicable to such Instruments during such Interest Accrual Period will be the sum of the Relevant Margin and the rate (or, as the case may be, the arithmetic mean (rounded as aforesaid) of the rates) determined in relation to such Instruments in respect of the last preceding Interest Accrual Period.

ISDA Rate Instruments

- 5.4 If the Pricing Supplement specifies the Interest Rate applicable to the Instruments as being ISDA Rate, each Instrument shall bear interest as from such date, and at such rate or in such amounts, and such interest will be payable on such dates, as would have applied (regardless of any event of default or termination event or tax event thereunder) if the Issuer had entered into an interest rate swap transaction with the Holder of such Instrument under the terms of an agreement to which the ISDA Definitions applied and under which:
- (i) the Floating Rate Option (as defined in the ISDA Definitions) is as specified in the relevant Pricing Supplement;
 - (ii) the Designated Maturity (as defined in the ISDA Definitions) is a period specified in the relevant Pricing Supplement; and
 - (iii) the relevant Reset Date (as defined in the ISDA Definitions) is either (A) if the relevant Floating Rate Option is based on the London inter-bank offered rate (LIBOR) for a currency, the first day of that Interest Period or (B) in any other case, as specified in the relevant Pricing Supplement.

Maximum or Minimum Interest Rate

- 5.5 If any Maximum or Minimum Interest Rate is specified in the Pricing Supplement, then the Interest Rate shall in no event be greater than the maximum or be less than the minimum so specified.

Accrual of Interest

- 5.6 Interest shall accrue on the Outstanding Principal Amount of each Instrument during each Interest Accrual Period from the Interest Commencement Date. Interest will cease to accrue as from the due date for redemption therefor (or, in the case of an Instalment Instrument, in respect of each instalment of principal, on the due date for payment of the relevant Instalment Amount) unless upon due presentation or surrender thereof (if required), payment in full of the Redemption Amount (as defined in Condition 6.9) or the relevant Instalment Amount is improperly withheld or refused or default is otherwise made in the payment thereof in which case interest shall continue to accrue on the principal amount in respect of which payment has been improperly withheld or refused or default has been made (as well after as before any demand or judgment) at the Interest Rate then applicable or such other rate as may be specified for this purpose in the Pricing Supplement until the date on which, upon due presentation or surrender of the relevant Instrument (if required), the relevant payment is made or, if earlier (except where presentation or surrender of the relevant Instrument is not required as a precondition of payment), the seventh day after the date on which, the Issue and Paying Agent, the Registrar or, as the case may be, the Transfer Agent having received the funds required to make such payment, notice is given to the Holders of the Instruments in accordance with Condition 15 that the Issue and Paying Agent, the Registrar or, as the case may be, the Transfer Agent has received the required funds (except to the extent that there is failure in the subsequent payment thereof to the relevant Holder).

Interest Amount(s), Calculation Agent and Reference Banks

- 5.7 If a Calculation Agent is specified in the Pricing Supplement, the Calculation Agent, as soon as practicable after the Relevant Time on each Interest Determination Date (or such other time on such date as the Calculation Agent may be required to calculate any Redemption Amount or Instalment Amount, obtain any quote or make any determination or calculation) will determine the Interest Rate and calculate the amount(s) of interest payable (the “**Interest Amount(s)**”) in respect of each Denomination of the Instruments (in the case of Bearer Instruments) and the minimum denomination (in the case of Registered Instruments) for the relevant Interest Accrual Period, calculate the Redemption Amount or Instalment Amount, obtain such quote or make such determination or calculation, as the case may be, and cause the Interest Rate and the Interest Amounts for each Interest Period and the relevant Interest Payment Date or, as the case may be, the Redemption Amount or any Instalment Amount, to be notified to the Issue and Paying Agent,

the Registrar or any Transfer Agent (in the case of Registered Instruments), the Issuer, the Holders in accordance with Condition 15 and, if the Instruments are listed on a stock exchange and the rules of such exchange so requires, such exchange as soon as possible after their determination or calculation, but in no event later than the fourth London Banking Day thereafter or, if earlier in the case of notification to the stock exchange, the time required by the rules of the relevant stock exchange which is, for the Luxembourg Stock Exchange, the first day of the relevant period. The Interest Amounts and the Interest Payment Date so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) without notice in the event of an extension or shortening of an Interest Accrual Period or the Interest Period. If the Instruments become due and payable under Condition 7, the Interest Rate and the accrued interest payable in respect of the Instruments shall nevertheless continue to be calculated as previously in accordance with this Condition but no publication of the Interest Rate or the Interest Amount so calculated need be made. The determination of each Interest Rate, Interest Amount, Redemption Amount and Instalment Amount, the obtaining of each quote and the making of each determination or calculation by the Calculation Agent shall (in the absence of manifest error) be final and binding upon the Issuer and the Holders and neither the Calculation Agent nor any Reference Bank shall have any liability to the Holders in respect of any determination, calculation, quote or rate made or provided by it.

The Issuer will procure that there shall at all times be such Reference Banks as may be required for the purpose of determining the Interest Rate applicable to the Instruments and a Calculation Agent, if provision is made for one in the Terms and Conditions.

If the Calculation Agent is incapable or unwilling to act as such or if the Calculation Agent fails duly to establish the Interest Rate for any Interest Accrual Period or to calculate the Interest Amounts or any other requirements, the Issuer will appoint the London office of a leading bank engaged in the London interbank market to act as such in its place. The Calculation Agent may not resign its duties without a successor having been appointed as aforesaid.

Calculations and Adjustments

- 5.8 The amount of interest payable in respect of any Instrument for any period shall be calculated by multiplying the product of the Interest Rate and the Outstanding Principal Amount by the Day Count Fraction, save that if the Pricing Supplement specifies a specific amount in respect of such period, the amount of interest payable in respect of such Instrument for such period will be equal to such specified amount. Where any Interest Period comprises two or more Interest Accrual Periods, the amount of interest payable in respect of such Interest Period will be the sum of the amounts of interest payable in respect of each of those Interest Accrual Periods.

For the purposes of any calculations referred to in these Terms and Conditions (unless otherwise specified in the Pricing Supplement), (a) all percentages resulting from such calculations will be rounded, if necessary, to the nearest one hundred-thousandth of a percentage point (with 0.000005 per cent, being rounded up to 0.00001 per cent.) and (b) all Relevant Currency amounts used in or resulting from such calculation, will be rounded to the nearest sub-unit of the Relevant Currency (half a sub-unit being rounded upwards). For this purpose, a “**sub-unit**” means, in the case of any currency other than Euro, the lowest amount of such currency that is available as legal tender in the currency of such country and, in the case of Euro, means one cent.

Definitions

- 5.9 “**Additional Business Centre(s)**” means the city or cities specified as such in the relevant Pricing Supplement;

“**Applicable Business Day Convention**” means the “**Business Day Convention**” which may be specified in the Pricing Supplement as applicable to any date in respect of the Instruments. Where the Pricing Supplement specifies “**No Adjustment**” in relation to any date, such date shall not be adjusted in accordance with any Business Day Convention. Where the Pricing Supplement fails either to specify an applicable Business Day Convention or “**No Adjustment**” for the purposes of an Interest Payment Date or an Interest Period End Date, then in the case of Instruments which bear interest at a fixed rate, “**No Adjustment**” shall be deemed to have been so specified and in the case of Instruments which bear interest at a floating rate, the Modified Following Business Day Convention shall be deemed to have been so specified. Different Business Day Conventions may

apply, or be specified in relation to, the Interest Payment Dates, Interest Period End Dates and any other date or dates in respect of any Instruments.

“Banking Day” means, in respect of any city, any day on which commercial banks are open for business (including dealings in foreign exchange and foreign currency deposits) in that city.

“Business Day” means:

- (i) in relation to any sum payable in euro, a Target Business Day and a day on which commercial banks and foreign exchange markets settle payments generally in each (if any) Additional Business Centre; and
- (ii) in relation to any sum payable in a currency other than euro, a day on which commercial banks and foreign exchange markets are open for business and settle payments in the Relevant Financial Centre in respect of the relevant Instruments and in each (if any) Additional Business Centre.

“Business Day Convention” means a convention for adjusting any date if it would otherwise fall on a day that is not a Business Day and the following Business Day Conventions, where specified in the Pricing Supplement in relation to any date applicable to any Instruments, shall have the following meanings:

- (i) **“Following Business Day Convention”** means that such date shall be postponed to the first following day that is a Business Day;
- (ii) **“Modified Following Business Day Convention”** or **“Modified Business Day Convention”** means that such date shall be postponed to the first following day that is a Business Day unless that day falls in the next calendar month in which case that date will be the first preceding day that is a Business Day;
- (iii) **“Preceding Business Day Convention”** means that such date shall be brought forward to the first preceding day that is a Business Day; and
- (iv) **“FRN Convention”** or **“Eurodollar Convention”** means that each such date shall be the date which numerically corresponds to the preceding such date in the calendar month which is the number of months specified in the Pricing Supplement after the calendar month in which the preceding such date occurred provided that:
 - (a) if there is no such numerically corresponding day in the calendar month in which any such date should occur, then such date will be the last day which is a Business Day in that calendar month;
 - (b) if any such date would otherwise fall on a day which is not a Business Day, then such date will be the first following day which is a Business Day unless that day falls in the next calendar month, in which case it will be the first preceding day which is a Business Day; and
 - (c) if the preceding such date occurred on the last day in a calendar month which was a Business Day, then all subsequent such dates will be the last day which is a Business Day in the calendar month which is the specified number of months after the calendar month in which the preceding such date occurred.

“Day Count Fraction” means, in respect of the calculation of an amount for any period of time (**“Calculation Period”**), such day count fraction as may be specified in the Pricing Supplement and:

- (i) If **“Actual/Actual (ISMA)”** is so specified, means:
 - (a) where the Calculation Period is equal to or shorter than the Regular Period during which it falls, the actual number of days in the Calculation Period divided by the product of (1) the actual number of days in such Regular Period and (2) the number of Regular Periods in any year; and
 - (b) where the Calculation Period is longer than one Regular Period, the sum of:
 - (A) the actual number of days in such Calculation Period falling in the Regular Period in which it begins divided by the product of (1) the actual number of days in such Regular Period and (2) the number of Regular Periods in any year; and

- (B) the actual number of days in such Calculation Period falling in the next Regular Period divided by the product of (1) the actual number of days in such Regular Period and (2) the number of Regular Periods in any year;
- (ii) if “**Actual/365**” or “**Actual/Actual (ISDA)**” is so specified, means the actual number of days in the Calculation Period divided by 365 (or, if any portion of the Calculation Period falls in a leap year, the sum of (A) the actual number of days in that portion of the Calculation Period falling in a leap year divided by 366 and (B) the actual number of days in that portion of the Calculation Period falling in a non-leap year divided by 365);
- (iii) if “**Actual/365 (Fixed)**” is so specified, means the actual number of days in the Calculation Period divided by 365;
- (iv) if “**Actual/360**” is so specified, means the actual number of days in the Calculation Period divided by 360;
- (v) if “**30/360**” is so specified, means the number of days in the Calculation Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months (unless (i) the last day of the Calculation Period is the 31st day of a month but the first day of the Calculation Period is a day other than the 30th or 31st day of a month, in which case the month that includes that last day shall not be considered to be shortened to a 30-day month, or (ii) the last day of the Calculation Period is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month)); and if “**30E/360**” or “**Eurobond Basis**” is so specified means, the number of days in the Calculation Period divided by 360 (the number of days to be calculated on the basis of a year of 360 days with 12 30-day months, without regard to the date of the first day or last day of the Calculation Period unless, in the case of the final Calculation Period, the date of final maturity is the last day of the month of February, in which case the month of February shall not be considered to be lengthened to a 30-day month).

“**Interest Accrual Period**” means, in respect of an Interest Period, each successive period beginning on and including an Interest Period End Date and ending on but excluding the next succeeding Interest Period End Date during that Interest Period provided always that the first Interest Accrual Period shall commence on and include the Interest Commencement Date and the final Interest Accrual Period shall end on but exclude the date of final maturity.

“**Interest Commencement Date**” means the date of issue of the Instruments (as specified in the Pricing Supplement) or such other date as may be specified as such in the Pricing Supplement.

“**Interest Determination Date**” means, in respect of any Interest Accrual Period, the date falling such number (if any) of Banking Days in such city(ies) as may be specified in the Pricing Supplement prior to the first day of such Interest Accrual Period, or if none is specified:

- (i) in the case of Instruments denominated in Pounds Sterling, the first day of such Interest Accrual Period; or
- (ii) in the case of Instruments denominated (or redenominated) in Euro, the date falling two Target Business Days prior to the first day of such Interest Accrual period, or
- (iii) in any other case, the date falling two London Banking Days prior to the first day of such Interest Accrual Period.

“**Interest Payment Date**” means the date or dates specified as such in, or determined in accordance with the provisions of, the Pricing Supplement and, if an Applicable Business Day Convention is specified in the Pricing Supplement, as the same may be adjusted in accordance with the Applicable Business Day Convention or if the Applicable Business Day Convention is the FRN Convention and an interval of a number of calendar months is specified in the Pricing Supplement as being the Interest Period, each of such dates as may occur in accordance with the FRN Convention at such specified period of calendar months following the date of issue of the Instruments (in the case of the first Interest Payment Date) or the previous Interest Payment Date (in any other case).

“**Interest Period**” means each successive period beginning on and including an Interest Payment Date and ending on but excluding the next succeeding Interest Payment Date provided always that the first Interest Period shall commence on and include the Interest Commencement Date and the final Interest Period shall end on but exclude the date of final maturity.

“Interest Period End Date” means the date or dates specified as such in, or determined in accordance with the provisions of, the Pricing Supplement and, if an Applicable Business Day Convention is specified in the Pricing Supplement, as the same may be adjusted in accordance with the Applicable Business Day Convention or, if the Applicable Business Day Convention is the FRN Convention and an interval of a number of calendar months is specified in the Pricing Supplement as the Interest Accrual Period, such dates as may occur in accordance with the FRN Convention at such specified period of calendar months following the Interest Commencement Date (in the case of the first Interest Period End Date) or the previous Interest Period End Date (in any other case) or, if none of the foregoing is specified in the Pricing Supplement, means the date or each of the dates which correspond with the Interest Payment Date(s) in respect of the Instruments.

“Interest Rate” means the rate or rates (expressed as a percentage per annum) or amount or amounts (expressed as a price per unit of Specified Currency) of interest payable in respect of the Instruments specified in, or calculated or determined in accordance with the provisions of, the Pricing Supplement.

“ISDA Definitions” means the 2000 ISDA Definitions as amended and updated as at the date of issue of the first Tranche of the Instruments of the relevant Series (as specified in the Pricing Supplement) as published by the International Swaps and Derivatives Association, Inc.

“Outstanding Principal Amount” means, in respect of an Instrument, its principal amount less in respect of any Instalment Instrument, any principal amount on which interest shall have ceased to accrue in accordance with Condition 5.6 or, in the case of a Partly Paid Instrument, the Paid Up Amount of such Instrument or otherwise as indicated in the Pricing Supplement except that the Paid Up Amount shall be deemed to be nil for Instruments which have been forfeited by the Issuer on or after the Forfeiture Date as provided for in Condition 1.7.

“Participating Member State” means a member state of the European Communities which adopts the euro as its lawful currency in accordance with the Treaty.

“Principal Financial Centre” means, in relation to any currency, the principal financial centre for that currency provided, however, that:

- (i) in relation to euro, it means the principal financial centre of such Member State of the European Community as is selected (in the case of a payment) by the payee or (in the case of a calculation) by the Calculation Agent; and
- (ii) in relation to Australian dollars, it means both Sydney and Melbourne and, in relation to New Zealand dollars, it means both Wellington and Auckland; in each case as is selected (in the case of a payment) by the payee or (in the case of a calculation) by the Calculation Agent.

“Reference Banks” has the meaning given in the relevant Pricing Supplement or, if none, four (or if the Principal Financial Centre is Helsinki, five) major banks selected by the Calculation Agent in the market that is most closely connected with the Reference Rate.

“Reference Rate” has the meaning given to it in the relevant Pricing Supplement.

“Relevant Financial Centre” has the meaning given to it in the relevant Pricing Supplement.

“Relevant Screen Page” means the page, section or other part of a particular information service (including, without limitation, the Reuter Money 3000 Service and the Moneyline Telerate Service) specified as the Relevant Screen Page in the relevant Pricing Supplement, or such other page, section or other part as may replace it on that information service or such other information service, in each case, as may be nominated by the person providing or sponsoring the information appearing there for the purpose of displaying rates or prices comparable to the Reference Rate.

“Relevant Time” means the time as of which any rate is to be determined as specified in the Pricing Supplement or, if none is specified, at which it is customary to determine such rate.

“Specified Currency” has the meaning given in the relevant Pricing Supplement.

“Target Business Day” means a day on which the Target System is open.

“Target System” means the Trans-European Automated Real-Time Gross Settlement Express Transfer (Target) System.

“Treaty” means the Treaty establishing the European Community, as amended by the Treaty on European Union.

Non-Interest Bearing Instruments

- 5.10 If any Redemption Amount (as defined in Condition 6.9) or Instalment Amount in respect of any Instrument which is non-interest bearing is not paid when due, interest shall accrue on the overdue amount at a rate per annum (expressed as a percentage per annum) equal to the Amortisation Yield defined in, or determined in accordance with the provisions of, the Pricing Supplement or at such other rate as may be specified for this purpose in the Pricing Supplement until the date on which, upon due presentation or surrender of the relevant Instrument (if required), the relevant payment is made or, if earlier (except where presentation or surrender of the relevant Instrument is not required as a precondition of payment), the seventh day after the date on which, the Issue and Paying Agent or, as the case may be, the Registrar having received the funds required to make such payment, notice is given to the Holders of the Instruments in accordance with Condition 15 that the Issue and Paying Agent or, as the case may be, the Registrar has received the required funds (except to the extent that there is failure in the subsequent payment thereof to the relevant Holder). The amount of any such interest shall be calculated in accordance with the provisions of Condition 5.8 as if the Interest Rate was the Amortisation Yield, the Outstanding Principal Amount was the overdue sum and the Day Count Fraction was as specified for this purpose in the Pricing Supplement or, if not so specified, 30E/360 (as defined in Condition 5.9).

6. Redemption and Purchase

Redemption at Maturity

- 6.1 Unless previously redeemed, or purchased and cancelled or unless such Instrument is stated in the Pricing Supplement as having no fixed maturity date, each Instrument shall be redeemed at its maturity redemption amount (the “**Maturity Redemption Amount**”) (which shall be its Outstanding Principal Amount or such other redemption amount as may be specified in or determined in accordance with the Pricing Supplement) (or, in the case of Instalment Instruments, in such number of instalments and in such amounts (“**Instalment Amounts**”) as may be specified in, or determined in accordance with the provisions of, the Pricing Supplement) on the date or dates (or, in the case of Instruments which bear interest at a floating rate of interest, on the date or dates upon which interest is payable) specified in the Pricing Supplement.

Optional Early Redemption (Call)

- 6.2 If this Condition 6.2 is specified in the Pricing Supplement as being applicable, then the Issuer may, having given the appropriate notice and subject to such conditions as may be specified in the Pricing Supplement, redeem all (but not, unless and to the extent that the Pricing Supplement specifies otherwise, some only) of the Instruments of the relevant Series at their call early redemption amount (the “**Early Redemption Amount (Call)**”) (which shall be their Outstanding Principal Amount or, in the case of Instruments which are non-interest bearing, their Amortised Face Amount (as defined in Condition 6.10) or such other redemption amount as may be specified in, or determined in accordance with the provisions of, the Pricing Supplement), together with accrued interest (if any) thereon on the date specified in such notice. In the event any Instruments of the relevant Series are redeemed pursuant to Condition 6.2 (so long as such Instruments are listed on the Luxembourg Stock Exchange) the Issuer shall inform the Luxembourg Stock Exchange of such early redemption.

The Issuer may not exercise such option in respect of any Instrument which is the subject of the prior exercise by the Holder thereof of its option to require the redemption of such Instrument under Condition 6.5.

- 6.3 The appropriate notice referred to in Condition 6.2 is a notice given by the Issuer to the Holders of the Instruments of the relevant Series in accordance with Condition 15, which notice shall be irrevocable and shall specify:
- the Series of Instruments subject to redemption;
 - whether such Series is to be redeemed in whole or in part only and, if in part only, the aggregate principal amount of and (except in the case of a Temporary Global Instrument or Permanent Global Instrument) the serial numbers of the Instruments of the relevant Series which are to be redeemed;
 - the due date for such redemption, which shall be not less than thirty days nor more than sixty days after the date on which such notice is given and which shall be such date or the next of

such dates (“**Call Option Date(s)**”) or a day falling within such period (“**Call Option Period**”), as may be specified in the Pricing Supplement and which is, in the case of Instruments which bear interest at a floating rate, a date upon which interest is payable; and

- the Early Redemption Amount (Call) at which such Instruments are to be redeemed.

Partial Redemption

6.4 If the Instruments of a Series are to be redeemed in part only on any date in accordance with Condition 6.2:

- in the case of Bearer Instruments, the Instruments to be redeemed shall be drawn by lot in such European city as the Issue and Paying Agent may specify, or identified in such other manner or in such other place as the Issue and Paying Agent may approve and deem appropriate and fair; and
- in the case of Registered Instruments, the Instruments shall be redeemed (so far as may be practicable) pro rata to their principal amounts, provided always that the amount redeemed in respect of each Instrument shall be equal to the minimum denomination thereof or an integral multiple thereof,

subject always to compliance with all applicable laws and the requirements of any stock exchange on which the relevant Instruments may be listed.

In the case of the redemption of part only of a Registered Instrument, a new Registered Instrument in respect of the unredeemed balance shall be issued in accordance with Conditions 2.4 to 2.9 which shall apply as in the case of a transfer of Registered Instruments as if such new Registered Instrument were in respect of the untransferred balance.

Optional Early Redemption (Put)

6.5 If this Condition 6.5 is specified in the Pricing Supplement as being applicable, then the Issuer shall, upon the exercise of the relevant option by the Holder of any Instrument of the relevant Series, redeem such Instrument on the date specified in the relevant Put Notice (as defined below) at its put early redemption amount (the “**Early Redemption Amount (Put)**”) (which shall be its Outstanding Principal Amount or, if such Instrument is non-interest bearing, its Amortised Face Amount (as defined in Condition 6.10) or such other redemption amount as may be specified in, or determined in accordance with the provisions of, the Pricing Supplement), together with accrued interest (if any) thereon. In order to exercise such option, the Holder must, not less than forty-five days before the date on which such redemption is required to be made as specified in the Put Notice (which date shall be such date or the next of the dates (“**Put Date(s)**”) or a day falling within such period (“**Put Period**”) as may be specified in the Pricing Supplement), deposit the relevant Instrument (together, in the case of an interest-bearing Instrument in bearer form, with all unmatured Coupons appertaining thereto other than any Coupon maturing on or before the date of redemption (failing which the provisions of Condition 9A.6 apply)) during normal business hours at the specified office of, in the case of a Bearer Instrument, any Paying Agent or, in the case of a Registered Instrument, the Registrar or any Transfer Agent together with a duly completed early redemption notice (“**Put Notice**”) in the form which is available from the specified office of any of the Paying Agents, the Registrar or, as the case may be any Transfer Agent, specifying, in the case of a Registered Instrument, the aggregate principal amount in respect of which such option is exercised (which must be the minimum denomination specified in the Pricing Supplement or an integral multiple thereof). No Instrument so deposited and option exercised may be withdrawn (except as provided in the Issue and Paying Agency Agreement). In the event any Instruments of the relevant Series are redeemed pursuant to Condition 6.5 (so long as such Instruments are listed on the Luxembourg Stock Exchange) the Issuer shall inform the Luxembourg Stock Exchange of such early redemption.

In the case of the redemption of part only of a Registered Instrument, a new Registered Instrument in respect of the unredeemed balance shall be issued in accordance with Conditions 2.4 to 2.9 which shall apply as in the case of a transfer of Registered Instruments as if such new Registered Instrument were in respect of the untransferred balance.

The holder of an Instrument may not exercise such option in respect of any Instrument which is the subject of an exercise by the Issuer of its option to redeem such Instrument under Condition 6.2.

Purchase of Instruments

- 6.6 The Issuer may at any time purchase Instruments in the open market or otherwise and at any price provided that all unmatured Receipts and Coupons appertaining thereto are purchased therewith. If purchases are made by tender, tenders must be available to all Holders of Instruments alike.

Cancellation of Redeemed and Purchased Instruments

- 6.7 All unmatured Instruments and Coupons and unexchanged Talons redeemed or purchased will be cancelled forthwith and may not be reissued or resold.

Further Provisions applicable to Redemption Amount and Instalment Amounts

- 6.8 The provisions of Condition 5.7 and the last paragraph of Condition 5.8 shall apply to any determination or calculation of the Redemption Amount or any Instalment Amount required by the Pricing Supplement to be made by the Calculation Agent (as defined in Condition 5.9).
- 6.9 References herein to “**Redemption Amount**” shall mean, as appropriate, the Maturity Redemption Amount, the final Instalment Amount, Early Redemption Amount (Call), Early Redemption Amount (Put) and Early Termination Amount or such other amount in the nature of a redemption amount as may be specified in, or determined in accordance with the provisions of, the Pricing Supplement.
- 6.10 In the case of any Instrument which is non-interest bearing, the “**Amortised Face Amount**” shall be an amount equal to the sum of:
- (i) the Issue Price specified in the Pricing Supplement; and
 - (ii) the product of the Amortisation Yield (compounded annually) being applied to the Issue Price from (and including) the Issue Date specified in the Pricing Supplement to (but excluding) the date fixed for redemption or (as the case may be) the date upon which such Instrument becomes due and repayable.

Where such calculation is to be made for a period which is not a whole number of years, the calculation in respect of the period of less than a full year shall be made on the basis of the Day Count Fraction (as defined in Condition 5.9) specified in the Pricing Supplement for the purposes of this Condition 6.10.

- 6.11 In the case of any Instrument which is non-interest bearing, if any Redemption Amount (other than the Maturity Redemption Amount) is improperly withheld or refused or default is otherwise made in the payment thereof, the Amortised Face Amount shall be calculated as provided in Condition 6.10 but as if references in subparagraph (ii) to the date fixed for redemption or the date upon which such Instrument becomes due and repayable were replaced by references to the earlier of:
- (i) the date on which, upon due presentation or surrender of the relevant Instrument (if required), the relevant payment is made; and
 - (ii) (except where presentation or surrender of the relevant Instrument is not required as a precondition of payment), the seventh day after the date on which, the Issue and Paying Agent or, as the case may be, the Registrar having received the funds required to make such payment, notice is given to the Holders of the Instruments in accordance with Condition 15 of that circumstance (except to the extent that there is a failure in the subsequent payment thereof to the relevant Holder).

7. Events of Default

- 7.1 The following events or circumstances (each an “**Event of Default**”) shall be acceleration events in relation to the Instruments of any Series, namely:
- (i) *Non-payment*: the Issuer fails to pay any amount of interest in respect of the Instruments of the relevant Series or any of them within 30 days of the due date for payment thereof; or
 - (ii) *Breach of other obligations*: the Issuer defaults in the performance or observance of any of its other material obligations under or in respect of the Instruments of the relevant Series and such default remains unremedied for 45 days after written notice requiring such default to be remedied has been delivered to the Issuer at the specified office of the Issue and Paying Agent by the Holder of any such Instrument.

