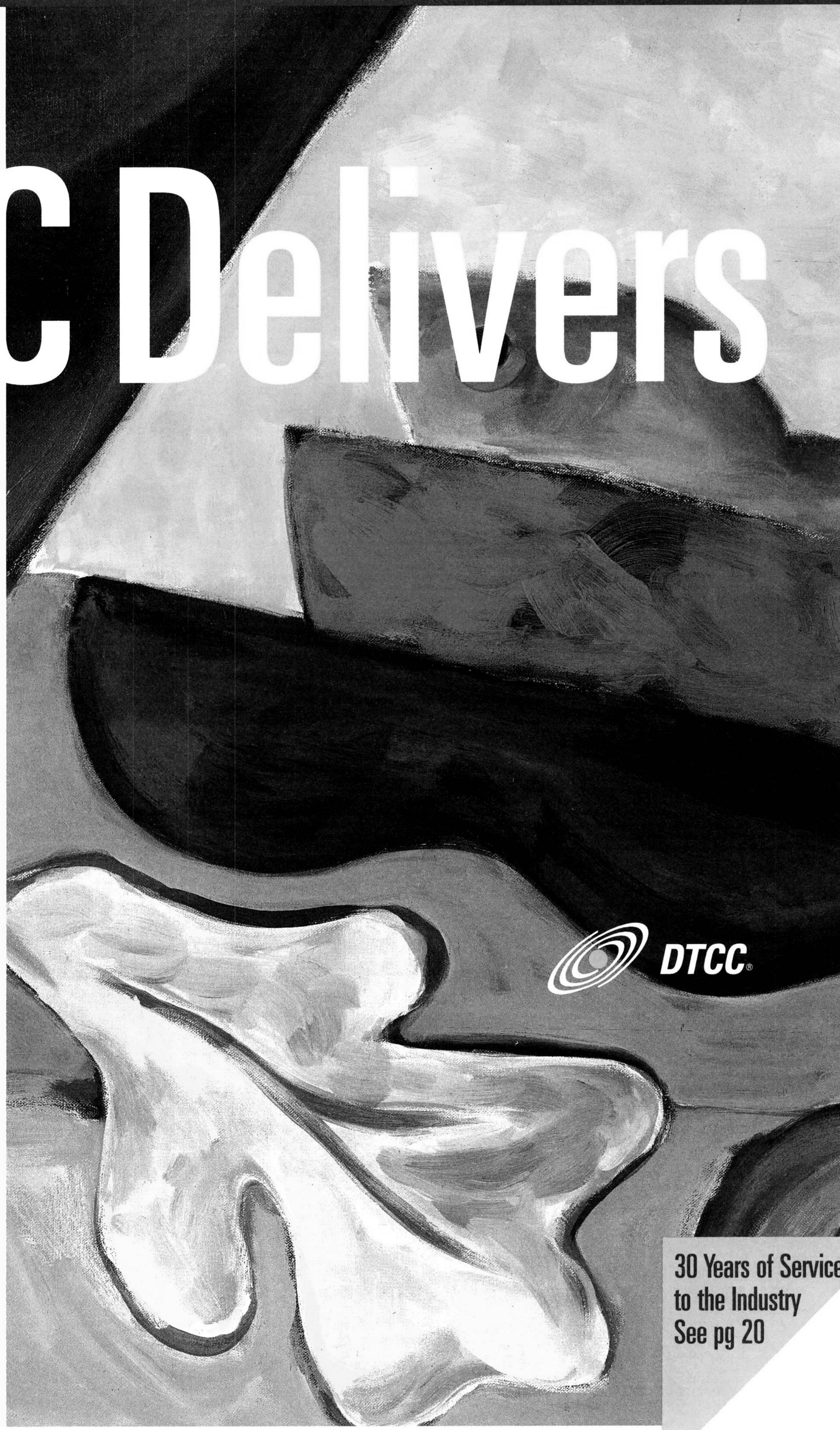
2002 ANNUAL REVIEW

DTCC Delivers



DTCC®

30 Years of Service to the Industry
See pg 20

Our purpose

is to help grow the world economy by furthering the development of low-cost, efficient capital.

Our mission

is, by 2005, to be the provider of choice worldwide for investment servicing solutions through leadership, innovation and technology.

Our values

provide the moral compass by which we operate, binding us together and underscoring our approach to business for all DTCC employees. They include integrity and trust, quality and excellence, customer focus, employee focus and respect, innovation and teamwork.

The Depository Trust & Clearing Corporation (DTCC) is a holding company for four subsidiary businesses – a depository and three clearing corporations – as well as the co-owner with Thomson Financial of Omgeo, a global joint venture. Through its subsidiaries, DTCC provides clearance, settlement and information services for equities, corporate debt, municipal debt, government securities, mortgage-backed securities and emerging markets debt. In addition, it is a leading clearinghouse for mutual funds and insurance products, linking funds and carriers with their distribution networks. DTCC has operating facilities in multiple locations in the United States and overseas.

Subsidiaries:

The Depository Trust Company (DTC) is a securities depository, providing custody and asset servicing for more than two million securities issues from the United States and more than 100 other countries and territories.

National Securities Clearing Corporation (NSCC) is a central counterparty and leading provider of centralized post-trade comparison, trade guarantee, netting, settlement and information services for equities, bonds, unit investment trusts, mutual funds and insurance transactions.

Fixed Income Clearing Corporation (FICC), created by the merger of Government Securities Clearing Corporation (GSCC) and MBS Clearing Corporation (MBSCC), began operations on January 1, 2003. FICC provides automated trade comparison, netting and settlement services for the U.S. Government securities marketplace and is the sole provider of automated post-trade comparison, netting, risk management and pool notification services for mortgage-backed securities.

Emerging Markets Clearing Corporation (EMCC) is a global provider of automated trade comparison, trade guarantee, settlement and risk management services for Brady bonds, as well as dollar-denominated emerging market sovereign, quasi-sovereign and corporate debt.

Joint Venture:

Omgeo is the leading provider of post-trade pre-settlement trade management solutions for institutional trades, linking investment managers, broker/dealers and custodians in more than 40 countries.

Contents

2002 Performance Highlights

Total number of equity
transactions processed: ***4.1 billion***

Value of equity
transactions processed: ***$81 trillion***

Value of government securities
transactions processed: ***$540 trillion***

Value of money market
settlement activity: ***$92 trillion***

Par value of
mortgage-backed transactions: ***$50 trillion***

Value of securities
settled through DTCC: ***$917 trillion***

Value of securities
on deposit: ***$20.5 trillion***

Value of mutual fund
transactions processed: ***$1.6 trillion***

Value of insurance applications,
premiums and commissions processed: ***$5.4 billion***

Jill M. Considine, Chairman & CEO

Dear Stakeholder:

For 30 years, DTCC subsidiaries have demonstrated their ability to deliver on a promise to meet the industry's need for certainty, reliability and world-class products and services.

