



Bank Polski

# The PKO Bank Polski SA Group Directors' Report for the first half of 2017

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## 1. FINANCIAL RESULTS OF THE PKO BANK POLSKI SA GROUP IN THE FIRST HALF OF 2017

### 1.1 SELECTED FINANCIAL DATA

Table 1. Selected financial data of the PKO Bank Polski SA Group

	30.06.2017	30.06.2016	Change
Net profit	1 382 PLN mn	1 512 PLN mn	-8.6% (y/y)
Result on business activities*	6 101 PLN mn	5 831 PLN mn	4.6% (y/y)
Net interest income	4 160 PLN mn	3 762 PLN mn	10.6% (y/y)
Net fee and commission income	1 443 PLN mn	1 302 PLN mn	10.8% (y/y)
Net other income**	498 PLN mn	767 PLN mn	-35.1% (y/y)
Administrative expenses	-2 938 PLN mn	-2 757 PLN mn	6.6% (y/y)
Tax on certain financial institutions (the bank tax)	-464 PLN mn	-369 PLN mn	25.7% (y/y)
Net impairment allowance	-783 PLN mn	-782 PLN mn	0.1% (y/y)
Total assets	286 PLN bn	272 PLN bn	5.1% (y/y)
Equity	34 PLN bn	32 PLN bn	8.7% (y/y)
ROA net	1.0 %	1.1 %	-0.1 p.p.
ROE net	8.4 %	9.2 %	-0.8 p.p.
C/I (cost to income ratio)	47.9 %	53.1 %	-5.2 p.p.
Net interest margin	3.2 %	3.1 %	0.1 p.p.
Share of impaired loans	5.7 %	6.5 %	-0.8 p.p.
Cost of risk	-0.74 %	-0.70 %	-0.04 p.p.
Capital adequacy ratio	16.85 %	15.21 %	1.64 p.p.

\* Result on business activities defined as operating profit before administrative expenses, tax on certain financial institutions and net impairment allowance and write-downs.

\*\* Net other income calculated as result on business activities before net interest income and net fee and commission income

The net profit of the PKO Bank Polski SA Group generated in the first half of 2017 amounted to PLN 1 382 million, which represents decrease by 8.6%, i.e. by PLN 130 million comparing to the previous year profit. The achieved level of net profit was determined by:

- 1) improvement of the result on business activities of the PKO Bank Polski SA Group, which amounted to PLN 6 101 million (+4.6% y/y) mainly due to:
  - an increase in the net interest income of 10.6% y/y, which was achieved thanks to an increase in the amount of interest-bearing assets,
  - improvement in the net commission income (an increase of nearly 11% y/y), among other things, as a result of handling investment funds, brokerage activities and the offer of insurance products,
  - a decrease in net other income of PLN 269 million, which was mainly associated with the settlement of the acquisition of *Visa Europe Limited* by *Visa Inc.* in June 2016, which was partly compensated with improved net other income and expense,
- 2) the introduction of tax on certain financial institutions (the bank tax) from 1 February 2016, which resulted in an increase in the respective charges of PLN 95 million y/y,
- 3) an increase in operating expenses of PLN 181 million, resulting from the settlement in the first quarter of 2017, of the annual contribution to the mandatory bank restructuring fund,
- 4) stabilization of the net impairment allowance and write-downs.



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The structure of the statement of financial position of the PKO Bank Polski SA Group (the Group, the Bank's Group), characterized by strong deposit base and a safe level of equity, made it possible to achieve an increase in the result on business activities through stable organic growth and acquisitions. The loan to deposit ratio (amounts due to customers) as at the end of June 2017 amounted to 98.7% (the ratio of loans to stable sources of funding<sup>1</sup> amounted to 85.2%), which proves the very good condition of liquidity of the Group.

As a result of actions taken in the first half of 2017 the Group:

- reached a total asset value of PLN 286 billion, reinforcing its position as a leader in the Polish banking sector,
- maintained a leading market share in loans and deposits with the level of 17.8% and 17.1% respectively,
- maintained the first position on the market of mortgage loans to individuals<sup>2</sup> with 30.2% share in sales and achieving sales on the level of more than PLN 6.7 billion,
- was the largest lender to small and medium sized enterprises of loans with de minimis guarantees and comprised 21.3% of market share<sup>3</sup>,
- increased the number of individual customer accounts by 128 thousand, and reinforced its leading position in this respect;
- took the lead in the field of covered bonds in Poland, also being the most active issuer,
- expanded the offer of insurance and investment products, and property insurance for customers, among other things, by launching, in the online banking system, the sale of new products not related to bank products; the Group's insurance offer is already used by more than 1.1 million customers,
- strengthened the capital position through increasing the level of own funds of accumulation of profit generated in 2016, which results on an increase in the capital adequacy ratio by 1.04 p.p. compared to year end of 2016 to a level of 16.85%.

## 1.2 THE MAIN EVENTS OF THE FIRST HALF OF 2017

In the first half of 2017 as in the whole year 2016, the banking sector operated in conditions of historically low levels of interest rates and high regulatory burdens, while the macroeconomic situation was favourable. A clear strengthening of economic activity both globally and in Poland, mainly due to the recovery in investments and growth in private consumption. The situation on the loan-deposit market was shaped by the advantageous situation on the labour market.

The PKO Bank Polski SA Group has progressed to the second year of 'Wspieramy rozwój Polski i Polaków' ('We support the development of Poland and the Poles') of strategy realization. The new strategy is an answer to the changing market environment and the need to adjust to new challenges facing the banking sector and the Polish economy. The direction of the transformation of the Bank's business model will remain closely connected with the growing digitization of social life and the strategy for economic development of Poland.

The Bank's Group continued sustainable development, focused on improving the quality of service and increasing the innovativeness of products and distribution channels, in particular in the field of electronic banking and mobile payments.

### THE GROUP SYSTEMATICALLY DEVELOPS A PACKAGE OF ELECTRONIC BANKING AND MOBILE SERVICES.

- Since March 2017, PKO Bank Polski SA's customers have the possibility of placing an application to the Tax Office for preparing a preliminary PIT-37 tax return for 2016 and for submitting it on behalf of the taxpayer through the iPKO e-banking platform. The new functionality 'Płacę z iPKO' enables faster, more comfortable and more secure online purchases and identifying a credit card as a source of money.

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<sup>1</sup> Stable sources of financing include amounts due to customers (including funds from the issue of Eurobonds) and external financing in the form of: subordinated liabilities, issue of own debt securities and amounts due to financial institutions.

<sup>2</sup> The data of The Polish Bank Association.

<sup>3</sup> According to the data provided by the Center of Sureties and Guarantees in Bank Gospodarstwa Krajowego.



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- A new payment method to be used in public administration agencies – by bank transfer initiated with a BLIK code from the IKO application is an important innovation introduced by PKO Bank Polski SA in cooperation with the National Clearing House (Krajowa Izba Rozliczeniowa SA (KIR)) and Polish Payment Standard (Polski Standard Płatności Sp. z o.o. (PSP)). The method allows the acceptance of payments at any counter of the office, directly in the PC station of a clerk, using a dedicated application provided by KIR.

THE BANK'S GROUP IS THE LEADING PARTNER OF THE POLISH ENTREPRENEURSHIP DUE TO ITS EXTENSIVE OFFER AND PROFESSIONAL CUSTOMER SERVICE.

The Group offers comprehensive solutions, which respond to the individual needs of the businesses taking into account their size, industry and stage of development. The Group provides its business customers with professional tools, which facilitate conducting business activities. The Group adjusts its current product offer based on analyses of customer expectations in order to be able to match the increasing competition and to satisfy its customers demand for loans and other banking products. As part of the activities undertaken in the first half of 2017:

- an automatic link to the register of the Central Registration and Information on Businesses (CEIDG) maintained by the Ministry of Development was created for use when opening a business account. Due to collecting data directly from the CEIDG, opening a business account has become simpler and faster.
- PKO Bank Polski SA and Polskie Górnictwo Naftowe i Gazownictwo SA (PGNiG) signed an agreement on strategic cooperation with regard to transaction banking. The agreement enables PGNiG's retail customers to settle their gas bills free of charge in nearly 1.2 thousand branches and 0.8 thousand agencies of PKO Bank Polski SA across the country.
- an investment project of a modern waste incineration plant in Poznań, co-financed by PKO Bank Polski SA, was completed. This is the largest investment project executed under public private partnership in Poland. The project is executed by a company, of which a 50% shareholder is a company established within the structure of the Marguerite Fund (the 2020 European Fund for Energy, Climate Change and Infrastructure). PKO Bank Polski SA is one of this fund's six major investors. The incineration plant in Poznań has received many awards from the European Commission.
- the branch of PKO Bank Polski in the Czech Republic (with its registered office in Prague) began operations. Through its branch in the Czech Republic, PKO Bank Polski SA would like to become the bank of first-choice for Polish companies operating on the Czech Republic's market and a gateway for Czech Republic's companies entering into the Polish market. The PKO Bank Polski SA branch in the Czech Republic (with its registered office in the Czech Republic's capital) is the second largest branch of the Bank abroad, after the PKO Bank Polski SA branch in the Federal Republic of Germany (with its registered office in Frankfurt am Main).
- a mutual product of PKO Bank Polski and Korporacja Ubezpieczeń Kredytów Eksportowych (KUKE) 'Polisa na Świat' ('World Insurance Policy') has come onto the market and is available in the Bank's facilities throughout Poland. Thanks to this strategic cooperation between PKO Bank Polski SA and KUKE (PFR Group), the Bank supports Polish companies in their expansion abroad.
- the work on a legal merger of PKO Leasing SA with Raiffeisen-Leasing Polska SA (RLPL) has finished. The acquisition of Raiffeisen-Leasing Polska SA increased the scale of corporate financing, particularly in the small- and medium-sized enterprises (SME) sector. The full operational merger of the two companies is expected to take place at the turn of 2017 and 2018.

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### 1.3 DIRECTIONS OF DEVELOPMENT OF THE PKO BANK POLSKI SA GROUP

Mission  
Strategy of the PKO Bank Polski SA for the years 2016 - 2020  
Strategic goals  
Implementation of the strategy

The development directions of PKO Bank Polski SA are set out in the Strategy for the years 2016-2020 'We support the development of Poland and the Poles' (the Strategy), which was approved by the Supervisory Board on 3 November 2016.

#### WHO WE ARE – OUR MISSION

##### 'WE SUPPORT THE DEVELOPMENT OF POLAND AND THE POLES'

We have been providing financial solutions to our customers almost 100 years, therefore, we understand the needs of the Poles and Polish companies.



Bank Polski

Consequently we change, we invest in development and we implement modern technologies responsibly to enable our customers to manage their finances anywhere, any time. We are proud of our history and our Polish roots.

We wish to have a positive impact on Poland – people, companies, culture and environment. As one of the largest banks in Central and Eastern Europe we care about the interests of our shareholders, customers, employees and local communities in a responsible manner.

#### STRATEGY OF PKO BANK POLSKI SA FOR THE YEARS 2016 – 2020

The new Strategy is a response to the changing market environment and the need to adjust the organization to new challenges facing the banking sector and the Polish economy. The direction of the transformation of the Bank's business model will remain closely connected with the growing digitization of social life and the strategy for economic development of Poland.

The Strategy for the years 2016-2020 based on strong foundations developed in previous years. Thanks to the implementation of 'Lider' and 'Codziennie Najlepszy' strategies, PKO Bank Polski SA strengthened its position as the unquestionable banking market leader in Poland, consistently developed the range and quality of e-banking and mobile banking (IKO) services, improved the processes and organizational efficiency, and built competence that will allow it to leverage growth through acquisitions.

#### STRATEGIC GOALS

By 2020, PKO Bank Polski SA intends to:

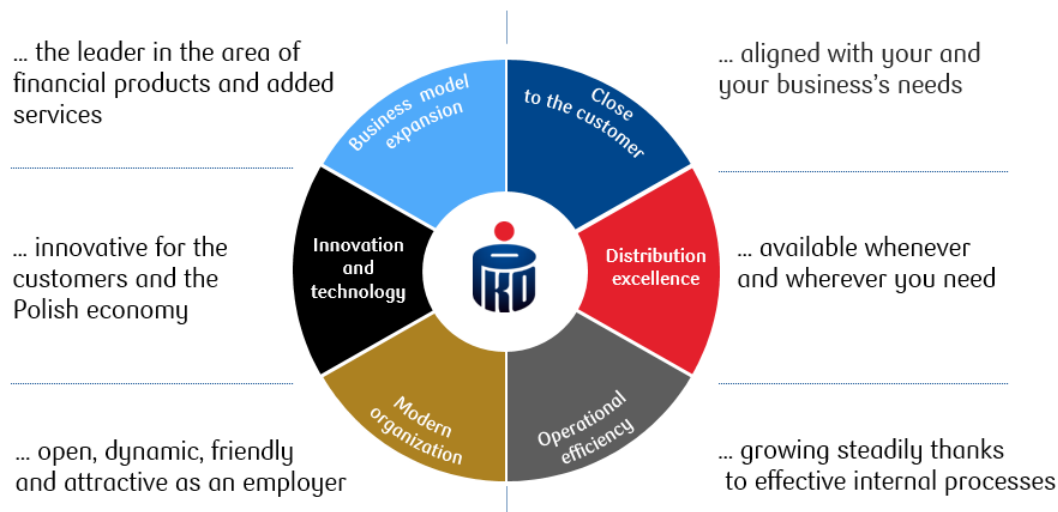
- achieve a return on equity (ROE) of more than 10%,
- reduce the cost to income (C/I) ratio to below 45%,
- maintain the cost of risk within the range of 75-85 b.p.,
- manage its capital adequacy in an efficient and reasonable manner, in order to maintain TCR and CET1 above the regulatory and supervisory requirements and, at the same time, allow the payment of dividend.

As the unquestionable banking market leader in Poland and the leader in all key market segments, the Bank shall address the following main strategic challenges by 2020:

1. supporting the development of Polish business, particularly in the small- and medium-sized enterprises segment,
2. increase of customer satisfaction,
3. increase in the number of customers using digital solutions,
4. process optimization – 'faster and paperless',
5. to be the best employer,
6. the development of innovation and search for the new sources of revenues,
7. to become a leader in the field of cooperation in the area of cyber security.

## IMPLEMENTATION OF THE STRATEGY

Thanks to the implementation of its Strategy, in 2020 PKO Bank Polski SA will be:



Strategy implementation is supported by six sustainable development levers:

### 1. CLOSE TO THE CUSTOMER

PKO Bank Polski SA will focus on supporting the development of the Polish business, particularly in the segment of small and medium-sized enterprises, as well as on customer satisfaction understood as building lasting relations with the Bank. This will be achieved through a simple and transparent offer, high quality advice, flexible pricing solutions, intuitive and fast sales processes, and a reduction in the volume of paper documentation.

### 2. DISTRIBUTION EXCELLENCE

Distribution channels will be developed based on the diagnosed needs of the customer to form a holistic model of multi-channel service system. The Bank will aim at providing consistent customer experience throughout all channels. These aims will be executed through the continued process of modernization of the network of branches playing a key role in building relations with customer and the market position, as well as further development of remote contact channels and an increase in the number and activity of customers using digital solutions.

### 3. OPERATIONAL EFFICIENCY

The Strategy involves the further improvement of internal processes. Decisions will be made in a fast and efficient manner with the use of high quality data analytics, process automation and dematerialization, innovative identification and authorization methods and preventing bureaucracy.

### 4. MODERN ORGANIZATION

A well-organized and motivated team will be the key to achieving strategic goals. The Strategy emphasizes the importance of creating a friendly, supportive and open working environment. It will be achieved through motivating leadership, modern knowledge management and promoting solutions that facilitate cooperation with the organization.

### 5. INNOVATION AND TECHNOLOGY

PKO Bank Polski SA will consistently invest in innovative solutions, actively engage in creating new market standards and innovative tools for customers and organizations, strengthen its role as a public trust institution and prevent cyber threats. The Bank will support the development of Polish innovators in the enterprise segment (micro, small, medium and corporate), and take part in projects with perspectives and become involved in areas and sectors of the future.

### 6. BUSINESS MODEL EXPANSION

This strategic lever will be implemented through the active monitoring of the domestic market for potential acquisitions, extending the availability of the offer of Group companies, international development supporting the expansion of the Bank's customer, alliances with strategic partners e.g. through loyalty platforms and cooperation with public institutions





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through e-State solutions. As part of its effort to become a leader in technological solutions, the Bank also plans to invest in selected new-technology companies.

The Bank will continue to combine creating value for the shareholders with social responsibility and sustainable development. In its daily work, it will integrate business goals with acting on behalf of all groups of stakeholders, at the same time pursuing social initiatives. The Bank's values and transparent communication will be the key foundations of building a dialogue with customers, employees, shareholders and the community.

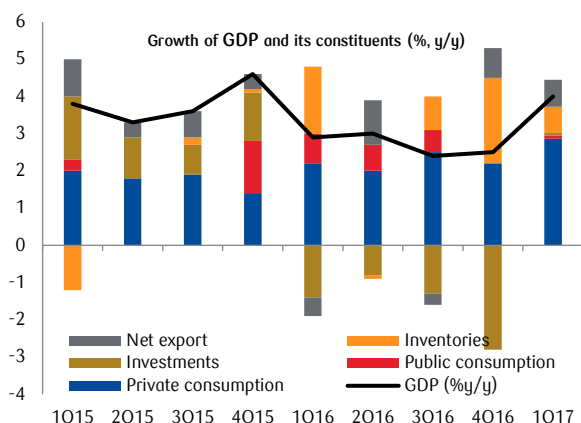
## 2. EXTERNAL BUSINESS ENVIRONMENT

- Macroeconomic environment
- Situation on the financial market
- Situation of the Polish banking sector
- Situation of the Polish non-banking sector
- The Ukrainian market
- Regulatory environment
- Factors that will affect the financial results of the Bank's Group in the second half of 2017

### 2.1 MACROECONOMIC ENVIRONMENT

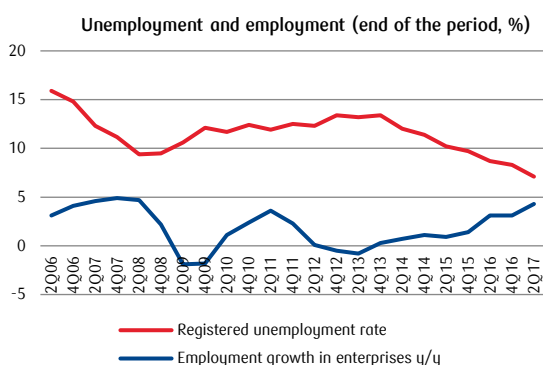
Macroeconomic factors influencing domestic economy in the first half of 2017:

- **CLEAR ACCELERATION OF ECONOMIC GROWTH**



Based on the monthly indicators of economic activity, GDP growth in the second quarter of 2017 may be estimated at approximately 3.7% y/y (vs 4.0% y/y in the first quarter of 2017, whereas changes in the GDP growth in subsequent quarters of 2017 mainly reflected the seasonality, not any changing trends), and was visibly higher than the growth rate in 2016. Private consumption stimulated by revival on the labour market and the 500+ programme, was the leading factor in the GDP growth. After a steep decline in 2016, there are symptoms of recovery in investments, among other things, the projected value of new investments, high level of lease activities (private investments), recovery of construction and assembly production, and an increase in the value of absorbed EU funds (public investments).

- **FURTHER IMPROVED LABOUR MARKET CONDITIONS**



The registered unemployment rate at the end of June went down to 7.1%, with a slight slow-down of the decline trend (to -1.6 p.p. y/y), which can be linked to the growing shortages of an effective labour force. The record low unemployment and record high number of vacancies result in the gradually growing pace of pay increases (in the business sector, it amounted to 4.6% y/y in January-June 2017, compared with 4.1% for the entire year of 2016), which improves the financial standing of households.

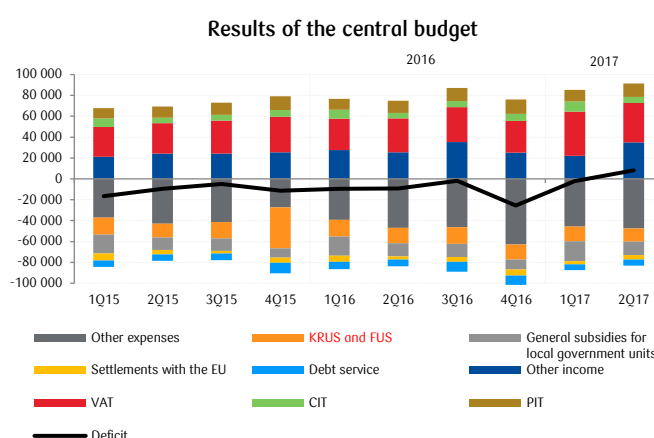
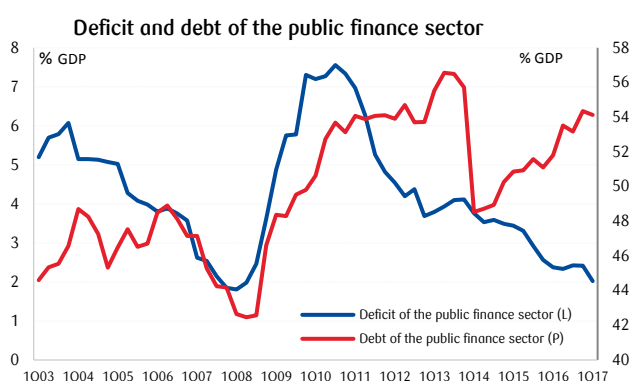
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**INFLATION WITHIN THE LIMIT OF THE NBP'S TARGET**

After a significant peak at the turn of the year (to 2.2% y/y in February), the CPI inflation rate slowed down to 1.5% y/y in June 2017, remaining within the admissible range of the NBP goal over the entire first half of the year. Prices of goods and fuels were the main drivers of changes in the CPI inflation rate. At the same time, the base inflation rate was in a moderately increasing trend. The recovery of the growth of prices after deflation in the previous years was not sufficiently strong to result in stronger market expectations of an increase in the NBP interest rates.

**RECORD SURPLUS OF THE STATE BUDGET**

At the end of June, the State budget recorded a surplus of PLN 5.9 billion, which is the best result in history in respect of such period. The contributing factors included: a cyclical increase in incomes, better collection of taxes, changes/postponements in tax payments schedules, low spending dynamics, and record distribution of the NBP profit. The fiscal deficit (according to the ESA) in the first quarter of 2017 went down to 2% GDP from 2.4% GDP in the first quarter of 2016, and was the lowest since 2008. In the same period, the public debt (according to the ESA) went down to 54.1% GDP from 54.4% GDP as at the end of 2016.



**MONETARY POLICY STABILIZATION**

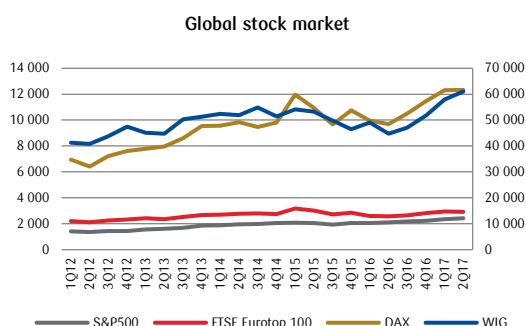
**NBP interest rates:**

- reference – 1.50%
- rediscount of bills – 1.75%
- lombard – 2.50%
- deposit – 0.50%

In the first half of 2017, the Monetary Policy Council (MPC) did not change the NBP's key interest rates. Combined with the marked increase in inflation, this led to real interest rates falling below zero. The tone of messages from members of the MPC, including the President of the NBP, indicates that interest rates will remain at an unchanged level not only until the end of 2017, but also over the major part of 2018.

**2.2 THE SITUATION ON THE FINANCIAL MARKET**

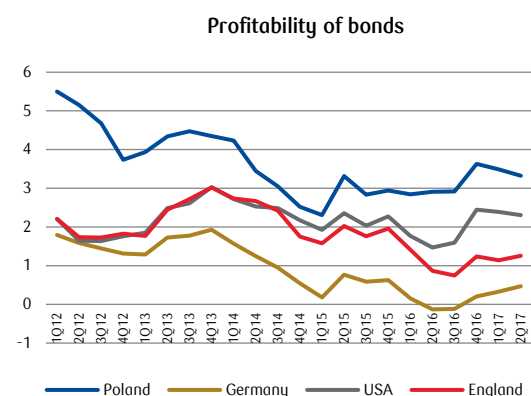
**STOCK MARKET**



The first half of 2017 proved to be very profitable for most on the global stock markets, including for the Warsaw exchange. WIG index increased by 18%, continuing the excellent positive trend started in mid-November of previous year. Particularly successful was the beginning of the year, while in the further part of the quarter side trend have been observed. The economic boom was owed thanks to the combination of global factors (good situation on international financial market) and local (positive data from domestic economy). The world stock exchanges grew on the back of the acceleration in economic growth combined with the restrained position of major central banks which signalled no rush in the tightening of the monetary policy. Similarly in Poland, the Monetary Policy Council of NBP toned down speculations regarding interest rate increases, despite the inflation recovery and very good economic situation. The combination of these factors created favourable conditions for investing in shares.

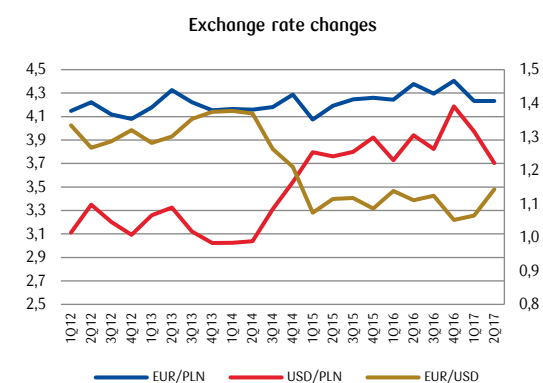
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**INTEREST RATE MARKET**



In the first half of 2017, a visible stabilization of the income curve was recorded on the Polish interest rate market. The spread between the 2-year and 10-year tenor on the Treasury bonds market narrowed to 141 b.p. at the end of June 2017 compared with 160 b.p. at the end of December 2016. This change was due to a stronger drop in the profitability of securities with longer maturity periods. The positive impact on the valuation of bonds at the short end of the curve resulted mainly from decreasing inflation expectations, low payroll pressure, as well as the NBP's declaration of maintaining interest rates unchanged for even as long as until the end of 2018. As a result, the profitability of 2-year Treasury securities dropped by 12 b.p. to 1.91%. Moreover, the valuation of 5-year and 10-year tenor bonds received support in the more moderate rhetoric of the main central banks worldwide, increase in political risk in Europe, and a global drop in commodity prices which resulted in lower inflation pressure worldwide. The easing concerns of an increase in interest rates in the USA resulted in an inflow of global capital to emerging markets. These changes led to a slight decrease in the profitability of 10-year Treasury securities of 31 b.p. to 3.33%.

**FOREIGN EXCHANGE MARKET**



The year 2017 began with a USD/EUR exchange rate at a level of 1.05, and in the first days of the new year it achieved 1.03. It was prevented from further reinforcement by the announcements of President of the USA, Donald Trump, who suggested that the US currency was 'too strong'. By the end of the first half of the year, the EUR/USD exchange rate gradually grew despite two interest rate increases in the USA (March, June) and relatively aggressive communications from the FED about, among other things, an imminent reduction in the trade balance. The main drivers of this situation included: (1) an improvement in the political climate in the Euro zone in connection with electoral successes of the mainstream parties, (2) waning trust of financial markets in the implementation of the economic programme announced by the President of the USA, Donald Trump, (3) speculations about the possibility of faster normalization of the monetary policy in the Euro zone in connection with messages from the ECB President, M. Draghi. As a result, the EUR/USD exchange rate as at the end of June 2017 was at a level of 1.14. From the beginning of the year, the PLN showed an upward trend against the EUR due to the improvement of investment moods in respect of emerging markets, related to robust economic information from China. As a result, the EUR/PLN exchange rate, which at the beginning of 2017 was around 4.40, ended the first half of 2017 at a level of 4.23.

**2.3 SITUATION OF THE POLISH BANKING SECTOR**

Financial result  
Statement of financial position

**FINANCIAL RESULT**

In the first half of 2017, the banking sector generated a net profit of PLN 6.9 billion, compared with PLN 8.3 billion in the first half of 2016. This represented a considerable drop in the net profit of 17% y/y, which nevertheless resulted mainly from a high reference level – in June 2016, banks generated revenue from Visa transactions whose impact on the net profit amounted to approx. PLN +2.0 billion (PLN 2.5 billion, gross). The financial results in the banking sector were supported by a favourable macroeconomic environment, including the acceleration of economic growth and good situation on the labour market.