- 7.2 If any Event of Default shall occur in relation to any Series of Instruments, all of the Instruments may, by written notice addressed and delivered by the Holders of at least 25 per cent. of the aggregate principal amount of the outstanding Instruments to the Issue and Paying Agent, be declared immediately due and payable whereupon, unless the Issuer shall have cured or otherwise rectified the Relevant Event they shall become immediately due and payable at the early termination amount of each Instrument (the “**Early Termination Amount**”) (which shall be its Outstanding Principal Amount or, if such Instrument is non-interest bearing, its Amortised Face Amount (as defined in Condition 6.10) or such other redemption amount as may be specified in, or determined in accordance with the provisions of, the Pricing Supplement), together with accrued interest without further action or formality. Notice of any such declaration shall promptly be given to all other Holders.
- 7.3 If the Issue and Paying Agent receives notice in writing from Holders of at least 50 per cent. in aggregate principal amount of the outstanding Instruments and/or a resolution is passed at a meeting of Holders duly convened and held in accordance with the Issue and Paying Agency Agreement to the effect that the Event(s) of Default giving rise to such declaration is or are cured or is or are waived by them following any such declaration and that such Holders request the Issue and Paying Agent to rescind the relevant declaration, the Issue and Paying Agent shall, by notice in writing to the Issuer and the Holders, rescind the relevant declaration whereupon it shall be rescinded and shall have no further effect. No such rescission shall affect any other or any subsequent Event of Default or any right of any Holder in relation thereto.

8. Taxation

- 8.1 All amounts payable (whether in respect of principal, interest or otherwise) in respect of the Instruments will be made free and clear of and without withholding or deduction for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the Czech Republic or any political subdivision thereof or any authority or agency therein or thereof having power to tax, unless the withholding or deduction of such taxes, duties, assessments or governmental charges (“**Taxes**”) is required by law. In that event, the Issuer will pay such additional amounts as may be necessary in order that the net amounts receivable by the Holder after such withholding or deduction shall equal the respective amounts which would have been receivable by such Holder in the absence of such withholding or deduction; except that no such additional amounts shall be payable in relation to any payment in respect of any Instrument or Coupon:
- (i) presented for payment by a Holder which is liable to such Taxes in respect of such Instrument or Coupon by reason of the Holder having some connection with the Czech Republic other than the mere holding of such Instrument or Coupon; or
 - (ii) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to any European Union Directive on the taxation of savings implementing the conclusions of the EU Council of Finance Ministers (the “**ECOFIN Council**”) meeting of 26-27 November 2000 or any law implementing or complying with, or introduced in order to conform to, such Directive; or
 - (iii) by or on behalf of a Holder who would have been able to avoid such withholding or deduction by presenting the relevant Instrument or Coupon to another Paying Agent in a Member State of the EU; or
 - (iv) more than 30 days after the Relevant Date except to the extent that the relevant Holder would have been entitled to such additional amounts if it had presented such Instrument or Coupon on the last day of such period of 30 days.
- 8.2 For the purposes of these Terms and Conditions, the “**Relevant Date**” means, in respect of any payment, the date on which such payment first becomes due and payable, but if the full amount of the moneys payable has not been received by the Issue **and** Paying Agent, or as the case may be, the Registrar on or prior to such due date, it means the first date on which, the full amount of such moneys having been so received and being available for payment to Holders, notice to that effect shall have been duly given to the Holders of the Instruments of the relevant Series in accordance with Condition 15.
- 8.3 Any reference in these Terms and Conditions to “**principal**” and/or “**interest**” in respect of the Instruments shall be deemed also to refer to any additional amounts which may be payable under

this Condition 8. Unless the context otherwise requires, any reference in these Terms and Conditions to “**principal**” shall include any premium payable in respect of an Instrument, any Instalment Amount or Redemption Amount and any other amounts in the nature of principal payable pursuant to these Terms and Conditions and “**interest**” shall include all amounts payable pursuant to Condition 5 and any other amounts in the nature of interest payable pursuant to these Terms and Conditions.

9. Payments

9A Payments – Bearer Instruments

9A.1 This Condition 9A is applicable in relation to Bearer Instruments.

9A.2 Payment of amounts (other than interest) due in respect of Bearer Instruments will be made against presentation and (save in the case of partial payment or payment of an Instalment Amount (other than the final Instalment Amount)) surrender of the relevant Bearer Instruments at the specified office of any of the Paying Agents.

Payment of Instalment Amounts (other than the final Instalment Amount) in respect of an Instalment Instrument which is a Definitive Instrument with Receipts will be made against presentation of the Instrument together with (where applicable) the relevant Receipt and surrender of such Receipt at the specified office of any of the Paying Agents.

The Receipts are not and shall not in any circumstances be deemed to be documents of title and if separated from the Instrument to which they relate will not represent any obligation of the Issuer. Accordingly, the presentation of an Instrument without the relative Receipt or the presentation of a Receipt without the Instrument to which it appertains shall not entitle the Holder to any payment in respect of the relevant Instalment Amount.

9A.3 Payment of amounts in respect of interest on Bearer Instruments will be made:

- (i) in the case of Instruments without Coupons attached thereto at the time of their initial delivery, against presentation of the relevant Instruments at the specified office of any of the Paying Agents outside (unless Condition 9A.4 applies) the United States; and
- (ii) in the case of Instruments delivered with Coupons attached thereto at the time of their initial delivery, against surrender of the relevant Coupons or, in the case of interest due otherwise than on a scheduled date for the payment of interest, against presentation of the relevant Instruments, in either case at the specified office of any of the Paying Agents outside (unless Condition 9A.4 applies) the United States.

9A.4 Payments of amounts due in respect of interest on the Instruments and exchanges of Talons for Coupon sheets in accordance with Condition 9A.7 will not be made at the specified office of any Paying Agent in the United States (as defined in the United States Internal Revenue Code and Regulations thereunder) unless (a) payment in full of amounts due in respect of interest on such Instruments when due or, as the case may be, the exchange of Talons at all the specified offices of the Paying Agents outside the United States is illegal or effectively precluded by exchange controls or other similar restrictions and (b) such payment or exchange is permitted by applicable United States law. If paragraphs (a) and (b) of the previous sentence apply, the Issuer shall forthwith appoint a further Paying Agent with a specified office in New York City.

9A.5 If the due date for payment of any amount due in respect of any Instrument is not a Relevant Financial Centre Day and a Local Banking Day (each as defined in Condition 9C.3), then the Holder thereof will not be entitled to payment thereof until the next day which is such a day, (or as otherwise specified in the Pricing Supplement) and from such day and thereafter will be entitled to receive payment by cheque on any Local Banking Day, and will be entitled to payment by transfer to a designated account on any day which is a Local Banking Day, a Relevant Financial Centre Day and a day on which commercial banks and foreign exchange markets settle payments in the relevant currency in the place where the relevant designated account is located and no further payment on account of interest or otherwise shall be due in respect of such delay or adjustment unless there is a subsequent failure to pay in accordance with these Terms and Conditions in which event interest shall continue to accrue as provided in Condition 5.6 or, if appropriate, Condition 5.10.

9A.6 Each Instrument initially delivered with Coupons, Talons or Receipts attached thereto should be presented and, save in the case of partial payment of the Redemption Amount, surrendered for final

redemption together with all unmatured Receipts, Coupons and Talons relating thereto, failing which:

- (i) if the Pricing Supplement specifies that this paragraph (i) of Condition 9A.6 is applicable (and, in the absence of specification, this paragraph (i) shall apply to Instruments which bear interest at a fixed rate or rates or in fixed amounts) and subject as hereinafter provided, the amount of any missing unmatured Coupons (or, in the case of a payment not being made in full, that portion of the amount of such missing Coupon which the Redemption Amount paid bears to the total Redemption Amount due) (excluding, for this purpose, but without prejudice to paragraph (iii) below, Talons) will be deducted from the amount otherwise payable on such final redemption, the amount so deducted being payable against surrender of the relevant Coupon at the specified office of any of the Paying Agents at any time within ten years of the Relevant Date applicable to payment of such Redemption Amount;
- (ii) if the Pricing Supplement specifies that this paragraph (ii) of Condition 9A.6 is applicable (and, in the absence of specification, this paragraph (ii) shall apply to Instruments which bear interest at a floating rate or rates or in variable amounts) all unmatured Coupons (excluding, for this purpose, but without prejudice to paragraph (iii) below, Talons) relating to such Instruments (whether or not surrendered therewith) shall become void and no payment shall be made thereafter in respect of them;
- (iii) in the case of Instruments initially delivered with Talons attached thereto, all unmatured Talons (whether or not surrendered therewith) shall become void and no exchange for Coupons shall be made thereafter in respect of them; and
- (iv) in the case of Instruments initially delivered with Receipts attached thereto, all Receipts relating to such Instruments in respect of a payment of an Instalment Amount which (but for such redemption) would have fallen due on a date after such due date for redemption (whether or not surrendered therewith) shall become void and no payment shall be made thereafter in respect of them.

The provisions of paragraph (i) of this Condition 9A.6 notwithstanding, if any Instruments should be issued with a maturity date and an Interest Rate or Rates such that, on the presentation for payment of any such Instrument without any unmatured Coupons attached thereto or surrendered therewith, the amount required by paragraph (i) to be deducted would be greater than the Redemption Amount otherwise due for payment, then, upon the due date for redemption of any such Instrument, such unmatured Coupons (whether or not attached) shall become void (and no payment shall be made in respect thereof) as shall be required so that, upon application of the provisions of paragraph (i) in respect of such Coupons as have not so become void, the amount required by paragraph (i) to be deducted would not be greater than the Redemption Amount otherwise due for payment. Where the application of the foregoing sentence requires some but not all of the unmatured Coupons relating to an Instrument to become void, the relevant Paying Agent shall determine which unmatured Coupons are to become void, and shall select for such purpose Coupons maturing on later dates in preference to Coupons maturing on earlier dates.

9A.7 In relation to Instruments initially delivered with Talons attached thereto, on or after the due date for the payment of interest on which the final Coupon comprised in any Coupon sheet matures, the Talon comprised in the Coupon sheet may be surrendered at the specified office of any Paying Agent outside (unless Condition 9A.4 applies) the United States in exchange for a further Coupon sheet (including any appropriate further Talon), subject to the provisions of Condition 11 below. Each Talon shall, for the purpose of these Conditions, be deemed to mature on the Interest Payment Date on which the final Coupon comprised in the relative Coupon sheet matures.

9B Payments – Registered Instruments

9B.1 This Condition 9B is applicable in relation to Registered Instruments.

9B.2 Payment of the Redemption Amount (together with accrued interest) due in respect of Registered Instruments will be made against presentation and, save in the case of partial payment of the Redemption Amount, surrender of the relevant Registered Instruments at the specified office of the Registrar or any Transfer Agent. If the due date for payment of the Redemption Amount of any Registered Instrument is not a Relevant Financial Centre Day (as defined in Condition 9C.3), then the Holder thereof will not be entitled to payment thereof until the next day which is such a day, and from such day and thereafter will be entitled to receive payment by cheque on any Local

Banking Day, and, will be entitled to payment by transfer to a designated account on any day which is a Local Banking Day, a Relevant Financial Centre Day and a day on which commercial banks and foreign exchange markets settle payments in the relevant currency in the place where the relevant designated account is located and no further payment on account of interest or otherwise shall be due in respect of such postponed payment unless there is a subsequent failure to pay in accordance with these Terms and Conditions in which event interest shall continue to accrue as provided in Condition 5.6 or, as appropriate, Condition 5.10.

- 9B.3 Payment of amounts (whether principal, interest or otherwise) due (other than the Redemption Amount) in respect of Registered Instruments will be paid to the Holder thereof (or, in the case of joint Holders, the first-named) as appearing in the register kept by the Registrar as at opening of business (local time in the place of the specified office of the Registrar) on the fifteenth Relevant Banking Day (as defined in Condition 2.6) before the due date for such payment (the “**Record Date**”).
- 9B.4 Notwithstanding the provisions of Condition 9C.2, payment of amounts (whether principal, interest or otherwise) due (other than the Redemption Amount) in respect of Registered Instruments will be made in the currency in which such amount is due by cheque (in the case of payment in Japanese Yen to a non-resident of Japan, drawn on an authorised foreign exchange bank and posted to the address (as recorded in the register held by the Registrar) of the Holder thereof (or, in the case of joint Holders, the first-named) on the Relevant Banking Day (as defined in Condition 2.6) not later than the relevant due date for payment unless prior to the relevant Record Date the Holder thereof (or, in the case of joint Holders, the first-named) has applied to the Registrar and the Registrar has acknowledged such application for payment to be made to a designated account denominated in the relevant currency (in the case of payment in Japanese Yen to a non-resident of Japan, a non-resident account with an authorised foreign exchange bank) in which case payment shall be made on the relevant due date for payment by transfer to such account. In the case of payment by transfer to an account, if the due date for any such payment is not a Relevant Financial Centre Day, then the Holder thereof will not be entitled to payment thereof until the first day thereafter which is a Relevant Financial Centre Day and a day on which commercial banks and foreign exchange markets settle payments in the relevant currency in the place where the relevant designated account is located and no further payment on account of interest or otherwise shall be due in respect of such postponed payment unless there is a subsequent failure to pay in accordance with these Terms and Conditions in which event interest shall continue to accrue as provided in Condition 5.6 or, as appropriate, Condition 5.10.

9C Payments – General Provisions

- 9C.1 Save as otherwise specified in these Terms and Conditions, this Condition 9C is applicable in relation to both Bearer and Registered Instruments.
- 9C.2 Payments of amounts due (whether principal, interest or otherwise) in respect of Instruments will be made in the currency in which such amount is due (a) by cheque (in the case of payment in Japanese Yen to a non-resident of Japan, drawn on an authorised foreign exchange bank or (b) at the option of the payee, by transfer to an account denominated in the relevant currency or to an account to which payments can otherwise be legally made specified by the payee (in the case of payment in Japanese Yen to a non-resident of Japan, a non-resident account with an authorised foreign exchange bank specified by the payee). All payments in respect of the Instruments are subject in all cases to any applicable fiscal or other laws and regulations in the place of payment, but without prejudice to the provisions of Condition 8. No commissions or expenses shall be charged to a Holder in respect of such payment.
- 9C.3 For the purposes of these Terms and Conditions:
- (i) “**Relevant Financial Centre Day**” means, in the case of any currency other than Euro, a day on which commercial banks and foreign exchange markets settle payments in the Relevant Financial Centre and in any other Relevant Financial Centre specified in the Pricing Supplement or in the case of payment in Euro, a day which is a Target Business Day (as defined in Condition 5.9); and
 - (ii) “**Local Banking Day**” means a day (other than a Saturday or Sunday) on which commercial banks are open for business (including dealings in foreign exchange and foreign currency

deposits) in the place of presentation of the relevant Instrument or, as the case may be, Coupon.

10. Prescription

- 10.1 Claims against the Issuer for payment of principal and interest in respect of Instruments will be prescribed and become void unless made, in the case of principal, within ten years or, in the case of interest, five years after the Relevant Date (as defined in Condition 8.2) for payment thereof.
- 10.2 In relation to Definitive Instruments initially delivered with Talons attached thereto, there shall not be included in any Coupon sheet issued upon exchange of a Talon any Coupon which would be void upon issue pursuant to Condition 9A.6 or the due date for the payment of which would fall after the due date for the redemption of the relevant Instrument or which would be void pursuant to this Condition 10 or any Talon the maturity date of which would fall after the due date for redemption of the relevant Instrument.

11. The Paying Agents, the Registrar, the Transfer Agents and the Calculation Agent

- 11.1 The initial Paying Agents, Registrar and Transfer Agents and their respective initial specified offices are specified below. The Calculation Agent in respect of any Instruments shall be specified in the Pricing Supplement. The Issuer reserves the right at any time to vary or terminate the appointment of any Paying Agent (including the Issue and Paying Agent), the Registrar, any Transfer Agent or the Calculation Agent and to appoint additional or other Paying Agents, another Registrar, additional or other Transfer Agents or another Calculation Agent, provided that it will at all times maintain (i) an Issue and Paying Agent, (ii) in the case of Registered Instruments, a Registrar, (iii) a Paying Agent (or in the case of registered Instruments, a Transfer Agent) with a specified office in a continental European city, (iv) so long as the Instruments are listed on the Luxembourg Stock Exchange and/or any other stock exchange, a Paying Agent and a Registrar or Transfer Agent each with a specified office in Luxembourg and/or in such other place as may be required by the rules of such other stock exchange, (v) in the circumstances described in Condition 9A.4, a Paying Agent with a specified office in New York City, (vi) a Calculation Agent where required by the Terms and Conditions applicable to any Instruments (in the case of (i), (ii), (iii) and (vi) with a specified office located in such place (if any) as may be required by the Terms and Conditions) and (vii) if European Council Directive 2003/48/EC or any other Directive implementing the conclusions of the ECOFIN Council meeting of 26-27 November 2000 is brought into force, the Issuer will ensure that it maintains a Paying Agent in an European Union member state that will not be obliged to withhold or deduct tax pursuant to such Directive or any law implementing, or complying with, or introduced to conform to, such Directive (if any). The Paying Agents, the Registrar, the Transfer Agent and the Calculation Agent reserve the right at any time to change their respective specified offices to some other specified office in the same city. Notice of all changes in the identities or specified offices of any Paying Agent, the Registrar, any Transfer Agent or the Calculation Agent will be given promptly by the Issuer to the Holders in accordance with Condition 14.
- 11.2 The Paying Agents, the Registrar, the Transfer Agents and the Calculation Agent act solely as agents of the Issuer and, save as provided in the Issue and Paying Agency Agreement or any other agreement entered into with respect to its appointment, do not assume any obligations towards or relationship of agency or trust for any Holder of any Instrument, Receipt or Coupon and each of them shall only be responsible for the performance of the duties and obligations expressly imposed upon it in the Issue and Paying Agency Agreement or other agreement entered into with respect to its appointment or incidental thereto.

12. Replacement of Instruments

If any Instrument, Receipt or Coupon is lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Issue and Paying Agent or such Paying Agent or Paying Agents as may be specified for such purpose in the Pricing Supplement (in the case of Bearer Instruments and Coupons) or of the Registrar or any Transfer Agent (in the case of Registered Instruments) (“**Replacement Agent**”), subject to all applicable laws and the requirements of any stock exchange on which the Instruments are listed, upon payment by the claimant of all expenses incurred in connection with such replacement and upon such terms as to evidence, security, indemnity and otherwise as the Issuer and the Replacement Agent may require. Mutilated or defaced Instruments, Receipts and Coupons must be surrendered before replacements will be delivered therefor.

13. Meetings of Holders; Appointment of Representative Committee and Modification

- 13.1 The Issue and Paying Agency Agreement contains provisions (which shall have effect as if incorporated herein) for convening meetings of the Holders of Instruments of any Series to consider any matter affecting their interest, including (without limitation) the modification by Extraordinary Resolution (as defined in the Issue and Paying Agency Agreement) of these Terms and Conditions and the Deed of Covenant insofar as the same may apply to such Instruments. An Extraordinary Resolution passed at any meeting of the Holders of Instruments of any Series will be binding on all Holders of the Instruments of such Series, whether or not they are present at the meeting, and on all Holders of Coupons relating to Instruments of such Series.
- 13.2 The Holders may, by a resolution passed at a meeting of Holders duly convened and held in accordance with the Issue and Paying Agency Agreement by a majority of at least 50 per cent. in aggregate principle amount of any Series of Instruments then outstanding, or by notice in writing to the Issuer (with a copy to the Issue and Paying Agent) signed by or on behalf of the Holders of at least 50 per cent. in aggregate principal amount of any Series of Instruments then outstanding, appoint any person or persons as a committee to represent the interests of the Holders if any of the following events has occurred and has not been remedied or otherwise rectified:
- (i) an Event of Default;
 - (ii) any event or circumstance which could, with the giving of notice, lapse of time, the issuing of a certificate and/or fulfilment of any other requirement provided for in Condition 7 become an Event of Default; or
 - (iii) any official public announcement by the Issuer to the effect that the Issuer is seeking, or intends to seek a restructuring of any Series of Instruments (whether by amendment, exchange offer or otherwise),

provided, however, that no such appointment shall be effective if the Holders of more than 25 per cent. of the principal amount of the outstanding Instruments of such Series have either (a) objected to such appointment by notification in writing to the Issuer (with a copy to the Issue and Paying Agent) during a specified period following notice of the appointment being given (if such notice of appointment is made by notice in writing to the Issuer) where such specified period shall be either 30 days or such other period as the committee may, acting in good faith, determine be appropriate in the circumstances, or (b) voted against such resolution at a meeting of Holders duly convened and held in accordance with the provisions of the Issue and Paying Agency Agreement.

Such committee shall, if appointed by notice in writing to the Issuer, give notice of its appointment to all Holders of the relevant Series of Instruments in accordance with Condition 14 as soon as practical after notice is given to the Issuer. Such committee, in its discretion, may, among other things (i) engage legal advisers and financial advisers to assist it in representing the interests of the Holders, (ii) adopt such rules as it considers appropriate regarding its proceedings and (iii) enter into discussions with the Issuer and/or other creditors of the Issuer. The Issuer shall pay any reasonably incurred fees and expenses of any such committee (including, without limitation, the fees and expenses of the committee's legal advisers and financial advisers, if any) within 30 days of the delivery to the Issuer of a reasonably detailed invoice and supporting documentation.

- 13.3 The Issuer may, with the consent of the Issue and Paying Agent, but without the consent of the Holders of the Instruments of any Series or Coupons, amend these Terms and Conditions and the Deed of Covenant insofar as they may apply to such Instruments to correct a manifest error. Subject as aforesaid, no other modification may be made to these Terms and Conditions or the Deed of Covenant except with the sanction of an Extraordinary Resolution.

14. Notices

To Holders of Bearer Instruments

- 14.1 Notices to Holders of Bearer Instruments will, save where another means of effective communication has been specified herein or in the Pricing Supplement, be deemed to be validly given if (i) published in a leading daily newspaper having general circulation in London (which is expected to be the *Financial Times*) and (ii) in the case of any Instruments which are listed on the Luxembourg Stock Exchange (so long as such Instruments are listed on the Luxembourg Stock Exchange and the rules of that exchange so require), in a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*) or (in the case of (i) or

(ii)), if such publication is not practicable, if published in a leading English language daily newspaper having general circulation in Europe. The Issuer shall also ensure that notices are duly published in compliance with the requirements of each stock exchange on which the Instruments are listed. Any notice so given will be deemed to have been validly given on the date of first such publication (or, if required to be published in more than one newspaper, on the first date on which publication shall have been made in all the required newspapers). Holders of Coupons will be deemed for all purposes to have notice of the contents of any notice given to Holders of Bearer Instruments in accordance with this Condition.

To Holders of Registered Instruments

14.2 Notices to Holders of Registered Instruments will be deemed to be validly given if sent by first class mail (or equivalent) or (if posted to an overseas address) by air mail to them (or, in the case of joint Holders, to the first-named in the register kept by the Registrar) at their respective addresses as recorded in the register kept by the Registrar, and will be deemed to have been validly given on the fourth weekday after the date of such mailing or, if posted from another country, on the fifth such day. With respect to Registered Instruments listed on the Luxembourg Stock Exchange, any notices to holders must also be published in a newspaper having general circulation in Luxembourg and, in addition to the foregoing, will be deemed validly given only after the date of such publication.

15. Further Issues

The Issuer may from time to time, without the consent of the Holders of any Instruments or Coupons, create and issue further instruments, bonds or debentures having the same terms and conditions as such Instruments in all respects (or in all respects except for the first payment of interest, if any, on them and/or the denomination thereof) so as to form a single series with the Instruments of any particular Series.

16. Currency Indemnity

The currency in which the Instruments are denominated or, if different, payable, as specified in the Pricing Supplement (the “**Contractual Currency**”), is the sole currency of account and payment for all sums payable by the Issuer in respect of the Instruments, including damages. Any amount received or recovered in a currency other than the Contractual Currency (whether as a result of, or of the enforcement of, a judgment or order of a court of any jurisdiction or otherwise) by any Holder of an Instrument or Coupon in respect of any sum expressed to be due to it from the Issuer shall only constitute a discharge to the Issuer to the extent of the amount in the Contractual Currency which such Holder is able to purchase with the amount so received or recovered in that other currency on the date of that receipt or recovery (or, if it is not practicable to make that purchase on that date, on the first date on which it is practicable to do so). If that amount is less than the amount in the Contractual Currency expressed to be due to any Holder of an Instrument or Coupon in respect of such Instrument or Coupon the Issuer shall indemnify such Holder against any loss sustained by such Holder as a result. In any event, the Issuer shall indemnify each such Holder against any cost of making such purchase which is reasonably incurred. These indemnities constitute a separate and independent obligation from the Issuer’s other obligations, shall give rise to a separate and independent cause of action, shall apply irrespective of any indulgence granted by any Holder of an Instrument or Coupon and shall continue in full force and effect despite any judgment, order, claim or proof for a liquidated amount in respect of any sum due in respect of the Instruments or any judgment or order. Any such loss aforesaid shall be deemed to constitute a loss suffered by the relevant Holder of an Instrument or Coupon and no proof or evidence of any actual loss will be required by the Issuer.

17. Waiver and Remedies

No failure to exercise, and no delay in exercising, on the part of the Holder of any Instrument, any right hereunder shall operate as a waiver thereof nor shall any single or partial exercise thereof preclude any other or future exercise thereof or the exercise of any other right. Rights hereunder shall be in addition to all other rights provided by law. No notice or demand given in any case shall constitute a waiver of rights to take other action in the same, similar or other instances without such notice or demand.

18 Redenomination, Renominalisation and Reconventioning

18.1 This Condition 18 is applicable to the Instruments only if it is specified in the relevant Pricing Supplement as being applicable.