Our theme this year, "DTCC Delivers," recognizes this legacy of service, acknowledging the 30th anniversary of The Depository Trust Company in May 2003 and the contributions of the clearing corporations, which are highlighted in a timeline later in this publication.

On a consolidated basis, DTCC subsidiaries since the 1970s have returned to our customers in excess of $1.4 billion in rebates and discounts. And if we consider the cumulative effect of fee reductions for clearance, settlement and custody services over three decades, the savings have been substantial.

But even more important is the steady stream of value-added services our subsidiaries have brought to the industry, which have linked trading parties, spurred growth in markets and helped our customers grow revenue.

Over the past 30 years, we have established a network of connectivity among virtually all broker/dealers, banks, mutual funds, major insurance carriers and financial intermediaries that allows us to offer a growing range of services. As the trend toward outsourcing in the industry continues, we look forward to meeting our customers' continuing requirements, leveraging our network of connectivity, and automating, standardizing and streamlining processes that reduce risk and lower costs.

DTCC's Overall Performance

In 2002, despite difficult market conditions, DTCC once again experienced record volumes across our business segments. Transaction volumes for the processing of equities increased 17%, fixed income volume was up 25% and 22% for government and mortgage-backed securities, respectively, and volume for distribution services, which includes mutual fund and insurance transactions, was up 15%. However, even in the face of rising volumes, through departmental reorganizations, productivity gains and other economies, DTCC reduced staffing by 12% in 2002, and 18% since 2000. This compares to industry-wide staff reductions of less than 9% since 2000.

DTCC's fee-based revenue generated almost $906 million in 2002, up 11% from $819 million in 2001. At the same time, DTCC cut overall expenses by more than 11% or $79 million over the past two years. And through tight fiscal management and volume growth, we were able to return to customers $198.7 million in rebates and discounts in 2002.

We were also pleased to see that in spite of very tight expense controls, staff reductions and significant increases in processing volumes, our customer satisfaction survey scores continued to climb, up 5.4% over 2001. This progress is based on the dedication of our employees and the introduction of a Six Sigma quality program, which is implementing the use of quantitative tools for measuring and improving service in each of our businesses.

Reporting individual business unit results tends to mask the full picture of DTCC's contributions to the industry. In 2002, on a combined basis, our subsidiaries settled almost $917 trillion in transactions across the markets we serve. Put another way, DTCC's clearance and settlement processes turn over the $10 trillion U.S. gross domestic product every three days.

Risk Management and Business Continuity

DTCC provides, and our customers have come to expect from us, a wide range of risk management services and highly reliable systems and operating capabilities. Managing risk is an essential part of why DTCC and all our subsidiaries were created and it is deeply ingrained in our culture. Whether it's business continuity, or the core industry initiatives for which we provide leadership, such as straight-through processing (STP), immobilization and dematerialization of securities certificates, real-time trade matching and others, mitigating risk is a key underlying objective.

Managing risk is an essential part of why DTCC and all our subsidiaries were created and it is deeply ingrained in our culture.

Organizationally, in 2002, we brought the risk management functions of all our subsidiaries under one umbrella. Our goal is to ensure DTCC has a comprehensive understanding of the exposure that member firms may have across market segments and, thereby, strengthen oversight of systemic risk.

Our backup operating locations and staff served DTCC well on 9/11 and the week that followed, but that experience has intensified our focus on business continuity planning. DTCC has undertaken an aggressive program to redesign our business continuity plans, including the acquisition of new remote data centers, the decentralization of critical staffing functions, reconfiguring our network to ensure connectivity with multiple telecommunication suppliers and implementation of a testing program with customers to validate their readiness to maintain connectivity with DTCC subsidiaries in the event of a crisis.

Actions initiated by DTCC in 2002, however, are only part of what will be a sustained effort to have contingencies well thought out and in place. DTCC is grateful for the collaboration and support received from our regulators, the Securities and Exchange Commission, the Federal Reserve Board, the New York State Banking Department, other government agencies and, most importantly, our customers.

Performance by Subsidiaries

While volume processed by NSCC reached a record high of 4.1 billion transactions in 2002, up 17%, the value of these broker-to-broker transactions for the year was $81 trillion, down 9% from 2001. Noteworthy is how NSCC handles both the average daily volume as well as the stresses of peak days, which on July 24, 2002, reached 24.7 million transactions (the same day the marketplaces traded 5.3 billion shares), up 52% from our daily average.

NSCC not only brings certainty to trade completion as a central counterparty, but through our netting system, the number of trade obligations requiring financial settlement are reduced, thereby helping the industry lower risk and optimize capital. Of the $81 trillion in transactions processed last year, 97% of those obligations netted out of the system and did not require the exchange of payment with the clearing corporation.

Since the book-entry movement of securities ownership takes place at the depository, DTC's and NSCC's roles are naturally linked.

At DTC, the number of book-entry deliveries in 2002, including institutional trade settlement activity, exceeded 224 million transactions, up 2% from 2001. The value of these securities processed by DTCC was nearly $104 trillion.

DTCC's depository also handled over 36,000 underwritings last year, up 3%, reflecting the difficult equity market environment. The value of underwriting distributions dropped to $2.2 trillion from $2.4 trillion in 2001.

cont'd on page 6

cont'd from page 5

Our depository currently holds in custody nearly 2.2 million equity and debt issues valued at $20.5 trillion, including $1.7 trillion from non-U.S. issuers in over 100 countries. Aside from safekeeping securities, the servicing of these assets is a major role for DTCC and offers tremendous economies of scale to our customers. In 2002, we surpassed a 30-year milestone, processing dividend and interest income payments in excess of $1 trillion, up 19%. The value of reorganization and redemption payments also grew to $808 billion from $713 billion in 2001.

During 2002, DTCC took a number of steps to forge ahead on STP initiatives that will substantially benefit our customers. These STP projects are broad in scope and will transform the industry in much the same way that DTC and NSCC did during the paperwork crisis of the 1970s. At NSCC, we've already made significant strides in moving to real-time capture of trade reporting and the first major updating of our Continuous Net Settlement (CNS) system is well under way. We've also begun implementing the initiatives outlined in our 2002 white paper for a new settlement process that will combine the settlement systems used by NSCC and DTC and introduce a new system giving customers greater control of their settlement inventory.

> For 30 years,
> DTCC subsidiaries have brought a steady stream of value-added services to the industry, which have linked trading parties, spurred growth in markets and helped our customers grow revenue.

Thirty years ago, DTC was formed to immobilize or eliminate the movement of physical securities on Wall Street. Not only has that goal been largely achieved, but we are now leading the industry toward dematerialization or the outright elimination of paper. This past year, we reduced, by another 19%, the number of certificates held in our vaults to 5.5 million.

