Message from the Chairman & CEO

DEAR SHAREHOLDERS,

2017 was the most successful year in the history of the OTP Group so far; our improving performance was acknowledged by investors, analysts and credit rating agencies as well as by the most important forums and publications that hand out professional awards. Based on our excellent figures, the Bank is one of Europe's most profitable and best-capitalised banks, and boasts one of the highest valuations.

The Bank Group's outstanding performance last year is attributable primarily to the favourable operating environment, and more specifically to the economic conditions in Hungary, which were the best in many years. 2017 was the first year since the crisis when economies grew in all the countries in which the Bank Group is present, and most macroeconomic indicators also developed positively. We expect these developments to continue into 2018.

In addition to achieving excellent financial indicators, it is at least as important for a bank to achieve its mission in terms of its core operations – that is, provide competitive, modern financial products and high-quality services to its customers – through increased activity and growing business volumes. 2017 marked a turn in this respect as well: we saw our performing loan portfolios grow in every market and every important product category. The fact that the Bank's liquidity has been stable for years provided a favourable background for dynamic lending: FX-adjusted deposits showed con siderable growth, and liquid reserves continued to increase. Improving business activity was also made possible by the OTP Group's strong capitalisation, which exceeds the average of our regional competitors.

While the development of the Group's profitability is essentially the result of excellent organic activity and continuous innovation, we also completed several successful acquisitions: Splitska bank of Croatia was consolidated in May 2017, followed by Vojvodjanska banka of Serbia in December, while we also managed to take over AXA Bank's Hungarian portfolio. As a result of the above, the Bank achieved a substantial increase in market share in the relevant markets and market segments. The Bank Group intends to continue its regional expansion going forward; the liquid capital in excess of the capital strength that the management considers optimal is to be allocated to further value-creating acquisitions. The successful acquisitions also mean that the Bank Group's balance sheet and earnings structure will be much more balanced, as the weight of non-Hungarian operations will increase continuously in the future.

As a key prerequisite for our future efficient and profitable operation, the changes to regulatory systems in any of our markets should not violate the principle of competitive neutrality, and governments and supervisory authorities should only intervene in trends to an extent that reasonably accommodates the principles of consumer protection and drives all market players toward financial awareness. After the financial crisis, it is almost inevitable that regulators tighten their requirements. Capital requirements have increased significantly several times in recent years, and new resolution mechanisms are being introduced. The current favourable period is necessarily a kind of preparation for another cyclical correction. I do hope that 2016 marked the end of a period of several lessons and major negative developments for us; in 2017 we had a successful year in every respect, and in 2018 we intend to build on the processes that have taken root.

Overview of financial performance in the year 2017

In 2017 the Bank Group achieved the highest accounting and adjusted profits in its history, which the result of several factors. The most significant of these is that the operating environment was favourable in every country. It is at least as important that as a result of the above, we saw a turnaround in lending: performing loans grew at a dynamic pace both through acquisitions and organically. In a supportive macroeconomic environment the quality of our loan portfolios continued to improve, and at the same time the costs of risk dropped by half; the proportion of loans 90+days overdue decreased substantially, and the annual risk cost ratio fell to the pre-crisis level, and indeed below it. The year-on-year development of consolidated profits was also affected positively by our acquisitions: the Croatian Splitska banka contributed 8 months' earnings, the Serbian Vojvodjanska banka contributed one month, while the purchase of AXA Bank's portfolio had a basis effect (only 2 months' profits were recognised in 2016). Finally, the cut in the Hungarian corporation tax rate from 19% to 9% and the further reduction in Hungary's bank tax rate also had a positive impact on our bottom line.

The Bank Group's accounting after tax profit was HUF 281.3 billion compared with a profit of HUF 202.5 billion a year earlier. The ROE calculated from the accounting profit was 18.5%. Similarly, to the year 2016, the difference between the accounting profit and the adjusted after tax profit was again small in 2017: the total amount of adjustment items (–HUF 2.7 billion, after tax) was limited.

The consolidated adjusted after tax profit was HUF 284.1 billion (+41% y/y), with Splitska banka and Vojvodanska banka contributing a total of HUF 11 billion in adjusted after tax profit to the results of the Group. The ROE calculated from the consolidated after tax results was 18.7%, while adjusted ROA was 2.37%.

