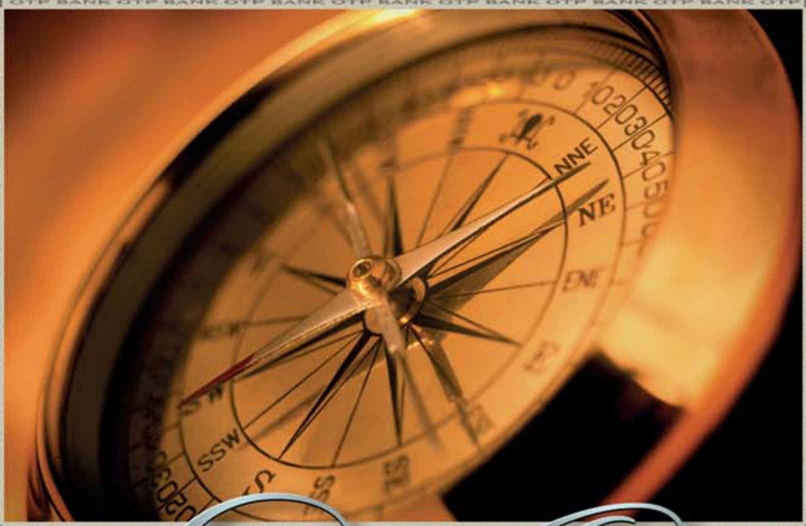

Annual Report

2003

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SENIOR MANAGEMENT OF OTP BANK LTD.

DR. SÁNDOR CSÁNYI
Chairman-CEO

DR. ZOLTÁN SPÉDER
Vice Chairman, Deputy CEO
STRATEGIC AND FINANCIAL DIVISION

CSABA LANTOS
Deputy CEO
RETAIL BANKING DIVISION

GÉZA LENK
Deputy CEO
CREDIT APPROVAL AND
RISK MANAGEMENT DIVISION

GYULA PAP
Deputy CEO
IT AND LOGISTICS DIVISION

DR. ANTAL PONGRÁCZ
Deputy CEO
STAFF DIVISION

LÁSZLÓ WOLF
Deputy CEO
COMMERCIAL BANKING DIVISION

MESSAGE FROM THE CHAIRMAN AND CHIEF EXECUTIVE OFFICER

Dear Shareholders,

With their exceptional performance in 2003, OTP Bank and the OTP Bank Group have proven that they are able to satisfy shareholder expectations over the long term. The results achieved in 2003 were outstanding not just by local standards but internationally as well.

The main value indicators for our shareholders are growth in after-tax profits, return on equity, earnings per share and increase in share price, as well as growth in the Bank's market value.

The OTP Bank Group closed 2003 with a consolidated after-tax profit of more than HUF 83 billion, which was 51% higher than in the previous year. Of this total, the profits of OTP Bank (HUF 71.5 billion) accounted for 86%, while among the results posted by the various subsidiaries, those of OTP Mortgage Bank (HUF 7.1 billion), OTP Fund Management (HUF 3.5 billion) and Merkantil Bank (HUF 2.4 billion) made notable contributions to the consolidated result. Also worthy of mention is the performance of new group member DSK Bank and its subsidiaries, whose consolidated after-tax profits were HUF 6.5 billion, of which HUF 1.5 billion originates from the period following their integration into the OTP Bank Group.

At the same time, return on average equity (ROAE) showed substantial growth, increasing at consolidated level from 26.2% in 2002 to 30.6% in 2003. Even in real terms – adjusting for an average yearly inflation rate of 4.7% – the increase (from 20.53% to 27.2%) is considerable.

Earnings per share also displayed strong growth. Consolidated, undiluted EPS was HUF 322 in 2003 compared with HUF 215 in the previous year – an increase of 50%.

The outstanding performance of the Bank and of the Bank Group in 2003 is reflected in the development of the company's share price, which increased during the year by 21%, to reach HUF 2,675 by year-end. An analysis of the movement of the share price over time shows that from the end of 1995 to the end of 2003, the price of the Bank's shares rose more than 28-fold (representing an average annual increase of 52%), while over this same period the BUX index barely rose more than six-fold (representing a 25% annual increase).

