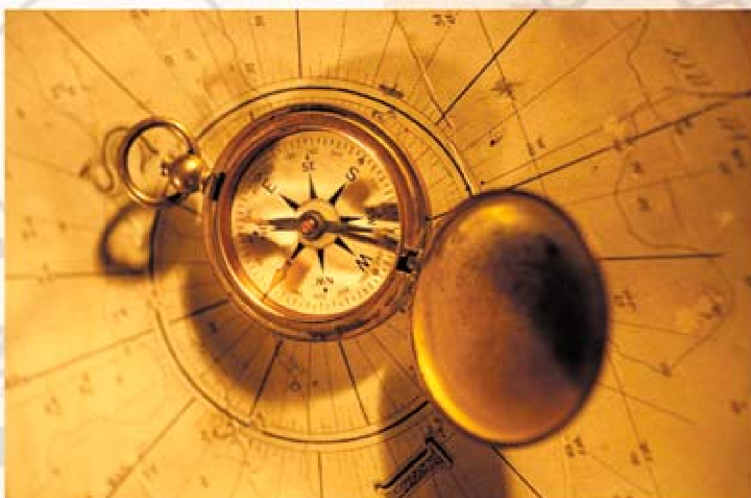

Annual Report

2002

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SENIOR MANAGEMENT OF OTP BANK LTD.

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Chairman–CEO

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

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RETAIL BANKING DIVISION

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Deputy CEO
IT AND LOGISTICS DIVISION

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Deputy CEO
STAFF DIVISION

LÁSZLÓ WOLF
Deputy CEO
COMMERCIAL BANKING DIVISION

MESSAGE FROM THE CHAIRMAN AND CHIEF EXECUTIVE OFFICER

It gives me great pleasure to be able to report to our shareholders that we have had yet another successful year. The OTP Bank Group closed 2002 with consolidated pre-tax profit of over HUF 68 billion, which represents a 19% increase over the previous year. The non-consolidated pre-tax earnings of OTP Bank were HUF 58 billion (a 22.6% increase), while among the various subsidiaries outstanding results were posted by OTP Fund Management with HUF 3.5 billion, Merkantil Bank with HUF 2.4 billion, and OTP Building Society and OTP-Garancia Insurance with HUF 1.6 billion each, in pre-tax earnings.

The market value of shares in OTP Bank increased by 34% (66% in dollar terms) in 2002, to reach HUF 2,210 per share, while the share index of the Budapest Stock Exchange, the BUX, grew by just 9.4% over the year. These changes are fully in line with the trends of previous years: From the end of 1995 to December 2002, the value of shares in the Bank increased by a factor of almost 20 (57% average annual growth), while over the same period the BUX only achieved a little over five-fold growth (a 26% annual average increase) – with even this increase largely attributable to the performance of OTP Bank shares within the index.

In 2002 the Bank continued to earn industry-wide recognition both in Hungary and abroad. As in previous years, OTP Bank was rated "Hungary's Best Bank" by Global Finance, Euromoney and The Banker. The reasons cited by these respected financial journals for bestowing the awards included the successful integration of Slovakia's IRB into the Group, the launch of OTP Mortgage Bank, outstanding product developments and OTP Bank's success in retaining its dominant position in the retail and municipality banking markets. In addition to receiving these most prestigious of international awards, OTP Bank was also voted "Issuer of the Year" by the members of the Budapest Stock Exchange, while the success of the Bank's product development work in the area of electronic banking services earned it a special award of "Mobile Bank of the Year".

In 2002 OTP Bank continued to focus on development work and projects aimed at maintaining the Bank's competitiveness and improving the effectiveness of its business operations over the long term. Accordingly, strategic projects commenced or planned in previous years – such as the introduction of SAP, the Back-Office Rationalisation Project, and creation of the Bank's Transactional Data Warehouse – were continued according to schedule, along with projects aimed at further developing the distribution network. The construction work on the Bank's new headquarters should also be mentioned here.

In 2002, the Bank was again successful in meeting the objectives of its medium-term strategy of supplementing organic growth with acquisitions, and achieving international growth by expanding within the region, most notably through the purchase of Slovakia's IRB Bank.

As the first step in IRB's integration into the OTP Bank group, the Slovakian bank underwent a complete image change: From August 2002, the financial institution continued its activities under the name OTP Banka Slovensko, a. s. (OBS).

The steps taken thus far in the restructuring of OBS have been welcomed by the market and our shareholders alike, which encourages us to seek further opportunities for regional expansion and for implementing our acquisitions strategy, while making the best possible use of the experience gained so far.

Finally, I would like to take this opportunity to thank all our employees, whose hard work over the year resulted in the Bank's and the Bank Group's outstanding successes in 2002. Thanks are also due to our shareholders for the trust they have placed in us, a confidence that I hope will continue to be justified by the future performance of the Bank.