- 18.2 If the country of the Specified Currency becomes or announces its intention to become, a Participating Member State, the Issuer may, without the consent of Holders, on giving at least 30 days' prior notice to Holders and the Paying Agents, designate a date (the "**Redenomination Date**"), being an Interest Payment Date under the Instruments falling on or after the date on which such country becomes a Participating Member State.
- 18.3 Notwithstanding the other provisions of these Terms and Conditions, with effect from the Redenomination Date:
- (i) the Instruments shall be deemed to be redenominated into euro in the denomination of euro 0.01 with a principal amount for each Instrument equal to the principal amount of that Instrument in the Specified Currency, converted into euro at the rate for conversion of such currency into euro established by the Council of the European Union pursuant to the Treaty (including compliance with rules relating to rounding in accordance with European Community regulations); provided, however, that, if the Issuer determines, with the agreement of the Issue and Paying Agent, then market practice in respect of the redenomination into euro 0.01 of internationally offered securities is different from that specified above, such provisions shall be deemed to be amended so as to comply with such market practice and the Issuer shall promptly notify the Holders, each listing authority, stock exchange and/or quotation system (if any) by which the Instruments have then been admitted to listing, trading and/or quotation and the Paying Agents of such deemed amendments;
 - (ii) if Instruments have been issued in definitive form:
 - (a) all unmatured Coupons denominated in the Specified Currency (whether or not attached to the Instruments) will become void with effect from the date (the "**Euro Exchange Date**") on which the Issuer gives notice (the "**Euro Exchange Notice**") to Holders that replacement Instruments and Coupons denominated in euro are available for exchange (provided that such Instruments and Coupons are available) and no payments will be made in respect thereof;
 - (b) the payment obligations contained in all Instruments denominated in the Specified Currency will become void on the Euro Exchange Date but all other obligations of the Issuer thereunder (including the obligation to exchange such Instruments in accordance with this Condition 18) shall remain in full force and effect; and
 - (c) new Instruments and Coupons denominated in euro will be issued in exchange for Instruments and Coupons denominated in the Specified Currency in such manner as the Issue and Paying Agent may specify and as shall be notified to Holders in the Euro Exchange Notice; and
 - (iii) all payments in respect of the Instruments (other than, unless the Redenomination Date is on or after such date as the Specified Currency ceases to be a sub-division of the euro, payments of interest in respect of periods commencing before the Redenomination Date) will be made solely in euro by cheque drawn on, or by credit or transfer to a euro account (or any other account to which euro may be credited or transferred) maintained by the payee with, a bank in the principal financial centre of any Member State of the European Communities.
- 18.4 Following redenomination of the Instruments pursuant to this Condition 18, where Instruments have been issued in definitive form, the amount of interest due in respect of the Instruments will be calculated by reference to the aggregate principal amount of the Instruments presented (or, as the case may be, in respect of which Coupons are presented) for payment by the relevant holder.
- 18.5 If the relevant Instruments are specified as Floating Rate in the relevant Pricing Supplement and Relevant Screen Page is specified in the relevant Pricing Supplement as the manner in which the Interest Rate(s) is/are to be determined, with effect from the Redenomination Date the Interest Determination Date shall be deemed to be the second TARGET Business Day before the first day of the relevant Interest Accrual Period.

19. Governing Law

- 19.1 The Instruments, the Issue and Paying Agency Agreement and the Deed of Covenant are governed by, and shall be construed in accordance with, English law.

20. Jurisdiction

- 20.1 The Issuer irrevocably agrees for the benefit of the Holders of the Instruments that the courts of England shall have jurisdiction to hear and determine any suit, action or proceedings, and to settle any disputes, which may arise out of or in connection with the Instruments or Coupons (respectively, “**Proceedings**” and “**Disputes**”) and, for such purposes, irrevocably submits to the non-exclusive jurisdiction of such courts.
- 20.2 The Issuer irrevocably waives any objection which it might now or hereafter have to the courts of England being nominated as the forum to hear and determine any Proceedings and to settle any Disputes and agrees not to claim that any such court is not a convenient or appropriate forum.
- 20.3 The Issuer agrees that the process by which any proceedings in England are begun may be served on it by being delivered to the Chief of the Consul Department at the Embassy of the Czech Republic currently located at 26-30 Kensington Palace Gardens, London W8 4QY. If the appointment of the person mentioned in this Condition 20.3 ceases to be effective, the Issuer shall forthwith appoint a further person in England to accept service of process on its behalf in England and notify the name and address of such person to the Issue and Paying Agent and, failing such appointment within fifteen days, any Holder of an Instrument shall be entitled to appoint such a person by written notice addressed to the Issuer and delivered to the Issuer or to the specified office of the Issue and Paying Agent. Nothing contained herein shall affect the right of any Holder of an Instrument to serve process in any other manner permitted by law.
- 20.4 The submission to the jurisdiction of the courts of England shall not (and shall not be construed so as to) limit the right of the Holders of the Instruments or any of them to take Proceedings in any other court of competent jurisdiction nor shall the taking of proceedings in any one or more jurisdictions preclude the taking of Proceedings in any other jurisdiction (whether concurrently or not) if and to the extent permitted by applicable law.
- 20.5 The Issuer consents generally in respect of any Proceedings to the giving of any relief or the issue of any process in connection with such Proceedings including (without limitation) the making, enforcement or execution against any property whatsoever (irrespective of its use or intended use) of any order or judgment which may be made or given in such Proceedings subject, in the case of any property, to the matters specifically provided for in Clause 20.6 below.
- 20.6 To the extent that the Issuer or any of its revenues, assets or properties shall be entitled to any immunity from suit, from the jurisdiction of any such court, from set-off, from attachment prior to judgment, from attachment in aid of execution of judgment, from execution of a judgment or from any other legal or judicial process or remedy, and to the extent that in any such jurisdiction there shall be attributed such an immunity, the Issuer irrevocably waives such immunity to the fullest extent permitted by the laws of such jurisdiction. Such waiver of immunities constitutes only a limited and specific waiver by the Issuer for the purposes of this Agreement and under no circumstances shall it be construed as a general waiver by the Issuer or a waiver with respect to proceedings unrelated to this Agreement. The Issuer does not waive any immunity in respect of property which is ambassadorial, consular or defence real property or buildings or the contents thereof, in each case situated outside the Czech Republic.

PROVISIONS RELATING TO THE INSTRUMENTS WHILST IN GLOBAL FORM

(A) *Relationship of Accountholders with Clearing Systems*

Each of the persons shown in the records of Euroclear, Clearstream, Luxembourg or any other clearing system as the holder of an Instrument represented by a Global Instrument (which expression includes a Temporary Global Instrument and a Permanent Global Instrument) must look solely to Euroclear, Clearstream, Luxembourg or such other clearing system (as the case may be) for such person's share of each payment made by the Issuer to the bearer of such Global Instrument (or the registered holder of the Global Registered Instrument, as the case may be), and in relation to all other rights arising under the Global Instruments, subject to and in accordance with the respective rules and procedures of Euroclear, Clearstream, Luxembourg or such clearing system (as the case may be). Such persons shall have no claim directly against the Issuer in respect of payments due on the Instruments for so long as the Instruments are represented by such Global Instrument or Global Registered Instrument and such obligations of the Issuer will be discharged by payment to the bearer of such Global Instrument (or the registered holder of the Global Registered Instrument, as the case may be), in respect of each amount so paid. References in these provisions relating to the Instruments in global form to "**holder**" or "**accountholder**" are to those persons shown in the records of the relevant clearing system as a holder of an Instrument.

(B) *Form and Exchange – Bearer Global Instruments*

- (1) TEFRA D or TEFRA C: The Pricing Supplement shall specify whether U.S. Treasury Regulation § 1.163-5(c)(2)(i)(D) (the "**TEFRA D Rules**") or U.S. Treasury Regulation § 1.163-5(c)(2)(i)(C) (the "**TEFRA C Rules**") shall apply. Each Tranche of Bearer Instruments is represented upon issue by a temporary global Instrument (a "**Temporary Global Instrument**"), unless the Pricing Supplement specifies otherwise and the TEFRA C Rules apply.

Where the Pricing Supplement applicable to a Tranche of Bearer Instruments specifies that the TEFRA C Rules apply, such Tranche is (unless otherwise specified in the Pricing Supplement) represented upon issue by a Permanent Global Instrument.

Interests in a Temporary Global Instrument may be exchanged for:

- (i) interests in a permanent global Instrument (a "**Permanent Global Instrument**"); or
- (ii) if so specified in the Pricing Supplement, definitive Instruments in bearer form ("**Definitive Instruments**") and/or (if so specified in the Pricing Supplement) Registered Instruments.

Exchanges of interests in a Temporary Global Instrument for Definitive Instruments or, as the case may be, a Permanent Global Instrument will be made only on or after the Exchange Date (as specified in the Pricing Supplement) and (unless the Pricing Supplement specifies that the TEFRA C Rules are applicable to the Instruments) provided certification as to the beneficial ownership thereof as required by U.S. Treasury regulations (in substantially the form set out in the Temporary Global Instrument or in such other form as is customarily issued in such circumstances by the relevant clearing system) has been received. An exchange for Registered Instruments will be made at any time or from such date as may be specified in the Pricing Supplement, in each case, without any requirement for certification.

- (2) *Limitation on entitlement under a Temporary Global Instrument after Exchange Date*. Holders of interests in any Temporary Global Instrument shall not (unless, upon due presentation of such Temporary Global Instrument for exchange (in whole but not in part only) for a Permanent Global Instrument or for delivery of Definitive Instruments and/or Registered Instruments, such exchange or delivery is improperly withheld or refused and such withholding or refusal is continuing at the relevant payment date) be entitled to receive any payment in respect of the Instruments represented by such Temporary Global Instrument which falls due on or after the Exchange Date or be entitled to exercise any option on a date after the Exchange Date.
- (3) *Certification of non-U.S. beneficial ownership*: Unless the Pricing Supplement specifies that the TEFRA C Rules are applicable to the Instruments and subject to paragraph (2) above, if any date on which a payment of interest is due on the Instruments of a Tranche occurs whilst any of the Instruments of that Tranche are represented by a Temporary Global Instrument, the

related interest payment will be made on the Temporary Global Instrument only to the extent that certification as to the beneficial ownership thereof as required by U.S. Treasury regulations (in substantially the form set out in the Temporary Global Instrument or in such other form as is customarily issued in such circumstances by the relevant clearing system) has been received by Euroclear or Clearstream, Luxembourg, or any other relevant clearing system which may be specified in the Pricing Supplement. Payments of amounts due in respect of a Permanent Global Instrument or (subject to paragraph (2) above) a Temporary Global Instrument (if the Pricing Supplement specifies that the TEFRA C Rules are applicable to the Instruments) will be made through Euroclear or Clearstream, Luxembourg or any Other relevant clearing system without any requirement for certification.

- (4) *Exchange for Definitive Instruments:* Interests in a Permanent Global Instrument will be exchanged (subject to the period allowed for delivery as set out in (i) below), in whole but not in part only and at the request of the Holder of such Global Instrument, for Definitive Instruments and/or (if so specified in the Pricing Supplement) Registered Instruments, (a) if Euroclear or Clearstream, Luxembourg or any other relevant clearing system is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business or (b) any of the circumstances described in Condition 7 occurs or, (c) at any time on the request of the bearer, if so specified in the Pricing Supplement. Whenever a Permanent Global Instrument is to be exchanged for Definitive Instruments and/or Registered Instruments, the Issuer shall procure the prompt delivery of such Definitive Instruments and/or Registered Instruments, duly authenticated and where and to the extent applicable, with Receipts, Coupons and Talons attached (each as defined in Condition 1.2 and Condition 1.3), in an aggregate principal amount equal to the principal amount of such Permanent Global Instrument to the Holder of the Permanent Global Instrument against its surrender at the specified office of the Issue and Paying Agent within 30 days of the Holder requesting such exchange. Furthermore, if,
- (i) Definitive Instruments have not been delivered in accordance with the foregoing by 5.00 p.m. (London time) on the thirtieth day after the Holder has requested exchange, or
 - (ii) the Permanent Global Instrument (or any part thereof) has become due and payable in accordance with the Conditions or the date for final redemption of the Permanent Global Instrument has occurred and, in either case, payment in full of the amount of the Redemption Amount (as defined in Condition 6.9) together with all accrued interest thereon has not been made to the Holder in accordance with the Conditions on the due date for payment,

then such Permanent Global Instrument (including the obligation to deliver Definitive and/or Registered Instruments) will become void at 5.00 p.m. (London time) on such thirtieth day (in the case of (i) above) or at 5.00 p.m. (London time) on such due date (in the case of (ii) above) and the Holder of the Permanent Global Instrument will have no further rights thereunder (but without prejudice to the rights which the such Holder or others may have under the Deed of Covenant). Under the Deed of Covenant, persons shown in the records of Euroclear and/or Clearstream, Luxembourg (or any other relevant clearing system as being entitled to interests in the Instruments will acquire directly against the Issuer all those rights to which they would have been entitled if, immediately before the Permanent Global Instrument became void, they had been the Holders of Definitive Instruments in an aggregate principal amount equal to the principal amount of Instruments they were shown as holding in the records of Euroclear and/or Clearstream, Luxembourg or other relevant clearing system (as the case may be).

(C) *Form and Exchange – Global Registered Instruments*

- (1) *Global Registered Instrument:* Registered Instruments held in Euroclear and/or Clearstream, Luxembourg (or other clearing system) will be represented by a Global Registered Instrument which will be registered in the name of a nominee for, and deposited with, a common depositary for Euroclear and Clearstream, Luxembourg (or such other relevant clearing system).
- (2) *Exchange:* The Global Registered Instrument will become exchangeable in whole, but not in part, for individual Registered Instruments if (a) Euroclear or Clearstream, Luxembourg is closed for business for a continuous period of 14 days (other than by reason of legal holidays) or announces an intention permanently to cease business, (b) any of the circumstances described in Condition 7

occurs, or (c) at any time at the request of the registered Holder if so specified in the Pricing Supplement.

Whenever the Global Registered Instrument is to be exchanged for Registered Instruments, such Registered Instruments will be issued in an aggregate principal amount equal to the principal amount of the Global Registered Instrument within five business days of the delivery, by or on behalf of the registered Holder of the Global Registered Instrument, Euroclear and/or Clearstream, Luxembourg, to the Registrar or the Transfer Agent (as the case may be) of such information as is required to complete and deliver such Registered Instruments (including, without limitation, the names and addresses of the persons in whose names the Registered Instruments are to be registered and the principal amount of each such person's holding) against the surrender of the Global Registered Instrument at the Specified Office of the Registrar or the Transfer Agent (as the case may be). Such exchange will be effected in accordance with the provisions of the Agency Agreement and the regulations concerning the transfer and registration of Instruments scheduled thereto and, in particular, shall be effected without charge to any Holder, but against such indemnity as the Registrar or the Transfer Agent (as the case may be) may require in respect of any tax or other duty of whatsoever nature which may be levied or imposed in connection with such exchange.

If (a) Registered Instruments have not been issued and delivered by 5.00 p.m. (London time) on the thirtieth day after the date on which the same are due to be issued and delivered in accordance with the terms of the Global Registered Instrument or (b) any of the Instruments evidenced by the Global Registered Instrument has become due and payable in accordance with the Conditions or the date for final redemption of the Instruments has occurred and, in either case, payment in full of the amount of principal falling due with all accrued interest thereon has not been made to the Holder of the Global Registered Instrument on the due date for payment in accordance with the terms of the Global Registered Instrument, then the Global Registered Instrument (including the obligation to deliver Registered Instruments) will become void at 5.00 pm (London time) on such thirtieth day (in the case of (a) above) or at 5.00 pm (London time) on such due date (in the case of (b) above) and the Holder will have no further rights thereunder (but without prejudice to the rights which the Holder or others may have under the Deed of Covenant). Under the Deed of Covenant, persons shown in the records of Euroclear and/or Clearstream, Luxembourg (or other relevant clearing system) as being entitled to interests in the Instruments will acquire directly against the Issuer all those rights to which they would have been entitled if, immediately before the Global Registered Instrument became void, they had been the registered Holders of Instruments in an aggregate principal amount equal to the principal amount of Instruments they were shown as holding in the records of Euroclear, Clearstream, Luxembourg or other relevant clearing system (as the case may be).

(D) *Amendment to Conditions*

The Temporary Global Instruments, Permanent Global Instruments and Global Registered Instruments contain provisions that apply to the Instruments that they represent, some of which modify the effect of the Terms and Conditions of the Instruments set out in this Information Memorandum. The following is a summary of certain of those provisions:

- (1) *Meetings:* The holder of a Permanent Global Instrument or of the Instruments represented by a Global Registered Instrument shall (unless such Permanent Global Instrument or Global Registered Instrument represents only one Instrument) be treated as being two persons for the purposes of any quorum requirements of a meeting of holders and, at any such meeting, the holder of a Permanent Global Instrument shall be treated as having one vote in respect of each minimum Denomination of Instruments for which such Global Instrument may be exchanged. (All holders of Registered Instruments are entitled to one vote in respect of each Instrument comprising such holder's holding, whether or not represented by a Global Registered Instrument).
- (2) *Cancellation:* Cancellation of any Instrument represented by a Permanent Global Instrument that is required by the Conditions to be cancelled (other than upon its redemption) will be effected by reduction in the principal amount of the relevant Permanent Global Instrument.
- (3) *Purchase:* Instruments represented by a Permanent Global Instrument may only be purchased by the Issuer if they are purchased together with the rights to receive all future payments of interest and Instalment Amounts (if any) thereon.

- (4) *Issuer's Options:* Any option of the Issuer provided for in the Conditions of the Instruments while such Instruments are represented by a Permanent Global Instrument or a Global Registered Instrument shall be exercised by the Issuer giving notice to the holders within the time limits set out in and containing the information required by the Conditions, except that the notice shall not be required to contain the serial numbers of Instruments drawn in the case of a partial exercise of an option and accordingly no drawing of Instruments shall be required. In the event that any option of the Issuer is exercised in respect of some but not all of the Instruments of any Series, the rights of accountholders with a clearing system in respect of the Instruments will be governed by the standard procedures of Euroclear, Clearstream, Luxembourg or any other clearing system (as the case may be).
- (5) *Holders' Options:* Any option of the holders provided for in the Conditions of any Instruments while such Instruments are represented by a Permanent Global Instrument or a Global Registered Instrument may be exercised by the Holder of such Permanent Global Instrument or Global Registered Instrument, giving notice to the Issue and Paying Agent within the time limits relating to the deposit of Instruments with a Paying Agent or the Registrar, in the case of a Global Registered Instrument substantially in the form of the notice available from any Paying Agent (or the Registrar, in the case of a Global Registered Instrument), except that the notice shall not be required to contain the serial numbers of the Instruments in respect of which the option has been exercised, and stating the principal amount of Instruments in respect of which the option is exercised and at the same time presenting for notation the Permanent Global Instrument or the Global Registered Instrument to the Issue and Paying Agent, or to a Paying Agent acting on behalf of the Issue and Paying Agent, (or the Registrar, in the case of a Global Registered Instrument).
- (6) *Notices:* So long as any Instruments are represented by a Permanent Global Instrument or Registered Global Instrument and such Permanent Global Instrument or Global Registered Instrument is held on behalf of a clearing system, notices to the holders of Instruments of that Series may be given by delivery of the relevant notice to the clearing system for communication by it to entitled accountholders in substitution for publication as required by the Conditions or by delivery of the relevant notice to the Holder of the Permanent Global Instrument or Global Registered Instrument except that so long as the Instruments are listed on the Luxembourg Stock Exchange and the rules of that exchange so require, notice shall also be published in a leading newspaper having general circulation in Luxembourg (which is expected to be the *Luxemburger Wort*).

(E) *Partly Paid Instruments*

While any Partly Paid Instalments due from the holder of Partly Paid Instruments are overdue, no interest in a Permanent Global Instruments or Registered Global Instrument representing such Instruments may be exchanged for an interest in a Permanent Global Instrument or for Definitive Instruments or a Registered Instrument (as the case may be). If any holder fails to pay any instalment due on any Partly Paid Instruments within the time specified, the Issuer may forfeit such Instruments and shall have no further obligation to such holder in respect of them.

FORM OF PRICING SUPPLEMENT

Form of Pricing Supplement for an issue by The Czech Republic *acting through the Ministry of Finance* under the Programme for the Issuance of Debt Instruments

PRICING SUPPLEMENT

[Date]

Series No.: [●]

Tranche No.: [●]

The Czech Republic
acting through the Ministry of Finance

Issue of
[Aggregate Principal Amount of Tranche] [Title of Notes]
€3,000,000,000 Programme for the Issuance of Debt Instruments

This document constitutes the Pricing Supplement relating to the issue of Instruments described herein.

Terms used herein shall be deemed to be defined as such for the purposes of the Terms and Conditions set forth in the Information Memorandum dated 3 June 2004. This Pricing Supplement contains the final terms of the Instruments and must be read in conjunction with such Information Memorandum.

[The following alternative language applies if the first tranche of an issue which is being increased was issued under an Information Memorandum with an earlier date.]

Terms used herein shall be deemed to be defined as such for the purposes of the Terms and Conditions (the “**Conditions**”) set forth in the Information Memorandum dated [original date]. This Pricing Supplement contains the final terms of the Instruments and must be read in conjunction with the Information Memorandum dated 3 June 2004, save in respect of the Conditions which are extracted from the Information Memorandum dated [original date] and are attached hereto.]

Include whichever of the following apply or specify as “Not Applicable” (N/A). Note that the numbering should remain as set out below, even if “Not Applicable” is indicated for individual paragraphs or sub-paragraphs. Italics denote directions for completing the Pricing Supplement.

- | | | |
|----|--|--|
| 1. | Issuer | The Czech Republic, <i>acting through the Ministry of Finance</i> |
| 2. | [(i)] Series Number: | [] |
| | [(ii)] Tranche Number: | [] |
| | | <i>(If fungible with an existing Series, details of that Series, including the date on which the Instruments become fungible)</i> |
| 3. | Specified Currency or Currencies: | [] |
| 4. | Aggregate Principal Amount: | |
| | [(i)] Series: | [] |
| | [(ii)] Tranche: | [] |
| 5. | [(i)] Issue Price: | [] per cent. of the Aggregate Principal Amount [plus accrued interest from [insert date] <i>(in the case of fungible issues only, if applicable)</i>] |
| | [(ii)] Net Proceeds: | [] <i>(Required only for listed issues)</i> |
| 6. | Specified Denominations: | [] |
| 7. | [(i)] Issue Date: | [] |
| | [(ii)] Interest Commencement Date
(if different from the Issue Date): | [] |

8. Maturity Date: *[specify date or (for Floating Rate Instruments) Interest Payment Date falling in or nearest to the relevant month and year]*
- [If the Maturity Date is less than one year from the Issue Date and either (a) the issue proceeds are received by the Issuer in the United Kingdom or (b) the activity of issuing the Instruments is carried on from an establishment maintained by the Issuer in the United Kingdom, (i) the Instruments must have a minimum redemption value of £100,000 (or its equivalent in other currencies) and be sold only to “professional investors” or (ii) another applicable exemption from section 19 of the FSMA must be available.]*
9. Interest Basis: *[Interest bearing/Non-Interest bearing]*
- [● % Fixed Rate]*
[[specify reference rate] +/- ● % Floating Rate]
[Other (specify)]
(further particulars specified below)
10. Maturity Redemption Amount: *[Specify if not the Outstanding Principal Amount]*
[Partly Paid]
[Instalment]
[Other (specify)]
11. Change of Interest or Redemption/Payment Basis: *[Specify details of any provision for convertibility of Instruments into another interest or redemption/ payment basis]*
12. Put/Call Options: *[Investor Put]*
[Issuer Call]
[(further particulars specified below)]
13. Status: Senior
14. Listing: *[Luxembourg/other (specify)/None]*
15. Method of distribution: *[Syndicated/Non-syndicated]*
16. Interest: *[Interest bearing / Non-interest bearing]*
(If fixed rate Instruments, specify rate)
17. Floating Rate Instruments: *[Applicable/Not applicable] (If not applicable, delete the remaining sub-paragraphs of this paragraph. Also consider whether EURO BBA LIBOR or EURIBOR is the appropriate reference rate after 1 January 1999)*
- (i) Manner in which Interest Rate is/are to be determined: *[Screen Rate Determination/ ISDA Determination/other (give details)]*
- (ii) Party responsible for calculating the Interest Rate(s) and Interest Amounts if not the [Issue and Paying Agent]): *[[Name] shall be the Calculation Agent (no need to specify if the Issue and Paying Agent is to perform this function)]*
- (iii) Screen Rate Determination:
- Reference Rate: *[For example, LIBOR or EURIBOR]*
 - Interest Determination Date(s): *[]*
 - Relevant Screen Page: *[For example, Moneyline Telerate page 3750/248]*
 - Relevant Time: *[For example, 11.00 a.m. London/Brussels time]*

- Relevant Financial Centre: *[For example, London/euro-zone (where Euro-zone means the region comprised of the countries whose lawful currency is the euro)]*
- (vi) ISDA Determination:
 - Floating Rate Option: []
 - Designated Maturity: []
 - Reset Date: []
- (v) Margin(s): [+/-][] per cent. per annum
- (vi) Minimum Interest Rate: [] per cent. per annum
- (vii) Maximum Interest Rate: [] per cent. per annum
- (viii) Business Day Convention: [Floating Rate Convention/Following Business Day Convention/Modified Following Business Day Convention/Preceding Business Day Convention/other (*give details*)]
- 18. Interest Payment Dates: []
- 19. Interest Period End Dates: [Applicable/Not Applicable] [] (*Specify. If nothing is specified, Interest Period End Dates will correspond with Interest Payment Dates.*)
- 20. Additional Business Centre(s): [Not Applicable/*give details*]
- 21. Day Count Fraction: []
- 22. Other Provisions Relating to Interest Calculations (including Amortisation Yield and other provisions (if non-interest bearing)): [Not Applicable/*give details*]

PROVISIONS RELATING TO REDEMPTION

- 23. Call Option: [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
 - (i) Early Redemption Amount (Call): []
 - (ii) Series redeemable in part: [*Specify, otherwise redemption will only be permitted of entire Series*]
 - (iii) Call Option Date(s)/Call Option Period: []
- 24. Put Option: [Applicable/Not Applicable]
(If not applicable, delete the remaining sub-paragraphs of this paragraph)
 - (i) Early Redemption Amount (Put): []
 - (ii) Put Option Date(s)/Put Option Period: []
- 25. Final Redemption Amount of each Instrument: []
- 26. Early Termination Amount: [*Specify, if not the Outstanding Principal Amount or, in the case of any Instruments which are non-interest bearing, the Amortised Face Amount*]

GENERAL PROVISIONS APPLICABLE TO THE INSTRUMENTS

- 27. Form of Instruments: [Bearer/Registered]

[Temporary Global Instrument exchangeable for a Permanent Global Instrument which is exchangeable for Definitive Instruments on [] days' notice/at any time/in the limited

- circumstances specified in the Permanent Global Instrument.]
- [Temporary Global Instrument exchangeable for Definitive Instruments on [] days' notice.]
- [Permanent Global Instrument exchangeable for Definitive Instruments on [] days' notice/at any time/in the limited circumstances specified in the Permanent Global Instrument].
28. Additional Financial Centre(s) or other special provisions relating to Payment Dates: [Not Applicable/(specify)] (*Relates to the date and place of payment, and not interest period end dates*)
29. Talons for future Coupons or Receipts to be attached to Definitive Instruments (and dates on which such Talons mature): [Yes/No. *If yes, give details*]
30. Details relating to Partly Paid Instruments: [Not Applicable/*give details*]
(*Amount of each payment comprising the Issue Price and date on which each payment is to be made and consequences (if any) of failure to pay, including any right of the Issuer to forfeit the Instruments and interest due on late payment*)
31. Details relating to Instalment Instruments: [Not Applicable/*give details*]
(*Amount of each instalment, date on which each payment is to be made*)
32. Redenomination, renominatisation and reconventioning provisions: [Not Applicable/The provisions [in Condition 18/annexed to this Pricing Supplement] apply]
33. Other terms or special conditions: [Not Applicable/*give details*]

DISTRIBUTION

34. (i) If syndicated, names of Managers: [Not Applicable/*give details*]
(ii) Stabilising Manager (if any) [Not Applicable/*give details*]
35. If non-syndicated, name of Dealer: [Not Applicable/*give details*]
36. TEFRA: [Not Applicable/The [C/D] Rules are applicable]
37. Additional selling restrictions: [Not Applicable/*give details*]

OPERATIONAL INFORMATION

38. ISIN Code: []
39. Common Code: []
40. Any clearing systems other than Euroclear and Clearstream, Luxembourg and the relevant identification number(s): [Not Applicable/*give details*]
41. Delivery: Delivery [against/free of] payment
42. Additional Paying Agent(s) (if any): [Not Applicable/*give details*]

[LISTING APPLICATION

This Pricing Supplement comprises the final terms required to list the issue of Instruments described herein pursuant to the €3,000,000,000 Programme for the Issuance of Debt Instruments of The Czech Republic *acting through the Ministry of Finance.*]

RESPONSIBILITY

The Issuer accepts responsibility for the information contained in this Pricing Supplement.