The net profit of the banking sector was stimulated by strong growth in net interest income (+11.1% y/y) and net fee and commission income (+9.0% y/y). In turn, the following factors had a negative impact:

- decrease in the result of other business activities, with a high reference level from 2016 (among other things, the aforementioned impact of profits from Visa transactions and the sale of subsidiaries by some banks),

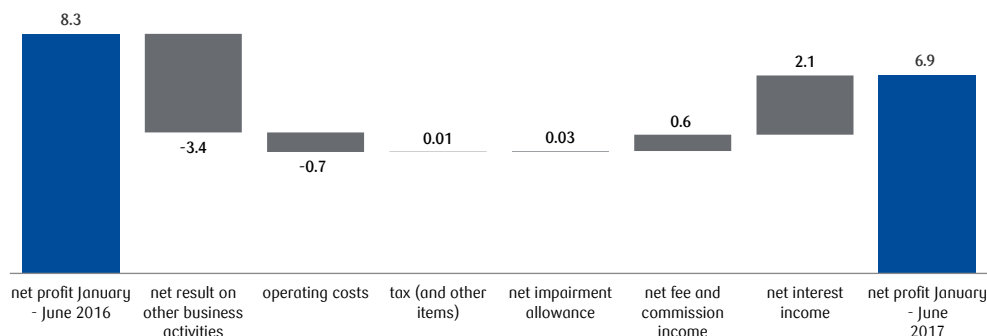


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- regulatory factors, including one-off charges levied on banks in respect of the Mandatory Restructuring Fund (in 2016, all contributions to BGF were settled on a straight-line basis) and an increase in the cost of the bank tax (which was implemented in February 2016).

Despite the favourable macroeconomic environment, the profitability (ROE<sup>4</sup>) of the banking sector was still at a relatively low level and amounted to 6.7% at the end of June 2017.

Change in the net profit of the banking sector (PLN billion)



Source: PFSA, the calculation of PKO Bank Polski SA; operating costs including the bank tax.

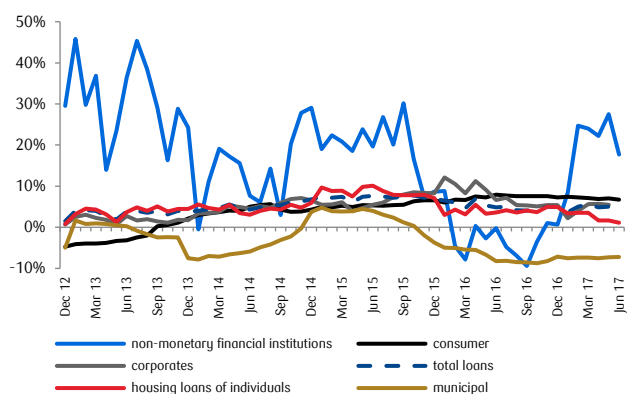
**STATEMENT OF FINANCIAL POSITION**

The continued economic recovery created favourable conditions for the stable growth of the banking sector. Total assets at the end of June 2017 went up to PLN 1 750 billion (+5.3% y/y compared with +7.0% y/y at the end of 2016), which was accompanied by a gradual acceleration of the growth rate of the volume of loans (after eliminating the foreign exchange rate impact) and the slowing pace in the growth of deposits.

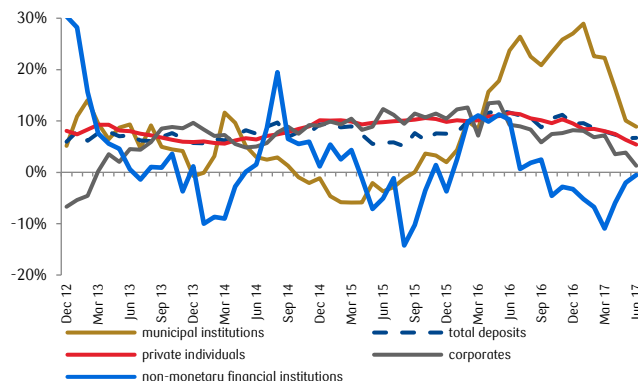
The good financial standing of households and low interest rates supported both the volume of consumer loans (+6.7% y/y at the end of the first half of 2017 compared with 7.3% y/y at the end of 2016), as well as housing loans denominated in PLN (+10.4% y/y compared with +10.5% y/y at the end of 2016). The increase in the volume of consumer loans was additionally supported by the continuing focus of banks on the sale of the most profitable products in the face of growing regulatory burdens. The slow-down of the growth rate of total housing loans for individual customers (1.1% y/y compared with 4.9% y/y at the end of 2016) resulted from a decrease in the volume of foreign currency housing loans for individual customers<sup>5</sup> (-11.5% y/y compared with -2.3% y/y at the end of 2016).

The growth rate of corporate loans increased in the first half of 2017 to 6.4% y/y (5.4% y/y at the end of 2016), which may reflect an increase in the demand from businesses for external financing.

The rate of change of loans in the banking sector (y/y)



The rate of change of deposits in the banking sector (y/y)



Source: NBP, calculations of PKO Bank Polski SA

<sup>4</sup> ROE – the net profit for the last 12 months to the average equity for the last 5 quarters

<sup>5</sup> The effect of appreciation y/y of Polish currency, without foreign currency loans granted by most banks and gradual repayment of remaining portfolio.



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In the first half of 2017, a decrease in the growth rate of deposits from individual customers to 5.4% y/y (from 9.5% y/y at the end of 2016) was recorded, which resulted from both the relatively high growth rate of private consumption and low interest rates on bank deposits, which encouraged seeking alternative forms of investing one's savings (investment funds, purchase of real properties for cash). At the same time, the share of current deposits in the structure of deposits of individual customers grew systematically (56% compared with 53% at the end of 2016), with an increasingly lower role of term deposits (44% compared with 47% at the end of 2016). In the first half of 2017 deposits of businesses also significantly slowed down to 1.3% y/y (from 8.2% y/y at the end of 2016), which could be related to growing investment activity.

Despite the slow-down at the end of the first half of 2017, the growth rate of deposits in the banking sector (6.7% y/y) was still higher than the growth rate of loans (4.6% y/y), and the excess of deposits over loans increased to PLN 21 billion compared with PLN 15 billion at the end of 2016. The loan/deposit ratio amounted to 98.2% (98.7% at the end of 2016).

## 2.4 SITUATION OF THE POLISH NON-BANKING SECTOR

### INVESTMENT FUNDS MARKET

In the first half of 2017, the assets of domestic investment funds grew by PLN 12.8 billion to PLN 271.9 billion which resulted from the robust increase in the first quarter and slight decline in the second quarter of 2017. The situation on the investment fund market was shaped by favourable conditions on the local stock market on the Warsaw Stock Exchange (WSE), stabilization of profitability on the debt market, historically low rates of return from bank deposits, and changes in the regulatory environment.

In the first half of 2017, the WIG index went up by 18%, which resulted in further growth of realized interest rates of 12M from investment funds with significant exposure to Polish stock. The majority of the main segments of the market of retail funds connected with the Polish stock market realized 12M return rates which were several times higher than average interest rates on new bank deposits. This was decisive for the attractiveness of instruments of the investment fund market as an alternative to depositing savings of households on the bank market and therefore stimulated an increase in the share of investment funds in their savings.

The increase in assets of investment funds in the first half of 2017 resulted mainly from a still increasing net inflow of funds from individual customers (PLN +7.3 billion compared with PLN +4.8 billion in the second half of 2016 and PLN +0.2 billion in the first half of 2016), a net outflow of funds of other investors (PLN -2.3 billion) and the positive result of management (PLN +6.9 billion).

The high net inflow of new funds from individual customers resulted in an increase in the share of their assets in the structure of total assets of investment funds from 50.6% as at the end of 2016 to 52.7% as at the end of the first half of 2017.

### OPEN PENSION FUNDS MARKET

In the first half of 2017 OFE was influenced by the improvement in labour market conditions, regulatory changes (including changes in the structure of the OFE investment portfolio) and improved conditions on the Warsaw Stock Exchange.

In the first half of 2017, assets of open pension funds increased to PLN 174.7 billion (+13.8%) compared with a decrease in the first half of 2016 (-4.0%). In the structure of OFE, the domestic equity instruments (mainly shares) maintained their dominant stable position (79.2%; an increase of 0.6 p.p. y/y). At the same time, the number of participants of Open Pension Funds continued to decline (by -80 thousand y/y to 16.3 million members).

### LEASING MARKET

In the first half of 2017 leasing market continued dynamic development, although its growth rate somewhat slowed. According to data of the Polish Leasing Association, leasing sector financed assets for the total amount of PLN 31.8 billion, at the rate of growth on the level of 11.6% y/y (against a growth of 16.6% y/y at the end of 2016).

The largest positive impact on the growth of the leasing market had leasing of passenger, commercial and heavy-duty vehicles to 3.5 tonnes (so-called light vehicles). The value of financed assets in this segment amounted to PLN 14.1 billion (+17.4% y/y), which accounted for ca. 44% of total funding granted by leasing companies.

The lease of machinery and equipment was the second rapidly developing segment with a high, double-digit growth (20.5% y/y), with the total value of new contracts at a level of PLN 8.1 billion. The high growth rate of this segment resulted, among other things, from a low reference level from the previous year, connected with limited investments of companies in view of the low absorption of EU funds from the perspective of the period 2014-2020. In the analysed period increased the financing of properties also increased (+11.1% y/y),

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but this segment continued to play a marginal role in the financing of investments by the leasing sector (1.2% of the total financing granted by lease companies).

In the first half of 2017, the lease market recorded a decline in respect of the financing of heavy transport vehicles (-2.4% y/y), with a value of leased-out assets of PLN 8.7 billion. In this segment, the steepest decline was noted in the bus financing segment (-11.9% y/y) as well as the financing of air, water and railway transport (-11.1% y/y).

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#### INSURANCE MARKET

In the first quarter of 2017, the main changes on the insurance market were due to demographic phenomena that resulted in an increase in the claims rate of protective products in the life insurance segment (Section I), improvement of y/y profitability of motor insurance and lower level of claims resulting from natural disasters in the segment of non-life insurance (Section II). The result of insurance companies obtained from investment activities was positively stimulated by the improved conditions on the local share market.

As at the end of the first quarter of 2017, the financial results of the insurance sector grew rapidly. The net profit increased by 67.5% y/y, reaching a level of PLN 1 024 million. This was the result of the very strong improvement in the net profit of the non-life insurance segment (PLN +539 million compared with PLN 33 million in the first quarter of 2016), and a decrease in the net profit of life insurance companies (PLN 485 million, -16% y/y).

Insurance companies recorded an increase in gross premiums written to PLN 16 billion (+18.4% y/y). This resulted from an increase in the premiums in both segments of the insurance market: +27.2% on the market of non-life insurance and +6.5% on the market of life insurance. At the same time, the value of damages recorded went up. In the first quarter of 2017, insurance companies recorded higher damages than in the previous year (+17.6% y/y). The increase was related to both the non-life insurance segment (+10.6% y/y), and life insurance segment (+23.2% y/y).

The costs of insurance activities went up y/y by 2.7%. This was the result of higher (y/y) costs of insurance activities of the non-life insurance segment (+6.5%), and a decrease (y/y) in the costs in the life insurance segment (-2.4%).

At the end of the first quarter of 2017, total assets of insurance companies as a whole increased to PLN 190 billion (+4.9% y/y), of which assets of the non-life insurance segment increased by +8.8%, and assets in the life insurance segment by +2.0%.

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#### FACTORING MARKET

In the first half of 2017, the factoring market showed a double-digit upward trend, although the growth rate slowed down. This is confirmed by data from 22 factoring companies which report to the Polish Factors Association. Their turnover reached PLN 83.6 billion, which means an increase of 13.6% y/y (20.6% y/y at the end of 2016). The rising awareness among businesses of the benefits which can be derived from factoring, the development of the banks' offer regarding various forms of financing operations that are an alternative to loans, as well as the increasingly better adaptation of the offer of factoring companies to the needs of even the smallest business entities – all this resulted in the continuation of the growth trend in respect of the number of customers serviced (+12.5% y/y to 8.1 thousand), and also the number of invoices financed (+17.4% y/y to approx. 4 million).

Customers of factoring companies primarily used full domestic factoring (without recourse). In this segment, the turnover grew by 25.1% y/y to a level of PLN 37.8 billion, which accounted for approx. 45% of the total turnover. Also domestic recourse factoring had a considerable share in the market structure, with a turnover of PLN 27.5 billion (+5.2% y/y).

The offering of export factoring enjoyed lesser popularity among enterprises, with the transaction volume of PLN 17.5 billion (+7.1% y/y). The share of import factoring was still marginal in the structure of market (1.0%).

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## 2.5 THE UKRAINIAN MARKET

### ECONOMIC SITUATION

In the first quarter of 2017, GDP of Ukraine grew by 2.5% y/y, and was affected by the trade blockade of Donbas (introduced informally in February 2017, and formally on 15 March 2017). In the period analysed, the growth of industrial production significantly decreased (3.6% in the fourth quarter of 2016 to -0.6% in the first quarter and -2.5% y/y on average in the period April-May), which implies that the GDP growth in the second quarter went down, even despite the visible acceleration of the growth of retail sale. The revival of consumption resulted primarily from the real wage growth due to an increase in the minimum pay (from UAH 1 500 to UAH 3 200) from January 2017, and lower inflation. The growth of real wages in the first half of 2017 oscillated at around 20% y/y.





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The improvement in the economic situation, increase in wages and salaries, and transfers from subordinated companies contributed to the record high surplus generated by the public financial sector in May 2017 (UAH 49.8 billion, 2.0% of GDP). The public debt (with guarantees) decreased to 78% of GDP from 81% of GDP, at the end of 2016. At the same time, the share of the Central Bank in the structure of Treasury securities went down – to the benefit of commercial banks.

The CPI inflation rate stabilized within the range of 12-16% y/y (15.6% in June 2017), whereas the increased price volatility still resulted from regulatory activities. The base inflation rate remained stable, within the range of 6-7% y/y. After a decline in January 2017, the USD/UAH exchange rate grew, and at the end of the first half of 2017 amounted to the level of 26.08 compared with 27.10 at the end of 2016. The reinforcement of UAH and stabilization of the basic inflation rate allowed the NBU to announce subsequent reductions in interest rates (on 13 April from 14.0% to 13.0%, and on 25 May to 12.5%).

**THE UKRAINIAN BANKING SECTOR**

According to the NBU data, the number of banks operating in Ukraine fell to 90 in May 2017 (compared with 96 in December 2016 and 102 in June 2016).

The value of total assets in the Ukrainian banking sector remained stable during first five months of the year at the level of approx. UAH 1.25 trillion. Equity has risen to UAH 151.1 billion from UAH 123.8 billion, acting at the end of May 2017 12.1% of total assets compared to 9.9% at the end of December 2016.

In the period January-May 2017 volume of loans decreased (by UAH 23.4 billion to UAH 1 002.7 billion). During analysed period decreased both corporate loans (UAH -34.3 billion) and household loans (UAH -3.5 billion), with an increase of non-resident loans. During analysed period value of bank deposits increased by UAH 17.6 billion to UAH 870.8 billion, combined with the decline in foreign currency loans volumes by UAH 13.2 billion. The main engine of deposits growth was public sector. LtD rate fell to 115.1% at the end of May 2017 from 120.3% in December 2016.

After the change in the classification of non-performing loans, their share in total loans amounts to 56.4% (the increase compared to the previously published value of approx. 22% results among other things from a rapid increase in write-downs on outstanding loans in the nationalized Privatbank). In the same period return ratios improved: ROA (1.3% vs -12.6%) and ROE (11.7% vs -116.7%). The capital adequacy ratio of the sector amounted to 12.4% as at the end of June 2017 (10% is the required level) compared with 12.7% as at the end of December 2016 and 12.5% at the end of June 2016.

**2.6 REGULATORY ENVIRONMENT**

In the first half of 2017 financial and organizational situation of the PKO Bank Polski SA Group was affected i.e. by the following:

**DEPOSIT GUARANTEE SYSTEM FEES**

Resolution No. 64/2016, 67/2016 and 15/2017 of the Bank Guarantee Fund ('BGF') Council for 2017, including: <ul style="list-style-type: none"> <li>the rules and terms of payment of contributions to the bank guarantee fund,</li> <li>the rate of bank's deposit guarantee fund,</li> </ul> and introduction of new charges, i.e. a contribution to the mandatory bank restructuring fund.	Impact on increase of costs of banks activity, including through the settlement in the first quarter of 2017 annual contribution to fund of compulsory banks restructuring.
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**PRUDENTIAL REQUIREMENTS**

Regulation of the European Parliament and the European Council No. 575/2013 on prudential requirements for credit institutions and investment companies changing the UE ordinance No. 648/2012, EBA technical standards and recommendations of the Polish Financial Supervision Authority (PFSA), in particular to increase the short-term liquidity rate LCR on 2017 to 80% from 70% in 2016.	Impact on the capital base of banks, supervisory prudential standards, business activity of banks.
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**RISK MANAGEMENT**

Recommendation C of the PFSA (PFSA Official Journal of 2016, item 15) changing the principles of managing the risk of loan concentration in universal and mortgage bank from 1 January 2017.	Impact on management of credit, market, operating and liquidity risk in banks.
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**INTERNAL CONTROL SYSTEM, RISK MANAGEMENT**

The regulation of the Minister of Development and Finance on the risk management system and internal control system, payroll policy and estimation of internal capital (Journal of Laws of 2017, item 637). Impact on the organization of the risk management system and internal control system.

**DE MINIMIS PROGRAMME**

Amendment (Journal of Laws of 2016, item 1471) to the regulation of the Minister of Finance concerning the provision of de minimis assistance in the form of loan repayment guarantees by Bank Gospodarstwa Krajowego which extended the operation of the De Minimis Programme for 2017 to 31 December 2017. Impact on the level of lending activities addressed to small and medium-sized enterprises.

**HOUSING LOANS**

- Recommendation 'S' of the PFSA on credit exposures secured with a mortgage (Official Journal of PFSA 2013, item 23), which increased the requirement for own borrower contribution from 15% to 20% since 1 January 2017.  
- the Act on state aid in acquiring a first apartment by young people (Journal of Laws of 2015, item 1865 with further amendments) setting out the maximum limit of support measures relating to co-financing under the 'Mieszkanie dla Młodych' programme in 2017.  
- preparation for the implementation, from 22 July 2017, of the Act on mortgage loans and supervision of mortgage loan intermediaries and agents (Journal of Laws of 2017, item 819), determining in particular the rules and procedures for concluding mortgage loan agreements. Impact on the level of lending, interest income and fee and commission income of the banks.  
Costs of implementation.

**WIND FARMS**

The Act on amendments to the Act on renewable energy sources and certain other Acts (Journal of Laws of 2016, item 925), and the Act on investments in wind power plants (Journal of Laws of 2016, item 961), which negatively affects the financial standing of wind farms, also through tax effects. Impact on the quality of the loan portfolio and the level of impairment allowances

**PAYMENTS THROUGH A BANK ACCOUNT**

The Act on Freedom of Economic Activity (Journal of Laws of 2015, item 584 with further amendments) decreasing, as of 1 January 2017, the limit of the value of transactions between entrepreneurs that must be settled through a bank account from EUR 15 thousand to PLN 15 thousand. Impact on deposits of corporate customers.

**TAXATION OF INVESTMENT FUNDS**

Amendment to the corporate income tax Act (Journal of Laws of 2016, item 1926) under which some close-ended investment fund with the CIT starting from 1 January 2017. Impact on the level of investment fund assets and the financial results of Investment Fund Companies.

**RESTRICTIONS FOR OPEN PENSION FUNDS (OPF)**

The Act on amending certain Acts in connection with the determination of the rules for payment of retirement benefits from resources accumulated in open pension funds (Journal of Laws of 2013, item 1717) which introduced, as of 1 January 2017, limits on the exposure of OPFs to shares in domestic companies (to 15% from 35% in 2016). Impact on the level of assets, business models and the financial results of OPFs.

The activity and results of the PKO Bank Polski SA Group influenced in the first half of 2017 new legislation introduced in the Ukraine (where operates, among others, a subsidiary KREDOBANK SA), including:

**DECREASE IN THE BASIC INTEREST RATES**

Resolutions of the Management Board of the Central Bank of Ukraine (NBU) No. 232/2017 and 318/2017 reducing the discount rate by 1 p.p. to 14% as of 14 April 2017, and by 0.5 p.p. to 12.5% as of 26 May 2017, respectively. Impact on business activities and net interest income.

**CASH SETTLEMENTS**

Decision of NBU No. 407/2016 reducing the maximum amount of cash settlements performed between private individuals and enterprises from UAH 150 thousand to UAH 50 thousand starting from 3 January 2017. Impact on the level of customer deposits and banks' income.



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**FOREIGN CURRENCY MANAGEMENT**

<p>- Decision of the NBU No. 7/2016 increasing the limits for purchases of foreign currencies on the interbank market since 9 February 2017. - Decision of the NBU No. 13/2017, 14/2017, 15/2017, 19/2017, 30/3017, 33/2017, 41/2017, 44/2017, among other, liberalizing the rules for trade in foreign currencies conducted by individuals and legal persons.</p>	<p>Impact on business activity of banks, foreign currency position management and the level of risk.</p>
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**CAPITAL REQUIREMENTS**

<p>Resolution No. 313/2015 of the Management Board of the NBU increasing the minimum capital adequacy ratio to 7% for 2017.</p>	<p>Impact on the capital base, supervisory prudential standards, business activity of the banks.</p>
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**COOPERATION WITH INTERMEDIARIES**

<p>NBU decision No. 50/2017 governing the rules of cooperation of banks with loan intermediaries.</p>	<p>Impact on the business activities of banks and the risk level.</p>
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**2.7 FACTORS THAT WILL AFFECT THE FINANCIAL RESULTS OF THE BANK'S GROUP IN THE SECOND HALF OF 2017**

The operations of the Bank's Group in the second half of 2017 will be influenced by the following external factors:

- continuation of favourable conditions in the global economy in particular in the Euro zone and in Germany,
- further tightening of the monetary policy in the USA and possible start of the normalization of the monetary policy by the European Central Bank,
- uncertainty as to the final form of Brexit,
- political uncertainty in Europe (the upcoming elections in Germany and Italy in view of strong Eurosceptical movements),
- implementation of the scenario of soft landing in China,
- increasing absorption of EU funds and revival of investment activities in the private sector,
- good consumer moods and further growth of real disposable incomes of households,
- increase of tension on the labour market resulting from strong demand for labour and limited supply (demographic factors, reduced retirement age), leading to reinforcement of the wage growth (and therefore growing costs of labour) and the risk of shortages of staff in some sectors;
- stabilization of the CPI inflation rate around a lower range of variation from the inflation goal,
- stabilization of the NBP interest rates, at least by mid-2018,;
- decline in deposits growth and an increase in the demand for loans, in particular corporate loans,
- political and economic situation in Ukraine,
- regulatory risk, in particular resulting from the resolution of the issue of currency loans, implementation of the Act on mortgage loan and supervision of mortgage loan intermediaries and agents effective from 22 July 2017, regulations concerning mortgage loans in foreign currencies (also in CHF), which will have an impact on increased capital requirements for banks which have such loans due to the increased risk and determination of the minimum LGD parameter.

### 3. FINANCIAL RESULTS OF THE PKO BANK POLSKI SA GROUP<sup>6</sup>

Key indicators  
Consolidated income statement  
Consolidated statement of financial position

#### 3.1 KEY FINANCIAL INDICATORS

The results achieved by the PKO Bank Polski SA Group in the first half of 2017, are represented by the following key financial efficiency indicators, which are shown in the table below.

Table 2. Financial indicators of the PKO Bank Polski SA Group

	30.06.2017	30.06.2016	Change (p.p.)
ROA net (net profit/average total assets)*	1.0%	1.1%	-0.1
ROE net (net profit/average total equity)*	8.4%	9.2%	-0.8
C/I (cost to income ratio)*	47.9%	53.1%	-5.2
Net interest margin (net interest income/average interest-bearing assets)*	3.2%	3.1%	0.1
Share of impaired loans**	5.7%	6.5%	-0.8
Cost of risk***	-0.74%	-0.70%	-0.04
Capital adequacy ratio (own funds/total capital requirement*12.5)	16.85%	15.21%	1.64

\* Income statement items used in calculating indicators capture the period of the last four quarters (annual recognition), while the statement of financial position items capture the average of the last five quarterly values of the respective assets and liabilities and equity.

\*\* Calculated by dividing the gross carrying amount of impaired loans and advances by the gross carrying amount of loans and advances to customers.

\*\*\* Calculated by dividing the net impairment allowance on loans and advances to customers over period of 12 months by average gross balance of loans and advances granted to customers at the beginning and end of reporting period and quarterly periods in between.

#### 3.2 CONSOLIDATED INCOME STATEMENT

Net interest income  
Net fee and commission income  
Net other income  
Administrative expenses  
Bank tax  
Net impairment allowance and write-downs

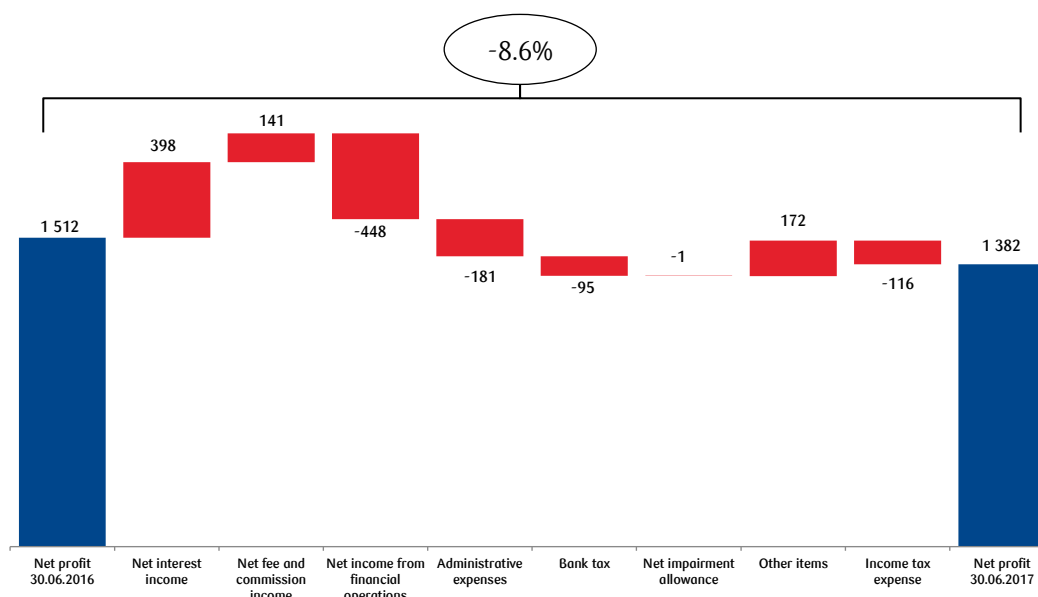
The consolidated net profit of the PKO Bank Polski SA Group generated in the first half of 2017 amounted to PLN 1 382 million and was lower by PLN 130 million than in the corresponding period of the previous year.

The following factors in particular had an impact on the annual change of the result:

- settlement, in June 2016, of the acquisition of *Visa Europe Limited* by *Visa Inc.*, which had an impact on the Bank's net result in the amount of approx. PLN 338 million,
- recognizing the entire annual contribution to the Mandatory Restructuring Fund of PLN 209 million in the first quarter of 2017,
- incomparability of charges connected with the bank tax, due to its implementation as of 1 February 2016.

<sup>6</sup> In this section, any differences in total balances, shares and growth rates result from rounding the amounts to PLN million and rounding percentages to one decimal place.

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In the PKO Bank Polski SA Group income statement for the first half of 2017, total income items amounted to PLN 6 101 million and was higher by PLN 270 million, i.e. 4.6% than in the analogical period of 2016, mainly due to an increase in net interest income and net fee and commission income, accompanied by a decrease in the net income on investment securities and an increase in general administrative expenses.

Table 3. Income statement of the PKO Bank Polski SA Group (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
Interest and similar income	5 313	4 852	461	9.5%
Interest expense and similar charges	-1 153	-1 090	-63	5.8%
<b>Net interest income</b>	<b>4 160</b>	<b>3 762</b>	<b>398</b>	<b>10.6%</b>
Fee and commission income	1 890	1 755	135	7.7%
Fee and commission expense	-447	-453	6	-1.3%
<b>Net fee and commission income</b>	<b>1 443</b>	<b>1 302</b>	<b>141</b>	<b>10.8%</b>
Dividend income	11	9	2	22.2%
Net income from financial instruments measured at fair value	13	-14	27	x
Gains less losses from investment securities	1	476	-475	-99.8%
Net foreign exchange gains (losses)	223	203	20	9.9%
Net other operating income and expense	250	93	157	2.7x
Net impairment allowance and write-downs	-783	-782	-1	0.1%
Administrative expenses	-2 938	-2 757	-181	6.6%
Tax on certain financial institutions	-464	-369	-95	x
<b>Operating profit</b>	<b>1 916</b>	<b>1 923</b>	<b>-7</b>	<b>-0.4%</b>
Share in profit (loss) of associates and jointly controlled entities	11	11	0	0.0%
<b>Profit before income tax</b>	<b>1 927</b>	<b>1 934</b>	<b>-7</b>	<b>-0.4%</b>
Income tax expense	-541	-425	-116	27.3%
<b>Net profit (including non-controlling shareholders)</b>	<b>1 386</b>	<b>1 509</b>	<b>-123</b>	<b>-8.2%</b>
Profit (loss) attributable to non-controlling shareholders	4	-3	7	x
<b>Net profit attributable to equity holders of the parent company</b>	<b>1 382</b>	<b>1 512</b>	<b>-130</b>	<b>-8.6%</b>

## NET INTEREST INCOME

Obtained in the first half of 2017 net interest income amounted to PLN 4 160 million and was PLN 398 million higher than in the first half of 2016. The improvement in the net interest income resulted from an increase in income connected with an increase in the loan portfolio and securities portfolio accompanied by a slight increase in interest expense.