Since the integration of NSCC and DTC, and the subsequent mergers of other clearing corporations under DTCC's umbrella, we've become practiced at leveraging innovations in product design and technical capabilities across the enterprise. Our pilot launch in 2002 of Networking for Equities leveraged product design developed for our mutual funds business with technical features of our Direct Registration System to help us create a book-entry environment for the handling of restricted securities. The success of this effort will significantly enhance our progress toward STP and the elimination of paper certificates.

We have also seen benefits from the recent integration of Government Securities Clearing Corporation (GSCC) and the MBS Clearing Corporation (MBSCC), now called the Fixed Income Clearing Corporation (FICC). Through FICC's leadership, we've developed a real-time trade matching system (RTTM) that moves the comparison process for fixed income activity closer to the time of trade execution. RTTM is another example of our drive for STP by allowing for earlier settlement guarantees, speeding detection and resolution of errors and reducing the risk of failed trades. Since RTTM streamlines and speeds the capture of trade information, even if the market were badly disrupted as we saw on 9/11, trade details would be safely stored and accessible to our customers.

FICC is already capturing 9 out of 10 government securities trades in real time and, late in 2002, RTTM was introduced for mortgage-backed securities transactions. FICC is now developing RTTM capabilities for municipal and corporate bonds for rollout late in 2003.

FICC is keenly aware of its role to minimize risk in a market, which, by cash value alone, is one of the largest in the world. The value of government securities trades netted in 2002 reached almost $540 trillion and the par value of mortgage-backed transactions exceeded $50 trillion, up 53% and 49%, respectively. Like NSCC, FICC's central counterparty role in government securities and the process of netting substantially reduce risk and bring certainty to this market. On a peak day in 2002, over $5 trillion entered FICC's netting system, and 85% of the obligations were eliminated.

Looking ahead, FICC is laying out an aggressive action plan for 2003 with two white papers on extending central counterparty capabilities to mortgage-backed security transactions and bringing STP and netting to the fixed income institutional market.

DTCC's distribution services businesses, which support mutual funds and insurance products, continued to have strong volume growth in 2002. Our Fund/SERV® system, which links broker/dealers, banks and other financial intermediaries with mutual fund families, completed 83 million transactions involving purchases, exchanges and redemptions, up 14% and valued at $1.6 trillion.

DTCC has continued to enhance Fund/SERV to support the growing requirements of our customers for cross-border trade processing. Fund/SERV continues to generate interest globally as a model for bringing lower cost and streamlined processing.

Closer to home, we worked with funds and the Investment Company Institute to modify Fund/SERV in 2002 to automate the processing of 529 Plan trades, which offer tax deferments for college savings. In addition, we collaborated this past year with the Money Management Institute to pilot a new service by mid-2003 for automating and standardizing the processing and reporting of Separately Managed Accounts.

Our Insurance Services business has likewise been growing its franchise of services. Broker/dealers, who may have shied away from marketing insurance products because this industry segment lacked the streamlined processes found in mutual funds, will find that DTCC is making significant strides to link insurance carriers to our network and fully automate the process of selling annuities and life insurance products.

We believe that through partnering agreements and continued collaboration with insurance carriers, DTCC can offer broker/dealers the ability to mainstream insurance products in their marketing mix. In 2002, our progress was already evident. Our volumes more than doubled, to 22.5 million transactions worth $5.4 billion, for the processing of applications, premiums and commission payments.

Omgeo, our joint venture with Thomson Financial, demonstrated remarkable progress even as global market conditions slowed. Omgeo processed up to one million institutional trades on a peak-volume day in 2002. Equally impressive, Omgeo has helped customers improve their same-day affirmation rates to 60-70%, compared with an industry average of 15% in 2001.

In the international arena, DTCC is a strong advocate of the objectives outlined in the recently released Group of Thirty Report, which is aimed at reducing costs and strengthening market efficiency. The report tracks many of our own efforts at DTCC, the latest of which is our Global Corporate Action (GCA) validation service, which we expect to pilot in 2003. GCA will replace the redundant manual operations and technology currently used around the world with an automated, centralized source of high-quality corporate action announcement information.

EuroCCP, the clearance and settlement service we developed for Nasdaq Europe, is a terrific example of how DTCC leveraged existing technology and staff to create a solution quickly and inexpensively. While market conditions resulted in trading volumes too low to initiate EuroCCP operations, DTCC management is proud of the speed and thoroughness of our response to Nasdaq Europe's request for the development of EuroCCP.

DTCC's Transformation

DTCC's mission statement, adopted three years ago, set a directional stake in the ground and has served to guide this organization. We have reinforced our ability to be ready and resourceful in seizing new business opportunities, anticipating customer needs, being quick to market with new solutions and working collaboratively with partners to deliver breakthrough services. We have also reinforced, through white papers and participation on industry committees, our determination to be a thought leader in helping solve issues affecting the global financial community.

DTCC is grateful to its board, which, despite the difficult market environment and our determination to keep expenses flat, has worked with us as we've looked to reallocate resources to where the development of new services can benefit the industry and will diversify DTCC's revenue base.

While valued for their broad perspective, insight and guidance, our board members have also demonstrated their ability on countless occasions to look beyond the pressures affecting their own businesses and support directions on issues that serve the greater good of the industry.

Each year, this letter ends on a note of thanks to our employees. If we started out the letter describing their dedication and commitment in appropriate detail, there'd be little room left here for other subjects. Suffice it to say that we have an exceptional team of talented professionals at DTCC, who take enormous pride in every task that we perform for the industry. For our employees, excellence isn't a slogan on a poster; excellence is what they bring to DTCC each day.

Jill M. Considine

Jill M. Considine
Chairman & CEO

NSCC functions as the world's largest central counterparty, helping the industry to manage risk by guaranteeing completion of all equity trades flowing through its systems.

Clearance & Settlement

Post-Trade Processing Volumes Climb at DTCC, Despite Down Market

Even as market values slid on Wall Street for the third year in a row, the volume of trading continued to climb.

On the New York Stock Exchange (NYSE) and Nasdaq, for example, the total number of shares traded rose to 805 billion, up 3% over 2001. As a result, DTCC's clearing corporations handled record volumes in 2002.

For National Securities Clearing Corporation (NSCC), which clears and settles all equity, corporate and municipal bond trading in U.S. markets, this contributed to a leap in the number of transactions processed to 4.1 billion, 17% above the record 3.5 billion handled in 2001. And the average number of transactions flowing through NSCC each day in 2002 rose to 16.2 million, versus 13.9 million in 2001.

NSCC, of course, also has to be prepared to handle days when trading and transaction volumes spike above normal levels. On July 24, volume on the NYSE and Nasdaq surged to 5.3 billion shares, creating a peak transaction volume of 24.7 million transactions through NSCC's systems. This was more than 52% higher than average daily transaction volume and 26% above the previous record for peak volume set in 2001.

Reflecting the market's doldrums, the value of transactions processed by NSCC in 2002 fell 9% to $81 trillion, from $89 trillion in 2001.

