



BUDAPEST
WATERWORKS

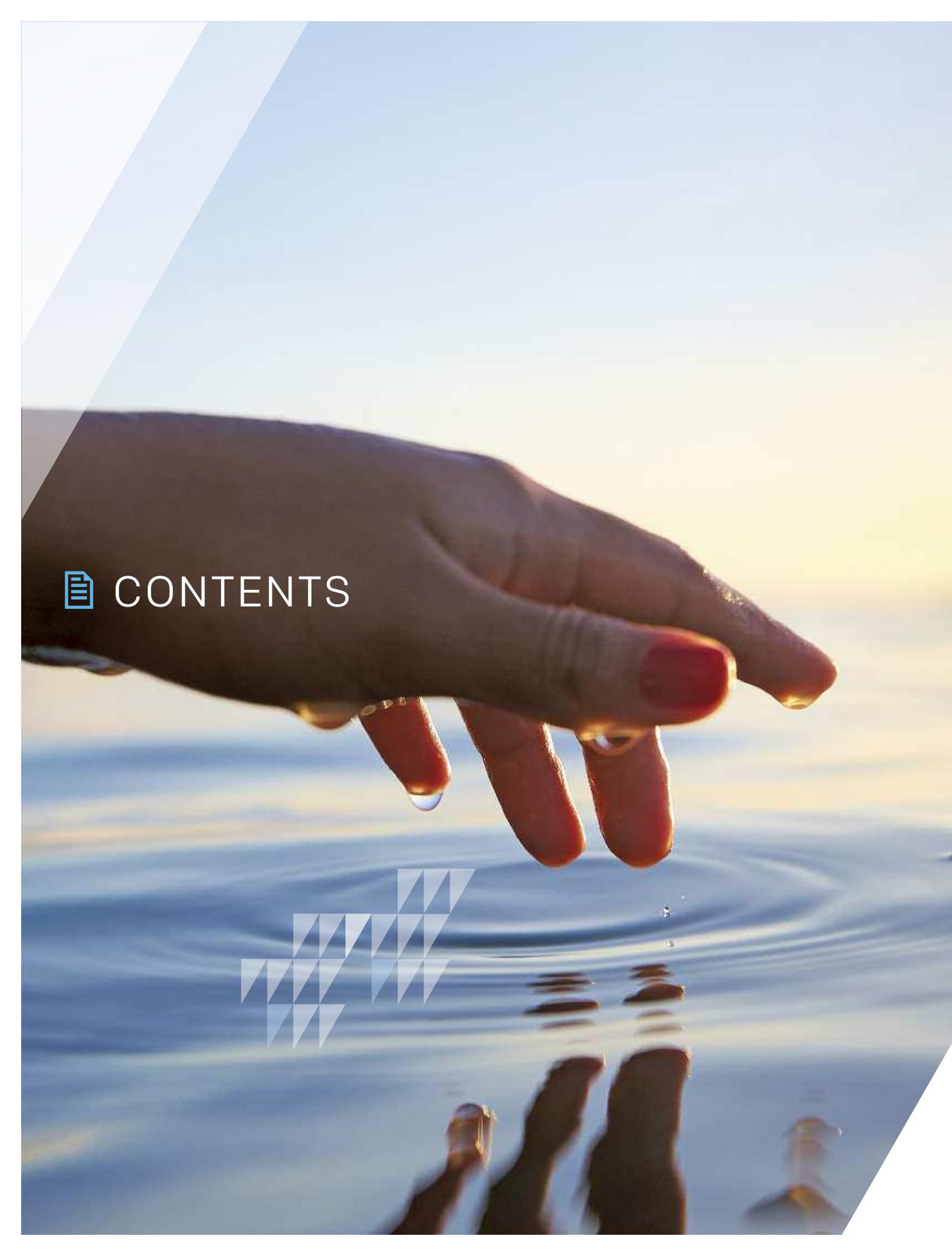


Annual Report

Budapest Waterworks

2016





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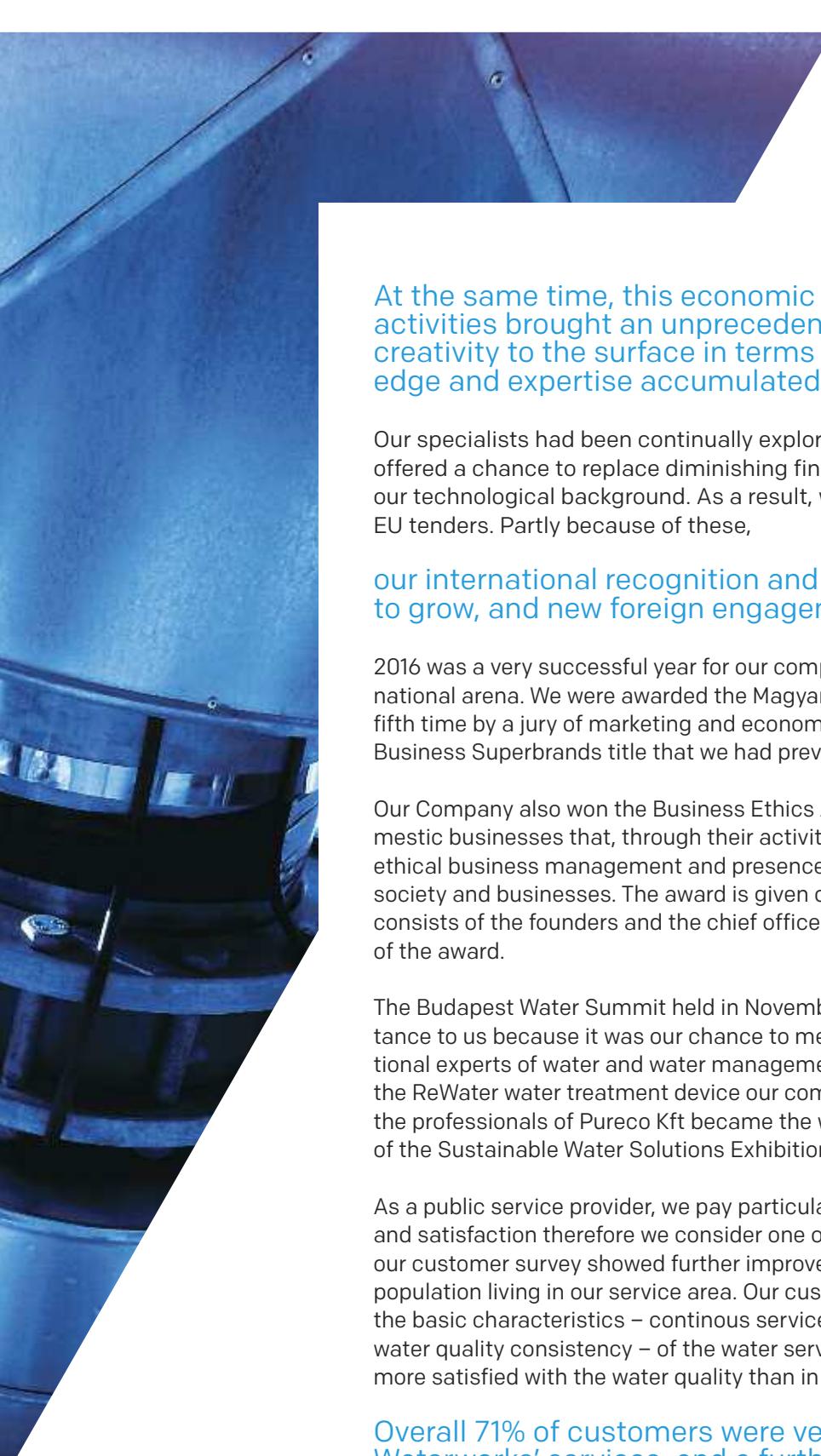
CEO's GREETING

2016 once again will be marked in Budapest Waterworks' nearly 150 years of history as a truly colourful and challenging year, but at the same time a year full of professional successes.

It was a challenge that required a great deal of attention, thoughtful, focused, high quality work not only from the managers but - I can honestly say - from all the employees of Budapest Waterworks to keep our economic stability, despite the economically unfavourable operating conditions, while taking into account the high standards set for ourselves, and not letting the service and safety level drop in terms of quality, quantity or continuity.

While on one side the reduction of utility fees, the supervisory fee, the utility and public service taxes, the increase in local tax and the repayment of a shareholder loan for repurchasing the equity package from foreign investors represented a major burden on the Company, a serious effort had been made to raise the level of water utility services provided for the settlements taken over in the past few years to match the level of service provided to our other service areas.

Furthermore, we couldn't continue the trend of making operational savings by not increasing the salaries, as on the sectoral level it is an increasingly urgent task to manage the problems caused by labour migration, lack of well-trained professionals, and lack of essential labour supply for the aging profession.



At the same time, this economic pressure on our day-to-day activities brought an unprecedented amount of energy and creativity to the surface in terms of utilising the huge knowledge and expertise accumulated at Budapest Waterworks.

Our specialists had been continually exploring tendering opportunities, which offered a chance to replace diminishing financial resources in order to develop our technological background. As a result, we participated in two successful EU tenders. Partly because of these,

our international recognition and acceptance have continued to grow, and new foreign engagement opportunities emerged.

2016 was a very successful year for our company both in Hungary and in the international arena. We were awarded the Magyar Brand (Hungarian Brand) prize for the fifth time by a jury of marketing and economic experts, which also confirms the Business Superbrands title that we had previously won four times.