Dr. Sándor Csányi
Chairman–CEO

Financial Highlights

Profit and Loss Account	2001 HUF mn	2002 HUF mn	Change %
Net interest income	98,342	102,715	4.4%
Non-interest income	42,775	64,447	50.7%
Total income	141,117	167,162	18.5%
Non-interest expenses	85,214	95,557	12.1%
Operating profits	55,903	71,605	28.1%
Increase in provisions	8,534	13,523	58.5%
Profit before taxation	47,369	58,082	22.6%
Profit after taxation	38,398	47,197	22.9%

Balance Sheet (as at 31st December)	2001 HUF bn	2002 HUF bn	Change %
Total assets	2,127.2	2,390.1	12.4%
Loans and advances to customer	769.8	951.7	23.6%
Retail loans	258.2	329.8	27.7%
Corporate loans	464.8	558.6	20.2%
Local government loans	46.7	63.3	35.6%
Interbank loans and advances	329.9	263.3	-20.2%
Government securities in the Bank's portfolio	481.1	401.9	-16.5%
Deposits from customers	1,811.2	2,011.0	11.0%
Retail deposits	1,405.6	1,523.7	8.4%
Corporate deposits	253.6	341.9	34.8%
Local government deposits	152.0	145.4	-4.3%
Total loans and advances	1,118.7	1,234.8	10.4%
Performing loans	1,074.1	1,183.4	10.2%
Qualified loans	44.6	51.4	15.2%
Provisions for possible loan losses	21.7	20.6	-5.0%
Shareholder's equity	158.5	205.8	29.9%

Performance ratios	2001	2002
Cost/income ratio, %	60.40	57.20
Return on Average Equity (ROAE), %	26.85	25.90
Return on Average Assets (ROAA), %	1.89	2.09
Capital adequacy ratio*, %	14.11	13.43
Undiluted EPS (HUF)	145.77	178.98
Diluted EPS (HUF)	137.13	168.56
Total assets per employee* (HUF millions)	256.50	272.50
Total income per employee (HUF thousand)	17,235.00	19,519.00

Market share (31st December)	2001	2002
Retail deposits, %	39	38
Retail loans, %	31	23
Corporate deposits, %	12	13
Corporate loans, %	12	13
Municipal deposits, %	78	66
Municipal loans, %	65	55

* On December 31.

Macroeconomic and Monetary Environment in 2002

Compared to the previous year, the Hungarian economic environment was less favourable in 2002, and economic policy goals were only partially achieved. The rate of economic growth slowed, the internal and external balance deteriorated, and, although there was a slight reduction in the foreign trade deficit, the amount of foreign capital entering the country fell short of the previous year. On the positive side, there was no further decline in investments, the rate of inflation plunged to a 15-year low, the employment situation improved somewhat – although the unemployment rate deteriorated slightly – and real wages increased at an exceptional rate. By international standards, the performance of the economy remains dynamic.

Gross domestic product (GDP) increased by 3.3% in 2002, which falls short of the 3.8% growth of previous year, but is still 2.5 percentage points above the EU average and higher than even the USA's rate of economic growth. Among the candidate countries for EU accession, the economies of the Czech Republic and Poland displayed slower growth, while Slovakia and Slovenia outperformed Hungary in terms of GDP increase. Over the course of the year, the trend in the GDP growth rate improved from one quarter to the next. In the first quarter of 2002, after hitting a low of 2.9%, the rate of GDP growth began to increase steadily, with the quarterly indexes showing 3.0%, 3.5% and 3.7% growth respectively. The economic growth was driven exclusively by domestic demand: The substantial state-sector wage increases led to a dramatic rise in household consumption, while government infrastructure investments and schemes to stimulate home construction boosted investment activity.

The unfavourable economic environment was also reflected in the **industrial output** figures. By 2002, the 18% growth experienced in 2000 had fallen to just 2.6%. Two years of stagnating domestic sales and a reduction in exports of industrial goods both contributed to this reduction. Rather than leading to an expansion of the market for domestically manufactured goods, the 11% increase in retail turnover resulted in more imports, which became cheaper as a result of the strengthening of the forint.