The high regard in which the Bank is held among the professional community both at home and abroad is clearly illustrated by the fact that in 2003 a number of prestigious international business and financial journals, such as Global Finance, Euromoney and The Banker, voted OTP Bank best Hungarian bank, while the national publication Figyelő Top 200 awarded our Bank the title of "Bank of the Year". As reasons for their choice, besides the outstanding results of the its financial operations, the magazines cited the Bank's successful Slovak and Bulgarian acquisitions.

Significant progress was made with regard to the integration of OTP Banka Slovensko and of the Bulgarian DSK Bank and its subsidiaries in 2003. As regards the DSK group, the corporate restructuring necessary to ensure operational efficiency has begun, as has the implementation of critical IT developments and the rationalisation of the branch network, while a number of new products have been launched, accompanied by intensive marketing campaigns. The new business policy of OTP Banka Slovensko, which has just completed its first full financial year as a member of the OTP Group, has also brought significant results. Successful efforts have been made to increase the number of customers of the Slovak subsidiary, most notably in the retail segment, and its share of the main markets has also grown.

Besides its successful regional expansion, OTP Bank has pressed ahead with its strategic projects that are vital in the interests of maintaining the Bank's competitiveness in the long run, and of improving operational efficiency and the standard of services. The introduction of SAP, aimed at modernising the Bank's management systems, continued, and in 2003 the main developments in the accounting and controlling area were implemented. The purpose of these is to improve the quality of information flow, rationalise and centralise financial processes, and to ensure strict cost control. By the end of 2003, a significant portion of the objectives of the previously launched Back Office Rationalisation project were achieved, retail loan services were enhanced, the efficiency of branch-office work was improved, and the creation of a central Back Office means the branches have been relieved of these administrative duties. The inputting of source data into the Transaction Database continued, and the use of the database for day-to-day business purposes has begun.

The activities and results of the Bank Group in 2003 represent a guarantee that in the years to come we will continue to create exceptional shareholder value, which is at the very heart of our business strategy. I hope that by doing so we will be able to retain the much appreciated confidence of our shareholders, and that besides our employees – to whom I would also like to express my sincerest thanks for their work throughout the year – they too will share in the future successes of the Bank and the Bank Group.

Dr. Sándor Csányi
Chairman and
Chief Executive Officer

FINANCIAL HIGHLIGHTS

(unconsolidated, according to HAR)

Profit and Loss Account	2002 HUF mn	2003 HUF mn	Change
Net interest income	102,715	118,182	15.1%
Non-interest income	63,543	85,580	34.7%
Total income	166,258	203,762	22.6%
Non-interest expenses	95,557	110,234	15.4%
Operating profits	70,701	93,528	32.3%
Increase in provisions	13,523	13,261	– 1.9%
Profit before taxation	58,082	86,701	49.3%
Profit after taxation	47,197	71,562	51.6%

Balance Sheet*	2002 HUF bn	2003 HUF bn	Change
Total Assets	2,390.1	2,758.6	15.4%
Loans and advances to customers	951.7	1,088.3	14.3%
Retail loans	329.8	318.2	– 3.5%
Corporate loans	558.6	691.2	23.7%
Municipal loans	63.3	78.9	24.6%
Interbank loans and advances	263.3	165.4	– 37.2%
Government securities in the Bank's portfolio	401.9	402.5	0.2%
Deposits from customers	2,011.0	2,234.9	11.1%
Retail deposits	1,523.7	1,656.3	8.7%
Corporate deposits	341.9	421.4	23.2%
Municipal deposits	145.4	157.2	8.1%
Total loans and advances	1,234.8	1,272.5	3.1%
Performing loans	1,183.4	1,216.7	2.8%
Qualified loans	51.4	55.7	8.5%
Provisions for possible loan losses	20.6	26.8	30.1%
Shareholder's equity	205.8	261.8	27.2%