Signed on behalf of the Issuer:

By:.....

Duly authorised

THE CZECH REPUBLIC

Geography and Population

The Czech Republic is situated in the heart of Europe, bordering Germany to the west, Poland to the north, Slovakia to the east and Austria to the south. Its borders are mostly formed by forested mountain ranges and hills, except in the south-east where it shares lowlands with Austria and Slovakia. A developed road and rail network connects its two main regions, Bohemia and Moravia.

The Czech Republic covers an area of approximately 30,000 square miles and its population is estimated to be approximately 10.2 million inhabitants. Approximately one quarter of the population of the Czech Republic lives in the country's five largest cities, the largest of which is Prague, the Czech capital, with an estimated population of approximately 1.2 million.

History

The origins of the first independent Czech state are found in the Middle Ages, when the region enjoyed economic and cultural prosperity, particularly under Emperor Charles IV. The country came under Habsburg rule for a period of 400 years, beginning in the early 16th century, and during the 19th century became a part of the Austro-Hungarian Empire. The independent state of Czechoslovakia was established as a democratic republic on October 28, 1918, following the collapse of the Austro-Hungarian Empire at the end of World

War I.

Between 1918 and 1938, Czechoslovakia was politically stable and economically prosperous. The country had inherited most of the Austro-Hungarian Empire's industrial capacity, and its labour force was considered highly skilled. Subsequent to Germany's invasions of Czechoslovakia in 1938 and 1939, the Czech regions of Bohemia and Moravia together became a German protectorate, while Slovakia became a separate republic under German rule. While many Czech and Slovak industrial areas were destroyed during World War II, Czechoslovakia did not suffer the devastation that other countries sustained.

In 1945, Czechoslovakia was re-established as an independent state. Parliamentary elections were held in May 1946, and resulted in the communist party coming to power. In 1948, the communist party took exclusive control of the Government, establishing a one-party state and drawing Czechoslovakia into the political and economic sphere of the Soviet Union. A new Constitution cemented communist party control. Two rounds of nationalisation, in 1945 and in 1948, eliminated private ownership of property in the country, and the communist regime remained in power for more than 40 years.

Demands for greater political freedom culminated in the appointment of a reform-oriented government during the spring of 1968. However, in August 1968, an invasion by Soviet and Warsaw Pact soldiers, widely known as the Prague Spring, forcibly suppressed these reform efforts.

Starting in November 1989, a short, non-violent struggle, which came to be known as the Velvet Revolution, initiated fundamental changes in the country's social, economic and political systems. The communist party was no longer able to depend upon Soviet political and economic support and lost political power, ceding power first to an interim coalition Government, then to free elections, and then, in June 1990, to the establishment of a new democratic Federal Assembly.

In April 1990, Czechoslovakia was renamed the Czech and Slovak Federal Republic (the "CSFR"), in formal recognition of the functional autonomy of the two republics. Initially, collaboration between the republics proved to be successful, ensuring broad support for the intensive reform programmes launched in 1991. However, by mid-1992, coalition building between the republics had become increasingly difficult and the complex parliamentary rules of the CSFR threatened to paralyse the political process. On November 25, 1992, the Federal Assembly enacted a law dissolving the CSFR. On the basis of this law, the Czech and Slovak Republics became formally independent states on January 1, 1993. Legally, each republic became a successor to the CSFR, and federal property was divided on a two-to-one ratio (Czech Republic to Slovak Republic), reflecting the relative size of populations and economies. Separate monetary systems and currencies were introduced by each republic in February 1993.

On May 1 2004, the Czech Republic became a member of the European Union.

The Czech Political System

In 1992, the Czech Republic adopted a new constitution, which provides for the separation of legislative, executive and judicial powers.

Parliament

The Parliament of the Czech Republic consists of two chambers: a Chamber of Deputies with 200 members, and a Senate with 81 members. The members of the Chamber of Deputies are elected for a four-year term and the members of the Senate are generally elected for a six-year term, with one-third of the total number of the Senate's seats elected every two years. Amendments to the Constitution and certain other legislative acts require the consent of both the Chamber of Deputies and the Senate. The Senate has the power to review the legislation passed by the Chamber of Deputies (except for acts approving the State budget and final State accounts, which are only approved by the Chamber of Deputies). The Chamber of Deputies can override a bill vetoed by the Senate by the votes of 101 Deputies. The Senate, unlike the Chamber of Deputies, cannot be dissolved. The Senate was initially formed and Senators elected in November 1996.

President

The President of the Czech Republic is the head of state, elected for a five-year term by a joint session of both chambers of the Parliament. The President may serve a maximum of two successive terms in office. Presidential authority is limited, but the President can dissolve the Chamber of Deputies under certain limited circumstances. The President may also veto a law, other than constitutional acts, passed by the Parliament; the Presidential veto can be overridden by the votes of 101 Deputies. Further, the President appoints and recalls the Prime Minister and other members of the government and accepts their resignations, recalls the Government (when so required under the Constitution) and accepts its resignation; appoints justices of the Constitutional Court, grants pardons for criminal acts; appoints the President and Vice-President of the Supreme Auditing Office; and appoints members of the Board of the Czech National Bank. Certain acts of the President are subject to the consent of the Government; this includes acts taken in the representation of the State in foreign relations, negotiation and ratification of international treaties, the appointment of judges and the declaration of amnesties.

The current President, Václav Klaus, was elected in February 2003 replacing the previous president and long-standing leader from the times of the Velvet Revolution, Václav Havel. Václav Klaus was one of the founding members of the Civic Democratic Party ("ODS") and served in a number of important public offices including the posts of the Federal Minister of Finance (1989-91), Prime Minister of the Czech Republic (1992-97) and Chairman of the Chamber of Deputies (1998-2002).

Government

Currently, the executive branch of government in the Czech Republic consists of seventeen members ("Ministers"), including the Prime Minister. The Prime Minister is appointed, and under certain limited circumstances may be dismissed, by the President. The President also appoints and dismisses, at the request of the Prime Minister, the other Ministers of the government (the "Government" or "Cabinet").

The current Prime Minister is Vladimír Špidla, who has held the position since the elections to the Chamber of Deputies in 2002.

Judiciary

Under the Constitution, judicial power in the Czech Republic is vested in the Constitutional Court and a system of general courts. The system of general courts consists of the Supreme Court, the Supreme Administrative Court, two Superior Courts, eight Regional Courts and eighty-six District Courts.

The Constitutional Court is charged with upholding the Constitution and constitutional laws. The Constitutional Court decides on the compatibility of laws with the Constitution and constitutional laws; the compatibility of generally binding legal regulations other than laws with the Constitution, constitutional laws and other laws; and the compatibility of certain international treaties with the Constitution with constitutional laws. The Constitutional Court has the authority to rule in certain constitutional matters, in particular on the matters of eligibility, election or capacity to hold the office of members of the Parliament and on the impeachment of the President. The Constitutional Court finally decides jurisdictional disputes between state bodies and local governments, rules on claims of individuals and legal entities whose constitutional rights were infringed and decides on the measures necessary to implement decisions of international tribunals. Judges of the Constitutional Court are appointed by the President with the consent of the Senate for a term of 10 years. All decisions of the Constitutional Courts are binding on all governmental bodies, legal entities and individuals.

The general courts are independent of other State authorities; they decide on all civil law and criminal law matters and they also examine the legitimacy of administrative bodies' decisions. The Supreme

Court, the Supreme Administrative Court, Superior Courts and Regional Courts have limited appellate and original jurisdiction. The Supreme Court, the Supreme Administrative Court and the Superior Courts exercise their original jurisdiction only in a limited number of cases. All judges of the general courts serve for life after appointment by the President. Judgments are declared in the name of the Czech Republic and always publicly. Judges are independent in their decision-making, they are bound only by law and international agreements which form a part of Czech law, and they have the power to consider whether legal acts other than laws are compatible with law or such international agreements.

As of May 1, 2004, enforceable judgments given in the courts of another EU member state became enforceable in the Czech Republic without review as to their substance, subject to their being declared enforceable upon application for such a declaration has been made by an interested party. Appeals against the above-mentioned declaration of enforceability in the Czech Republic, of judgments issued by the courts of other EU member states, will only be upheld if the recognition/enforcement of such judgment is, amongst others: manifestly contrary to public policy; unfair due to the defendant not being given an adequate opportunity to prepare a defence; irreconcilable with a judgment given in the Czech Republic between the same parties; or irreconcilable with an earlier judgment involving the same cause of action and between the same parties in another jurisdiction.

The Czech Republic is a party to the 1958 New York Convention on Recognition and Enforcement of Foreign Arbitral Awards which allows the enforcement and recognition in the Czech Republic of arbitration awards rendered in other participating states.

Public Defender of Rights

The Public Defender of Rights (ombudsman) was established as a new independent State body in 2000. The mission of the Public Defender of Rights is to assist individuals and legal entities in defending their rights and freedoms in relation to the acts of public administration authorities that violate the law or principles of a democratic legal state and proper administration, as well as in relation to complaints concerning the failure of such authorities to take action, procrastination and improper or unethical behaviour or conduct on the part of public officials.

Local Government

There is currently a two-tier system of local government in the Czech Republic, consisting of 14 regional and over 5,500 municipal authorities. Municipal governments have the authority to impose local levies within the limits established by law. The municipal authorities, as well as regional governments and the national Government, share power to regulate, *inter alia*, transportation, education and other issues.

Recent Political Developments

The elections for the Chamber of Deputies held in June 2002 brought a victory for the Czech Social Democratic Party ("CSSD"), with 30.2% of the vote, followed by ODS with 24.4% of the vote, the Communist Party with 18.5% of the vote and a coalition of the Christian Democratic Party-Czechoslovak People's Party ("KDU-CSL") and the Freedom Union which gained 14.3% of the vote.

The following table shows a breakdown of the distribution of seats in the Chamber of Deputies as a result of the 2002 elections:

	Chamber of Deputies
Coalition Parties Total	101
– Czech Social Democratic Party (CSSD)	70
– Coalition of Christian Democratic Party-Czechoslovak People's Party (KDU-CSL) and the Freedom Union.....	31
Opposition Parties and Unaffiliated Total	99
– Civic Democratic Party (ODS).....	58
– Communist Party	41
Total	200

Source: Czech Statistical Office

Vladimír Špidla, the current Prime Minister and leader of CSSD, formed a coalition government with KDU-CSL and the Freedom Union after the elections, which held a narrow majority. The Civic Democrats (ODS) were the largest party of opposition whilst the Communists retained a significant number of seats. The new Government confirmed its commitment to EU integration and embarked upon a reform of public finances, aimed at revitalizing the economy and promoting economic growth.

The narrow majority of the coalition parties in the Chamber of Deputies undermines the position of the Government in pursuing its political goals. This becomes particularly apparent when the votes of all the Deputies of the coalition are necessary to adopt a resolution in the Chamber of Deputies, for instance, when a veto of the Senate or the President must be overruled. The Government has proved on several occasions, however, that it can both activate the coalition Deputies and obtain the support of some other Deputies, mainly from the Communist Party.

The coalition majority in the Chamber of Deputies was threatened in March 2004 when two Deputies of the Freedom Union left the party and discussions broke up regarding their prospective defection to the ODS. In the middle of May 2004 both Deputies remain members of the Freedom Union's club but the press continues to report on their intention to join another political party. On the side of the opposition, a Deputy elected for ODS was expelled by both the party and its club in late 2003, though he remains in the Chamber as an unaffiliated Deputy.

Due to a different voting system, the composition of the Senate differs from the composition of the Chamber of Deputies, particularly as regards the affiliation of Senators and their clubs with political parties. The parties nominate candidates to the elections for the Senate who are known to the constituencies, rather than on the basis of them being loyal party members. Some Senators are elected as independent candidates without the support of any major political party. Only CSSD, KDU-CSL and ODS have political clubs, which identify themselves with the respective parties; 52 out of 81 Senators are Members of these clubs.

With respect to the composition of the Senate as of May 17, 2004, 33 Senators were elected with the support of the "Coalition of Four" (KDU-CSL, the Freedom Union, ODA and DEU) or of one of the participating political parties, 26 Senators were elected with the support of ODS, 10 Senators were elected with the support of CSSD, 3 Senators were elected with the support of the Communist Party and 9 Senators were elected without any support from a major political party. 21 Senators were unaffiliated to a political party. As of May 17, 2004, the Senators were grouped into 6 senator clubs, with 3 Senators not participating in any club.

The following table provides a breakdown of the seats in the Senate among individual clubs:

	Senate
Coalition Clubs Total	26
– Czech Social Democratic Party Club (CSSD)	10
– Club of Christian Democratic Party-Czechoslovak People's Party (KDU-CSL)	16
Other Clubs and Independent Senators	55
– Open Democratic Club ⁽¹⁾	16
– Civic Democratic Party Club (ODS)	26
– "Club of Independent"	5
– "Club of Unaffiliated"	5
– Senators not participating in any club	3
Total	81

Source: Czech Statistical Office

(1) In 2003, the Club of Freedom Union (i.e., the coalition party) was transformed by a decision of the participating senators into the Open Democracy Club. The Open Democracy Club publicly proclaims that it does not consider itself a part of the coalition and is open to Senators affiliated with other political parties as well as those not affiliated with any political party.

International Relations

The Czech Republic became a member of the United Nations in January 1993, as a successor to Czechoslovakia, which had been a member since 1945; in the same year the Czech Republic also became a member of the Council of Europe. On March 12, 1999 the Czech Republic joined the North Atlantic Treaty Organisation ("NATO") as a full member and in 1995 it became a member of the OECD. The

Czech Republic is a member of the International Monetary Fund (the “IMF”), the International Bank for Reconstruction and Development (the “World Bank”), the International Finance Corporation (the “IFC”), the Multilateral Investment Guarantee Agency (the “MIGA”), the European Bank for Reconstruction and Development (the “EBRD”), and the World Trade Organisation (the “WTO”), which is based on the General Agreement on Tariffs and Trade (the “GATT”). The Czech Republic also participates in the Bank for International Settlements (the “BIS”).

European Union

The Czech Republic joined the EU on May 1, 2004. Pavel Telička was appointed as the first Czech representative to the Commission; he will be working alongside Commissioner for Health and Consumer Protection, David Byrne, for an initial period of six months following the accession. After accession, the Government plans to finalize a document setting out the Czech Republic’s policies within the EU for the period from 2004 through 2013. Further, the first elections to the European Parliament are scheduled to take place on June 11 and 12, 2004. The Czech Republic will elect 24 members to the European Parliament.

The Czech Republic participated in the work of the European Convention that resulted in the preparation of a draft Treaty establishing a Constitution for Europe. The Czech Republic took a favourable position on the draft Treaty, during the intergovernmental conference held in November 2003, subject to certain limited reservations. In particular, the Czech Republic required that each EU member state should have one Commissioner with voting power, and that there should be limits on the system of qualified voting, based on population, in order to avoid smaller EU member states being disadvantaged.

The Czech Republic intends to integrate further into the European structures through accession to the “Schengen” system that enables a higher degree of free movement of individuals among the participating states and regulates the protection of common external borders. The Czech Republic is gradually changing its legislation so as to be ready for the “Schengen” system by the year 2006 or 2007.

Disputes

The Czech Republic is involved in a number of disputes:

The largest pending dispute of the Czech Republic is with affiliates of the Japanese bank, Nomura. The dispute arose from the failure of IPB, a.s. (“IPB Bank”), a large Czech bank which Nomura (together with other parties) had controlled. Forced administration and the subsequent assumption of all assets and liabilities by a healthy Czech bank was required to avoid a run on the bank and potential damage to the Czech banking system. A Nomura affiliate, Saluka, filed a claim for CZK 40.6 billion against the Czech Republic under the Czech-Dutch Investment Protection Treaty, alleging expropriation of property and unfair treatment. The claim is pending before an arbitral tribunal composed under the UNCITRAL Arbitration Rules. The State filed a counterclaim in this arbitration against Saluka for CZK 100 – 260 billion, for damage caused to the Czech Republic when averting the crisis directly threatening the banking system caused by the failure of IPB Bank in June 2000. The Czech Republic also commenced a separate arbitration in Switzerland (Zurich) in a dispute involving the National Property Fund and the Czech Republic on one side and a London based affiliate of Nomura and Saluka on the other, for the same amount of damages as stated above, resulting from an alleged breach of the share purchase agreement relating to shares of IPB Bank concluded between the NPF and Nomura in March 1998. In May 2004, the UNCITRAL arbitration tribunal ruled that it did not have jurisdiction to decide on the Czech Republic’s counterclaim and would proceed only with the original Nomura claim for CZK 40.6 billion.

In an action concerning the same subject matter as the above disputes, the failed bank sued the Czech Republic – through the Czech Office for the Protection of Economic Competition – before a Czech court for CZK 80 billion, alleging improper official procedures on the part of the Office in approving state aid for CSOB a.s. when the banking business of IPB Bank was sold to CSOB a.s. This law suit was suspended when the IPB Bank was declared bankrupt.

In relation to IPB Bank, the Czech Republic is also sued by RTP, a.s., a Czech company, which claims an amount of CZK 3.625 billion as a compensation for damage suffered by the loss in value of shares of IPB Bank. According to RTP, a.s., the damage allegedly arose as a result of the State’s failure to conduct proper supervision of IPB Bank.

Between 1999 and 2003, the Czech Republic was a defendant in two arbitration proceedings commenced by CME Czech Republic B.V. (“CME”) and its controlling shareholder Ronald Lauder under the Czech-

Dutch and Czech-U.S. Investment Protection Treaties respectively, relating to CME's investments in a television service organization (CNTS) that provided broadcasting services to CET 21, a broadcasting licence-holder (for TV Nova) in the Czech Republic. The operations of CNTS in the Czech Republic were halted when the broadcasting license-holder for TV Nova severed its business relationship with CNTS. The claimants alleged that the Czech Republic, acting through the Broadcasting Council, had failed to take adequate steps to protect their investment. While the claim by Ronald Lauder was dismissed, the Czech Republic was ordered to pay compensation to CME in the amount of USD 269 million plus interest (CZK 10.5 billion). The Czech Republic has since paid the compensation in full.

Diag Human, a.s., a Czech company involved in the blood plasma business, is currently claiming up to CZK 10 billion in compensation and lost profits from the Czech Republic, based on a 1992 statement of the Minister of Health about the company which is alleged to have caused the company to lose business in the Czech Republic. Diag Human, a.s. originally sought compensation for damage to its reputation and lost profits through the courts but subsequently agreed with the State to resolve the dispute by arbitration. Based on a partial award, the Czech Republic has already paid the company CZK 326 million in damages; the lost profits claim remains unresolved. The new Minister of Health (appointed in April 2004) has announced the Government's intention to settle the claim.

In February 2004, Israeli investor Phoenix Action Ltd. started proceedings based on the Czech – Israeli Investment Protection Treaty at the International Centre for Settlement of Investment Disputes ("ICSID") claiming USD 43 million in damages for assets frozen by the Czech customs authorities in relation to the violation of customs duties by its investment vehicle in the Czech Republic. Phoenix claims that Czech law enforcement authorities either took improper action or failed to act with respect to assets acquired from bankrupt companies in the Czech Republic.

A Dutch financial group, Investmart B.V., and Italian investor Mr. Catalfamo are negotiating with the State to settle a claim for losses in the amount of CZK 10 billion allegedly suffered as a result of the failure of Union banka, a.s., in which Investmart held a 98% stake. Investmart alleges that when the bank's own management declared the bank insolvent and Investmart proposed a general settlement with creditors, the State conducted the proceedings in an unfair and discriminatory manner and caused the bank to go bankrupt. No claim has been filed yet, but the representatives of Investmart and Mr. Catalfamo have filed a notice of dispute calling for an amicable resolution, as required under the investment protection treaties between the Czech Republic and the Netherlands and/or Italy.

Since 2003, the Luxembourg-based company, European Media Ventures S.A., has been negotiating with the State to settle a claim for approximately USD 45 million in damages. According to European Media Ventures, it allegedly suffered the loss as a result of a decision of the Broadcasting Council to approve the transfer of a TV broadcasting license from the license-holder, with whom European Media Ventures had a service agreement, to a third party, rather than the company established by agreement between the license-holder and European Media Ventures to take control of the license. This act is claimed to have destroyed the value of European Media Venture's investment, giving rise to a claim under the Czech-Belgian/Luxembourg Investment Treaty. Although the period for amicable resolution required under the treaty has expired, European Media Ventures has not yet formally filed a claim.

A Dutch company, Eastern Sugar B.V., alleges that it suffered damage as a result of an alleged breach by the Czech Republic of the Czech – Dutch Investment Protection Treaty which caused harm to its investment in the Czech Republic, made through its subsidiary company, Eastern Sugar Česká republika a.s. The damage allegedly resulted when the Czech Republic amended a governmental decree on the distribution of national quotas on the production of sugar among individual sugar producers. In April 2004, the parties were in preliminary discussions concerning a claim for damages of approximately EUR 100 million. The obligatory period for an amicable settlement elapses on June 12, 2004.

THE CZECH ECONOMY

Economic Performance

The economy of the Czech Republic has undergone significant changes since the fall of communism in 1989. Although previous communist governments had pursued conservative macroeconomic policies, which resulted in a relatively balanced monetary and fiscal position for their successors, substantial economic restructuring was required to adapt the Czech economy to two significant developments: the dissolution of the Council for Mutual Economic Assistance (“COMECON”), the former intergovernmental body co-coordinating the economic development of its members; and the collapse of the Soviet Union in 1991, which until that time had been the CSFR’s largest trading partner.

Prior to 1990, the CSFR’s economic structure was focused primarily on heavy industry and lacked developed service and financial sectors. The new post-communist CSFR government elected in 1990 sought to establish a free market economy, implement extensive privatisation of publicly owned enterprises, open foreign trade, unify exchange rates, encourage competition and establish legal systems that would permit the development of a conventional commercial sector. Successive new governments permitted foreign investment and maintained relatively strict fiscal and monetary policies. However, the collapse of the Soviet Union led to a significant contraction in the Czech Republic’s main export markets, causing significant economic disruption throughout the country. The Czech economy began to grow again in 1993 and growth rate peaked at 5.9% in 1995 driven by strong domestic demand. In the late 1990s development was affected by two factors: difficulties in the state owned banking sector and the Russian crises. This resulted in negative growth rates in 1997 and in 1998. Since then, growth performance has been robust and the Czech economy has continued to grow at a rate of above 2% despite a significant global economic slowdown.

Since 2000, foreign direct investment has had a strong influence on the economy. The banking sector has been privatised and foreign companies now own a large majority of banking sector assets. Furthermore, the Czech Republic has seen strong inflows into new production capacity, particularly in the manufacturing sector.

The following table sets out certain macroeconomic statistics regarding the Czech Republic for the four years ended 2003:

	2000	2001	2002	2003
Economic Data				
Nominal GDP (CZK billions).....	1,985	2,175	2,276	2,410
Real GDP (growth in %)	3.3	3.1	2	2.9
Real exports (growth in %).....	17	11.9	2.8	6.7
Real imports (growth in %).....	17	13.6	4.3	7.6
Registered rate of unemployment (as at the year end (%)).	8.8	8.9	9.8	10.3
Consumer prices (growth in %)	3.9	4.7	1.8	0.1
Producer prices (growth in %)	4.9	2.9	(0.5)	(0.3)
State Budget; Public and External Debt				
State budget surplus (deficit) (CZK billions)	(51.8)	(66.7)	(45.9)	(107.4)
as a % of GDP	(2.3)	(3.1)	(2.0)	(4.5)
<i>General Government surplus (deficit) under ESA 95 methodology</i>				
<i>as a % of GDP.....</i>	<i>(96.7)</i>	<i>(149.8)</i>	<i>(154.6)</i>	<i>(328.5)</i>
Total revenues incl. Grants (CZK billions)	613.3	618.8	676.2	704.2
as a % of GDP	29.5	28.8	31.0	29.0
State debt (CZK billions), unconsolidated.....	289.3	345	395.9	493.2
as a % of GDP	14.6	15.9	17.4	20.5
General government debt, after consolidation				
(CZK billions).....	332.4	404.5	444.5	554.2
as a % of GDP	16.7	18.6	19.5	23
<i>General government debt under ESA 95 (CZK billions)</i>				
<i>as a % of GDP.....</i>	<i>391.1</i>	<i>585.5</i>	<i>695.6</i>	<i>956.2</i>
Gross external debt (CZK billions)	342.5	457.3	578.9	748.7
as a % of GDP	16.7	18.6	19.5	23
Balance of Payments Data				
Current account (EUR billions)	(2.9)	(3.7)	(4.4)	(4.9)
as a % of GDP	(5.3)	(5.7)	(6)	(6.5)
Exports (EUR billions)	31.5	37.3	40.7	43.1
Imports (EUR billions)	34.9	40.7	43.0	45.3
CNB foreign exchange reserves (EUR billions)	14.16	16.40	22.61	21.34

Source: CNB, Czech Statistical Office and Ministry of Finance

Gross Domestic Product

Real GDP has grown steadily since 2000, increasing by 2.9% in 2003. Economic growth in 2003 was generated in particular by increased household consumption. It was supported by high levels of growth in wages and disposable income, stable levels of consumer prices and low interest rates. Some recovery was also observed in the area of investment expenditure, shifting the trigger of economic growth from consumption to investments at the end of 2003. The growth of domestic demand was partly offset by an increase in the foreign trade deficit (in constant prices) and pressure from the fiscal deficit.

The sectoral breakdown of GDP remained stable in 2003 in comparison with the previous year. Economic development in industry has been driven mainly by private companies under foreign control (representing roughly half of total revenues, more than one third of direct exports and a third of total employment in 2003). This favourable influence stems from the launch of new production capacities in new industrial zones and from the recovery of production in the traditional mining and machinery sectors. The relatively stable growth in recent years contrasts with the significant economic slowdown in the Eurozone, where GDP growth slowed to less than 1% in each of the years 2002 and 2003.

The following table sets out a breakdown of the sources of GDP by various economic sectors in 2002 and 2003:

Sector	2002	2003
	(%)	
Agriculture, hunting, forestry, fishing	3.8	3.5
Mining	1.2	1.2
Manufacturing	27.5	27.2
Electricity, gas and water supply	4.1	3.9
Construction	6.8	7.0
Wholesale and retail trade; repair	15.2	14.6
Hotels and restaurants.....	2.1	2.1
Transport, storage, communication	9.2	9.5
Financial services.....	4.2	4.0
Real estate sector	12.9	12.9
Other service activities + indirectly measured financial services	13.0	14.2

Source: Czech Statistical Office

Inflation

Year-on-year average consumer price inflation (CPI) has decreased steadily in the last three years, dropping to 0.1% in 2003. However, in April 2004, CPI rose to 2.3% (year-on-year). The low inflation level was mainly due to global disinflation factors and a strong currency. CPI has been below the Czech National Bank's targets since they were introduced in 2002.