Our Company also won the Business Ethics Award in 2016 which recognises domestic businesses that, through their activity and conduct, exemplify responsible, ethical business management and presence, and strengthen the trust between society and businesses. The award is given once a year by a professional jury that consists of the founders and the chief officers of previous recipient companies of the award.

The Budapest Water Summit held in November 2016 was not only of great importance to us because it was our chance to meet with the most renowned international experts of water and water management in our homeland, but also because the ReWater water treatment device our company developed in collaboration with the professionals of Pureco Kft became the winner of the Water Innovation Award of the Sustainable Water Solutions Exhibition.

As a public service provider, we pay particular attention to our customers' feedback and satisfaction therefore we consider one of our main achievements in 2016, that our customer survey showed further improvement in satisfaction ratings among the population living in our service area. Our customers were extremely satisfied with the basic characteristics – continuous service, water pressure, pressure fluctuation, water quality consistency – of the water service in 2016. Respondents were also more satisfied with the water quality than in previous years.

Overall 71% of customers were very satisfied with Budapest Waterworks' services, and a further 23% were satisfied.

I would like to express my gratitude to all our colleagues who, through their hard work, knowledge and expertise ensured that despite the difficult circumstances our company closed a successful year in 2016 and helped to further strengthen the prestige and recognition of the water sector and Budapest Waterworks.

Csaba Haranghy
CEO

BUDAPEST WATERWORKS

In terms of size and high quality technology Budapest Waterworks, with its nearly one and a half century history, is one of the leading water utility service providers in Central-Eastern Europe.





The water utility services are supported by world class technology. Our more than 5000 km long drinking water supply network enmesh the city and its agglomeration. Both the drinking water production and the associated supply system are fully automated by now. Budapest's drinking water supply is entirely based on 740 bank filtered horizontal filtering and drilled wells. Our Company's subsidiary, DUNA KÚT Kft fills a key role in the construction and maintenance of the water wells. The over seven hundred drinking water production wells produce almost a million m³ of drinking water per day.

In recent years, the Company played a significant role in the wastewater treatment of the capital, and in the wastewater treatment and sewage disposal of the agglomeration. Budapest Waterworks implemented multi-billion HUF improvements – thanks to EU and domestic grants – in the municipal utilities managed by the Company, thereby also contributing to the protection of the environment and fresh water reserves.

The professional, planning and construction knowledge based on nearly one and a half centuries of

operating experience and outstanding engineering skills provide an excellent background for technical development projects, such as the development of mobile water treatment units and investments implemented in facility and network management using internal resources.

In the Company's internationally certified and accredited laboratory, we examine 190 000 parameters of more than 10 000 organic and inorganic chemical, microbiological, microscopic biological and toxicological test samples per year.

It is of particular value to the regions' decision makers that in the period elapsed since the regime change Budapest Waterworks had already gone through the phases of the market, technological, operational and economic development that the other cities concerned are yet to face. Regional cooperations serve the realisation of the shareholders' objectives by strengthening alternative, not directly water sales related revenues, increasing the value of the Company, acquiring professional experience and expanding our know-how in the core activity.

→ Scope of activities

In terms of our main activity, Budapest Waterworks is a water utility service provider company. Until 2003 our Company – contrary to the common practice in Hungary – dealt exclusively with drinking water production and supply. From 2004 onwards the scope of our activities expanded initially through subsidiaries, then later with the addition of wastewater and sewage services as well as the operation of sewage networks and wastewater treatment plants. Our Company currently supplies over 2 million people with healthy drinking water, and in addition to the drinking water production, drinking and industrial water supply it also provides sewage and wastewater disposal as well as wastewater treatment services for its customers in Budapest and a further 12 municipalities in the agglomeration by relying on its world-class technological background.

Budapest Waterworks has been carrying out direct wastewater treatment services since 2013. On 1st June 2013 the Company took over the operation of the Central Wastewater Treatment Plant in Budapest, the construction of which was one of Central Europe's largest and most significant environmental investments, with a biological wastewater treatment capacity of 350 000 m³/day. The environmentally friendly, completely enclosed (covered) plant uses revolutionary new solutions that combine physical, chemical, and biological treatment elements. As a result of the takeover, Budapest Waterworks also oper-

ates the small power plant which provides approximately 60% of the facility's energy demand.

In order to compensate for the freezing of the water- and sewage service fees and the continuously decreasing water consumption, there is a growing emphasis on the increase of revenues from other sources. In addition to the core activity, customer service also provides an extra revenue source (data service, management activities, submeter services). The Company also earns income by letting out some of its properties such as offices and holiday homes, and by performing technical (such as cartography, geodesy), laboratory (drinking- and bathing water testing) and other services.

The Company's international presence has also increased since 2013. Budapest Waterworks plays an active role on the international markets by providing consulting and engineering services. The reconstruction works of the Sri Lanka water treatment plants that commenced in 2013 continued in 2016. Although the revenue generated by this project was lower than in the previous years, it still produced a significant income for the company. In 2016 another major international project has been launched, whereby the Company has to solve the water supply of several Indonesian settlements by constructing the necessary facilities. The construction works of some of these facilities will continue in 2017.



→ Service area



Act CCIX of 2011 (Vksztv.) which laid new foundations for water utility services resulted in significant changes for the Company's activity and service areas. In the course of 2013, our scope of activities in both the drinking water- and wastewater treatment fields was further expanded by taking over the water utility supply services of several settlements.

As a result the Company now directly operates a 5900 km long pipe network out of which the drinking water pipe system is longer than 5300 km, the industrial water pipe system is 45 km long and the wastewater network is nearly 540 km long. Additionally, Budapest Waterworks also operates six wastewater treatment plants.

→ Key figures

148 years

of operating experience in Budapest



Significant water utility service provider in Central Europe

Technological developments

19
Patents



International professional experience



Excellent water quality by European standards



Drinking water

- **5380** km water network
- **159** million m³/year production
- **1** million m³ daily capacity
- **766** wells
- **2** treatment plants



Wastewater

- **90** million m³/year treated wastewater
- **370 000** m³ daily capacity
- **539** km wastewater network
- **6** treatment plants

159 million m³
annual water production



16,1%
non-revenue water

1868

Foundation

1904

Construction of the Káposztásmegyer waterworks

1911

Construction of the Margaret Island water tower, the symbol of our Company

1945

Continuous water supply in Budapest during WW II

1963

Construction of the first horizontal well on Margaret Island

1997

Privatization

↙ MOST IMPORTANT COMPETENCIES



Customers

- **2 000 000** supplied population
- **1730** employees



Revenues



23,6 billion HUF
→ drinking water

8 billion HUF
→ wastewater

8,4 billion HUF
→ export /other

2004

2012

2013

Residential water fee 2016

Appearance of
the wastewater
sector

Repurchase

BKSZTT
take over

172.4 HUF/m³+VAT
in Budapest

→ Owners

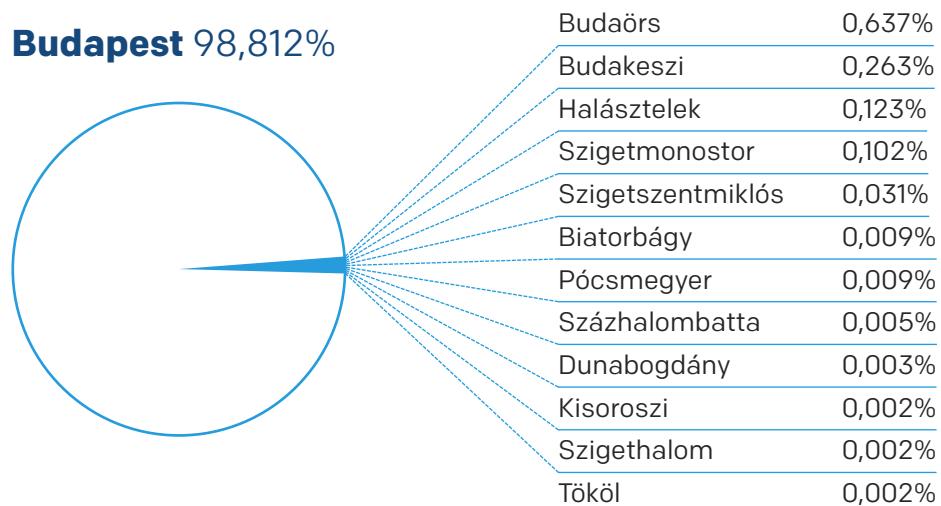
Budapest Waterworks operates as public limited company. After repurchasing the minority share package from foreign investors in 2012 and thus changing the ownership structure of the Company, it is now wholly owned by Municipalities.

As a result of Act CCIX of 2011 (Vksztv.) changes in the Company's activity and service area significantly transformed the structure of the municipal sharehol-

ders as well: the service area expansion meant that the municipalities responsible for the service in the area also became shareholders, thus by the end of 2015 the circle of owner municipalities increased to 13, which has not changed in 2016.

The main shareholder of the Company, owning 98.812 % of the shares is the Municipality of Budapest.

Ownership structure as of 3rd December 2016



→ Management

**Chairman of the Board
of Directors**
András Sármay

Board of Directors
József Dámsa
Dr Csaba Gór
Csaba Haranghy
Béla Hegyeshalmi
János Rimóczi
Bálint Theisz

**Chairman of the
Supervisory Board**
Dr Dénes Kosztolányi

Supervisory Board
János Danada
Sándor Katona
András Kolozs
Máté Kovács
Józsefné Stiffel

Auditor
BDO Magyarország
Könyvvizsgáló Kft.