Performance Ratios	2002	2003
Cost/income ratio, %	57.50	54.10
Return on Average Equity (ROAE), %	25.90	30.60
Return on Average Assets (ROAA), %	2.09	2.78
Capital Adequacy Ratio*, %	13.43	10.54
Undiluted EPS (HUF)	178.98	269.21
Diluted EPS (HUF)	168.56	255.58
Total Assets per employee* (HUF millions)	272.50	345.70
Total income per employee (HUF thousand)	19,414.00	23,986.00

Market share*	2002	2003
Retail deposits, %	38	36
Retail loans, %	23	14
Corporate deposits, %	13	14
Corporate loans, %	13	12
Municipal deposits, %	66	75
Municipal loans, %	55	54

* on December 31

MACROECONOMIC AND MONETARY ENVIRONMENT IN 2003

The Hungarian economy was characterised by serious imbalances in 2003. Due to unfavourable trends in the global economy, the pace of economic growth slowed, the internal and external balances worsened, inflows of foreign direct investment proved insufficient to finance the current account deficit, and national debt levels rose. The forint depreciated, interest rates increased, and in the second half of the year the downward trend in inflation reversed, though the average annual rate still remained below that of the previous year. By the end of 2003, nearly two years of growth in employment levels had come to an end, and the unemployment rate had fallen to 5.5%. There was extremely rapid growth in real wages, due mainly to the low base figure and to the public-sector pay increases implemented in the course of the year. Despite all these factors, a positive change occurred in economic fundamentals during the year, although the quantifiable impact of this change is not yet reflected in the aggregate annual figures.

After a rise of 3.5% in the previous year, **gross domestic product** grew by 2.9% in 2003, which was 2.5 percentage points higher than the eurozone average, and was close to growth levels in the US. Of the countries about to join the EU, economic growth in the Czech Republic and Slovenia slowed, as was the case in Hungary, with GDP growth remaining below 3% in real terms, while among the Baltic states, Latvia and Lithuania posted growth rates in excess of 7%. Slovakia and Estonia achieved growth of more than 4%, and Poland 3.7%.

The slowdown reached its lowest point towards the middle of the year, and then in the second half a positive change occurred in the Hungarian economy. With respect to production, the added value of industrial – and more specifically, manufacturing – output was the main driver behind the acceleration in growth, while with regard to the of use of GDP, an upturn in exports and manufacturing-sector investments, as well as a drop-off in household consumption were all indicative of a favourable trend.

Industrial output in 2003 outperformed even the most optimistic of expectations. After moderate, 2.8% overall growth in 2002, output grew by 6.4% in 2003. The upswing was due to the general global economic recovery, a strengthening of foreign and domestic demand, and a stocking up on inventory following the depletion in stock levels during the previous economic downturn. The improving performance was to a large extent concentrated among the multinational corporations, while small and medium-sized companies were less able to participate in the upswing. Despite the various investment-incentive schemes, their opportunities for growth were limited due to tough competition and low profitability levels.

Following an exceptionally high increase of 17.8% in the previous year, **construction industry output** rose by a total of just 0.7% in 2003. During the year, the marked decline in state construction projects was offset by a growth in residential construction, and thus, after a fall caused by the inclement weather in the first quarter, output began to climb once again. Production levels in the largest sub-branch of the construction industry – structurally complete buildings – fell by 9%, while, by comparison, that of building services and of construction finishing works increased by 13.8% and 16.7%, respectively. Two contrary trends were observable in the construction industry last year: the output of the larger firms (i.e. those employing more than 300 people) fell by 5.2%, while that of smaller companies (employing less than 5 people) rose by 16.2%. This was mainly due to the marked increase in production volumes related to building services and construction finishing works. That the upswing in the sector has come to an end is suggested by the fact that the volume of contracts concluded at the end of the year was some 50% lower than the exceptionally high base figure of the previous year. Within this, the number of contracts concluded for the construction of buildings decreased by 26.9%, and those for the construction of other facilities by 63.3%.

In 2003 the number of residential units built exceeded all expectations. The more than 35,500 apartments taken occupancy of represented an increase of 13% over the previous year, and authorisation for the construction of a further 59,000 new units shows an increase of 22%. Most of the apartments were completed in the second half of the year. New residential units had not been built in this quantity since 1991, while the number of construction permits was the highest since 1986.