The following table sets out the average rates of inflation (against the preceding year) for the years 1999 to 2003:

	1999	2000	2001	2002	2003
	(%)				
CPI.....	2.1	3.9	4.7	1.8	0.1
PPI – industry	1.0	4.9	2.9	(0.5)	(0.3)

Source: Czech Statistical Office, Czech National Bank

Employment

The transition to a market economy in the Czech Republic has caused significant changes in employment and unemployment patterns. Registered rate of unemployment grew very slowly during the mid 1990s, but jumped to 9.4% at the end of 1999, from where it has slowly grown to 10.3% at the end of 2003.

The following table sets out the registered rate of unemployment as at the end of each of years 1999 to 2003 and the average unemployment rate (in accordance with ILO methodology) for the same years:

	1999	2000	2001	2002	2003
	(%)				
Registered rate of unemployment ..	9.4	8.8	8.9	9.8	10.3
ILO Unemployment rate	8.7	8.8	8.1	7.3	7.8

Source: Czech Statistical Office

The ratio of the economically active population to the total population has decreased over recent years and the sectoral structure of employment has been approaching that of other EU countries. However, a number of structural shortcomings persist, which result in increasing unemployment rates, especially when it comes to long-term unemployment. Significant regional disparities in unemployment and high unemployment rates of vulnerable groups, notably young and older workers, are other consequences. The key structural problems include, in particular, the low regional and professional mobility of workers, the relatively liberal system of social benefits, high taxes on labour and the absence of a universal lifelong learning scheme.

From a structural perspective, a relatively high percentage (27.3%) work in the manufacturing sector. This is high compared to the Eurozone, where less than 20% of total employment is in the manufacturing

sector. The fact that this high fraction has been maintained despite significant cut backs in old industrial enterprises shows the impact of new investment into this sector. One of the principal factors driving the Czech Republic's strong position in manufacturing is a well qualified labour force, particularly within the technical disciplines, such as engineering.

The service sector's share of total employment in the Czech Republic is 56.2%.

The following table illustrates the general composition of employment and unemployment rates at the end of each year from 1999 to 2003:

	As at the year ended 31 December				
	1999	2000	2001	2002	2003
	<i>(in thousand persons)</i>				
Agriculture, hunting and related service activities	190.2	177.9	177.8	184.2	172.1
Forestry, fishing, operation of fish hatcheries and farms	50.5	47.5	47.4	43.7	41.1
Mining and quarrying	70.4	67.7	67.1	61.1	53.3
Manufacturing	1,281.5	1,315.2	1,310.4	1,318.2	1,294.3
Electricity, gas and water supply	77.5	87.8	87.3	83.8	77.1
Construction	439.0	429.8	427.7	425.2	438.7
Trade, rep. of motor vehicles, and personal and household goods	612.9	608.3	604.9	619.8	627.8
Hotels and restaurants.....	156.3	159.4	158.7	170.5	170.7
Transport, storage and communications.....	373.2	364.2	362.6	367.6	358.8
Financial intermediation and insurance.....	99.6	102.0	101.4	95.2	96.3
Real estate, renting and business activities.....	266.0	257.8	256.0	269.1	284.9
Public administration and defence; compulsory soc. security	342.9	341.0	339.3	325.7	331.9
Education.....	298.9	301.6	300.0	309.1	287.8
Health and social work	290.7	306.0	304.3	304.2	306.9
Other community, social and personal services ...	175.8	179.2	178.2	179.4	185.1
Private households with employed persons	1.7	1.3	1.3	3.3	4.3
Extra-territorial organizations and bodies.....	2.0	0.8	0.8	1.1	0.9
Not identified	2.4	2.6	2.6	3.8	1.2
Employed in national economy (LFS, average)...	4,731.6	4,750.2	4,727.7	4,764.9	4,733.2
Total labour force (LFS, average).....	5,218	5,186	5,146	5,139	5,132
Unemployed.....	443.2	470.0	443.8	477.5	521.6
Rate of unemployment (average in %)......	8.5	9.0	8.5	9.2	9.9
Unemployed (LFS)	454	455	418	374	399
ILO Unemployment rate (LFS)	8.7	8.8	8.1	8.1	7.8

Source: Czech Statistical Office, Ministry of Labour

Wages

Nominal wage trends largely reflect overall inflation developments, showing a significant decline in nominal wage growth from the mid 1990s to 2000. Real wage growth patterns have been driven more by cyclical trends in the economy, but variation in real wage growth rates has generally been small, on a regional comparison. Given moderate negative current inflation, this has led to an increase in the real wage growth rate to just above 7%.

The following table sets out the annual percentage change in the average nominal wage and the average real wage for the years 1999 to 2003:

	1999	2000	2001	2002	2003
	<i>(%)</i>				
Average gross nominal wages	8.4	6.4	8.7	7.2	6.8
Average real wages.....	6.2	2.4	3.8	5.3	6.7

Source: Czech Statistical Office

BALANCE OF PAYMENTS AND FOREIGN TRADE

Balance of Payments

The following table sets forth the balance of payments of the Czech Republic for the years 1999 through 2003:

	As at the year ended 31 December				
	1999	2000	2001	2002	2003
	<i>(EUR millions)</i>				
Current Account	(1 371.9)	(2 945.2)	(3 652.2)	(4 426.1)	(4 937.1)
Balance of trade	(1 784.9)	(3 393.0)	(3 423.6)	(2 314.8)	(2 179.1)
Exports.....	24 639.6	31 482.7	37 251.2	40 711.2	43 079.1
Imports.....	26 424.5	34 875.7	40 674.8	43 026.0	45 258.2
Balance of services.....	1 125.2	1 532.1	1 701.3	709.2	415.7
Revenues	6 611.6	7 436.3	7 912.7	7 501.4	6 882.0
Transportation	1 451.1	1 509.0	1 686.8	1 835.7	1 901.7
Travel	2 959.2	3 231.4	3 466.0	3 125.1	3 150.0
Other	2 201.3	2 695.9	2 759.9	2 540.6	1 830.3
Expenditures	5 486.4	5 904.2	6 211.4	6 792.2	6 466.3
Transportation	734.0	773.5	896.9	952.0	1 059.1
Travel	1 403.4	1 386.4	1 549.2	1 673.0	1 708.9
Other	3 349.0	3 744.3	3 765.3	4 167.2	3 698.3
Balance of Incomes.....	(1 265.5)	(1 487.7)	(2 451.3)	(3 752.2)	(3 663.0)
Credit	1 743.3	2 118.5	2 490.8	2 167.7	2 336.7
Debit.....	3 008.8	3 606.2	4 942.1	5 919.9	5 999.7
Current transfers	553.3	403.4	521.4	931.7	489.3
Credit	1 230.8	1 027.6	1 068.1	1 515.9	1 468.8
Debit.....	677.5	624.2	546.7	584.2	979.5
Capital Account	(2.0)	(5.6)	(9.7)	(3.9)	(2.6)
Revenues	17.3	6.3	2.7	7.2	6.2
Expenditures	19.3	11.9	12.4	11.1	8.8
Financial Account	2 889.4	4 157.5	5 071.5	11 288.7	5 145.5
Direct investments	5 848.5	5 357.1	6 111.5	8 793.0	2 083.7
Abroad	(84.3)	(46.4)	(184.5)	(219.4)	(205.6)
In the Czech Republic.....	5 932.8	5 403.5	6 296.0	9 012.4	2 289.3
Portfolio investments.....	(1 308.7)	(1 914.4)	1 022.7	(1 517.2)	(1 184.4)
Assets	(1 778.8)	(2 432.8)	129.3	(2 453.6)	(2 697.2)
Liabilities	470.1	518.4	893.4	936.4	1 512.8
Financial derivatives	0.0	(39.4)	(94.5)	(138.9)	121.2
Assets	–	(126.4)	(276.0)	(501.7)	222.4
Liabilities	–	87.0	181.5	362.8	(101.2)
Other investments	(1 650.4)	754.2	(1 968.2)	4 151.8	4 125.0
Assets	(2 474.7)	1 006.3	(1 353.9)	4 320.4	2 105.4
Long-term	(647.5)	598.8	38.9	931.8	35.0
Short-term	(1 827.2)	407.5	(1 392.8)	3 388.6	2 070.4
Liabilities	824.3	(252.1)	(614.3)	(168.6)	2 019.6
Long-term	(34.9)	(736.1)	(125.0)	92.6	670.5
Short-term	859.2	484.0	(489.3)	(261.2)	1 349.1
Sub-Total	<u>1 515.5</u>	<u>1 206.7</u>	<u>1 409.6</u>	<u>6 858.7</u>	<u>205.8</u>
Net errors and omissions, FX differences.....	33.7	(319.5)	560.7	182.2	199.4
Total	<u><u>1 549.2</u></u>	<u><u>887.2</u></u>	<u><u>1 970.3</u></u>	<u><u>7 040.9</u></u>	<u><u>405.2</u></u>

Source: CNB

Current Account

The current account deficit of the Czech Republic has slowly increased over the last four years, from EUR 2.9 billion in 2000 to EUR 4.9 billion in 2003. As a percentage of GDP, however, the current account deficit has increased from 4.8% in 2000 to 6.5% in 2003. The principal reason behind the growth in the current account deficit, despite the slight improvement in trade balance, is the decrease in the balance of services surplus, mainly driven by weaker demand for certain services (including telecommunications and technology).

The financial account surplus has slowly grown over the last four years from EUR 4.2 billion in 2000 to EUR 5.1 in 2003, except for the year 2002 in which the financial account surplus more than doubled, due principally to the receipt of privatisation proceeds from the sale of Transgas.

Foreign Trade

In 2003, the trade balance deficit improved slightly, following a more significant improvement in 2002. This was principally driven by increased growth in the volume (and to a lesser extent the price) of exports, which exceeded growth in the volume and price of imports.

From a territorial perspective, a significant trade balance surplus was achieved with EU countries in the amount of approximately CZK 104 billion in 2003, compared to CZK 60 billion in 2002. This was partly offset by increased trade deficits with other countries with developed market economies (most importantly Japan), developing countries and non-European countries with transition economies.

The following table provides information about the development and the territorial composition of the Czech Republic's balance of trade for the period from 1999 to 2003:

	As at and for the year ended 31 December				
	1999	2000	2001	2002	2003
	<i>(CZK millions, in current prices)</i>				
Total imports	973,169	1,241,924	1,386,319	1,325,671	1,441,202
Index.....	104.8	127.6	111.6	95.7	108.7
Market economies.....	718,337	892,019	990,720	920,044	986,854
– of which EU countries	624,970	770,507	856,813	798,115	853,933
Developing countries.....	43,920	57,619	75,305	96,506	106,472
Transition economies and CIS in					
total.....	188,364	261,383	275,579	244,648	269,251
– of which CEFTA.....	127,589	159,071	174,115	160,256	177,876
OECD Countries.....	780,213	1,044,611	1,157,392	1,075,705	1,158,428
Total exports	908,756	1,121,099	1,269,634	1,254,860	1,371,810
Index.....	106.9	123.4	113.2	99.0	109.3
Market economies.....	677,520	838,375	954,150	942,384	1,038,332
– of which EU countries	628,914	768,746	875,324	858,345	957,950
Developing countries.....	29,908	42,844	42,438	43,771	39,972
Transition economies and CIS in					
total.....	198,145	236,420	268,922	261,742	281,990
– of which CEFTA.....	161,653	189,360	215,697	209,524	229,059
OECD Countries.....	744,760	1,007,555	1,146,877	1,127,760	1,242,688

Source: Czech Statistical Office

The commodity structure of foreign trade confirmed the continuing trend of increasing trade surplus in the categories of machinery and transport equipment and manufactured goods. Increased trade deficits were recorded in the areas of chemical products (in particular pharmaceuticals) and fuels, partly due to increased import prices of natural gas and crude oil.

The following table sets forth the composition of imports and exports of the Czech Republic for each of the years 1999 through 2003, according to category of commodities, classified in accordance with the Standard International Trade Classification:

	As at and for the year ended 31 December				
	1999	2000	2001	2002	2003
	<i>(in %)</i>				
Imports					
Food, beverages, tobacco.....	5.5	4.6	4.4	4.6	4.5
Crude materials except fuels.....	3.2	3.2	2.9	2.9	2.8
Mineral fuels, lubricants.....	6.7	9.6	9.1	7.6	7.5
Animal and vegetable oil, fats, waxes.....	0.3	0.2	0.2	0.2	0.3
Chemicals and related products.....	12.2	11.2	10.9	11.2	11.4
Manufactured goods.....	21.1	20.8	20.2	20.6	20.1
Machinery and transport equipment.....	39.4	40.0	42.2	42.4	42.8
Miscellaneous manufactured goods.....	11.6	10.4	10.1	10.6	10.6
Exports					
Food, beverages, tobacco.....	3.8	3.7	3.4	3.2	3.3
Crude materials except fuels.....	3.8	3.5	3.0	2.8	2.8
Mineral fuels, lubricants.....	2.9	3.1	3.0	2.9	2.9
Animal and vegetable oil, fats, waxes.....	0.1	0.1	0.1	0.1	0.1
Chemicals and related products.....	7.4	7.1	6.4	6.0	5.9
Manufactured goods.....	26.0	25.4	24.4	23.4	23.1
Machinery and transport equipment.....	42.4	44.5	47.4	49.6	50.1
Miscellaneous manufactured goods.....	13.6	12.6	12.3	12.1	11.9

Source: Czech Statistical Office

Trade Policy

Throughout the 1990s, the Czech Republic took a number of steps to integrate its economy into world trade. As early as 1993, it signed an association agreement with the EU, and concluded a free trade agreement with CEFTA. In 1995, the Czech Republic became a member of the WTO. Since 1994, CEFTA membership benefited the Czech Republic by eliminating or discounting customs duties on the export of industrial products and by providing concessions regarding trade in agricultural products with member countries.

On 1 May 2004, the Czech Republic became a member of the EU.

Foreign direct investment

Supported by investment incentives, the Czech Republic registered significant increases in foreign direct investment ("FDI") inflows, especially during the last four years. From 1993 to the end of 2003, the Czech Republic received in total CZK 1,288 billion (EUR 40.4 billion) in FDI.

The following table sets forth historical records of foreign direct investments in the Czech Republic and Czech direct investments abroad in years 1999 to 2003:

	As at and for the year ended 31 December				
	1999	2000	2001	2002	2003
	<i>(CZK millions)</i>				
Direct investment:					
Abroad.....	(3,107.6)	(1,653.7)	(6,289.2)	(6,759.3)	(6,546.5)
Equity capital and reinvested earnings	(2,585.3)	(1,245.9)	(5,848.5)	(5,376.8)	(324.1)
Other capital.....	(522.3)	(407.8)	(440.7)	(1,382.5)	(6,222.4)
In the Czech Republic.....	218,811.5	192,421.1	214,585.3	277,689.5	72,899.5
Equity capital and reinvested earnings	192,615.5	171,777.2	185,981.4	270,061.0	66,811.9
Other capital.....	26,196.0	20,643.9	28,603.9	7,628.5	6,087.6
Net direct investment.....	215,703.9	190,767.4	208,296.1	270,930.2	66,353.0

Source: CNB

Lower privatisation revenues in 2003 (compared to unusually high levels in 2002, due to the privatisation of Transgas which was sold to RWE), combined with the outflow of capital resulting from the acquisition by Český Telecom, a.s. (the incumbent Czech telecommunications operator), of a 49% share in Eurotel Praha, s.r.o., from Atlantic West B.V. (for USD 1.05 billion) and the divestment by TelSource of its shares in Český Telecom, a.s., were the main reasons for the drop in FDI inflow in 2003, which amounted to CZK 72.9 billion (approximately EUR 2.3 billion).

Of the total amount of FDI inflow during the period from 1993 to 2003, approximately one third went into manufacturing (especially into the production of machines, electrical and optical equipment and means of transport) and 20% was directed into the banking and insurance industry, approximately 13% into trade and maintenance and nearly 8% into real estate services.

The following table sets forth the distribution of net FDI in the Czech Republic by industry sector during each of the years 1999 to 2003:

As at and for the year ended 31 December					
	1999	2000	2001	2002	2003
<i>(CZK millions)</i>					
Non-manufacturing					
Agriculture, hunting, and forestry	219	323	1,104	(63)	53
Mining and quarrying	8,619	2,970	1,387	905	89
Electricity, gas, and water supply	11,528	7,951	10,258	12,579	6,404
Construction	503	3,877	2,971	6,042	2,127
Trade, hotels and restaurants	50,826	21,185	26,773	8,221	18,348
Transport, storage and communications	6,806	9,838	31,376	143,864	(58,966)
Financial intermediation	52,078	36,033	60,234	48,485	25,628
Real estate and business activities	14,566	28,905	17,356	12,189	23,659
Education	0	28	23	0	34
Health and social work	128	640	62	903	72
Other social and personal services	4,059	1,561	161	11,802	1,070
Non-manufacturing Total	<u>149,331</u>	<u>113,312</u>	<u>151,706</u>	<u>244,928</u>	<u>18,518</u>
Manufacturing					
Food and tobacco	12,428	6,801	9,376	2,602	3,424
Textiles, wearing apparel, and leather	1,602	2,621	3,921	(1,144)	(193)
Wood, paper and publishing	7,202	1,985	5,693	2,294	4,273
Refined petroleum and chemicals	13,646	11,507	4,150	8,353	6,620
Non-metallic products	10,905	4,435	5,830	2,401	2,627
Basic metals and metal products	6,384	9,662	3,275	6,595	14,428
Machinery and equipment	15,626	40,610	30,690	10,719	22,358
Recycling and other manufacturing	1,689	1,489	(56)	942	844
Manufacturing Total	<u>69,481</u>	<u>79,109</u>	<u>62,880</u>	<u>32,762</u>	<u>54,381</u>
Total	<u>218,812</u>	<u>192,421</u>	<u>214,586</u>	<u>277,690</u>	<u>72,899</u>

Source: Czech National Bank

The following table sets forth the composition of net FDI in the Czech Republic by country during each of the years 1999 to 2003:

	As at and for the year ended 31 December				
	1999	2000	2001	2002	2003
	(CZK millions)				
Western Europe					
Belgium.....	47,802	2,041	6,135	14,300	4,312
Denmark.....	1,478	3,972	5,965	3,083	238
France.....	8,037	8,969	58,553	4,644	14,724
Germany.....	44,968	51,024	49,956	152,286	23,338
United Kingdom.....	3,605	6,085	16,496	(7,205)	7,656
Italy.....	1,625	1,392	(79)	4,153	1,980
Netherlands.....	39,126	39,983	36,078	40,222	(44,040)
Austria.....	28,831	28,478	10,048	24,930	17,247
Sweden.....	4,384	5,696	781	3,554	537
Switzerland.....	12,243	8,813	6,665	8,869	7,425
Canada.....	375	5,970	2,764	(3,654)	430
United States.....	20,095	11,675	9,309	6,201	5,745
Japan.....	167	1,787	1,120	3,794	7,140
Other.....	6,078	16,536	10,794	22,512	26,167
Total	218,812	192,421	214,585	277,689	72,900

Source: Czech National Bank

Investment Incentives

As part of its economic transformation efforts, the Czech Republic has pursued a policy of encouraging foreign direct investment as a means of attracting capital, infusing new managerial skills and creating employment opportunities.

Since 2000, the Government has offered a standardized package of investment incentives for industrial companies, offered pursuant to terms specified in Czech law and not limited to foreign investors. This programme includes the following measures: reduced corporate income tax for new investors; financial support for creating new places of work; financial support for the training of employees; customs duty exemptions; the provision of subsidies to municipalities to create industrial zones; and the provision of financial support when introducing environmentally friendly technologies.

The European Commission has reviewed aid granted to investors under this programme on an individual basis, and is expected to approve the framework of certain future aid which may be provided pursuant to Czech law as an aid scheme.

Portfolio investments

In 2003, the balance of portfolio investments recorded a net outflow of funds in the amount of CZK 37.7 billion (approximately 15.6% of GDP). The aggregate amount of portfolio investments by Czech entities reached CZK 85.9 billion in 2003. Domestic investors (in particular banks and other financial institutions) invested funds primarily in long-term foreign bonds, and in this area there was a net outflow of about CZK 85.8 billion. Portfolio investments by foreign investors in the Czech Republic amounted to CZK 48.2 billion in 2003. They were mainly focused on equity securities, whereas investments in bonds declined. A higher demand for Czech securities as portfolio investments was recorded in the fourth quarter of 2003 in connection with the sale of the shares of Český Telecom, a.s. by TelSource. The total amount of Czech bonds issued on international capital markets in foreign currencies increased in 2003 by CZK 7.3 billion, which was largely due to the issuance of eurobonds by the City of Prague and the Czech Export Bank in the aggregate amount of USD 170 million and USD 150 million, respectively.

Other investments

The balance of other investments recorded a net inflow of foreign capital in 2003 in the amount of CZK 131.4 billion (EUR 4.1 billion). Year-on-year, this represents an increase of approximately CZK 3.4 billion. The largest net recipients of funds were banks (approximately CZK 80.2 billion). The

Government sector's share of the total inflow of capital was CZK 18.2 billion, largely resulting from the receipt of loans by both the central government and by municipalities for the construction of transportation infrastructure (primarily loans from EIB). The corporate sector was also a significant recipient of foreign capital (CZK 33.0 billion, including a loan to Český Telecom, a.s. for the purchase of Eurotel shares).

PRIVATISATION AND TRANSFORMATION INSTITUTIONS

National Property Fund

The National Property Fund of the Czech Republic (the “NPF”) was established in 1991 as a special purpose vehicle to carry out Czech privatisations. The basic function of the NPF is to execute the sale of State enterprises in accordance with privatisation projects approved by the Government (or the Ministry of Finance in certain cases) and temporarily to manage State interests in certain companies prior to their privatisation. The NPF itself does not decide on the manner or timing of privatisations.

The NPF currently operates under the direct political supervision of the Chamber of Deputies, which also approves the NPF’s budget and elects the Presidium and the Supervisory Board of the NPF.

As the purpose for which the NPF was formed has been substantially fulfilled, it is currently proposed that the NPF be liquidated, perhaps as soon as the end of 2005. The manner of liquidation has not yet been determined, but it will ultimately need to be approved by Parliament.

Privatisation

From 1991 through the end of 2003, total NPF revenues from privatisations reached CZK 413.6 billion (approximately EUR 13.0 billion) (corresponding to a book value of approximately CZK 982 billion). In 2003, privatisation revenues amounted to CZK 24.3 billion, compared to CZK 125.8 billion in 2002, CZK 59.4 billion in 2001, CZK 20.1 billion in 2000 and CZK 25.5 billion in 1999.

During 1999 and 2001, the Czech Republic largely completed the privatisation of the banking sector by selling majority stakes in three of the largest banks (Československá obchodní banka, a.s., Česká spořitelna, a.s. and Komerční banka, a.s.) to foreign investors.

Following the completion of the privatisation of the banking sector, the Government commenced the privatisation of national monopolies, particularly in the energy and gas industries. In 2001 and 2002, the Czech gas monopoly company, Transgas a. s., and eight regional gas distribution companies were sold to RWE Gas AG of Germany, in what was the largest privatisation in Czech history. In 2002, the NPF successfully privatised a major Czech steel company, Nová Huť, a.s. to LNM Holdings N.V.

In 2003, the NPF disposed of most of its remaining equity interests in the regional energy distribution companies by concluding an agreement with ČEZ, a.s. (the incumbent electricity producer in the Czech Republic (still controlled by the NPF), pursuant to which ČEZ, a.s. purchased stakes in distribution companies from the NPF partly in exchange for the transfer by ČEZ, a.s. of its 51.1% stake in ČEPS, a.s. (a company operating the electricity transmission system in the Czech Republic) to a subsidiary of the NPF.

In 2003, the NPF announced a tender process for the sale of its stake in Unipetrol, a.s., one of the largest oil and petrochemical companies in Central and Eastern Europe. In April 2004, PKN ORLEN of Poland submitted a binding offer to purchase Unipetrol, a.s., which was accepted by the Government. The negotiations with the bidder are currently underway and the sale is expected to be completed by the end of 2004.

The following table provides summary information about the most important privatisations completed during the years 1999 through 2003:

Company	Business	Acquiror	Purchase Price
<i>(CZK billions, except where noted otherwise)</i>			
2003			
Energy distribution companies (8 companies)	Electricity	ČEZ	31.94
Vítkovice, a.s.	Steel	Lahvárna Ostrava	0.08
2002			
Nová Huť, a.s.	Steel	LNM Holdings	USD 6 million
2001			
Pražské vodovody a kanalizace, a.s.	Water supply	Veolia Water	6.1
Komerční banka, a.s.	Banking	Société Générale	EUR 1.19 billion
České radiokomunikace, a.s.	Telecommunications	Bivideon	6.82
Česká pojišťovna, a.s.	Insurance	PPF	3.87
Jan Becher-KV Becherovka, a.s.	Liquor	SALB	1.38
Transgas, a.s. and 8 regional gas distribution companies	Gas	RWE Gas	EUR 4.1 billion (plus EUR 1.3 billion in 2002)
2000			
Paramo	Chemicals	Unipetrol	0.14
Česká spořitelna, a.s.	Banking	Erste Bank	19.38
Železnobrodské sklo, a.s.	Glass	Bijou Terra	0.28
1999			
ČSOB	Banking	KBC Bank N.V.	23.89

Source: NPF

(1) In this table privatization transactions are listed according to the year in which the relevant sale and purchase agreement was signed by the NPF. The actual transfer of the shares and the payment of the purchase price customarily may often occur in a subsequent year due to various conditions which may be set forth in the agreement and which need to be satisfied before the consummation of the transaction.

As at 31 December 2003, the remaining assets held by the NPF comprised interests in 10 strategic companies (i.e., companies which are considered to be particularly important to the Czech economy) with an aggregate book value of approximately CZK 100 billion and 168 non-strategic companies with an aggregate book value of approximately CZK 33.3 billion.

A list of the residual interests held by the NPF in strategic companies as at 31 December 2003 is provided below, together with details of their current status:

Company	Business	Book Value of NPF Stake	NPF Stake	Status
<i>(CZK millions)</i>				
ČEPRO, a. s.	Oil & Gas	2,660	100.00	No plan adopted
České aerolinie, a. s.	Airline	1,557	56.92	No plan adopted
Český Telecom, a. s.	Telecommunication	16,459	51.10	Preparation of tender procedure
ČEZ, a. S.	Electricity	40,041	67.61	No plan adopted
MERO ČR, a. S.	Oil & Gas	8,431	100.00	No plan adopted
OKD, a.s.	Coal mining	11,150	45.88	Sale agreement signed with Karbon Invest a.s. for CZK 2.25 billion on 8 April 2004
Severočeské doly, a. s.	Coal mining	4,986	55.40	Tender procedure closed in December 2003, no bidder selected yet
Sokolovská uhelná, a. s.	Coal mining	3,303	48.69	Sale agreement signed with Sokolovska tezební, a.s. for CZK2.6 billion on 29 March 2004
Škoda Praha, a. s.	Heavy engineering	305	54.77	In January 2004, the NPF's stake decreased to approximately 24% due to capital increase by ČEZ through debt/equity swap
Unipetrol, a. s.	Chemicals	11,422	62.99	Tender procedure finalised, negotiations with the bidder underway
Total		100,313		

Source: Annual Report of the NPF for 2003 (except "Status")

Apart from the companies controlled through the NPF, the State also operates the Czech Post Office (Česká pošta, s.p.), the Czech Airport Authority (Česká správa letišť, s.p.) and Czech Railways (České dráhy, a.s.). Currently there are no definitive plans as to whether and when any of these operations will be privatised.

