

DANUBIUS HOTELS
GROUP



ANNUAL REPORT
2003



DANUBIUS
HOTELS

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STATEMENT BY THE CHAIRMAN

Dear Shareholders,

Let me present to you our Annual report and add a few comments to the figures. Last year I wrote and it was no exaggeration that the year 2002 presented the greatest challenges we have had to face and it seemed inevitable that 2003 would be even tougher. Unfortunately, this prediction proved only too accurate and, as you will have seen, the year 2003 was the hardest year in the life of the company and this was reflected in our results.

Of course, Danubius is not the only company in the hospitality and tourism business to have been affected by international events largely outside our control. The conference of

the World Tourism Organisation held this year, pronounced that the performance of world tourism in 2003 showed the most negative trend in the history of the industry. Since the events of 11th September 2001, the growth prospects of the tourism industry have been shattered. In 2003, the effects of the Iraq war lingered well into the second half of the year and the unexpected spread of the SARS virus raised further uncertainties for travellers. Economically, much of Europe continued close to a recession and particularly in Germany, a recovery still seems some considerable way off. In addition to these major factors, there has been a succession of other terrorist incidents or scares, leading to a series of new security and control measures being introduced by airlines and others in the industry. All of these developments raised further questions in the minds of potential guests.

In Hungary, the market has also been dramatically affected by the hotel construction boom over recent years which has doubled the capacity of five-star hotels in Budapest, increased the number of four-star hotel rooms

by 60% and also created many more countryside spa facilities, often with the assistance of subsidies from the Government. This substantially increased capacity was accompanied by an actual decrease in the total number of guest nights compared to the prior year in both 2002 and 2003.

As we look forward to 2004, I am pleased to say that there are some encouraging signs of business picking up in the first quarter, but further new hotel openings are planned in Budapest and the regions and so competition will continue to be evermore intense.

Unfortunately I have had to set out a rather bleak picture of the industry. But despite this, your company has made good progress in a number of areas and I would like to emphasise some important and positive features of the company's operation last year.

First, our reorganised Sales and Marketing Department fought hard to preserve our market position despite the increasing competition and, in the autumn when business started to recover somewhat after the war we were rewarded with an overall improvement in our market share in Hungary. We are actively looking to penetrate new markets, to mention just one, China, as our main traditional market in Germany continues to stagnate.

Second, our group revenues increased to HUF 37 billion, which includes our efforts in Hungary, but also reflects a greater contribution from our foreign subsidiaries, particularly in the Czech Republic and Slovakia.



STATEMENT BY THE CHAIRMAN

Third, although events dictated we should be cautious with our capital expenditure programme in 2003, we used this year to plan key developments. Accordingly, 2004 will see an acceleration of capital projects in Hungary, a major programme to start the modernisation of our operations in Piestany, including investment in I.T. and the initial refurbishment of the famous Irma Spa, and the continuation of our successful investment strategy in Marienbad to upgrade more hotels to a four-star level and provide more spa and wellness facilities for our guests. Also our brand new hotel and spa facilities in Sovata, Romania will be strongly promoted in the market.

Fourth, we increased the scope of our operation with a management agreement for a new Hungarian hotel opening this year in Visegrád and have agreed to manage a thermal spa hotel which, following refurbishment, is scheduled to open in the traditional spa town of Buxton, England, in approximately three years' time.

With regard to our results in 2003, the setback of HUF 1.6 billion at operating profit level is largely explained by the factors I mentioned earlier. However, I would like to add that because of the difficult market conditions, we have implemented a vigorous cost control policy throughout the year, resulting in further reductions in headcount and improvements in efficiency. We are determined to continue this process as we are faced with some unavoidable cost increases such as VAT and cost pressures associated with joining the European Union. Also, there is no doubt that, particularly in Budapest, it will take some considerable time for the recovery in the market and hence, the number of guests, to match the increased capacity available.

You will also see from our results that accounting conventions required us to book an unrealised foreign exchange loss of some HUF 1.4 billion. This loss relates to loans which will be repaid in coming years and it is far from certain what the realised loss or profit will be in the final event. Indeed, much of the loss has been reversed in the first quarter of 2004 due to the strengthening of the HUF in that period. It would be extremely unwise for me to attempt to make any prediction as to what will happen to exchange rates later this year and in the future, except perhaps to say that I hope Hungary's welcome accession to the European Union and likely eventual membership of the Euro should help to create a more stable environment for our business.

As shareholders, you will have monitored the rather flat performance of our share price during the year, which naturally reflected investors' uncertainties about the industry. In our business targets for 2004, you will read about our planned improvement in performance for the current year - a plan, which of course anticipates a reasonably settled international situation. Nevertheless, it seems that our ideas have been welcomed by the stock market since our share price showed a welcome increase at the beginning of April.

Following our prudent policy of the past and in light of the disappointing results in 2003, I hope you will understand why we decided not to propose a dividend.

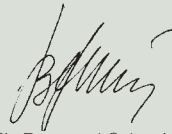
I believe strongly that dividends can only be paid out of profits and that to go against this principle would only reduce the resources necessary to sustain the company's longer-term development. As a shareholder in the company like you, as well as the Chairman of the Board of Directors, I also hope and expect that, in 2004, we will see an improved situation, which will allow us to return to our previous policy of dividend payment.

STATEMENT BY THE CHAIRMAN

Finally, let me express my thanks for your support as shareholders during this difficult year. I can assure you that the Board and management of the company, together with all our employees, understand that we must continue to fight hard if we are to succeed in these tough and competitive times. We are all fully committed to improving the performance and the results of the company.

Your company owns and manages many wonderful properties, has a leading reputation for its health spa services and a loyal and dedicated staff. Whilst joining the European Union is certainly no panacea, it does provide an opportunity for Hungary, the Czech Republic and Slovakia to promote themselves on the world stage and this should have a positive influence on our business, despite all the other problems facing the industry.

Thank you again for your understanding and patience. I continue to believe that the foundations of this company are extremely sound and that, being able to rely on the hard work and commitment of all our people, our shareholders will, once again, see an improved picture in the future.



Sir Bernard Schreier

PRESIDENTIAL GREETING

Dear Shareholders,

Last year I greeted you in the Annual Report by listing a row of difficulties. Unfortunately, I have similar news to report to you this year too. However, I believe there are times in the life of a company as well when it does everything possible in his power but to no avail; gives its utmost to achieve the best performance but in vain, consequently the final result is not one that is justified. This is what happened to Danubius now: both the management and the colleagues delivered a good work, but the results were not forthcoming as outside circumstances were against us.

The list of events hitting international tourism in the past years is quite long and in 2003 we had to present to you several negative factors in our interim reports. The war in Iraq at the beginning of the year followed by the SARS epidemic weakened the tourist industry. Then the terror acts committed in different parts of the world during the year made recovery difficult. This was coupled with the economic recession in the main sending countries and the unfavourable changes that took place in the home countries of our company group, especially on the decisive Hungarian market.

Nevertheless, our company has survived several difficult periods. Even now we think if we try to face the problems and continuously search for solutions, sooner or later our work shall yield fruits and if coupled with a favourable turn in external circumstances we will be able to report to you about increasing profits from year to year. We trust that 2004 will be the start of such a period as all our efforts targeted long-term increase of the turnover and the profit and some promising signs were already emerging in tourism at the end of 2003 and the beginning of the year.

The increase of hotel capacity continued to grow on the Hungarian market. We are up against competition from new hotels opening in the capital and in the country spa resorts. We strived to moderate the decrease of the number of foreign guests with intense marketing drive and strengthened our activities on markets from where guests are likely come to Hungary. In order to be able to win domestic guests, we have prepared some attractive packages – especially in the one-two day fitness/wellness programmes of ever-increasing popularity – and we have continuously established connections with the spreading Health Funds, through which we hope that a new circle of clients will have access to our hotels. No complex reconstruction projects were implemented in our hotels in Hungary in 2003 since we have introduced some cost cutting measures in this, just like in many others fields. At the same time we endeavour to keep abreast with the latest guest requirements, therefore we decided to prepare in 2003 and to implement in 2004 the entire air conditioning of numerous hotels.

Unfortunately, we had to cut back our reconstruction costs last year; still there are some projects we are truly proud of. A prominent example is the entire reconstruction of Hotel Sovata in Romania, in the course of which the whole hotel was reshaped and turned into a top quality three star hotel. The long closed therapy centre was equally renewed and reopened. Our work has been acknowledged by the Romanian Tourism Centre too: Hotel Sovata was awarded hotel of the year in 2003 by its official professional gazette. Hungarian and Romanian guests both like to visit our hotels in Sovata but we hope that



PRESIDENTIAL GREETING

through vigorous marketing activities this hotel of outstanding quality will attract visitors to this beautiful region from other parts of Europe as well.

The unfavourable international events had less effect on the Czech and Slovakian companies, as their guest composition is made up of visitors mostly from domestic and German territories at the same time some shortfall can be experienced here in 2003 too. It is a great task to integrate the activities and procedures of these two subsidiaries into the group but we are on our way to our objective and in 2003 significant steps were made in the areas of standardising sales, information technology and the reporting system. We continued the reconstruction programmes in the Czech Republic simultaneously to improving quality and we prepared the complex reconstruction of a hotel and health centre in Slovakia to be realised in 2004.

We maintained our severe cost and head count management last year too, and made several steps to counterbalance the negative external circumstances, nevertheless our results – for the first time in the life of our company – turned to a loss. Further chapters of the Annual Report will give detailed account of the exchange rate losses suffered due to the revaluation of the loans that have a great impact on the volume and direction of the results. It has probably become evident from my report until now that I have to tell bad news for the shareholders. Following this difficult year and aware of the accounting results I have to inform you that the Board of Directors did not approve the paying of dividend.

2004 will be a vital turning point in the history of Hungary, the Czech Republic and Slovakia as well. These countries – alongside with seven others – will join the EU on 1 May. Thus three from the four “member states” of the Danubius Group can be considered as a unit from certain aspects. This historical event is likely to have a positive effect on tourism in general, since business tourism is expected to grow, at the same time the number of tourists will also go up, which will be enhanced a lot by the spreading of budget flights. In Hungary, tourism will hopefully be less focused on Budapest, consequently our company will be able to take advantage of the higher rate and occupancy reserves inherent in the countryside (non-spa) hotels. The increase of turnover is only one aspect. By joining the EU some legal provisions and stipulations will become obligatory for the Hungarian, Czech and Slovakian hotels and enterprises a part of which will facilitate connections with the European countries and each other, however, others will produce surplus requirements which will have to be met by the new member countries sooner or later. However, the European Union is operating different funds in order to help the new member states and the enterprises working there in catching up and meeting new requirements. Therefore new financial sources, not available before, open up for the enterprises, which can be obtained by way of application. Our company shall endeavour in all three countries to follow the tenders invited and to acquire sources for projects where possible.

Finally, let me thank the persistent and demanding work of all Danubius employees, the co-operation of our partners and last but not least the support our shareholders gave our company throughout the past year. Let me assure you on behalf of the management that we will continue to face the future with optimism and we believe that the effect of the favourable changes experienced at the beginning of the year will keep up and we will be able to report to you in a brighter tone about 2004.


Sándor Betegh

We invite You

To enjoy the preventive and healing effect of the Hungarian, Czech, Slovakian and Romanian spas and treatments in our health spa hotels

The Hungarian health spa hotels, top class 4 star units, offering a full range of treatments, are located in Budapest and in Hungary's best known spa resorts, Hévíz, Sárvár and Bükfürdő.

In the Czech Republic's Bohemian Mountains lies the world famous Marienbad health resort. The town's significance is due to its beautiful location together with its mineral springs and its unique health complex found in the heart of the town. The valley encircled by hills, the clean air, the quiet forests together lend a special atmosphere to this place. Applications of the famous Marienbad mineral water include treatments for stomach, circulatory and urological ailments as well as locomotor disorders.



Spa Hotels in Hungary

- Danubius **Thermal Hotel Margitsziget** (4* superior)
- Danubius **Grand Hotel Margitsziget** (4* superior)
- Danubius **Thermal and Conference Hotel Helia** (4*)
- Danubius **Thermal Hotel Hévíz**, Hévíz (4*)
- Danubius **Thermal Hotel Aqua**, Hévíz (4*)
- Danubius **Thermal Hotel Sárvár**, Sárvár (4*)
- Danubius **Thermal & Sport Hotel Bük**, Bükfürdő (4*)

Spa Hotels in the Czech Republic

- Hotel Villa **Butterfly** (4*)
- Spa Hotel **Hvězda-Skalník** (4*)
- Spa Hotel **Nové Lázně** (4*)
- Spa Hotel **Centrální Lázně** (3*)
- Spa Hotel **Vltava-Berounka** (3*)
- Spa Hotel **Svoboda** (3*)
- Spa Hotel **Pacifik** (3*)
- Spa Hotel **Labe** (3*)

Piestany is one of Europe's favourite health spas. Its fame is enhanced by the healing powers of its thermal water and mud, along with the high-quality medical services and picturesque setting.

Located in the Valley of the River Váh in Slovakia, this exquisite health spa is just 70 kilometers from the Hungarian border. A high degree of medical expertise, coupled with quality service, offers relief for rheumatic ailments, spinal pains, motor disorders and also provide ample opportunity for rejuvenation for those in search of a relaxing experience.

Located at the western foot of the Transylvanian Harghita and Gurghiu Mountains, 500 meters above sea-level, the resort and health spa Sovata has been known across Europe for over a century.

Beyond its beautiful landscapes, its fame is largely due to Bear Lake (Lacu Ursu), the only so-called helio-thermal lake on the continent. The high salt content of the ground is dissolved within the lower layers of the lake with temperatures reaching as high as 50 degrees Celsius due to heat absorbed from sunrays through the upper, fresh-water layers. Called also the "Dead Sea" of Transylvania because of its high concentration of dissolved salts, this lake offers relief for a number of ailments.