The outstanding performance of the **agricultural sector** in 2001 was followed by two drought years. In both of these periods this was caused by a combination of unfavourable weather conditions, world-market recession and even less favourable market conditions. Overall, production fell by 5.6% in 2003, with crop production down 13–14% from the base figure, and livestock production are 3–4% lower. Sales of agricultural produce stagnated, with sales of crops and garden produce falling 5%, and sales of livestock and animal produce rising by 5.5% over the year.

The **domestic use of GDP** grew by 5.5% in 2003. The growth in the volume of **national economy investments** was lower than in the previous year, up by just 3.1%. The expansion in household consumption was notable, although the pace of growth was slightly slower.

The composition of capital investments differed fundamentally from that of 2002, and changed to an altogether healthier growth trend. The relatively high growth in 2002 had been largely due to state investments, while in the private sector manufacturing investments, critical for companies in the industry, had fallen by nearly 10%. In 2003 manufacturing investments became the principal economic driver, growing by 11.3%. This favourable change is reflected in the sectoral and technical distribution of investments: In 2002, a 10% growth in construction-industry investments had been accompanied by a stagnation in machinery investments, and in 2003, with the cut-backs in state-funded projects, construction declined, while machinery investments increased by 12.3%.

Household consumption, which accounts for nearly two-thirds of the domestic use of GDP, rose by 6.5% compared to the previous year, significantly outstripping the rate of growth of GDP itself, while gross household savings were 13% higher at current prices than in the previous year, and 6.9% higher in real terms. This growth in consumption was due largely to the increase in real wages that occurred in 2002. The average gross monthly salary of HUF 137,187 exceeded that of the previous year by 12.0%, and the **average net income** of HUF 88,751 represented an increase of 14.3%. The increase in gross income was lower in the private sector, at 8.9%, and the rise in net average income was 12.3%. The mid-year pay increases in 2003 affected mainly public sector workers. In the state sector average gross salaries for the year increased by 17.5% to HUF 160,843, and average net income by 18%, to HUF 99,659, exceeding the average salary levels in the private sector. The fact that net incomes rose more quickly than gross incomes was due to the abolition of income tax on the minimum wage, the partial adjustment of taxation to inflation, and the modification of employee tax discounts. On the national-economy level, the increase in wages coupled with falling inflation led to a notable, 9.2%, increase in **real wages,** though this was more modest than that of the previous year.

In the **jobs market,** the growth in the employment rate came to an end, and the unemployment rate worsened somewhat over the year as a whole, from 5.8% to 5.9%.

Inflation reached its lowest rate in mid-2003, at which point the trend changed, and inflation rose continuously. Despite this, the growth in prices slowed on average over the year, from 5.3% to 4.7%, although the twelve-month price change measured in December grew from 4.8% to 5.7%. The pace of growth in consumer prices in most consumer goods categories (food, clothing, other articles, fuel) slowed, while the price of alcoholic drinks, tobacco products and household energy grew, and in the case of consumer durables prices effectively fell. The monthly producer price indices indicated a growth rate that was still below 1% in the first half of the year, and then with the weakening of the forint, the rate began to rise steadily, increasing by an average of 2.4% over the year.

Economic growth, which was slow to commence, was accompanied by a significant worsening of the **external and internal balances.**

The **public finance** deficit was HUF 1,054 billion in 2003 – the equivalent of 5.7% of the annual GDP. The deficit was significantly lower than in the previous year, but notably in excess of the target rate of 4.5% of GDP. The Maastricht ratio was –5.9%. National debt levels grew to 59%. Besides the unfavourable trends in the global economy, a series of economic policy errors committed while trying make good on election promises resulted in a major overstepping of the budgeted annual spending limits. Despite austerity measures taken during the year to curb state expenditure, public spending exceeded the planned figure by HUF 471 billion. Expenditure by central government and welfare organisations, as well as funds expended on interest payments and housing subsidies, all exceeded the predetermined limits. Another factor that led to an increase in the deficit was the loss of revenue that resulted from the altered scheduling of VAT payments and retransfers.