Table 4. Interest income and expense of the PKO Bank Polski SA Group (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
<b>Interest and similar income on:</b>	<b>5 313</b>	<b>4 852</b>	<b>461</b>	<b>9.5%</b>
Loans and other advances to banks	63	54	9	16.7%
Loans and advances to customers	4 446	4 068	378	9.3%
Securities	661	545	116	21.3%
Derivative hedging instruments	143	182	-39	-21.4%
Other	0	3	-3	x
<b>Interest expense and similar charges on:</b>	<b>-1 153</b>	<b>-1 090</b>	<b>-63</b>	<b>5.8%</b>
Amounts due to banks	-79	-39	-40	2x
Amounts due to customers	-810	-795	-15	1.9%
Debt securities in issue and subordinated liabilities	-215	-195	-20	10.3%
Other*	-49	-61	12	-19.7%
<b>Net interest income</b>	<b>4 160</b>	<b>3 762</b>	<b>398</b>	<b>10.6%</b>

\* Including: costs of debt securities available for sale, trading financial assets, financial assets designated upon initial recognition at fair value through profit and loss.

In the first half of 2017, interest income amounted to PLN 5 313 million and in comparison with previous year was higher by PLN 461 million, mainly as a result of an increase in:

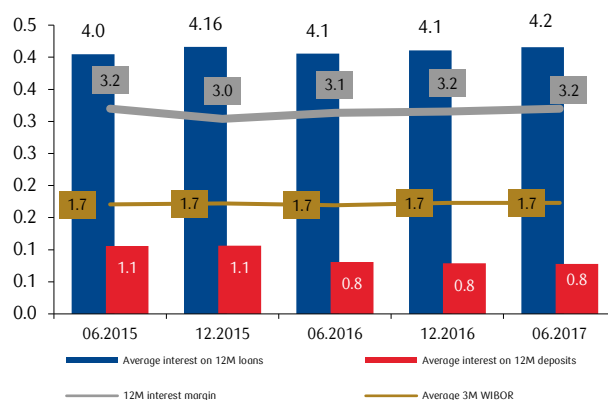
- income on loans and advances to customers by PLN 378 million y/y due to a 6.4% increase in the gross loan portfolio of retail segment, both for corporate, housing and consumer loans, as well as in lease receivables portfolio,
- income on securities of PLN 116 million y/y determined by an increase in the average volume of securities (mainly Treasury bonds),

In the first half of 2017, interest expense amounted to PLN 1 153 million and went up by 5.8% y/y, which resulted mainly from an increase in:

- costs of amounts due to banks of PLN 40 million y/y in respect of handling loans received from financial institutions,
- costs of amounts due to customers of PLN 15 million y/y, resulting from an increase in the deposits volume,
- costs of own issues due to an increase in the volume of covered bonds and own bonds issued by Bank Hipoteczny SA.

The interest margin increased by approx. 0.1 p.p. y/y to 3.2% at the end of June 2017. Average interest-bearing assets increased by 7.0% y/y (mainly the portfolio of loans and advances to customers and securities), and the annualized net interest income increased by 9.6%, mainly as a result of higher interest income on loans and securities (the effect of an increase in volume and profitability), accompanied by a stable level of interest expense.

At the end of June 2017, the average interest rate on loans of PKO Bank Polski SA amounted to 4.2% and the average interest rate on deposits in total stood at 0.8% against 4.1% and 0.8% in the first half of 2016 respectively.



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**NET FEE AND COMMISSION INCOME**

Net fee and commission income amounted to PLN 1 443 million in the first half of 2017 and was PLN 141 million higher than in the same period of the previous year, which resulted from PLN 135 million higher commission income and PLN 6 million lower commission expense.

Table 5. Fee and commission income and expense of the PKO Bank Polski SA Group (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
<b>Fee and commission income on:</b>	<b>1 890</b>	<b>1 755</b>	<b>135</b>	<b>7.7%</b>
debit and credit cards	521	503	18	3.6%
maintenance of bank accounts	434	438	-4	-0.9%
loans and advances granted	306	306	0	0.0%
maintenance of investment and open pension funds (including management fees)	274	216	58	26.9%
cash transactions	50	50	0	0.0%
servicing foreign mass transactions	50	41	9	22.0%
brokerage activities and issue arrangement	100	66	34	51.5%
offering insurance products	44	5	39	8.8x
sale and distribution of court fee stamps	3	5	-2	-40.0%
investment and insurance products	39	51	-12	-23.5%
other*	69	74	-5	-6.8%
<b>fee and commission expense on:</b>	<b>-447</b>	<b>-453</b>	<b>6</b>	<b>-1.3%</b>
card activities	-284	-285	1	-0.4%
commission paid to external entities for sales of products	-37	-33	-4	12.1%
cost of construction investment supervision and property valuation	-21	-20	-1	5.0%
settlement services	-17	-18	1	-5.6%
commission for operating services provided by banks	-10	-9	-1	11.1%
sending text messages (SMS)	-10	-7	-3	42.9%
assets management	-8	-8	0	0.0%
fees incurred by the Brokerage House	-11	-7	-4	57.1%
other	-49	-66	17	-25.8%
<b>Net fee and commission income</b>	<b>1 443</b>	<b>1 302</b>	<b>141</b>	<b>10.8%</b>

\*i.a. commissions for customer orders, fiduciary services, guarantees and letters of credit

The level of net fee and commission income was primarily determined by the following factors:

- commission income higher by PLN 58 million y/y due to handling investment funds and pension funds, as a result of the increased interest of customers in this form of savings as an alternative to low interest rates, which resulted in particular in an increase in sales commission and the repurchase of IF and management commission, with over 17% y/y growth in the value of IF's assets,
- increase in income from brokerage activities and organization of issue of PLN 34 million y/y, resulting from an increase in commissions from the securities exchange turnover, as a result of improved economic conditions on the WSE and increased activity of BH's customers, both in the retail and corporate customer segment – the value of BH turnover on the secondary stock market in the first half of 2017 accounted for 16% of the market turnover, and after elimination of intermediation in the sale of Pekao shares 9.8% vs 8.2% in the first half of 2016. Moreover, there was an increase in commissions from the role of an agent for the issue of Treasury bonds due to the increased interest of customers in this form of investing,
- increase in commissions from offering insurance products of PLN 39 million y/y, mainly as a result of sale of insurance products, in connection with the acquisition of a lease company,
- increase of PLN 18 million y/y in the net result from debit and credit cards due to a larger number of cards and higher non-cash transactions rate.

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## NET OTHER INCOME

In the first half of 2017 net other income amounted to PLN 498 million and decreased yearly by PLN 269 million. Net other income was mainly determined by the following:

- a decrease in gains less losses from investment securities by PLN 475 million y/y, which resulted from the reference base – in June 2016 the acquisition of *Visa Europe Limited* by *Visa Inc.* was settled, which affected the profit in the amount of PLN 418 million,
- improved result on the remaining operating activities of PLN 157 million, mainly due to the completion of a development project and start of handing over premises to customers in one of the companies in the Group, development of insurance companies activities (PKO Życie Towarzystwo Ubezpieczeń SA and PKO Towarzystwo Ubezpieczeń SA), and the higher contribution of lease activities.

Table 6. Net other income of the PKO Bank Polski SA Group (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)	
Dividend income	11	9	2	22.2%	
Net income from financial instruments measured at fair value	13	-14	27	x	
Gains less losses from investment securities	1	476	-475	-99.8%	
Net foreign exchange gains (losses)	223	203	20	9.9%	
Net other operating income and expense	250	93	157	2.7x	
<b>Net other income</b>	<b>498</b>	<b>767</b>	<b>-269</b>	<b>-35.1%</b>	

## ADMINISTRATIVE EXPENSES

In the first half of 2017, administrative expense amounted to PLN 2 938 million and were higher by 6.6% in comparison with the same period of previous year.

Their level resulted mainly from:

- an increase in contributions and payments to the BGF of PLN 86 million y/y, i.e. of 39.3%, due to the fact that the existing fees (mandatory and prudential) have been replaced with contributions for financing the deposit guarantee fund and for financing mandatory restructuring, calculated in accordance with new methodologies, and due to the recognition of the annual fee for financing mandatory restructuring in full amount in the first quarter of 2017,
- an increase in the costs of employee benefits of PLN 82 million, i.e. of 5.9%,
- an increase in amortization and depreciation costs of PLN 26 million, i.e. of 6.6%, accompanied by a decrease in overheads and taxes of PLN 13 million, i.e. of 1.7%.

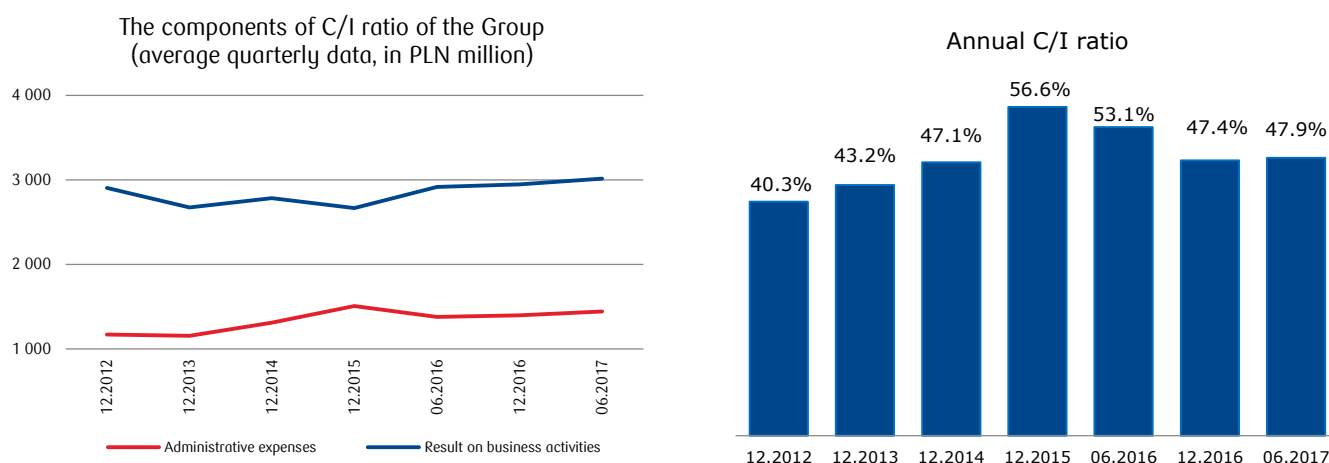
As at 30 June 2017, the number of employees in the PKO Bank Polski SA Group amounted to 28 825 FTE, which constituted a decrease of 42 FTE y/y.

Table 7. Administrative expenses of the PKO Bank Polski SA Group (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)	
Employee benefits	-1 482	-1 400	-82	5.9%	
Overheads	-691	-709	18	-2.5%	
Amortization and depreciation	-420	-394	-26	6.6%	
Contribution to the Bank Guarantee Fund (BGF)	-305	-219	-86	39.3%	
Taxes and other charges	-40	-35	-5	14.3%	
<b>Total</b>	<b>-2 938</b>	<b>-2 757</b>	<b>-181</b>	<b>6.6%</b>	

As at the end of June 2017, the effectiveness of the operations of the PKO Bank Polski SA Group measured with the annual C/I ratio amounted to 47.9% and improved by 5.2 p.p. y/y, both due to the improved result of business activities (+6.5% y/y), and due to a decrease in the level of administrative expenses (-4.0% y/y).

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### TAX ON CERTAIN FINANCIAL INSTITUTIONS

Pursuant to the Act, starting from 1 February 2016 banks and other financial institutions are obligated to pay tax on certain financial institutions. Tax burden on the Bank's Group in the first half of 2017 amounted to PLN 464 million, of which the majority was attributable to PKO Bank Polski SA (PLN 450 million). PKO Bank Polski SA remains the largest taxpayer of this tax in the banking sector.

### NET IMPAIRMENT ALLOWANCE AND WRITE-DOWNS

In the first half of 2017, the net impairment allowance and write-downs were at a similar level as in the first half of 2016 and amounted to PLN (-)783 million.

Table 8. Net impairment allowance of the PKO Bank Polski SA Group (in PLN million)

	01.01-30.06.2017	01.01-30.06.2016	Change (in PLN million)	Change (in %)
<b>Net impairment allowance, of which:</b>				
Loans and advances to customers	-750	-721	-29	4.0%
Investments in associates and jointly controlled entities	-13	-2	-11	6.5x
Other	-20	-59	39	-66.1%
<b>Total</b>	<b>-783</b>	<b>-782</b>	<b>-1</b>	<b>0.1%</b>

The share of impaired loans at the end of June 2017 was 5.7%, which represents a decrease of 0.8 p.p. y/y resulting from improvement in corporate loans quality. Improvement of the loan portfolio quality ratios accompanied by an increase in the gross loan portfolio of 6.4% y/y results from the continuation of the existing risk management policy of the Group and strict monitoring of the receivables portfolio.

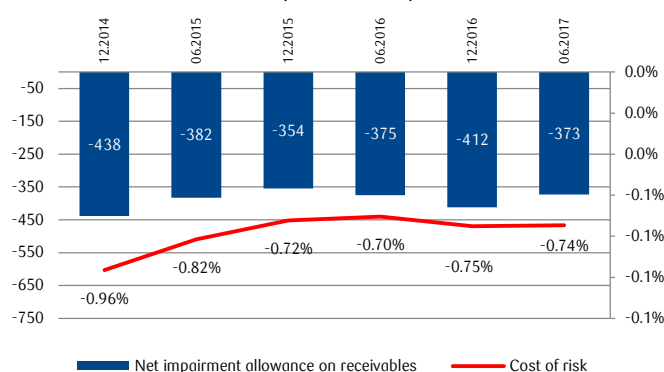
As at the end of June 2017, the cost of risk<sup>7</sup> was at a level of 0.74% and slightly deteriorated by 0.04 p.p. compared with the first half of 2016.

<sup>7</sup> Calculated by dividing the net impairment allowance on loans and advances to customers for the 12 months ended 30 June 2017 by the average balance of gross loans and advances to customers at the beginning and end of the reporting period and intermediate quarterly periods.

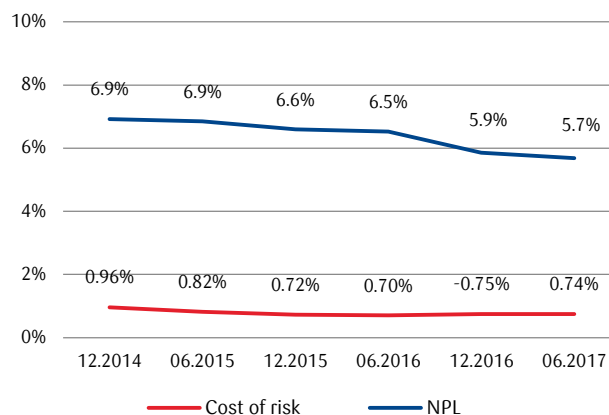


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**Net impairment allowance on the Group's receivables  
(interim data)**



**Costs of risk and the Group's NPL**



**3.3 CONSOLIDATED STATEMENT OF FINANCIAL POSITION**

Main items of the statement of financial position  
 Loans and advances to customers  
 Securities  
 Amounts due to customers  
 External financing  
 Equity and capital adequacy ratio

**MAIN ITEMS OF THE STATEMENT OF FINANCIAL POSITION**

The statement of financial position of the parent entity has the greatest impact on the statement of financial position of the PKO Bank Polski SA Group. It determines both the size of total assets and the structure of assets and equity and liabilities.

As at the end of June 2017, total assets of the Bank's Group amounted to PLN 286.4 billion, which represents an increase of PLN 0.8 billion since the beginning of the year.

The increase in the volume of loans and advances to customers of PLN 4.0 billion with a decrease of amounts due from banks and of the securities portfolio of PLN 2.0 billion y/y and PLN 0.6 billion, respectively had the key impact on the increase in assets of the Group. The increase in assets was financed mainly with an increase in amounts due to customers of PLN 2.2 billion y/y and an increase in equity of PLN 1.8 billion y/y, with a decrease in amounts due to banks.



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Table 9. Main items of the statement of financial position of the PKO Bank Polski SA Group (in PLN million)

	30.06.2017	31.12.2016	Change (in PLN billion)	Change (in %)
Cash and balances with the Central Bank	13 637	13 325	312	2.3%
Amounts due from banks	3 339	5 345	-2 006	-37.5%
Loans and advances to customers	204 620	200 606	4 014	2.0%
Securities	50 834	51 405	-571	-1.1%
Other assets	13 959	14 892	-933	-6.3%
<b>Total assets</b>	<b>286 389</b>	<b>285 573</b>	<b>816</b>	<b>0.3%</b>
Amounts due to banks	16 707	19 212	-2 505	-13.0%
Amount due to customers	207 248	205 066	2 182	1.1%
Liabilities due to insurance operations	3 031	2 944	87	3.0%
Debt securities in issue and subordinated liabilities	17 873	17 032	841	4.9%
Other liabilities	7 190	8 750	-1 560	-17.8%
<b>Total liabilities</b>	<b>252 049</b>	<b>253 004</b>	<b>-955</b>	<b>-0.4%</b>
Equity	34 340	32 569	1 771	5.4%
<b>Total liabilities and equity</b>	<b>286 389</b>	<b>285 573</b>	<b>816</b>	<b>0.3%</b>
Loans/Deposits	98.7%	97.8%		0.9 p.p.
Loans/Stable sources of financing*	85.2%	83.7%		1.5 p.p.
Interest bearing assets/Assets	90.4%	90.1%		0.2 p.p.
Interest paying liabilities/Liabilities	84.4%	84.5%		-0.1 p.p.

\* Stable sources of financing include amounts due to customers and external financing in the form of: issue of securities, subordinated liabilities and amounts due to financial institutions.

### LOANS AND ADVANCES TO CUSTOMERS

The gross loan portfolio consisted mainly of mortgage loans, which were at a level of PLN 108.0 billion at the end of June 2017. The increase in the loan portfolio of PLN 4.1 billion at the end of June 2017 compared with the end of 2016 resulted mainly from an increase in corporate loans (PLN +4.7 billion) and consumer loans (PLN +0.9 billion), accompanied by a decrease in the level of amounts due from repurchase agreements (PLN 1.2 billion) and a stable level of housing loans (increase in PLN loans accompanied by a decrease in housing loans as a result of currency exchange rate fluctuations). In the first half of 2017, the share of housing loans and advances in the structure of the gross loan portfolio amounted to 50.8%, business loans - 28.9% and consumer loans - 12.0%.

### SECURITIES

As at the end of June 2017, the Group's securities portfolio amounted to PLN 50.8 billion, which represented a decrease of PLN 0.6 billion compared with the end of 2016, and accounted for 17.7% of the Group's assets. In the structure of the portfolio by type, the main items were debt securities issued by the State Treasury, with a decrease in the share of NBP bills.

### AMOUNTS DUE TO CUSTOMERS

Amounts due to customers constitute the basic source of asset financing. They amounted to PLN 207.2 billion at the end of June 2017, and went up by PLN 2.2 billion compared with the beginning of the year. Amounts due to individual customers of PLN 149.9 billion (PLN +1.9 billion compared with the end of 2016) were the main item in the structure of amounts due to customers by type, and represented 72.3% thereof. Another significant category were the amounts due to corporate customers of PLN 48.0 billion (PLN -0.7 billion compared with the end of 2016), which accounted for a 23.1% share in the structure of amounts due to customers. The positive change in the customer deposit structure is due to an increase in the share of current deposits accompanied by a decrease in term deposits.



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## EXTERNAL FINANCING

The PKO Bank Polski SA Group is an active participant of the debt securities issuance market, both domestic and international. This activity is aimed at diversifying the sources of business financing and to adapt them to regulatory requirements.

As at the end of June 2017 the main item in these sources of financing constituted loans received from monetary financial institutions, including above all credit line from Nordea Bank AB (publ), being a part of the transaction of acquisition of the Nordea Group's assets by PKO Bank Polski SA in 2014 (received for the purpose of financing the acquired portfolio of mortgage loans). According to the agreement, from April 2017, the aforesaid financing is subject to gradual amortization.

Debt securities in issue were another significant category of long-term financing. Their increase of PLN 1.8 billion compared with the end of the year resulted mainly from the issue of covered bonds and own bonds by PKO Bank Hipoteczny SA, which was accompanied by a decrease in bonds issued by the Bank and Finance AB (FX effect).

The volume of subordinated liabilities decreased as a result of exercising the call option in respect of the earlier repayment of a subordinated loan of CHF 224 million.

Detailed information on issues conducted by the Group is provided in note 34 to the PKO Bank Polski SA Group's consolidated financial statements for the first half of 2017.

## 4. EQUITY AND ADEQUACY MEASURES

Equity and its profitability  
The capital adequacy measures  
Dividend

### 4.1 EQUITY AND ITS PROFITABILITY

Equity of the PKO Bank Polski SA Group amounted to PLN 34.3 billion and increased by 5.4% since the beginning of the year and accounted for 12% of liabilities and equity as at the end of June 2017.

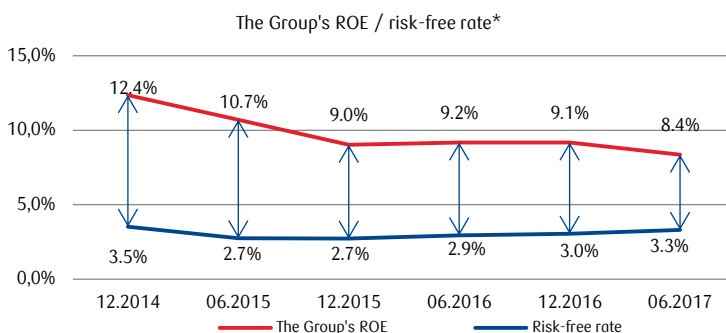
Table 10. Equity and capital adequacy ratio of the PKO Bank Polski SA Group (in PLN million)

	30.06.2017	31.12.2016	Change (in PLN million)	Change (in %)
<b>Equity, of which:</b>	<b>34 340</b>	<b>32 569</b>	<b>1 771</b>	<b>5.4%</b>
Share capital	1 250	1 250	0	0.0%
Reserve capital	27 374	24 491	2 883	11.8%
General banking risk fund	1 070	1 070	0	0.0%
Other reserves	3 646	3 608	39	1.1%
Cash flow hedges	-93	-109	16	-14.3%
Financial assets available for sale	35	-347	382	x
Currency translation differences from foreign operations	-233	-221	-12	5.4%
Undistributed profits	-66	-19	-47	3.5x
Net profit for the period	1 382	2 874	-1 492	-51.9%
Actuarial gains and losses	-11	-11	-1	4.8%
Non-controlling interest	-12	-16	4	-25.9%
Share in other comprehensive income of an associate	-2	-1	-1	2.5x
<b>Own funds</b>	<b>31 877</b>	<b>30 873</b>	<b>1004</b>	<b>3.3%</b>
<b>Capital adequacy ratio (%)</b>	<b>16.85%</b>	<b>15.81%</b>	<b>x</b>	<b>1.04 p.p.</b>



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Significant reinforcement of the capital base (an increase in average equity of 8.6% y/y), with the dynamics of the annualized financial result of (-)1.0% y/y translated into decrease of the return on equity ratio (ROE) to the level of 8.4 p.p versus 9.2 p.p. at the end of June 2016.



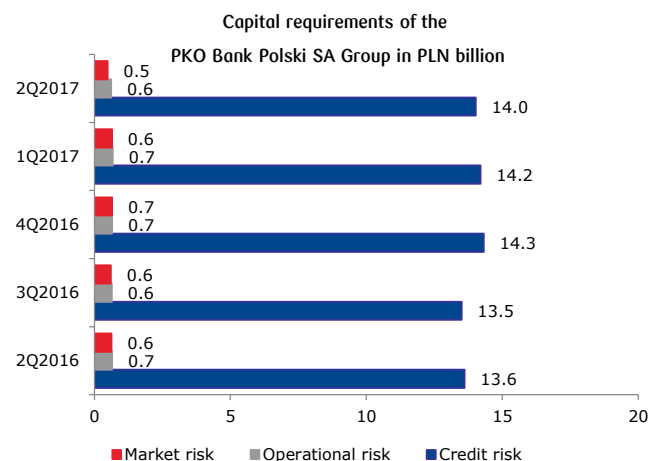
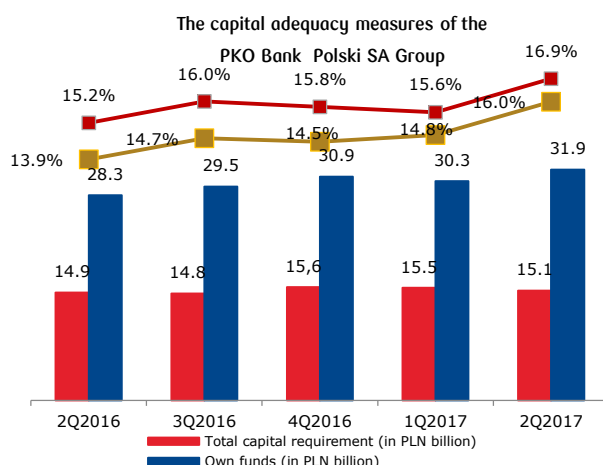
\* risk-free rate is calculated as the annual average of return of 10-year State Treasury bonds.

**4.2 THE CAPITAL ADEQUACY MEASURES**

The level of the PKO Bank Polski SA Group's capital adequacy in the first half of 2017 remained at a safe level, significantly above the supervisory limits. On 30 June 2017 the capital adequacy measures have been calculated based on the provisions of the CRR Regulation, taking into account the prudential consolidation.

In the first half of 2017 PKO Bank Polski SA Group continued efforts to provide adequate capital buffer, as well strengthen its capital position.

As at 30 June 2017 compared with 31 December 2016, the total PKO Bank Polski SA Group's capital adequacy ratio increased by 1.04 p.p. to the level of 16.85%, basic capital ratio Tier 1 by 1.49 p.p. to the level of 16.00%.



The increase in the adequacy ratios in the first half of 2017 was mainly determined by an increase in own funds of approx. PLN 1 billion as a result of retaining all profit of 2016, (part of which was already transferred to own funds in the previous year upon being granted the consent of the PFSA).

The decrease in the own funds requirement in the first half of 2017 of approx. PLN (-)0.5 billion compared with 31 December 2016 was caused by, among other things, a decrease in currency exchange rates.

**4.3 DIVIDEND**

The dividend policy of PKO Bank Polski SA assumes the realization of profit distributions over a long period in compliance with the principle of prudent management of the Bank and the Bank's Group, in line with the Bank's and Group's financial capabilities, taking into account the requirements and recommendations of the PFSA in respect of dividend policy. The applicable dividend policy provides a possibility of making payments from the excess of capital above the minimum Tier 1 ratio of 14.62%, which has been set by the Financial Supervision Authority for the purposes of dividend distribution by the Bank (current report 3/2017).



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On 9 March 2017, PKO Bank Polski SA received an individual recommendation from the Polish Financial Supervision Authority to retain the total profit generated in the period from 1 January 2016 to 31 December 2016. On 22 June 2017, the General Shareholders' Meeting of PKO Bank Polski SA passed a resolution (No. 7/2017) on the distribution of the net profit of PKO Bank Polski SA earned in 2016, in accordance with which the total profit in the amount of PLN 2 888 million was recognized in equity in the following manner:

- reserve capital in the amount of PLN 2 850 million,
- other reserves in the amount of PLN 38 million.

Retaining the profit for 2016 in the amount of PLN 2 888 million effectively caused an increase in equity of PLN 1 299 million, since a part of the profit earned in the period from January 2016 to September 2016 of PLN 1 589 million was already recognized in own funds with the PFSA approval in 2016.

## 5. FINANCIAL RESULTS OF PKO BANK POLSKI SA<sup>8</sup>

Key indicators  
Income statement  
Statement of financial position

### 5.1 KEY INDICATORS

The results achieved by PKO Bank Polski SA in the first half of 2017 are reflected in the key financial performance indicators, which levels are presented in the following table.

Table 11. Financial indicators of PKO Bank Polski SA

	30.06.2017	30.06.2016	Change (p.p.)
ROA net* (net profit/average total assets)	0.9%	1.1%	-0.2
ROE net* (net profit/average total equity)	7.8%	9.1%	-1.3
C/I (cost to income ratio)*	47.1%	51.2%	-4.1
Net interest margin* (net interest income/average interest-bearing assets)	3.1%	3.1%	0.0
Share of impaired loans**	5.7%	6.5%	-0.8
Cost of risk***	-0.74%	-0.69%	0.0
Capital adequacy ratio (own funds/total capital requirement*12.5)	18.82%	16.11%	2.71

\* Income statement items used in calculating indicators capture the period of the last four quarters (annual recognition), while the statement of financial position items capture the average of the last five quarterly values of the respective assets and liabilities.

\*\* Calculated by dividing the gross carrying amount of impaired loans and advances by the gross carrying amount of loans and advances to customers.