Spa Hotels in Slovakia

- Spa Hotel **Balnea Esplanade** (3*)
- Spa Hotel **Balnea Palace** (3*)
- Spa Hotel **Balnea Grand** (3*)
- Spa Hotel **Balnea Splendid** (3*)
- Spa Hotel **Thermia Palace** (3*)
- Pro **Patria** (2*)
- Hotel **Jalta** (2*)
- Hotel **Park** (2*)

Hotels in Romania

- Danubius Hotel **Sovata** (3*)
- Hotel **Bradet** (2*)
- Hotel **Faget** (2*)

We invite You

*To stay in one of our city hotels
in Budapest or in Marienbad during your business trip*

Downtown, Castle hill, Danube embankment, green park
and Margaret Island location. Hotels from 3* to 5* categories offer
from standard hotel services up to the most luxurious one.
Corporate and preferential prices for short- and weekend stays not only
in Budapest, but in the countryside as well.



City Hotels in Budapest

- Hilton Budapest (5* de luxe)
- Danubius Hotel **Gellért** (4*)
- Radisson SAS **Béke** Hotel (4*superior)
- Best Western Grand Hotel **Hungaria** (4*)
- Congress Park Hotel **Flamenco** (4*)
- Hotel **Astoria** (4*)
- Hotel **Budapest** (4*)
- Hotel **Erzsébet** (3* plus)
- Hotel **Stadion** (3*)

City Hotels in Marienbad

- Hotel Villa **Butterfly** (4*)

We invite You

To taste the delicious traditional national foods in our restaurants

During your business trip, or holiday enjoy delicious national foods like

Halászlé (Fish soup), Borjúpörkölt galuskával (Veal stew with dumpling), Töltött káposzta (Stuffed cabbage), Fogasfilé (Pike-perch), Somlói galuska (Somló noodle) in one of our Hungarian restaurant,

Ciorbă supe (Ciorba Soup), File de păstrăvi (Trout Filet), Platou ardelenesc (Transylvanien Mixed Grill), Mămăligă cu smântână (Cornmeal Porridge) in Romania,



Pečená kachna s červeným zelím, variace českých knedlíků
(Roast Duck with Stewed Red Cabbage, Variation of Czech Dumplings),

Plzeňský guláš vařené vejce, párek, cibule, krokety a špekové knedlíky
(Beef Goulash-Pilsen Style, Boiled Egg, Frankfurter, Onion, Croquette and Dumpling in Bohemian Style),
in our Czech restaurants or

the real slovakian Bryndzové halušky so slaninkou
(Potato dumplings with sheep cheese).

Do not miss to start with Borovicska in Slovakia or in the Czech Republic
and to enjoy the well known Hungarian wines or Czech beers.

We invite You

*To organise conferences, meetings and events
in our well equipped facilities*

To ensure the highest quality, we have created Danubius Quality Conference, a product that is your guarantee of the best possible services. With modern equipment, comfortable surroundings and attractive conditions, our hotels take care of your every need. Our conference and banqueting rooms, catering from small parties to conferences of up to 1100 participants, can satisfy the demands of all our clients.



Our health spa hotels in Marienbad, Piestany and Sovata are ideal for organising conferences, seminars, business meetings and lunches, banquets and cocktail parties. In the breaks or spare-time you can enjoy the spa, fitness and sport services of these hotels.

We invite You

To spend your holiday in a Hungarian resort

Enjoy the sunshine and water sports at Lake Balaton, discover the historical sights and natural beauty of cities and their surroundings in Pécs, Sopron and Győr.
Offers ranges from short stays to family holidays.



Resort and Countryside Hotels in Hungary

Bio-Sport Hotel **Lövé**r, Sopron (4*)
Hotel **Helikon**, Keszthely (3*)
Hotel **Annabella**, Balatonfüred (3*)
Hotel **Marina**, Balatonfüred (3*)
Hotel **Rába**, Győr (3*)
Hotel **Palatinus**, Pécs (3*)
Hotel **Pát**ria, Pécs (3*)

We invite You

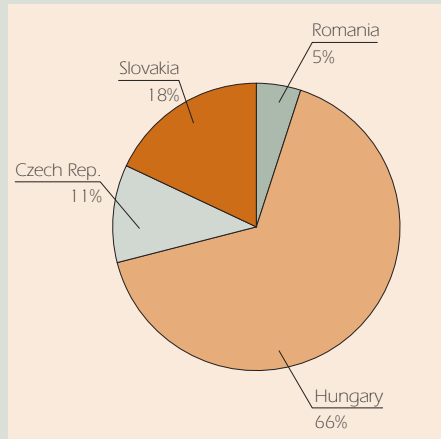
*To use the fitness, wellness,
sport and beauty services of our hotels*

Danubius Premier offers a complete wellness experience based on our quality fitness product. Our aim is to help you escape and revitalise your mind, body and soul. Under the brand name, Danubius Premier, we offer the perfect balance of quality, purpose built fitness facilities and fun, activity programmes to help you relax and re-charge.

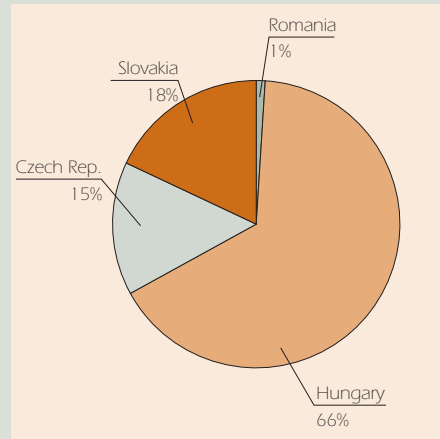


FIGURES AND RATIOS IN HOTEL BUSINESS – IN 2003

Distribution of the number of rooms



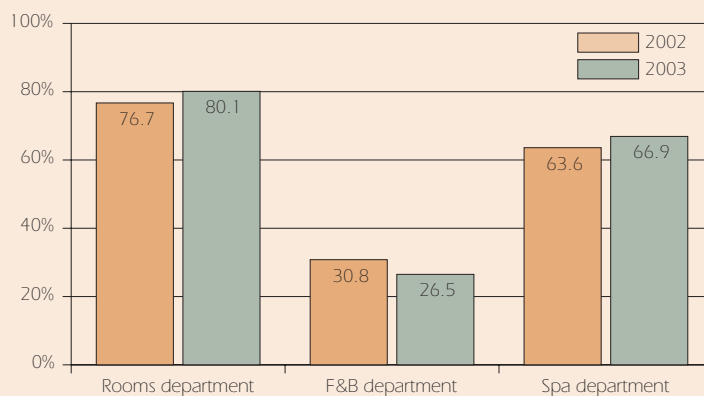
Distribution of revenues



HUF million

	Hungarian hotels	Czech hotels	Slovakian hotels	Romanian hotels
Profit of rooms department	9,937	2,407	1,383	183
Profit of F&B	2,231	365	288	78
Profit of spa department	1,027	787	2,219	
Profit of other minor departm.	-36	55	-708	11
Departmental profit	13,159	3,614	3,182	272
Profit margin	54.6%	64.1%	47.5%	81.0%

Profit margin of departments

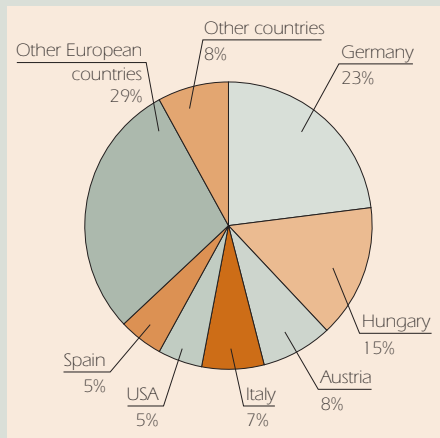


FIGURES AND RATIOS IN HOTEL BUSINESS – IN 2003

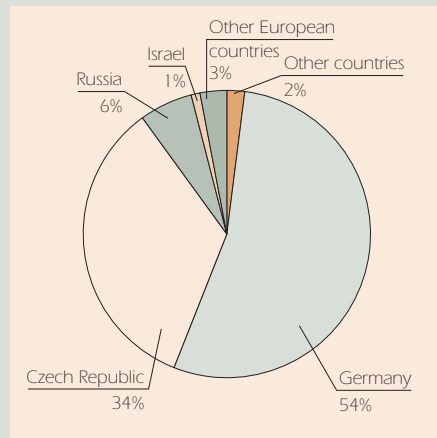
	Hungarian hotels	Czech hotels	Slovakian hotels	Romanian hotels
Number of rooms	5,578	923	1,538	302
Occupancy	58.3%	76.5%	75.6%	48.6%
Average rate (in HUF)	11,383	14,077	5,128	2,552
Number of staff	3,192	689	1,733	197
Average number of staff / rooms	0.57	0.75	1.13	0.65

Distribution of guestnights

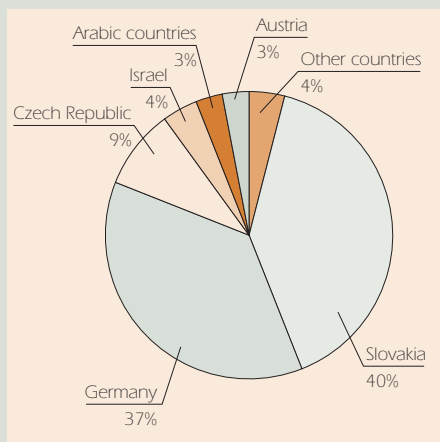
In the Hungarian hotels



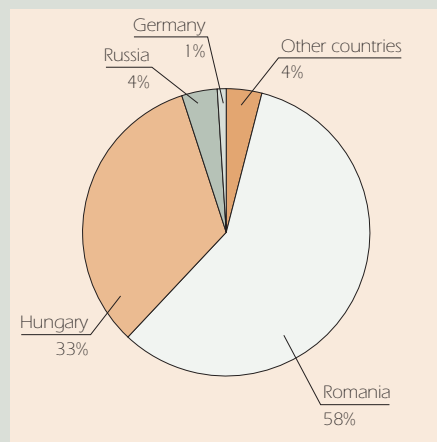
In the Czech hotels



In the Slovakian hotels



In the Romanian hotels



TOURISM IN HUNGARY, IN THE CZECH REPUBLIC, IN SLOVAKIA AND IN ROMANIA

A new era started in tourism on 11 September 2001 and the war and terror acts occurring from time to time in the period since then as well as virus infections put obstacles in the way of recovery. In addition to the general lessening of the incentive to travel, the recession of the German economy poses a problem for the Hungarian, Czech and Slovakian tourism. Despite all of the above, the signs of improvement already show at the end of 2003 and the beginning of 2004 and opinions declared at the WTO conference in Madrid in January and at the Berlin tourism fair held in March reflect optimism from the experts of the industry.

Statistical data of the Hungarian tourism indicate the stagnation and/or a moderate decrease of the performance of the branch in 2003.

	2003	2002	Change
Number of rooms in hotels (on 31 st December)	38,600	36,925	104,5%
Number of guestnights (in hotels, in thousand)	11,542	11,681	98,8%
From this: foreign	7,260	7,529	96,4%
domestic	4,282	4,152	103,1%
Room occupancy in hotels	44,1%	45,1%	+1%
Room revenue in hotels (HUF million)	73,738	74,034	99,6%
From this: foreign	56,511	58,319	96,9%
domestic	17,227	15,761	109,3%

The capacity increase, which made participants of the domestic hotel industry face a serious problem continued: 14 new hotels opened up at national level the majority of which appeared in Budapest and on the Balaton side. This led to 37% increase in the hotel room supply in the past five years. While the number of three-four star hotel rooms went up by one and a half times, that of the five star rooms doubled.

The demand did not follow the increase in supply. The number of guest nights was only 10% higher in 2003 compared to that five years ago and growth was only 40–65% in the higher categories. Last year the total number of guest nights spent in the hotels went down unfortunately, which is made up of the decrease in the number of foreign guests and the increase of domestic guests. This has been the trend for years since 14% less guest nights were recorded in 2003 from Germany, representing the majority of the share, than five years before, however, the number of domestic guest nights went up by 22% during the same period.

The disproportion of the number of rooms and number of guests shows in the movement of the hotel room occupancy and the room revenues.

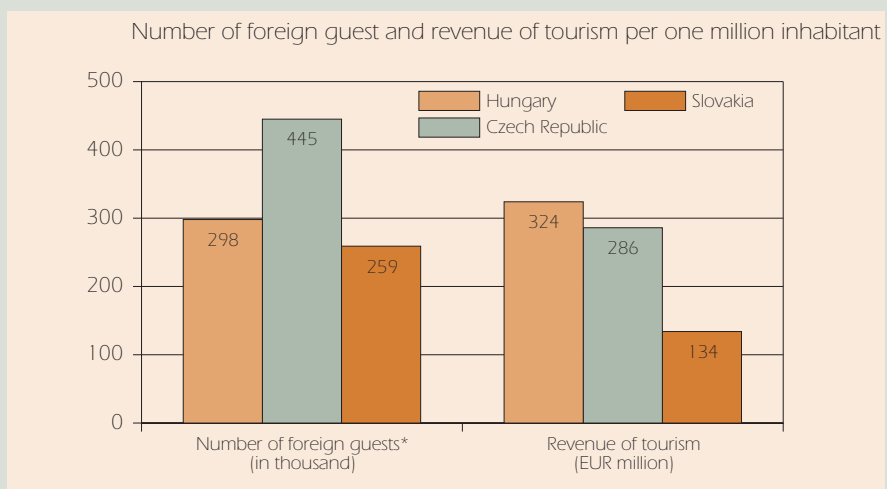
Room revenues also went down last year (by 0.4%). A positive change took place in the room rates paid by domestic guests (+9.3%), which went up to a greater extent than the number of guest nights.

The geographical and natural conditions of **Slovakia** are quite outstanding still these are not reflected by the performance of the tourism.

Although the number of guests in the past five years continued to grow (+20%) especially the number of foreign guests went up significantly (42%) and there are more and more domestic tourists as well (+9% compared to 1999) still experts would like better results. According to them a growth that is slower than what circumstances and conditions would allow is due to the lack of domestic and foreign capital as well as human factors. As a consequence of the lack of capital, capacity did not increase significantly in Slovakia but the problems indicated when presenting the Hungarian tourism occur here too. Tourists from Germany and overseas were lagging behind in Slovakia too, their number decreased by 7% and 10% in the past year and the gap was mostly compensated with the increase of guests from the surrounding countries: Hungarians spent 10% more, while Czechs 13% more guest nights in Slovakia.