CEO
Csaba Haranghy

CFO
Ferenc Keszler

DIRECTORS

Technical Investment Director
Gábor Imre Pálffy

**International Business
Development Director**
Tamás Miklós Benze

Support Services Director
Róbert Fritsch

Customer Service Director
Péter Bognár

Water Sector Operational Director
Géza Csörnyei

→ Our mission

Budapest Waterworks supplies about 2 million people with excellent quality drinking water that is an essential element for life, and provides wastewater treatment services to protect fresh water reserves.

Our Company aims to maintain – through efficient business management, sustainable development, quality management, an environmentally conscious approach to ensure the safety of the drinking water, and providing safe work conditions – its position as an outstanding domestic water utility provider and to win the recognition of our interested partners. Our further goal is to achieve international recognition for our service portfolio.



→ Social engagement

Budapest Waterworks as a responsibly operating large company aims to harmonise its business goals with its social responsibility, with particular regard to environmental protection, sustainable development and supporting those in need. In addition to providing high-level service, the Company also pays special attention to act in the interest of the general public.

→ Environmental protection

Our Company's management is committed to the protection of the environment, the prevention of environmental pollution and the continuous strengthening of the Company's environmentally conscious activities. In accordance with the increasing expectations and beyond our core activities we traditionally pay special attention to the detection and management of environmental problems and the prevention of environmental pollution. Environmental protection, drinking water production and water supply form an integral unit in our activities and with this in mind we devote significant funds to the efficient protection of our water resources and the environment.

In order to continuously improve the quality of drinking water and our environmental performance according to our environmental policy, we introduced an environmental management system that encompasses the entire company, which is certified by the MSZ EN ISO 14001: 2005 standard.

With the expansion of Budapest Waterworks' activities the focus on environmental protection has increased significantly. BKSZTT (Budapest Central WWTP), which our company has been operating since 1st June 2013 also obtained ISO 9001 and 14001 certifications.

As a result of the biogas production and introducing technical optimisations, BKSZTT's average yearly energy self-sufficiency level exceeded 62% in terms of electrical energy demand in 2016, and reached nearly 78 % taking into account the total energy demand of the plant. Consequently, our already very good position has further improved compared to international benchmarks. Our gas engines have reached 40 thousand hours of operation this year, therefore we had to carry out some major maintenance works during which period the operating hours were reduced.

The plant constantly maintains its green areas, by planting trees and replanting vegetation, ensuring the 70% proportion of green areas.

The fusion of our commitment to environmental protection and our aspirations for innovation, resulted in winning an EU tender which allowed us to jointly establish an experimental urban farm with Biopolis Plc. The farm presents, with spectacular solutions, the meeting of the water as a vital medium and an innovative, method of crop production that although still rare at present but is expected to become natural in the future. Due to the aeroponic crop production technology which had been developed specifically for urban conditions and which constitutes the base of the Living Island, high quality food crops can be grown in a very small area, without soil and sunshine.

→ Grants

We developed the grant policy of Budapest Waterworks along reasonable and transparent principles. We strived to define guidelines and objectives that reflect the Company's commitment to society and also meet the expectations of the consumers and society at large.

We determine the annual grant budget based on the joint assessment of the economic results and the expected effects among the participants of our operational environment.

The four cornerstones of our grant policy are: responsibility for the environment, healthy living, commitment to ensuring cultured leisure time opportunities for the disadvantaged and those living in our service area.

Therefore in 2016, we primarily helped organisations, institutes, events and charities that were either connected to sports, healthy living, environmental protection and raising environmental awareness. We consider supporting professional water management and water production organizations and events in these fields of utmost importance as we need to ensure the future of water utility services by furthering the education of upcoming generations.

→ Missionary activities

A main priority of Budapest Waterworks' strategy is to provide assistance in areas left without healthy drinking water after a disaster situation. In cooperation with the professional disaster management agencies, our Company has been engaged in the management of domestic disaster situations and emergency water supply since 1986.

In order to support this activity, our professionals joined forces with external partners in 2009 and created a state-of-the-art mobile water cleaning and packaging units that is modular, mounted on pallets and equipped with sand-, ultra-, reverse osmosis filters and a UV disinfectant. A saltwater module was added to the unit in 2014. Beyond the humanitarian aims, our cross-border relief efforts greatly contributed to increase the international awareness and reputation of our Company.

The introduction of the container based, technologically complex ReWater water purification unit provided a new milestone in terms of providing temporary water supply under extraordinary circumstances. The unit is capable of producing clean, healthy drinking water from any sweet water or communal wastewater that has undergone biological purification. The unit has been awarded the Water Innovation Award of the Sustainable Water Solution Exhibition, which was the accompanying event of Budapest Water Summit 2016.





Budapest Waterworks management in 2016

→ Financial situation

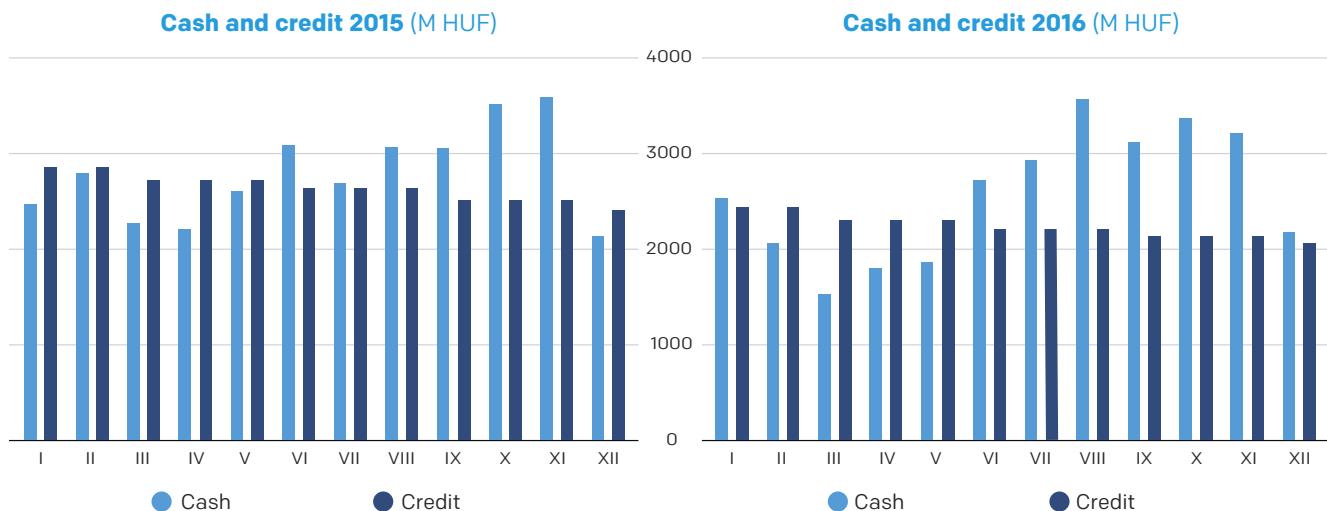
The Company's financial situation and liquidity was stable, and we managed to fulfill all our payment obligations in time.

The replacement of foreign investors' shares was realised by repurchasing our own shares, for which the Company received a shareholder loan. Out of the remaining HUF 4.2 billion loan in 2016 the Company paid back a further HUF 500 million, so the debt by the end of the year was reduced to HUF 3.7 billion.



Finance
Air transport
production
Industrials
energy industry

The closing net cash was HUF 2 196 million which is 1% higher than at the end of year 2015.



→ Revenues

The total revenue of the Company amounted to HUF 39 977 million, which is HUF 2 439 million (5.8%) less than in 2015. Net sales revenue decreased by 4.4% which represents a decrease of HUF 1 723 million.

The 361 million decrease in the drinking water revenue was due to less favourable weather conditions in terms of water consumption compared to last year.

The HUF 1 327 million revenue from sewage services exceeded the revenue in the previous year by HUF 217 million. The increase is mainly due to the fact that several settlements have implemented sewage system developments using KEOP (Complex Water Safety Programme) resources and as a result, the number of sewage system connections increased.

Revenues from other activities decreased by HUF 1 695 million in comparison with the previous year. Revenues from technical activities were higher, among other things due to network troubleshooting services carried out for FŐTÁV (Central Heating Plc). Thanks to Budapest Funeral Institute's (Budapesti

Temetkezési Intézet) move to the central office building there was an increase in the rental revenue.

Revenues from export decreased as the Sri Lanka Project is coming to an end. At the same time, the Indonesian Project – given that our company is involved in it via a subsidiary – produced a smaller revenue as project profit despite the same level of economic performance due to the difference in the method of settlement.

Revenues (M HUF)	2015	2016
Drinking water revenue	23 984	23 623
Sewage service revenue	1 155	1 372
Wastewater treatment revenue	6 651	6 767
Other activities	7 516	5 821
Total net sales	39 306	37 583
Other revenues*	1 787	1 265
Own performance value	1 323	1 129
Total	42 416	39 977

→ Costs, expenditures

Cost and expenditures decreased by 4% compared to 2015. The decrease in expenditures is due to the lower network error rate and the more favourable fuel and electricity prices, while the value of services used increased mainly due to the water utility rental fee payable after taking over the water utility services of Százhalombatta based on a lease and operating agreement, and as a result of maintenance work carried out by external contractors.

In 2016, personnel expenses were HUF 662 million more than in 2015 due to the implemented salary increases, and the increased staff numbers resulting from the new activities (troubleshooting carried out for FÖTÁV and the takeover of Százhalombatta's water utility services).