\*\*\* Calculated by dividing the net impairment allowance on loans and advances to customers by average gross balance of loans and advances to customers.

<sup>8</sup> In this chapter, any differences in total balances, percentages and dynamics result from rounding the amounts to PLN million and rounding percentages to one decimal place.



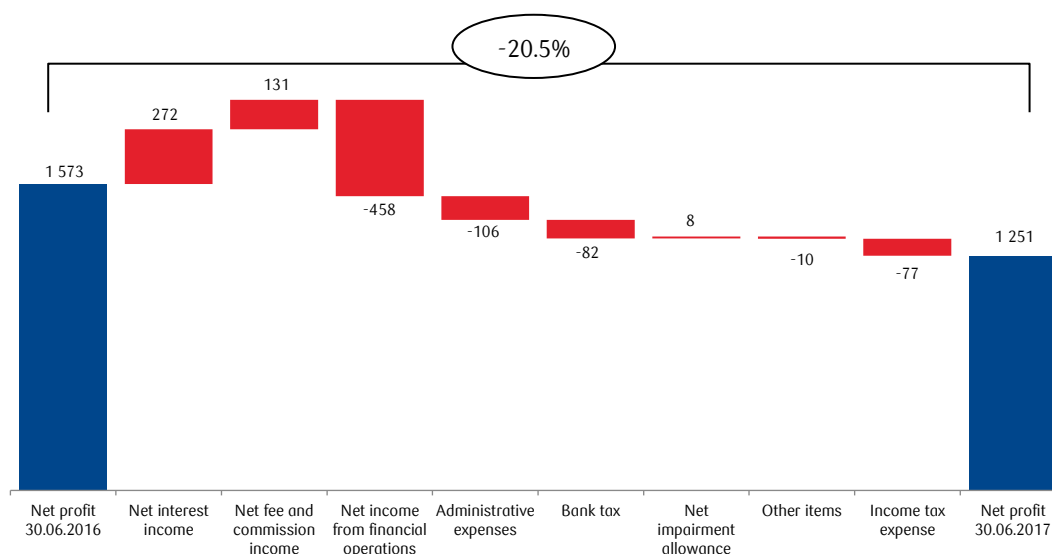
## 5.2 INCOME STATEMENT

Net interest income  
Net fee and commission income  
Net other income  
Administrative expenses  
Bank tax  
Net impairment allowance and write-downs

In the first half of 2017, PKO Bank Polski SA realized net profit of PLN 1 251 million (-20.5% y/y), mainly due to a decrease in net income on financial instruments (the effect of a high reference base in the first half of 2016), an increase in the burden of the bank tax and an increase in contributions to the BGF, whereas at the same time the net interest income and net fee and commission income increased.

The following events had a significant impact on the annual change in net income:

- settlement, in June 2016, of the acquisition of *Visa Europe Limited* by *Visa Inc.*, in which PKO Bank Polski SA participated; the respective net result of the Bank on this transaction was recognized in the amount of approx. PLN 338 million,
- recognizing the entire contribution to the Mandatory Bank Restructuring Fund of PLN 209 million in the first quarter of 2017,
- incomparability of charges related to the tax on certain financial institutions due to its coming into effect as of February 2016.



In PKO Bank Polski SA income statement for the first half of 2017, the sum of revenue positions amounted to PLN 5 524 million and was by PLN 65 million, i.e. by 1.2% lower than in the first half of 2016, mainly due to a decrease in net income on investment securities of PLN 478 million, accompanied by an increase in net interest income and net fee and commission income.

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Table 12. Income statement of PKO Bank Polski SA (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
Interest and similar income	4 924	4 648	276	5.9%
Interest expense and similar charges	-1 057	-1 053	-4	0.4%
<b>Net interest income</b>	<b>3 867</b>	<b>3 595</b>	<b>272</b>	<b>7.6%</b>
Fee and commission income	1 753	1 611	142	8.8%
Fee and commission expense	-437	-426	-11	2.6%
<b>Net fee and commission income</b>	<b>1 316</b>	<b>1 185</b>	<b>131</b>	<b>11.1%</b>
Dividend income	124	149	-25	-16.8%
Net income from financial instruments measured at fair value	2	-18	20	x
Gains less losses from investment securities	-1	477	-478	x
Net foreign exchange gains (losses)	204	210	-6	-2.9%
Net other operating income and expense	12	-9	21	x
Net impairment allowance	-745	-753	8	-1.1%
Administrative expenses	-2 604	-2 498	-106	4.2%
Tax on certain financial institutions	-450	-368	-82	22.3%
<b>Operating profit</b>	<b>1 725</b>	<b>1 970</b>	<b>-245</b>	<b>-12.4%</b>
<b>Profit (loss) before income tax</b>	<b>1 725</b>	<b>1 970</b>	<b>-245</b>	<b>-12.4%</b>
Income tax expense	-474	-397	-77	19.4%
<b>Net profit (loss)</b>	<b>1 251</b>	<b>1 573</b>	<b>-322</b>	<b>-20.5%</b>

## NET INTEREST INCOME

The net interest income generated in the first half of 2017 amounted to PLN 3 867 million and was PLN 272 million higher than in the same period of the previous year. The improvement in the net interest income resulted from an increase in revenue connected with an increase in the loan portfolio and securities portfolio, with a similar level of interest expense.

Table 13. Interest income and expense of PKO Bank Polski SA (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
<b>Interest and similar income on:</b>	<b>4 924</b>	<b>4 648</b>	<b>276</b>	<b>5.9%</b>
Loans and other advances to banks	96	66	30	45.5%
Loans and advances to customers	4 022	3 878	144	3.7%
Securities	630	519	111	21.4%
Derivative hedging instruments	176	182	-6	-3.3%
Other	0	3	-3	x
<b>Interest expense and similar charges on:</b>	<b>-1 057</b>	<b>-1 053</b>	<b>-4</b>	<b>0.4%</b>
Amounts due to banks	-65	-43	-22	51.2%
Amounts due to customers	-901	-903	2	-0.2%
Debt securities in issue and subordinated liabilities	-42	-47	5	-10.6%
Other*	-49	-60	11	-18.3%
<b>Net interest income</b>	<b>3 867</b>	<b>3 595</b>	<b>272</b>	<b>7.6%</b>

\* including: costs of debt securities available for sale, trading financial assets, financial assets designated upon initial recognition at fair value through profit and loss.

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## NET FEE AND COMMISSION INCOME

The net fee and commission income in the first half of 2017 amounted to PLN 1 316 million and increased by PLN 131 million compared with the previous year. The improvement in the net result was due to an increase in revenue, among other things, related to the handling of investment funds, brokerage activities and organization of issues, as well as in respect of lending activities and offering insurance products, which was accompanied by a decrease in commission and fee expense.

Table 14. Fee and commission income and expense of PKO Bank Polski SA (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
<b>Fee and commission income on:</b>	<b>1 753</b>	<b>1 611</b>	<b>142</b>	<b>8.8%</b>
Debit and credit cards	514	499	15	3.0%
Maintenance of bank accounts	424	431	-7	-1.6%
Loans and advances granted	322	306	16	5.2%
Offering insurance products	46	24	22	91.7%
Maintenance of investment and open pension funds (including management fees)	180	129	51	39.5%
Cash transactions	44	46	-2	-4.3%
Servicing foreign mass transactions	50	41	9	22.0%
Brokerage activities and issue arrangement	102	68	34	50.0%
Investment and insurance products	8	7	1	14.3%
Sale and distribution of court fee stamps	3	5	-2	-40.0%
Other*	60	55	5	9.1%
<b>Fee and commission expense on:</b>	<b>-437</b>	<b>-426</b>	<b>-11</b>	<b>2.6%</b>
Card activities	-280	-282	2	-0.7%
Commission paid to external entities for sales of products	-44	-41	-3	7.3%
Cost of construction investment supervision and property valuation	-21	-20	-1	5.0%
Settlement services	-17	-18	1	-5.6%
Commission for operating services provided by banks	-9	-8	-1	12.5%
Sending text messages (SMS)	-10	-7	-3	42.9%
Fees incurred by the Brokerage House	-11	-7	-4	57.1%
Other	-45	-43	-2	4.7%
<b>Net fee and commission income</b>	<b>1 316</b>	<b>1 185</b>	<b>131</b>	<b>11.1%</b>

\*i.a. commissions for customer orders, fiduciary services, guarantees and letters of credit

## NET OTHER INCOME

In the first half of 2017, net other income amounted to PLN 341 million and went down PLN 468 million y/y. The level of net other income was mainly determined by the decrease in net income on investment securities of PLN 478 million y/y, which resulted from the reference base – in June 2016 the acquisition of *Visa Europe Limited* by *Visa Inc.* in which PKO Bank Polski SA participated, was settled; in this respect, the amount of PLN 418 million was recognized in the Bank's net result.

Table 15. Net other income of PKO Bank Polski SA (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
Dividend income	124	149	-25	-16.8%
Net income from financial instruments measured at fair value	2	-18	20	x
Gains less losses from investment securities	-1	477	-478	x
Net foreign exchange gains (losses)	204	210	-6	-2.9%
Net other operating income and expense	12	-9	21	x
<b>Net other income</b>	<b>341</b>	<b>809</b>	<b>-468</b>	<b>-57.8%</b>

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## ADMINISTRATIVE EXPENSES

In the first half of 2017, administrative expenses amounted to PLN 2 604 million and were higher by PLN 106 million.

Table 16. Administrative expenses of PKO Bank Polski SA (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
Employee benefits	-1 316	-1 281	-35	2.7%
Overheads	-594	-616	22	-3.6%
Amortization and depreciation	-363	-358	-5	1.4%
Contribution to the Bank Guarantee Fund (BGF)	-305	-218	-87	39.9%
Taxes and other charges	-26	-25	-1	4.0%
<b>Total</b>	<b>-2 604</b>	<b>-2 498</b>	<b>-106</b>	<b>4.2%</b>

The level of administrative expenses was determined mainly by:

- an increase in contributions to the BGF of PLN 87 million, i.e. of 39.9%, as described in section 3.2 hereof,
- an increase in the employee benefits expense of PLN 35 million, i.e. of 2.7%,
- an increase in the amortization and depreciation expense of PLN 5 million, i.e. of 1.4%,
- a decrease in overheads and taxes of PLN 22 million, i.e. of 3.6%,

As at 30 June 2017, the number of employees in PKO Bank Polski SA amounted to 24 725 FTE, which constituted a decrease of 718 FTE y/y.

The business effectiveness of PKO Bank Polski SA as measured by the C/I ratio on an annual basis was 47.1% and improved by 4.1 p.p. y/y, due to both an increase in the operating profit (+1.4% y/y) and a decrease in the level of administrative expenses incurred (-6.7% y/y).

## TAX ON CERTAIN FINANCIAL INSTITUTIONS

By virtue of law, starting from February 2016 banks and other financial institutions are obliged to pay tax on certain financial institutions. Tax burden on PKO Bank Polski SA in the first half of 2017 amounted to PLN 451 million. PKO Bank Polski SA remains the largest taxpayer of this tax in the banking sector.

## NET IMPAIRMENT ALLOWANCE AND WRITE-DOWNS

In the first half of 2017, the net impairment allowance and write-downs were at the similar level as in the first half of 2016 and reflected the prudent approach of PKO Bank Polski SA to the recognition and valuation of credit risk.

Table 17. Net impairment allowance of PKO Bank Polski SA (in PLN million)

	01.01- 30.06.2017	01.01- 30.06.2016	Change (in PLN million)	Change (in %)
<b>Net impairment allowance, of which:</b>				
Loans and advances to customers	-693	-702	9	-1.3%
Other	-52	-51	-1	2.0%
<b>Total</b>	<b>-745</b>	<b>-753</b>	<b>8</b>	<b>-1.1%</b>

As at the end of June 2017, the ratio of impaired loans amounted to 5.7% (a decrease of 0.8 p.p. y/y) due to the improvement in the quality of corporate loans.

In the first half of 2017, the cost of risk<sup>9</sup> was at a level of -0.74% and slightly deteriorated by 0.06 p.p. compared with the end of the first half of 2016.

<sup>9</sup> Calculated by division of net impairment allowance and write-downs of loans and advances to customers for 12 month period ended 30 June 2017 by the average, gross balance of loans and advances to customers at the beginning and at the end of reporting period and quarterly periods in between.





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### 5.3 STATEMENT OF FINANCIAL POSITION

The total assets of PKO Bank Polski SA decreased by PLN 2.2 billion (-0.8%) compared with the end of 2016, and at the end of June 2017 it was at a level of PLN 270.8 billion. The decrease resulted mainly from a decrease in the level of amounts due to banks and the level of debt securities in issue and subordinated liabilities, partly compensated by an increase in the deposit and capital base. Despite lower total assets, PKO Bank Polski SA maintained its position as the largest financial institution in the Polish banking sector.

In terms of assets, the largest increases were recorded in the portfolio of loans and advances to customers (PLN +1.5 billion), which constituted the most significant part of the assets of PKO Bank Polski SA, and reached a 70.4% share in total assets.

In the first half of 2017, the process of transferring PLN housing loans to PKO Bank Hipoteczny SA was continued, and the total value of the loan portfolio transferred in the first half of 2017 amounted to PLN 2.2 billion. Moreover, the level of housing loans was affected by the appreciation of the Polish zloty against the Swiss franc and the euro.

The main source of assets financing are still amounts due to customers, which amounted to PLN 211.3 billion at the end of June 2017 (PLN +1.9 billion compared to the end of 2016) with 78.0% share in total liabilities. A significant increase in amounts due to customers is associated with maintaining a secure balance sheet structure of PKO Bank Polski SA.

Table 18. Main items of the statement of financial position of PKO Bank Polski SA (in PLN million)

	30.06.2017	31.12.2016	Change (in PLN million)	Change (in %)
Cash and balances with the Central Bank	13 568	13 277	291	2.2%
Amounts due from banks	5 977	8 471	-2 494	-29.4%
Loans and advances to customers	190 556	189 067	1 489	0.8%
Securities	47 418	48 032	-614	-1.3%
Other assets	13 270	14 110	-840	-6.0%
<b>Total assets</b>	<b>270 789</b>	<b>272 957</b>	<b>-2 168</b>	<b>-0.8%</b>
Amounts due to banks	16 501	18 721	-2 220	-11.9%
Amount due to costumers	211 264	209 371	1 893	0.9%
Debt securities in issue and subordinated liabilities	2 282	4 232	-1 950	-46.1%
Other liabilities	6 519	8 044	-1 525	-19.0%
<b>Total liabilities</b>	<b>236 566</b>	<b>240 368</b>	<b>-3 802</b>	<b>-1.6%</b>
Total equity	34 223	32 589	1 634	5.0%
<b>Total liabilities and equity</b>	<b>270 789</b>	<b>272 957</b>	<b>-2 168</b>	<b>-0.8%</b>
Loans/Deposits (amounts due to customers)	90%	90%	x	-0.1 p.p.
Loans/Stable sources of financing*	83%	82%	x	1.5 p.p.
Interest bearing assets/Assets	90%	90%	x	0.1 p.p.
Interest paying liabilities/Liabilities	85%	85%	x	-0.2 p.p.

\*Stable sources of financing include amounts due to customers and external financing in the form of: own issue of securities (including covered bonds) and amounts due to financial institutions.

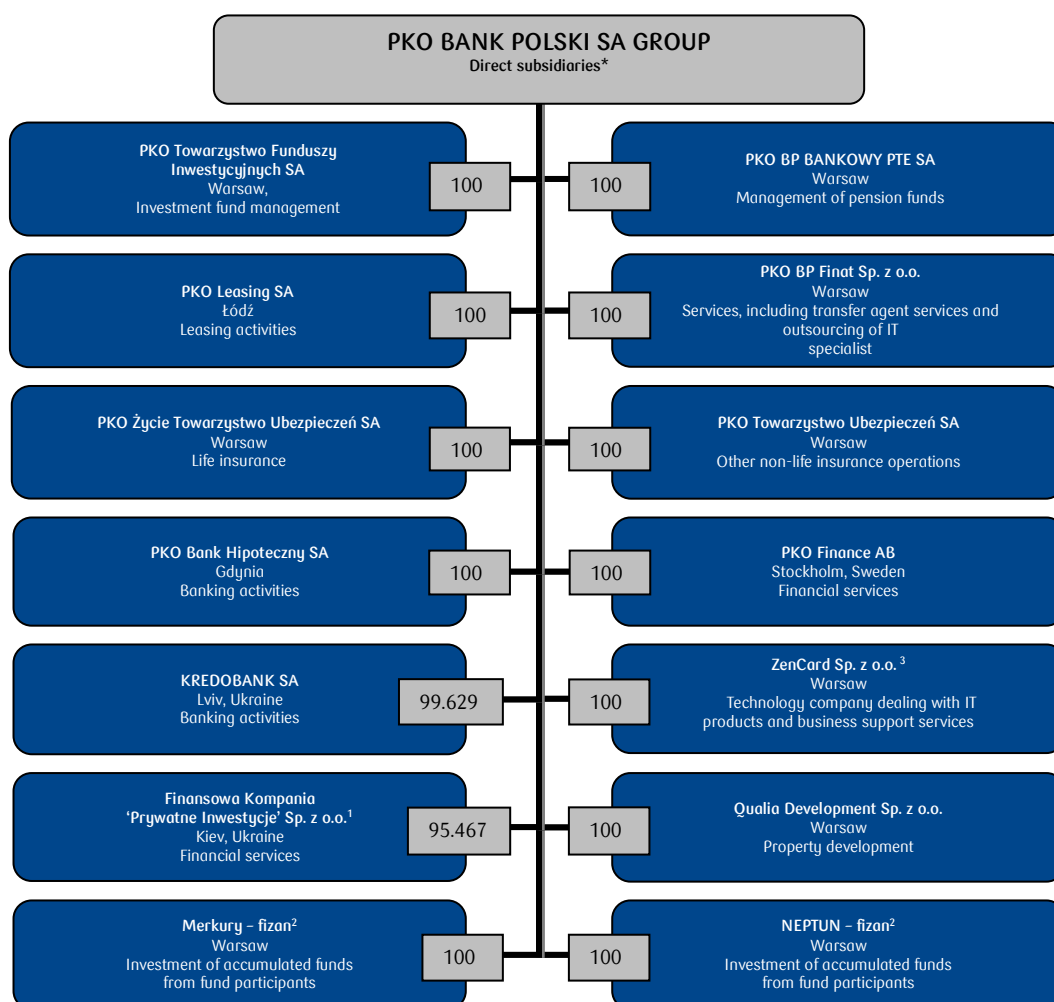
## 6. ORGANIZATION OF THE PKO BANK POLSKI SA GROUP

Entities included in the financial statements  
Key changes in the structure of the Bank's Group  
Related party transactions

### 6.1 ENTITIES INCLUDED IN THE FINANCIAL STATEMENTS

As at 30 June 2017, the PKO Bank Polski SA Group consisted of the Bank, as the parent company and the 43 direct and indirect subsidiaries. In the consolidated financial statements PKO Bank Polski SA Group is presented as the parent company of the PKO Bank Polski SA Group and its subsidiaries as defined in IAS 27 'Consolidated and Separate Financial Statements'.

The PKO Bank Polski SA Group comprises the following direct subsidiaries:



\* recognized in the consolidated financial statements of the PKO Bank Polski SA Group under the full method.

- 1) The second shareholder of the Company is 'Inter-Risk Ukraine' Additional Liability Company.
- 2) PKO Bank Polski SA holds the Fund's investment certificates; share of the Fund's investment certificates held are presented as the share in capital.
- 3) The company was acquired on 26 January 2017.

The full description of the Group is included in the condensed interim financial statements of the PKO Bank Polski SA Group for the six month period ended 30 June 2017.

## 6.2 KEY CHANGES IN THE STRUCTURE OF THE BANK'S GROUP IN THE FIRST HALF OF 2017

The following significant events affecting the structure of the PKO Bank Polski SA Group took place in the first half of 2017.

### COMPLETION OF THE LEGAL MERGER OF PKO LEASING SA AND RAIFFEISEN – LEASING POLSKA SA

On 28 April 2017, the merger of PKO Leasing SA (as the acquirer) and RLPL (as the acquiree) was registered in the National Court Register ('NCR'). The merger was carried out by way of transferring all assets of RLPL to PKO Leasing SA (merger through acquisition), without increasing the share capital of PKO Leasing SA and without replacing the shares. Therefore, PKO Leasing SA assumed all the rights and obligations of RLPL. The process of the business combination will be concluded with an operational merger which is planned to be completed at the turn of 2017 and 2018.

At the same time, on 28 April 2017, the following changes in the names of companies in the PKO Leasing SA Group were registered in the KRS:

- Raiffeisen-Leasing Real Estate Sp. z o.o. to PKO Leasing Nieruchomości Sp. z o.o.,
- 'Raiffeisen Insurance Agency' Sp. z o.o. to PKO Agencja Ubezpieczeniowa Sp. z o.o.,
- Raiffeisen-Leasing Service Sp. z o.o. to PKO Leasing Finanse Sp. z o.o.

### ACQUISITION AND CAPITAL CONTRIBUTION TO ZENCARD SP. Z O.O.

On 26 January 2017, PKO Bank Polski SA acquired 100% of the shares in ZenCard Sp. z o.o. and took up shares in the increased share capital of the Company. The aforementioned changes were registered in the NCR on 14 March 2017.

ZenCard Sp. z o.o. provides services in respect of IT and computer technology. The Company has built a platform for creating discount and loyalty programmes which, at the same time, allows for the virtualization of loyalty cards. This platform is integrated with a payment terminal and allows resignation from numerous separate loyalty cards or separate applications installed on mobile phones in return for a single customer payment card which at the same time is the virtual loyalty card of each vendor. The Company's strategic partner is CEUP eService Sp. z o.o. - one of the largest settlement agents in Poland. The Bank is interested in using the Company's and its founders' know-how in respect of solutions developed by the Company, in particular in respect of creating loyalty programmes with the use of payment cards and supporting its own promotional campaigns.

A full description of the changes in the Group's structure that took place in the first half of 2017 and will have an impact on subsequent quarters of 2017 is provided in the note 42 of condensed interim financial statements of the PKO Bank Polski SA Group for the six-month period ended 30 June 2017.

## 6.3 RELATED PARTY TRANSACTIONS

In the first half of 2017, PKO Bank Polski SA provided to its related (subordinated) entities services on arm's-length terms in respect of maintaining bank accounts, accepting deposits, extending loans and advances, the issue of debt securities, granting guarantees and current exchange operations as well as offering participation units and investment certificates in funds, lease products, factoring products, and insurance products of companies in the PKO Bank Polski SA Group, and also services offered by the Brokerage House of PKO Bank Polski SA. It provided PKO Bank Hipoteczny SA with services in respect of intermediation in the sale of housing loans to individual customers, the performance of post-sale activities in respect of such loans, and supporting activities, under an outsourcing agreement. It provided infrastructure to selected companies in the Bank's Group, as well as offered IT services and leased out office space. In cooperation with Centrum Elektronicznych Usług Płatniczych eService Sp. z o.o., it provided services for settling payment transactions.

The list of significant transactions of PKO Bank Polski SA with subordinated entities, including amounts of loans due to the Bank from these entities as at 30 June 2017 is presented in Note 47 of the condensed interim financial statements of PKO Bank Polski SA for the six-month period ended 30 June 2017.

## 7. ACTIVITIES OF THE PKO BANK POLSKI SA GROUP

Segments of the Group's activity  
Market position of the Group  
International cooperation  
Activities of other entities of the Group  
Sponsorship activities  
Charity activities  
Prizes and awards

### 7.1 SEGMENTS OF THE GROUP'S ACTIVITY<sup>10</sup>

Retail segment  
Corporate and investment segment

The PKO Bank Polski SA Group conducts business activities within segments offering specific products and services targeted at specific groups of customers. The manner in which the business areas are divided ensures consistency with the sales management model and offers customers a comprehensive product offer comprising both traditional banking products and more complex investment products. Currently, the Group conducts its business activities within the retail segment and the corporate and investment segment.

#### RETAIL SEGMENT

The retail segment offers a full range of banking products and services for individuals as part of retail and private banking. Moreover, it comprises transactions conducted with small and medium enterprises, developers, housing associations and property managers. The products and services offered to customers in this segment include, amongst others: current accounts, savings accounts, term deposits, private banking services, investment and insurance products, credit and debit cards, electronic banking services, consumer and housing loans, corporate loans, leases.

NUMBER OF CUSTOMERS: 9.3 MN  
LOANS VOLUME: 148 BN  
DEPOSITS VOLUME: 165 BN

#### CORPORATE AND INVESTMENT SEGMENT

The corporate and investment segment comprises transactions with large corporate customers and financial institutions. This segment offers the following products and services: maintaining current accounts and term deposits, safekeeping of securities, currency products and derivatives, business loans, leasing and factoring. In this segment, PKO Bank Polski SA also concludes, on its own or as part of consortiums with other banks, agreements for the financing of large projects in the form of loans and issues of non-treasury securities. Moreover, the segment comprises own operations, i.e. investing activities, brokerage activities, interbank transactions, transactions in derivatives and debt securities.

NUMBER OF CUSTOMERS: 14.5 THD  
LOANS VOLUME: 45 BN  
DEPOSITS VOLUME: 39 BN

<sup>10</sup> In this sub-chapter the Bank's management information is presented; any differences in total balances, shares and growth rates result from rounding.



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7.1.1 RETAIL SEGMENT

- Customers of the segment
- The loan offer in the retail segment
- Deposit and investment offer
- Other products and services in the retail segment
- Distribution network and access channels

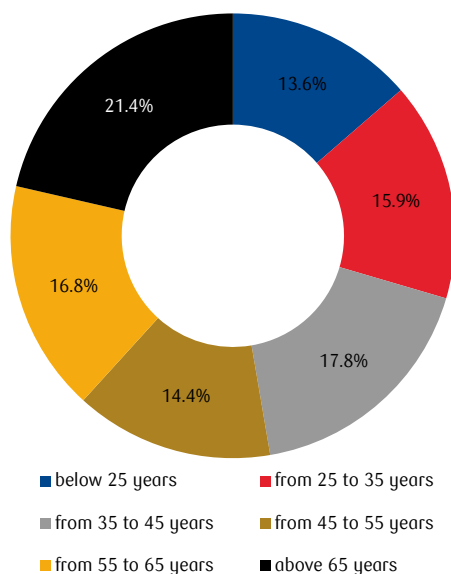
In the first half of 2017 PKO Bank Polski SA continued sustainable development in the area of retail segment and focused on identifying and satisfying consumers' needs, with whom the Bank builds strong, long-term relationship. Efforts has been made to improve the quality of service by i.a., increasing innovation in the new financial solutions, not only in the products but also the distribution channels, in particular in the field of electronic banking and mobile payments.

CUSTOMERS OF THE SEGMENT

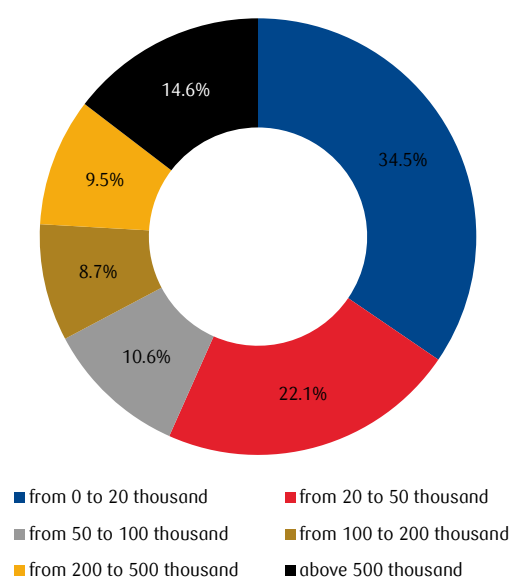
At the end of June 2017 number of serviced customers in retail segment reached 9.3 million, in which 8.9 million were individuals. More than a half of retail segment customers regularly use electronic banking. The most active group of customers using this type of service channel are customers aged between 18 and 35.

Trustworthy Bank's brand, ability in combining tradition with modernity and transparent product offer, which includes changing customer preferences, makes the Bank recognizable not only in urban centres. Due to the wide range of distribution channels most of the Bank's customers (67.2%) lives in municipality under 100 thousand citizens. What is more, in terms of the demographic profile, 47% of customers are aged under 45.

Age structure of Bank's customers



Distribution of the Bank's customers by place of residence



The most important distribution channel, from the point of view of acquired retail customers, was branch network. Acquisition of new customers is carried out mainly through the sale of current accounts (nearly 79%).



## THE LOAN OFFER IN THE RETAIL SEGMENT

The PKO Bank Polski SA Group's offer covers a wide range of loan products. Individuals can benefit from the financing, including:

- consumer loans available in the form of cash loans, mortgage-backed loans, revolving loans and credit cards,
- funding available in the form of housing loans,

Offer for small and medium-sized enterprises includes:

- SME loans,
- investment and working capital loans,
- leasing transaction.

As of the end of the first half of 2017 total financing provided to retail segment customers exceeded PLN 155 billion.