The **Czech Republic** pursues the most intense country image from among the three countries introduced and this seems to be reflected in the guest statistical data. Both the number of foreign and domestic guests went up by 6% last year, although the length of stay moderated. The number of Germans lessened here too (-5%), however, guest numbers were up not only from the surrounding countries but several West European and overseas countries (Britain +38%, The Netherlands +33%, USA +18%) as well.

In the sequence of the three countries based on the number of guests arriving to the commercial accommodation places, Czech Republic is first, whereas revenues from tourism are the highest in Hungary (exceeding those in the Czech Republic by 11%).



* Number of foreign guests at commercial accommodation establishments
 Source: Hungarian, Czech and Slovakian Statistical Office, National Bank of Hungary, World Tourism Organisation

REPORT OF THE BOARD OF DIRECTORS

Major Problems for Tourism Worldwide – 2003

The performance of world tourism in 2003 was presented as the most negative trend in the history of the industry at a conference of the World Tourism Organisation held in Madrid in January this year. Since the events of September 11th 2001, the projections for the growth of world tourism have been shattered by terrorist activity, conflicts, particularly of course the Iraq war, economic recession and the spread of the SARS virus and other epidemics. As a result everyone involved in the hospitality and travel industries has suffered and a series of crisis measures were introduced by airlines, travel agents and hotels.

Europe certainly bore its share of these negative developments and within the performance of Danubius Hotels Rt., all the domestic Hungarian hotels were affected, but particularly the city centre properties in Budapest. These trends compounded the problems already being experienced in Budapest through a continuing and substantial growth in hotel capacity.

Overall, the Danubius Group showed a small growth in revenues because the fallback in Hungary was compensated by revenues from investments from other countries in the region. However, this moderate growth could not cover cost increases, driven particularly by the inflationary effects on payroll levels with EU accession in sight.

All of these factors resulted in a 2003 gross operational profit of Huf 5.9bn which was 80.4% of 2002. However, as we reported in a previous flash report the bottom line result continues to be affected by a substantial unrealised foreign currency loss, now of Huf 1.325bn, as well as by increased depreciation charges.

Prospects for 2004

As we anticipated in the third quarter flash report, the fourth quarter of 2003 saw an improvement in business. At the WTO meeting, somewhat more optimistic signs were emerging from the USA, Japan and Western Europe but the situation is still fragile. The German economy remains weak and recovery could be a long process whilst the world is getting accustomed to the new conditions created by international tourism and the other factors referred to above. It is still uncertain how any pickup in world tourism will continue to develop.

If we can go through a more peaceful and settled time then we can hope for improvement. However, 2004 has already seen tourist scares causing airline cancellations and delays, more burdens on travellers through enhanced security arrangements. Opening of some further new capacity is also expected in Budapest this year.

In terms of our Hungarian business, after the significant set back in guest nights at national level in the first quarter (-6.5%), the rate gradually decreased (-3.1%, -2.5%, -1.2% in the next quarters) followed by a fourth quarter increase of room revenues which led to only a 1.4% overall annual decrease by the year-end.

With regard to occupancy, the decrease of 2.9% in the first half was moderated to an overall 0.7% by the year end at Danubius Hotels Rt. Owing to this improvement in the second half and the weakening of the HUF, average rates increased by 4.3% at group level as compared to the prior year.

Tourist Market

The cautious improvement in the **Hungarian hotels** in the second half did not compensate for the first half-year set back, either in the number of guests or in the number of guest nights. A special change in guest composition was experienced. The domestic customer continues to grow in importance and the fight for winning guests with good spending power is ever increasing on the Hungarian tourist market. The ratio of domestic guest nights went up to 15.2% by the end of 2003 but this was even higher at popular holiday resorts (Hotel Löver in Sopron 70.9%, Hotel Helikon in Keszthely 42.2%, Thermal Hotel Bük 30.9%). The increase of the ratio of domestic guests did not influence revenues and average spend positively, especially in the field of therapies since the domestic guests choose 2–3 day week-end holiday programmes and take less advantage of medical treatments.

This change in the structure of guests is not only characteristic of Hungary. Most of the European countries have been taking special care for a couple of years to promote domestic holidays to their own citizens to off-set reduced overseas turnover. Looking at the guest composition of Danubius, the number of guests arriving from the German speaking territories (with the exception of Switzerland) has shown a decreasing trend. The number of overseas (USA, Canada, Japan) guest nights, which dramatically fell back after September 2001, are still down but by a lesser amount. A national publicity campaign was launched trying to turn this trend around. However, the results will only be seen by the end of 2004. In line with the government agreements drawn up with China, we were able to welcome the very first Chinese guests in our Budapest hotels. Their share is not yet 1% but we must bear in mind that the official tourist turnover started only in the second-half of January 2004. The missing overseas and West European guest nights were primarily compensated for by tourism from the surrounding countries although, as a result of previous efforts made in France and Sweden, satisfactory growth was recorded from these territories.

The guest groups in our Czech and Slovakian hotels were less influenced by the consequence of the world political events mentioned earlier. Due to their guest composition, occupancy and revenues were adversely affected by the weakening of the German economy and of course the attempt of the German government to motivate own citizens for domestic holidaymaking.

Although German guests are spending less time in fewer numbers at the **Marienbad** hotels, their share in revenues did not decrease in spite of the fact that their 53.5% share in total guest nights was 3.6% lower compared to the previous year. A growth in the proportion of local guests in our Czech hotels (from 31.9%) was also experienced. Russian guests showed the third largest increase of 1%.

The number of guest nights in our **Slovakian** hotels did not change much. The 0.3% net drop is worth mentioning only because the majority of the decrease was from the German guest group, which was mostly compensated by spa guests arriving from the Czech Republic. Approximately 40% of the guest nights was spent by guests referred to the spa by the Slovakian social security, followed by German guests with a 36.6% share. Czech guests increased by 9.4%, the Austrians by 3.1% but some Arab countries reduced guest nights due to international problems.

Hotel Sovata started operating gradually in the course of 2003 and Hungarian and Romanian guests already show keen interest for the services of the hotel making up 90% of the guests. Since the summer opening of the spa section it has been in the process of being introduced to the market through significant marketing activities to win spa guests. Hotel Sovata was awarded hotel of the year in Romania in 2003.

Consolidated Balance Sheet

- Our company held 51% of the shares in Preventív Rt., the company responsible for the safety and security of all Hungarian hotels, which was included in the consolidated statements of the group. Preventív Rt. carried out a capital increase at the end of the year 2002 in which Danubius Hotels did not participate. In consequence, our ownership share decreased to 32.75% and so Preventív Rt. is no longer among the companies consolidated.
- The value of own capital contains the whole year profit of both SLKP and Salina Invest Rt. in 2003.

No other network change distorts comparability.

The value of assets went up by the value of the activated investments of Hotel Sovata and other domestic and foreign hotels, while liabilities follow the movements of the loans. Total assets of the company increased by HUF 1.3 billion as opposed to 31 December 2002 and its value surpasses HUF 68 billion.

The value of total working assets is by 5% less than in the previous year which is due to the decrease of the accounts receivables (-7,7%) and the VAT receivable (-70%) among the other receivables.

In the 2.8% growth of invested assets, the value of other invested assets went up by HUF 413 million from which HUF 381 million increase is the cash held on deposit for the finance of the reconstruction in Piestany and HUF 31 million is because Preventív Rt. is no longer consolidated and its value is included in this row. The value of deferred tax assets increased significantly (+59%), the majority of which was created for the accrued loss of the former years (+ HUF 306 million compared to last year).

Significant change in liabilities took place in trade accounts payable and in short-term liabilities owing to the loan repayment obligation due in 2004 and a tax obligation of SKK 20 million. Long-term loans of the company went down by approximately HUF 400 million. The HUF 1.16 billion increase in the translation reserve reflects the exchange rate changes of national currencies compared to the HUF in the IFRS.

Consolidated loans as of 31 December 2003: EUR 72.7 million, USD 6.6 million and ROL 90 billion.

REPORT OF THE BOARD OF DIRECTORS

Consolidated Profit and Loss Statement

Our company achieved a revenue of HUF 36.9 billion in 2003 as opposed to HUF 35.7 billion in the previous year. The Slovakian company – as a result of its all year consolidation – contributed to the 3.2% revenue increase by HUF 6.7 billion compared to the HUF 3.9 billion of the previous period (seven months). The Hungarian companies performed 65.6% of the group level revenues, the Slovakian companies 18.2%, the Czech firms 15.3% and the Romanian units 0.9%.

47.2% of the operational revenues came from room sales, 30.4% from food and beverage, 16.4% from spa at group level.

HUF million

	2002*	2003**	Of which			
			H	CZ	SK	RO
Total operational revenue	35,545	36,777	24,109	5,635	6,697	336
<i>share</i>			65.6%	15.3%	18.2%	0.9%
Room departmental profit	12,616	13,909	9,936	2,407	1,383	183
F&B profit	3,250	2,962	2,231	365	288	78
Spa profit	3,063	4,033	1,027	787	2,219	0
Other departmental profit	522	-678	-36	55	-708	11
Departmental profit	19,451	20,226	13,158	3,614	3,182	272
Departmental profit margin	54.7%	55.0%	54.6%	64.1%	47.5%	81.0%

* including the 7 months consolidated data of the Slovakian hotels

** Hotel Sovata was closed in the first quarter of 2003 due to reconstruction works, half of the rooms were opened to the public in April the other half in June.

HUF million

Items	Departmental profit 2003		Compared to prior year
	20,226		
	Items of decreasing effect	Items of increasing effect	+775
Other revenues		243	-716
Interests received		110	-85
Administrative and general costs	12,986		-1,651
Depreciation	3,983		-612
Other expenditures	1,605		+156
Interests paid	806		+40
Foreign currency loss (gain) – unrealised	1,325		-1,883
Total	20,705	353	-4,751
Profit (loss) from ordinary activities before income tax and minority interests		-126	-3,976

The changes of costs exceeding revenue increase reflect the inflation surpassing increase of raw material prices and public utility fees. The majority of the significant increase in administrative and general costs was caused by the five months consolidation cost surplus of SLKP. Costs benefited by the settlement of ongoing rental disputes about some 5th district properties and certain receipts from the insurance claim concerning the Gellért flood in 2002. The total HUF 2.67 billion operating cost increase was not compensated by the HUF 1.23 billion operating revenue surplus, therefore at operating level the HUF 5.9 billion profit is HUF 1.44 billion less compared to the previous year.

The HUF 612 million increase in depreciation is primarily due to the asset value increased as a result of investments in the Slovakian and Romanian hotels, the different consolidation period of the Slovakian hotels and the one-time write-offs of the Romanian small value fixed assets. Interests and other financial revenues continued to go down, though to a lesser extent, alongside moderate expenditures. Of the HUF 2.1 billion ordinary profit fall compared to the previous period HUF 612 million is the depreciation increase and HUF 770 million is the one off profit achieved on the sale of Hotel Eger in 2002. This further deteriorated year on year by HUF 1.9 billion, which is the difference of the EUR and the unrealised technical rate loss calculated on the loans compared to the previous year. The HUF 126 million loss before tax indicates almost HUF 4 billion profit deterioration.

The income tax benefit was HUF 473 million in 2003 from which HUF 744 million is the deferred tax benefit. It contains the release of the tax on the unrealised technical gain accounted on loans in the last two years (due to the technical loss of this year) and the corporate tax difference of the foreign subsidiaries (Czech corporate tax change is from 31% to 28% and Slovakian from 25% to 19%).

Revenues of the Hungarian hotels show 2.2% lessening as a result of occupancy going down by 1.3% and alongside the same average rates as last year, which is a slight improvement as opposed to last year's (2002/2001) 5.8% decrease.

It seems expedient to value the profitability figures of the subsidiaries in the national currencies owing to the distorting effect of the exchange rate changes.

Although the occupancy figures of the Czech hotels moderated by 2.4% (76.5%) total revenues went up by 5% through a notable 23% improvement of the average rates (calculated in CZK).

The 2.7% revenue decrease of the Slovakian hotels calculated in SKK is the consequence of the 3.8% (75.6%) occupancy increase (calculated for the entire year at base level) and the 8.3% decrease of average rates.

Wage and head count management

We have carried out wage management and streamlined head count thoughtfully and endeavoured to increase efficiency and work with an optimal head count adjusted to the turnover. We have realised 5.8% cut on head count alongside 2.3% increase of wages at group level. A part of the reduced work force was replaced by outsourcing from professional companies. The modification of employee contracts enabled us to move staff from one hotel to another.

We have organised more than 60 further education and development training courses for our employees with the aim of creating value at our company, best internal practices

and outside experience. Around one thousand students from industrial trade and vocational schools as well as one hundred high school students spent their practical training course in our hotels.

Reconstruction and developments

The ongoing recession of the tourism industry largely determined our development and investment activities enabling us to carry out exclusively the most necessary works and reconstructions. This comprised mainly maintenance and development works ensuring the smooth operation of the hotels including mandatory works.