I am pleased to report that the Bank achieved, and indeed exceeded, its key goals for 2017, and accordingly

- our profitability was much higher than the 15%-plus ROE set as a target alongside a 12.5% CET1 ratio. The actual figure was 22.5%! I should emphasise that most key group members posted a year-on-year improvement in ROE; the performance of the Ukrainian subsidiary (47.1%) was outstanding in this respect.
- performing loans increased by 10% organically and by 25% including acquisitions, that is, by HUF 1,401 billion in total. Within the overall figure, we saw particularly robust growth in corporate loans (+34%, or 14% without the acquisition effect) and consumer loans (32% and 14%, respectively); it is pleasing that finally in 2017 the mortgage loan portfolio grew as well (+10%, or 2% without acquisitions). There were many excellent standalone performances:
  In Hungary we saw growth in every category, in Bulgaria the increase in retail portfolios gained new momentum, while in the Russian market the volume of consumer loans increased by almost 20%.

- the net interest margin dropped by 16 basis points, that is, within the indicated range, without the acquisition effect. It should be emphasised, however, that the overall impact of the interest rate environment was negative: benchmark rates fell (the 3-month BUBOR, for example, plummeted from 37 basis points to 3 basis points in a year), yield levels decreased all round, and competition intensified in our biggest markets (Hungary, Bulgaria, Russian consumer loans).
- risk costs dropped by half year-on-year as a result of the supportive macroeconomic environment. All our risk indicators improved: the DPD90+ ratio dropped to 9.2% – and to 6.4% in Hungary – while the annual risk cost ratio was 0.43%, versus 1.14% in 2016.
- in terms of operating costs we fell slightly short of the 2017 target. The reason is that wage inflation was considerably higher than planned in almost every country we operate in, while there was a tangible increase in the costs related to continuous developments and digitalisation, plus our increasing business activity entailed a higher marketing spend.
- with regard to acquisitions, we had two successful deals in 2017, spending a total of EUR 550 million (425 + 125) on buying Splitska banka and Vojvodjanska banka. Both transactions were completed at below book value, integration is in progress, and we expect all cost synergies to be tangible by 2019–2020.
- As for dividends, in 2016 we paid HUF 53.2 billion in dividends from an accounting profit of HUF 202.5 billion; subject to the approval of the general meeting, we are planning to pay out HUF 61.32 billion from our 2017 profit. This means that after a dividend per share of HUF 192.5 in 2016, our shareholders can expect a dividend of about HUF 220 this year. Total dividends will increase by 15% year-on-year.

The foreign subsidiary banks' share of the annual consolidated, adjusted after tax profit decreased from 38% to 35% despite the fact that several of them improved their annual results significantly and the foreign profit contribution was also boosted by the two successful acquisitions. The reason lies in the outstanding performance seen in Hungary.

OTP Group's IFRS consolidated Common Equity Tier1 (CET1) ratio was 15.3% at the end of 2017 (–0.5 pp year-on-year). This already includes the effect of the net profit for the year, less accrued dividends. The year-on-year drop is attributable in part to the total –190bp effect related to the acquisition of Splitska banka and Vojvodjanska banka, and also to the 15% year-on-year growth in total dividends and the larger risk-weighted assets (RWA).

Individual performances of banks in the group

OTP Core (the Group's Hungarian core operation) achieved a HUF 168.6 billion adjusted after tax profit in 2017 (+38% year-on-year). The result for the year was shaped by the improving operating profit and the favourable development in risk costs. Performing loans increased by 11% year-on-year, outstripping consolidated organic growth. The higher income derived from improving business activity offset the negative impact of the ongoing erosion of interest margins. The quality of the loan portfolio continued to improve; the DPD90+ ratio dropped by 3.4 pps year-on-year to 6.4%, and provisions totalling HUF 30.8 billion were released over the year as a whole.

Dynamic lending growth was evident in every loan category: consumer loans increased by 25%, corporate loans by 18%, micro and small business loans by 13% and mortgage loans by 2% year-on-year. It is pleasing that mortgage loan applications and disbursements continue to show double-digit growth, and the Bank is a key player in the disbursement of subsidised home loans: within the framework of the so-called Family Home Ownership Subsidy (CSOK) programme the Bank received subsidy applications of HUF 39 billion in 2017, and the volume of disbursements increased to HUF 52.6 billion.