→ Accounts receivable

Gross receivables decreased from HUF 5 733 million to HUF 4 285 million compared to 2015, accumulated impairment losses + HUF 101 million, which meant that the net accounts receivable changed from HUF 5162 million in 2015 to HUF 3 815 million in 2016.

Outstanding receivables from our own invoiced clientele decreased from 2 696 million HUF to 1 109 million HUF compared to last year.



→ Equity

The composition of the equity had been influenced by three factors: the increasing effect of the HUF 379 million after tax profit in 2016, the retained earnings-reducing effect of the HUF 11 million additional capital contribution paid to subsidiaries and placing the HUF 803 million earned in 2015 into profit reserve.

Equity (M HUF)	2014	2015	2016
Equity	11 803	12 606	12 974
Registered capital	7 978	7 978	7 978
Capital reserve	0	0	0
Profit reserve	2 381	3 825	4 617
Tied-up reserve	0	0	0
Profit after tax	1 444	803	379

→ Earnings

The Company's operational profit was HUF 607 million. The financial result of the Company was minus HUF 3 million, which means a HUF 173 million improvement in result compared to the previous year. The Company's pre-tax profit was HUF 604 million.

The total tax liability of Budapest Waterworks for 2016 is HUF 225 million adjusted with tax base modifying items. Out of this amount, HUF 35 million is corporate tax liability, and HUF 65 million must be paid in taxes abroad for international projects. In 2013, the public utility provider tax was introduced in addition to the corporate tax payable by Budapest Waterworks: the public utility provider tax rate is 31 %, which in 2016 amounted to HUF 125 million based on the results of 2016.

Profit after tax is HUF 379 million.

The Company did not pay dividends in 2016, as they were placed in the 2017 profit reserve.

In 2016 the operating profit increased by depreciation was HUF 6 373 million, compared to HUF 6 907 million in 2015.

→ Profit and loss statement

	2015 (M HUF)	2016 (M HUF)
Revenues		
Drinking water	23 984	23 623
Sewage service revenue	1 155	1 372
Wastewater treatment revenue	6 651	6 767
Industrial water	194	179
Revenue of other activities	2 360	2 737
Wastewater pumping revenues	15	12
Export revenue	4 947	2 893
Total net sales revenue	39 306	37 583
Other revenues*	1 787	1 265
Own performance value	1 323	1 129
Total revenues	42 416	39 977
 Expenditures		
Material costs	2 967	2 720
Electricity costs	2 541	2 361
Material-type services used	8 497	8 580
Cost of sold goods, mediated services	4 722	2 912
Other services	1 441	1 471
Total material expenses	20 168	18 044
Labour costs	7 216	7 669
Personnel costs	937	1 028
Salary contribution	2 180	2 298
Personnel expenses	10 333	10 995
Depreciation	5 417	5 767
Other expenditures*	5 082	4 564
Total expenditures	41 000	39 370
 Operational profit or loss	1 416	607
 Earnings before Interest and Taxes, plus Depreciation and Amortisation	6 907	6 373
Financial operations revenue	126	145
Financial operations expenses	302	148
Financial profit or loss	-176	-3
 Profit or loss before tax	1 240	604
 Tax liability	437	225
 Profit or loss after tax	803	379

* The reason for the decrease in revenue was that due to changes in the business structure the Company participates in the Indonesian project through its subsidiary, thus the revenue generated there does not appear directly as own revenue only at the project revenue level.

→ Balance sheet*

	2015 (M HUF)	2016 (M HUF)
A. Fixed assets	111 018	114 190
I. Intangible assets	615	671
II. Tangible assets	110 106	113 239
Technical equipment, machinery, vehicles	109 384	112 769
Investments	722	470
III. Invested financial assets	297	280
B. Current assets	9 069	7 497
I. Inventories	967	544
II. Receivables	5 926	4 757
Receivables from trade and services (customers)	5 162	3 815
Other receivables	764	942
III. Securities	0	0
Bonds purchased for sale	0	0
Own shares, business shares, shares purchased for sale	0	0
IV. Liquid assets	2 176	2 196
Cash and cheques	2	3
Bank deposits	2 174	2 193
C. Accrued income and deferred expenses	3 246	3 358
TOTAL ASSETS	123 333	125 045
D. Equity	12 606	12 974
I. Equity capital	7 978	7 978
II. Capital reserve	0	0
III. Accumulated profit reserve	3 825	4 617
IV. Fixed reserve	0	0
V. Profit after tax	803	379
E. Provisions	431	303
F. Liabilities	106 739	107 828
I. Long-term liabilities	99 214	102 025
II. Short-term liabilities	7 525	5 803
Advance payments from customers	828	366
Liabilities (suppliers)	4 531	2 415
Short-term credits	375	375
Other current liabilities	1 791	2 647
G. Accrued expenses and deferred income	3 557	3 940
TOTAL LIABILITIES	123 333	125 045

* The balance sheet does not include the impacts of the realignment of balance sheet items carried out in connection to the affiliated companies.

→ Audit Report



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Independent Auditor's Report

to the Shareholders of Fövárosi Vízművek Zrt.

Opinion

We have audited the financial statements of Fövárosi Vízművek Zrt. (the „Company”) for the year 2016 which comprise the balance sheet as at December 31, 2016 (which shows an equal amount of total assets and total liabilities of HUF 125 045 millions and an after-tax profit for the year of HUF 379 millions), as well as the related profit and loss account for the year then ended and the notes to the financial statements including a summary of significant accounting policies.

In our opinion, the accompanying financial statements give a true and fair view of the financial position of the Company as at December 31, 2016 and its financial performance for the year then ended in accordance with Act C of 2000 on Accounting (hereinafter: "the Accounting Act") effective in Hungary.

Basis for the opinion

We conducted our audit in accordance with the Hungarian National Standards on Auditing and the effective Hungarian laws and other regulations on audits. Our responsibilities under these standards are further described in the "*The auditor's responsibilities for the audit of the financial statements*" section of our report.

We are independent of the Company in compliance with the Hungarian ethical requirements pertaining to our audit of the financial statements, and we have fulfilled our other ethical responsibilities in accordance with the same ethical requirements.

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

Emphasis of Matter

We draw attention to the information under Section "5.9 Shareholders' equity" in the supplementary notes, which describes that an amount of HUF 1 399 million out of the retained earnings in the accompanying financial statements has not been considered by the Company as part of the free retained earnings, i.e. above amount is taken into account as tied-up capital, with reference to Section 39 (3) of the Accounting Act, in case limit of dividend distribution is calculated.

Our opinion is not qualified in respect of this matter.



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Other Matters

The financial statements of the Company for 2015 were audited by PricewaterhouseCoopers Könyvvizsgáló Kft. who issued an unqualified audit opinion in the auditor's report dated May 30, 2016.

Other information: the business report

Other information comprises the business report of Fövárosi Vízművek Zrt. for 2016. Management is responsible for the other information and for the preparation of the business report in accordance with the relevant provisions of the Accounting Act and other regulations. Our opinion on the financial statements provided in the section of our report entitled "Opinion" does not apply to the other information.

Our responsibility in connection with our audit of the financial statements is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated.

Furthermore, in accordance with the Accounting Act, our responsibilities regarding the business report also include reviewing the business report to assess whether the business report was prepared in accordance with the relevant provisions of the Accounting Act and other regulations, if any.

In our opinion, the business report of Fövárosi Vízművek Zrt. for 2016 corresponds to the financial statements of Fövárosi Vízművek Zrt. for 2016 and the business report was prepared in accordance with the provisions of the Accounting Act.

As the Company is not subject to additional requirements under any other regulation in connection with the business report, our opinion on the business report does not include an opinion under Section 156 (5) h) of the Accounting Act.

In addition to the above, based on the information obtained about the Company and its environment, we must report on whether we became aware of any material misstatements in the other information and, if so, on the nature of such material misstatements. We have nothing to report in this regard.

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

Management is responsible for the preparation and fair presentation of the financial statements in accordance with the Account Act, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

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

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



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The auditor's responsibilities for the audit of the financial statements

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

As part of an audit in accordance with the Hungarian National Standards on Auditing, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

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

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



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 Konyvvizsgáló Kft.
 1103 Budapest, Köér utca 2/a,
 Laurus Irodaházak C épület
 1476 Budapest, Pf.138.

Report on other legal or regulatory obligations: unbundling of accounts

Referring to our obligation prescribed by Section 49 (4) of Act CCIX of 2011 on Water Utility Supply and Section 105/A (1) of Act LXXXVI of 2007 on Electric Energy, we certify that the rules the Company has adopted and applied in connection with the requirement of unbundling of accounts as well as the pricing of transactions between the various activities contain effective facilities to avoid cross-subsidization between the various divisions of the Company.

Budapest, 3 March 2017

BDO Hungary Audit Ltd.
 1103 Budapest, Köér utca 2/A
 Registration number: 002387

Zsuzsanna Jasper
 Zsuzsanna Jasper
 Managing Director

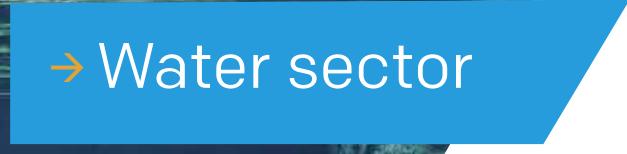
Péter Kékesi
 Péter Kékesi
 Certified Auditor
 Chamber registration No.:
 007128



This is the translation of the original Hungarian statutory report. In case of any discrepancies, the original Hungarian version prevails.