In 2003 development expenditures totalled HUF 1.5 billion as follows:

1. Among the modernisation of service areas the following should be highlighted:
 - kitchen reconstruction works in **Hotel Aqua** were completed, and connecting technical units were installed (refrigeration block, dish washer, extractor fans)
 - the replacement of the complete boiler house in **Hotel Marina** in Balatonfüred means both the modernisation of the heating system and cost reduction on the supply of hot water and heat. The entire water supply system was changed in the tower building. A lift for the disabled was built to connect the lobby and the restaurant.
 - the kitchen in **Hotel Rába** in Győr was furnished with a deep freeze and a cooling chamber.
The parking lot was secured by a remote controlled hydraulic structure instead of a gate.
2. In the area of face lifting and operational aspects, the following projects should be pointed out:
 - the lobby of **Hotel Béke** was renovated with a new attractive front office counter and seating furniture, new floor covering and a new meeting room for guests was added. Seventy-three bathrooms were also refurbished.
 - the completion of the entire refurbishment of the brasserie of **Hotel Gellért** that suffered water damages earlier was of vital importance, producing one of the most popular brasserie restaurants opened to the public before the Christmas holidays,
 - the refurbishment of the mud section of the therapy department in **Thermal Hotel Aqua** was completed by the beginning of the year as the first phase of the reconstruction of the most used therapy department,
 - forty-nine room units were refurbished on the 8th floor of **Hotel Stadion**, completing the room refurbishment programme started two years ago,
 - on the 5th and 6th floors of **Hotel Helia** a total of 90 room units were refurbished including the connecting corridors and lift halls,
 - the first phase of the front face lift of **Hotel Marina** is ready, currently cooling chamber developments are in process in line with new HACCP stipulations,
 - new windows and doors were put in 56 rooms in **Hotel Annabella** accompanied by black out curtains,
 - **Hotel Lóvér** in Sopron has a new signage,
 - sixty rooms were freshened up in **Thermal Hotel Sárvár** by partial renewal of the furniture, wall papering, wall to wall carpet laying and some new room textiles,
 - the outer windows in the historical wing of **Hotel Astoria** were replaced by sound proof, insulated window structures and heat-proof aluminium shutters,

- the coffee shop in **Hotel Budapest** was furnished with a new counter system,
 - some built in furniture in 80 rooms of **Grand Hotel Margitsziget** was renewed,
 - the north façade of **Thermal Hotel Hévíz** was renewed to match the landscape and the new insulating cover produces significant energy cost saving,
 - balconies were renewed in 50 rooms in **Hotel Helikon** and the doors on the loggias were replaced,
 - the elevator renewal programme was set forth in several hotels in line with requirements set by the supervisory authorities
3. A new computer programme package supporting maintenance work was developed and installed in all units of our hotel company by the end of the year providing up to date central supervision over cost sensitive fields of decisive importance such as energy use and technical operations and maintenance.

Technical preparations are in process for outstanding developments of the near future as well.

- The renewal of the dilapidated facade and roof structure of the building will soon be started as the first phase of the reconstruction of Hotel **Nádor** in Pécs together with execution works of the under surface parking area connecting to the earlier built public road access.
- We have invited a tender for a reconstruction of the historical wing of Hotel **Astoria** and in February we start the main building service system and simultaneously the air conditioning of 33 rooms on the Magyar street side.
- In order to be able to find a solution to meet the pressing guest requirements for air conditioning, it will be introduced to **Hévíz Thermal, Bük, Sárovar, Palatinus, Pátria** and **Stadion**.

At the company **Léčebné Lázně, in Marienbad** the total costs of reconstruction and repairs reached CZK 91.5 million (HUF 729 million) in 2003.

Main works done:

- Full refurbishment of the basement and 1st floor of the Hotel Pacific, including new kitchen and 9 new rooms of 4-star category. Working out a master plan for the realization of the 2nd and 3rd reconstruction stages of the hotel.
- At the Nové Lázně reconstruction, extension and modernization of service areas in the hotel, including new Vienna Coffee Shop with summer terrace and new air-conditioning, kitchen and equipment was completed. A new mineral water drinking facility was built in the basement. A new health department for doctors and guests in the basement was executed. Two lifts in the hotel were modernized. Refurbishment of 6 new luxury rooms (of which 3 apartments) is under way, starting on 1st December 2003.
- Following works were made compulsory by the local Construction Office: securing and maintaining the landmark buildings Kavkaz (Edward) and Snezka, repairing and painting steel construction and repairing roof insulations of the main Colonnade.
- New boring for mineral water (New Forest Spring).

The main reconstruction works in **Piestany** in 2003 were the following: refurbishment of the kitchen in the Pro Patria and rooms on two floors in Balnea Esplanade, the renewal of the transformer stations in Balnearehabilitation Centre II. as well as the replacement of two lifts in Spa Hotel Balnea Grand were completed, works on the golf course were also finished and the boiler house in Hotel Zahorie in Smrdaky was renewed. The

refurbishment of the cupola in Irma bath was launched, and the reconstruction of Thermia Palace and the pools and traction bath in Balnearehabilitation Centre II. is in the phase of preparation. The planning of the general reconstruction of the Island's heating system was started. Together with the long-term development plan of the information technology system the company has spent SKK 83.6 million (HUF 511 million) on reconstructions completed during the year 2003.

In **Sovata** we have refurbished in several phases and opened to the public all rooms and common areas in Hotel Sovata in the first quarter of 2003 and the reconstruction of the spa section was completed by the end of July. We have spent USD 6 million on these works and in connection with the extensive reconstruction of the hotel the integrated information technology system supporting the front office, restaurant and spa activities was also introduced. (Through this we have lived up to our contractual capital increasing obligations in 2003).

The lessee of the Bradet left the hotel making it possible for us to take it into possession and start repair, renewal and painting works already in the fourth quarter, which we plan to complete before the spring opening in 2004.

Environment protection

Following investments were implemented in the hotels of Danubius Rt. in 2003 with the aim of environment protection:

- the heating oil containers put out of use in Hotel Annabella and Hotel Marina was started to be replaced and their use terminated,
- up to date cooling chambers protecting environment were built in Hotel Rába, Hotel Annabella and Thermal Hotel Sárvár,
- a modern wastewater pump was put into operation in Thermal Hotel Margitsziget,
- in the course of the reconstruction of the south wing façade of Thermal Hotel Hévíz we have applied a technical solution – in co-operation with the Balaton-Felvidék National Park – to ensure the safety of the protected bats.

Stock Exchange trading, ownership structure

According to 31 December 2003 data 53.4% of the subscribed capital made up of 8 285 437 ordinary shares is owned by domestic and foreign investments of CP Holdings Ltd., of which a share over 5% is owned by Interag Rt. (29.38%), Israel Tractors (6.12%) and CP Holdings Ltd. (17.90%). Further 29.16% of the shares is owned by foreign financial investors among whom Citibank as safe custody manager nominated 20.42% shares.

The share of the employees of the company is 1.15%, and the company continues to own 4.52% own shares. Domestic private persons, institutions and pension funds own 11.77% of shares.

A total of 4256 deals were made for 1 356 439 shares of Danubius Hotels Rt. on 250 trading days to the tune of HUF 4340 million in 2003 producing an average share price of 3199 HUF /share. The closing price in 2003 was HUF 3305.

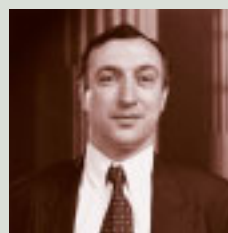
The organisation of the company has not changed during 2003, and changes in the rows of leading office bearers were published with the AGM resolutions.

THE BOARD OF DIRECTORS



Sir Bernard Schreier

Chairman of the Board; Chairman and Chief Executive Officer of CP Holdings Limited and subsidiaries, and Investor Holding Rt.; Vice President of Bank Leumi Plc.



Robert Levy

Joint Managing Director of CP Holdings Ltd. and subsidiaries.



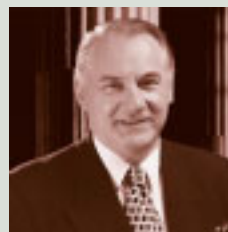
Sándor Betegh

Chief Executive Officer of Danubius as of October 1990 (President and CEO between 1991 and May 1996).



John Smith

Joint Managing Director of CP Holdings Ltd. and subsidiaries and Investor Holding Rt.



József László

Manager of SAS Scandinavian Airlines in Budapest until 1998; currently Head of the English Language Section of the Collage of Commerce, Catering and Tourism.



Iris Gibbor

Director of CP Holdings Ltd.



Ing. Lev Novobilsky

General Manager of Léčebné Lázně a.s.



Dr. István Fluck

General Vice President of FEM, Director and Chief Physician of Budapest Spa Rt.



Dr. Imre Deák

Senior Vice President of Danubius as of December 1990.



János Tóbiás

Vice President, Finance of Danubius as of 1991.

CONSOLIDATED BALANCE SHEET

Danubius Hotel and Spa Rt. and Subsidiaries
Consolidated Balance Sheet

(All amounts in million HUF)

	Notes	At December 31,	
		2003	2002
Assets			
Cash and cash equivalents	3	3,768	3,825
Accounts receivable	4	1,467	1,590
Other receivables and prepayments	5	1,171	1,252
Income tax receivable	19	439	594
Inventory	6	566	527
Total current assets		7,411	7,788
Property, plant and equipment	7	62,476	61,448
Intangible assets	8	(2,471)	(2,556)
Other non-current assets	9	881	468
Deferred tax assets	19	432	271
Total non-current assets		61,318	59,631
Total assets		68,729	67,419
Liabilities and Shareholders' Equity			
Trade accounts payable		1,687	2,279
Advance payments from guests		240	173
Income tax payable	19	44	19
Other payables and accruals	11	2,034	1,657
Current portion of long-term debt	12	5,442	4,396
Provisions	10	701	856
Total current liabilities		10,148	9,380
Long-term debt	12	15,434	15,813
Deferred tax liabilities	19	1,801	2,401
Total non-current liabilities		17,235	18,214
Minority interests	13	2,462	2,538
Shareholders' Equity			
Share capital	14	8,285	8,285
Capital reserve		7,435	7,847
Treasury shares	14	(1,162)	(1,574)
Retained earnings		23,076	22,635
Translation reserve		1,250	94
Total shareholders' equity		38,884	37,287
Total liabilities and shareholders' equity		68,729	67,419

CONSOLIDATED STATEMENT OF INCOME

Danubius Hotel and Spa Rt. and Subsidiaries
Consolidated Statement of Income

(All amounts in million HUF)

	Notes	Year ended December 31,	
		2003	2002
Revenue			
Rooms		17,355	16,452
Food and beverage		11,165	10,562
Spa		6,027	4,818
Other departmental revenues		1,987	2,754
Interest income		110	195
Other revenue	16	243	959
Total revenue	28	36,887	35,740
Costs and expenses			
Rooms		3,446	3,836
Food and beverage		8,203	7,312
Spa		1,994	1,755
Other departmental expenses		2,665	2,232
Administrative and general	17	12,986	11,335
Interest expense		806	846
Foreign currency loss / (gain)		1,325	(558)
Depreciation and amortisation		3,983	3,371
Other expenses	18	1,605	1,761
Total costs and expenses		37,013	31,890
Profit/(loss) before tax and minority interests		(126)	3,850
Income tax (expense) / benefit	19	473	(934)
Net profit after tax		347	2,916
Minority interests	13	94	(11)
Net profit for the year		441	2,905
Earnings per share (expressed in HUF per share):	20	56	367

CONSOLIDATED STATEMENT OF CHANGES IN SHAREHOLDERS' EQUITY

Danubius Hotel and Spa Rt. and Subsidiaries
Consolidated Statement of Changes in Shareholders' Equity

(All amounts in million HUF)

	Note	Share Capital	Capital Reserve	Treasury Shares	Retained Earnings	Translation Reserve	Total
December 31, 2001		8,285	7,792	(1,536)	19,730	458	34,729
Net profit for the year					2,905		2,905
Gain on treasury shares transactions			38	(38)			–
2001 Dividend on treasury shares			17				17
Translation of foreign subsidiaries						(364)	(364)
December 31, 2002		8,285	7,847	(1,574)	22,635	94	37,287
Net profit for the year					441		441
Loss on treasury shares transactions	14		(412)	412			–
Translation of foreign subsidiaries						1,156	1,156
December 31, 2003		8,285	7,435	(1,162)	23,076	1,250	38,884

CONSOLIDATED CASH FLOWS

Danubius Hotel and Spa Rt. and Subsidiaries
Consolidated Statement of Cash Flows

(All amounts in million HUF)

	Note	Year ended December 31,	
		2003	2002
Cash flows from operating activities:			
Net profit		441	2,905
Adjustments for:			
Income tax	19	(473)	934
Minority interest	13	(94)	11
Interest income		(110)	(195)
Interest expense		806	846
Depreciation and amortisation		3,983	3,371
Foreign exchange (gain) / loss		1,325	(558)
Gain on sale of fixed assets		(59)	(766)
Changes in assets and liabilities:			
Accounts receivable and other receivables		651	(140)
Inventory		(39)	(4)
Accounts payable and other current liabilities		(254)	(69)
Cash generated from operations		6,177	6,335
Interest paid		(830)	(850)
Corporate income tax paid		(523)	(561)
Net cash flow provided by operations		4,824	4,924
Cash flows from investing activities:			
Purchase of fixed assets		(3,684)	(3,566)
Net cash outflow on acquisition of subsidiaries		—	(8,013)
Interest received		70	203
Proceeds on sale of fixed assets		375	1,067
Increase in restricted cash		(381)	(185)
Other cash inflows/(outflows)		(198)	(92)
Net cash flow used in investing activities		(3,818)	(10,586)
Cash flows from financing activities:			
Net increase/(decrease) in long-term debt		(1,063)	5,928
Sale of treasury shares		1,162	1,574
Purchase of treasury shares		(1,162)	(1,574)
Dividend paid		—	(389)
Dividend on treasury shares		—	17
Net cash flow provided by financing activities		(1,063)	5,556
Increase / (decrease) in cash and cash equivalents		(57)	(106)
Cash and cash equivalents at beginning of year		3,825	3,931
Cash and cash equivalents at end of year	3	3,768	3,825

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

1 The Company and its recent history

Danubius Hotel and Spa Rt. ("Danubius" or "the Company") is a company limited by shares incorporated under the laws of the Republic of Hungary. The Company and its subsidiaries (the "Group") provide hospitality services in Hungary, Czech Republic, Slovakia and Romania, with an emphasis on 3, 4 and 5 star spa and city hotels. The Company's shares are listed on the Budapest Stock Exchange. Currently 53.4% of the Company's shares are owned by CP Holdings Limited, a UK private company, and companies controlled by CP Holdings Limited.

Danubius is a holding company and has two principal subsidiaries in Hungary, a hotel operator and a property management company. The Hungarian hotel operations were reorganised on January 1, 2002. The hotel units were reorganised into regional centres primarily based on their geographical location.

The Company has a 95.36% shareholding in Léčebné Lázně a.s., a hotel company with operations in Marienbad, Czech Republic and a 100% shareholding in Gama 45 s.r.o (which owns a hotel in Marienbad).