Table 19. Financing of retail segment customers of the PKO Bank Polski SA Group (in PLN million)

	30.06.2017	31.12.2016	30.06.2016	Change since:	
				31.12.2016	30.06.2016
<b>Gross loans and leasing receivables from:</b>					
retail and private banking	25 559	24 581	24 246	4.0%	5.4%
mortgage banking	101 443	101 389	98 803	0.1%	2.7%
PLN	70 638	67 301	63 733	5.0%	10.8%
foreign currency	30 805	34 088	35 069	-9.6%	-12.2%
small and medium enterprises, of which:	28 463	28 117	23 844	1.2%	19.4%
loans	20 726	20 779	21 542	-0.3%	-3.8%
leasing	7 736	7 338	2 302	5.4%	236.0%
<b>Total financing</b>	<b>155 465</b>	<b>154 087</b>	<b>146 893</b>	<b>0.9%</b>	<b>5.8%</b>

### RETAIL AND PRIVATE BANKING LOANS

Retail customers can use both the standard cash loan, as well as the current financing available under the revolving loans and credit cards.

In the first half of 2017, PKO Bank Polski SA continued its activity to support sales of consumer loans as part of a marketing campaign under the slogan:

- 'Wybierz swoją drogę do Mini Ratki', promoting the multi-channel nature of the offer. The offer was targeted at customers looking for short-term financing, rapid credit decision and a minimum of formalities;
- 'Pozwól Mini Ratce ścisnąć twoje raty' promoting the consolidation of loan liabilities from outside PKO Bank Polski SA.

PKO Bank Polski SA systematically takes measures to increase effective access to credit offer for retail and private banking customers, regardless of distribution channel. As a result of the changes implemented in the loan offer for retail banking customers, in the first half of 2017:

- regular customers of the Bank can obtain the expected amount of the loan to an account even within 30 minutes through access to personalized credit offer,
- it is possible for a person who does not have his/her files at PKO Bank Polski SA to submit a full application for a cash advance,
- a solution was implemented for newly concluded cash advance agreements thereby making the interest rate dependent on the changes in the NBP reference rate,
- in respect of revolving loans of the Personal and Private Banking customers the amount of the Bank exposure which can be obtained without the consent of a spouse was increased from PLN 50 thousand to PLN 80 thousand.



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### MORTGAGE BANKING LOANS

For many years the PKO Bank Polski SA Group has been the leader in financing the housing needs of Poles. According to the data presented by the Polish Bank Association it shows that at the end of June 2017 the PKO Bank Polski SA Group was the first on the market with 30.2% share in sales of housing loans for individuals. Since the beginning of the year a total amount of granted loans equalled to approx. PLN 6.7 billion.

Retail banking customers can use flagship mortgage products known as 'WŁASNY KĄT' available in 'Mieszkanie dla Młodych' programme as well.

In described period PKO Bank Polski SA granted under the 'Mieszkanie dla Młodych' programme over 4.4 thousand loans for a total amount to PLN 0.7 billion. The program consists of subsidies from the state budget to own contribution and additional financial support in the form of repayment of part of the loan.

Until 31 August 2020 a special offer available for holders of Large Family Card is valid, which states that provision for granting the 'Własny Kąt Hipoteczny' housing loan is reduced to 50% of standard provision for granting the loan.

### LOANS FOR SMALL AND MEDIUM ENTERPRISES

PKO Bank Polski SA consistently supports Polish entrepreneurship. Companies from the sector of small and medium enterprises are provided with funding for current and investment needs through a wide and flexible range of loans. Thanks to the agreements 'Portfelowa Linia Gwarancyjna de minimis' and 'Portfelowa Linia Gwarancyjna COSME' signed between PKO Bank Polski SA and Bank Gospodarstwa Krajowego under the government and EU aid programme for small and medium-sized enterprises, entrepreneurs receive support in the form of BGK guarantees - de minimis and guarantees of counter guarantees granted by the European Investment Fund under the programme COSME. The aim is to increase the availability of loan and the mobilization of additional resources for current operations of the company.

In the first half of 2017 the Bank still is the largest lender of the twenty-one banks providing loans with de minimis guarantees and holds 21.3% of market share (according to the data provided by the Center of Sureties and Guarantees of Bank Gospodarstwa Krajowego, as at 30 June 2017). Guarantee limit granted to PKO Bank Polski SA in the first quarter of 2017 once again was increased and after increase amounted to PLN 7.8 billion.

The value of loans granted under the 'Portfelowa Linia Gwarancyjna COSME' as of 30 June 2017 equalled to nearly PLN 213 million, and the amount of granted guarantees amounted to over PLN 170 million. Currently the value of the guarantee limits under the PLG COSME programme valid to 28 September 2017 amounts to PLN 250 million, after the increase in the fourth quarter of 2016.

### LEASING FOR SMALL AND MEDIUM ENTERPRISES

PKO Bank Polski SA with the members of its Group ensures a comprehensive offer of various forms of financing. Lease is the second (after loans) main source of financing for businesses. Depending on the customer needs, the following items are, among other things, financed through lease:

- vehicles, plant and machinery,
- investment projects (e.g. technological lines),
- office equipment and furniture,
- computer hardware,
- medical equipment,
- agricultural plant and machinery,
- real estate.

Beside standard products, the offer includes fleet leasing services and cooperation with suppliers.

As at the end of June 2017, lease receivables in the retail segment exceeded PLN 7.7 billion.



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DEPOSIT AND INVESTMENT OFFER

The Group promotes long-term savings among its customers, by both varied product offering (among other things, Treasury bonds, investment products of PKO Towarzystwo Funduszy Inwestycyjnych SA, term deposits, or regular saving products), as well as educational and informational activities.

In the first half of 2017 PKO Bank Polski SA continued activities aimed at offering more attractive deposits for retail segment customers, taking into account current market conditions and competitive position. At the same time, activities aimed at diversifying sources of financing were carried out.

As of 30 June 2017 deposits of PKO Bank Polski SA of the retail segment amounted to PLN 164.6 billion and from the beginning of the year increased by PLN 1.8 billion (i.e. by 1.1%). The increase in deposits of retail and private banking contributed to this, due to growth of current deposits volume, with a decrease of the level of term deposits.

Table 20. Deposits of the retail segment customers of the PKO Bank Polski SA Group (in PLN million)

	30.06.2017	31.12.2016	30.06.2016	Change since:	
				31.12.2016	30.06.2016
<b>Customer deposits, of which:</b>					
retail and private banking	142 273	140 021	134 377	1.6%	5.9%
small and medium enterprises	22 307	22 734	20 469	-1.9%	9.0%
<b>Total deposits</b>	<b>164 580</b>	<b>162 755</b>	<b>154 846</b>	<b>1.1%</b>	<b>6.3%</b>

CURRENT AND SAVING ACCOUNTS

PKO Bank Polski SA remains the market leader in terms of the number of current accounts, which as of 30 June 2017 amounted nearly to 7.0 million.

The number of accounts stems from the varied offer in terms of customer preferences. Products offered by the Bank to individual customers include: PKO Konto bez Granic, PKO Konto za Zero, PKO Konto dla Młodych and PKO Junior. PKO Bank Polski SA adjusted its offer to beneficiaries of 'Rodzina 500+' programme introducing dedicated 'Konto za Zero Rodzina 500+'. Since the beginning of 2016, the Bank sold over 21 thousand accounts of this type, including over to 3 thousand new accounts in the first half of 2017.

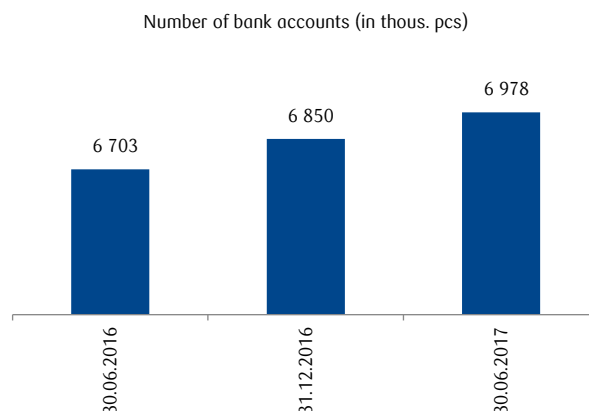
Moreover, in the second quarter of 2017, PKO Bank Polski SA carried out a promotion which allowed customers who opened PKO Konto Dziecka or PKO Konto Pierwsze to obtain an e-card with a value of PLN 50 to be used in one of the online shops.

For customers of small and medium enterprises interested in complex, modern and price attractive services, PKO Bank Polski SA offers two packages:

- PKO Konto Firmowe for individuals running business, freelancers and farmers who appreciate support of their finances with modern electronic banking services, as well as with individual advisor in the Bank branch,
- PKO Rachunek dla Biznesu created for enterprises, who anticipate an offer to be perfectly suited to their needs and appreciate the cooperation with individual bank advisor. The Bank offers to owners of PKO Rachunek dla Biznesu access to advanced online banking platform iPKO business, all *cash-management* services and many more modern banking products and services including the cheapest on the market SEPA online transfers or even access to simple currency exchange thanks to free iPKO dealer platform.

As of the first quarter of 2017, the process of opening a business account uses an automatic link to the Central Register and Information on Economic Activity (CEIDG) maintained by the Ministry of Development. Direct input of data from CEIDG makes the process of opening a business account simpler and faster.

In June 2017, a monthly campaign 'PLN 100 for your company from PKO Bank Polski' was launched. In accordance with the campaign; entrepreneurs who open a corporate account PKO Konto Firmowe with a debit card and make payments to ZUS within 30 days in the amount of at least PLN 250, receive a bonus of PLN 100.







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#### TERM DEPOSITS AND REGULAR SAVING PRODUCTS

The dominant share of deposits in the retail segment are deposits of retail and private banking customers. The Bank offers to individual customers, among others, deposits with progressive and standard interest rate and structured deposits.

The most popular term deposits among customers in the Bank's retail and private banking offer were:

- the products added to the offer in 2017: a 12M online deposit, a 12M deposit for new funds and a 12M deposit with threshold-based interest rate;
- 6M internet deposit available in the electronic banking system.

In the period under discussion, the following products were included in the Bank's offer:

- an account of saving and investment term deposits 'Sumoinwestycja' – which combines a 12-month term deposit opened in connection with the acquisition of participation units – 50% of funds is allocated to a selected subfund: debt (PKO Skarbowy, PKO Papierów Dłużnych Plus) or equity (PKO Stabilnego Wzrostu, PKO Akcji Plus); interest rate on the deposit part of the product depends on the fund option and customer segment;
- a term deposit for active ones ('dla przedsiębiorczych') with a fixed interest rate, on the condition of making non-cash transactions with a debit card issued to the current account in the total amount of PLN 6 thousand in the period when the deposit is opened – a product dedicated to customers in the small and medium-sized enterprises sector, sold via iPKO, Contact Center and Remote Banking Office.

Structured instruments are part of the standard offer of the Bank dedicated to individual customers. In the first half of 2017 the Bank has conducted 11 subscriptions of structured deposits, including:

- deposits based on the USD/PLN exchange rate (18-month with 1% guaranteed interest and 36-month with 2.0% guaranteed interest throughout the product's life, 18-month with 0.9% guaranteed interest and 36-month with 1.8% guaranteed interest throughout the product's life) and
- deposits based on the EUR/PLN exchange rate (18-month with 0.9% guaranteed interest, 18-month with 1% guaranteed interest, 36-month with 1.8% guaranteed interest and 36-month with 2.0% guaranteed interest throughout the product's life).

In the period under discussion, the offer of long-term saving products was revitalized. As a result, in the second quarter of 2017, the existing term saving deposits (Kapitał na Marzenia, Kapitał na Emeryturę, Kapitał na Własny Kąt, Kapitał dla Dziecka) were replaced with a new product: term saving deposit account 'Program Budowania Kapitału' ('Capital Building Programme'). The change in this product group resulted from observations of the market and the needs of customers who used the Bank's previous offer for making regular savings.

#### INVESTMENT FUNDS

As a result of cooperation with PKO Towarzystwo Funduszy Inwestycyjnych SA ('TFI SA') customers of retail and private banking are offered 40 non-dedicated funds, with total assets of PLN 21.6 billion<sup>11</sup>.

The Group constantly extends its offer in the area of investment funds. Since the beginning of 2017 issuance of investment certificates of closed-end non-public investment funds was conducted among customers, including PKO Globalnej Strategii Series I, PKO Absolutnej Stopy Zwrotu Europa Wschód – Zachód Series D, PKO Strategii Obligacyjnych Series H.

#### SALES OF STATE TREASURY BONDS

PKO Bank Polski SA is the only bank to sell and service retail bonds issued by the State Treasury, under an agreement concluded with the Minister of Finance. Treasury bonds are sold through the extensive sales network of PKO Bank Polski SA, which is a significant convenience for all persons who wish to invest in those instruments. In the first half of 2017, ca. 30 million of bonds were sold.

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<sup>11</sup> source: report of the Chamber of Fund and Asset Managers, as at 30 June 2017.

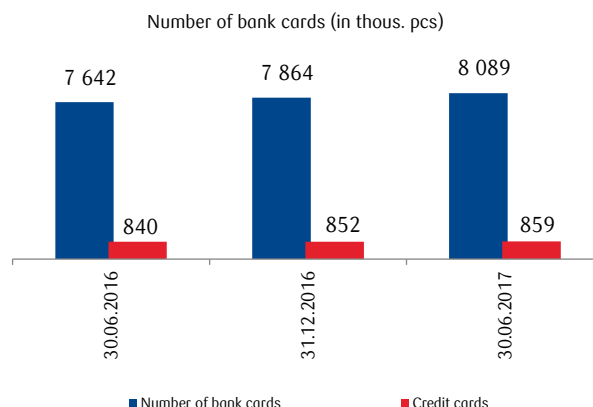
## OTHER PRODUCTS AND SERVICES IN THE RETAIL SEGMENT

### BANKING CARDS

As at 30 June 2017 the number of PKO Bank Polski SA bank cards amounted to approx. 8.1 million, including 0.9 million credit cards. Therefore, PKO Bank Polski SA is the leader in the Polish bank sector in respect of payment cards issued.

In the first half of 2017, a new multi-currency MasterCard card for Personal Banking and Private Banking customers was implemented in the Bank's offer. The card can be linked to foreign currency accounts in EUR, USD, GBP. Funds for covering card transactions are automatically drawn from an account in the currency of the transaction, as a result of which the customer does not incur currency exchange costs. The Bank also made it possible to request a new card at a branch and in remote access channels such as iPKO and the PKO Bank Polski SA Contact Center (CC), as well as the replacement of a 'single-currency' card with a multi-currency card via iPKO and CC, and to manage the multi-currency option (attaching foreign currency accounts in USD, EUR, GBP to the card) via iPKO, CC and in the Bank's branch.

In the same period, *cashback* transactions were implemented for Inteligo cards – the possibility of cash withdrawal while paying with the card at a POS.



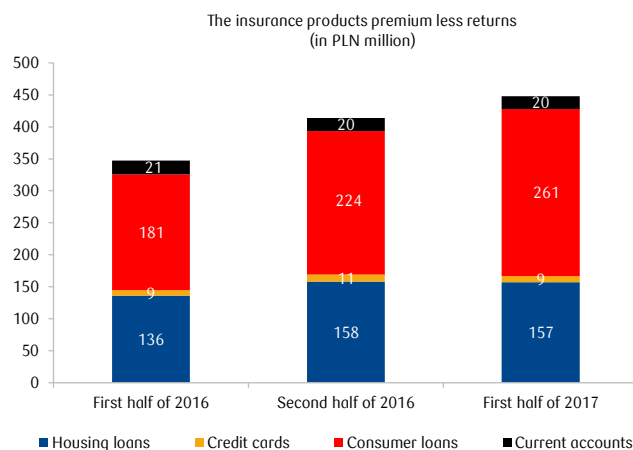
### INSURANCE PRODUCTS

The Group continuously develops an offer of insurance products increasing attractiveness of banking products combined with them and giving customers opportunity to secure their debts, assets and to receive help in case of an accident. Insurance products are offered to retail and private banking as well as to the small and medium enterprises segment connected with banking products such as:

- consumer and mortgage loans (life and loss of income source insurance, insurance of the walls of a building and low contribution insurance and bridge insurance, as well as insurance for customers in the SME segment),
- current accounts (ROR) (i.a. life and accident insurance, assistance insurance),
- bank cards (i.a. security package to credit cards, travel insurance, loan repayment insurance).

The offer has been enriched with new insurance products:

- loss of income source or hospital treatment due to accident insurance for credit card holders,
- individual insurance:
  - loss of income source insurance and life insurance for 'Pożyczka Gotówkowa', addressed to customers of the Primary Customer and Private Banking segment,
  - property insurance for loans or mortgages loans (i.e. insurance of real properties, movables, third-party liability (OC), assistance),
  - loss of income source insurance for loans or mortgage loans,
  - insurance of repayment of SME advances in the event of the temporary inability to repay or downtime in business activities,
  - insurance of short-term receivables – KUKI 'Polisa na świat',
- insurance not related to banking products.





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In the first half of 2017, customers of internet banking were provided with the possibility to buy new products not related to bank products via the remote channel (iPKO). First of them is life insurance 'Moje Życie 24' ('My Life 24') in which the customer decides which risks are to be insured (death, permanent and total inability to work, or serious illness). The second product introduced in the remote channel is insurance 'Mój Dom24' ('My Home 24') in which customers can insure their property in a comprehensive manner against various chance events, such as damage by water, flood, theft with burglary or power surges. The product also comprises third-party liability (OC) insurance in private life and Assistance insurance. At the same time, activities aimed at implementing another type of insurance available in the remote channel (iPKO), as well as in the mobile channel (IKO), i.e. tourist insurance, are underway.

In the first half of 2017, the sale of a new product delivered by KUKI was launched – insurance of short-term receivables called 'KUKI Polisa na świat'. This product is addressed to small and medium-sized enterprises and its scope is related to receivables from the customer's trade transactions under trade loan with domestic and foreign counterparties from approximately 100 countries.

From 2017, insurance with an equity fund has been withdrawn from the Bank's offer.

**PRIVATE BANKING**

PKO Bank Polski SA is consistently developing Private Banking, focusing on close cooperation within the Group, allowing customers access to a wide range of products and financial instruments.

Private Banking offices are located in 9 major cities in Poland: Warsaw, Gdańsk, Krakow, Katowice, Poznan, Wrocław, Łódź, Szczecin and Bydgoszcz (opened as part of Private Banking Office in Gdańsk). Private Banking Center of PKO Bank Polski SA manages assets portfolio worth PLN 19.8 billion.

**DISTRIBUTION NETWORK AND ACCESS CHANNELS**

**BRANCH NETWORK AND AGENCIES**

As at 30 June 2017, the retail distribution network of PKO Bank Polski SA consisted of 1 161 branches and 8 private banking offices. Compared with the end of 2016 the total number of branches decreased by 18.

Development of multi-channel distribution model extensively influences the increase of the efficiency of the on-site sales network. Optimization of the branch network takes place in a continuous manner, however the final decision not to close the certain branch located a certain micro-market is taken on a basis of economic assessment with regard to the potential development of the micro-market. The improvements are a multidimensional process, which covers activities such as changing of the nature of branches and reducing their number. The process of reducing large branches is carried out with the simultaneous universalization of smaller branches and transformation small branches into agencies in explanatory situations.

As part of the projects of the Bank and as a result of gained experience, universally applicable branch format is constantly evolving in the direction of the best operating conditions, tailored to the changing technology. At the same time, work is being carried out to determine the future of branches, taking into account the needs of customers, changes on the bank services market and the social role of PKO Bank Polski SA. One of the main challenges is to balance the proportion between aiming at a modern image and self-service devices, and the customer need to ensure the desired effectiveness.

Table 21. Operating data of the retail segment

	30.06.2017	31.12.2016	30.06.2016	Change since:	
				31.12.2016	30.06.2016
<b>Number of branches in the retail segment</b>	<b>1 180</b>	<b>1 198</b>	<b>1 227</b>	<b>-18</b>	<b>-47</b>
regional retail branches	11	11	11	0	0
retail branches	1 161	1 179	1 208	-18	-47
private banking branches	8	8	8	0	0
Number of ATMs	3 213	3 206	3 200	7	13
Number of agencies	790	837	857	-47	-67



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The Bank is constantly improving conditions for customers in the branch network. These activities focus on the modernization of the branches and moving them to the new attractive locations. Essential complement to the network of branches and ATMs is a network of agencies. As at 30 June 2017 PKO Bank Polski SA collaborated with 790 agencies and in comparison to 31 December 2016 the number of agencies has decreased by 47. The decrease in the number of agencies is a result of efforts to increase network's efficiency.

#### **ELECTRONIC BANKING**

Customers of the iPKO retail service can benefit from a package of electronic banking services. Moreover, for small and medium enterprises there is a possibility of using electronic banking services under the name iPKO Biznes. These services provide customers with access to information about accounts and products, as well as allow them to make transactions through: Internet, self-service terminals and telephone.

Bank systematically promotes the remote use of the Internet account, separate account management and other banking products in the transaction service, which allows customers faster and easier access to their products, as well as lowering the cost of using banking services.

New possibilities features implemented to the offer during the first half of 2017:

- adding a new iPKO functionality of complete remote process of opening and managing the First Savings Account, which is dedicated to children and adolescents (aged 0–18) and their parents;
- the possibility of ordering from iPKO a new debit card with a city function (for Warsaw and Wrocław), replacing the existing traditional card with a new card with a city function, or opening a new account on the Bank's webpage for which a debit card with a city function can be ordered at the same time;
- the launch of a new function which allows indicating a credit card as the source of money in the 'Płacę z iPKO' or 'Płacę z Inteligo' service, to make online shopping faster, more convenient and safer;
- adding a new insurance product, 'Moje Życie24', to the Bank's offer; the insurance is available on iPKO only and it is addressed to holders of current accounts (ROR).
- providing iPKO and Inteligo customers with the possibility to submit a request for the '500+' allowance;
- managing independently the daily limit of electronic transactions performed through the Inteligo online service, the mobile service and telephone service;
- allowing the use of the e-service 'Sprawdź swoje punkty karne' ('Check your penalty points') through iPKO electronic banking and Inteligo account with the use of a respective 'Profil Zaufany' ('Trusted Profile');
- temporarily blocking debit and credit cards.

Since 15 March 2017, the Bank's customers can use iPKO and Inteligo online banking services to send PIT-WZ application forms to the Tax Office for preparing a preliminary tax return for 2016 on the PIT-37 form and filing it on behalf of the taxpayer.

#### **MOBILE BANKING IKO**

PKO Bank Polski SA provides customers with modern technological solutions giving them full, simple, functional access to banking services by using the mobile that is safe and accessible everywhere at the same time. IKO is the most popular and the most developed system of mobile payments in Poland. It combines the functions of mobile banking with the ability to make mobile payments. The total number of application IKO activations has already exceeded one million four hundred thousand units. The application is constantly enriched with new functionalities. The changes have transformed the IKO application used for payments or withdrawals to mobile application being the bank in the phone.

On the basis of IKO, Polish standard of mobile payments, BLIK, was created. It is now used by the customers of PKO Bank Polski SA, Alior Bank, Bank Millennium, BZ WBK, ING Bank Śląski, mBank, Orange Finanse and T-Mobile Usługi Finansowe. BLIK is a universal form of payments and cash withdrawals from ATMs without using cash or credit card, created together with partner banks and the National Clearing House. As at 30 June 2017, the network of acceptance of mobile payments (IKO, BLIK) included more than 198 thousand devices (eService, First Data and PayTel, IT Card terminals) throughout the country. In connection with the implementation of the BLIK system, IKO application now enables cash withdrawal from more than 16 thousand of PKO Bank Polski SA ATMs and Bank Millennium SA, Bank Zachodni WBK SA, ING Bank Śląski SA, Euronet ATMs (about 7 thousand) and IT Card (about 1.8 thousand).

PKO Bank Polski SA introduced new option available for customers: 'Płacę z iPKO' payment method – transaction authorization through entering BLIK code generated in IKO application. Thanks to implemented change payments can be performed in most of online shops in Poland, which use the services of Dotpay, eCard, PayU, Przelewy24, Tpay.com, First Data and CashBill and Blue Media. This change also appeared on the biggest Polish e-commerce bidding platform.



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The IKO mobile application offers convenient access to a bank account and funds with the use of a telephone, including:

- fast view of the account balance and history,
- transfers to other persons and firms and between own accounts,
- transfers to telephones between applications operating in the BLIK system,
- payments in shops and on the Internet using BLIK code (instead of a card),
- cash withdrawals from ATMs using BLIK code (instead of a card),
- cash deposits in ATMs using BLIK code (instead of a card),
- contactless payments with the use of telephones with Android and NFC systems,
- viewing information on the products held and managing them,
- topping up telephones,
- opening deposits,
- saving in money boxes,
- card operations: repayment, assigning PIN, changing limits,
- map of branches, ATMs and locations where you can pay with BLIK,
- transfers using QR Code data, creating QR Code with transfer details.

PKO Bank Polski SA allowed its youngest customers under 13, access the bank account through PKO Junior mobile application. Application is not only handy but safe as well, additionally is enriched with financial education and development of entrepreneurial attitudes functions. Mobile equivalent of PKO Junior service is modern and intuitive.

The promotion on interbank BLIK mobile transfers regarding no commission charges has been extended for the year 2017.

As a result of the changes and improvements implemented, in the second quarter of 2017, more than 2.2 million customers logged in to their accounts from mobile devices. Customers who log in through IKO represent 43% of all mobile customers.

### THE PKO BANK POLSKI SA CONTACT CENTER

The PKO Bank Polski SA Contact Center (CC) plays an important role in the retail segment customer's service. The aim of this unit is to conduct the sale of products offered by the Bank during incoming and outgoing calls and to provide efficient and effective customer service, using remote communication.

In the PKO Bank Polski SA's call centre works several hundreds of consultants who are at the customers' disposal 24 hours a day. In addition to taking calls, consultants answer the customers' questions and applications in an electronic format - by e-mail and through the webpage. Customers may also send messages in the iPKO or Inteligo transaction service and via a special section on Facebook.

The tasks of the CC are in particular:

- sale of banking products via incoming and outgoing calls,
- supporting remote sale processes initiated on the web,
- handling of incoming calls from customers of the retail segment,
- outgoing calls initiated by the Bank (information tasks),
- handling security issues (incoming and outgoing),
- support for e-mail correspondence,
- answering questions asked by customers via infosite and iPKO service,
- internal customer service (professional helpdesk for employees in branches),
- early monitoring of receivables.



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## 7.1.2 CORPORATE AND INVESTMENT SEGMENT

Customers of the segment  
Lending activity and structured financing  
Deposit activity and transaction banking  
Financial institutions  
International banking  
Brokerage activities  
Treasury products  
Interbank market  
Fiduciary services  
Sales network

PKO Bank Polski SA consequently bases the development of corporate business on building stable relationships with customers through high quality services, specialized competence of the sales network and cooperation based on partnership. Current business financing (through working capital loans and tools of trade financing) as well as openness to participation in the implementation of development plans (through investment loans), and support in the implementation of local government projects, invariably constitute the main priorities of the Bank's corporate and investment segment.

The Bank having analysed market expectations, systematically adjusts its extensive offer of products and services in order to meet customer expectations. As a result based on new solutions, a broad range of transaction products and products mitigating financial risks (liquidity, settlement, interest rate, currency and commodity price risks) were being developed consistently, and financing structure needs were addressed in a flexible manner.

An international trade financing offer has been parallelly developed. The Bank became a strategic partner of Grupa Polskiego Funduszu Rozwoju in respect of providing export support. The value of support offered by PFR under the International Expansion of Polish Enterprises Programme which is supported by PKO Bank Polski SA, totals approx. PLN 60 billion.

### CUSTOMERS OF THE SEGMENT

In the first half of 2017 Corporate and Investment Segment was servicing 14.5 thousand customers, including over 1 thousand of strategic customers, nearly 1 thousand of foreign customers and more than 4 thousand units of local government and central government institutions together with budget-related and related entities.

The Bank held its position as an undisputed leader in providing services for local governments, by participating in local projects with custom character and by winning in tenders for providing services to the local governments units of all levels. In total, the Bank provides services for 6 from 16 voivodships in Poland.

### LENDING ACTIVITY AND STRUCTURED FINANCING

As at the end of June 2017 total financing provided to corporate customers, including bonds issued and lease receivables, exceeded PLN 65 billion.

Table 22. Financing of PKO Bank Polski SA Group's corporate customers (in PLN million)

	30.06.2017	31.12.2016	30.06.2016	Change since:	
				31.12.2016	30.06.2016
Gross corporate loans	45 464	41 630	42 063	9.2%	8.1%
Leasing receivables	6 692	6 591	4 854	1.5%	37.9%
Debt securities*	13 222	13 331	13 031	-0.8%	1.5%
municipal	7 056	7 148	7 158	-1.3%	-1.4%
corporate	6 166	6 183	5 873	-0.3%	5.0%
<b>Total financing</b>	<b>65 378</b>	<b>61 552</b>	<b>55 094</b>	<b>6.2%</b>	<b>18.7%</b>

\* Data presented including securities classified to the category loans and advances to customers.

PKO Bank Polski SA supports their customers' strategic investment projects realization through advisory regarding financing form choice as well as flexible terms of financing and repayment. The Bank is working closely with local government units and finances investment projects contributing to the local community.