BUDAPEST WATERWORKS' ACTIVITIES IN 2016





→ Water sector

→ Water production capacities

The water production and distribution facilities were operating throughout the year with adequate capacity and operational availability. As a result of the takeover of Százhalombatta water utility operation, the nominal water production capacity increased compared to last year, to 1 010 cubic meter per day on 31st December 2016 compared to the 967 cubic meter in 2015.

The Company was able to fully meet water demands at all times.

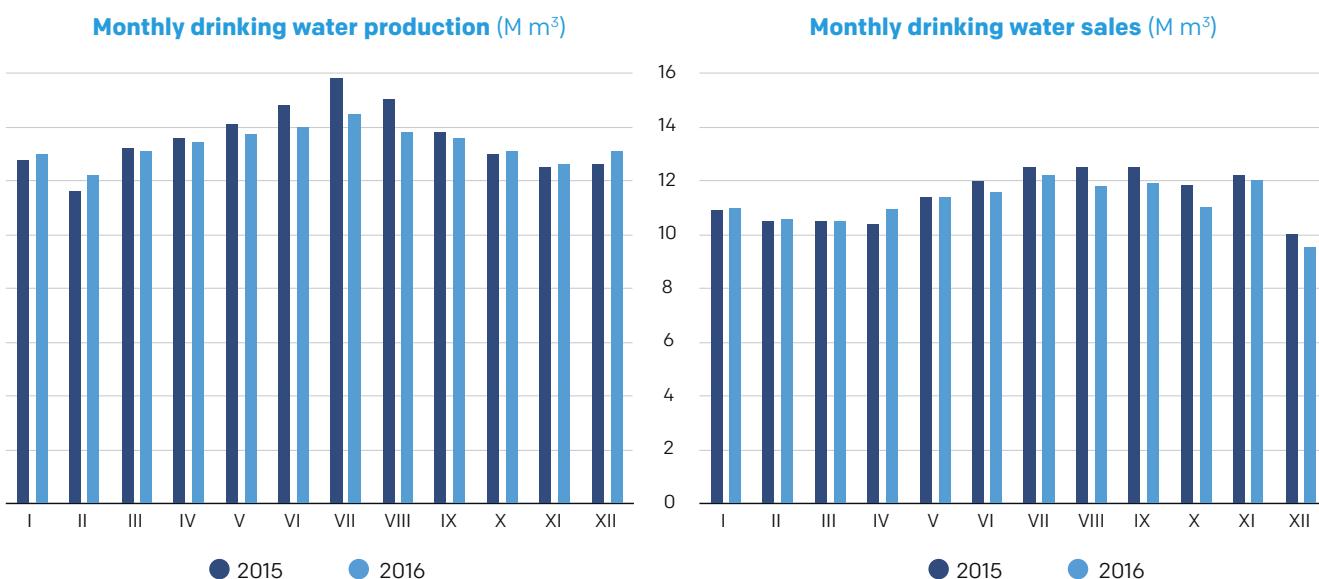
→ Drinking, industrial water production and sales

In 2016 drinking water production amounted to 159 086 thousand m³, which is 2.3% lower than in the previous year.

The highest daily production was 573 thousand m³ in July which is 33 thousand m³ less than the maximum production in the previous year. The 435 thousand m³ daily average drinking water production is 11 thousand m³ less than in the previous year.

The invoiced drinking water volume (without accruals) was 134 735 thousand m³ in 2016. Compared to the sales of the previous year this represents a decrease of 1.8%. Taking the accruals into consideration the decrease is 2.2%.

The annual industrial water production amounted to 1 386 thousand m³ in 2016, which is 15.9% lower than in 2015.

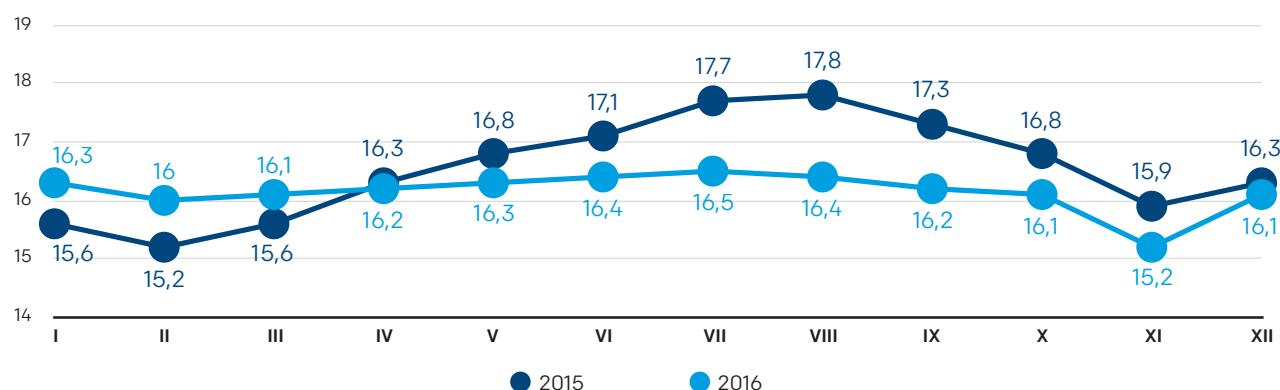


→ Non-revenue water

The value of non-revenue water – calculated of the cumulative production and sales data of the last 12 months up to the reference month – was 16.1% in 2016, which is 0.2 % lower than in 2015. The previously launched projects aimed to reduce the amount of

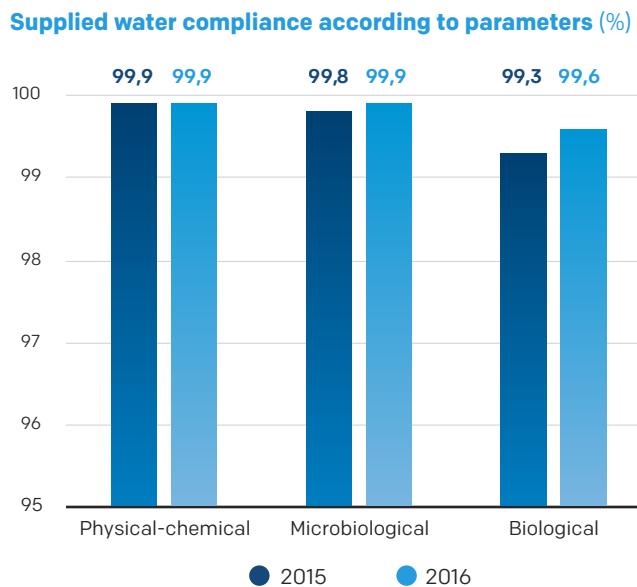
non-revenue water continued in 2016, such as pressure management (development of pressure-controlled areas, pumping stations, fine-tuning pressure boosters, zone conversions), DMA-development, improvement of water loss analysis monitoring.

Non-revenue water 2015–2016 (%)



→ Water quality

Budapest Waterworks continued to carry out providing water services in strict compliance with the Hungarian and EU regulations regarding water quality in 2016, ensuring adequate water quality for the population, industrial and public entities, and for associated companies.



The Company monitors drinking water quality according to the sampling plan approved by the Public Health Authority (Government Office of the Capital City Budapest, Policy Administration Services of Public Health formerly National Public Health and Medical Officer Service), based on the parameters and requirements stipulated in the Government Decree No. 201 of 2001. (25 Oct) and the related legislations regarding quality standards and drinking water monitoring.

The monitoring process of water quality covers all of the factors affecting the quality of the drinking water. In 2016 the Company conducted an analysis of 184 920 parameters in the course of testing 9 906 samples. Out of the total samples taken, with regards to the supplied water (points of consumption, reservoirs, pumping stations, inlet points) 73 642 parameters were analysed in 3 448 samples. Compliance based on the parameter numbers was **99.84%** and total compliance based on the sample numbers was **97.53%**. Both values are higher than last year's data.



→ Wastewater sector





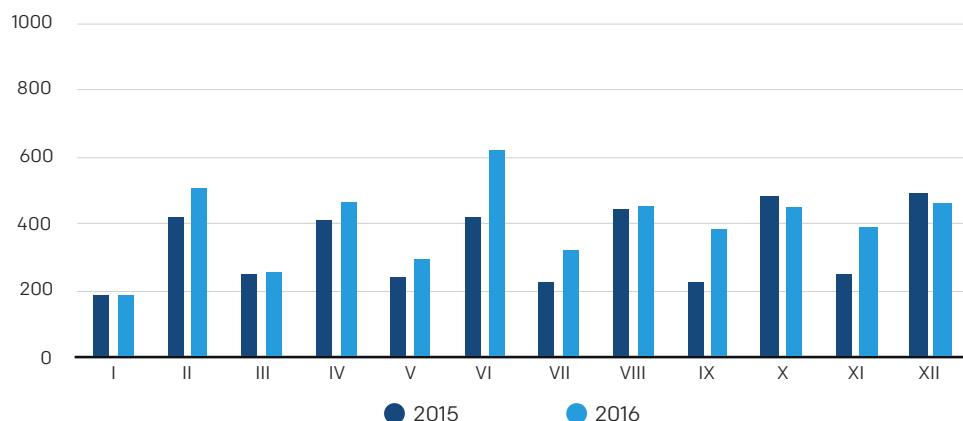
→ Wastewater treatment, sewage services

The Company's wastewater treatment and sewerage service activities have been further strengthened. A major change occurred when in April 2016 the Company took over the operation of the sewage services and wastewater treatment plant of Százhalmabatta. With this addition, Budapest Waterworks now manages the sewage services of 10 settlements, and is responsible for the operation of six wastewater treatment plants.