In 2001 a consortium in which Danubius had a 20% interest, acquired a 82.17% share in Balneoclimaterica SA, which owns a hotel and real estate complex in Sovata, Romania. In 2002 the consortium acquired further 11.8% in Balneoclimaterica SA and Danubius acquired an additional 36.52% stake in the consortium company, Salina Invest SA. In 2003 the equity of Salina Invest SA was increased, in which the owners were not equally participated and as a result the share of Danubius decreased by 0.09%. As at December 31, 2003 Danubius owned 56.43% (December 31, 2002: 56.52%) of the shares of Salina Invest SA and had a 53.03% (December 31, 2002: 53.11%) effective interest in Balneoclimaterica SA (see note 25).

In May 2002 Léčebné Lázně a.s. acquired a 67% shareholding in Slovenské Liečebné Kúpele Piestany a.s. ("Piestany"), a Slovakian hotel company with operations in Piestany and Smrdaky. Subsequently Danubius acquired a further 20.66% shareholding in two instalments during 2002. As at December 31, 2002 and 2003 the Group owned an 84.55% effective interest in Piestany (see note 25).

2 Significant accounting policies

Statement of Compliance

The Company and its subsidiaries maintain their official accounting records and prepare financial statements for domestic purposes in accordance with national accounting regulations in Hungary, Czech Republic, Slovakia and Romania as appropriate. The accompanying consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") adopted by the International Accounting Standards Board (IASB), and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) of the IASB and, as a consequence, reflect adjustments not recorded in the Hungarian, Czech, Slovak and Romanian statutory records of the respective group companies.

Basis of preparation

The consolidated financial statements are prepared in Hungarian Forint (HUF) and are presented in millions of Forints.

The consolidated financial statements are prepared under the historical cost convention. In connection with the transformation of the former state enterprise into the Company on July 31, 1991 the Company revaluated fixed assets and other non-current assets to their estimated market values at that date, based on independent valuations. These amounts became the accounting and tax bases reported in the Company's financial statements.

The accounting policies have been consistently applied by the Group enterprises and are consistent with those used in the previous year.

The financial statements were authorised for issue by the Board of Directors on March 12, 2004.

Use of estimates and assumptions

Preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions affecting the reported amounts of assets and liabilities, and of income and expenses in the reporting period. Actual results may differ from these estimates.

Basis of consolidation

SUBSIDIARIES

Subsidiaries are those enterprises controlled by the Company. Control exists when the Company has the power, directly or indirectly, to govern the financial and operating policies of an enterprise so as to obtain benefits from its activities. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The consolidated financial statements include the financial statements of the Company and its significant subsidiaries after elimination of all material inter-company transactions and balances, including any unrealised gains.

ASSOCIATES

Associates are those enterprises in which the Group has significant influence, but not control, over the financial and operating policies. The consolidated financial statements include the Group's share of the total recognised gains and losses of associates on an equity accounted basis, from the date that significant influence commences until the date that significant influence ceases. When the Group's share of losses exceeds the carrying amount of the associate, the carrying amount is reduced to nil and recognition of further losses is discontinued except to the extent that the Group has incurred obligations in respect of the associate.

INVESTMENTS

Investments in which the Company has less than 20% ownership are carried at cost, less provision for impairment.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

The Company's principal subsidiary companies at December 31, 2003 are as follows:

Name	Principal Activity	Country of Incorporation	Group interest held at December 31, 2003	Group interest held at December 31, 2002
Hungária Szálloda-Ingatlankezelő Rt.	Property management	Hungary	99.9%	99.9%
Danubius Szállodaüzemeltető és Szolgáltató Rt.	Hotel operator	Hungary	100%	100%
Léčebné Lázně a.s.	Hotel operator	Czech Republic	95.36%	95.36%
Gama 45 s.r.o	Hotel operator	Czech Republic	100%	100%
Slovenské Léčebné Kúpele Piestany a.s.	Hotel operator	Slovakia	84.55%	84.55%
Salina Invest SA	Holding company	Romania	56.43%	56.52%
SC Balneoclimaterica SA	Hotel operator	Romania	53.03%	53.11%

Foreign currency transactions

Transactions in foreign currency are translated into the local currency of operation at the rate of exchange prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies at the balance sheet date are translated into the local currency of operation at the year end rates of exchange. The resulting foreign currency exchange gains and losses are recognised in the statement of income.

Financial statements of foreign operations

The Group's foreign operations are not considered an integral part of the Company's operations. Accordingly, the assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on consolidation, are translated to HUF at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated to HUF at the average exchange rate for the year. Foreign exchange differences arising on translation are recognised directly in equity.

The measurement currency of the Romanian entities is USD and their local financial statements denominated in ROL are converted to USD applying standards applicable in hyperinflationary economies. Income and expenses of the Romanian entities are recorded at an average USD/ROL rate for the month, non-monetary assets and liabilities

are recorded at the initial translated cost, and monetary items are translated at the period-end USD/ROL rate. USD determined items are recorded in the exact USD amount. Any resulting foreign exchange gains and losses are recorded in the income statement. The financial statements denominated in USD are then translated to HUF as discussed above.

Property, plant and equipment

Items of property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses. The cost of self-constructed assets includes the cost of materials, direct labour and an appropriate proportion of production overheads.

DEPRECIATION

Fixed assets are stated at 1991 valuation or at cost, if acquired subsequently, less accumulated depreciation and less impairment losses. Depreciation is provided using the straight-line method. The depreciation rates used by the Group are from 2% to 5% for buildings and leasehold improvements and 14.5% to 33% for machinery and equipment. Land and capital projects in progress are not depreciated.

REFURBISHMENT

Significant refurbishment costs which increase the future economic benefits embodied in the item of property, plant and equipment are capitalised and depreciated in accordance with the policy described above.

LEASED ASSETS

Leases under which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Plant and equipment acquired by way of finance lease is stated at an amount equal to the lower of its fair value and the present value of the minimum lease payments at inception of the lease, less accumulated depreciation (see above) and impairment losses.

Intangible assets

GOODWILL

Goodwill arising on an acquisition represents the excess of the cost of the acquisition over the fair value of the net identifiable assets acquired. Goodwill is stated at cost less accumulated amortisation (see below) and impairment losses.

NEGATIVE GOODWILL

Negative goodwill arising on an acquisition represents the excess of the fair value of the net identifiable assets acquired over the cost of acquisition.

To the extent that negative goodwill relates to an expectation of future losses and expenses that are identified in the plan of acquisition and can be measured reliably, but which have not yet been recognised, it is recognised in the income statement when the future losses and expenses are recognised. Any remaining negative goodwill, but not exceeding the fair values of the non-monetary assets acquired, is recognised in the income statement over the weighted average useful life of those assets that are

depreciable/amortisable. Negative goodwill in excess of the fair values of the non-monetary assets acquired is recognised immediately in the income statement. The carrying amount of negative goodwill is deducted from the carrying amount of intangible assets.

AMORTISATION

Amortisation is charged to the income statement on a straight-line basis over the estimated useful lives of intangible assets. Goodwill is amortised from the date of initial recognition; other intangible assets are amortised from the date they are available for use. Goodwill is amortised on a straight-line basis over 20 years and negative goodwill is amortised over 20 and 30 years depending on the useful life of the underlying hotel asset.

OTHER INTANGIBLE ASSETS

Other intangible assets that are acquired by the Group are stated at cost less accumulated amortisation and impairment losses (see below). Where the Group has the legal right to use a particular property the value of these rights is amortised over the term for which the Group holds the rights, including property rights on Margaret Island, Budapest, which are being amortised over 100 years.

Debt securities

Debt securities are classified as held to maturity and are stated at amortised cost. Investments held to maturity are recognised/derecognised on the day they are transferred to/by the Group.

Inventory

Inventory is stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated selling expenses. The cost of inventory is determined on the weighted average cost basis and includes expenditure incurred in acquiring the inventory and bringing it to its existing location and condition.

Cash and cash equivalents

Cash equivalents are liquid investments with original maturities of three months or less.

Trade and other receivables

Trade and other receivables are stated at their cost less impairment losses (see below).

Impairment

The carrying amounts of the Group's assets, other than inventories and deferred tax assets, are reviewed at each balance sheet date to determine whether there is any indication of impairment. An impairment loss is recognised whenever the carrying amount of an asset exceeds its recoverable amount. Impairment losses are recognised in the income statement.

Provisions

A provision is recognised in the balance sheet when the Company has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation.

Trade and other payables

Trade and other payables are stated at their cost.

Interest-bearing loans

Interest-bearing loans are stated at their cost. The loans denominated in foreign currencies at the balance sheet date are translated into the local currency of operation at the year-end rates of exchange.

Revenue recognition*GOODS SOLD AND SERVICES RENDERED*

Room revenue (based on completed guest nights), food and beverage, spa revenue and other departmental revenue are each recognised as the service is provided, net of VAT.

RENTAL INCOME

Rental income from property is recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives granted are recognised as an integral part of the total rental income.

Operating lease payments

Payments made under operating leases are recognised in the income statement on a straight-line basis over the term of the lease. Lease incentives received are recognised in the income statement as an integral part of the total lease expense.

Interest Income

Interest income is recognised in the income statement as it accrues, taking into account the effective yield on the asset.

Income taxes

Income tax on the profit or loss for the year comprises current and deferred tax. Income tax is recognised in the income statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

Current tax is the expected tax payable on the taxable income for the year, using tax rates enacted, or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantially enacted at the balance sheet date.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

A deferred tax asset is recognised only to the extent that it is probable that future taxable profits will be available against which the asset can be utilised. Deferred tax assets are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Pension Plan

The Company operates a defined contribution pension plan for Hungarian employees. Pension costs are charged against profit in the period in which the contributions are payable. The assets of the fund are held in a separate trustee administered fund.

Fair value of financial instruments

The carrying values of financial instruments approximate fair values due to either the short-term duration or the proximity of interest rates of the various instruments to market rates.

Segment reporting

Group operations are presented in respect of geographical areas only. Management considers that it operates in a single business segment, hotel operations.

3 Cash and cash equivalents

	December 31,	
	2003	2002
Cash in hand and at bank	3,727	3,779
Marketable securities	41	46
	3,768	3,825

4 Accounts receivable

	December 31,	
	2003	2002
Trade receivables	1,851	1,837
Allowance for doubtful receivables	(384)	(247)
	1,467	1,590

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

5 Other receivables and prepayments

	December 31,	
	2003	2002
Receivables from non-consolidated subsidiaries	36	53
Prepayments and accrued income	696	539
VAT receivables	61	255
Other receivables	378	405
	1,171	1,252

Receivables from non-consolidated subsidiaries include a short-term loan of HUF 20 million provided to Marcali Szálloda Kft. (2002: HUF 45 million).

6 Inventory

	December 31,	
	2003	2002
Food and beverages	232	211
Materials	318	291
Goods for resale	16	25
	566	527

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

7 Property, plant and equipment

	Land	Buildings and improvements	Furniture, fittings and equipment	Capital projects in Progress	Total
Cost/Valuation:					
December 31, 2002	9,034	64,811	15,458	1,009	90,312
Effect of movements in exchange rates	426	1,483	675	42	2,626
Additions	24	2,548	1,018	–	3,590
Transfers	–	470	176	(646)	–
Disposals	(14)	(624)	(440)	–	(1,078)
December 31, 2003	9,470	68,688	16,887	405	95,450
Depreciation:					
December 31, 2002	–	17,981	10,883	–	28,864
Effect of movements in exchange rates	–	389	512	–	901
Depreciation charge for year	–	2,386	1,588	–	3,974
Disposals	–	(394)	(371)	–	(765)
December 31, 2003	–	20,362	12,612	–	32,974
Net book value:					
December 31, 2002	9,034	46,830	4,575	1,009	61,448
December 31, 2003	9,470	48,326	4,275	405	62,476

The net book value of property, plant and equipment pledged was HUF 28,266 million as at 31 December 2003. Further information about assets pledged as security for mortgages is given in note 12.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

8 Intangible assets

	Goodwill	Negative goodwill	Property usage rights	Software and other intangibles	Total
Cost					
December 31, 2002	733	(5,044)	538	1,122	(2,651)
Effect of movements in exchange rates	–	–	3	–	3
Additions	–	(51)	4	141	94
Disposals	–	–	(8)	(11)	(19)
December 31, 2003	733	(5,095)	537	1,252	(2,573)
Depreciation:					
December 31, 2002	95	(988)	60	738	(95)
Effect of movements in exchange rates	–	–	–	–	–
Amortisation charge for year	37	(228)	35	165	9
Relating to disposals	–	–	(6)	(10)	(16)
December 31, 2003	132	(1,216)	89	893	(102)
Net book value:					
December 31, 2002	638	(4,056)	478	384	(2,556)
December 31, 2003	601	(3,879)	448	359	(2,471)

At 31 December 2003 intangible assets include HUF 448 million, net of amortisation, (2002: HUF 478 million) for land usage rights relating to two hotels on Margaret Island held under licenses given by the Municipality of Budapest.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

Positive and negative goodwill relates to the following acquisitions:

	December 31,	
	2003	2002
Léčebné Lázně a.s.	733	733
Accumulated amortisation	(132)	(95)
Total positive goodwill	601	638
Hungar Hotels	2,993	2,993
Hotel Héla	154	154
Gama 45 s.r.o.	407	407
Slovenské Liečebné Kúpele Piestany a.s.	1,541	1,490
Accumulated amortisation	(1,216)	(988)
Total negative goodwill	3,879	4,056

9 Other non-current assets

	December 31,	
	2003	2002
Investments in non-consolidated subsidiaries	186	183
Investments in associates	31	–
Loans given to employees	8	28
Long-term receivable	75	–
Restricted cash	566	185
Other investments, unquoted	15	72
	881	468

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

The non-consolidated subsidiaries are:

Name	Principal activity	2003		2002	
			Share %		Share %
Marcali Szálloda Kft.	Hotel	121	50.2	121	50.2
Kastélykert Kft.	Hotel	43	100	43	100
Hungaria Hotel und Reisen GmbH.	Travel agency	9	100	9	100
Sopron Szakképző Iskola és Kollégium Alapítvány	College	5	100	5	100
Danubius Rendezvényszervező Kft.	Agency	3	100	–	–
Nádor Konferenciaközpont		3	100	3	100
Hotel Kastély Kft.	Hotel	2	50.0	2	50.0
		186		183	

The above subsidiaries are immaterial to the Group and have not been consolidated. Investments in associates represent a 32.75% share in Preventív Rt. at December 31, 2003, a company which provides security services to the Group in Hungary.