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PKO Bank Polski SA offers its customers wide access to funds for financing even the most complex investment projects, as well as the services of advisors focused on selecting the optimum form of financing and terms of repayment. In the first half of 2017, the Bank signed: i.e.:

- 8 loan agreements in a banking consortium totalling PLN 12 billion, with the Bank's share of nearly PLN 2.5 billion,
- a loan agreement of PLN 3.2 billion PLN,
- a working capital loan agreement amounting to PLN 70 million and two annexes extending the period of financing totalling PLN 180 million,
- an annex to a corporate bond issue programme agreement executed by a consortium of banks, increasing the programme amounts to PLN 2.4 billion (the Bank's share has increased by PLN 0.6 billion),
- agreement for a bond issue programme in the amount of PLN 2.3 billion, under which the Bank acquired a bond with a value of PLN 0.2 billion,
- 46 municipal bond issue agreements with a value of PLN 245 million and 12 annexes extending the period of financing for the amount of PLN 41 million.

As part of the Group's product offer, its corporate customers can use products and services under leases. Virtually all fixed assets are financed with leases, depending on customer needs. Apart from standard products, the offer also includes the services of renting a car fleet and cooperation with suppliers.

As at the end of June 2017, lease receivables in the corporate and investment segments amounted to PLN 6.7 billion.

**DEPOSIT ACTIVITIES AND TRANSACTION BANKING**

The volume of corporate customers' deposits at the end of first half of 2017 amounted to PLN 38.7 billion and increase by PLN 1.1 billion from beginning of the year.

Table 23. Corporate customers' deposits of PKO Bank Polski SA Group (in PLN million)

	30.06.2017	31.12.2016	30.06.2016	Change since:	
				31.12.2016	30.06.2016
Corporate deposits	38 722	37 639	40 022	2.9%	-3.2%

PKO Bank Polski SA is constantly enhancing the quality of its transaction banking services. Services are dedicated to entities characterized by extensive organizational structure (e.g. capital groups) continuously developed, allowing customers to use various kinds of products and services to facilitate settlement of transactions with domestic and foreign partners. As part of providing electronic services, the leading product for the segment is the iPKO biznes electronic banking system. The iPKO biznes application has been expanded with new functionalities to improve the comfort of use, including among others simplified and redesigned possibilities of key operations on the site, so they were even more user-friendly and intuitive. Currently iPKO biznes application allows customers to monitor and manage accounts, payment cards and loans and to submit orders for all kinds of transfers. New functionalities are also being implemented with the aim of making it easier for customers to manage funds in complex organizational structures.

At the same time, the Bank is extending its offer by developing dedicated products based on cash pooling solutions. In particular, due to the fact that the Bank has a branch in the Federal Republic of Germany and a newly opened branch in the Czech Republic, the cross-border and multi-currency versions of this cash management tool have been made available.

**FINANCIAL INSTITUTIONS**

PKO Bank Polski SA has extensive network of nostro accounts in foreign banks, over 1 400 SWIFT established relationships with banks in different countries and markets, provides more than 200 loro accounts for foreign banks, which are utilized to settle transactions of banks, both in Poland and in other markets.

In addition to settlement services, PKO Bank Polski SA also provides services to foreign banks, their Polish branches, and domestic banks, offering them modern corporate solutions supporting their own operations and liquidity management. The Bank actively supports the operations of its corporate and retail customers on foreign markets and regularly extends the range of currencies that are available to the Bank's customers.



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In the first half of 2017, the Bank entered into negotiations with banks in Singapore and South Africa to provide settlement infrastructure for some new currencies, including the Singapore dollar (SGD) and South African rand (ZAR). Settlements in these currencies launched in the second quarter of 2017.

PKO Bank Polski SA works also with more than 650 domestic and foreign non-banking financial institutions, including investment funds, pension funds, insurance companies, payment companies, currency brokers and brokerage houses. For such entities the Bank mainly maintains current accounts and deposit accounts and offers them a wide range of treasury products.

### INTERNATIONAL BANKING

PKO Bank Polski SA actively participates in the development of the international expansion of its customers, offering them support in foreign markets. Initiatives are taken to facilitate financial support for Polish companies operating on the international markets, with respect to support in the identification of opportunities and winning contracts and directly in the area of international settlements. To facilitate such activities, the Bank follows in the steps of its customers: it has already opened branches in Federal Republic of Germany and in the Czech Republic. Other directions of expansion are being considered. In the offer of foreign entities is a full range of services and products for corporate customers comprising i.a.:

- transaction banking (including international *cash pooling*),
- electronic banking,
- treasury products,
- trade finance,
- corporate loans.

On the basis of strong relations with the majority of leading Polish groups, the Bank supports their activities and investments abroad on particularly favourable terms compared with local competitors, and therefore effectively participates in the development of the international expansion of its customers.

For the entities operating in the territory of Ukraine banking services are being provided by KREDOBANK SA which is a part of the PKO Bank Polski SA Group.

Moreover the Bank provides specialized support to foreign companies operating in Poland, e.g. from the Scandinavian countries, South Korea and Ukraine. For this purpose teams of experts dedicated to serve companies from these countries have been operating, which favours tightening economic relations. The wide range of products offered and the team of high quality advisors make PKO Bank Polski SA increasingly appreciated by foreign customers.

### BROKERAGE ACTIVITIES

The Brokerage House of PKO Bank Polski SA ('BH', 'the Brokerage House') is one of the leaders of the capital market in Poland, as evidenced by its big share in the turnover on the secondary stock market and participation in significant issues on the primary market.

In the first half of 2017, the BH's turnover on the secondary stock market amounted to nearly PLN 47 billion, which represented more than 16% of the market and gave the Brokerage House first place.

The activities of the BH on the primary market is realization with the following transactions:

- the function of the Global Coordinator, Joint Bookrunner and Offeror in the DINO POLSKA SA's IPO – transaction value: PLN 1.6 billion,
- the function of the Joint Bookrunner in the transaction of sale of Famur shares – the transaction value was close to PLN 0.6 billion,
- the function of Global Coordinator and Offeror in the transaction of public issue of bonds of Echo Investment SA – the value of bonds sold was PLN 100 million,
- participation in the public issue of consecutive series of BEST SA bonds – sales amounting to PLN 150 million,
- a member of the distribution consortium in the public offering of E series bonds of Giełda Papierów Wartościowych w Warszawie SA (the Warsaw Stock Exchange) – transaction value: PLN 60 million,
- intermediary in the call to subscribe for the shares of the company VANTAGE DEVELOPMENT SA announced by Fedha Sp. z o.o. – transaction value: PLN 56 million,
- the underwriter in respect of municipal bonds of the Piła Commune, the City of Siedlce, and Opolskie Voivodship – total value of bonds placed on the market: PLN 70 million,
- intermediation in the organization of sale of the shares of the companies Macrologic SA and UNIMOT.





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It should be noted that the Brokerage House acts as the retail bond issue agent and actively participates in trading in bonds on the WSE. Its share in the turnover exceeds 40% and it holds first place on the market.

The Brokerage House is also an active participant of the NewConnect market. The value of turnover, which exceeded PLN 143 million as at the end of June 2017 (the market share of approx. 8.5%) gives the BH the fourth position on the market.

At the end of June of 2017 BH provided 150 thousands security accounts and cash accounts and had 178 thousand of registry accounts. BH, in terms of securities accounts, ranks in the fourth position among 39 participants in the market (by data from KDPW).

### TREASURY PRODUCTS

PKO Bank Polski SA has an extensive offer of Treasury products for retail and corporate customers, such as deposit and foreign exchange instruments, hedging instruments against foreign exchange risk, interest rate risk and risk of commodity prices. Every product can be adjusted to the individual needs of the Customers and entered into through any distribution channel the customer considers convenient.

The biggest turnover is realized by the Bank on foreign exchange transactions. As compared with the same period of the previous year, in the first half of 2017 there was a 20% increase in turnover on spot transactions, and the Bank's share in the SPOT market for non-financial customers was 12.4%.

### INTERBANK MARKET

The Bank is the Treasury Securities Dealer and Money Market Dealer, which acts as a market maker on the domestic interest rate and foreign exchange market. In the competition for the selection of Treasury Securities Dealer 2018, the Bank took third place in the third assessment and the fifth in the general ranking. The Bank's share in SPOT transactions executed on the interbank market amounted to 18%; its share in IRS transactions amounted to 7% and in FRA transactions - 17%.

The Bank holds a significant portfolio of securities, which represents approximately 15% of total assets. The portfolio is financed from funds not used for the purposes of lending activity and comprises mainly Treasury Securities denominated in PLN. The function of portfolio is related to the current liquidity management and the function of the investment portfolio.

### FIDUCIARY SERVICES

The Bank maintains security accounts and facilitates for customers, domestic and foreign market transactions and acts as a depository for pension and investment funds. As at the end of the June of 2017 assets held by the customers on fiduciary accounts maintained by the Bank amounted to PLN 76.7 billion and were higher by circa 16.7% as compared to the value noted in the corresponding period of the previous year.

### SALES NETWORK

The sales network of the corporate segment includes 32 Regional Corporate Centres covering seven Corporate Macro-regions and the Branch in the Federal Republic of Germany, which serves corporate customers of PKO Bank Polski SA in the Federal Republic of Germany.

In April 2017, PKO Bank Polski SA opened its branch in the Czech Republic with head office in Prague. The Bank's branch in the Czech Republic is the second branch of the Bank abroad. The Czech Republic branch offers: maintaining settlement accounts, handling non-cash settlements, investing surpluses of funds in the form of deposits, short-, medium- and long-term financing, and providing liquidity management and *trade finance* services.

Table 24. Operational data of corporate segment

	30.06.2017	31.12.2016	30.06.2016	Change since:	
				31.12.2016	30.06.2016
<b>Number of branches in the corporate and investment segment:</b>	<b>41</b>	<b>40</b>	<b>40</b>	<b>1</b>	<b>1</b>
regional corporate branches	7	7	7	0	0
corporate centres	32	32	32	0	0
branch of PKO Bank Polski SA in Federal Republic of Germany	1	1	1	0	0
branch of PKO Bank Polski SA in Czech Republic	1	0	0	1	1

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## 7.2 MARKET POSITION OF THE GROUP

At the end of June 2017 the Bank maintained its leading position of the loan market and the deposit market (in terms of market share). The Group companies also occupy leading positions in various sectors of the financial services market.

At the end of first half of 2017, the loans market share of PKO Bank Polski SA (including PKO Bank Hipoteczny SA) amounted to 17.8% and compared to the end of 2016 remained unchanged.

The deposits market share amounted to 17.1%, which represents a decrease of 0.2 p.p. in relation to the end of 2016 and was caused by a faster growth in the volume of deposits of institutional customers on the whole market compared with the Bank.

Table 25. Market share

	30.06.2017	31.12.2016	30.06.2016	Change 30.06.2017/ 31.12.2016	Change 30.06.2017/ 30.06.2016
<b>Loans for:*</b>	<b>17.8%</b>	<b>17.8%</b>	<b>17.6%</b>	<b>0 p.p.</b>	<b>0.2 p.p.</b>
private individuals, of which:	22.9%	22.8%	22.8%	0.1 p.p.	0.1 p.p.
housing	25.9%	25.7%	25.5%	0.2 p.p.	0.4 p.p.
PLN	28.6%	28.6%	28.5%	0 p.p.	0.1 p.p.
foreign currency	21.3%	21.4%	21.5%	-0.1 p.p.	-0.2 p.p.
consumer and other	16.0%	15.8%	16.0%	0.2 p.p.	0 p.p.
institutional entities	13.0%	12.9%	12.5%	0.1 p.p.	0.5 p.p.
<b>Deposits for:</b>	<b>17.1%</b>	<b>17.3%</b>	<b>17.3%</b>	<b>-0.2 p.p.</b>	<b>-0.2 p.p.</b>
private individuals	20.7%	20.7%	20.6%	0 p.p.	0.1 p.p.
institutional entities	12.3%	12.4%	12.7%	-0.1 p.p.	-0.4 p.p.
<b>Leasing**</b>	<b>12.3%</b>	<b>7.5%</b>	<b>7.1%</b>	<b>4.8 p.p.</b>	<b>5.2 p.p.</b>
<b>IFC assets</b>	<b>8.1%</b>	<b>7.6%</b>	<b>7.2%</b>	<b>0.5 p.p.</b>	<b>0.9 p.p.</b>
<b>Non-Treasury debt securities (indebtedness)</b>	<b>29.5%</b>	<b>29.1%</b>	<b>27.9%</b>	<b>0.4 p.p.</b>	<b>1.6 p.p.</b>
<b>Brokerage activities</b>					
trading in the secondary market***	16.2%	9.4%	8.2%	6.8 p.p.	8 p.p.

Source: NBP, GPW, Polish Leasing Association

\* Data according to Webis, the NBP's reporting system. Market shares were updated in third quarter 2016 as a result of a change in the presentation of market data for the period from September 2014 to September 2016. After the change, receivables from mortgage banks, which had previously been presented as 'Other receivables' classified as consumer loans, are now presented as 'Housing loans'.

\*\* Share as at 31.12.2016 includes 1 month of sale of Raiffeisen - Leasing Polska SA.

\*\*\* Taking into account the effect of brokering the sale of Pekao SA shares in the first half of 2017. After eliminating this effect, the share of brokerage activity in the secondary market would amount to 9.8%.

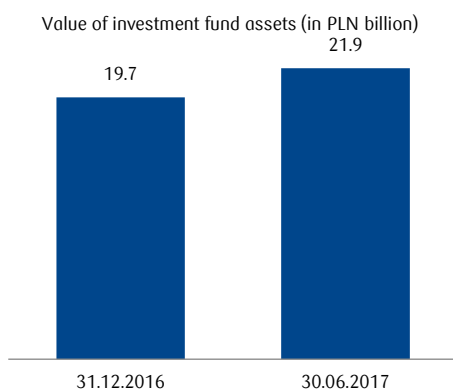
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### 7.3 ACTIVITIES OF OTHER ENTITIES OF THE GROUP<sup>12</sup>

Among strict banking activity the PKO Bank Polski SA Group provides specialist financial services relating to leasing, factoring, investment funds, pension funds and insurance, and debt collection services, transfer agent, IT services outsourcing and support in the conduct of business for other entities, as well as real estate development and management of real estate.

#### CHARACTERISTIC OF SELECTED PKO BANK POLSKI SA GROUP ENTITIES

##### PKO TOWARZYSTWO FUNDUSZY INWESTYCYJNYCH SA



In the first half of 2017 PKO Towarzystwo Funduszy Inwestycyjnych SA generated a net profit in amount of PLN 29.3 million (in the first half of 2016 net profit amounted to PLN 30.1 million).

The value of fund assets under management of the company as at the end of the first half of 2017 amounted to PLN 21.95 billion, which represents an 11.5% increase in comparison to the end of 2016. The increase in the value of assets was mainly associated with the positive net profit from sales and the result from assets management.

PKO Towarzystwo Funduszy Inwestycyjnych SA is ranked second in terms of the net value of assets, with a 8.1% share in the market of investment funds, and first in terms of the value of non-dedicated fund\* assets managed with a 14.6% market share.

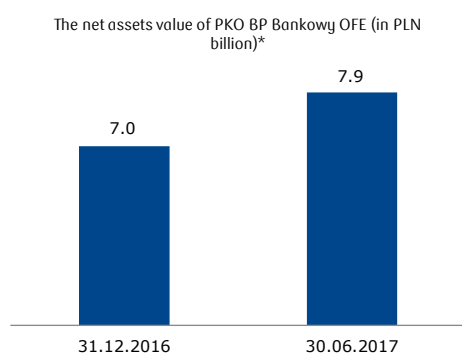
As of 30 June 2017, the company was managing 42 investment funds and subfunds. In the first half of 2017 the company's offer was expanded by the fund PKO Obligacji Wysokodochodowych Globalny FIZ and 14 issues of investment certificates of closed end funds were performed, under which it company obtained assets with a total gross value of PLN 471.2 million.

\* Source: The Chamber of Fund and Asset Managers (Izba Zarządzających Funduszami i Aktywami).

##### PKO BP BANKOWY PTE SA

In the first half of 2017, PKO BP BANKOWY PTE SA earned a net profit of PLN 2.8 million (compared to PLN 3.9 million in the same period of 2016).

##### The results of the Open Pension Fund (OFE)\*:



As at the end of June 2017 net assets value of PKO BP Bankowy OFE managed by PKO BP Bankowy PTE SA amounted to PLN 7.9 billion, which represents a 13.0% increase in comparison to the end of 2016. The increase of net assets value resulted mostly from the rate of return on Fund's assets. As at the end of June 2017 PKO BP Bankowy OFE had over 934 thousand members.

PKO BP Bankowy OFE ranks eighth on the pension fund market in terms of OPF net asset value and ninth in terms of the number of OPF members.

As at 30 June 2017, PKO BP Bankowy OFE had the second highest rate of return on investments for a period of 36 months among the 12 open pension funds operating on the market. PKO BP Bankowy OFE earned a rate of return of 22.42% for the period from 30 June 2014 to 30 June 2017. Taking second place in the

above-mentioned ranking allowed the company to realize an investment premium rate of 85.68%.

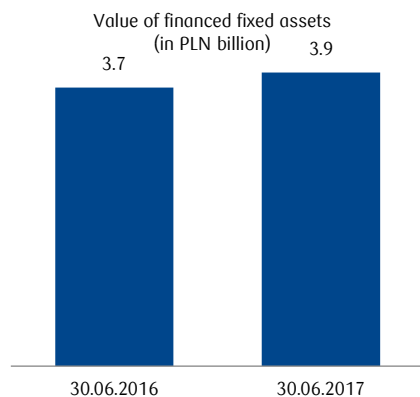
According to the calculations of \* Source: [www.knf.gov.pl](http://www.knf.gov.pl)

<sup>12</sup> Financial results presented in the description are taken from financial statements of individual companies which were prepared in accordance with IFRS, excluding financial statements of insurance companies which were prepared in accordance to Polish Accounting Standards. In terms of capital groups the presented financial result is the result of parent company of this group.

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**PKO LEASING SA GROUP**

In the first half of 2017, the PKO Leasing SA Group (ie. PKO Leasing SA and its subsidiaries) achieved net profit of PLN 25.5 million.

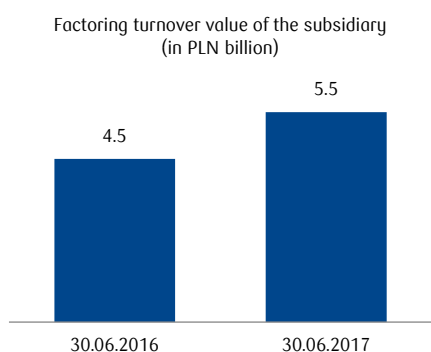


**Leasing activities:**

In the first half of 2017, the lease companies of the PKO Leasing SA Group financed fixed assets with a total value of PLN 3.9 billion, which represents a 4.7% increase compared with the same period of 2016 (data for the first half of 2016 calculated taking into account the present structure of the PKO Leasing SA Group). The change is due to an increase in the services provided in the vehicles and plant and machinery segment. As at the end of June 2017 the combined carrying value of amounts due from customers for financing of fixed assets (mature and not-mature) and the carrying value of fixed assets leased by the PKO Leasing SA Group under operating lease agreements was PLN 14.3 billion.

In terms of the value of funds provided in the first half of 2017 for the financing of fixed assets, the PKO Leasing SA Group occupied first position on the lease services market with a market share of 12.3%\*.

\* Source: Polish Leasing Association



**Factoring activity:**

In the first half of 2017, PKO Faktoring SA provided domestic and export factoring services without recourse and with recourse, reverse factoring and factoring schemes for suppliers.

In the first half of 2017 the value of factoring turnover amounted to PLN 5.5 billion (for comparable period of 2016 the company's turnover was PLN 4.5 billion); at the end of June 2017 the number of customers amounted to 446.

As at 30 June 2017, PKO Faktoring SA was ranked ninth among factoring firms belonging to the Polish Factors Association, with a market share of 6.6%.

**PKO ŻYCIE TOWARZYSTWO UBEZPIECZEŃ SA GROUP**

In the first half of 2017, the PKO Życie Towarzystwo Ubezpieczeń SA Group (ie. PKO Życie Towarzystwo Ubezpieczeń SA and its subsidiary, Ubezpieczeniowe Usługi Finansowe Sp. z o.o.) generated a net profit of PLN 9.3 million (in the first half of 2016, the Group generated the year with a net profit of PLN 6.4 million).

The result of the first half of 2017 reflects the strategy of building a portfolio of insurance offered via the distribution network of PKO Bank Polski SA and cost synergies obtained in the area of insurance services provided by entities of the Bank's Group.

PKO Życie Towarzystwo Ubezpieczeń SA offers a wide range of insurance products. The Company focuses on insuring the lives and health of its customers, it offers independent products and products linked to the banking products offered by PKO Bank Polski SA.

The value of gross written premiums from insurance contracts as at 30 June 2017 amounted to PLN 248.1 million and the number of insured persons was 689 thousand.

**PKO TOWARZYSTWO UBEZPIECZEŃ SA**

In the first half of 2017, PKO Towarzystwo Ubezpieczeń SA earned a net profit of PLN 2.2 million (in the first half of 2016 the company incurred a net loss of PLN 3.4 million due to a relatively short period of operating activity - the sales started in the first quarter of 2016). The company's business activities comprise non-life insurance (type II of insurance).

The company's offer comprises individual insurance against loss of income for the Bank's cash borrowers and a comprehensive offer of accident insurance, hospital treatment insurance, real estate and movable property insurance, private life third party liability insurance, Assistance, and insurance against loss of income for customers of PKO Bank Polski SA and PKO Bank Hipoteczny SA who take mortgage loans. Moreover, the company offers insurance for loans granted in the segment of small and medium enterprises (loss of income, business downtime, hospital treatment, surgery, serious illness).

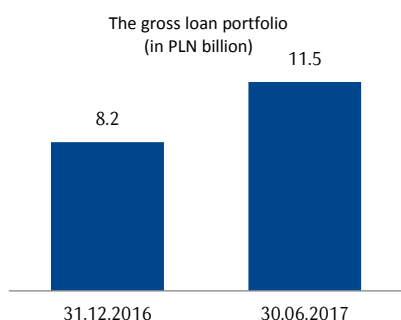


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In the second quarter of 2017, the company introduced GAP Group Insurance to its offer against a financial loss due to a total loss to a leased vehicle. The insurance offer was prepared in cooperation with PKO Leasing SA and is addressed to its customers.

Gross written premiums under the insurance contracts concluded by the company as at 30 June 2017 amounted to PLN 232.2 million, and the number of insured persons was 475 thousand.

**PKO BANK HIPOTECZNY SA**



PKO Bank Hipoteczny SA started its operational activity in April 2015. The principal purpose of PKO Bank Hipoteczny SA is to issue covered bonds, which serve as the main source of long-term financing of mortgage loans. It specializes in granting mortgage housing loans to individual customers and purchases receivables in respect of such loans from PKO Bank Polski SA. It acquires loans for its portfolio based on strategic cooperation with PKO Bank Polski SA. In the first half of 2017, the Company achieved net profit in the amount of PLN 25.1 million (versus PLN 0.25 million in the same period of 2016).

In the first half of 2017, under the Framework Agreement for the Sale of Receivables signed in 2015 with PKO Bank Polski SA, PKO Bank Hipoteczny SA acquired another housing loans portfolios secured with mortgages totalling PLN 2.2 billion. The total value of the gross loan portfolio of PKO Bank Hipoteczny SA as at 30 June 2017 amounted to PLN 11.5 billion, including housing loans secured with mortgages acquired under the agreement with PKO Bank Polski SA amounting to PLN 7.9 billion.

In the first half of 2017, the Company carried out four issues of covered bonds:

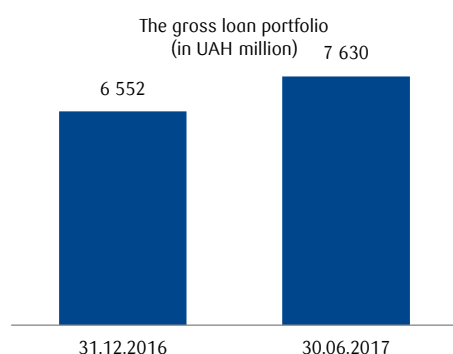
- a) two foreign issues addressed to institutional investors with a nominal value of EUR 525 million,
- b) two domestic issues addressed to institutional investors with a nominal value of PLN 765 million

Foreign issues are executed under the International Covered Bond Issue Programme, which is addressed to the European market and launched on the basis of the Base Prospectus approved in September 2016 by Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg, and domestic issues are executed under the Domestic Covered Bond Issue Programme, which is addressed to the domestic market and launched on the basis of the Base Prospectus approved in November 2015 by the PFSA.

After two years of operation, PKO Bank Hipoteczny SA became the leader of the Polish market of covered bonds in terms of the volume of covered bonds issued. The total value of covered bonds issued and outstanding (at the nominal value) as at the end of the first half of 2017 amounted to PLN 6.1 billion.

**KREDOBANK SA GROUP**

**(DATA ACCORDING TO IFRS BINDING FOR THE PKO BANK POLSKI SA GROUP)**



In the first half of 2017 the KREDOBANK SA Group (i.e. KREDOBANK SA and its subsidiary Finansowa Kompania 'Idea Kapital' Sp. z o.o.) generated net profit of UAH 222.9 million (PLN 32.5 million) i.e. by UAH 78 million higher than in the same period of 2016. Such results are the effect of KREDOBANK SA development in all business segments along with effective liquidity, margin and risk management.

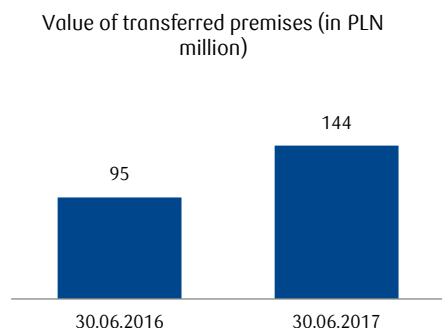
Loan portfolio of the KREDOBANK SA Group (gross) in the first half of 2017 increased by UAH 1 078 million, ie. by 16.5% and amounted to UAH 7 630 million as of the day 30 June 2017 (loan portfolio gross expressed in PLN at the end of the first half of 2017 was equal to PLN 1 087 million). Increase of the loan portfolio value in UAH was mainly a result of the increase of new loans sales.

The value of term deposits of the KREDOBANK SA Group of customers in the first half of 2017 have increased by UAH 126 million, i.e. by 3.15 % and as at 30 June 2017 amounted to UAH 4 146 million (term deposits expressed in PLN as of the end of the first half of 2017 amounted to PLN 590 million). Increase of the deposit value in UAH is the effect of the dynamic growth of numbers of Company's customers.

As at 30 June 2017 branch office network of KREDOBANK SA comprised the Central Branch in Lviv and 107 subordinated branches in 22 out of 24 Ukrainian districts. In the first half of 2017 location of the 2 subordinated branch was changed, 1 new branch was opened and 5 branches were closed.

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QUALIA DEVELOPMENT SP. Z O.O. GROUP



The Qualia Development Sp. z o.o. Group (i.e. Qualia Development Sp. z o.o. and its subsidiaries) generated a net profit of PLN 55.6 million in the first half of 2017 (the net profit of the Group for the first half of 2016 amounted to PLN 6.3 million). The result for the first half of 2017 is mainly the effect of completing the fourth stage of the Neptun Park project and commencement of handing over the premises to the customers.

In the first half of 2017, the Group's activities were focused on:

- selling premises in investments completed in Warsaw (Nowy Wilanów - Royal Park) and in Gdańsk (Neptun Park, fourth stage);
- executing the fourth (final) stage of the Neptun Park investment in Gdańsk, including obtaining a permit for use and handing over the premises to buyers;
- running hotel business on the basis of projects completed in Gdańsk and in Międzyzdroje;
- selling process of the selected properties and companies of the Qualia Development Sp. z o.o. Group.

## 7.4 SPONSORSHIP AND CHARITY ACTIVITIES BY PKO BANK POLSKI SA

### SPONSORSHIP ACTIVITIES

Sponsorship activities realized by PKO Bank Polski SA in the first half of 2017 were aimed at building the image of the Bank as a reliable financial institution, socially engaged, modern and open to the customers' needs. They were consistent with the Bank's mission, which involves supporting the development of Poland and the Poles, a positive impact of the organization on people, firms and the environment and building the Bank's reliability in a consistent manner.

The sponsorship activities of PKO Bank Polski SA was both nationwide and local and covered the following areas:

- Culture and art - protecting the national heritage in the area of culture and art, cultivating tradition;
- Science and education - promoting science (mainly mathematics and economics), supporting educational projects aimed at the development of entrepreneurship and promotion of innovations;
- Sport - encouraging activity, supporting mass sports, including runs often connected with charity activities and commemorating important events in Polish history;
- Business - strengthening the Bank's position on the financial market, supporting Polish business, building and maintaining and building business relations;
- Events/projects that are important for local communities - promoting the Bank's image as an important and active partner of business circles, local authorities and cultural centres.

Additionally, in each of these areas the Bank strived to take actions to promote patriotic and historical values.