Developments carried out within the framework of the KEOP (Complex Water Safety Programme) Investments in the area of Szigetszentmiklós, Budakeszi, Szigetmonostor and Pócsmegyer in 2014–2015 greatly contributed to the modernisation of the wastewater networks of these settlements, as a result of which further newly canalised settlement areas have been added to the operation and asset management portfolio of the Company.

As a result of the network developments, the length of the wastewater network operated by Budapest Waterworks grew from 417 km to 539 km this year, while the number of large public booster stations on the network increased from 81 to 144. By the end of 2016 the Company was also operating 500 public small booster stations of the Presskan system in Tököl and 1 021 boosters that belong to private homes.

In 2016 the wastewater treatment plants received a total of 5 923 thousand m³, a daily average of 16 183 m³ of wastewater, which means a 77% of capacity utilisation. As a result of the KEOP (Complex Water Safety Programme) developments the previous overload of the plants has been eliminated.

Sewage service (thousand m³)

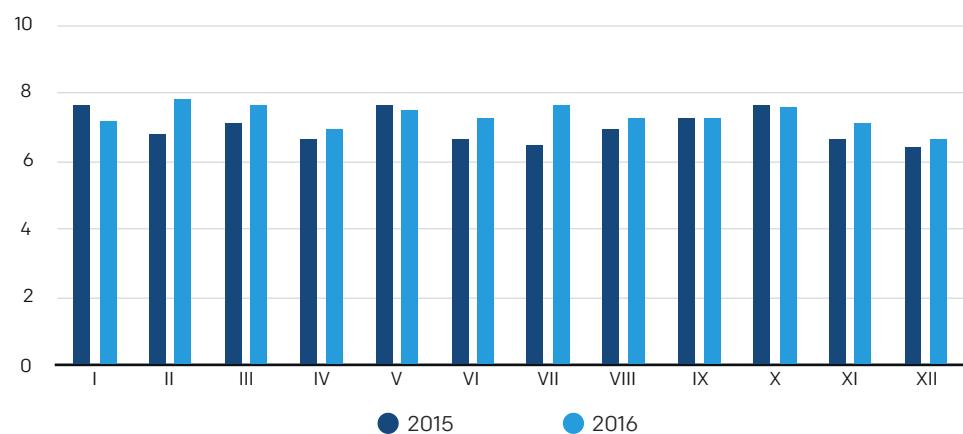
With the accruals, a total of HUF 1 372 million in revenue had been generated from sewage services, consisting of HUF 4 million of base fees, HUF 1 233 million from consumption charges, HUF 54 million revenues from wastewater treatment and HUF 81 million from water load fees.

In the course of 2016 the Central Wastewater Treatment Plant in Budapest issued invoices for a total of 88.2 million m³ of treated wastewater which represented a 4.7% increase compared to the previous year.

Taking into consideration the 350 thousand m³/day maximum capacity of the plant, the average 249 thousand m³/day load resulted in a 71% average capacity utilisation rate.

The HUF 6 767 million wastewater treatment service revenue was HUF 116 million higher than in the previous year. The main revenue sources within the wastewater treatment were: HUF 2 587 million from wastewater treatment service fees, nearly HUF 413 million from water load charges, HUF 2 879 million from rental fees, HUF 874 million from sludge treatment service fees, and HUF 14 million from property insurance.

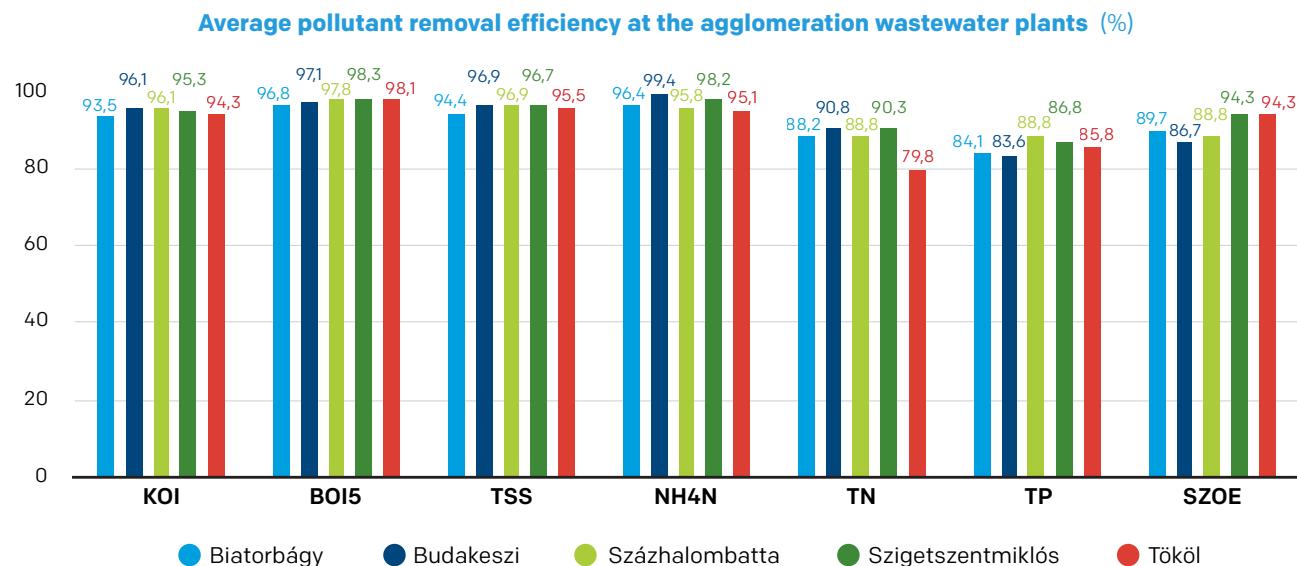
The Company has been in negotiations with the Municipality of Budapest with regards to reimbursement of the additional costs incurred in the third cleaning phase, since the purpose of this investment was to comply with the TP80 TN70-80 percentage removal efficiency EU regulation expected by the Municipality, as opposed to local regulations.

Monthly wastewater treatment (M m³)

→ Wastewater quality

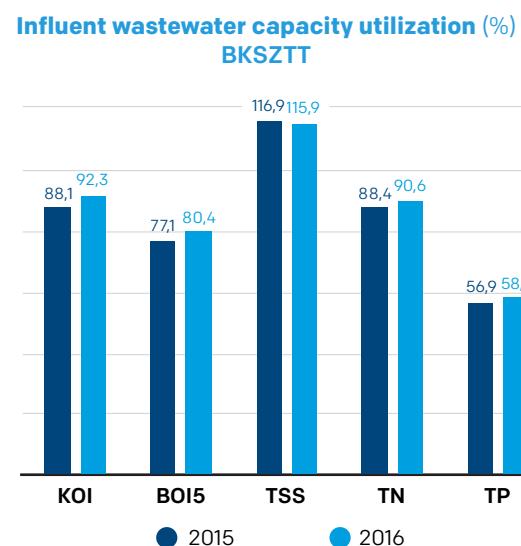
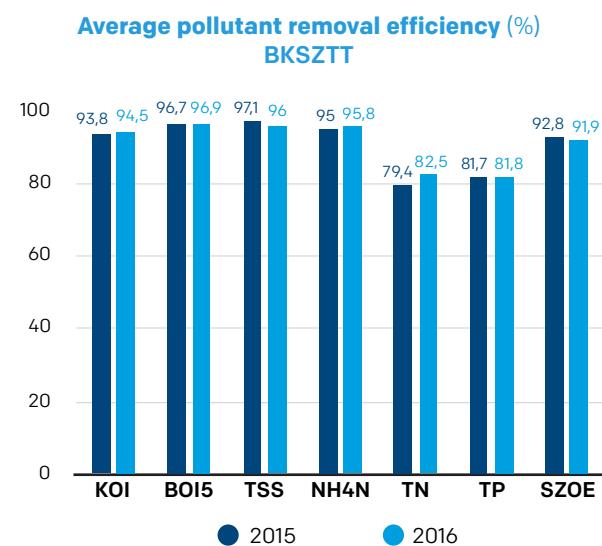
Accredited measurements are carried out on a monthly basis in the wastewater plants that were taken over by our company in the agglomeration zone. Both the inlet and outlet wastewater are analysed based on 7 different parameters. In 2016 a total of 57 measurements were carried out. Out of the 339 parameters examined

in the 57 samples, only 3 parameters (significantly less than in 2015) exceeded the limit value in a particular month. The exceedances can be traced back to substantial rainfalls on the day of or the day before the measurement, which caused a sudden increase in the inlet wastewater amount to the plants.



At the Budapest Central Wastewater Treatment Plant 24 accredited measurements are carried out per year on the inlet, on the pre-settled, and on the outlet wastewater points, in a pre-determined schedule.

In 2016, all the measured values were within the specified value range with only one exception. Additionally, technological measurements are also carried out daily in the wastewater laboratory of the plant.