The long term receivable relates to proceeds from the sale of a hotel in Romania and is due in six instalments with the final instalment due on 1 October 2007. The long-term receivable is presented at discounted value.

As at 31 December 2003 other non-current assets includes HUF 566 million cash held on deposit for the finance of the reconstruction in Plestany and therefore its use is restricted to that purpose (see note 22).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

10 Provisions

	Acquisition of Piestany	Other	Total
Balance at 31 December 2002	621	235	856
Provision made during the year	–	85	85
Provision reversed during the year	–	(229)	(229)
Provision used during the year	(11)	–	(11)
Balance at 31 December 2003	610	91	701

In 2002 a provision for legal cases of HUF 621 million was provided at the acquisition of Piestany from which HUF 11 million was utilized in 2003 as a result of a lost legal case.

At December 31, 2003 other provisions comprise a provision of HUF 52 million for obligations related to termination and long service benefits agreed in 2003 for employees in Slovakia and HUF 39 million in respect of various legal cases.

In 2002 other provisions primarily included provisions for potential retrospective rental charges relating to properties rented by the Group from a District Municipality in Budapest. The provision was released in 2003 as an agreement has been reached with the municipality and the municipality has dropped its claims for additional rental payments.

11 Other payables and accruals

	December 31,	
	2003	2002
Payroll	543	539
Social security	324	300
Taxes payable	346	320
Accrued expenses	636	489
Other	185	9
	2,034	1,657

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

12 Long term debt

The Group's bank loans fall due for repayment, as follows:

	December 31,	
	2003	2002
Within 1 year	5,442	4,396
1 to 2 years	4,600	4,452
2 to 5 years	10,537	10,331
over 5 years	297	1,030
Total debt	20,876	20,209
Amounts due in less than one year	(5,442)	(4,396)
	15,434	15,813

Outstanding loans comprise the following:

	December 31,	
	2003	2002
Danubius Hotel and Spa Rt.		
1. MKB long term USD loan at interest rate of LIBOR +0.75%, secured by mortgages on the Budapest Hilton.	1,354	1,470
2. MKB long term Euro loan at interest rate of EURIBOR +0.75%, secured by mortgages on the Budapest Hilton.	1,325	1,197
3. K&H long term Euro loan, interest rate of EURIBOR +0.75%, secured by mortgages on the Hotel Radisson SAS Béke and Hotel Flamenco.	1,652	1,990
4. MKB long term Euro loan at interest rate of EURIBOR +0.75%, secured by mortgages on the Budapest Hilton and Hotel Budapest.	1,987	1,795
5. MKB long term Euro loan at interest rate of EURIBOR +0.75%, secured by mortgages on the Budapest Hilton and Grand Hotel Hungária.	1,295	1,171
6. MKB long term Euro loan at interest rate of EURIBOR +0.75%, secured by mortgages on the Thermal Hotel Sárvár.	1,943	1,756
7. MKB short term Euro loan at interest rate of EURIBOR +0.4%, secured by mortgages on the Thermal Hotel Sárvár.	–	1,218
8. MKB long term Euro loan at interest rate of EURIBOR +0.95%, secured by mortgages on the Thermal Hotel Sárvár	1,347	–
9. MKB long term Euro loan at interest rate of EURIBOR +0.95%, secured by mortgages on the Thermal Hotel Sárvár	1,295	–
Danubius Szállodaüzemeltető és Szolgáltató Rt.		
K&H Bank long term Euro loan, interest rate of LIBOR + 1.25% secured by mortgage on the Hotel Hélia.	–	299

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

	December 31,	
	2003	2002
Hungária Szálloda-Ingatlankezelő Rt.		
1. K&H long term Euro loan, interest rate of EURIBOR +0.75%, secured by mortgages on the Hotel Radisson SAS Béke and Hotel Flamenco.	1,749	2,254
2. K&H long term Euro loan, interest rate of EURIBOR +1.4%, secured by mortgages on the Hotel Radisson SAS Béke and Hotel Flamenco.	1,818	1,826
Léčebné Lázne a.s.		
1. Komerční Banka short term Euro loan at interest rate of EURIBOR +0.65%, secured by mortgages on buildings.	–	568
2. K&H and ČSOB long term Euro loan, interest rate of EURIBOR +1.4%, secured by mortgages on buildings and investment of HUF 6,464 million in Piestany.	3,639	3,297
Slovenské Liečebné Kúpele Piestany a.s.		
Short term bank loan in Slovak Crowns and Euro at interest rate of 5% and BRIBOR +1,25%, secured by mortgages on buildings.	828	1,327
Salina Invest SA		
Romanian Commercial Bank long term loan, 24% interest, guaranteed by a first rank mortgage on Sovata Hotel and bank accounts of Balneoclimaterica.	615	–
Other bank loans	29	41
Total debt	20,876	20,209

LIBOR was 2.39%, EURIBOR was 2.09% and BRIBOR was 6.06% at December 31, 2003. (LIBOR was 1.38%, EURIBOR was 2.90% and BRIBOR was 4.90% at December 31, 2002.)

13 Minority Interests

	December 31,	
	2003	2002
Hungária Szálloda-Ingatlankezelő Rt.	6	6
Preventív Rt.	–	72
Léčebné Lázne a.s.	406	406
Slovenské Liečebné Kúpele Piestany a.s.	1,335	1,348
Salina Invest SA and SC Balneoclimaterica SA	715	706
	2,462	2,538

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

	December 31,	
	2003	2002
Opening balance	2,538	399
Income attributable to minority shareholders	(94)	11
Deconsolidation of Preventív Rt.	(72)	–
Capital increase in subsidiary	90	–
Share in subsidiary sold to minority Shareholders	–	74
Minority share in subsidiaries acquired	–	2,054
	2,462	2,538

In 2003 Preventív Rt. ceases to be consolidated as the Group's interest in that company reduced to 32.75%.

14 Share Capital

	December 31,	
	2003	2002
Ordinary shares	8,285	8,285

Registered share capital at December 31, 2003 consists of 8,285,437 (2002: 8,285,437) authorised, issued and fully paid ordinary shares, each of par value HUF 1,000.

At December 31, 2003, the Company owned 374,523 of its own shares (Treasury shares) which cost HUF 1,162 million (2002: 374,523 shares, which cost HUF 1,574 million). The Hungarian Companies Act required Treasury shares to be sold within one year from the date of purchase. From 1 January 2004, there is no such requirement. The loss of HUF 412 million on treasury shares sold and subsequently repurchased in 2003 was recorded as a decrease in capital reserve (2002: gain of HUF 38 million).

15 Retained Earnings

Dividends are available for distribution from the Company's retained earnings calculated according to Hungarian Accounting Law. The amount available for distribution as dividends at December 31, 2003 is HUF 23,263 million (2002: HUF 23,843 million).

If dividends are paid to non-resident shareholders, a withholding tax of up to 20% must be paid. The rate payable is dependent on the country of residence of the shareholder. The withholding tax is also payable by individual shareholders who are resident in Hungary (resident legal entities are exempt).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

16 Other revenue

This comprises:

	2003	2002
Sale of Hotel Eger	–	749
Gain on sale of fixed assets	59	17
Proceeds from insurance	112	60
Other revenue	72	133
	243	959

In 2002 Danubius sold Hotel Eger, a Hungarian countryside hotel, realising a net gain of HUF 749 million.

17 Administrative and general expenses

	2003	2002
Payroll and related costs	4,557	4,303
Release of rental fee provision (see Note 10)	(229)	–
Utility costs	2,315	1,926
Maintenance expenses	1,436	1,117
Management fees to CP Holdings Limited (related party)	301	293
Fees to branded hotel chains (Hilton, Radisson SAS)	535	284
Marketing expenses	661	533
Bank and insurance fees	473	491
Commissions	53	60
Professional and membership fees	637	786
Telecommunication charges	212	183
Rental expense	190	289
Security costs	245	242
Miscellaneous expenses	1,600	828
	12,986	11,335

The group had 5,665 employees as at 31 December 2003 (5,977 as at 31 December 2002).

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

18 Other expenses

	2003	2002
Local taxes	695	558
Other taxes	687	1,005
Doubtful debt and other provisions	223	198
	1,605	1,761

19 Income Tax

The tax charge / (benefit) for the year comprises:

	2003	2002
Current tax	271	561
Deferred tax	(744)	373
	(473)	934

The deferred tax charge / (benefit) comprises:

	2003	2002
Origination and reversal of temporary differences	(225)	372
Reduction in tax rate	(213)	–
Benefit of tax losses recognized	(306)	1
	(744)	373

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

A reconciliation of the difference between the income tax expense and taxation at the statutory tax rate, is shown in the following table:

	2003	2002
Profit / (loss) before tax and minority interest	(126)	3,850
Hungarian Statutory tax rate (%)	18	18
Theoretical tax	–	693
Changes in tax burden as a result of:		
Differences in tax rates		
Czech subsidiaries	30	–
Slovak subsidiary	15	–
Romanian subsidiaries	–	(10)
Net effect of deferred tax		
Czech subsidiaries	12	160
Slovak subsidiary	(98)	(33)
Romanian subsidiaries	(98)	–
Hungarian operations	(560)	246
Current tax payable on the profit of Property management company	188	–
Other differences	38	(122)
Income tax expense / (benefit)	(473)	934

HUNGARIAN OPERATIONS

The corporate income tax rate in Hungary was 18% for 2003 and 2002 and will decrease to 16% starting from 2004. The current tax expense was HUF 188 million (2002: HUF 498 million).

The Hungarian deferred tax reconciling items comprise:

	2003	2002
Valuation of the foreign currency loan	(261)	143
Tax losses	(330)	–
Tax benefit for capital expenditure	(14)	103
Different depreciation rates	45	–
	(560)	246

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

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In 2003 a deferred tax liability of HUF 261 million was released due to the reversal of a temporary difference which arose on the year end valuation of foreign currency loans. In the statutory accounts the foreign currency gain was accrued in accordance with Hungarian Accounting Law, whereas the gain was recorded in the income statement for IFRS reporting.

In certain companies of the group there are tax losses which will expire in 2006, 2007 and 2008. Deferred tax assets of HUF 330 million have been recognised in respect of these items in 2003 in the Hungarian companies because it is probable that future taxable profit will be available against which these companies can utilise the benefits therefrom.

A deferred tax liability of HUF 103 million was provided in 2002 for a temporary difference arising on capital expenditure for 2003, for which a tax benefit has been claimed in advance for 2002 in compliance with Hungarian Tax Law. The deferred tax liability decreased by HUF 14 million in 2003 due to the amortisation of the assets and the recalculation of the liability using the 16% tax rate.

An additional deferred tax liability of HUF 45 million was provided in 2003 for different depreciation rates applied on buildings for tax calculation (5%) and for IFRS reporting (3.5%, 4%, 5%) purposes (2002: nil.).

CZECH SUBSIDIARIES

The corporate income tax rate in the Czech Republic was 31% for 2003 and 2002 and will decrease to 25% for 2004. The current tax expense of Léčebné Lázně a.s. was nil in 2003 (2002: nil). No current tax expense was borne by Gama 45 s.r.o as it utilised all remaining tax loss carry-forwards. The deferred tax expense of HUF 12 million (2002: HUF 160 million) is attributable to HUF 85 million movements in temporary differences during the year of the Czech subsidiaries partially offset by the HUF 73 million decrease of deferred tax liability due to the decrease of corporate income tax rate to 25%.

SLOVAK SUBSIDIARY

The corporate income tax rate in the Slovakian Republic was 25% for 2003 and 2002 and will decrease to 19% for 2004. The current tax expense of Piestany was HUF 83 million in 2003 (HUF 53 million in 2002). The deferred tax benefit of HUF 98 million is attributable to the HUF 138 million decrease of deferred tax due to the recalculation of the balance using the 19% rate partially offset by movements in temporary differences during the year.

ROMANIAN SUBSIDIARY

The corporate income tax rate in the Romania for 2003 was 25% (2002: 25%). The total current tax expense was nil for Salina Invest SA (2002: HUF 10 million) and for SC Balneoclimaterica SA (2002: nil). The deferred tax benefit of HUF 98 million (2002: nil) is mainly attributable to the movements in temporary differences during the year of the Romanian subsidiaries.

Current Corporate income tax receivables and liabilities

Corporate taxes receivable include corporate income tax overpayments of HUF 439 million in Hungary and the foreign subsidiaries (2002: HUF 594 million) as a result of advance payments required by the tax authorities based on the actual income tax paid for 2002.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

Corporate tax payables of HUF 44 million (2002: HUF 19 million) include income tax of Slovenské Liečebné Kúpele Piestany a.s. calculated as a net balance of tax charged based on the profit for 2003 less advances paid during the year.

Deferred tax assets and liabilities

Deferred tax assets and liabilities as at 31 December 2003 and 31 December 2002 are attributable to the following:

	Assets		Liabilities	
	2003	2002	2003	2002
Subsidiaries				
Property, plant and equipment	60	44	149	241
Fair value adjustment on properties:				
Léčebné Lázně a.s.	–	–	658	752
Piestany	–	–	423	575
Repairs and maintenance provision	–	–	543	432
Tax value of loss carry-forwards	160	24	–	–
Legal provisions	116	155	–	–
Other items	60	48	28	37
	396	271	1,801	2,037
The Company				
Capital expenditure benefit	–	–	89	103
Exchange gain on loans	–	–	–	261
Tax value of loss carry-forwards	170	–	–	–
Other	–	–	45	–
	566	271	1,935	2,401
Offset of assets and liabilities	(134)	–	(134)	–
	432	271	1,801	2,401

A fair value adjustment is made to the fixed assets (primarily land and hotel buildings) of Léčebné Lázně a.s., to reflect the difference between the historical cost of these assets recorded in the Czech statutory accounts and their value at acquisition by the Group. The deferred tax liability is related to this fair value adjustment (28% in 2003 and 31% in 2002 on the revaluation surplus).