In an uncertain market, investors increasingly sought the relative safety of fixed income securities, especially U.S. government securities, driving up the volume of fixed income transactions processed by Government Securities Clearing Corporation (GSCC) to 17.3 million, a 25% increase over 2001, and the number of mortgage-backed securities transactions increased to 1.4 million, up 22%.

NSCC functions as the world's largest central counterparty, helping the industry to manage risk by guaranteeing completion of all equity trades flowing through its systems. NSCC nets trades to a single position for each security for each broker. It also nets the

financial obligations involved to a single money position for each broker. This process sharply reduces the number of settling transactions, the number of securities movements and the number of financial obligations requiring settlement.

For example, on a peak volume day in 2002, NSCC's netting system reduced the value of obligations requiring financial settlement by 97% — from $492 billion to $13.3 billion. In effect, broker/dealer firms had to mobilize cash to pay for only 3% of the total trades, which, in turn, lowered credit risk and operational costs for them and their customers throughout the industry.

DTCC's depository handled a record 224.3 million book-entry deliveries in 2002, up 2% over the previous year, which includes broker-to-broker and institutional transactions. The value of the deliveries, at nearly $104 trillion, was 14% below the value recorded in 2001. ❖

Staying the STP Course

For DTCC, whose subsidiary companies were created to automate, centralize and streamline the processing of securities trades, mutual fund transactions and market-based insurance products, straight-through processing (STP) has always been a principal focus. So it's no surprise that throughout 2002 DTCC continued to push ahead with STP projects aimed at leading the industry toward greater efficiencies and innovative technology solutions — all initiatives that will benefit the industry regardless of whether or when the settlement cycle is shortened. STP efforts during 2002 included building technology to accelerate the receipt and transmission of trading information; moving to electronic storage and submission of documents to eliminate paperwork and improve business continuity; and upgrading the settlement system to increase straight-through functions and make it more responsive to customer needs.

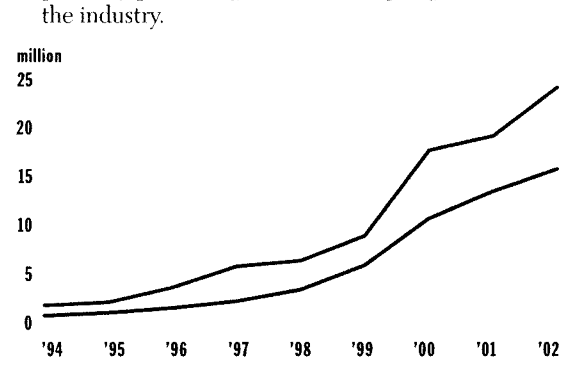
In a key STP improvement implemented in 2002, both the New York and American Stock Exchanges began submitting all trade information to NSCC in real time for the first time. As a result, by year-end, NSCC was receiving more than 40% of all trade data in real time.

With other markets now moving quickly in the same direction, the expectation is that, by year-end 2003, more than 90% of all equity trades will be received in real time, with the remaining data arriving in multiple batches throughout the day. Nasdaq, for example, expects to begin real-time trade data submission in the first half of 2003, while major electronic communications networks (ECNs) anticipate making this move in the second half of the year.

Capturing transaction information in real time allows DTCC to get trade information earlier, which enables us to evaluate risk more effectively. It also eases pres-

cont'd on page 10

Ensuring capacity for the markets: NSCC provides the systems capacity to support routine and peak-day processing volumes and spur growth for the industry.



Average daily transaction processing volumes vs. peak-day volumes.

cont'd from page 9

sure on systems capacity and reduces the risk of processing delays in the event of an interruption in the clearance and settlement system. And if an exchange or trading platform itself experiences a problem, real-time data feeds minimize the possibility that trade information will be lost for clearance and settlement purposes.

Updating Systems for STP

Throughout 2002, we continued to modernize a number of our systems, making them better able to respond to STP requirements. For example, we constructed a new Trade Repository that has a modern, flexible database and will, in the future, provide near real-time capabilities so that customers can review trades and resolve problems or issues immediately. In mid-2003, the new repository will replace the current Compared Trade Information database as the sole system for trade information.

Work also continued in 2002 on the rewrite of the Continuous Net Settlement (CNS) system, the first wholesale revision of the system since it began operation more than 25 years ago. Early in the year, we released specifications for the changes participants need to make in their systems to use the revised CNS. The first of these changes, set for adoption in 2003, involves automating how balance orders are handled. The rest of the changes needed for the new CNS are scheduled for implementation in 2004. ❖

A New Vision for Settlement

In another key building block for STP, DTCC is working to bring the biggest changes ever to its settlement system,

making it far more flexible and streamlined.

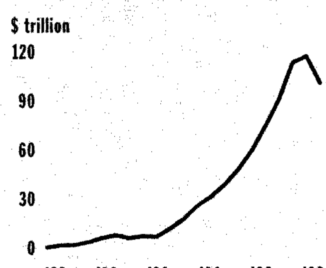
These include a new Inventory Management System (IMS) that will give customers better control over the flow and timing of their securities deliveries — and thus cut down on fails, reclaims and settlement exceptions. With IMS, customers will have the option to set up standing delivery profiles at the depository. Transactions flowing into the system will be staged for processing based on this delivery profile rather than, as they are in the current system, submitted for processing simply according to standard rules set by the depository's system. Submissions that currently don't meet requirements for processing are recycled in a DTC-determined order. The IMS, on the other hand, will ensure deliveries are processed in the order intended by the customer.

The first phase of the new system, which we began building in 2002 and expect to be available during the second half of 2003, replaces the authorization process for institutional deliveries and expands it to other transactions. It also allows participants to submit deliveries for any future settlement date, and provides a mechanism to recycle failed transactions automatically into the next day, eliminating the current need for firms to resubmit a dropped delivery. A second phase will allow customers to recalibrate delivery profiles based on delivery type on any given day.

Another key capability planned for implementation in 2003 is a "transaction look-ahead" capability. In the current system, if a participant has a delivery that is tied to a receive, but the receive would put the participant over its net debit cap at the depository, the receive is not processed for settlement until the participant puts up additional credits or cash, or until offsetting deliveries are processed. "Look-ahead" processing automatically sees whether transactions for a customer are in the pipeline and then links them in order to avoid "debit cap gridlock."

We are also consolidating the separate settlement systems maintained by DTC and NSCC. While these money settlement systems have long been linked and cross-endorsed on settlement day,

Speeding settlement:
The depository saves investors and the securities industry millions of dollars, hours and effort by settling trades in a book-entry environment.



The total value of book-entry or paperless deliveries.

DTCC is taking the next step by combining them into a single platform, scheduled to begin operating in mid-2003. This combined system will provide earlier settlement and greater efficiency, especially to companies participating in both NSCC and the depository. It will also reduce payments to or from settlement banks to a single wire transfer for both DTC and NSCC obligations. ❖

Managing Risk in Real Time

Managing and mitigating risk – both financial and operational – is an essential goal for DTCC, contributing immeasurably to the safety and soundness of the markets. And in today's world of finance, new technologies, growing volumes, new market practices and exposure to terrorism and other external events all place increasing demands on our risk management capacities. As a result, the company broadened its risk management focus in 2002.