The **current account deficit** – calculated using a new method – amounted to EUR 6.5 billion for the year, which is EUR 1.6 billion higher than in 2002. A major contributory factor to the change in the current account balance relative to the previous year and measured in accordance with international standards, was the increase in the trade deficit. Indeed, there was only a slight change in the income and transfer balance (including reinvested incomes). The deterioration in the balance of services was related to weak performance in tourism.

The country's gross external debt level (including shareholders' loans) increased by EUR 6.7 billion to EUR 45.7 billion, and net debt grew by EUR 3 billion, to EUR 19.3 billion. As of the end of 2003, the government sector and the National Bank of Hungary (MNB) accounted for 44.6% of the nation's net debt.

In response to speculative attacks on the forint at the start of the year, national reserves were raised from HUF 9.9 billion to above HUF 14 billion, and at year-end they slightly exceeded the EUR 10 billion level generally regarded as acceptable.

The **foreign trade** deficit grew by some EUR 800 million during the year, approaching EUR 4.3 billion by year-end. Export volumes expanded by nearly 9%, and import volumes by 10% over the year as a whole. The fact that net exports fell only slightly over the year was due largely to the favourable trends that began in the second half, with the growth in exports exceeding that of imports in each of the three months of the last quarter. A notable characteristic in terms of foreign trade in 2003 was that the share of Hungarian exports to developed countries, including the EU, declined by 1.7%. Within exports to developed economies, the share of machinery exports increased dynamically, while exports of manufactured goods fell by 6.5%. Hungary's exports to central and eastern European countries expanded by an impressive 20%, as a result of which the share of this region in Hungary's total exports increased to nearly 16%.

MONETARY POLICY

2003 was characterised by a volatile and difficult-to-predict monetary environment. Within the space of one year, the benchmark central-bank rates – if we also take into account the changes to the interest rate corridor – ranged from 3.5% to 13.5%, while the forint exchange rate fluctuated significantly. The speculative attacks in January and the depreciation of the mid-rate in June also contributed to the fluctuations in the value of the forint. The unpredictability of monetary policy was due primarily to the tensions between inflationary targets and budgetary policy objectives, as well as the speculative money flows to which they gave rise.

In 2003, in response to the growing volatility of the forint, the central-bank base rate increased from 6.5% to 12.5%. The course that interest rates followed during the year was not consistent, however. At the start of the year, the inconsistency between exchange rate policy and inflationary targets led to a strengthening of the forint, and then, as it reached the edge of the band, to a speculative attack. At this point the central bank tried to ward off a further increase in forint purchases by cutting interest rates and widening the interest corridor. Up until mid-year, the forint exchange rate was essentially stable, but then the 2.27% shifting of the band in June led to the forint's losing some 6 or 7% in value within just one day.

Overnight lending rates rose from 7.5% to 13.5% over the course of the year, and from 3.5% to 11.5% for overnight borrowing. The width of the interest corridor determined by the overnight deposit and loan interest rates rose from +/–1 percentage point to +/–3 percentage points, and then returned to the January rate. Despite the growth in inflation in the second half of the year, the Monetary Council's 300-basis-point rate hike had, by the end of the year, resulted in a rise in the real interest rate on two-week deposits to around 7%, leading once again to an inflow of speculative capital.

The **statutory reserve regulations** did not change significantly in 2003, with the reserve rate having remained unchanged at 5% since August 2002. The interest compensation paid on the statutory reserve increased in several stages, in line with changes in the benchmark rate, by a total of 600 basis points, from 5.75% to 11.75%.

Major reserve-related regulatory changes are set to come into force from January 1, 2004, the purpose of which is to improve the competitiveness of the banking sector, and to bring Hungary's regulations into line with ECB directives.

Government bond yields on the shorter maturities remained stable at 6% until June, after which the two-stage interest rate hike led to a rise in yields, first to just above 9%, and then to above 12% in November. The extent of the yield increase on government bonds of over one year's maturity was inversely proportional to the length of their maturity, with yields on three-year papers increasing from 6.66% to 10.19%, and yields on ten and fifteen-year bonds rising by just 1.5 percentage points. The yield curve, which had been virtually flat at the start of the year, had become strongly inverted by the end of the year.