The Bank's net loan/deposit ratio is 49%, so it has ample liquidity to meet the demand for loans in Hungary, which we hope will strengthen further.

The **Hungarian Merkantil Bank and Car** realised record-high adjusted after tax profit in 2017 (almost HUF 8.3 billion) and substantially increased its FX-adjusted performing loan portfolio.

OTP Fund Management also realised its highest-ever profit at HUF 8.3 billion, and improved its domestic market position significantly.

The **DSK Group** effectively repeated its performance of the previous year, and its HUF 47.4 billion after tax profit remains the second highest within the OTP Group. Loan repricing resulted in shrinking margins, which had a negative effect on interest income, but we managed to partly offset this with a 7% increase in performing loans. In addition to the outstanding performance seen in the corporate segment, retail loan volumes also registered notable growth. Stable profitability was in part the result of the improvement in portfolio quality; the annual ROE was 20%.

The **Russian subsidiary bank** (excluding Touch Bank) realised an after tax profit of HUF 27.8 billion (+35% year-on-year). Operating earnings rose by 16% year-on-year, and the consolidating macroeconomic environment caused a marked improvement in portfolio quality. The Russian subsidiary bank posted the highest organic growth in performing loans at group level (+22%), while the consumer loan portfolio, which is key to profitability, increased by 19%. The bank's annual ROE ratio was 21%.

The digital bank **Touch Bank,** which functions as a stand-alone key business line, continued to make a loss (–HUF 7.4 billion) in the third year of its operation; an improvement in the profitability of the bank has not yet been attained.

The **Ukrainian subsidiary bank** managed to improve its after tax earnings significantly, reporting a HUF 14.1 billion profit. Profitability was essentially determined by the 83% year-on-year drop in total risk costs; the DPD90+ ratio fell by 15.5 pps year-on-year to 26.4%. The FX-adjusted performing loan portfolio grew by 11%. The bank boasts the highest profitability among the Group's subsidiary banks; its ROE was 47.1%.

The **Croatian subsidiary bank** realised an after tax profit of HUF 17.1 billion in 2017, including Splitska banka's 8-month result of HUF 10.9 billion (without Splitska banka the Croatian operation increased its earnings by 63% to HUF 6.2 billion). The annual ROE improved from 5.2% to 9.3%. The FX-adjusted performing loan portfolio grew by 153% year-on-year, and organically, it increased by 6%.

The **Romanian subsidiary bank's** adjusted annual profit exceeded HUF 3 billion (+83% year-on-year). The FX-adjusted performing loan portfolio grew by 10% year-on-year.

Among the smaller subsidiary banks, **the operations in Slovakia, Montenegro and Serbia all reported losses** (their negative earnings were HUF 2 billion, HUF 155 million and HUF 2.9 billion, respectively). The Serbian figure already includes Vojvodjanska banka's December profit contribution (HUF 73 million). As a result of the acquisition, the FX-adjusted performing loan portfolio almost quadrupled in Serbia (without Vojvodjanska banka, portfolio growth was 17%); the optimal operating size and the expected cost synergies will hopefully improve the profitability of the Serbian operation significantly. In Montenegro we continued to clean the loan portfolio and improved our lending activity.

Share price

The Bank Group's continuously improving financial performance is also reflected in its share price: the 40% annual increase achieved in 2016 was followed by another 28% rise in 2017, and the stock closed at HUF 10,720. As a result of the further improvement seen since then, OTP Bank is the only player in the regional peer group whose share price exceeds the pre-crisis historic high; the Bank's current P/BV ratio is 2.1, while its market capitalisation was EUR 10.5 billion in the middle of March 2018.

Acquisition developments

2017 brought two successful acquisitions, and in both cases we managed to buy banks whose size was much bigger than that of the original operation. In May we consolidated the Croatian Splitska banka, followed by the Serbian Vojvodjanska banka in December. The two deals meant contributions of 8 months and 1 month, respectively, to the Group's 2017 consolidated after tax profit. The transactions improved our positions significantly in both markets. Our share in terms of total assets grew from 4.9% to 11.2% in Croatia and from 2% to 5.5% in Serbia, while the number of branches almost doubled and tripled in the two countries, respectively. The purchases boosted our performing loan and deposit portfolios. Both transactions were completed below book value.

In July 2017 the Chinese supervisory authority (CBRC) gave OTP Bank permission to open a representative office. The office operates in Beijing as a classic representative office, and as such it cannot conduct any specific business activities in the first two years.