In 2002, we brought the risk management functions of all our subsidiaries under one umbrella to ensure DTCC has a comprehensive understanding of the exposure that member firms may have across market segments and, thereby, strengthen oversight of systemic risk.

We have also started to manage risk in real time. The first phase of a new real-time risk management system was introduced on a trial basis in 2002 and will become fully operational in 2003. IMPACT, as the system is called, will automatically monitor and flag risks as they develop from trading patterns and provide them for evaluation by NSCC risk specialists. This gives DTCC a better chance to spot and evaluate potential risks in today's fast-moving markets.

Even though the depository has always maintained full collateralization for settlement, the telecommunications disruptions that occurred following 9/11 forced DTCC to reevaluate the way the industry handles high-value money market instruments, such as commercial paper, during emergencies. While DTCC put interim measures into effect quickly, we are also working with The Bond Market Association to develop a longer-term response. Both organizations issued a white paper to the industry in January 2003 proposing new procedures to help ensure settlement finality, alert participants more quickly to operational problems and generally provide more control over the maturity presentments process. To make the proposed procedures operational, the depository has begun development of the necessary system changes in what is expected to be a multiyear effort.

We have also refocused our internal risk management efforts. In 2002, we launched a new, far-reaching enterprise risk management initiative. Its goal is to identify and assess nonmarket risk factors such as technology, reputational and other operational risks, and then establish accountability within DTCC for managing those risks. Current plans call for an internal operational risk management assessment to be initially conducted semiannually, so that the review and any actions flowing from it will become a standard component of DTCC's ongoing risk management activities. ❖

Bringing risk management functions under one umbrella ensures DTCC has a comprehensive understanding of the exposure member firms may have across market segments.

cont'd on page 12

cont'd from page 11

Business Continuity: Reinforcing the Safety Net

Better, more complete planning for business continuity was a principal concern for the entire securities industry in 2002. And even though DTCC's systems, with operating facilities in multiple locations, remained fully operational after the attacks of 9/11, this continues to be a top priority for DTCC as well.

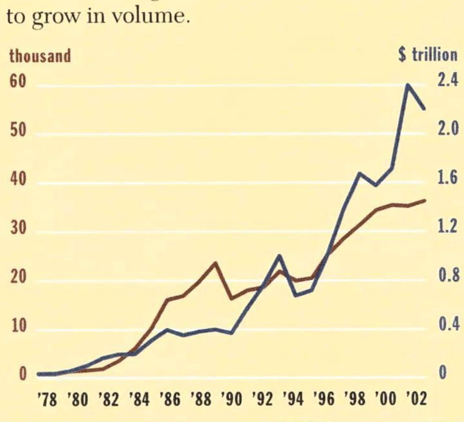
Among many initiatives taken, the company made a multimillion-dollar investment in additional data processing facilities. Another initiative involved improving telecommunications links with participants.

In 2002, DTCC enhanced our communications network to ensure that all the depository's data processing facilities can remain connected. If one location fails to function, data or voice communications can be routed to other sites. In addition, DTCC has obtained approval from the U.S. government's National Communications System to have the depository's telecommunications rated as a "national priority" for restoration following a disaster.

The depository also announced that, beginning in 2003, major participants are required to conduct annual telecommunications testing from their primary and backup locations to all of the various DTC processing centers. NSCC will begin similar customer tests in 2003.

Staff dispersal is another critical component of our ability to respond to disasters or outages. By year-end 2002, DTCC had further decentralized critical operating technology and frontline relationship management staff. DTCC senior executives also rotate among our locations so that top management remains dispersed in the event of an emergency. ❖

Supporting underwriting activity:
DTC has significantly streamlined the process of underwriting new issues, which continue to grow in volume.

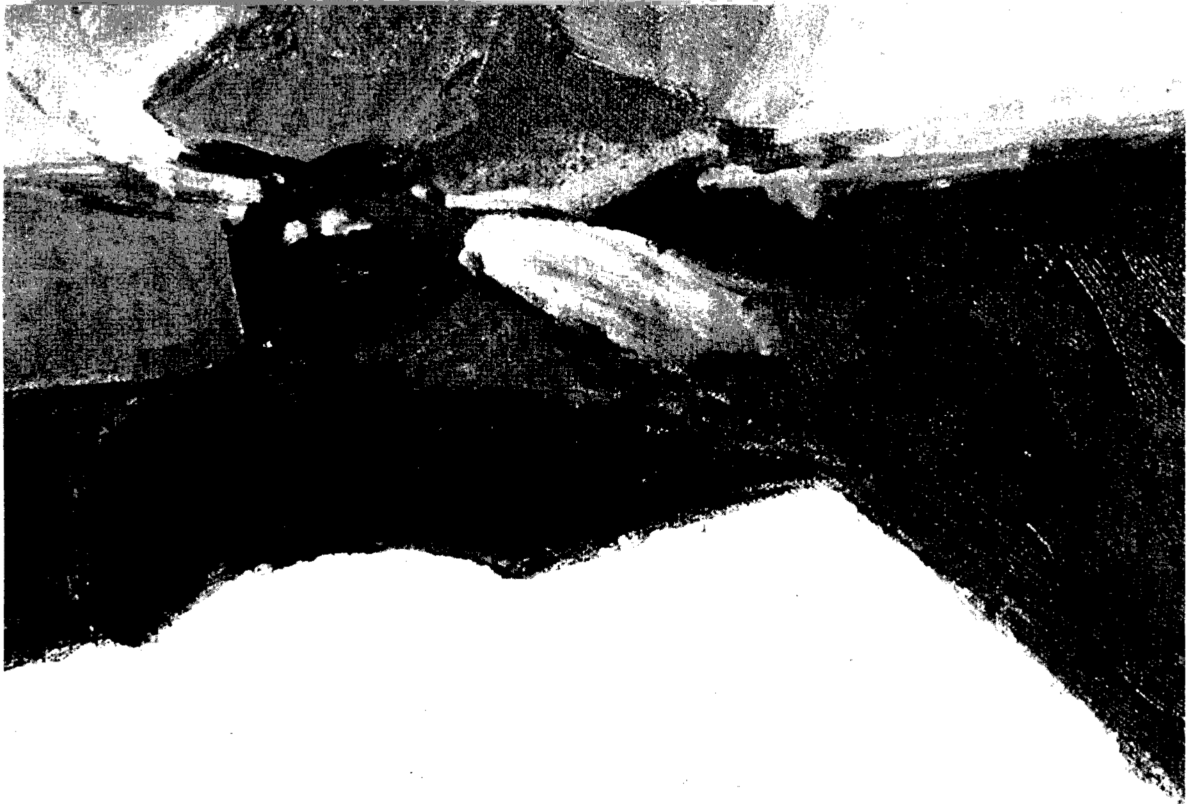


Total annual DTC underwriting activity including value and number of underwritings completed.