Growth in the **construction industry,** which has continued unabated for several years, reached 20.1% in 2002. The upswing in the construction industry can be attributed to an increase in domestic demand. Of the various sub-sectors, the volume of "other" construction work (roads, bridges, drainage) saw the most dynamic growth (28%), which is chiefly the result of an increase in state-financed infrastructure investments. The construction of buildings increased by 15% due to new home construction, the refurbishment of public buildings and the building of new commercial properties. A 21.1% increase in new orders suggests that the upswing in this sector is likely to continue. However, within this figure, the volume of new contracts for the construction of buildings decreased sharply compared to the base period, while the volume of new contracts for "other" forms of construction increased by 44.5% in 2002, following a reduction of 17.6% in the previous year. The pace of the upturn in home construction, which commenced after the trough of 1999, slowed in 2002. The 31,500 new homes handed over for use in 2002 represented a 12% increase over the previous year, while the 49,000 new home construction permits issued represented a 2% year-on-year increase, and came close to the estimated ceiling for sustainable growth. The overall slowdown in the growth of new home construction contained regional disparities. Some 71% of new homes were built in large cities. The rate of growth was 46% in Budapest and 28% in county seats, but in smaller towns and villages the number of new homes constructed fell by 8%.

Following an outstanding year in 2001, performance in the **agricultural sector** was much less favourable in 2002. Overall, after a temporary period of growth, output dropped once again in 2002, due to a combination of natural and market factors. Sales of agricultural products increased by around 2%, within which sales of plant-cultivation and horticultural products stagnated and sales of livestock and animal products saw a slight upturn, increasing 3.6% over the year.

The **domestic use of GDP** increased by **5.1%** in 2002. **Investment volume** exceeded the previous year's level by 5.8%. There was considerable investment activity in the area of infrastructure development: The volume of construction projects has increased by 10.7%, while the volume of machinery investments has decreased by 0.6–0.5% over the past two years.

Due to the downswing in the world economy, the level of corporate investment was extremely low. Investments by manufacturing industry companies, which account for 21% of all investments, decreased by over 9%, while investments made by companies from the realty and economic services sector, which constitute 27% of total investments, were up 14.5%. The greatest increases in state-sector investments were in the areas of public administration and defence (32.2%), and health and social security (35.1%).

Household consumption, which accounts for around two thirds of domestic GDP use, increased – at a substantially higher rate than GDP – by 8.8%, while gross household savings rose by 12.9% at current prices and 7.2% in real terms in comparison to the previous year. **Average gross wages** of the employed (HUF 122.453) increased by 18.3%, while **average net wages** (HUF 77,607) were 19.6% higher than in the previous year. Within this figure, gross average wages in the private sector increased at the less dynamic rate of 13.3%, while net average wages in the private sector increased by 16%. The higher increase in net wages resulted from the exemption from income tax payment obligations of people earning the statutory minimum wage. The state-sector wage increases of 2001 and 2002 mainly affected the employees of institutions funded from the central budget and social-insurance. In this sector, gross average wages increased to HUF 136.891 (by 29.2%), and net average wages to HUF 84,475 (by 27.5%), thus exceeding the average wage levels of the private sector. Taking the economy as a whole, the wage increases coupled with the drop in inflation resulted in an extremely dynamic 13.6% increase in **real wages.**

The level of activity on the **labour market** improved somewhat, but the unemployment rate deteriorated slightly, from 5.7% to 5.8%.

Annual average inflation fell substantially in 2002, from 9.2% to 5.3%. The evidence of a downward trend in inflation is further supported by the fact that over the course of the year the forint exchange rate remained within the upper half of its intervention band, often brushing the maximum limit. There was no imported inflationary pressure on domestic prices, even despite fluctuations in oil prices; and the world economy was also mainly characterised by a downward inflationary trend. The rate of increase in consumer prices slowed in every consumption category, while the prices of consumer durables effectively decreased.

The slowing in growth was accompanied by a significant deterioration in the economic balance. This deterioration, even discounting the unfavourable trends in the world economy, had already started in 2001 as a result of the general election. The preparations for the election, the campaign promises and their subsequent fulfilment led to a drastic overstepping of annual budgetary targets.

The **public finance deficit** for 2002 – calculated using the ESA95 method applied in the EU – amounted to HUF 1,573.0 billion, or 9.5% of annual GDP and more than three times the annual projection. At the end of 2002 the Parliament adjusted the budgetary targets for the year. The purpose of the modifications was to include settlements undertaken by the state but hitherto managed outside of public finance, the takeover of debts from state-owned companies and settlements related to ÁPV Rt., in the central budget. At year's end the **central budget** had a deficit of HUF 1,474.7 billion, of which around HUF 650 billion was attributable to one-off items related to the modification of the annual targets. Disregarding these one-off items, the public finance deficit amounted to 5-6% of GDP.