The proceeds earned by the NPF from privatisations do not form part of the State budget of the Czech Republic and may only be used for purposes provided by law. Historically, privatisation proceeds have been used principally to cover losses of the Czech Consolidation Agency, to provide financial resources for the infrastructure and housing funds, to cover deficits of the social insurance system and to cover payment obligations arising from environmental indemnities provided by the NPF to privatised companies in connection with their privatisation. They may also be used for other purposes determined by the Government resolutions within the limits set by law.

Pursuant to the accounting methodology used by the Czech Republic, the NPF has always formed part of the General Government. Accordingly, the results of the operation of the NPF and its assets and liabilities are included (and have historically been included) in the consolidated General Government deficit and debt.

The NPF has granted a significant amount of indemnities and guarantees to governmental institutions as well as private companies. Most importantly, they include indemnities provided to privatised companies and privatisation investors against environmental losses resulting from past ecological burdens relating to the privatised companies, guarantees provided to the Czech Consolidation Agency in relation to certain transactions and guarantees provided to privatised companies for the purposes of supporting their viability.

In April 2004, an arbitration tribunal upheld a claim for CZK 2.05 billion raised by Petrcíle s.r.o., a Czech management company for the privatisation of a steel company Nová Huť, against the State. The claim was based on the fact that the withdrawal by the National Property Fund from the contract for the privatisation of the steel company was invalid. The NPF has challenged in Czech court the arbitration award on the grounds permitted under the Czech Act on the Arbitration Proceedings and the Enforcement of Arbitration Awards. Upon the request of the NPF the court has deferred the payment until a final decision on the complaint.

Czech Consolidation Agency

The Czech Consolidation Agency (“CKA”) was founded by a special law (the “CKA Act”) in 2001, to assume all the assets and liabilities of the Consolidation Bank (“KOB”), a state financial institution formed in 1991 as a specialised bank to address the problem of non-performing loans that had arisen in the banking system after 1989.

The role of CKA is to administer, collect and realise non-performing receivables from distressed companies, including banks, assumed pursuant to Government decisions. CKA also executes, in accordance with Government instructions, revitalization and restructuring programmes relating to Czech businesses and provides funding and other forms of support to projects selected by the Government.

Unlike its predecessor, CKA is not a bank, but it holds a securities dealer license. CKA may issue bonds and, with the prior consent of the Government, acquire interests in companies or even establish new companies. CKA has its own budget, which is not part of the State budget. However, the liabilities of CKA are fully guaranteed by the State pursuant to the CKA Act.

CKA is managed by a Board of Directors headed by a General Director. The Supervisory Board has mainly overview authority. Pursuant to the CKA Act, the approval of the Supervisory Board is needed for certain important actions and decisions, such as the establishment of a subsidiary, or any transaction undertaken in excess of CZK 500 million. Members of the Supervisory Board are appointed by the Chamber of Deputies for a five-year term (and include MPs).

Pursuant to the CKA Act, CKA should terminate its activities and cease to exist as of 31 December 2011 whereupon all its assets and liabilities will be transferred to the State budget. It is currently under discussion whether termination should occur earlier, as of the end of 2007, however, the ultimate timing and manner of CKA’s termination has not yet been determined and is dependent upon a law being adopted to this effect.

Due to the nature of its operations, CKA (as well as its predecessor, KOB) has been, and is expected to continue, generating losses which represent a contingent liability for the Czech Government.

The following table sets out certain data in respect of CKA:

	As at the year ended 31 December		
	31 December 2003	31 December 2002	31 December 2001
	(CZK millions)		
Assets			
Cash and deposits with central banks.....	5	11	13
Due from banks.....	2,350	53,332	32,373
a) repayable on demand.....	25	63	81
b) other receivables	2,325	53,269	32,292
Due from customers	62,169	85,808	123,771
Debt securities	1,520	1,102	3,106
Shares, mutual shares and other interests.....	11,793	1,542	1,706
Participation interests with significant influence	4,300	4,411	3,888
Participation interests with controlling influence.....	665	563	–
Long-term intangible fixed assets.....	26	41	89
Long-term tangible fixed assets.....	791	935	1,723
Other assets.....	90,833	98,636	76,040
Prepayments and accrued income	6	6	8
Total assets	174,458	246,387	242,717
Liabilities			
Due to banks.....	94,637	112,739	114,256
Due to customers	8,083	30,314	29,320
a) repayable on demand.....	3,345	25,316	2,199
b) other receivables	4,738	4,998	27,121
Liabilities from debt securities.....	43,570	33,312	13,863
Other liabilities.....	7,011	2,487	9,219
Accruals and deferred income	115	105	27
Provisions.....	4,003	38,383	43,960
Share capital.....	5,950	5,950	5,950
Reserve funds and revenue reserves.....	22,976	26,004	29,321
Capital funds.....	6,205	76,527	54,449
Revaluation reserve	90	–	–
Accumulated losses from previous periods.....	–	–	(41,526)
Loss for the accounting period	(18,182)	(79,434)	(16,122)
Total liabilities	174,458	246,387	242,717

Source: 2003 Annual Report of CKA

CKA recorded a loss for the year 2003 in the amount of CZK 18.2 billion, which will be covered up to the amount of CZK 12.2 billion by CKA's reserve fund, by a payment of CZK 5.2 billion from the Ministry of Finance and by a payment from the NPF amounting to CZK 0.8 billion.

CKA's loss for the year 2002 of CZK 79,434 million was covered in part by CKA's reserve fund (CZK 3,021 million), and by a payment from the NPF of CZK 149 million. Currently, there are discussions underway between CKA's management and the Ministry of Finance as to how the remaining part of the loss for 2002, in the amount of CZK 76,264 million, will be covered; a one-off solution through the issuance of State bonds is being considered.

The losses incurred in 2001 and 2002 (including the accumulated loss recorded in 2001) were fully paid by 31 December 2003 and are fully reflected in the General Government debt and public finances.

The following table sets forth information about KOB's/CKA's losses according to the years in which the losses were incurred by KOB/CKA and the years in which they were covered by using the funds from the State Budget:

	Loss covered in						Prelim 2003	Forecast 2004
	1997	1998	1999	2000	2001	2002		
	(CZK billions)							
Loss generated in:								
-1996.....	5.1	—	—	—	—	—	—	—
-1997.....	—	10.4	—	—	—	—	—	—
-1998.....	—	—	—	14.4	—	—	—	—
-1999.....	—	—	—	—	24.0	12.1	—	—
-2000.....	—	—	—	—	3.6	—	—	—
-2001.....	—	—	—	—	—	33.2	18.6	—
-2002 (a part only).....	—	—	—	—	—	—	—	19.0
Total	5.1	10.4	0.0	14.4	27.6	45.3	18.6	19.0

Source: Czech Consolidation Agency, Ministry of Finance

The performance of CKA in future years will largely depend on the results of the realization of its remaining non-performing loans and other assets. Although CKA has created specific provisions in the past to reflect the generally poor quality of its assets, there is no assurance that the current level of provisioning will be sufficient to avoid additional losses in the future.

Under ESA 95 methodology, CKA forms part of the General Government. Therefore, the General Government's deficits and debt are directly affected by the overall performance of CKA. Pursuant to the fiscal accounting methodology used by the Czech Republic (GFS 86 methodology), however, CKA is not included in the consolidated General Government results and its performance therefore does not directly affect the General Government deficits in the current year, but only when State Budget funds are used to cover the relevant loss.

The Government has recently passed a resolution pursuant to which CKA should restructure approximately CZK 390 million of its claims against a Czech municipality that became insolvent. As part of the restructuring, it is anticipated that CKA would forgive up to CZK 300 million of its claims against the municipality. The Government has indicated that it may need to provide an aid to other indebted municipalities.

MONETARY AND FINANCIAL SYSTEM

Czech National Bank

Established in 1993, the CNB is the central bank of the Czech Republic, and the successor within the Czech Republic to Státní banka Československá, the central bank of the former CSFR. The CNB is constituted and operates as an independent institution, as set forth in the Czech Constitution.

The primary objective of the CNB is to ensure price stability as a prerequisite of balanced and long-term sustainable growth. Price stability thus takes precedence over exchange rate stability. The CNB is responsible for setting and implementing both monetary and foreign exchange policy. The CNB's power to determine monetary policy is not subject to any review or consent by the Government. The CNB also administers the official monetary reserves, regulates the banking sector and acts as banker to the Government.

The supreme governing body of the CNB is the Bank Board, consisting of the Governor, two Vice-Governors and four other senior officers of the CNB appointed by the President of the Czech Republic for a term of six years (Vice-Governors and other members of the Bank Board are appointed by the President, based on a recommendation from the Governor). The Bank Board sets monetary policy, determines the instruments for implementing that policy, and decides upon the fundamental monetary policy measures of the CNB and other fundamental measures. Board members, who may not hold other government positions, cannot normally be removed from office but may only serve two terms. The current CNB Governor was appointed in December 2000.

Monetary Policy

As set forth in the Czech Constitution and the Act on the Czech National Bank (the "CNB Act"), the CNB's primary monetary policy objective is to maintain price stability. Without prejudice to this primary objective, the CNB aims to support the general economic policies of the Government leading to sustainable economic growth.

The current monetary-policy regime of the central bank is based on direct inflation targeting. In March 2004, the CNB announced that the inflation target for the period beginning January 2006 is a year-on-year consumer price index (CPI) change of 3%. The CNB will at the same time endeavour to ensure that actual inflation out turn does not differ by more than one percentage point in either direction from this target. The inflation target will be in force continuously until the Czech Republic joins the Eurozone.

The declared inflation target of 3% follows smoothly on from the previous monetary policy of continuous band-targeting, which had been applied by the CNB since January 2002. The inflation-targeting band had consistently decreased from 3-5% in January 2002 to 2-4% in December 2005.

The inflation target was designed as a starting point for the future fulfilment of the convergence criteria and should correspond to the long-term inflation expectations of the financial markets. The inflation target has been set slightly above the price stability level declared by the ECB, which reflects the expectation of long-term real convergence of the Czech economy with the Eurozone average.

The CNB continues to regard its inflation targets as medium-term targets from which actual inflation may deviate temporarily. Such a deviation comes into consideration especially if the economy is hit by an "exogenous shock". If such a shock deflects expected inflation from the target, the CNB does not respond to the primary impacts of the shock. It will apply an exemption ("escape clause") from the obligation to hit the inflation target and accept the deviation of the inflation forecast from the target caused in this way. There can be a whole range of shocks which create room for applying such escape clauses. They include, for example, major deviations in world prices of energy raw materials or major deviations in agricultural producer prices. A specific type of exogenous shock comprises administrative measures that have strong price impacts, in particular, major changes in the structure or rates of indirect taxes and major changes in the segment of regulated prices.

The following table sets forth the principal annual interest rates as at the end of each of the four years ended on 31 December 2003:

	As at the year ended 31 December			
	2000	2001	2002	2003
		(%)		
Discount Rate.....	5.00	3.75	1.75	1.00
Lombard Rate.....	7.50	5.75	3.75	3.00
Repo rate (2 weeks)	5.25	4.75	2.75	2.00

Source: Czech National Bank

Exchange Rate Policy

In the early 1990s, political and economic reforms were accompanied by a series of devaluations. In October 1995, a new foreign exchange act was adopted, liberalising foreign exchange restrictions, introducing full current account convertibility and extending convertibility for capital account purposes. With this new law, the Czech Republic complied with all the requirements of Article VIII of the International Monetary Fund Agreement. Until 1997, the exchange rate of the Czech currency was pegged to a basket of currencies. The last change in this basket was made in 1993, when the Czech koruna was pegged to a basket comprising 65% Deutschmarks and 35% U.S. dollars. In 1997, the fixed exchange rate policy was replaced by a managed floating rate system.

The exchange rate is not a direct instrument of monetary policy. However, the CNB has used exchange rate interventions to curb any extreme movements in the exchange rate of the Czech currency in cases in which the CNB believed that the changes had not been justified by economic fundamentals. There has been no FX interventions from the CNB since October 2002.

The pressures on the appreciation of the Czech currency experienced in 2001 and 2002 led the CNB and the Government to agree on steps to slow the appreciation of the Koruna. These measures included, *inter alia*, the postponement of foreign-currency Government bond issuance; the use of foreign exchange privatisation revenues to repay the foreign commitments of the state and state institutions; the settlement of a portion of the privatisation sales in Czech koruna, borrowed from banks; the conversion of government foreign exchange revenues into Czech koruna at the CNB rate (i.e., off the market); and the lowering of monetary policy interest rates. The CNB has also entered into an agreement with the Government to have larger-level privatisation proceeds placed in a special privatisation account.

The following table sets forth the exchange rate of the Czech koruna against the EUR and U.S. dollar, as an average rate, during each of the four years ended on 31 December 2003:

	As at the year ended 31 December			
	2000	2001	2002	2003
CZK/EUR	35.61	34.08	30.81	31.84
CZK/USD.....	38.59	38.04	32.74	28.23

Source: CNB

Banker to the Government

The CNB acts as banker to the Czech Republic, providing cash management and accounting services. It keeps the accounts of the State Budget, State funds and State financial assets and liabilities. The CNB may also purchase government bonds or other securities underwritten by the Government provided, however, that it does not hold them for longer than one year. Under the CNB Act, the CNB may act on behalf of the Ministry of Finance in relation to the issue and servicing of State bonds and is required to keep a register of short-term securities maturing within one year.

Gold, Bank Notes and Coins

In addition to maintaining the foreign currency reserves, the CNB also holds gold reserves as part of its international reserves (See "Monetary and Financial System International Reserves"). The CNB has reported that it has reduced its level of gold reserves to an amount that is no longer significant, and that its policy going forward is to hold more liquid financial instruments. The CNB has the exclusive right to issue bank notes and coins in the Czech Republic and supervises the printing of notes, the minting of

coins and the general circulation of money. Its obligations in respect of notes issued are not required to be covered to any extent by gold or convertible currencies.

Other Activities

The CNB is responsible for preparing drafts of any legislation dealing with the Czech currency, the money market, the payments system and the role of the CNB. It is also required under the CNB Act to regulate the payment system among banks and the clearing of accounts between them, and to establish a banking information system.

International Reserves

The international reserves of the CNB increased substantially in 2002, due to strong privatisation inflows in foreign currency, which were absorbed by the CNB. At the end of 2003, gross international reserves stood at EUR 21.34 billion, equivalent to approximately 28.7% of the GDP for 2003.

The following table sets out the Czech Republic's international reserves for the years ended 31 December, 2001 to 2003:

	As at the year ended 31 December		
	2001	2002	2003
		(EUR billion)	
Reserves.....	16.40	22.61	21.34
% of GDP	24.1	31.0	28.7

Source: Czech National Bank

The active management of reserves investments results in further growth of international reserves assets, which is considered undesirable. The Board has stated that, in this situation, it is appropriate to implement a strategy to sell at least part of the reserves investments revenues on the market. These sales will act against the growth in the volume of sterilisation which represents the largest part of the CNB's liabilities. The sales of reserves investments revenues will be carried out gradually, in small volumes and if the market conditions (including liquidity, depth and trend changes) are considered appropriate.

Strategy of the Czech Republic with respect to ERM II

The strategy of the Czech Republic, with respect to its participation in the Exchange Rate Mechanism (ERM II) and the introduction of the Euro as the official Czech currency, was jointly prepared by the Czech National Bank, the Ministry of Finance and the Ministry of Industry and Trade and approved by the Government in 2003. The document summarises the starting points for the Czech Republic's integration into European monetary structures and discusses the positive effects and potential risks associated with joining the Eurozone. The document recommends that the Czech Republic join the Euro area as soon as economic conditions allow, rather than as soon as possible.

By joining the EU, the Czech Republic automatically participates in the third stage of EMU with the status of "Member State with a derogation" concerning adoption of the Euro. Under the EU legislation, prior to adopting the Euro, the Czech Republic must have fulfilled the following convergence criteria ("Maastricht criteria"):

- price stability – a member state maintains a sustainable price performance and achieves an average rate of inflation (measured over a period of one year before the examination) that does not exceed, by more than 1.5 percentage points, the average rate of inflation of the three member states which perform the best in terms of price stability;
- long-term interest rates – a member state has had an average nominal long-term interest rate (measured over a period of one year before the examination) that does not exceed, by more than 2 percentage points, that of, at most, the three best performing Member States in terms of price stability;
- the government budgetary position – a member state has a ratio of planned or actual government deficit to GDP that does not exceed 3%, unless either (i) the ratio has declined substantially and continuously and reached a level that comes close to the reference value, or, alternatively (ii) the excess of the reference value is only exceptional and temporary and the ratio remains close to the reference value;

- government debt – a member state has a ratio of government debt to GDP that does not exceed 60%, unless the ratio is sufficiently diminishing and approaching the reference value at a satisfactory pace; and
- exchange rate – requires participation for at least two years in the ERM II and observance of the normal fluctuation margins close to central parity provided for by the mechanism for at least two years.

The convergence required for entering the Euro area is formally assessed annually and the final decision is subsequently made by a summit of EU Member States acting on the recommendation of the ECOFIN Council.

The Czech Republic has publicly stated that it does not intend to stay in the ERM II for a period longer than the required minimum of two years (required by the exchange rate condition) and, accordingly, that it anticipates entering the ERM II only when conditions have been established which enable it to introduce the Euro at the time of the assessment of the exchange-rate criterion, i.e., two years after joining the ERM II.

As the CNB and the Government do not expect the Czech Republic to have met all the Maastricht criteria by 2006, a decision was made that the Czech Republic would stay outside the ERM II as of the date of the country's accession to the EU. According to statements made by the CNB and the Government, the Czech Republic is not expected to adopt the Euro prior to 2009 – 2010.

Czech Banking System

General

The Czech banking sector consists of 35 banks (17 of which are controlled by foreign persons or entities), including 9 branches of foreign banks. Foreign investors have secured a dominant role in the sector's capital, with a share of around 85% as at 31 December 2003, which is 3 percentage points higher compared to the previous year. Foreign capital effectively manages around 97% of the total assets in the banking sector. The planned privatisation of the commercial banks was completed in 2002. The state has retained stakes in the banking institutions established only in order to support exports and small and medium-sized enterprises.

The total assets of the banking sector rose slightly (by less than 2%) in 2003, reaching CZK 2,529 billion. Primary deposits amounted to approximately 77% of total liabilities in December 2003, which represents an increase of 3.4% by volume, compared to the previous year. The banking market is significantly concentrated. One group of four large banks account for 63% of client loans and 68% of primary deposits.

Total loans recorded a year-on-year growth of almost 10%, accounting for around 40% of total assets at the end of 2003. The growth of loans is mainly attributable to household loans (most notably housing loans and consumer credit), which grew by 34% in contrast with a slight decrease in corporate lending (a year-on-year decline of 1%). The share of household loans compared to total loans nevertheless remains relatively small, being approximately 22% (of which 71% represents housing loans and 29% represents consumer credit).

The decline in corporate lending is partly due to stricter creditworthiness requirements applied by the banks. This approach has led to a decrease in low-quality assets in both absolute and relative terms. During the course of 2003, the ratio of non-performing loans to total loans fell below 5%. The liquidity of the sector is high as quick assets account for around 36% of total assets.

The interbank market in the Czech Republic is relatively well developed. Roughly half of all interbank transactions are undertaken with foreign partners (90% of them being based on EU countries), although non-resident assets account for less than 19% of total assets (60% being attributable to the EU). Foreign exchange assets represent only around 16%.

Banks are becoming increasingly active in the derivatives area. At the end of 2003, the nominal volume of these transactions exceeded 130% of total assets. Broken down by underlying asset, interest-rate derivatives made up around 70% of the total, and FX derivatives made up 30%. As regards transaction type, swaps accounted for 56% of the total, forwards for 41%, and options for around 4%.

In 2003, the banking sector turned in a profit of approximately CZK 30 billion (based on unaudited preliminary data), which is roughly the same result as in 2002. The average return on assets in the Czech banking sector reached 1.2% in 2003; return on equity was approximately 24%. Preliminary results show

that only two banks recorded losses in 2003. Total profit from financial activities was derived mainly from interest income (approximately 60%). Profit from fees and commissions has grown consistently and reached approximately 30% in 2003.

Average capital adequacy exceeded 14% at the end of 2003. Most banks had ratios of more than 12% (only four banks fell below this threshold).

Legal Issues concerning the Establishment and Enforcement of Creditor's Rights

Despite substantive legislative developments in the past years, certain legal obstacles continue to prevent the establishment of a stable system of secured lending in the Czech Republic. The most burdensome obstacles include the lengthy enforcement proceedings in court that secure creditors' rights, inefficient insolvency proceedings and lengthy, administratively demanding registration requirements for certain business information in public registries.

Lengthy Court Proceedings. Although legislative steps have gradually been taken to improve Czech civil procedures and the court system, enforcing one's rights effectively through the Czech courts continues to be a difficult and time-consuming process. Specifically, it is not unusual for the judicial enforcement of a creditor's rights to last several years. Moreover, the position of a creditor in court proceedings may be relatively weak, since the legal tools available to prevent the debtor from evading payment of its debts from its assets, are not used effectively.

Inefficient Insolvency Proceedings. The main problem with existing Czech insolvency legislation is that it is generally not able to effectively address a debtor's insolvency in any way other than through liquidation. In contrast to many modern foreign jurisdiction insolvency laws, under the Czech Bankruptcy and Composition Act, it is not possible to reorganize the assets of a debtor by reorganizing the debtor's enterprise in accordance with a court-approved plan, while allowing the debtor to continue to operate its business, which could ultimately lead to a better satisfaction of the debtor's creditors (compared to a sale of assets). The relevant bankrupt's estate may only be realised through a sale carried out by the bankruptcy trustee and subject to the approval of the bankruptcy court.

Creditors with secured claims have a prior claim to the property that is the subject of their secured claim. However, the distribution of proceeds from a realisation of the property is subject to the approval of the bankruptcy court, which may cause considerable delays. In accordance with the Czech Bankruptcy and Composition Act, the rights of secured creditors to separate satisfaction are limited to 70% of the proceeds of the sale of the relevant part of the bankrupt's assets by the administrator, after deduction of costs relating to the maintenance, management and sale of the collateral.

The Government is working for almost two years on a new insolvency act which intended to improve the position of creditors. Although the draft bill is expected to be submitted to Parliament shortly, the timing of the introduction and the final form of this new insolvency law is still uncertain.

Lengthy and Burdensome Registrations. Numerous kinds of legal and business information are required to be registered in various public registries in the Czech Republic (e.g., the Commercial Registry, which is the main business registry in the Czech Republic, the Land Registry, the Register of Pledges, etc.) on which, generally, third parties may rely. Moreover, certain rights and obligations may only be created upon their actual registration in the relevant public registry (e.g., the incorporation of a legal entity, the establishment of certain kinds of security, the transfer of certain legal titles, etc.).

Unfortunately, the process of registering certain information or creating certain rights and obligations by the act of registration, which is usually important for commercial entities, is often a lengthy and bureaucratic one. Since the registration authorities are usually not bound by any specific time limits, it may, in particular cases, take several weeks or months to effect a registration.

Currently, the Lower House of Parliament is debating a new law which would make the registration procedure in the Commercial Registry less formal and more flexible. However, the draft bill does not suggest that any changes should be made to the current registration procedures applicable for the Land Registry, the Register of Pledges, or other public registries.

Banking Supervision

The CNB is responsible for the general supervision of the banking system and, as part of its responsibilities, carries out inspections to establish whether banks operating in the Czech Republic are acting in compliance with the banking licences granted to them. The CNB also regulates the capital adequacy and liquidity of such banks. In addition, it supervises their credit policies and controls their

dealings in the foreign exchange market. All banks in the Czech Republic are required to maintain an account with the CNB.

The CNB is the licensing authority for all new banks as well as for any foreign banks wishing to establish operations in the Czech Republic. According to the single passport rule adopted by the EU law, banks with their registered seat in the member states of the European union may establish operations in the Czech Republic without the need to obtain a licence from the CNB. Generally, such foreign banks remain under the supervision of their domestic bank authorities.

Deposit insurance

Czech banks and branches of foreign banks are required to maintain adequate insurance from a deposit insurance fund administered by the CNB (the “Fund”). All deposits, including interest, in both Czech or foreign currency, are insured. Up to 90% of the aggregate deposit is insured, up to EUR 25,000, for any one depositor at any particular bank. The annual contribution of each bank or branch of a foreign bank into the Fund amounts to 0.1% of the average of total deposits of insured accounts, including interest, for the 12 months preceding January 31 of each year. Compensation for an insured deposit is payable after written confirmation from the CNB of the bank’s inability to discharge its obligations to the depositor or, in case of a branch of a foreign bank, after similar confirmation from the bank’s relevant supervisory authority.

Banking Regulation

The banks operating in the Czech Republic are regulated by the CNB Act, the Czech Banking Act and regulations issued by the CNB. To the extent that banks act as securities dealers, they are also regulated by rules applicable to securities dealers and are subject to a supervision of the Securities Commission. In an effort to continue to harmonise the Czech banking system with that of the EU, Parliament adopted a substantial amendment to the Czech Banking Act in 2002. This Amendment (introducing, *inter alia*, the concept of banking supervision on a consolidated basis) came into force on May 1, 2002 with the exception of certain provisions that came into force as of the Czech Republic’s accession to the EU on May 1, 2004. In an effort to modernise the Czech banking system in accordance with international standards, the CNB has issued a number of regulations relating to: (i) liquidity and statutory minimum reserves; (ii) capital adequacy; (iii) credit exposure; and (iv) the classification of credit exposures and the creation of provisioning for such loans. These regulations also apply to the branch offices of foreign banks to the extent provided in each regulation.

Integration of Authorities Supervising the Financial Market

The supervisory authority over Czech financial markets is currently divided among four agencies – banking supervision is performed by the Czech National Bank, supervision over the capital market is performed by the Czech Securities Commission, supervision over insurance companies and pension funds is performed by the Ministry of Finance, and savings and credit unions are supervised by the Credit Union Authority. In 1993, these four supervisory authorities set up a special Committee for coordination of supervision over the financial market in order to analyze the possibilities of integration of the supervisory function carried out by these institutions, into a single supervisory authority. The Committee recognised that there are reasons for gradual integration of the present four supervisors into a single authority and recommended that the integration be implemented in steps – first to consolidate the Credit Union Authority and banking supervision (in 2005) and subsequently to consolidate the supervision over insurance companies and pension funds with supervision over the capital market (around 2006). This would result in a two-pillar model, which would then be finally consolidated in a single integrated supervisory authority by the time of accession of the Czech Republic to the EMU.

Czech Capital Markets

The Czech capital markets are primarily governed by the Capital Markets Act, the Securities Act, the Bonds Act, the Securities Commission Act, the Collective Investment Act, and regulations issued mainly by the Czech Securities Commission. Most of the relevant laws were significantly amended in the spring of 2004 in order to harmonise Czech capital markets law with the requirements of the European Union. As of May 1, 2004, the legal framework established by these acts and regulations substantially implements all relevant EU directives regulating capital markets.