A fair value adjustment is made to the fixed assets (primarily land and hotel buildings) of Piestany, to reflect the difference between the historical cost of these assets recorded in

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

the Slovak statutory accounts and their value at acquisition by the Group. The deferred tax liability is related to this fair value adjustment (25% in 2003 and 19% in 2002 on the revaluation surplus).

Léčebné Lázně a.s. records a provision for repairs and maintenance in its Czech statutory accounts related to the future repair expenses of its premises, in accordance with Czech accounting and tax legislation. This provision is reversed in these IFRS financial statements and a deferred tax liability is set up for this timing difference.

20 Earnings per share

The calculation of basic earnings per share is based on the net profit attributable to ordinary shareholders of HUF 441 million in 2003 (2002: HUF 2,905 million) and the weighted average number of ordinary shares outstanding during 2003 of 7,910,914 (2002: 7,910,914).

	December 31,	
	2003	2002
Weighted average number of issued ordinary shares	8,285,437	8,285,437
Weighted average number of treasury shares	(374,523)	(374,523)
Weighted average number of qualifying ordinary shares	7,910,914	7,910,914
Net profit for the year in million HUF	441	2,905
Earnings per share (HUF/share)	56	367

There are no dilutive factors to earnings per share disclosed above.

21 Operating leases

Leases as lessee

Non-cancellable operating lease rentals are payable as follows:

	December 31,	
	2003	2002
Less than one year	125	125
Between one and five years	–	125
	125	250

The Group leases its head office building under an operating lease. The lease runs for an initial period of three years, with an option to renew the lease in 2004. Lease payments are adjusted annually.

The Group did not hold any assets under finance leases at 31 December 2003 (2002: nil)
Leases as lessor

The group has no significant non-cancellable operating lease rental receivables as at 31 December 2003.

22 Commitments at December 31, 2003

The Group plans to spend approximately HUF 3 billion on hotel refurbishment and construction in 2004.

At the acquisition of Piestany, the Group committed to a SKK 700 million (HUF 4,459 million) reconstruction program on hotel buildings by 2006.

In 2001 Danubius was granted the right to a subsidy of HUF 500 million from the Hungarian Government for the reconstruction of Hotel Nádor in Pécs. The amount will be paid to Danubius in line with the progress of the hotel reconstruction which was estimated to cost HUF 2.6 billion. Danubius has an obligation to renew the façade and the garage of Hotel Nádor in 2004 for an estimated cost of approximately HUF 250 million. No decision has been made yet about when the remaining reconstruction work will commence.

23 Contingent Liabilities

The Group did not have any significant contingent liabilities as at 31 December 2003.

24 Pension Plans

The Group's employees participate in State pension plans to which employers and employees pay contributions. The pension liability resides with the State in Hungary, Czech Republic, Slovakia and Romania.

Danubius has a pension plan in addition to the State plan, which is available for all Hungarian employees after six months employment. The contribution expense was HUF 220 million (2002: HUF 206 million). The Group pays contributions equal to 5% of the salary of employees who are members of the fund. The assets of the fund are held in separate trustee administered funds and are not included in these financial statements.

There are no pension plans for the Czech, Slovak and Romanian subsidiaries.

25 Acquisition of subsidiaries in 2002

The group acquired two subsidiaries in Slovakia and Romania during 2002. The assets, liabilities and costs of acquisition were as follows:

(1) Slovenské Liečebné Kúpele Piestany a.s.

Effect on the consolidated financial statements:

Balance sheet at acquisition	
Intangible assets	34
Fixed assets	10,803
Fair value adjustment to fixed assets	2,341
Deferred tax liability on fair value adjustment	(585)
Net deferred tax asset	261
Current assets, including cash	906
Loans	(1,381)
Other short term liabilities	(816)
Legal Provision	(621)
Net assets	10,942
Danubius Group share of net assets (87.12%)	9,533
Less: Purchase consideration for cash	7,663
Acquisition costs	380
Negative Goodwill	1,490

Piestany has been consolidated since June 1, 2002 and the consolidated financial statements include seven months operations for 2002. The acquisition resulted in a negative goodwill of HUF 1,490 million which is being amortised over thirty years on the straight-line basis reflecting the amortisation period of the hotel properties.

In the 7 months to 31 December 2002 the subsidiary contributed net loss of HUF 17 million to the consolidated profit for 2002.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

(2) Salina Invest SA

Balance sheet at acquisition	
Fixed assets	1,837
Negative goodwill at subsidiary level	(1,077)
Current assets, including cash	1,104
Net deferred tax liability	(252)
Other short term liabilities	(66)
Minority interest	(158)
Net assets	1,388
Danubius Group share of net assets of Salina SA (56.52%)	784
Less: Purchase consideration, including HUF 130 million investment in 2001	1,114
Goodwill at group level	(330)
Goodwill	–

Salina Invest SA and Balneoclimaterica SA have been consolidated from October 1, 2002. In the 3 months to 31 December 2002 the subsidiary contributed net loss of HUF 33 million to the consolidated profit for 2002.

26 Related Party Transactions

Transactions with related parties are summarised as follows:

	2003	2002
Management fee to CP Holdings	301	293
Rental fee to Interag Rt.	146	116
Services provided by Interag Rt.	5	37
Service provided to Interag Rt.	(1)	(1)
Service provided by Investor Rt.	13	13
Service provided to Investor Rt.	(3)	(4)
Service provided by Preventiv Security Rt.	242	–

Related party receivables and payables are not significant as at December 31, 2003. Interag Rt., Investor Rt. and Preventív Security Rt. are each subsidiary companies of CP Holdings.

The Group considers the pricing of all transaction with related parties to be at arm's length.

27 Financial instruments

The Group has financial assets, which include cash and cash equivalents, investments in state treasury bills and accounts receivable. The Group has financial liabilities which include, inter alia, bank loans, suppliers and accounts payable. The fair values of these financial instruments are not materially different from their stated value.

CURRENCY RISK

The Group's sales prices are primarily quoted in Euro or US dollars and income is received in foreign currency or local currency.

The Group had loans of USD 6.6 million (2002: USD 6.6 million), EURO 72.1 million (2002: EURO 81 million), SKK 27.4 million (2002: nil) and ROL 90,000 million (2002: nil) outstanding at 31 December 2003 (see note 12).

Management periodically reviews the merits of entering into foreign currency hedging contracts or other derivative products, but has not entered into any such contracts.

INTEREST RATE RISK

Interest rates on loans are listed in note (see note 12).

Management has not entered into any interest rate hedging contract as management believes the contracted interest rates are favourable for the Company.

CREDIT RISK

Financial assets which may be subject to credit risk consist of short term investments, cash at bank and trade receivables. Short term investments are government securities, cash is held at reputable banks and the allowance for doubtful receivables reflects credit risk on trade receivables. The Company has no significant concentrations of credit risk.

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

28 Segment reporting

Geographical segments

December 31, 2003

	Operations in Hungary	Operations in Czech Republic	Operations in Slovakia	Operations in Romania	Elimination	Consolidated
Revenue	24,463	5,388	6,701	335	–	36,887
Inter-segment revenue	426	–	–	–	(426)	–
Total revenue	24,889	5,388	6,701	335	(426)	36,887
Profit/(loss) per segment	3	505	60	(127)	–	441
Cost to acquire fixed assets	1,614	394	351	1,325	–	3,684
Depreciation and amortisation	2,599	550	704	130	–	3,983
Current assets	5,934	1,008	653	253	(437)	7,411
Non-current assets	49,315	13,982	14,090	1,740	(17,809)	61,318
Current liabilities	6,367	1,389	2,319	510	(437)	10,148
Non-current liabilities	12,009	7,010	–	657	(2,441)	17,235
Minority interest	8	404	1,335	715	–	2,462
Net assets	36,865	6,187	11,089	111	(15,368)	38,884

NOTES TO THE CONSOLIDATED FINANCIAL STATEMENTS

All amounts in million HUF

December 31, 2002

	Operations in Hungary	Operations in Czech Republic	Operations in Slovakia	Operations in Romania	Elimination	Consolidated
Revenue	26,133	5,678	3,857	72	–	35,740
Inter-segment revenue	516	–	–	–	(516)	–
Total revenue	26,649	5,678	3,857	72	(516)	35,740
Profit/(loss) per segment	2,485	470	(17)	(33)	–	2,905
Current assets	5,465	1,156	896	824	(553)	7,788
Non-current assets	48,640	13,534	13,210	1,132	(16,885)	59,631
Current liabilities	5,712	1,210	2,685	145	(372)	9,380
Non-current liabilities	13,061	7,695	158	231	(2,931)	18,214
Minority interest	78	406	1,348	706	–	2,538
Net assets	35,254	5,379	9,915	874	(14,135)	37,287

Eliminations principally comprise the equity consolidation and inter group loans. Inter-segment pricing is determined on an arm's length basis.

Business segments

Management considers hotel operations as the only business segment, therefore all amounts included in the financial statements are part of that segment.

29 Subsequent events

As of January 1, 2004 VAT on room revenue was increased by 3% in Hungary which will decrease room revenues by approximately HUF 600 million. This unfavourable change will be partly offset by the decrease in VAT and income tax at the foreign subsidiaries.

RECONCILIATION OF THE PROFIT ACCORDING
TO THE HUNGARIAN ACCOUNTING STANDARDS
TO THE PROFIT ACCORDING
TO THE INTERNATIONAL FINANCIAL
REPORTING STANDARDS

in million HUF

	Changes in income	
	+	-
Profit after tax according to the HAS	831	
Exchange loss on loans		1 450
Difference in negative goodwill depreciation	244	
Difference in positive goodwill depreciation		192
Exchange difference of foreign subsidiaries' revaluation	144	
Deferred tax	744	
Other minor items	26	
Profit for the year according to the IFRS	347	

CONSOLIDATED STATEMENT OF INCOME

(ACCORDING TO HUNGARIAN ACCOUNTING STANDARDS)

HUF 000

			index	Distribution of revenue %	
	2002	2003		2002	2003
Net domestic revenue	35,209,684	38,048,149	108.1%	100.0%	100.0%
Capitalized value of own performance	165	9	5.5%		
Other revenues	833,373	450,356	54.0%	2.4%	1.2%
From this: re-booked loss in value of assets	21,375	12,134	56.8%	0.1%	
Raw material costs	6,005,049	7,018,039	116.9%	17.1%	18.4%
Value of services used	7,293,857	8,447,099	115.8%	20.7%	22.2%
Value of other services	993,590	924,266	93.0%	2.8%	2.4%
Purchase price of goods sold	117,202	218,282	186.2%	0.3%	0.6%
Value of services sold	1,204,005	592,375	49.2%	3.4%	1.6%
Material-type expenditures	15,613,703	17,200,061	110.2%	44.3%	45.2%
Salaries and wages	8,755,921	9,614,766	109.8%	24.9%	25.3%
Other payments to personnel	932,920	885,636	94.9%	2.6%	2.3%
Contribution to salaries and wages	3,243,401	3,419,721	105.4%	9.2%	9.0%
Total payroll and related costs	12,932,242	13,920,123	107.6%	36.7%	36.6%
Depreciation	3,437,825	3,958,338	115.1%	9.8%	10.4%
Other expenditures	1,311,750	1,266,223	96.5%	3.7%	3.3%
From this: loss in value of assets	27,876	21,518	77.2%	0.1%	0.1%
Operating profit	2,747,702	2,153,769	78.4%	7.8%	5.7%
Dividend and profit sharing received	2,131	6,813	319.7%		
Exchange gain on sale of shares	652,732			1.9%	
From this: mother – daughter					
Interest, exchange gain of financial investments	34,371			0.1%	
From this: mother – daughter					
Other interests received	147,831	106,541	72.1%	0.4%	0.3%
From this: mother – daughter	5,625				
Other financial income	966,393	1,435,006	148.5%	2.7%	3.8%
Revenues from financial activities	1,803,458	1,548,360	85.9%	5.1%	4.1%
Exchange loss of financial investments	3,261				
From this: mother – daughter					
Interests payable	785,631	763,968	97.2%	2.2%	2.0%
From this: mother – daughter	302				
Loss of value of shares, securities and bank deposits					
Other financial expenditures	780,891	1,651,421	211.5%	2.2%	4.3%
Expenditures from financial activities	1,569,783	2,415,389	153.9%	4.5%	6.3%
Financial profit or loss	233,675	-867,029		0.7%	
Profit from ordinary activities	2,981,377	1,286,740	43.2%	8.5%	3.4%
Extraordinary revenues	253,206	6,096	2.4%	0.7%	
Extraordinary expenditures	355,456	231,560	65.1%	1.0%	0.6%
Extraordinary profit or loss	-102,250	-225,464			
Profit before tax	2,879,127	1,061,276	36.9%	8.2%	2.8%
Corporate tax payable	583,145	230,070	39.5%	1.7%	0.6%
Profit after tax	2,295,982	831,206	36.2%	6.5%	2.2%
Dividend payable	140				
Use of profit reserve for dividends		44,683			
Minority interests	-13,796	-75,347			
Net profit as per balance sheet	2,309,638	951,236	41.2%	6.6%	2.5%

CONSOLIDATED BALANCE SHEET

(ACCORDING TO HUNGARIAN ACCOUNTING STANDARDS)