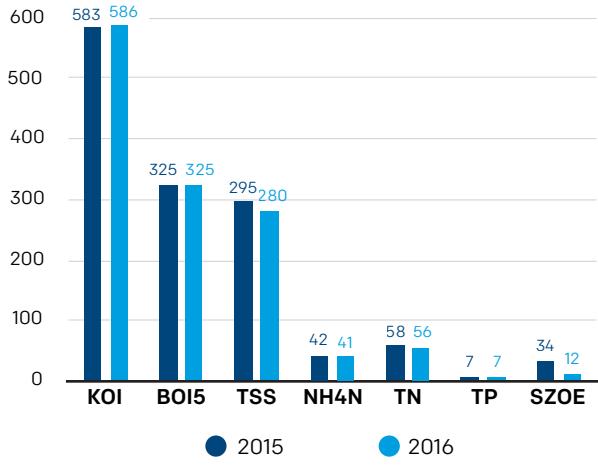
The outlet water quality values are excellent. The quality of the treated water released back into the Danube meets the strict European standard. With respect to the two most important parameters of fresh water eutrophication, the total nitrogen (TN) removal efficiency significantly exceeds 70% and the total phosphorous (TP) removal efficiency is above 80%.

The inlet water quality values – apart from suspended solids – remained below the design value (100%). This is important, because the amount of incoming

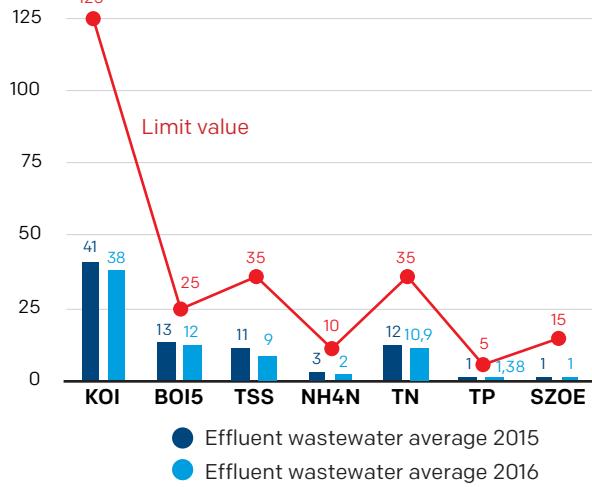
pollutants have an effect on the technological processes, and an increase of the pollution levels generates an increase in the operation and maintenance costs.

The total suspended solid load deserves a special mention. The daily average suspended solid load to the plant exceeds the maximum design value. Through careful operation, the Company continued to control the overload; however it required continuous and increased attention in terms of equipment maintenance.

Influent wastewater quality – BKSZTT (mg/l)



Effluent wastewater quality – BKSZTT (mg/l)



→ Service charges

→ Drinking water and sewage service charges

The charges for drinking water and wastewater services are determined by the Pricing Authority. As of 2012, pursuant to the provisions of the Water Utility Service Act, municipality pricing had been replaced with central price regulation.

In the future, the fees for utility drinking water supply, utility wastewater drainage and treatment will be determined – taking into account the proposal of the Hungarian Energy and Public Utility Regulatory

Authority – by a ministerial decree issued by the minister responsible for water utility services. As the charges have not changed since the Act came into effect, the Company continued to charge the same fees in 2016 that have been effective since 2013. With regards to the water utility provision services of the agglomeration settlements, Budapest Waterworks charges the previously used water and wastewater service fees adjusted according to the requirements of decreasing the public utility charges.

The most common water service charges in the Company's service area

	2015	2016
Budapest residential water consumption fee (HUF/m ³)	172,40	172,40
Budapest industrial and public water consumption fee (HUF/m ³)	198,90	198,90

→ Wastewater treatment charges (Budapest Central WWTP)

Under the terms of the Wastewater Treatment Service Agreement between the Municipality of Budapest, Budapest Sewage Works (FCSM) and Budapest Waterworks, Budapest Sewage Works is obligated to pay a water treatment service fee to the operator of the Central Wastewater Treatment Plant since 1st June 2013.

The wastewater treatment service fee includes, in addition to the wastewater treatment, the water load and the sludge recycling fees and rental and property insurance charges. The wastewater treatment fee is

a charge proportional to the amount of the treated volume (HUF/m³) and is invoiced by the Company based on the inlet wastewater volume. The water load charge is determined on the basis of the existing legislation, while the sludge recycling fee, the rental fee and the property insurance charges will be invoiced according to the actual incurred costs.

The law stipulates that the wastewater acceptance fee falls under central price regulation. The determination of this fee shall be the competence of the minister responsible for water utility services in the future.



→ Additional services

Capitalising on the technical, operational and service experience accumulated over almost one and a half centuries of its existence and its well-trained professionals, Budapest Waterworks successfully participates in international projects that aim to modernise the drinking- and wastewater service system of certain areas either within the framework of intergovernmental cooperation or through independent tenders.

Our well-trained and prepared experts who regularly publish in Hungarian and foreign professional journals and are invited to conferences all over the world, are the backbone of our domestic and fast-growing international successes in the drinking water and sewage service, and water and wastewater treatment sectors.

We have entered into negotiations with several cities recently regarding consultancy, technology development and prime contracting services.

Within the framework of our cooperation we provide our partners with services, technological and management solutions that can help them raise their standard of service and ensure a higher level of supply security, increase operational efficiency, reduce losses, and improve customer satisfaction. An example for such cooperation is the agreement with the

National Water Supply and Drainage Board of Sri Lanka's capital city, Colombo, for the reconstruction works of two water treatment facilities. In this project our company had to carry out the modernisation and improve the safety of the plants that supply water for part of Colombo (a city of 2.4 million inhabitants) and the surrounding area. The expansion of the capacity required by the contracts and improvement of the cleaning efficiency were successfully implemented on both plants, and additionally, Budapest Waterworks had also developed a new sludge management technology. The project was completed with the technical acceptance procedure on 26th February 2017, which date marked the beginning of the one year technical support and warranty period.

Negotiations have been ongoing in preparation of the contract for construction of a water treatment plant on the Red River near Hanoi, Vietnam.

The public procurement project announced by the Indonesian Public Works Ministry was awarded to the consortium of Budapest Waterworks and Artha Enviromata Jo Joint Operation led by Budapest Waterworks. Within the framework of the project, the consortium is entrusted with constructing water treatment units in a total of 34 settlements on three islands of Indonesia (Sumatra, Java and Sulawesi).

In October 2016 a team of 5 volunteers from Budapest Waterworks had been asked through the Ministry of Foreign Affairs and Trade of Hungary to ensure the drinking water supply of the approximately three thousand people living in a refugee camp in Hatay

province, on the Turkish-Syrian border. The treatment unit was funded by the state of Hungary, and it is still in operation servicing the local population. In addition to ensuring the continuous drinking water supply, the team's other priority was to provide a solution to ensure the reliable and undisrupted operation of the water purification unit after their return home, so the IT and operation specialists of the Company have developed and are still operating a remote internet connection through a laptop.

Representing Hungary, Budapest Waterworks was one of the participants in the EU-founded 18-month-long project called EUrban Water Aid (EUWA). The task of the participants was to carry out a complex urban water purification and flood rescue field practice on the Tisza river. Budapest Waterworks participated with mobile water purification equipment and with a team of experts in the large international field practice.

Within the framework of an international programme created by two world organizations, UN-Habitat and GOWPA, Budapest Waterworks, Subotica Waterworks and Budapest Sewage Works have signed a partnership agreement to facilitate the capacity development of Subotica Waterworks.

Our Company has successfully passed a major test in a EU tender based on an unprecedented international collaboration. The AquaNES project aims to support innovative water management and water purification processes by emphasising the joint use of natural and artificial water purification technologies. We were able to participate in Budapest Waterworks' first research-development and innovation project financed directly by the EU as a member of an international consortium. We submitted the winning tender prepared in cooperation with 7 institutes from seven other countries. The project also had significant non-quantifiable benefits such as knowledge transfer, the emergence of new market opportunities in Europe and additionally, the right to use the products produced for the project.

Following a discussion between Hungarian and Russian professionals and as a continuation of market research and negotiations supported by the Hungarian Government in 2015, we have started negotiations in 2016 with the leaders of the Ural Federation District regarding a potential cooperation to modernise the public water supply and drainage system as required by the Russian Federation and the management of water supply in cities with a concession from the state.

→ Investments

The Company's total investments amounted to a total of HUF 5 592 million in 2016, while the value of investments rolled forward to 2017 is HUF 194 million. A total of 15 km of pipelines were upgraded in 2016, out of which 14 km was part of the water network, and 1 km was part of the wastewater network reconstruction works.

→ Maintenance, operation

In 2016 the Company spent 5 617 million HUF on maintenance and operation. Works related to the water network represented a HUF 209 million higher value than in the preceding year.

Maintenance, operation (M HUF)

	2015	2016
Troubleshooting	2 351	2 321
Water network	1 594	1 691
Water production	183	169
Wastewater	418	282
Support area	156	179
Maintenance	2 365	2 228
Water network	642	719
Water production	428	371
Wastewater	394	317
Support area	901	821
Operation	939	1 068
Water network	441	476
Water production	498	436
Wastewater	0	156
TOTAL	5 655	5 617

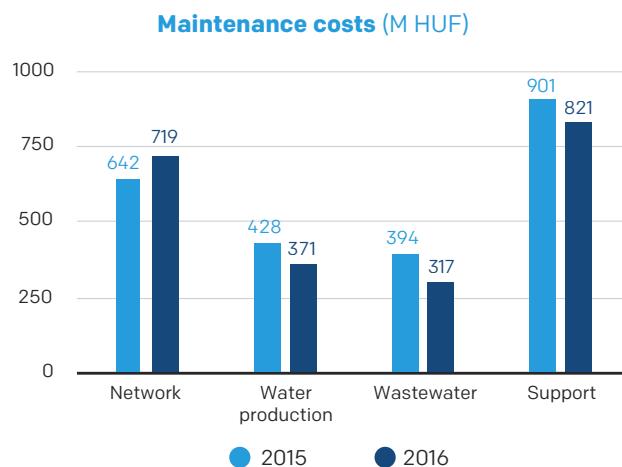
→ Preventive maintenance

In 2016, the costs of preventive, scheduled maintenance was 5.8% lower compared to the preceding year, while the Company spent 12% more on network maintenance, mainly on the maintenance of the service pipes and fittings.