Czech Securities Commission

The Czech Securities Commission, together with the Ministry of Finance, is responsible for the regulation and supervision of the Czech capital markets. The Czech Securities Commission was established in 1998, when the Securities Commission Act became effective. The governing body of the Securities Commission is the Presidium, which consists of the Chairman and four other members. The Chairman and the other members of the Presidium are appointed by the Czech President, based on proposals made by the Czech Government. The Chairman of the Securities Commission presides over the Presidium, directs its work and acts on its behalf.

The powers of the Securities Commission include: (i) the supervision of securities dealers, investment companies, investment funds, unit trusts, pension funds, clearing houses, stock exchanges and certain other participants in the capital markets (consisting primarily of monitoring and enforcing compliance with applicable capital market regulations); (ii) the licensing of securities dealers, investment companies, investment funds, pension funds, clearing houses, stock exchanges and certain other participants in the capital markets; (iii) monitoring compliance by issuers of publicly tradable securities with their reporting and information disclosure duties; (iv) the supervision of take-over bids; and (v) monitoring compliance with insider trading restrictions. In certain cases stipulated by relevant acts, the Czech Securities Commission is authorised to issue regulations to implement provisions of those acts. As private enforcement of securities laws in the Czech Republic through Czech courts is often very difficult and time consuming, monitoring of capital markets remains largely in the hands of the Securities Commission.

To enforce the laws regulating the Czech capital markets, the Securities Commission may impose remedial measures and issue fines up to CZK 100 million. In emergency situations, the Czech Securities Commission may, among other things, impose preliminary injunctions to block transfers of securities or funds of persons subject to administrative proceedings conducted by the Securities Commission. The decisions of the Czech Securities Commission may be appealed; however, an appeal against revocation of the relevant licence required under special legislation (such as securities brokerage licence) does not have suspensory effect.

Securities may be accepted for trading on a public market (or publicly offered) only if all the conditions applicable for the securities and the issuer thereof under the Capital Markets Act are fulfilled and the Securities Commission has approved the required prospectus (or a condensed prospectus in certain cases) for such securities.

The prospectus must contain specified information, including financial information for the preceding three years, a description of the issuer's business activities and a description of the securities to be publicly traded or offered. The organiser of a public market, i.e., the stock exchange, decides on the admission of the securities for trading on its public market, subject to conditions stipulated by the Capital Markets Act, and has the right to apply further conditions for the acceptance of securities for trading on the market.

Guarantee Fund

Securities dealers in the Czech Republic are required to maintain adequate insurance from a guarantee fund administered by the Czech Securities Commission (the "Guarantee Fund"). Each securities dealer is required to make a monthly contribution in the amount of 0.01% of the asset value of its clients, determined as at end of that particular month. The annual contribution has to be at least CZK 10,000. When the Securities Commission declares that a securities dealer is unable to discharge its obligations, its clients' deposits are insured up to 90% of the aggregate deposit, up to an amount in CZK equivalent to EUR 20,000 per each client. Some customers, however, such as professional investors, are excluded from the compensation scheme.

Prague Stock Exchange

The Prague Stock Exchange ("PSE") commenced operations in April 1993 after a 54-year moratorium. The PSE is the principal public securities market in the Czech Republic on which shares, bonds and unit certificates are traded.

The PSE is a private organisation comprising 28 members as of April 30, 2004. Only licensed securities dealers who are members of the PSE are permitted to trade on the PSE, which is regulated by the Capital Markets Act and its internal rules.

As at 30 April 2004, equity securities representing 62 companies were registered for trading on the PSE, of which, equity securities representing five companies were registered for trading in the Main Market, 32

in the Secondary Market, 25 in the Free Market and none in the New Market. The total equity market capitalisation at such date with respect to companies registered for trading in the Main Market and all companies registered for trading on the PSE was approximately CZK 592,067,200,000 and CZK 781,431,700,000, respectively.

Trading. Prompt trades can be divided into automatic trades, block trades and SPAD trades with the participation of market makers.

Automatic trades (order-driven system) and SPAD trades (price-driven system) are concluded through the PSE's trading system and are guaranteed through the exchange guarantee fund, securing obligations and covering risks resulting from PSE trades and their settlement. SPAD is based on the exploitation of the function performed by market makers (MM). During the open phase, all MMs are obliged to publish their quotations (buying and selling prices) for issues for which they act as MM. Based on these quotations, the best quotation (that is the highest buying price and the lowest selling price) is set for each issue. It is only possible to contract trades within the allowable spread, presently defined by the best quotation expanded by 0.5% up or down. There are two types of automatic trades: auction and continual. Within the auction regime, priority is given to the order with the higher buying price or lower selling price. Under the continual regime, trades are contracted on the basis of the continual input of orders for the purchase and sale of securities. If orders with the same price are entered, priority is given to the order entered earlier.

Block trades are effected in two ways: between PSE members and between a PSE member and a non-member. The price for a contracted trade is neither limited nor tied to the official price of a security. Block trades are effected outside the PSE system but are then registered by PSE members within the system. Guarantees do not apply to these trades.

Settlement. Univyc, a. s. ("Univyc"), a wholly-owned subsidiary of the PSE, is licensed by the Czech Securities Commission to settle trades on the PSE. The manner in which trades are settled depends on whether the securities are in a certificated or book-entry form. The majority of securities traded on the PSE are in a book-entry form and are registered at the Securities Centre, a computerised register of all Czech book-entry form securities (described below). Settlement of trades on the PSE is generally effected on the third business day following the trading day. Univyc maintains accounts of the members of the PSE and a number of accounts of non-members of the PSE and records the securities traded. Univyc ensures cash settlement through the Clearing Centre of the Czech National Bank and the delivery of the securities in a book-entry form to the purchaser on its account at the Securities Centre, or on its account with Univyc, where applicable.

The members of the PSE have created the Guarantee Fund of the Prague Stock Exchange, administered by Univyc to guarantee the fulfilment of the obligations of members of the PSE arising from automatic trades and the trades in the SPAD system.

RM System

The RM System is a privately owned entity in which securities trading takes place through a computerised bid and offer matching system that operates every business day. Trades through the RM System may be placed either by a securities broker or directly by an investor. Trading on the RM System is conducted through a network of 59 designated locations. The auction price varies during the course of the day according to the actual bids and offers. Settlement takes place on the same trading day. Book-entry securities traded on the RM System are settled through the Securities Centre.

OTC Market

In addition to the regulated securities markets (the PSE and RM System), securities (mainly debt securities) are also traded on the over-the-counter ("OTC") market and settled directly at the Securities Centre. The Securities Centre publishes the volumes and prices of the securities traded on the OTC market on a weekly basis.

Securities Centre

Most securities traded on the PSE are in book-entry form, registered at the Securities Centre, which is the computerised book-entry register for most Czech book-entry securities. Short-term debt securities may also be registered at the Czech National Bank registration and trading system. The Securities Centre maintains two registers, one containing a list of all securities holders, the other a list of all issuers and

their outstanding securities. Transfers of securities are effected upon registration of such transfer at the Securities Centre on the basis of an instruction or order to register the transfer of the particular security.

Collective Investment

On May 1, 2004, a new Collective Investment Act became effective and substituted former Investment Companies Act of 1992. The Collective Investment Act regulates collective investment and activities of investment funds and investment companies. The Czech Securities Commission supervises compliance with the Collective Investment Act and is empowered to impose sanctions for non-compliance, including fines and various remedial measures.

PUBLIC FINANCE

General Government Account

The public finance sector in the Czech Republic comprises the Central Government and Local Government, which together are referred to as the General Government. The Central Government Budget consists of the State Budget (including National Fund operations), Extra-Budgetary Funds and Social Security Funds (which is now limited to public health insurance). The fiscal year applicable to the Central Government Units and Local Governments is the calendar year.

Methodology

Unless otherwise indicated, all data in this section are presented in accordance with the methodology of the International Monetary Fund (as set forth in the Manual on Government Finance Statistics, IMF 1986, hereinafter the “GFS 86 methodology”), which is the methodology currently used by the Government.

In order to comply with the accession obligations of the Czech Republic, the Czech Republic has started to implement procedures that should enable it to produce government sector data on the basis of ESA 95 methodology. While the Government currently does not anticipate using ESA 95 methodology for its fiscal accounting, the Czech Statistical Office is responsible for compiling the government sector data on the basis of ESA 95 methodology (at present, however, such data are only available in less detailed formats and are released with significant delays).

The methodological changes carried out by the Czech Statistical Office (on the basis of Eurostat recommendations) to comply with ESA 95 methodology significantly affect the public finance results and budgets of the Czech Republic. Generally, ESA 95 methodology monitors revenues and expenditures on an accrual basis, whereas GFS methodology monitors revenues and expenditures on a cash basis. The biggest effect of the adopted methodological changes on the data presented on the public finance sector derives from (i) the reclassification of exercised state guarantees as government debt and increases of the deficit, and (ii) the extension of the definition of the general government sector (i.e., the inclusion of the Railway Infrastructure Administration and other quasi-governmental institutions).

General Government Budget Overview

The following table sets forth main fiscal trends in the Czech Republic (under GFS 86 methodology, except where noted otherwise) as at and for the four years ended December 31, 2003, and the budget for 2004:

	2000	2001	2002	2003	Budget 2004
<i>(CKZ billions, except where noted otherwise)</i>					
Central Government Budget:					
State Budget surplus (deficit).....	(51.8)	(66.7)	(45.9)	(107.4)	(113.9)
Revenues incl. Grants.....	613.3	618.8	676.2	704.2	756.1
Expenditures and net lending	665.2	685.5	722.2	811.5	870
Extra-Budgetary Funds surplus (deficit).....	(9.4)	24.3	40.2	(20.5)	(41.3)
Revenues	15.5	59.7	73.1	76.6	56.6
Expenditures and net lending	24.9	35.4	32.9	97.1	98
Social Security Funds surplus (deficit)	2.1	1.4	(1.2)	0.1	(0.3)
Revenues	117.7	132.3	136.0	147.6	153
Expenditures and net lending	115.6	130.8	137.3	147.5	153.2
Local Government Budgets:					
Local Government Budgets surplus (deficit).....	(2.5)	(11.2)	(4.3)	(2.9)	(6.3)
Revenues	181.8	192.4	236.6	298.9	292.3
Expenditures and net lending	184.3	203.6	240.9	301.9	298.6
General Government Budget, after consolidation,					
surplus (deficit)	(62.0)	(52.2)	(11.7)	(130.1)	(161.3)
Share of GDP in %	(3.1)	(2.4)	(0.5)	(5.4)	(6.3)
General Government Budget, after consolidation and excluding net lending, surplus (deficit)	(86.9)	(111.0)	(153.4)	(130.3)	(180.4)
Share of GDP in %	(4.4)	(5.1)	(6.7)	(5.4)	(7.0)
<i>General Government surplus (deficit) under ESA</i>					
95 methodology	(96.7)	(149.8)	(154.6)	(328.5)	(144.1)
Share of GDP in %	(4.9)	(6.9)	(6.8)	(13.6)	(5.6)

Source: Ministry of Finance

In 2003, the consolidated General Government Budget recorded a deficit of approximately CZK 130 billion, representing 5.4% of the GDP. Under ESA 95 methodology, the deficit of the general government sector reached CZK 328.5 billion, representing 13.6 % of GDP in 2003. The difference between the results reported under GFS 86 methodology and ESA 95 methodology, and the steep increase of the deficit under ESA 95 methodology compared to previous years is largely attributable to the imputation of exercised State guarantees to the State Budget in 2003, under ESA 95 methodology. ESA 95 methodology requires that the whole amount of a state guarantee is included in the State Budget as a capital transfer, if and when the guarantee is exercised for the first time (irrespective of whether the payment is required in respect of the whole amount of the guarantee, any part of the guarantee or interest only). This one-time measure resulted in a rise in expenditure equal to the total amount of the guarantees in questions, irrespective of when the remaining parts of the guarantees are or may be called for payment. The above-mentioned re-classification of guarantees accounted for as much as 7.7 % of GDP (under ESA 95 methodology) in 2003. If adjusted by the one-off impact of the reclassification of exercised state guarantees, the deficits (under ESA 95 methodology) would amount to 6.0 % of GDP in 2003. The remaining difference between the results presented under ESA 95 methodology and GFS 86 methodology, in the amount of 0.6% of GDP, can be explained by differences in the definition of 'General Government' (for instance, CKA forms part of the General Government under ESA 95 methodology, but not under GFS 86 methodology) and time differences resulting from the use of the cash-based method (GFS 86 methodology) and the accrual method (ESA 95 methodology).

2003 State Budget

Central Government contributes most to the overall budgetary deficit, since it is in charge of carrying out the financially most demanding spending programs (e.g., social benefits, major infrastructure investments) and it also absorbs the financial impact of operations linked to the transformation of the Czech economy (such as the operations of transformation institutions and state guarantees to the banking sector).

The following tables set forth, by category, the actual revenues and expenditures of the State Budget (excluding the operations of the National Fund) in 2000 to 2003, together with budgeted revenues and expenditures for 2004:

	2000	2001	2002	Prelimin. 2003	Budget 2004
	(CZK billions)				
Revenues					
Tax revenues	557.7	597.8	627.0	668.5	718.6
Income tax	87.1	147.4	159.0	172.9	180.1
Social security contributions	222.2	242.3	258.5	273.1	292.6
Property taxes	6.0	6.4	7.9	8.8	11.8
Local taxes on goods and services					
Value added tax	145.9	121.2	118.4	125.7	140.2
Excise tax	70.9	65.8	68.6	72.8	84.2
Customs duties	13.6	10.0	9.8	10.3	3.9
Other tax revenue	1.6	0.1	0.1	0.3	0.4
Non-tax revenues ⁽¹⁾	11.6	16.6	19.9	18.1	10.6
Sub-total (Current revenues)	1.3	1.4	1.5	686.6	729.2
Capital revenues	0.4	0.5	1.4	0.5	1.2
Grants	11.8	1.1	25.2	4.6	12.7
Repayments	4.5	8.5	23.2	3.5	10.9
Total revenues	<u>581.4</u>	<u>616.0</u>	<u>673.6</u>	<u>691.8</u>	<u>743.1</u>
Expenditures					
Current expenditures	575.7	641.8	695.7	740.4	790.2
Expenditures on goods and services	48.5	56.5	63.9	72.3	70.5
Interest payments ⁽¹⁾	1.6	16.9	12.8	17.9	27.4
Subsidies and other current transfers	455.4	487.7	531.9	570.9	611.7
Transfers to central level government	50.6	34.1	34.0	39.4	41.1
Subsidies	99.8	104.5	111.5	89.0	102.6
– of which to non-financial public enterprises	66.9	51.1	41.7	36.1	35.8
Transfers to other level of government	30.3	52.8	68.4	111.2	107.9
Transfers to nonprofit institutions and households	272.0	293.0	315.2	329.2	339.6
Transfers Abroad	2.7	3.2	2.9	2.2	20.5
Capital expenditure	51.6	40.0	41.2	47.1	60.2
Fixed capital assets, stocks, and land	14.3	12.9	10.3	10.9	15.7
Capital transfers	35.5	25.4	29.7	34.3	42.8
Domestic	35.5	25.4	29.7	34.3	42.8
To central level government	0.0	0.0	0.0	0.2	0.0
To other levels of government	13.8	10.0	11.3	14.3	16.0
To non-financial enterprises	13.9	11.0	13.6	14.1	20.4
Abroad	0.0	0.0	0.0	0.0	0.0
Total expenditure	<u>627.3</u>	<u>681.8</u>	<u>736.9</u>	<u>787.5</u>	<u>850.4</u>
Lending	4.7	10.4	5.6	16.9	18.7
Domestic	4.4	10.2	5.5	16.8	18.7
Abroad	0.3	0.2	0.1	0.0	0.0
Total expenditure including lending	<u>632.0</u>	<u>692.2</u>	<u>742.5</u>	<u>804.3</u>	<u>869.1</u>
Surplus (deficit) including net lending	(46.1)	(67.7)	(45.7)	(109.1)	(115.0)
as a % of GDP	(2.3)	(3.1)	(2.0)	(4.5)	(4.5)
Surplus (deficit) excluding net lending	(45.8)	(65.8)	(63.3)	(95.7)	(107.2)
as a % of GDP	(2.3)	(3.0)	(2.8)	(4.0)	(4.2)

Source: Ministry of Finance (Macroeconomic forecast, April 2004)

(1) In 2003, the non-tax revenues under GFS 1986 exclude the amount of premiums from the issuance of state bonds, totalling CZK 4.4 billion; the same amount is deducted from the expenditure side (interest payable). With respect to 2004, they are no longer budgeted.

State Budget 2004

The 2004 State Budget was approved by Parliament on 3 December 2003 and came into effect on 1 January 2004. The revenues for 2004 are budgeted at CZK 754.1 billion and expenditures at CZK 869.4 billion (the expenditures were originally budgeted to reach CZK 869.1 billion, but were subsequently increased by CZK 0.35 billion to reach approximately CZK 869.4 billion), resulting in a budgeted deficit of CZK 115.3 billion.

For the four months ending 30 April 2004, revenues amounted to CZK 244.0 billion (representing 32.4% of the total budgeted revenues for 2004) and expenditures stood at CZK 282.1 billion (representing 32.4% of the total budgeted expenditures for 2004), resulting in a deficit of CZK 38.1 billion (compared to a CZK 64.5 billion deficit recorded for the same period in 2003).

The results for the four months ending 30 April 2004 were notably influenced by the increased collection of VAT and excise taxes, which reached 35.5% of the total budgeted collection of these taxes for 2004 (exceeding the four-month pro rata amount of the total budgeted collection of these taxes for 2004 by CZK 4.7 billion).

As part of the second stage of the Public Finance Reform (See section entitled “Public Finance Reform” below), Parliament approved amendments to the VAT law, effective from 1 May 2004. These changes were designed to further harmonize the structure of the VAT rates with that of the other EU Member States and mainly consisted of a decrease in the standard rate from 22% to 19% and the application of the standard rate to some of the goods and services that had been subject to the reduced rate (5%). The above changes have not been reflected in the current State Budget and, according to estimates of the Ministry of Finance, could have a positive impact on the revenues of the State Budget of up to CZK 9 billion. On the other hand, the Government has decided to make certain exceptional one-off social payments to pensioners and families with children to moderate the immediate impact of the changes in VAT tax rates. Accordingly, with effect from 1 June 2004, pensioners will generally each be eligible to receive an exceptional pension supplement of CZK 1,000 and families with children, fulfilling certain conditions, will be entitled to receive a one-time contribution payment of CZK 2,000 per child. These additional social payments, payable in 2004, have not been reflected in the current State Budget for 2004. However, according to estimates of the Ministry of Finance, the combined effect of these additional social payments and the above-mentioned changes in the VAT law on the 2004 State Budget should be neutral.

Relations with EU Budget

Starting from May 2004, the Czech Republic, as a Member State of the EU, is obliged to make annual payments to the EU budget on a basis comparable to that of other EU Member States. Overall, it is expected that approximately EUR 2.57 billion will be paid by the Czech Republic into the EU budget over the first three years following accession, including EUR 544 million in 2004. Payments by the Czech Republic will be partly offset by budget compensation payments from EU to the Czech Republic in the aggregate amount of EUR 840 million over the first three years, including EUR 332 million in 2004.

In addition to budget compensation payments, the Czech Republic is eligible to receive payments from preaccession funds (Phare, Ispa, Sapard) and obtain additional payments from structural and cohesion funds and agricultural funds. The actual amount of payments obtained from these sources will, however, also depend on the Czech Republic having a sufficient number of viable projects, complying with the Convergence Programme and securing the sufficient funds from the State Budget to cover co-payments.

Taking into account the availability of the above funds, the Ministry of Finance of the Czech Republic has stated that it anticipates that it may be a net recipient, vis-à-vis the EU budget, of up to EUR 450 million in 2004 and of up to EUR 1.3 billion during the period from 2004 to 2006 (assuming the use of approximately 70% of the amounts available under the funds, including approximately 50% in 2004).

Public Finance Reform

The Czech Republic's current levels of fiscal deficits pose an obstacle to compliance with the EU Maastricht convergence criteria. In order to restore State finances to a sound fiscal position and to bring the structure of the Government revenues and expenditures closer to that of other EU countries, the Government has adopted a strategy of public finance consolidation that is designed to achieve a gradual reduction in the budget deficit. The goal of this strategy is to reduce the General Government deficit (both under the GFS 86 and ESA 95 methodologies) to below 4.0% of GDP in 2006 and below 3.5% of GDP in 2007. Public finance reform has been laid out in two stages, as described below.

The measures approved by the Government as part of the first stage of the reform focused mainly on raising tax revenues and restraining the growth of social transfers and government consumption. The measures currently contemplated by the Government for the second stage of the reform process focus on the stimulation of economic growth, in particular by strengthening incentives for higher labour participation, and by tax enhancements (such as the shortening of depreciation periods). Most of the measures contemplated by the Government as part of the reform require an act of the Parliament in order to be implemented. Therefore, the ability of the Government to carry out the public finance reform is dependent on political support from Parliament.

In the second half of 2003, Parliament passed a number of laws to implement the first stage of the public finance reform. These included, most importantly:

On the revenue side:

- effective from 1 January 2004, the VAT rate for certain goods and services was changed from the reduced rate (5%) to the standard rate (22%) in order to achieve the alignment of VAT rates with those applicable in the EU; the standard rate was subsequently decreased to 19% effective from 1 May 2004;
- the increase of excise duties on certain commodities where Czech rates were lower than the minimum rates applied in the EU (this included the increase of excise duties on fuels effective from 1 January 2004 and the increase of excise duties on certain types of cigarettes, phased in by 31 December 2006);
- the reduction of corporate income tax rate to 28% from 1 January 2004, 26% from 1 January 2005, and finally to 24% from 1 January 2006;
- an amendment to personal income tax rules, requiring that self-employed persons pay at least the minimum amount of tax corresponding to a notional income of 50 percent of the average wage; and
- a gradual rise in the social security assessment base of self-employed individuals during a phase-in period ending in 2006.

On the expenditure side:

- structure changes of the pension system (restricting early retirement schemes, gradual increases in the statutory retirement age, and lower indexation of pension benefits);
- reduction in sickness benefits; and
- abolition of transportation allowances.

The measures approved by the Government for the first stage of the public finance reform also include a plan to decrease the number of employees at the level of Central Government by 6% during the period from 2004 to 2006, reduce state subsidies provided to housing savings schemes, reduce military spending and administrative costs of ministries.

Currently, the second stage of public finance reform is being prepared, which is aimed at promoting economic growth and strengthening the long-term sustainability of public finances. The proposed measures include, most importantly, the shortening of depreciation periods, and the increase in tax-deductible allowances for financial donations in the area of research and development.

In connection with these implemented and proposed tax and spending reforms, the Government has also decided to introduce fiscal targeting in the form of binding medium-term expenditure ceilings; a legislative proposal to Parliament to amend the Budgetary Rules Act has accordingly already been submitted. The introduction of medium-term expenditure ceilings is designed to strengthen the medium-term orientation of the budgetary process and to encourage fiscal discipline.

Sustainability of Public Finance

National authorities and international organisations have produced demographic projections that forecast a rapid increase in the proportion of elderly people in the Czech Republic over the next fifty years. Although the Czech Republic currently belongs among those countries having relatively young population, when compared to the average age in the 15 “old” EU Member States, its share of the elderly will likely substantially exceed the EU-15 average within the next fifty years, as the pace at which its population is ageing, is one of the fastest, when compared with that of the EU-15’s.

Unfavourable trends outlined by these demographic projections led the Government (in addition to the measures adopted or proposed as part of the public finance reform) to initiate discussions across the parliamentary spectrum on thorough pension reform. This resulted in an agreement to establish an expert committee in April 2004, which will assess various pension reform proposals. Reform suggestions cover structural changes to the current benefit system, a transition towards a defined contribution system financed on a “pay-as-you-go” basis, and the option of a partial, voluntary re-allocation of individual contributions into private pension funds.

Similarly to the pension system, the Czech health care system also threatens the long-term sustainability of Czech public finances. Although a number of short-term stabilising measures were put in place in relation to the health care sector, comprehensive health care reform is also planned.

GENERAL GOVERNMENT DEBT

General Government Debt

The General Government debt has steadily grown for the past few years, reaching CZK 554 billion at the end of 2003, representing 23% of GDP (an increase of 3.5% of GDP against 2002).

Under ESA 95 methodology, however, the General Government debt reached 39.7% of GDP in 2003, compared to 30.6% in the previous year. The steep increase in the level of General Government debt in 2003 (both in absolute numbers and as a share of GDP) is largely attributable to changes in the classification of issued state guarantees, which account for approximately 10% of GDP.

As the highest deficit is run up by Central Government, its debt accounts for the largest portion (93% under ESA 95 methodology) of total debt. The rest is made up almost exclusively by the debt of Local Governments.

The following table sets forth the composition of general government debt as at and for the five years ended 31 December 2004:

	As at and for the year ended December 31				
	2000	2001	2002	2003	Forecast 2004
	<i>(CZK billions, except otherwise noted)</i>				
State Debt (consolidated)	289.3	345.0	395.9	493.2	606.7
as of GDP	14.6	15.9	17.4	20.5	23.9
Internal portion	93.1%	97.4%	97.6%	97.3%	96.2%
External portion	5.9%	2.6%	2.4%	2.7%	3.8%
Extra-budgetary funds debt	14.3	22.4	3.2	2.1	13.7
Social Security Funds debt	0.7	0.5	0.4	0.3	0.2
Local authorities debt	41.4	49.0	56.7	72.8	82.5
General Government debt,					
consolidated	332.4	404.5	444.5	554.2	26.8
as % of GDP	16.7	18.6	19.5	23.0	26.8
<i>General Government debt under</i>					
ESA 95	391.1	585.5	695.6	956.2	1,032.5
as % of GDP	19.7	26.9	30.6	39.7	40.6

Source: Ministry of Finance, Czech Statistical Office

State Debt Service, Schedule of Payments and Debt Management Strategy

The following table illustrates the historical expenses related to State debt during the four years ended 31 December, 2003 and estimated expenses for the year ended 31 December 2004:

	As at and for the year ended December 31				
	2000	2001	2002	2003	Budget 2004
	<i>(CZK millions)</i>				
Principal repayments	21,838	28,220	16,439	32,940	39,053
Interest payments	17,378	16,989	18,629	21,328	26,729
Fees	34	40	46	90	300
Realized exchange rate loss		620	270	210	0
Total State debt service	39,250	45,869	35,383	54,568	66,082
Debt service (excl. principal repayments) as % of State budget expenses	2.8%	2.5%	2.5%	2.7%	3.1%

Source: Ministry of Finance

The following table sets forth the schedule of repayments on Treasury bonds (which do not include Treasury-bills) and internal and external loans (including loans from the European Investment Bank) as at 30 April 2004 for the periods indicated (which data do not take into account any borrowings or bond issues anticipated after April 30, 2004):

	Total principal repayment	Internal principal repayment	External principal repayment
	<i>(CZK billions)</i>		
2004 (from 1 May 2004).....	34.0	33.9	0.1
2005.....	22.1	22.0	0.1
2006.....	58.0	58.0	–
2007.....	21.7	20.0	1.7
2008.....	45.0	41.0	4.0
2009.....	13.2	13.0	0.2
2010.....	21.4	21.0	0.4
2011.....	50.7	50.3	0.4
2012.....	0.4	–	0.4
2013.....	42.4	42.0	0.4
2014.....	0.4	–	0.4
2015 and thereafter.....	67.5	61.6	5.9

Source: Ministry of Finance

Note: The amounts set forth in the table do not include any repayment in respect of the bills of exchange issued by the Czech Republic to IBRD and EBRD as payment for its membership in these institutions.