ASSETS	Title	2003		HUF 000
		1 January	31 December	
	Invested assets	62,704,434	63,022,418	
	Intangible assets	548,734	486,151	
	Capitalized value of transformation			
	Capitalized value of research and development			
	Intangible assets	40,156	21,530	
	Intellectual products	408,212	403,971	
	Goodwill			
	Advanced payment for intangible assets	100,366	60,650	
	Revaluation of intangible assets			
	Tangible assets	61,859,788	62,200,190	
	Real estates and related intangible assets	55,914,364	57,117,954	
	Technical equipment, machinery and vehicles	3,799,922	3,241,973	
	Other equipment, fittings and vehicles	978,953	805,788	
	Breeding stock			
	Capital projects	1,164,734	1,019,774	
	Advanced payments for capital projects	1,815	14,701	
	Revaluation of tangible assets			
	Financial investments	295,912	336,077	
	Long-term shares in daughter companies	251,603	220,671	
	Long-term loans to daughter companies			
	Other long-term investments	15,550	15,550	
	Long-term loans given to other investments			
	Other long-term loans	28,759	99,856	
	Long-term securities			
	Revaluation of financial investments			
	Working assets	8,946,421	8,591,600	
	Stocks	526,892	566,818	
	Raw materials	462,235	508,641	
	Work in process, intermediate and semi-finished products			
	Livestock	60		
	Finished goods			
	Goods	64,597	57,482	
	Advance payments for stocks		695	
	Receivables	2,869,980	2,504,831	
	Debtors	1,681,929	1,596,396	
	Receivables from daughter companies	54,502	61,924	
	Receivables from other investments	12,848	12,848	
	Bills of exchange			
	Other receivables	1,120,701	833,663	
	Securities	1,602,077	1,255,401	
	Shares in daughter companies			
	Other investments			
	Treasury shares	1,572,996	1,214,223	
	Short-term securities	29,081	41,178	
	Total cash and bank	3,947,472	4,264,550	
	Cash at hand and cheques	187,950	141,160	
	Bank deposits	3,759,522	4,123,390	
	Accruals	701,154	683,110	
	Accruals of revenues	449,615	420,839	
	Accruals of costs and expenditures	251,539	262,271	
	Deferred expenses			
	TOTAL ASSETS	72,352,009	72,297,128	

CONSOLIDATED BALANCE SHEET

HUF 000		LIABILITIES		
		2003		Title
1 January	31 December			
40,228,539	41,055,508			Own capital
8,285,437	8,285,437			Subscribed capital
374,523	374,523			From this: par value of repurchased shares
				Not yet paid subscribed capital
7,138,139	7,138,139			Capital reserve
15,039,629	17,186,840			Profit reserve
1,642,996	1,161,021			Tied-up reserve
				Revaluation reserve
2,309,638	951,236			Profit per balance sheet
3,343,185	4,067,557			Change in subsidiaries' capital
2,469,515	2,265,278			Profit sharing of externalities
856,009	741,769			Provisions
850,318	741,769			Provisions for possible liabilities
				Provisions for possible losses
5,691				Other provisions
28,962,904	30,008,655			Liabilities
5,523,500	5,523,500			Subordinated liabilities
				Subordinated liabilities to daughter companies
				Subordinated liabilities to other investments
				Other subordinated liabilities
5,523,500	5,523,500			Capital consolidation difference from subsidiaries
15,767,314	15,839,395			Long-term liabilities
18,000	9,000			Long-term loans
				Convertible bonds
				Liabilities from bond issue
4,219,983	3,906,444			Project loans
11,525,261	11,913,827			Other long-term loans
				Long-term liabilities to daughter companies
				Long-term liabilities to other investments
4,070	10,124			Other long-term liabilities
7,672,090	8,645,760			Short-term liabilities
15,667	9,000			Short-term credits
				From this: convertible bonds
4,425,464	5,028,311			Short-term loans
164,774	216,736			Advance payments from debtors
1,576,691	1,556,658			Creditors
				Bills of exchange
286	145			Short-term liabilities to daughter companies
				Short-term liabilities to other investments
1,489,208	1,834,910			Other short-term liabilities
2,304,557	491,196			Accruals
206,712	141,971			Accruals of revenues
648,672	342,230			Accruals of costs and expenditures
1,449,173	6,995			Deferred revenues
72,352,009	72,297,128			TOTAL LIABILITIES

REPORT OF THE SUPERVISORY BOARD

The Supervisory Board observed precisely the regulations set by the Company Act and the Articles of Association as well as the internal Rules of Procedure approved by the last Annual General Meeting. Since the last report the Supervisory Board held 5 meetings and 1 extraordinary meeting attended regularly by the chairmen of the Supervisory Boards of Danubius Szállodaüzemeltető és Szolgáltató Rt. (Danubius Management Co.) and Hungária Szálloda-Ingatlankezelő Rt. (Hungária Property Co.). Pending on the subject, the three supervisory boards held several joint meetings as well. The Supervisory Board pursued its activities according to the approved work schedule and always had a quorum. The chairman of the Supervisory Board participated regularly at the meetings of the Board of Directors of the company.

Managers of the company concerned with the items of the agenda were invited to the meetings of the board at all times where they complemented verbally their reports submitted in writing, gave answers to the questions and expressed their opinions on the comments. Four times, the quarterly flash reports, prepared for the stock exchange, constituted the key topic of the talks covering the financial situation of the Company, the business activities and the state of the business plan and the expected performance as well as the general outlook for tourism. In addition, according to the approved work schedule, the Supervisory Board discussed the following issues during 2003:

- Review of human policy issues, the situation with young replacements, vocational training.
- Marketing and sales activities, experience of the regional restructuring,
- Capital expenditure and reconstruction issues.

On every occasion, the Supervisory Board received an account on current matters from the leader of the internal auditors.

Summarising the resolutions passed at the meetings the Supervisory Board concluded that

- The Rt. has pursued its activities by fully observing the prevailing acts and legal provisions,
- The financial obligations were entirely met in line with the plan,
- The capital expenditure and reconstruction projects were implemented –taking into account the possibilities given by economic situation and the trend of the competitors– according to a proper schedule.

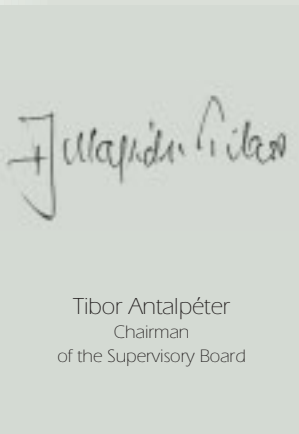
Considering all the above, the Supervisory Board proposes to the AGM that the financial balance of the company be approved.

The Supervisory Board has discussed the company's 2003 annual report at its meeting held on 21 April 2004 and in view of the auditor's report proposes that they be approved by the AGM with total assets of HUF 45.258.168 thousand and as per balance sheet profit of HUF – 1.062.795 thousand and profit after tax of HUF – 1.062.795 thousand.

Having read the auditor's report the Supervisory Board proposes that the consolidated statement of Danubius Rt. be approved showing total assets at HUF 72.297.128 thousand and HUF 831.206 thousand profit after tax as well as HUF 951.236 thousand B/S profit.

The Supervisory Board supports the Board of Director's proposal that regarding the unfavourable market conditions no dividend payment should burden the 2003 profit after tax this year.

Budapest, 21 April 2004



THE SUPERVISORY BOARD



Tibor Antalpéter

Chairman of the Supervisory Board from
18 October 2002
Ambassador of the Republic of Hungary to
London from 1990 to 1995.



Dr. Gábor Boér

Deputy Chief Executive Officer of Investor
Holding Rt. since 1990,
Chief Executive Officer of
Interag Holding Rt. since 1997.



Dr. Ákos Horvátth

Associate Professor at the Department of
Tourism at the Collage of Commerce,
Catering and Tourism.



Mrs. Erzsébet Surányi

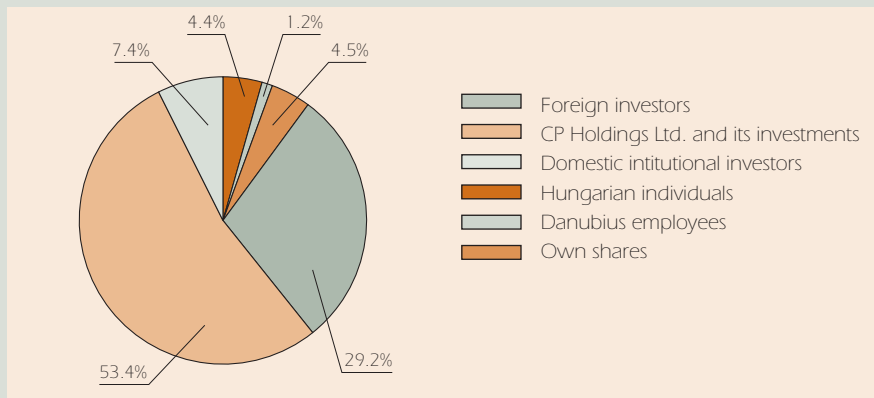
Worked in the Ministry of Finance from 1967
to 2000; currently Senior Counsellor
in Administration and Tax Advisor.

DANUBIUS SHARES ON THE BUDAPEST STOCK EXCHANGE IN 2003

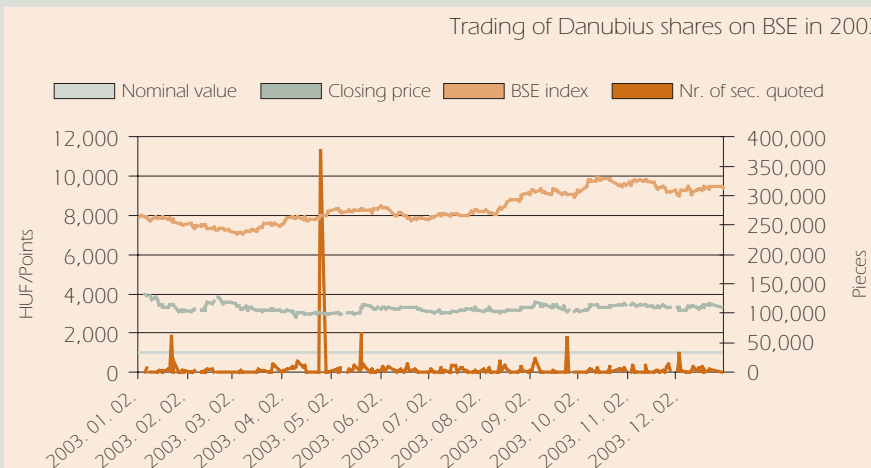
T trading on the Budapest Stock Exchange

	2002	2003
Number of trading days	244	250
Number of deals	4,246	4,256
Number of securities traded	1,475,634	1,356,439
Value of securities traded (HUF million)	5,658.7	4,339.7
Average price (HUF)	3,835	3,199
Minimum price (HUF)	3,060	2,880
Maximum price (HUF)	4,545	4,000
Closing price (HUF)	4,000	3,305

Shareholders' structure on 31st December 2003



Trading of Danubius shares on BSE in 2003



BUSINESS TARGETS 2004

Danubius Hotels Rt. plans HUF 38.9 billion revenue, HUF 3.6 billion operating profit and HUF 2.7 billion profit before tax for 2004. At the time of the preparation of the budget HUF 265 EUR rate was used, therefore we do not count on any revaluation difference on the loans.

When setting our targets we trust that further success of the international efforts will prevent terrorist acts, safe travel conditions will develop, diseases will be located and controlled and the economic results seen at the end of the year will continue to be improving on our key markets.

The majority of the planned increase in revenues arises from the 4-5% occupancy growth expected at company level that will result in 63% average occupancy at group level. Assuming that despite further increase of the Hungarian hotel capacity this year, the decreasing trend in the domestic hotels experienced in the last couple of years will come to a stop and in 2004 we will manage to surpass the previous year – despite unfortunately significantly increasing spa capacities and beside maintaining the average good occupancy of the Danubius spa hotels – by a better sale of city hotels. According to the forecasts, we reckon with an increasing interest from overseas countries and European states other than the traditional partners. The budget flights of the new airlines will be to our help in this respect. In addition, we still reckon with a strengthening domestic demand. Our action plan for 2004 approved by the Board of Directors also supports these endeavours.

The performance of our foreign subsidiaries must enhance growth as well, on the one hand by the whole year operation of our Hotel Sovata in Romania and on the other hand by the 1-2% higher occupancy of the Czech and Slovak hotels than the previous year as a result of improving German market conditions.

From another aspect, the planned revenue increase is based on the improvement of average rates/average spending. In case of our domestic hotels there are a lot of reserves in the average rates of our city hotels, which we hope to exploit by the probable growth in business guests before and after the accession to the EU. A further possibility arises in the increasing number of related events prompting additional revenues. We expect a favourable turn in leisure tourism as well that could stop last year's decrease in average rates in 2004. As a result of reconstruction works carried out in our foreign hotels in the course of 2003, a reasonable increase of average rates can be expected primarily in the Romanian and Slovakian hotels.

We have budgeted our costs based on 6.5% inflation rate and the increase of wage costs are in line with this. The VAT rates modified as a result of the Hungarian, Czech and Slovakian government measures have the most negative effect on the Hungarian hotels and particularly since these were taken at the end of the year and could not be realised in the contracts concluded earlier.

We are continuously investigating how to exploit possibilities emerging in spa tourism. We are not only analysing the quality and the range of services but also how to win more guests and from which territories. We are looking to establish sales representations abroad in areas where the Hungarian presence is not strong enough, nevertheless, based on our analysis, interest is shown for our services. On the domestic market the establishment of Health Funds in Hungary could be promising.

BUSINESS TARGETS 2004

A management agreement signed for the operation of a new hotel to be opened in 2004 will also increase revenues.

Our personnel management continues to be determined by the prevailing strict head count stop. We still apply outsourcing in certain areas to ensure efficient management of basic work time and the modification of contracts for the variable work area enables us to shift labour force between units and to increase efficiency.

In addition to the planned HUF 4.5 billion reconstruction costs one significant domestic item serving technical quality improvement needs mentioning. Air conditioning of 6 units will be carried out in the framework of a special rental contract concluded for four years, which will help getting closer in quality to the new hotels opened in the past two-three years. We continue the modernisation of the Czech hotels and the up-grading of the operating three-star hotels to four-star ones. Our EUR 12 million plans include the complete reconstruction of a Slovakian hotel by which we live up to our obligations set in the privatisation agreement not later than 31 December 2006. In Romania we carry on improving the quality of the Sovata units by the small reconstruction of Hotel Bradet. Our company shall continue to do everything in its power to secure and increase the value of shareholders' assets. They are regularly informed about the performance of the company from the quarterly issued flash reports and they can find every detailed financial report on the web page www.danubiusgroup.com as well as information about the services of the company.

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nyomtatás a csomagolásig...



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