### CULTURE AND ARTS

As a sponsor of culture and arts, PKO Bank Polski SA involved in cooperation with opinion-forming cultural institutions. The Bank continued cooperation with the National Museum in Warsaw as a sponsor of the modernized Gallery of Medieval Art, which exhibits the richest collection of art from this period in Poland. The Gallery was one of the most frequently visited permanent exhibitions. The Bank participated in the organization of the 'New Series of Portraits of Polish Monarchs. Świerzy vs. Matejko' exhibition, presented in the National Museum in Gdańsk. The presentation of 49 portraits sponsored by the Bank was an enormous success.

In the first half of 2017, the Bank was also involved in the organization of the 22nd Summer Jazz Festival in Kraków - the biggest jazz festival in Poland and one of the larger ones in Europe.

The Bank continued its Strategic Partnership with the National Music Forum - an institution established in 2014 as a result of the combination of the Wrocław Philharmonic and the International Festival Wroclavia Cantans. The major partners of the programme of supporting culture also include the following: the National Philharmonic in Warsaw, the Philharmonic of Warmia and Mazury in Olsztyn, the Łódź Philharmonic, the Podkarpacka Philharmonic in Rzeszów, the





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Silesian Philharmonic in Katowice, the Kraków Opera, Opera Nova in Bydgoszcz, Polish Theatre in Warsaw, Silesian Theatre in Katowice and Drama Theatre in Wałbrzych. The Bank also supports the artistic projects of the Museum of Cinematography in Łódź and the Raczyński Family Library in Poznań.

Commemorating distinguished people and events in Polish history as part of patriotic education projects was also an important element of the Bank's sponsorship activities. In the first half of 2017, the Bank took part in the celebrations of the National Day of Remembrance of the 'Cursed Soldiers'. The Bank helped to organize concerts: 'Niezłomnym honor' and 'Wilczy ślad. Piosenki Niezłomnych'.

Other patriotic and historical projects carried out in the period include: the 'Poland - a Great Project' Congress, the 4th edition of the Małopolski Competition 'Footsteps of Cursed Soldiers' and the 79th anniversary of the announcement of 'Prawdy Polaków spod Znaku Rodła'.

### SCIENCE AND EDUCATION

As a socially responsible company, the Bank supported projects associated with science and education and promoted the development of entrepreneurship and innovation among adolescents. In the first half of 2017, a cooperation in respect to a major educational project, the General Knowledge about Poland and the Contemporary World Contest - one of the oldest contests for students organized by the University of Warsaw and the EUROPEA Foundation was continued. In cooperation with various institutions of higher education, the Bank sponsored teams of IT specialists from the Jagiellonian University, Warsaw University and Wrocław University participating in the ACM International Collegiate Programming Contest 2017, the most prestigious IT competition in the world, aimed at promoting gifted and ambitious students. Participation of the team of the University of Warsaw was a success as it won the gold medal. The Bank continued the 'Ekonomia na Bank' project executed with the Silesian University in Katowice. As part of this project, the Bank's experts conducted a series of workshops and lectures at the selected departments and units of the Silesian University.

The Bank is also involved in various initiatives addressed to children, such as the 'Ambassador of School Inventions', a competition organized by the Patent Office of the Republic of Poland and aimed at recognizing the most interesting designs, inventions, other technical solutions, board and computer games presented by inventors and constructors up to the age of thirteen.

The Bank also took part in the Liberty Institute School of Leadership project, which was aimed at preparing young people for conducting business, social and political activities, or the Polish Leaders Congress (Kongres Liderów Rzeczypospolitej). Moreover, the Bank once again participated in the 'Dukaty Decjusza' series of educational workshops aimed at popularizing knowledge of economics among primary and lower secondary school students.

The Bank is also open to the ideas of others, in particular new businesses whose innovative solutions are their main asset. An example of such action is continued cooperation on the Acceleration Programme as part of the MIT Enterprise Forum Poland, which is aimed at promoting and supporting the implementation of technological projects. Such cooperation resulted in implementing the Let's fintech with PKO Bank Polski SA path dedicated to modern technologies in the area of finance.

As part of supporting innovation and educational activities, the Bank participated in the publication of the Investment agreement? What to remember? (Umowa inwestycyjna? O czym pamiętać?) manual prepared by the Trio Legal Sznajdek Granicki Law Firm. The aim of the publication is to reach the startup community with content they should find interesting and valuable.

### SPORT

PKO Bank Polski SA has been involved in important sports events for a number of years. As part of the programme 'PKO Bank Polski - Let's Run Together' (PKO Bank Polski - Biegajmy razem), the Bank encourages the Poles to exercise together. The Bank supports dozens of various running events in all parts of Poland. The following ones should be noted in particular: the 3 May Constitution Run (a part of the Warsaw Run Trio), PKO Wrocław Night Half Marathon, PKO Poznań Half Marathon, PKO Rzeszów Half Marathon, and the PKO Gdynia Grand Prix series: the Birthday Run with PKO Bank Polski, the European Run with PKO Bank Polski, the Świętojański Run with PKO Bank Polski SA. The Bank also sponsored the Footsteps of Wolf Run - Run to the Memorial of Cursed Soldiers (Bieg Tropem Wilczym - Bieg Pamięci Żołnierzy Wyklętych). It was a unique event, as the run took place in more than 270 Polish cities at the same time with the participation of more than 60 000 runners.

As part of the Bank's running programme, every Saturday or Sunday at 9.30 at more than 80 athletic stadiums in all parts of Poland (and at some of them also on Monday evenings), irrespective of the weather and the number of participants,



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free running meetings are organized by the 'Biegam Bo Lubię' initiative whose strategic partner is PKO Bank Polski. The practice is led by professional coaches and everyone who wants to be fit and feel good can take part.

In addition to runs, which definitely prevailed as far as sport sponsorship is concerned, the Bank also supported other prestigious sports events such as Cavaliada - a series of International Horse Jumping Competitions.

**BUSINESS**

As one of the financial market leaders in Poland, PKO Bank Polski took an active part in the organization of seminars and conferences at which different business circles exchanged their experience and creative solutions. The most important events of this type included: the 7th European Financial Congress in Sopot, IMPACT'17 Congress, the 5th International Marine Congress, Wall Street 21, the Conference of the Chamber of Brokerage Houses, the 'On the path towards sustainable development' conference held by the wGospodarce.pl portal, the 'Strong stock exchange in a strong economy' debate held by the wSieci weekly, the 'Cities on the Internet' Conference and the 'Poland - a Great Project' congress.

Furthermore, the Bank took part in the biggest international conference in Central and Eastern Europe focused on technology, new media and support for new businesses.

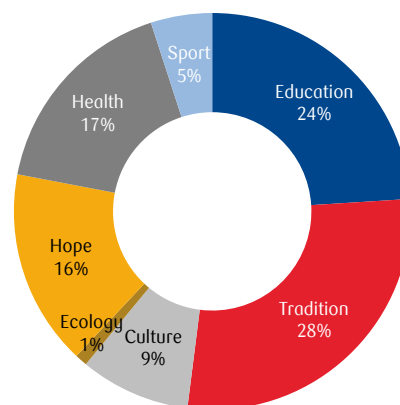
Additionally, the Bank was involved in an international congress with the participation of the Prime Ministers of the Visegrad Group States. The persons invited to this two-day meeting included innovators from the region, representatives of start-ups, non-governmental organizations and public administration. The following devices were presented during the Congress: a self-service device and a mobile biometric device.

For the second time, the Bank was the Strategic Partner of the Polish Entrepreneur of the Year 2016 Competition organized by the *Gazeta Polska Codziennie* daily. The aim of the Competition was to recognize the entrepreneurs, exporters, managers, philanthropists and experts supporting development of the Polish economy and popularizing economic patriotism. Prizes were awarded in the following categories: exporter, innovator, industry leader, SME, philanthropist. The editors of *Gazeta Polska Codziennie* also granted a special distinction.

The bank also supported the following initiatives: 'The Man of the Year' and 'Wprost Eagles' of the *Wprost* weekly, or the Economic Awards Gala of the Polish Radio, in which the Bank won the 'National Treasure' category.

The Bank also supported smaller events addressed to entrepreneurs and local authorities, which were important for the local communities. They included regional harvest festivals, local celebrations, festivities, meetings with entrepreneurs and important regional events in the areas supported by the Bank.

The Foundation's engagement in the implementation of projects in particular areas (share in a budget)



**CHARITY ACTIVITIES OF THE PKO BANK POLSKI SA'S FOUNDATION**

**FOUNDATION'S AIMS**

The aim of the PKO Bank Polski SA Foundation, which is a part of the 2013-2016 Strategy is to deepen customer relationships, understood as the co-financing of projects aimed at building social solidarity enhancing the emotional ties of all stakeholders with the Founder's brand. Multiplication of good also helps build the employer's brand. The Foundation sees the common good in building civil society and participates in projects, often initiated by the employees of the Bank - Volunteers. Foundation supports substantively and financially numerous projects of environments and societies that are important for the development of the Poland.

**FOUNDATION'S ACTIVITIES**

The main financing source of the Foundation are donations from the Funder transmitted in accordance with the Foundations Financial Plan. Additional funds for grants come from the profit generated during the non-cash transactions made by customers of Inteligo associated with the affinity cards: 'Good brings profit' ('Dobro procentuje') (since 2013). PKO Bank Polski SA every three months divided profit from each transaction conducted using the charity cards.





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During the seven years since the start of operation, the Foundation has donated more than PLN 82.5 million for social activities. Subsidized initiatives are parts of one of the seven programme areas: EDUCATION, TRADITION, HOPE, HEALTH, CULTURE, ECOLOGY, SPORT.

From the beginning of 2017, the implementation of 34 strategic projects, including 4 special strategic projects (which do not require to establish a partnership with an external organization): Banking blood donation, Banking Collection, Banking and Gift John Weber Collection, the foundation donated PLN 4.7 million. The Foundation makes every effort to ensure that the strategic projects evolve and reach the largest possible number of Beneficiaries. The Foundation is preparing its own project, 'A compass to start with', aimed at supporting former foster care children who have reached full legal age and are starting an independent life, in particular in the process of gaining professional experience (internship, practical training).

In a partnership at the local level for the implementation of 150 projects the Foundation provided PLN 2.1 million. Individual help, both for children and adults amounted to more than PLN 1.1 million. Number of individual beneficiaries amounted to 77, among which 17 persons are employees of PKO Bank Polski SA or their families. Help for 73 individuals was granted by the Charity Action running as part of a special project of the Foundation at the individual level.

In addition, the Foundation mediates in the process of making donation in the form of IT equipment and furniture withdrawn from use of the branches of the Bank.

**CORPORATE VOLUNTEERING**

Since 2013 the Corporate Volunteering system has been functioning in the Bank and close to 1.3 thousand active Volunteers are registered. Those persons may propose their own local or individual social projects. Cooperation between the Foundation and the Volunteers is aimed at verifying the reliability of the proposer and building relations between the Bank and the local community. Additionally, all Volunteers may register their extra-banking engagement, sharing good practices and inform the Fund of local initiatives which are worth supporting.

Charity influences shaping the image of PKO Bank Polski SA as a socially-responsible business. The support provided by the Foundation contributes to building strong relationships with the environment of the Bank and to strengthen mutual trust.

**7.5 PRIZES AND AWARDS GRANTED TO THE PKO BANK POLSKI SA GROUP**

In the first half of 2017 the PKO Bank Polski SA Group was awarded numerous prizes and awards. We have been recognized for social activities of Group companies, for innovative products and services, excellent customer service, management staff of the Bank, excellent financial results and the overall business of the Bank and the Bank's Group.

**DYNAMIC DEVELOPMENT AND EXCELLENT FINANCIAL RESULTS**

<b>50 LARGEST BANKS IN POLAND</b>	PKO Bank Polski SA won, in another consecutive year, the ranking of the Financial Monthly BANK in 2016 - '50 largest banks in Poland'. The ranking is prepared by independent market analysts, which, based on financial data of banks for the previous year, evaluate the market position of financial institutions compared with the whole banking sector.
<b>A ROSE WITHOUT A THORN</b>	PKO Bank Polski was granted a special distinction in the 2016 ranking of the best banks 'A Rose without a thorn' organized by the 'Home & Market' monthly. The editors appreciated the business activities of the Bank and its Group companies, which directly affect the Bank's position of the banking sector leader. The ranking is based on the results of an analysis of the banks' financial results.
<b>THE POLISH BANKING LEADER</b>	In accordance to the 'Polish banking in numbers' report prepared by PRNews.pl and Bankier.pl, PKO Bank Polski is the unquestionable leader of the Polish banking sector in many areas, including the number of customers and the number of debit cards issued. It also holds the first place in the sector in mobile and Internet banking.
<b>STARS OF BANKING</b>	PKO Bank Polski took the first place in the 'business structure' category in the 'Banking stars' ranking published by the 'Dziennik Gazeta Prawna' daily. It owes this victory to excellent scores in the categories of loans granted and deposits received. At the same time, PKO Bank Hipoteczny was ranked first in the 'specialist banks' category. This was due to its activity in covered bond issues.



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<p><b>THE BANK MANAGER OF THE YEAR</b></p>	<p>Zbigniew Jagiełło, the President of the Management Board of PKO Bank Polski, won the Bank Manager of the Year 2016 competition organized by the <i>Gazeta Bankowa</i> magazine. The winner of the competition is selected by a jury, which takes into account, among other things, management effectiveness, financial results, and compliance with the principles of fair competition. Other contestants also evaluate the candidates nominated for the award.</p> <p>For Zbigniew Jagiełło it is the third award in this competition - he was the Bank Manager of the Year in 2015 and also in 2012.</p>
<p><b>THE BEST FINANCIAL DIRECTOR</b></p>	<p>Bartosz Drabikowski, Vice-President of the Management Board of PKO Bank Polski, became one of the 10 Best Financial Directors. The candidates were evaluated for their approach to the institution's financial strategy and effectiveness - both their own and their team's. He was also appreciated for his skills and the ability to plan and make right decisions in the changing market conditions.</p> <p>The Best Financial Director title was awarded to outstanding financial experts. The ranking was prepared by the 'Gazeta Finansowa'.</p>
<p><b>ACTIONS AWARDED IN THE AREA OF CORPORATE SOCIAL RESPONSIBILITY (CSR)</b></p>	
<p><b>THE STATE BUDGET PILLAR</b></p>	<p>PKO Bank Polski SA received the State Budget Pillar award granted by the <i>Rzeczpospolita</i> daily for its last year's CIT payments to the state budget. The Bank is the biggest payer among financial institutions and the second among all entities participating in the ranking.</p> <p>The State Budget Pillar award is a component of the annual ranking of the biggest firms in the Polish economy - the 'Top 500'.</p>
<p><b>THE NATIONAL TREASURE</b></p>	<p>In the first edition of the Polish Radio Economic Awards, PKO Bank Polski was appreciated for its involvement in the repolonization of bank Pekao SA and won the National Treasure category.</p> <p>The Polish Radio Economic Awards are granted to the best enterprises which significantly contribute to the development of the Polish economy and international promotion of Poland and engage in charitable, pro-social and environmental activities.</p>
<p><b>INVESTOR RELATIONS SURVEY LEADER</b></p>	<p>PKO Bank Polski SA was ranked first in the investor relations survey of WIG30 companies conducted among individual investors by the <i>Parkiet</i> Stock Exchange Journal and the Chamber of Brokerage Houses. With an average score of 4.4 (on the 1 to 6 scale), the Bank took the leading position in the ranking based on scores granted by individual investors and <i>Parkiet</i> readers. It received a similar score (4.36) and took tenth place in the ranking reflecting the opinions of analysts and institutional investors.</p>
<p><b>TRANSPARENT COMPANY OF THE YEAR</b></p>	<p>PKO Bank Polski SA was awarded the title of 'Transparent company 2016'. The title is given in the ranking of WIG20 companies in the category of communication of public companies with the market, prepared by the Accountancy and Taxes Institute and <i>Parkiet</i> Stock Exchange Journal. The Bank received a high rating for financial reporting, investor relations and corporate governance principles.</p> <p>The 'Transparent Company of the Year' ranking is an initiative, which is addressed to WIG20, WIG40 and WIG80 public companies. Its aim is to assess the companies' transparency and based on a survey.</p>
<p><b>THE BEST EMPLOYER IN POLAND</b></p>	<p>PKO Bank Polski SA is the first Polish commercial institution chosen by students as a place of work. It was among the best employers in Poland in the Business TOP 100 Universum Global ranking. Apart from the Bank, the following entities received this title: Google Poland, Microsoft, the National Bank of Poland.</p> <p>Universum Global every year prepares a ranking of the best employers in the world. 27.6 thousand young people from 64 Polish universities took part in the survey. On the basis of their opinions, the best 100 employers in Poland were selected.</p>
<p><b>EMPLOYER OF THE YEAR</b></p>	<p>PKO Bank Polski SA once again received the Employer of the Year title in the survey conducted by the international student association AIESEC. It took a high, fifth position and was the only Polish entity in the top five.</p> <p>The jubilee, 25th edition of the ranking was conducted with the participation of students of more than 30 higher education institutions in Poland. In their opinion, the most important factors affecting the selection of a desirable employer included: good atmosphere, financial terms of employment, work satisfaction. A clear career path, promotion criteria, training and professional development opportunities were also important.</p>
<p><b>GOLDEN COLUMNS (ZŁOTE SZPALTY)</b></p>	<p>PKO Bank Polski SA received two Golden Columns in the Power of Content Marketing Awards Szpalty Roku competition. In the category Content Marketing - Sport, the project 'PKO Bank Polski. Let's Run Together' received an award for a commercial charity campaign, involvement of employees and good PR. The campaign '#zkopyta', promoting Cavaliada, received an award for the best autonomous project in the social media campaign category. The jury appreciated it for the involvement of volunteers, reaching the target group and unimposing brand promotion.</p> <p>Columns of the Year (Szpalty Roku) is a competition organized by the Content Marketing Poland Association. It is aimed at promoting standards in the creation of content marketing projects.</p>
<p><b>THE NICOLAUS COPERNICUS MEDAL</b></p>	<p>The Polish Bank Association awarded the Nicolaus Copernicus Medals to Piotr Mazur, Vice-President of the Management Board of PKO Bank Polski SA in charge of the Risk Management Division for his</p>



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<b>RECEIVED FROM THE POLISH BANK ASSOCIATION</b>	contribution to the development and security of domestic banking, and to Piotr Galas, Director of the Corporate Customer Department and Paweł Bizoń from the Public Sector Customer Department at PKO Bank Polski for their contribution to banking sector development and strengthening of the Polish economy.
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**PKO BANK POLSKI SA – LEADER OF MODERN TECHNOLOGIES**

<b>MOBILE BANK OF THE YEAR</b>	PKO Bank Polski SA received the 'Golden Bell' award for the IKO mobile application in the Mobility Trends competition, in the Mobile Bank of the Year 2016 category. It won the Internet voting. The Mobility Trends competition, organized by the MIT MEDIA Group, the publisher of the Mobility magazine about mobile technologies, is aimed at recognizing the modern solutions which won the biggest interest of customers in a given year. As at the end of 2016, the application reached one million activations, a scale previously unheard of on the Polish banking market
<b>MOBILE TRENDS AWARDS 2016</b>	PKO Bank Polski SA received the Mobile Trends Awards 2016 trophy in the 'mobile banking' category for the IKO application (a proprietary mobile application of PKO Bank Polski SA, on the basis of which the interbank mobile payment standard BLIK was built). It was the sixth time that the Mobile Trends Awards were granted for the best mobile solutions. The winners were selected by a Jury composed of IT and mobile experts, but Internet users could also vote.
<b>THE 2016 LEADER</b>	The jury of the 2016 Leader technology competition recognized PKO Bank Polski SA for its original project 'the Offer Factory' (Fabryka Ofert). The jury appreciated the innovative solution for analysing customer's needs, automatic generation of personalized offers and their distribution through all sales channels. The aim of this competition, organized by <i>Gazeta Bankowa</i> , is to reward the firms and institutions from the fastest-growing sectors of the Polish economy for their special achievements in the area of modern and innovative technologies.
<b>SAP INNOVATION AWARD 2017</b>	PKO Bank Polski SA received the SAP Innovation Award 2017 for BEHEX - a Big Data solution for collecting and analysing behaviour of the IKO mobile banking application users. The competition committee, consisting of SAP experts, appreciated the innovative nature of the project and the excellent combination of banking know-how with SAP technology.

**THE BEST OF PRODUCTS AND SERVICES**

<b>ZŁOTY BANKIER OF 2016</b>	In the eighth edition of the ranking of the Złoty Bankier PKO Bank Polski SA won the award in the mortgage category for housing loan 'Własny Kąt Hipoteczny'. It has been praised for accessibility, price terms and conditions for debt overpayment and the lending period. Złoty Bankier is the highest ranking assessing banking services and products in Poland. For years the Bank determined the direction for Polish banking indicating the best offer on the market. The organizers of the ranking are: Bankier.pl and the 'Puls Biznesu'.
<b>COMPERIA STARS LEADER 2016</b>	PKO Bank Polski SA won the mortgage loans category in the Comperia Stars 2016 project. The 'Your own place with a mortgage' ('Własny Kąt hipoteczny') loan offered by the Bank won as many as seven (out of 12) monthly rankings prepared by the Comperia.pl portal. As part of the Comperia Stars 2016 project, selected financial products, such as mortgage loans, cash loans, deposits, savings accounts were analysed every month. The criteria for selecting the products were chosen by bank customers. The winners were the entities whose products won a given category the most frequently.
<b>BEST CONTACT CENTER</b>	The Contact Center of PKO Bank Polski SA received an award for the 'Best Call Centre' in the Institution of the Year 2016 service quality survey conducted by the MojeBankowanie.pl web portal. Experts appreciated the consultants' skills, their attitude and the ease of obtaining information by customers.
<b>MASTER OF SALES</b>	PKO Bank Polski SA won the 'Master of Sales' title for the highest amount of guarantees granted in the BGK Master of Sales of Guarantees from the POIG Guarantee Fund competition. In 2016, the Bank granted guarantees in the total amount of PLN 66 million for loans in the total amount of PLN 120 million. As a result, it used the biggest amount of funds from the <i>de minimis</i> guarantee limit among the 10 banks participating in the programme.
<b>BEST CONTACT CENTER</b>	The PKO Bank Polski SA Contact Centre remains the unquestionable service leader in the banking sector. In the 15th wave of the call centre survey conducted by ARC Rynek i Opinia it received a score of 97.7 points (out of 100), which was much above the average (79.2) for all 12 banks participating in the survey. The Contact Centre stood on the podium in this survey for the 12th time and took first place for the eleventh time. The consultants of PKO Bank Polski SA received good notes in such categories as technical service, professionalism, kindness and involvement. The Contact Centre also received good notes in the e-mail contact survey. It got 29.4 points (out of 30) for response time.
<b>PORTFOLIO OF THE YEAR WPROST 2017</b>	PKO Bank Polski SA won in the 'safety' category of the 3rd edition of the Portfolio of the year competition organized by the <i>Wprost</i> weekly. The jury appreciated the Bank's actions aimed at providing millions of



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	<p>Poles with simple and safe access to financial services, the use of new technologies in the security systems and education of customers. It is the third victory of the Bank in this competition. Last year it received the 'Bank for the individual customer' title, and in 2015 its private banking offer was considered the best. The aim of the competition is to promote financial institutions offering the most interesting financial products and services which are new on the market and to recognize sector leaders.</p>
<b>STRONG BRAND</b>	
<b>THE STRONGEST FINANCIAL BRAND</b>	<p>PKO Bank Polski SA remains the strongest financial brand in Poland. It is confirmed by the results of the 13th edition of the prestigious ranking of 'The Most Valuable and Strongest Polish Brands 2016' by the <i>Rzeczpospolita</i> daily, which evaluates recognition on the market, popularity of products, and above all brand value. The Bank's brand was valued at PLN 3.2 billion. Its value has increased by PLN 2 billion since the first ranking in 2006. PKO Bank Polski SA is the third most valuable brand in Poland. The ranking is open to brands that originated in Poland, irrespective of the country of origin of their present owner.</p>
<b>BROKERAGE ACTIVITY</b>	
<b>ACTIVE CAPITAL MARKETS PARTICIPANTS</b>	<p>In their summary of the year 2016 on the stock exchange, the Warsaw Stock Exchange and KDPW granted awards to PKO Bank Polski SA and the Brokerage House of PKO Bank Polski SA. BH was recognized for the highest turnover generated by a market maker on non-treasury bonds traded in sessions on the Catalyst market and the biggest share in the volume of index options trading among market makers. PKO Bank Polski SA took the first place for the highest value of OTC transactions settled with KDPW_CCP in 2016.</p>
<b>THE BEST STOCK MARKET ANALYSTS</b>	<p>Piotr Łopaciuk and Artur Iwański from the Brokerage House of PKO Bank Polski SA took the first and the second place, respectively, in the ranking of the best stock market analysts organized by the <i>Parkiet</i> Stock Exchange Journal. Overall, the Brokerage House analysts won 9 places on the podium in sector classifications, and the entire team took second position. The winners were selected by the managers of IFC, OPF and asset management. The total number of specialists evaluated was 133.</p>
<b>AWARDS GRANTED TO OTHER ENTITIES OF THE GROUP</b>	
<b>LEADER OF THE GROWING INVESTMENT FUND MARKET</b>	<p>PKO TFI SA was recognized by the independent opinion-forming centre <i>Analizy Online</i> as the leader among investment fund companies in terms of the number of customers. In the first quarter of 2017, the number of customers of PKO TFI SA increased by almost 18 thousand. This constitutes one third of all new investment fund customers. As a result, the TFI became the market leader, at the same time outpacing the second best fund in terms of an increase in the number of customers.</p>
<b>'GOLDEN PORTFOLIO'</b>	<p>The 'Golden Wallet' is an award granted by the <i>Parkiet</i> Stock exchange journal to the most efficient managers of investment fund companies (IFC). The award was given to the manager of the PKO Surowców Globalny fund at PKO TFI SA. The PKO Surowców Globalny Fund achieved a rate of return exceeding 76% in 2016 – it is the best result among investment funds operating on the capital market for the past year.</p>
<b>HIGH SCORES</b>	<p>In the first half of 2017, the independent research centre <i>Analizy Online</i> maintained a high score (4 stars) for the PKO Zrównoważony subfund and the PKO Akcji Nowa Europa subfund. According to <i>Analizy Online</i>, the products with 4 or 5 stars are funds that should be included in the investors' portfolios.</p>
<b>AWARD FOR EXCELLENCE</b>	<p>The editors of 'The Covered Bond Report' granted to PKO Bank Hipoteczny SA the Award for Excellence for the volume of covered bonds issued. They appreciated the role of PKO Bank Hipoteczny SA as the pioneer of the covered bond market in Poland and in Central and Eastern Europe and noted that 'the long-awaited first-time quotation of covered bonds denominated in euro started a new era in the Polish market history'. The Awards for Excellence are given once a year by 'The Covered Bond Report' to institutions which made the biggest contribution to the development of the covered bond market.</p>
<b>THE MAIN PRIZE OF THE PRIME MINISTER</b>	<p>ZenCard Sp. z o.o. was appreciated for its innovative activity and received the Main Prize of the Prime Minister in the 'start-up for export' competition at Impact'17 4.0 Economy. In the first half of 2017, the company also received the 'Best Start-up 2017' award at the FutureTech 2017 congress in Warsaw.</p>
<b>HIGH POSITIONS IN RANKINGS IN UKRAINE</b>	<p>In the first half of 2017, KREDOBANK SA occupied high positions in various rankings in Ukraine, including the first place in the mortgage loan category and the second place in the car loan category in the 'top 50 banks in Ukraine' ranking organized by the Financial Club in April, and the second place in the 'Best Product for Small and Medium Business' ranking organized by the <i>Business</i> magazine in June.</p>



## 8. RISK MANAGEMENT

### 8.1 PRINCIPLES OF RISK MANAGEMENT

Risk management is one of the most important internal processes both in PKO Bank Polski SA including in foreign Bank's branches as well as in other companies of the PKO Bank Polski SA Group. Risk management aims at ensuring profitability of business activity, while ensuring proper level of capital adequacy measures and control of risk level and maintaining it within the risk tolerance and limits system applied by the Bank and the Group, in the changing macroeconomic and legal environment. The risk management system supports the execution of the Bank's Strategy in compliance with the Risk Management Strategy. It takes into account the execution of capital objectives desired by the Bank, the risk tolerance level and the capital planning process, including the policy concerning the sources of obtaining capital.

In the PKO Bank Polski SA Group the following types of risk have been identified, which are subject to management (risks considered material were underlined<sup>13</sup>): credit, concentration, currency mortgage loans risk, interest rate, currency, liquidity (including financing risk), commodity price, equity securities prices, other price risk, derivative, operational, lack of compliance and misconduct risk, macroeconomic changes, models, business, loss of reputation, capital, excessive financial leverage and insurance risk<sup>14</sup>.

A detailed description of management policies for particular risks was presented in the Report on capital adequacy and other information subject to publication.

#### PURPOSE OF RISK MANAGEMENT

The purpose of risk management by striving to maintain the risk level within the adopted risk tolerance is to:

- 1) protect shareholder value,
- 2) protect customer deposits,
- 3) support the Group in conducting effective operations.