State debt is almost exclusively denominated in CZK and the exposure to currency risk is therefore very low (USD 5 million as at 30 April 2004). A large proportion of State debt is concentrated in short-term debt. Both refinancing and interest rate risks are currently the most significant risks for government financing.

The medium-term target of refinancing risk management is to restructure the debt portfolio through further decreasing the share of Treasury-bills and increasing the share of fixed-yield medium- and long-term treasury bonds. The first step is to reduce the share of short-term state debt, maturing within one year, from the current level of more than 40% to the band of 25 to 30% and thereafter to below 20% by the end of the year 2006. From the year 2007 this 20% target for short-term debt is planned to be one of the benchmark criteria for risk management.

Due to the relatively high share of State debt that matures within one year, the exposure to interest rate risk is relatively high. More than 40% (45% as at 31 March 2004) of the debt portfolio is exposed to unexpected changes in interest rates occurring within one year. This exposure is mitigated by interest rate swaps. These activities contributed to a decrease in interest rate re-fixing by more than 6 percentage points at the end of March 2004. Therefore, the portfolio of interest rate swaps in the Czech Republic represents another flexible instrument which allows the State, in a synthetic manner (i.e., in parallel with its issuing activities), to manage the debt portfolio duration and to distribute the re-fixing of nominal interest rate payments of State debt in time.

At the end of 2003 the modified duration of State debt reached the value of 3.3 years, which is in line with the target band of 3-4 years set in November 2002 for this year. It can be deduced, from the level of State debt and its interest rate structure, that a 1 percentage point increase in interest rates will increase interest payments within a one-year period by 1.8 billion CZK (0.1% of GDP), taking account of the stabilization effect of interest rate swaps.

A new target band for the modified duration of State debt for the year 2004, in the range of 3.3 to 4.3 years, was announced for the purposes of interest rate management in December 2003. Compared to 2003, there is a symmetrical shift of the band upwards by 0.3 years. Considering the high levels of growth in State debt, and increasing nominal exposure to interest risks, the strategy of extending the duration seems to be the best course of action also for the coming years. At the end of March 2004, the modified duration of State debt (including interest rate swaps) reached 3.4 years.

Since 2002, the Czech Republic has also been using derivatives as part of its debt management strategy. Individual transactions are executed by a department of the Ministry of Finance on the basis of framework agreements entered into with various counterparties.

The Czech Republic has in the past used derivatives to swap floating rate interest payments into fixed rate interest payments, i.e., the Czech Republic agreed to pay to the counterparty amounts calculated by reference to a certain notional amount, using a fixed interest rate, and to receive payments calculated by reference to the notional amount, using a floating interest rate (these are used to cover interest payments under outstanding Treasury-bills). Accordingly, the interest rate swaps play an important role in the current strategy focusing on the extension of the debt portfolio duration and the distribution of the refixing of the nominal interest rate payments of the State debt in time.

Government Guarantees

Until 2001, the Czech Republic extended State guarantees each year in support of Czech private-sector or public-sector enterprises. Since 2001, a State guarantee may be extended only pursuant to a specific law passed by Parliament. The annual level of State guarantees is currently not limited, but by law the aggregate value of State guarantees granted may not exceed 40% of the projected budgetary expenses in a given year, and any further State guarantee may be granted only after a decrease in the volume of the guarantees under this limit.

As at 31 December 2003, the aggregate amount of liabilities covered by outstanding State guarantees (other than guarantees set forth in special laws) was approximately CZK 290 billion. These guarantees comprised:

- (i) guarantees provided in respect of certain environmental projects (such as the de-sulphurisation of power plants). As at 31 December 2003, the aggregate outstanding amount of guarantees of this type amounted to approximately CZK 5.5 billion;
- (ii) guarantees relating to infrastructure projects (such as the construction of railways corridors, the Prague airport terminal and highways). As at 31 December 2003, the aggregate outstanding amount of these guarantees was approximately CZK 57 billion;
- (iii) guarantees relating to the consolidation of the Czech banking system (such as guarantees issued in relation to the restructuring of Investiční a Poštovní banka, a.s., (“IPB”) and in connection with the arbitration proceedings by Československá obchodní banka, a.s. (“CSOB”) against Slovenská inkasní, s.r.o., described below in more detail). As at 31 December 2003, the aggregate outstanding amount of these guarantees was approximately CZK 205 billion; and
- (iv) guarantees issued in respect of various other projects (such as the construction of a congress center, and the production of military jets). As at 31 December 2003, the aggregate outstanding amount of these guarantees was approximately CZK 22 billion.

Although, under national methodology, high-risk State guarantees were treated as contingent until an actual payment, ESA 95 methodology requires that high-risk State guarantees be imputed to government debt in the year in which the guarantee is exercised for the first time, even if the payment is requested in respect of the interest or only a portion of the guaranteed amount. Such re-classification of outstanding guarantees increases the government deficit and debt reported under ESA 95 in the relevant year.

Some of the above-mentioned guarantees have already been presented to the Czech Republic for payment and others are likely to result in payments becoming due from the Czech Republic in the future. Under the ESA 95 methodology, the whole amount of a state guarantee must be included in the State Budget as a capital transfer, if and when the guarantee is exercised for the first time (irrespective of whether the payment is required in respect of the whole amount of the guarantee, any part of the guarantee or interest only). Of the total amount of contingent liability represented by these guarantees and indemnities, CZK 34.5 billion was reflected in the consolidated General Government debt and deficits under the national fiscal accounting methodology as at 31 December 2003; by contrast, CZK 253.4 billion is reflected under the ESA 95 methodology.

The highest increase in government debt and deficit occurred in 2003. This was due, in particular, to the reclassification of the following two non-standard guarantees concerning the banking sector:

Guarantee to CNB, related to the IPB case

On the basis of a government resolution, the Ministry of Finance issued a counter-indemnity to CNB in respect of CNB’s indemnity provided to CSOB against losses which CSOB could incur in connection with its purchase of an ailing Czech bank (IPB). The State’s liability is limited, both in terms of the maximum amount (CZK 160 billion) and in terms of duration (the guarantee expires in 2016). In 2003, the Ministry

of Finance paid an advance payment to CNB on the basis of this guarantee, amounting to CZK 2 billion. For the year 2004, an amount of CZK 2.7 billion is budgeted for this purpose.

Guarantee to CSOB, related to Slovenska inkasni, s. r. o. ("SI")

On the basis of a government resolution, the Ministry of Finance of the Czech Republic, the Ministry of Finance of the Slovak Republic and CSOB concluded a framework agreement regarding CSOB's restructuring. In line with this agreement, CSOB transferred, i.e., sold, a range of non-performing assets to so-called payment-collection units established by the Ministries of Finance of both countries. Both units were established for the purpose of enforcing and collecting bad debts. Both are refinanced by CSOB and CSOB's resulting losses are to be covered by the respective State. Pursuant to the above-mentioned framework agreement, the Czech Ministry of Finance provides compensation for the losses of Česká inkasní, s. r. o. However, unlike its Czech counterpart, the Ministry of Finance of the Slovak Republic did not cover the losses of Slovenská inkasni, s. r. o., which resulted in a CSOB bringing a claim against this company. In 1997, CSOB initiated an arbitration against the Slovak Republic at the International Centre for the Settlement of Investment Disputes (ICSID) in Washington, which is still pending. In order to eliminate the danger of CSOB's financial destabilisation, the Ministry of Finance of the Czech Republic concluded a "Stabilisation Agreement" with CSOB, stipulating that the Ministry would pay 90% of the nominal value of outstanding claims alleged to be owed by SI and/or Slovak Republic to CSOB under the framework agreement by December 31, 2002. The payment date for this claim, totalling up to CZK 22 billion, was subsequently (by way of an amendment to the Stabilisation Agreement) postponed until December 31, 2004, with the possibility of a further postponement of three days, i.e., until January 3, 2005. In 2003, an amount of CZK 0.57 billion was paid to CSOB on the basis of this guarantee. The final cost of this guarantee, to a large extent, is dependent on the results of the ICSID arbitration.

In addition to the *ad-hoc* State guarantees mentioned above, the liabilities of certain quasi-governmental institutions are guaranteed by the Czech Republic as a whole, based on specific provisions of law under which the institutions were established. These institutions include, most importantly, the Czech Consolidation Agency (See section entitled "Privatisation and Transformation Institutions – Czech Consolidation Agency"), the Export Guarantee and Insurance Company, the Czech Export Bank and the Railways Infrastructure Administration.

Gross External Debt

The following table sets out the external debt of Czech institutions, including the Government, from 2000 to 2003:

	2000	2001	2002	2003
	<i>(EUR millions)</i>			
Government	1,163.3	978.8	1,533.6	2,152.1
<i>Short-term</i>	60.3	14.5	24.1	21.9
Money market instruments	60.3	14.5	24.1	21.9
Loans	—	—	—	—
Trade credits	—	—	—	—
Other debt liabilities	—	—	—	—
<i>Long-term</i>	1,103.0	964.3	1,509.5	2,130.2
Bonds and notes	541.6	668.0	1,209.6	1,437.2
Loans	306.3	296.3	299.9	693.0
Trade credits	—	—	—	—
Other debt liabilities	255.1	—	—	—
Monetary authorities (CNB)	5.4	6.3	5.0	3.7
<i>Short-term</i>	0.3	2.1	1.4	0.7
Money market instruments	—	—	—	—
Loans	—	—	—	—
Currency and deposits	0.3	2.1	1.4	0.7
Other debt liabilities	—	—	—	—
<i>Long-term</i>	5.1	4.2	3.6	3.0
Bonds and notes	—	—	—	—
Loans	4.8	4.2	3.6	3.0
Currency and deposits	—	—	—	—
Other debt liabilities	0.3	—	—	—
Banks	9,175.9	8,781.8	8,150.0	8,847.1
<i>Short-term</i>	6,447.6	6,017.5	5,616.3	6,481.0
Money market instruments	2.0	61.0	40.5	45.8
Loans	719.9	334.7	185.2	160.3
Currency and deposits	5,348.1	5,227.9	5,091.2	6,017.8
Other debt liabilities	377.6	393.9	299.4	257.1
<i>Long-term</i>	2,728.3	2,764.3	2,533.7	2,366.1
Bonds and notes	317.2	460.1	522.9	469.7
Loans	1,909.2	1,614.7	1,669.4	1,522.5
Currency and deposits	501.9	682.5	341.4	256.7
Other debt liabilities	—	7.0	—	117.2
Other sectors	9,629.2	11,073.0	11,225.3	11,793.0
<i>Short-term</i>	2,096.9	2,867.6	2,699.2	2,840.2
Money market instruments	3.7	—	—	—
Loans	236.8	1,135.7	757.4	1,351.2
Currency and deposits	—	—	—	—
Trade credits	1,856.4	1,731.9	1,941.8	1,489.0
Other debt liabilities	—	—	—	—
<i>Long-term</i>	7,532.3	8,205.4	8,526.1	8,952.8
Bonds and notes	469.4	410.1	513.8	581.5
Loans	6,344.3	7,106.1	7,464.8	7,626.0
Currency and deposits	—	—	—	—
Trade credits	718.6	689.2	547.5	438.5
Other debt liabilities	—	—	—	—
Direct investment: Intercompany lending	3,311.3	4,527.8	4,823.6	4,802.7
Debt liabilities to affiliated enterprises	—	—	—	—
Debt liabilities to direct investors	3,311.3	4,527.8	4,823.6	4,802.7
Gross External debt	23,285.1	25,367.7	25,737.5	27,598.6

Source: Czech National Bank

The following table sets forth the composition of the external debt by type of creditors in accordance with the CNB methodology as at 31 December in each of the years 2000 through 2003:

	2000	2001	2002 ¹	2003 ²
	(EUR millions)			
DEBT IN CONVERTIBLE CURRENCIES	23,030.0	25,367.7	25,737.5	27,598.6
<i>of which:</i>				
Long-term	13,232.3	14,561.9	15,785.9	16,620.5
<i>by debtor:</i>				
CNB	5.1	4.2	3.6	3.0
Commercial banks	2,728.3	2,764.3	2,533.7	2,366.1
Government	847.9	964.3	1,509.5	2,130.2
Other sectors	9,651.0	10,829.1	11,739.1	12,121.2
<i>by creditor:</i>				
Foreign banks	6,517.8	7,170.3	7,297.2	7,607.9
Governments	97.0	74.2	55.3	–
Multilateral institutions	1,924.2	2,216.4	2,211.9	2,585.4
Suppliers and direct investors	2,837.3	3,312.8	3,760.4	3,606.9
Other investors	1,856.0	1,788.2	2,461.1	2,820.3
Short-term	9,797.7	10,805.8	9,951.6	10,978.1
<i>by debtor:</i>				
CNB	0.3	2.1	1.4	0.7
Commercial banks	6,447.6	6,017.5	5,616.3	6,481.0
Government	60.3	14.5	24.1	21.9
Other sectors	3,289.5	4,771.7	4,309.8	4,474.5
<i>by creditor:</i>				
Foreign banks	5,794.7	6,007.7	5,322.8	6,770.3
Suppliers and direct investors	3,049.0	3,636.0	3,552.4	3,123.3
Other investors	954.0	1,162.1	1,076.4	1,084.5
DEBT IN NON-CONVERTIBLE CURRENCIES	255.1	0.0	0.0	0.0
<i>of which:</i>				
Long-term	255.1	–	–	–
Short-term	–	–	–	–
TOTAL EXTERNAL DEBT	23,285.1	25,367.7	25,737.5	27,598.6
<i>of which:</i>				
Long-term	13,487.4	14,561.9	15,785.9	16,620.5
Short-term	9,797.7	10,805.8	9,951.6	10,978.1
Total external long-term debt	13,487.4	14,561.9	15,785.9	16,620.5
– use of IMF credits				
– public and publicly guaranteed debt	6,993.1	6,350.9	6,560.9	6,854.5
– private non-guaranteed debt	6,494.3	8,211.0	9,225.0	9,766.0

Source: Czech National Bank

Relationship with Multilateral Financial Institutions

The Czech Republic has received several loans from the European Investment Bank (“EIB”) to help finance infrastructure projects, flood-related measures and other projects. Currently, there are five loan agreements in place between the Czech Republic and EIB with an aggregate principal amount of EUR 935 million. As at 27 May 2004, the total outstanding principal amount of loans received by the Czech Republic under these loan agreements reached CZK 13.70 billion (approximately EUR 427 million). In May 2004, Parliament authorized the execution of another loan agreement with EIB in the principal amount of up to EUR 310 million to finance the building of a ring road around Prague and the Government approved a new legislative proposal to authorize the execution of a further loan agreement with EIB in the principal amount of CZK 12 billion for the purpose of building a highway.

Furthermore, the Czech Republic has issued bills of exchange to the International Bank for Reconstruction and Development and European Bank for Reconstruction and Development as payment for its membership in these institutions. As at 31 December 2004, the aggregate principal amount of these securities was CZK 1.6 billion.

Other than as mentioned above, the Czech Republic does not currently use financing from multilateral financial institutions.

TAXATION

The following is a general description of certain tax considerations relating to the Instruments. It does not purport to be a complete analysis of all tax considerations relating to the Instruments, whether in the relevant countries or elsewhere. Prospective purchasers of Instruments should consult their own tax advisers as to which countries' tax laws could be relevant to acquiring, holding and disposing of Instruments and receiving payments of interest, principal and/or other amounts under the Instruments and the consequences of such actions under the tax laws of those countries. This summary is based upon the law as in effect on the date of this Information Memorandum and is subject to any change in law that may take effect after such date.

Interest

Under the existing laws and regulations of the Czech Republic and their prevailing interpretations, interest income on the Instruments of an individual or a legal person which is not for tax purposes treated as a resident of the Czech Republic (together, “**Non-Czech Holders**”) will not be subject to taxation in the Czech Republic, and no withholding of any Czech tax will be required on any such payments.

Interest income on the Instruments of an individual or a legal person which is for tax purposes treated as a resident of the Czech Republic (together, “**Czech Holders**”) is not subject to any Czech withholding tax. However, such income should be declared by the Czech Holders in their annual tax returns and ordinary Czech corporate or personal income tax, as applicable, must be paid.

Capital Gains

Income or gains realised by Non-Czech Holders (not holding the Instruments through a permanent establishment in the Czech Republic) from the sale of the Instruments to a Non-Czech Holder (not acquiring the Instruments through a permanent establishment in the Czech Republic) will not be subject to any Czech income or capital gains tax.

Income or gains realised by Non-Czech Holders from the sale of the Instruments (a) to a Czech Holder or (b) to a Czech permanent establishment of another Non-Czech Holder would be subject to taxation in the Czech Republic and, in addition, if the Non-Czech Holder is not a tax resident of a country being a member of the European Economic Area, the purchaser would be required to withhold one per cent. security tax from the purchase price. This security tax could be, subsequently, credited against the final Czech tax liability of the Non-Czech Holder. Both the taxation and withholding obligation mentioned above may be eliminated if the Non-Czech Holder qualifies for the benefits of a double tax treaty concluded by the Czech Republic and if such treaty is applicable.

Income or gains realised by Czech Holders from the sale of the Instruments are generally subject to Czech corporate or personal income tax, as applicable. Income or gains realised by Czech Holders, which are individuals, from the sale of the Instruments, which were not included in the business property of such individual, are exempt from Czech personal income tax, as applicable, if the holding period exceeds six months.

Other Taxes

No Czech stamp duty, registration, transfer or similar taxes will be payable in connection with the acquisition, ownership, sale or disposal of the Instruments by Czech Holders or Non-Czech Holders.

EU Savings Directive

On 3 June 2003 the EU Council of Economic and Finance Ministers adopted a new directive regarding the taxation of savings income. The directive is scheduled to be applied by Member States from 1 January 2005, provided that certain non-EU countries adopt similar measures from the same date. Under the directive each Member State will be required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to an individual resident in that other Member State; however, Austria, Belgium and Luxembourg may instead apply a withholding system for a transitional period in relation to such payments, deducting tax at rates rising over time to 35 per cent. The transitional period is to commence on the date from which the directive is to be applied by Member States and to terminate at the end of the first fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments.

SUBSCRIPTION AND SALE

Instruments may be sold from time to time by the Issuer to any one or more of Deutsche Bank AG London and Morgan Stanley & Co. International Limited (the “**Dealers**”). The arrangements under which Instruments may from time to time be agreed to be sold by the Issuer to, and purchased by, Dealers are set out in a dealership agreement dated 3 June 2004 (the “**Dealership Agreement**”) and made between the Issuer and the Dealers. Any such agreement will, *inter alia*, make provision for the form and terms and conditions of the relevant Instruments, the price at which such Instruments will be purchased by the Dealers and the commissions or other agreed deductibles (if any) payable or allowable by the Issuer in respect of such purchase. The Dealership Agreement makes provision for the resignation or termination of appointment of existing Dealers and for the appointment of additional or other Dealers either generally in respect of the Programme or in relation to a particular Tranche of Instruments.

United States of America

Bearer Instruments: Regulation S Category 1; TEFRA D or TEFRA C as specified in the relevant Pricing Supplement.

Registered Instruments: Regulation S Category 1; Rule 144A Eligible if so specified in the relevant Pricing Supplement.

The Instruments have not been and will not be registered under the United States Securities Act of 1933 (the “**Securities Act**”) and are subject to U.S. tax law requirements. Subject to certain exceptions, Instruments may not be offered or sold within the United States or to U.S. persons. Each of the Dealers has agreed that, except as permitted by the Dealer Agreement, it will not offer, sell or deliver Instruments within the United States or to U.S. persons.

In addition, until 40 days after the commencement of any offering, an offer or sale of Instruments from that offering within the United States by any dealer whether or not participating in the offering may violate the registration requirements of the Securities Act.

United Kingdom

Each Dealer has represented, warranted and agreed that:

- (a) In relation to any Instruments having a maturity of less than one year:
 - (i) it is a person whose ordinary activities involve it in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of its business; and
 - (ii) it has not offered or sold and will not offer or sell any Instruments other than to persons:
 - (A) whose ordinary activities involve them in acquiring, holding, managing or disposing of investments (as principal or agent) for the purposes of their businesses; or
 - (B) who it is reasonable to expect will acquire, hold, manage or dispose of investments (as principal or agent) for the purposes of their businesses,where the issue of the Instruments would otherwise constitute a contravention of Section 19 of the Financial Services and Markets Act 2000 (“**FSMA**”) by the Issuer; and
- (b) It has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to any Instruments in, from or otherwise involving the United Kingdom.

Czech Republic

No approval or permit has been sought or obtained from the Czech Securities Commission in accordance with the Czech Capital Markets Act or otherwise in respect of the Instruments or the Information Memorandum. No application has been filed nor has any permission been obtained nor has any other arrangement been made for accepting the Instruments for trading on any public market in the Czech Republic. Pursuant to Section 36 of the Czech Capital Markets Act, the offering of securities issued by the Czech Republic (such as the Instruments) does not constitute public offering in the Czech Republic and is therefore exempt from the Czech regulation of public offering of securities.

Japan

The Instruments have not been and will not be registered under the Securities and Exchange Law of Japan and, accordingly, each Dealer has undertaken that it will not offer or sell any Instruments directly

or indirectly, in Japan or to, or for the benefit of, any Japanese Person or to others for re-offering or resale, directly or indirectly, in Japan or to any Japanese Person except under circumstances which will result in compliance with all applicable laws, regulations and guidelines promulgated by the relevant Japanese governmental and regulatory authorities and in effect at the relevant time. For the purposes of this paragraph, “Japanese Person” shall mean any person resident in Japan, including any corporation or other entity organised under the laws of Japan.

Switzerland

Each Dealer has agreed that any issue of Instruments denominated in Swiss Francs will be in compliance with the guidelines of the Swiss National Bank regarding issues of Swiss Franc denominated debt securities.

Federal Republic of Germany

Each Dealer agrees not to offer or sell Instruments in the Federal Republic of Germany other than in compliance with the Securities Selling Prospectus Act (*Wertpapier-Verkaufsprospektgesetz*) of 13 December 1990 (as amended), or any other laws applicable in the Federal Republic of Germany governing the issue, offering and sale of securities.

General

Other than with respect to the admission to listing, trading and/or quotation by such one or more listing authorities, stock exchanges and/or quotation systems as may be specified in the Pricing Supplement, no action has been or will be taken in any country or jurisdiction by the Republic, or the Dealers that would permit a public offering of Instruments, or possession or distribution of any offering material in relation thereto, in any country or jurisdiction where action for that purpose is required.

Persons into whose hands this Information Memorandum or any Pricing Supplement comes are required by the Issuer and the Dealers to comply with all applicable laws and regulations in each country or jurisdiction in or from which they purchase, offer, sell or deliver Instruments or have in their possession or distribute such offering material, in all cases at their own expense.

Each Dealer has agreed and each further Dealer appointed under the Programme will be required to agree that it will (to the best of its knowledge and belief) comply with all applicable securities laws and regulations in force in any jurisdiction in which it purchases, offers, sells or delivers Instruments or possesses or distributes this Information Memorandum.

The Dealership Agreement provides that the Dealers shall not be bound by any of the restrictions relating to any specific jurisdiction (set out above) to the extent that such restrictions shall, as a result of change(s) or change(s) in official interpretation, after the date hereof, of applicable laws and regulations, no longer be applicable but without prejudice to the obligations of the Dealers described in the paragraph headed “**General**” above.

Selling restrictions may be supplemented or modified with the agreement of the Issuer. Any such supplement or modification will be set out in the relevant Pricing Supplement (in the case of a supplement or modification relevant only to a particular Tranche of Instruments) or (in any other case) in a supplement to this Information Memorandum.

GENERAL INFORMATION

1. Application has been made to list Instruments issued under the Programme on the Luxembourg Stock Exchange and, in connection therewith, the Luxembourg Stock Exchange has assigned registration number 13010 to the Programme. Prior to the listing of any Instruments, the legal notice relating to the issue will be registered with the Luxembourg trade and companies register (*Registre de commerce et des sociétés, Luxembourg*), where copies of this document may be obtained upon request.

However, Instruments may be issued pursuant to the Programme which will not be listed on the Luxembourg Stock Exchange or any other stock exchange or which will be listed on such stock exchange as the Issuer and the relevant Dealer(s) may agree.

2. The issuance of Instruments under the Programme is authorised pursuant to Act No. 190/2004 on Bonds and specific Acts Nos. 120/2003 and 313/2004 for the financial year in which the issuance of any Instruments is to take place. The Issuer has obtained or will obtain from time to time all necessary consents, approvals and authorisations in connection with the issue and performance of the Instruments.
3. There are no legal, arbitration or administrative proceedings against or affecting the Issuer (and no such proceedings are pending or threatened) which have or may have, individually or in the aggregate, a significant effect on the financial position of the Issuer.
4. For so long as the Programme remains in effect or any Instrument shall be outstanding, copies and, where appropriate, English translations of the following documents may be inspected during normal business hours at the specified office of the Issue and Paying Agent and Principal Registrar in London and the specified office of the Paying Agent in Luxembourg:

- (a) Act No. 190/2004 on Bonds and specific Acts Nos. 120/2003 and 313/2004;
- (b) the Issue and Paying Agency Agreement;
- (c) the Deed of Covenant; and
- (d) the Dealership Agreement,

and copies and, where appropriate, English translation of the following documents may be obtained during normal business hours at the specified office of the Issue and Paying Agent and at the specified office of the Paying Agent in Luxembourg:

- (e) this Information Memorandum (and any supplements thereto); and
 - (f) any Pricing Supplement relating to Instruments which are admitted to listing, trading and/or quotation by any listing authority, stock exchange and/or quotation system. In the case of any Instruments which are not admitted to listing, trading and/or quotation by any listing authority, stock exchange and/or quotation system, copies of the relevant Pricing Supplement will only be available for inspection by a Holder of the relevant Instruments upon production of evidence satisfactory to the Issuer and the relevant Paying Agent as to its holding of such Instruments and identity.
5. The net proceeds of the issue of each Tranche of Instruments will be used for covering deficits of the State Budget for the years 2003 and 2004.
 6. The Instruments have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The appropriate common code and the International Securities Identification Number in relation to the Instruments of each Series will be specified in the Pricing Supplement relating thereto. The relevant Pricing Supplement shall specify any other clearing system as shall have accepted the relevant Instruments for clearance together with any further appropriate information.
 7. Bearer Instruments (other than Temporary Global Instruments) and any Coupon appertaining thereto will bear a legend substantially to the following effect: "Any United States person who holds this obligation will be subject to limitations under the United States income tax laws, including the limitations provided in Sections 165(j) and 1287(a) of the Internal Revenue Code." The sections referred to in such legend provide that a United States person who holds a Bearer Instrument or Coupon generally will not be allowed to deduct any loss realised on the sale, exchange or redemption of such Bearer Instrument or Coupon and any gain (which might otherwise

be characterised as capital gain) recognised on such sale, exchange or redemption will be treated as ordinary income.

8. Pursuant to Section 2(3) of the Czech Bonds Act, the issuance of each Series and/or Tranche of the Instruments must be notified to the Czech Securities Commission no later than on the date of issue of the relevant Instruments setting out the place of issue and amount of relevant Series or Tranche and the form, yield and maturity of the relevant Instruments.

THE ISSUER

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