Although the water production sector spent 13.3% less on maintenance than in the previous year, however due to the effective cost management more works have been completed than in 2015. Continuing the rationalisations of the previous years, some of the works that did not affect the service level remained in deferred status.

In the wastewater sector, a large portion of the HUF 58 million maintenance cost was spent on the maintenance of the large booster stations and the wastewater network of the agglomeration settlements. Simultaneously, the maintenance works of the site buildings, wastewater plants and the presskan system in Tököl were also carried out.

The total of HUF 189 million preventive maintenance costs of the Budapest Central WWTP represented a 2% rise. Nearly half of all maintenance costs occurred on the water line, but the costs of the sludge management works, the gray- and green surface maintenance and the biogas recovery were also significant.

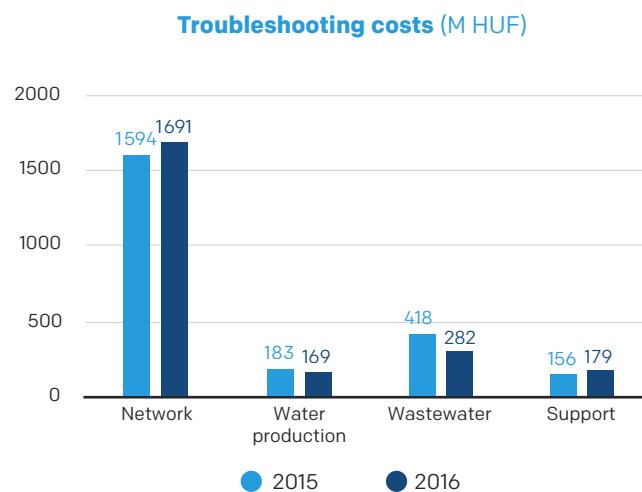


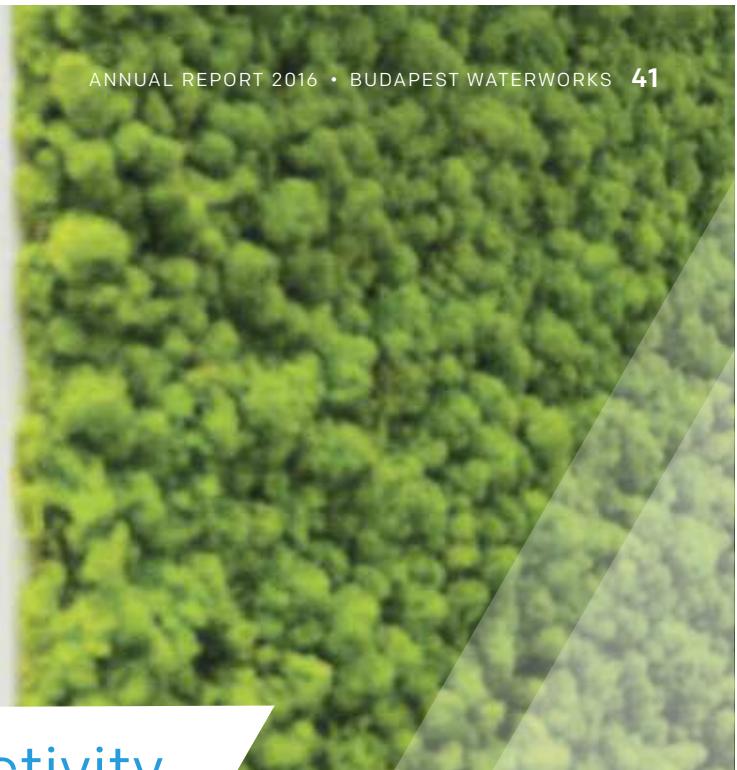
→ Troubleshooting

The number of network failures decreased by a total of 8.8% compared to 2015. Despite this, the network troubleshooting costs were HUF 97 million higher than in 2015, which resulted from the number of hours spent on repair works.

The number of failures in the water production facilities increased by 27.6 % compared to 2015, while the amount spent on repairs decreased by 7.7%.

Troubleshooting costs of the wastewater sector and the agglomeration, decreased by 57% compared to the last year. The repair works on the large pumping stations and presskan system of Tököl represented the bulk of the HUF 111 million total cost. In the case of Budapest Central WWTP in 2016 most of the repair works were done on the water line and the sludge line, but the repair costs carried out on the biogas recovery were also significant. Altogether, the percentage of troubleshooting works increased by 8.4% compared to 2015 and the costs were 8.9% higher than in the preceding year.





→ Customer service activity

Budapest Waterworks' customer service areas are certified according to the MSZ EN ISO 9001:2008 standard. SAP's IS-U module provides the IT background for this activity, as well as handling the record-keeping of water meters, the organisation of meter replacements, meter reading and invoicing, invoice management and debt collection and customer relations. Results of the customer satisfaction surveys demonstrate that they are greatly satisfied with the online customer service.

The Company's environmentally conscious approach is reflected in the electronic process of the incoming requests as a result of which the work is not only faster and more flexible but also paperless.

In 2016, the company introduced the automatic customer service feedback feature of the call centre, through which at the end of the call customers can rate the received service, the preparedness and politeness of the administrator.

The www.vizmuvek.hu website is also available in a mobile friendly version; moreover, customers can get up-to-date information about maintenance, news, or methods of administration via smartphone.

In addition to the phone and online administration, we still have many people visiting our customer service offices in person where, for the sake of more comfortable and efficient administration, five other capital city service providers joined Budapest Waterworks in 2015 to cater for customers' needs.

The company is present in Budapest with two more customer service points. In the service areas outside of Budapest we also operate customer service branch offices and customer points previously established by local municipalities.

In its personal customer service offices Budapest Waterworks also performs customer service activities for other service providers.

In 2016 the "one stop" customer service was used by nearly 1 million people, we received over 400 thousand phone calls, 150 thousand visitors in person, 110 thousand letters and nearly 30 thousand e-mails. Our online customer service was visited by over 160 thousand people.

The Otthon+ (Home+) application introduced in 2015 provides customers with easy, fast and secure access. The application which by 2016 was already used by nearly 20 thousand customers is available on Android and IOS smartphones as well as on Windows Phones.

A 24 hour toll-free number was launched to record meter readings in August 2015. The number that can be called from landlines also serves a faster and more convenient administration.

According to the resolution of the Hungarian Energy and Public Utility Regulatory Authority we renewed our Business Policy in 2016. The Policy is also available on the company's website.

→ Human resources

→ Headcount

In 2016 the annual average statistical headcount was a total of 1770 people, out of which the number of full time employees was 1746. The increase in staff number was mainly due to the demand caused by taking on troubleshooting activities for FÖTÁV and taking over Százhalombatta's water supply services.

→ Payroll management

In 2016 the Company implemented a 2 plus 2 percent pay increase according to the agreement with the workers' unions, from which the second raise was calculated based on the performance in the first six months of the year.

→ Education, training

The Company's total budget for training in 2016 was HUF 50 million, thus the Company's employees attended a total of 3194 trainings.

As in recent years, we prioritised trainings that helped to ensure that the Company complied with its legal obligations and employees were able to keep up-to-date with the legislative changes and gain the professional knowledge necessary to fulfill their responsibilities. We also continued to put great emphasis on internally organised development programmes and trainings in 2016. In order to help the integration of new employees, the internally organised training programme called Company School (Cégiskola) was utilised on multiple occasions similarly to previous years' practice.

In 2016, the Company launched an internal trainer and instructor programme, which is currently training 18 of our co-workers who are expected to conduct their first training sessions in the spring of 2017.

→ Organizational changes

Budapest Waterworks restructured multiple departments in 2016, continuing the practice of previous years. The primary objective of these changes was efficiency improvement and optimal structuring of the processes.

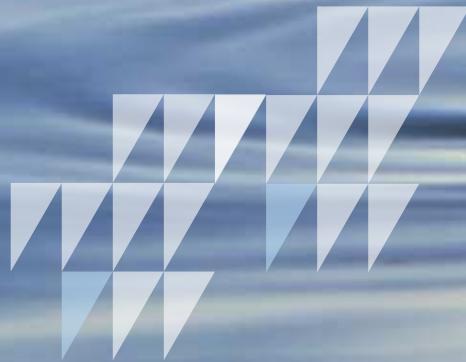
The larger organizational changes mainly affected the Water- and Wastewater sector operation directorates, and the Customer Service Directorate. Within the Customer Service Directorate the Meter Reading and Field Investigation Department had been established, which took over the responsibilities and activities from the Water Sales Department related to main- and submeter readings.

As of 1st May 2016 the Chief Technology Officer (CTO) position had been eliminated and in parallel, the Water Management Directorate and the Wastewater Management Directorate continued their activities in one organization, as Operations Directorate. At the same time the change also meant that the Technical Investment Directorate and the Operations Directorate became directly supervised by the CEO's Office.





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CEO's office, 2016





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