Underwriting: Another Year, Another Record

While 2002 proved to be the slowest year in decades for new equity issues, it turned out to be a record-setting year for the issuance of other securities. New issues in the bond market climbed to a record $5.4 trillion in 2002, up more than 18% over the previous year. The depository, in turn, handled a record 36,019 underwritings in 2002, an overall volume increase of 3% from 2001, which was a record year itself. The value of underwritings in 2002 declined slightly to $2.2 trillion from 2001's record $2.4 trillion.

Driving the wave of securities underwriting were interest rates that drifted to their lowest level in nearly 40 years. To take advantage of these rates, numerous cities, counties and other bonding authorities offered a record $472.5 billion in new issues in 2002, many of them to refinance debt previously issued at higher rates.



The volume of municipal debt underwritings handled by the depository climbed to 19,524, up 7% over 2001.

Low interest rates also fueled record levels of underwriting business for asset-backed securities, collateralized mortgage obligations and certificates of deposit, which together rose 25% over the strong growth experienced in 2001. Distribution of non-U.S. corporate equity and debt offerings through the depository remained a sizable business in 2002, with one out of every 10 offerings channeled through DTC's Underwriting service from a non-U.S. source.

In the face of these sustained high volumes, the depository's Underwriting unit moved aggressively during 2002 to take advantage of the Internet, shifting as much business as possible into an all-electronic environment. In a major step toward STP, the company launched an Electronic Files Library, an online capability that accepts, processes and stores securities-offering documents electronically, thus eliminating the large volume of paperwork normally required for new issues.

Another Internet-based initiative developed during 2002 and set for launch in 2003 is a new Web Underwriting service. For underwriters and their syndicate members, the opportunity to electronically submit new issuance eligibility requests and related information provides added speed and efficiency. The service funnels their offering information directly through the Internet onto the depository's database. ❖

Streamlining Bond Trade Reporting

The Securities and Exchange Commission (SEC) has been pressing

the securities industry for greater transparency in reporting over-the-counter (OTC) bond trade prices for a number of years now. In response, the NASD launched its new Trade Reporting and Compliance Engine (TRACE) in 2002. DTCC immediately recognized that, while the new system satisfied requirements to report transaction prices, it also put new reporting burdens on member firms, which would have been required to submit information twice — once to TRACE for reporting purposes, and again to NSCC for clearance and settlement.

To eliminate these redundant reports and make it easier and faster to transmit prices, NSCC built an interface linking its own Fixed Income Transaction System (FITS) directly to the TRACE system. With that interface in place, broker/dealers only have to submit data to NSCC, which can automatically forward the information to TRACE to satisfy trade-reporting requirements.

In another move that will bring greater efficiency to the bond markets, NSCC expects to move its corporate and municipal bond comparison into a system managed by DTCC's Fixed Income Clearing Corporation. The merger with that system, which now clears government bond and mortgage-backed securities, will have two objectives. One is to bring real-time trade matching to corporate and municipal bond trading by year-end 2003, which will help to ensure safer and more efficient settlement. The other is to allow firms to comply with the new regulatory requirement that mandates submission of municipal bond trades within 15 minutes of their execution, beginning in mid-2004. This feed is expected to prove highly useful, especially as TRACE's corporate OTC bond reporting system begins to provide trade pricing data on an additional 3,700 fixed income instruments. ❖

Asset Services

Over Two Million Securities Serviced...and Growing

Asset Services was another DTCC business where momentum remained strong, despite the continued downturn in the market and a sputtering economy. In 2002, DTCC's depository (DTC) processed a record volume of reorganizations, redemptions, dividend and interest payments, with a value of nearly $1.9 trillion, up almost 17% from the prior year.

Custody and asset services hark back to the earliest days of DTC as a central location to immobilize securities and streamline their servicing from "cradle to grave." Today, this is one of DTCC's largest, though often unsung, businesses. It is a high-volume processing operation based on rigorous procedures, secure and reliable systems, economies of scale and years of experience. To accomplish this work, DTCC deals with as many as 4,000 paying agents around the world, eliminating the need for customers to maintain their own operations to do so.

Over the past 30 years, DTC has steadily expanded the number and type of securities it handles, and today, nearly 2.2 million securities issues are depository-eligible — most held in book-entry or paperless form. These include equities, corporate and municipal debt, American and Global Depositary Receipts, collateralized mortgage obligations and exchange-traded funds, as well as commercial paper and other money market instruments.

International issues represent close to 10% of the overall value of securities held, with DTC servicing securities from issuers in more than 100 countries and territories. ❖

Blazing a Paperless Trail

DTCC plays a leadership role in the securities industry's long-standing drive to eliminate physical certificates. Over the past 30 years, DTCC has partnered with the industry to create a series of innovative strategies that advance this effort.

The goal is to facilitate paperless transactions, which streamlines processing, lowers costs and reduces the risks associated with lost, stolen, forged or counterfeit certificates. And 2002 saw remarkable progress on this front. The number of certificates held in the depository's vaults declined 19% to 5.5 million, down 1.3 million from 2001. Over the past 10 years, the total number of certificates is down about 20 million.

Due to the U.S. securities markets' tradition of providing paper certificates to investors, DTC has developed multiple strategies to deal with different investors and classes of securities. These include immobilization and "dematerialization," which are two sides of the same coin. Immobilization takes certificates out of circulation, storing them at central locations, while dematerialization adds another dimension by using electronic ownership records.

DTC's earliest programs, designed more than 20 years ago, are still used today. These include Fast Automated Securities Transfer (FAST), which streamlines transfer processing through the issuance of jumbo balance certificates registered in the depository's name but held at agents, and Book-Entry-Only (BEO) issuance, which began as a way to deal with the high volume of municipal bond issuances and involves no certificates whatsoever.

More recently, the depository has developed other novel ways to give investors greater flexibility, while ensuring the safety of ownership records of securities held in certificateless form. These include the Direct Registration System (DRS) and Networking for Equities (NFE).

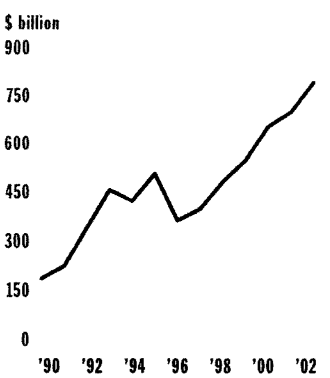
Securities transactions under DRS, which lets investors hold securities positions in their names directly on the books of the transfer agent or issuer, grew to more than 400,000 in 2002, an increase of 40% over the previous year. At the same time, volume for the DRS Profile Modification System (Profile), which electronically links transfer agents and broker/dealers, increased dramatically — to 300,000 in 2002, more than 10 times the number processed the prior year.

With the 2002 pilot launch of NFE, DTCC began tackling the largest single group of securities still held in certificate form — restricted securities. These include private placements or other securities not registered in public offerings that may have limitations on their transferability.