Innovation, accolades, corporate social responsibility

OTP Bank considers it a strategic priority to exploit the opportunities that lie in innovation and to use digital applications as efficiently as possible. The Digital Transformation Programme, launched in 2015, does not only contribute to our customers' satisfaction but also provides continuous support for our business successes. In the last two years we introduced a full online application process for personal loans within the framework of the programme; our goal is that by 2018 the online channel should account for 20% of the sales of this product. We launched a financial package called e-Biz for small and medium-sized businesses, while the Simple Wallet and the Simple App (parking, purchase of toll stickers, theatre and cinema tickets) are among the most popular mobile applications in Hungary. At the same time, paperless, digital administration also accounts for an increasing share of banking processes.

The Bank Group's excellent performance and innovative services have earned it countless professional accolades: OTP Bank has for many years received the **Best Bank in Hungary** award from financial journals **The Banker, Euromoney and Global Finance,** and besides these, OTP's private banking service is also the proud holder of the title of best domestic service provider. OTP won the **Bank of the Year** award in the 2017 Mastercard competition, the highest accolade given to commercial banks providing retail services in Hungary, and also received the **Most Innovative Bank of the Year** and the **Retail Mobile and Online Banking Solution of the Year** awards. In addition, Global Finance selected OTP Bank as the **Best FX Service Provider in Hungary** in 2017.

OTP Banks is traditionally one of the largest donors in Hungary; our targeted donations are focused primarily on developing financial literacy, raising awareness, creating opportunities, helping the disenfranchised and those in need, as well as supporting culture and the arts and creating and preserving value.

Expectations for 2018

As I have mentioned in the introduction, in 2018 we essentially expect the favourable trends to continue at Group level. Obviously, there will be quite a few challenges: competition will intensify in most markets, while low interest rate levels will keep margins under pressure. The possible solution is to increase business volumes and strengthen the effectiveness of cost management. It should be emphasised, however, that in the present environment, where growth demands substantial additional financial and human resources – just think of the shortage of skilled labour that looks like becoming a permanent fixture in the region and the accompanying upward pressure on wages, or the increase in marketing and consultancy costs that are needed to support business – it is not realistic to expect a nominal decrease in operating costs for now. The management maintains its objective of strengthening our positions in markets where our presence falls short of the optimal market size.

Based on the above, the management has articulated the following expectations with respect to 2018:

- Besides the HUF 15 billion (after tax) negative impact of the Hungarian and Slovak bank tax, the impact of further acquisitions may result in significant adjustments items.
- The growth rate of FX-adjusted performing loans could come close to the 2017 organic rate (+10%) without the possible effect of further acquisitions. Within that, retail loans could make a more pronounced contribution to growth, while corporate portfolios are expected to increase at a more modest rate after an exceptionally strong 2016 and 2017.
- The net interest margin is likely to decrease further; it could shed another 10–15 basis points in 2018 as a whole versus the level seen in 4Q (4.38%). The forecast takes into account the effect of the acquisitions completed in 2017, but does not include the impact of any potential new acquisitions.
- The quality of loan portfolios could continue the favourable trend: the DPD90+ ratio may drop further, but total risk costs may increase due to growing loan volumes, the application of IFRS 9 rules and the expected decrease in the reversal of provisions.
- FX-adjusted operating costs (less any acquisition effect) could rise at a higher rate than in 2017, by approx. 6%, due to wage inflation and the ongoing digital transformation.
- The management plans to allocate most of the capital generated in excess of the capital required for organic growth to further value-creating acquisitions.

I am confident that market players will view our 2018 goals as realistic and not understated. I strongly believe that in addition to organic growth, the most effective way to increase shareholder value is to make further acquisitions that promise good returns and come with significant cost synergies.

While retaining the values that we have always upheld, there is a need for constant renewal. This is not only something that is dictated by the competition; for ourselves, too, we need to set objectives that are in line with what is expected of a market-leading financial institution, and which also offer a realistically attainable vision for our employees and customers. We have every reason to believe that the OTP Group will fulfil society's expectations that, while ensuring stable, predictable operation, it will provide individuals and communities with high-quality service and a positive customer experience in the management of their day-to-day finances.

I truly appreciate your help and support in achieving the objectives described above.

Dr. Sándor Csányi
Chairman & CEO