Over the year, the **current account deficit** – calculated using the new method – totalled EUR 2.8 billion, which represents a EUR 0.8 billion increase against the previous year. Almost a quarter of the deficit was accumulated in the last month of the year. A decisive role in the deficit's increase was played by the deterioration in the services balance – exacerbated by a further increase in the burgeoning earnings deficit – which the improvements in the balance of trade and the balance of unreciprocated current-account transfers were unable to compensate. Tourist trade was a decisive factor in the development of the services balance, accounting for 96% of its deterioration. The EUR 2.2 billion import surplus in the trade balance represented a EUR 300 million reduction against the previous year. Repatriated profits totalled EUR 1.7 billion, or EUR 166 million more than in the previous year. A net amount of

EUR 891 million arrived in the country in the form of **foreign direct investment** (working capital and portfolio investments), a 10% increase over last year. This is only sufficient to cover a third of the current account deficit. The country's gross external debt (including loans from the owners of companies) increased by EUR 1 billion to EUR 38.6 billion, while the net debt grew by EUR 2.1 billion to EUR 15.7 billion. At the end of 2002, 48.3% of the net debt came from the government sector and the national bank. International reserves decreased to EUR 9.9 billion, which was EUR 2.3 billion lower than at the end of the previous year.

The **foreign trade deficit** was EUR 3.4 billion (USD 3.3 billion), or EUR 130 million less than in 2001. This deficit is equivalent to 9.4% of total exports. The volume of exports grew 6% over the year, while imports increased by 5%. The growth in exports exceeded that of imports during the first three quarters of the year, but the gap between the two growth rates narrowed steadily, and in the last quarter the rate of growth in imports exceeded that of exports by 4 percentage points. Consequently, 40% of the foreign trade deficit for 2002 was accrued in the last quarter of the year.

MONETARY POLICY

In 2002 the National Bank of Hungary (NBH) continued its monetary policy focused on meeting inflation targets. The measures taken by the central bank during the course of the year were characterised by its attempts to compensate for lax fiscal policies. The basic forecast was that the central bank planned to achieve the 4.5% inflation target for the end of 2002, and the 3.5% target for December 2003 – with a tolerance of +/–1% – through the use of strict monetary-policy measures. In December 2002 consumer inflation was close to the centre of its target band, at 4.8%, largely due to the implementation of a coherent monetary policy.

The broadening of the forint exchange-rate band in May 2001 limited the available arsenal of monetary policy tools to making changes in the benchmark interest rate, and to using the prime rate to influence inflationary expectations and thus achieve inflationary targets.

The central bank's interest-rate policy during the year was aimed primarily at achieving its inflation-related targets and at curbing the extraordinarily high demand that arose from the exceptional level of government spending. In accordance with the Central Bank Act and international practices, the **central bank prime rate** functions as a benchmark rate in monetary policy. In 2002 there were no restrictions on the placing of central bank deposits at the central bank prime rate, which decreased by a total of 125

basis points, from 9.75% to 8.5%, over the course of the year. However, the interest rate did not follow a smooth downward path. The 8.5% prime rate was first achieved as early as the second half of February. Following this, at the end of May, the Monetary Council increased the benchmark rate by 50 basis points on two occasions, in response to unfavourable inflation forecasts and growing risk premiums. The NBH maintained the 9.5% prime rate until mid-November, when it was forced back down to 8.5% by an undesirable strengthening of the forint, an interest-rate reduction by the ECB and a reduction in risk premiums resulting from the favourable outlook regarding Hungary's accession to the EU.

The overnight lending rate decreased from 11.25% to 9.5%, while the rate on overnight deposits fell from 9.75% to 8.25% by the end of the year. The interest corridor for overnight deposits and loans narrowed from +/–1.5% to +/–1.0%. The steady decrease in inflation, and the two 50-point interest-rate increases carried out by the Monetary Council, had pushed the real interest attainable on two-week deposits up to 5% by the middle of the year, which led to a massive influx of speculative capital.

Within the framework of the further development of the **mandatory reserve** system, the reserve ratio was reduced from 6% to 5% with effect from 1 August 2002. The range of liabilities constituting the base for the calculation of reserves was narrowed twice during the course of the year, with liabilities accumulated through repo deals, as well as all types of liability-side accruals and other liability-side accounting items removed from the list. The rate of interest compensation payable on mandatory reserves increased by 50 basis points in September, and a further 50 basis points in October, from 4.25% to 5.25%.

The purpose of the changes to the regulations on reserves was to improve the competitiveness of the banking system, as well as to comply with ECB directives.

Short term **yields on the government securities market** decreased from 9-9.7% to 7.5-8% by the end of December. In the first quarter, the yields on government securities with a maturity of less than one year decreased steadily, while yields on the longer-term papers increased unabated until the middle of the year. From May, the interest rates for yields of one year or less increased, and by August-September they exceeded the level of the beginning of the year. By the end of the year, the yields on government papers of all maturities had decreased to a greater or lesser extent, and the interest rates on the various maturities came closer together, with the result that the inverse nature of the yield curve weakened steadily.