In the first phase, NFE converts securities to book-entry form and maintains customer-level information. NFE ultimately will allow for the complete dematerialization of restricted issues, as well as other types of securities, and provides an all-electronic environment for processing them.

On another front in 2002, DTCC developed a plan to eliminate physical certificates of certain nontransferable issues. Reducing the number of these securities will lower overall cost for the industry, since they represent about a quarter of the depository's certificate inventory and cost a considerable sum to safekeep and maintain. DTCC expects to begin this program later this year. ❖

Bringing STP to corporate actions: DTC provides high-volume systems, economies of scale and security to corporate actions processing.



Value of reorganization, redemption and maturity payments processed by DTC each year.

Helping Customers Outsource Physical Processing

DTCC's goal of centralizing services to leverage economies of scale and bring efficiencies

to customers includes the safekeeping and processing of the industry's remaining physical securities. Outsourcing these activities to DTC enables banks and brokers to replace the high fixed costs of vault management, insurance and security with a variable cost structure to better manage operating costs and risks.

In 2002, DTCC introduced major improvements in the depository's Custody services, which include Custody Vault, Custody Reorg and the Branch Deposit Service. Changes include improved customer communications, more robust reporting, a streamlined implementation process and certain fee reductions. A driving force in many of these enhancements was the work of a DTCC Six Sigma Quality team, whose goals included improving customer service and reducing processing time and cost. ❖

Streamlining Corporate Actions Processing

Stock splits, spin-offs, bankruptcies, conversions,

exchanges, mergers and tender offers are just a few of the corporate actions handled in this pressure-packed, time-sensitive business. In 2002, DTCC's depository processed more than 10,500 of these transactions, up 4% from

cont'd on page 16

cont'd from page 15

the prior year. Redemptions and calls, which are another class of corporate actions, also increased in 2002, rising to over 250,000, or 13% above the prior year's level. Payments for all of these transactions climbed to $808 billion, also up 13% over 2001 and easily topping previous records.

DTCC is working aggressively to enhance its corporate action capabilities and extend its services globally. These initiatives dovetail with DTCC's industry-wide effort to bring greater levels of straight-through processing (STP) globally.

Each corporate action has a multiplier effect. A single transaction may involve hundreds of financial firms, which then results in thousands of communications sent and/or payments allocated to investors. Although a great deal of processing for depository-eligible issues is centralized at DTC, firms still retain a considerable portion of time-consuming, labor-intensive work, which is known to be among the most complex and challenging work in the back office.

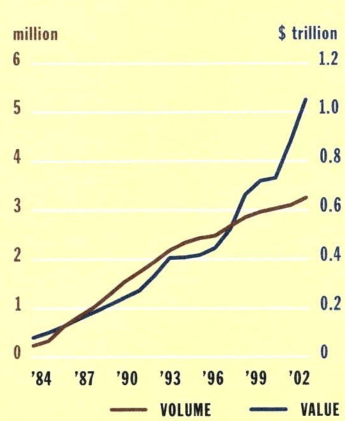
In 2002, DTCC focused on two major development efforts to revolutionize corporate action processing. The industry will begin to reap the benefits of these initiatives in 2003.

The Global Corporate Action (GCA) validation service, expected to be launched in 2003 as a pilot program, is an automated, centralized source of "scrubbed" corporate action announcement information. It is expected to deliver huge economies of scale by eliminating redundant operations and technology in the industry. GCA validates information, including data sourced from commercial information providers, through an intricate process of mapping, normalizing, consolidating and verifying the information, eliminating the need for each bank and broker/dealer to complete this work independently.

GCA will improve the quality of information distributed, reduce costs, lower operational risk and simplify processing from the initial announcement capture through the data validation process. Initially, GCA will cover securities traded in the Americas and Europe, and will provide worldwide coverage by year-end.

In late 2003, DTCC also plans to introduce another corporate action initiative. The Global Corporate Action Hub (GCAH) is a flexible, real-time messaging solution, which will eliminate the manual point-to-point exchange of corporate action information. Through streamlined communications among investment managers, custodians and broker/dealers, GCAH will reduce risk and costs. The service will support the new ISO 15022 corporate action message standards and global market practices, and offer expanded file-to-file transmission capabilities for high-volume processors of corporate actions. ❖

Simplifying the industry's income payments: DTC's centralized processing system makes it possible each day for participants to efficiently allocate dividend and interest payments to investors.



The volume and value of cash dividend and interest payments DTC handles each year.

Income Paid Surpasses $1 Trillion Mark

For the first time in the depository's 30-year history,

the value of dividend and interest income payments processed exceeded $1 trillion in 2002, up 19% from $880 billion the prior year. The total number of dividend and interest distributions the depository administered rose 3% to a record 3.2 million payments.

Disbursements on collateralized mortgage obligations (CMOs) and other structured securities, in particular, skyrocketed in 2002, owing in part to low interest rates, which caused many homeowners to refinance their mortgages. The average principal and interest disbursements for a monthly payable date in 2002 surged by 63% to $26 billion from $16 billion the prior year.

To strengthen processing and bring greater payment standardization on these complex issues, DTCC embarked on a number of projects last year, implementing internal enhancements and safeguards, while working with the industry to establish more rigorous reporting standards for agents and trustees. ❖

Fixed Income

Fixed Income Moves Under One Roof

Merging Government Securities Clearing Corporation (GSCC) and MBS Clearing Corporation

(MBSCC) to create the new Fixed Income Clearing Corporation (FICC) was the right idea at the right time. The merger represents a significant step in responding to industry needs for greater synergies, cost reductions and efficiencies in the post-trade processing of fixed income instruments — at a time when our customers are challenged by an increasingly competitive and cost-conscious marketplace.

FICC's formation caps industry synergy efforts for fixed income processing that started with the consolidation of GSCC and MBSCC technology and staff in 2001. The new company, which began operations January 1, 2003, gives customers a common approach to fixed income processing and enhances DTCC's ability to meet our goal to bring innovative, cost-effective technology to customers. This includes moving toward Real-Time Trade Matching (RTTM) for all eligible fixed income transactions; developing uniform standards for messaging, reporting, netting and settlement; building a common risk management platform; and establishing uniform rules and membership standards.

The merger should also bring cost reductions, allowing FICC and customers to eliminate redundant communications facilities, achieve efficiencies from standardization of processing, reap opportunities for cross-training and portability of staff, and reduce other expenses such as separate regulatory reports and financial statements. ❖

The creation of FICC gives customers a common approach to fixed income processing and enhances DTCC's ability to bring them innovative, cost-effective technology.

Record Volume Processed ...Without a Hitch

2002 was another record-breaking year for processing volumes in

what, from a dollar-value point of view, is the world's largest securities marketplace — government securities and mortgage-backed securities.

Tremendous market volatility and uncertainty continued to drive investors to seek the relative safety of U.S. government instruments and to take advantage of historically low interest rates to purchase homes or refinance mortgages. As they did so, Government Securities Clearing Corporation (GSCC) and MBS Clearing Corporation (MBSCC) successfully maintained the highest levels of reliability and risk management to capture and process this growing volume.

On 17.3 million transactions in 2002, up 25.4% from 2001, the total value of government securities trades netted and settled rose

cont'd on page 18

cont'd from page 17

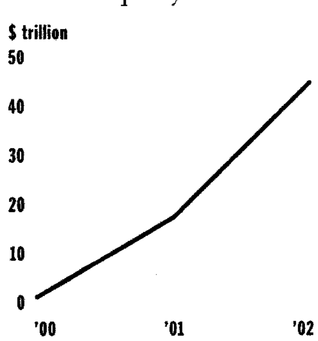
to \$539.6 trillion, a 53% increase over 2001. Of this, repurchase agreements (repos) accounted for the largest dollar volume processed on any given day. (Repos are an elaborate, multi-layered financial instrument increasingly used by entities to meet financing needs and for collateralized securities lending between one another.) For instance, the average daily dollar value of term General Collateral Finance (GCF) Repos skyrocketed in 2002 to \$589 billion, an increase of 257% over the previous year.

The importance of netting increased with the surging value and volume in 2002. Our systems and risk management policies continued to protect our members even as some \$2.2 trillion buy/sell and repo trades in government securities entered the net on average each day. Of this, some \$1.6 trillion or 76% was eliminated from settlement each day through netting, compared to \$1 trillion, or 71%, in 2001 on a daily value of \$1.4 trillion.

In 2002, GSCC also recorded another record peak day. On August 15, more than \$5 trillion in trading activity entered the net, resulting in some \$759 billion in obligations requiring financial settlement for a netting factor of 85%.

In the world of mortgage-backed securities, the total par value of transactions compared in 2002 topped \$50 trillion, a 49% increase over 2001. The par value eliminated through netting rose to \$23.1 trillion, representing a 43% increase over 2001. The current face value processed through the Electronic Pool Notification (EPN) service reached \$8.5 trillion, a 31% increase over 2001. Corresponding messages processed hit 869,000, an increase of 28%, while the number of pools delivered grew to nearly 10.2 million, compared to 9.1 million in 2001, up 12%. ❖

Increasing liquidity through GCF Repos: GSCC customers have quickly seized the opportunity to utilize General Collateral Finance (GCF) Repos as a growing source of liquidity.



Dollar value of GCF Repo-compared trades for 2000–2002.

RTTM's Impact Grows on Fixed Income Processing

Real-Time Trade Matching (RTTM) is a core requirement to help the multi-trillion-dollar fixed income marketplace achieve straight-through processing (STP). In addition to operational efficiencies, the goal of an STP infrastructure is to strengthen risk protection for our fixed income customers. RTTM provides this protection by moving the comparison process for government and mortgage-backed securities closer to the time of trade execution, allowing for an earlier settlement guarantee.

RTTM utilizes standardized interactive messaging to maximize the volume of trades that match on trade date. In doing so, RTTM is a strong example of FICC's goal to promote safe and efficient settlement by reducing intra-day market and operational risk, and to provide customers with the ability to receive immediate trade status notification for the prompt detection and resolution of errors.

Today, more than 96% of all government securities volume is submitted either interactively or by multi-batch through the RTTM system.

In September 2002, FICC rolled out a modified version of the RTTM system for mortgage-backed securities. Most major mortgage-backed securities dealers are testing the application and expect to go live with it in mid-year 2003. Introducing RTTM for mortgage-backed securities also helps lay the foundation for FICC to become the central counterparty for these transactions.

Next will come an RTTM system for corporate and municipal bonds and Unit Investment Trusts (UITs), currently processed by National Securities Clearing Corporation (NSCC). This will be tested in the third quarter of 2003, with rollout planned for the fourth quarter.

In 2002, FICC also enhanced the RTTM system, originally rolled out for government securities, as part of FICC's ongoing efforts to provide flexible, functional and innovative products and services that keep pace with customer needs. Additions include introducing "demand" processing and instituting "DK" capabilities, both of which will help achieve 100% intra-day trade comparison. (Demand processing allows for trade matching based on unilateral input by an authorized trade submitter against an approved counterparty. "DK" capabilities allow customers to notify their counterparties if they don't agree with the data submitted by them, which will, in turn, preclude the demand trade from matching.)

Joint development of RTTM has brought an estimated $47 million in clearing corporation savings (based on what GSCC, MBSCC and NSCC would have spent individually versus actual spending on a combined basis). ❖

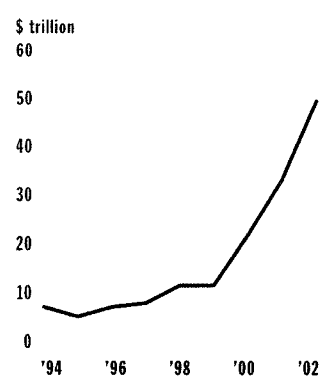
Supporting RTTM With a Common Web Front-End

To support Real-Time Trade Matching (RTTM), FICC is developing a Web-based user interface, RTTM Web, for both trade capture and trade reconciliation. As another demonstration of how FICC continues to enhance and leverage its technology, this interface will support all RTTM systems, and serve as a single point of entry for all fixed income trades.

RTTM Web, through a series of interconnected windows and sophisticated query tools, will allow members to obtain real-time status information for all transactions received and/or updated by the RTTM system. It will also provide a facility for retrieving and viewing intra-day, end-of-day and historical print image reports.

FICC plans to roll out RTTM Web for mortgage-backed securities in mid-2003. We will then leverage standards defined for MBS RTTM Web to develop the Corporate and Municipal RTTM Web and the Government Securities RTTM Web that will follow in December 2003 and later in 2004, respectively. ❖

Managing demand in mortgage markets: MBSCC has successfully supported U.S. mortgage markets as investors seek to capitalize on low interest rates, resulting in rising dollar volumes for mortgage-backed securities.



Total annual par value of transactions compared by MBSCC.

FICC Solutions That Enhance Services

FICC continues in the tradition of GSCC and MBSCC, which established reputations for working to provide customers with cutting-edge technology that maintains safety and soundness, while helping them grow their businesses and reduce costs. Key initiatives under way include:

STP for Institutional Settlement

In response to an industry-wide initiative, FICC recently distributed a white paper to the industry that proposes alternatives for encompassing as many fixed income institutional trades in FICC's netting and settlement processes as possible — essentially bringing STP capabilities to the fixed income institutional market. This would also maximize netting, promote efficient settlement on a trade-for-trade basis and eliminate redundant communications and software development.

Such an infrastructure would include the use of a common message hub to provide a single point of connectivity for all market participants, the adoption of common message standards and the use of FICC's established processing mechanisms for centralized netting and settlement.

This initiative would involve collaboration from all market

cont'd on page 26