Risk management goals are achieved in particular by providing appropriate information on risk so as to ensure that the decisions are taken in full awareness of the particular risks involved.

#### MAIN PRINCIPLES OF RISK MANAGEMENT

Risk management in the Group is based especially on the following principles:

- 1) the Group manages all of the identified types of risk,
- 2) the risk management system is appropriate to the scale of the operations and to the materiality, scale and complexity of a given risk and tailored to new risk factors and sources on a current basis,
- 3) the risk management methods (in particular the models and their assumptions) and the risk measurement or assessment systems are tailored to the scale and complexity of the risk, current and envisaged Group's activity and environment in which the Group operates, and are also verified and validated on a periodical basis,
- 4) the area of risk management and debt recovery remains organizationally independent from business activities,
- 5) risk management is integrated with the planning and controlling systems,
- 6) the risk level is monitored on a current basis.
- 7) the risk management system supports the implementation of the Group's strategy in compliance with the risk management strategy, in particular with regard to the level of risk tolerance.

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<sup>13</sup> The significance of the individual types of risk is established at the Group's level. When determining criteria of classifying a given type of risk as significant, an influence of the significance of the risk on the Group's activities is taken into account, whereas the following risk types are distinguished: risk considered as significant a priori – being managed actively, potentially significant – for which significance monitoring is performed periodically, other non-defined or non-occurring in the Group types of risk (insignificant and non-monitored). Based on quantitative and qualitative information, an assessment of significance of given types of risk is performed in the Group periodically. As a result of assessment, a given type of risk is being classified as significant/insignificant. In particular, monitoring is conducted if significant change in activities took place or the profile of the Group changed.

<sup>14</sup> Risk is significant only in insurance companies.



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**THE RISK MANAGEMENT PROCESS**

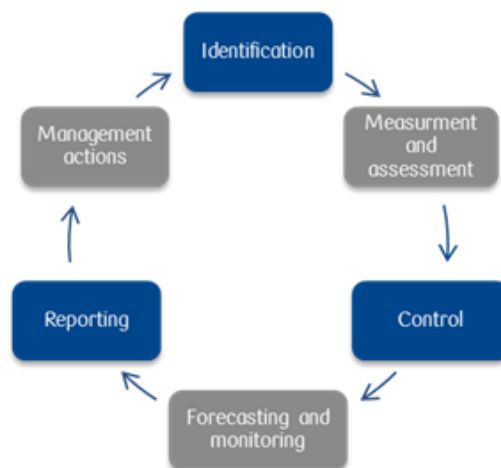
The process of risk management in the Bank's Group consists of the following elements:

▪ **RISK IDENTIFICATION**

Identification of risk aims to recognize of actual and potential sources of risk and estimation of the significance of the potential influence on the financial situation of the Group. Within the risk identification process, types of risk perceived as material in the Bank's, particular Group companies or the entire Group activity are identified.

▪ **RISK MEASUREMENT AND ASSESSMENT**

Risk measurement covering determination of risk assessment measures adequate to the type and significance of the risk, data availability and quantitative risk assessment by means of determined measures, as well as risk assessment aimed at identifying the scale or scope of risk, taking into account the achievement of goals of risk management. Within risk measurement, work related to the valuation of the risks for the purpose of pricing policy and stress-test are being conducted on the basis of assumptions providing a fair risk assessment. Stress-test scenarios cover, among other things, the requirements following from the recommendations of the Polish Financial Supervision Authority. Additionally, complex stress-tests are performed in the Group (KTWS), which constitute an integral element of risk management and supplementary stress-tests specific for particular risks. KTWS also cover an analysis of the impact of changes in the environment (in particular the macroeconomic conditions) and the Bank's operations on the Group's financial position.



▪ **RISK CONTROL**

Risk control is to determine of tools used on diagnosis or reducing the level of risk in specific areas of the Group's activity. This includes determination of control mechanisms adjusted to the scale and complexity of the Bank's and Group's activities especially in the form of strategic tolerance limits for the individual types of risk. The functioning of control mechanisms is ensured by the use of appropriately designed control mechanisms, such as monitoring of the incidents of exceeding strategic risk tolerance limits.

▪ **RISK FORECASTING AND MONITORING**

Forecasting and monitoring risk consists of preparing risk level forecasts and monitoring deviations from forecasts or adopted reference points (e.g. limits, thresholds, plans, measurements from the previous period, recommendations and suggestions issued by the supervisory and control authority) and also carrying out stress-test (specific and complex). Forecasts of the level of risk shall be reviewed. Risk monitoring is performed with the frequency adequate to the materiality and volatility of a specific risk type.

▪ **RISK REPORTING**

Risk reporting consists of periodic informing the authorities of the Bank about the results of risk measurement or risk assessment, taken actions and actions recommendations. Scope, frequency and the form of reporting are adjusted to the managing level of the recipients.

▪ **MANAGEMENT ACTIONS**

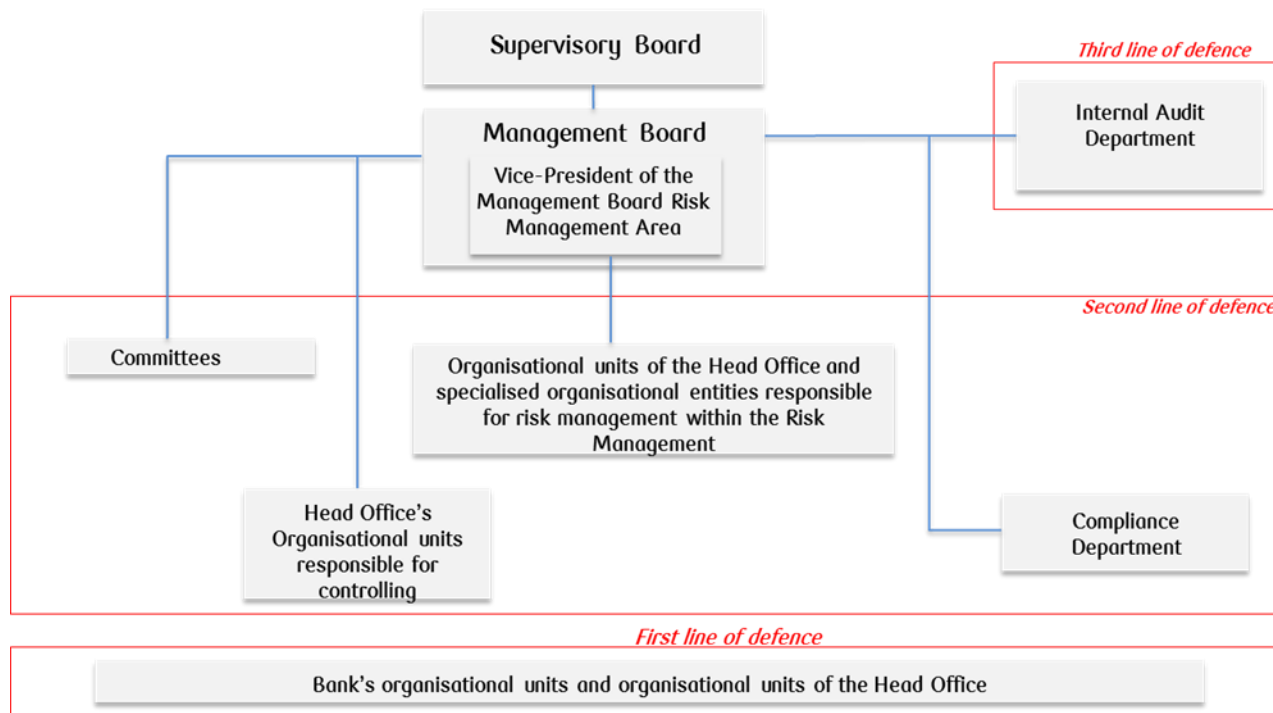
Management actions consist particularly of issuing internal regulations affecting the management process of different types of risk, establishing the level of risk tolerance, setting limits and thresholds, issuing recommendations as well as making decisions about the use of tools supporting risk management. The objective of taking management actions is to form the risk management and the risk level.

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**THE ORGANIZATION OF RISK MANAGEMENT IN THE GROUP**

Risk management in the Bank takes place in all of the organizational units of the Bank.

The organization of risk management in PKO Bank Polski SA is presented in the chart below:



The risk management system is supervised by the Supervisory Board, which controls and evaluates its adequacy and effectiveness. It evaluates whether the individual risk management system elements are used to ensure the correctness of the process of determining and achieving the Bank's detailed objectives. In particular, it verifies whether the system applies formalized principles for determining the amount of risk assumed and the risk management principles, as well as formalized procedures for identification, measurement or assessment and monitoring of risk relating to the Bank's operations, taking into account also the anticipated future risk levels. It verifies whether the risk management system includes formalized risk limits and principles to be applied in the event of exceeding the limits and whether the adopted reporting system makes it possible to monitor the level of risk. The Supervisory Board evaluates whether the risk management system is adjusted to new risk factors and sources on an ongoing basis. The Bank's Supervisory Board is supported, among other things, by the following committees: the Supervisory Board Remuneration Committee, the Supervisory Board Risk Committee and the Supervisory Board Audit Committee.

In respect of risk management, the Management Board of PKO Bank Polski SA is responsible for strategic risk management, including supervising, controlling and monitoring actions taken by the Bank in respect of risk management. Takes the most important decisions affecting the risk profile of the Bank and adopts internal Bank's regulations concerning risk management. The Management Board is supported by the following committees operating in the Bank:

- 1) the Risk Committee (the 'RC'),
- 2) the Assets & Liabilities Management Committee (the 'ALCO'),
- 3) the Bank's Credit Committee (the 'BCC'),
- 4) the Operating Risk Committee (the 'ORC').

The risk management system is carried out in three, mutually independent levels:

- **THE FIRST LEVEL OF DEFENCE** is composed of organizational structures selling products and serving customers and other organizational structures of the Bank whose operations generate risk, operating on the basis of the Bank's internal regulations in this respect,



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- **THE SECOND LEVEL OF DEFENCE** comprises the activities of the compliance unit, as well as identification, measurement or assessment, control, monitoring and reporting of risks that are significant for the Bank and any threats and irregularities identified - these tasks are executed by the Bank's specialized organizational structures operating on the basis of the Bank's internal regulations; the aim of such structures is to ensure that the operations performed on the first level are properly designed and that they mitigate the risks and support the risk measurement and analysis and efficiency of the operations,
- **THE THIRD LEVEL OF DEFENCE** comprises the internal audit, which performs independent audits of various elements of the Bank management system, including the risk management system and the internal control system excluding the audit unit; internal audit operates separately from the first and the second level and may support their operations by providing consultations, but cannot affect the decisions made.

On all three levels, the employees use control mechanisms adjusted to the specific nature of the Bank's operations or monitor the compliance with them independently.

Information on actions taken as part of the risk management and internal control systems and the results of such actions are provided cyclically to the Management Board and the Supervisory Board.

The purpose of the internal control system is to ensure:

- the effectiveness and efficiency of the Bank's operations,
- reliability of financial reporting,
- compliance with the risk management principles at the Bank,
- compliance of the Bank's operations with generally applicable laws, internal regulations of the Bank, supervision recommendations and market standards adopted by the Bank.

The Bank's organizational structure is adjusted to the volume and profile of the risk incurred by the Bank and it is aimed at ensuring effective management of such risk and avoiding conflict of interest, in particular through: distinguishing separate organizational structures managing the individual risks; independence of the organizational structures responsible for risk identification, measurement or assessment, control, monitoring and reporting from the structures whose operations generate risk and full independence of the internal audit structures and the compliance unit in this respect; independence of the organizational structures monitoring the safety of the Bank's IT and information protection system from the Bank's operational structures. The materiality and level of risk associated with the Bank's operations affect the scope of responsibility and level of independence of the organizational structures other than the internal audit and compliance units.

#### RISK MANAGEMENT IN THE GROUP

The Bank supervises activities of the individual subsidiaries of the PKO Bank Polski SA Group. As part of this supervision, the Bank supervises the entities' risk management systems and provides support in the development of these systems. Also, it reflects business risk of the particular entities in the risk reporting and risk monitoring system of the entire Group.

The internal management regulations of certain types of risk in the Bank's Group entities are defined by internal regulations implemented by those entities, after consulting the Bank's opinion and having taken into account the recommendations issued by the Bank. The internal regulations of the entities concerning risk management are introduced based on consistency principle and comparable assessment of particular types of risk within the Bank and Group entities, including the scope and nature of the link entities included in the Group, the specificity and scale of the entity's activity and the market on which it operates.

Risk management at the Group companies is supervised in particular by engaging the Head Office organizational units and specialized organizational units from the Risk Management Division, Compliance Department, Planning and Controlling Department or the Bank's committees in expressing opinions on transactions entered into by the Group companies in accordance with the Bank's internal regulations. A list of the companies which have a material effect on the Group's risk profile is prepared at least once a year. For such companies, the Head Office organizational units and specialized organizational units from the Risk Management Division and the Compliance Department define, according to Bank's internal regulations, the approach to the minimum quantitative strategic tolerance limits for material risks specific to a given company and a method of reporting them.





## 8.1.1 CREDIT RISK

Definition
Management objective
Measurement and assessment of credit risk
Managing foreign currency risk of mortgage loans for households

### DEFINITION

Credit risk is defined as a risk of occurrence of losses due to counterparty's default of payments to the Bank or as a risk of decrease in economic value of amounts due to the Bank as a result of deterioration of counterparty's ability to repay amounts due to the Bank.

### MANAGEMENT OBJECTIVE

The objective of credit risk management is to minimize losses on the credit portfolio and minimize the risk of occurrence of loans threatened with impairment exposure, while keeping expected level of profitability and value of credit portfolio at the same time.

The Bank and other companies of the Group are primarily driven by the following principles of credit risk management:

- loan transaction is subject to comprehensive credit risk assessment, which is reflected in an internal rating or credit scoring,
- credit risk relating to loan transactions is measured on the stage of examining loan application and on a regular basis, as part of the monitoring process taking into consideration changes in external conditions and in the financial standing of the borrowers,
- the independence of credit risk assessment is ensured when such assessment is performed by credit risk units which are independent from business units or when models used in credit risk assessment are built and validated independently of the business units,
- terms of loan transactions that are offered to a customer depend on the assessment of credit risk level generated by the transaction,
- loan granting decisions are made only by authorized persons,
- credit risk is diversified particularly by geographical location, by industry, by product and by customers,
- expected credit risk level is mitigated by collateral received by the Bank, margins from customers and allowances (provisions) for credit losses.

The above-mentioned principles are executed by the Bank through the use of advanced credit risk management methods, both on the level of individual credit exposures and on the level of the whole credit portfolio of the Bank. These methods are verified and developed to ensure compliance with the internal rating method-based requirements (IRB), i.e. advanced credit risk measurement method, which can be used while calculating requirements as regards own funds for credit risk after being approved by the Polish Financial Supervision Authority.

The Group entities, which have significant credit risk levels (the KREDOBANK SA Group, the PKO Leasing SA Group, PKO Bank Hipoteczny SA and a subsidiary: Finansowa Kompania 'Prywatne Inwestycje' Sp. z o.o.) manage their credit risk individually, but the methods used by them for credit risk assessment and measurement are adjusted to the methods used by PKO Bank Polski SA, taking into account the specific nature of the activities of these companies.

Any changes to the solutions used by the Group's subsidiaries are agreed every time with the Bank's units responsible for risk management.

The PKO Leasing SA Group, the KREDOBANK SA Group and the subsidiaries: Finansowa Kompania 'Prywatne Inwestycje' Sp. z o.o. and PKO Bank Hipoteczny SA regularly measure credit risk, and submit the results of such measurements to the Bank.

The KREDOBANK SA Group and the PKO Leasing SA Group have organizational units responsible for risk, which are in particular responsible for:



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- developing methods of credit risk assessment, recognizing provisions and allowances,
- controlling and monitoring credit risk during the lending process,
- the quality and efficiency of restructuring and debt-collection of the amounts due from customers.

In these companies, the credit decision limits depend primarily on: the amount of the exposure to a given customer, the amount of an individual credit transaction and the period of credit transaction.

The process of credit decision-making in the KREDOBANK SA Group, the PKO Leasing SA Group is supported by credit committees, in the case of credit transactions which generate increased credit risk level.

Appropriate organizational entities and units of the Risk Management Area participate in managing the credit risk in the Group entities by giving their opinions on projects and periodically reviewing internal regulations of these companies relating to the assessment of credit risk and preparation of recommendations relating to amendments in the drafts of regulations. The Bank supports implementation of the recommended changes in principles for assessing credit risk in the Group entities.

### MEASUREMENT AND ASSESSMENT OF CREDIT RISK

#### CREDIT RISK MEASUREMENT AND ASSESSMENT METHODS

In order to assess the level of credit risk and profitability of loan portfolios, the Bank uses different credit risk measurement and valuation methods, including:

- probability of Default (PD),
- expected Credit Loss (EL),
- unexpected Credit Loss (UL),
- loss Given Default (LGD),
- credit Value at Risk (CVaR),
- share and structure of impaired loans exposures,
- ratio of loans with recognized impairment (under IAS) to impairment allowances (coverage ratio),
- cost of credit risk.

The Bank develop regularly the scope of credit risk measures used, taking into account the internal rating-based method (IRB) requirements, and extends the use of risk measures to fully cover Bank's loan portfolio with these methods.

The portfolio credit risk measurement methods allow i.a. to reflect the credit risk in the price of products, determine the optimum conditions of financing availability and determine rates of impairment allowances.

The Bank performs analysis and stress-tests regarding the influence of potential changes in macroeconomic environment on the quality of Bank's loan portfolio. The test results are reported to the Bank's authorities. The above-mentioned information enables to identify and take measures to limit the negative influence of unfavourable market changes on the Bank's performance.

#### RATING AND SCORING METHODS

The Bank assesses the risk of individual credit transactions with the use of scoring and rating methods, which are created, developed and supervised by the Credit Risk Centre of Corporate Customer and Credit Risk Centre of Retail Customer. These methods are supported by specialist IT application software. The scoring method is defined by Bank's internal regulations whose main aim is to ensure uniform and objective assessment of credit risk during the lending process.

The Bank assesses the credit risk of retail customers in two dimensions: creditworthiness assessed quantitatively and qualitatively. The quantitative assessment of creditworthiness consists of evaluation of the customer's financial situation, whereas the qualitative assessment involves scoring and evaluating the customer's credit history obtained from internal records of the Bank and external databases.

In the case of corporate customers from the small and medium enterprises segment that meet certain criteria, the Bank assesses credit risk using the scoring method. Such assessment refers to low-value, uncomplicated loan transactions and it is performed in two dimensions: customers' borrowing capacity and his creditworthiness. The assessment of borrowing capacity involves examination of the customer's economic and financial situation, whereas the creditworthiness assessment involves scoring and evaluation of the customer's credit history obtained from internal records of the Bank and external databases.



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In other cases, the rating method is widely used.

The evaluation of credit risk related to financing corporate customers is performed in two dimensions: in respect of the customer and of the transaction. The assessment measures comprise the assessment of the credibility of the customer, i.e. rating; and the assessment of the transaction, i.e. liability repayment capacity in the specified amount and timing.

Rating models for corporate customers were prepared using internal data of the Bank which ensures that they are tailored to the risk profile of the Bank's customers. Models are based on a statistical dependence analysis between the default and a customer's risk scoring. Scoring includes an assessment of the financial indicators, qualitative factors and evaluation of behavioural factors. The customer's risk assessment depends on the size of the enterprise for which analysis is made. In addition, the Bank uses a model for assessment of credited entrepreneurs in the formula of specialist financing, which allows adequate credit risk assessment of large projects involving mainly financing of housing and commercial real estate.

The rating models are implemented in the IT tool supporting the Bank's credit risk assessment related to financing institutional customers.

In order to examine the correctness of functioning of method applied in the Bank, the methodologies of credit risk assessment connected with individual credit exposures are subject to periodical reviews.

The credit risk assessment process in Bank takes into account the requirements of the Polish Financial Supervision Authority as defined i.a. in the recommendation S, relating to best practices for the management of mortgage-secured loan exposures, recommendation T relating to best practices for the management of retail credit exposures, recommendation C relating to the concentration risk management.

The information about ratings and scoring is widely used in the Bank for the purposes of credit risk management, the system of credit decision making powers and in the credit risk assessment and reporting system.

#### **MONITORING OF CREDIT RISK**

Monitoring of credit risk is performed at individual credit transaction level and at portfolio level.

Monitoring of credit risk at the individual credit transaction level is governed, in particular, by the Bank's internal regulations concerning:

- the principles for the recognition of impairment allowances for credit exposures and write-downs of loans payable in respect of unsettled forward transactions,
- the rules of functioning of the Early Warning System in the Bank,
- early monitoring of delays in the collection of receivables,
- the principles for the classification of credit exposures and determining the level of specific provisions.

In order to shorten the time of reaction to the warning signals observed, signalling an increase in the credit risk level, the Bank uses and develops an IT application, an Early Warning System (EWS).

Monitoring of credit risk at the portfolio level consists of:

- 1) supervising the level of the portfolio credit risk on the basis of:
  - a) the adopted tools used for measuring credit risk, taking into consideration the identified sources of credit risk,
  - b) the analysis of the effects and actions taken as part of system management,
- 2) recommending preventive measures in the event of identifying an increased level of credit risk.

#### **THE BANK'S EXPOSURE TO CREDIT RISK CREDIT RISK REPORTING**

The Bank prepares monthly and quarterly credit risk reports. The reporting of credit risk covers specifically cyclic information on the risk exposure of the credit portfolio. In addition to the information concerning the Bank, the reports also contain information about the credit risk level for the Group subsidiaries (i.a. KREDOBANK SA Group and the PKO Leasing SA Group), which have significant credit risk levels.



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#### MANAGEMENT ACTIONS CONCERNING CREDIT RISK

Basic credit risk management tools used by the Bank include:

- minimum transaction requirements (risk parameters) determined for a given type of transaction (e.g. minimum LTV value, maximum loan amount, required collateral),
- the principles of defining credit availability, including cut-offs – the minimum number of points awarded in the process of creditworthiness assessment with the use of a scoring system (for retail customers and SMEs) or the customer's rating class (for corporate customers), which a customer must obtain to receive a loan,
- concentration limits:
  - limits from the Regulation (EU) No. 575/2013 of the European Parliament and the European Council on prudential requirements for credit institutions and investment firms (the CRR) and the Banking Law,
  - additional limits mitigating credit concentration risk, taking into account the requirements of Recommendation C, including strategic risk tolerance limits, e.g. the limit of exposure to a single entity and related entities, applicable to the Bank's and the Group's funds,
- industry-related limits – limits which reduce the risk level related to financing institutional customers that conduct business activities in industries characterized by high level of credit risk,
- limits on credit exposures related to the Bank's customers – the limits defining the appetite for credit risk as result of among others the recommendations S and T,
- credit limits defining the Bank's maximum exposure to a given customer or country in respect of wholesale operations and settlement limits and limits for the period of exposure,
- competence limits – they define the maximum level of credit decision-making powers with regard to the Bank's customers, the limits depend primarily on the amount of the Bank's exposure to a given customer (or a group of related customers) and the loan transaction period; the competence limit depends on the credit decision-making level (in the Bank's organizational structure),
- minimum credit margins – credit risk margins relating to a given credit transaction concluded by the Bank with a given corporate customer, but the interest rate offered to a customer cannot be lower than the reference rate plus credit risk margin.

#### USE OF CREDIT RISK MITIGATION TECHNIQUES - COLLATERAL

Collateral management policy as regards credit risk plays a significant role in establishing minimum transaction terms. The Bank's and the companies of the Group collateral management is meant to secure properly the credit risk, to which the Group is exposed, including first of all the fact of establishing collateral that will give the actual possibility of using them as a possible source of their claims.

In assessing collateral, the following factors are taken into account in particular:

- the economic and financial or social and financial situation of the entities providing personal guarantees,
- the condition and market value of the assets accepted as collateral and their vulnerability to depreciation in the period of maintaining the collateral (the impact of the technological wear and tear of a collateralized asset on its value),
- potential economic benefits of the Bank resulting from a specific method of securing receivables, including, in particular, the possibility of reducing impairment allowances,
- the method of establishing collateral, including the typical duration and complexity of formalities, as well as the necessary costs (the costs of maintaining collateral and the enforcement against the collateral), using the Bank's internal regulations concerning the assessment of collateral,
- the complexity, time-consuming nature and economic and legal conditions of the effective realization of collateral, in the context of enforcement restrictions and the applicable principles for the distribution of the sums obtained from individual enforcement or in the course of bankruptcy proceedings, the ranking of claims.

The type of collateral depends on the product and the customer segment. The policy regarding collateral is defined by the internal regulations of the subsidiaries of the Group.

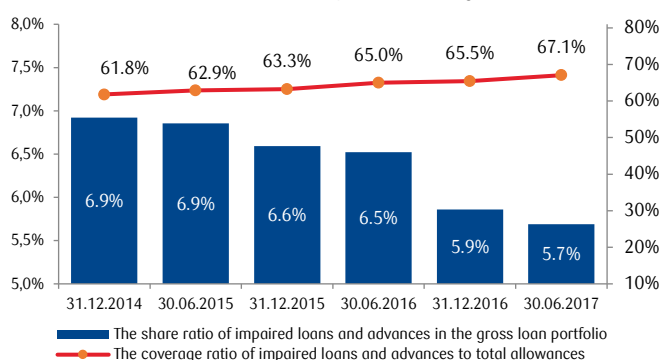
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Table 26. Loan portfolio structure and impairment losses of the PKO Bank Polski SA Group (in PLN million)

	30.06.2017			31.12.2016		
	Gross	Allowances	Net	Gross	Allowances	Net
<b>Loans and advances to customers</b>						
individual basis, of which:						
impaired	5 692	-2 419	3 273	6 551	-2 608	3 943
not impaired	4 575	-2 412	2 163	5 049	-2 594	2 455
portfolio basis	1 117	-7	1 110	1 502	-14	1 488
impaired	7 538	-5 013	2 525	7 183	-4 766	2 417
not impaired	7 528	-5 013	2 515	7 171	-4 766	2 405
group basis (IBNR)	10	0	10	12	0	12
group basis (IBNR)	199 508	-686	198 822	194 875	-629	194 246
<b>Loans and advances granted - net</b>	<b>212 738</b>	<b>-8 118</b>	<b>204 620</b>	<b>208 609</b>	<b>-8 003</b>	<b>200 606</b>

In the first half of 2017 the gross value of loans extended by the Group, assessed using the individual method decreased by PLN 859 million, and assessed using the portfolio method and using the group method increased respectively by PLN 355 million and PLN 4 633 million.

Share of loans and advances with impairment recognized for the PKO Bank Polski SA Group and their coverage ratio with total impairment losses



The share ratio of impaired loans of the PKO Bank Polski SA Group in gross loan portfolio as at 30 June 2017 amounted to 5.7% and dropped by 0.2 p.p. y/y compared with 31 December 2016.

The coverage ratio of impaired loans for the PKO Bank Polski SA Group as at 30 June 2017 amounted to 67.0%, compared with 65.5% as at 31 December 2016.

## RISK MANAGEMENT OF FOREIGN CURRENCY MORTGAGE LOANS FOR HOUSEHOLDS

As the result of the abandonment of EUR/CHF peg by the Swiss National Bank in January 2015 there was a significant appreciation of the Swiss franc against foreign currencies, including the Polish zloty. In the first half of 2017 the exchange rate of the Swiss franc decreased (by approx. 2-3%) in relation to the years 2015 and 2016 (it should be noted that the exchange rates of the Swiss franc in 2015 and 2016 were similar). The Bank constantly analyses the impact of these events on the financial results including the risk of deterioration in the quality of the portfolio of mortgage loans denominated in CHF. The risk is partly mitigated by a decline in reference interest rates, CHF LIBOR and continuing downward trend of the CHF exchange rate.

Due to the fact that the significant appreciation of the CHF against Polish zloty is always a risk arising of an excessive burden for household which took mortgage loans indexed to CHF, thus timely debt service, from the beginning of the 2015 the public debate continues on how to reduce the risk of insolvency of these borrowers. Emerging proposals for system solutions, submitted in form of civil or parliamentary bills, as well as presented by the public and supervisory authorities, may result in incurring losses by the Bank on the portfolio in the future periods.

The Bank has taken a number of actions designed to help the customer and at the same time to reduce the growth of the credit risk associated with the appreciation of the CHF- among other, lowering transaction exchange rates CHF/PLN at which amount payable in CHF is converted (i.e. currency spread) and taking into account the negative LIBOR for all customers.

The Bank monitors the volatility of the exchange rate of the CHF, the value of the portfolio of housing loans denominated in CHF and the impact of the changes in the foreign exchange rates on the capital adequacy on a current basis.

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The value of the portfolio of loans denominated in CHF granted for households systematically decreases. As at the end of the first half of 2017 the value of this portfolio amounted to PLN 27.1 billion compared to PLN 29.8 billion as at the end of 2016 and PLN 30.8 billion as at the end of 2015.

### 8.1.2 INTEREST RATE RISK

<b>DEFINITION</b>	The interest rate risk is a risk of incurring losses on the Group's statement of financial position and off-balance sheet items sensitive to interest rate fluctuations, as a result of changes in the interest rates on the market.
<b>MANAGEMENT OBJECTIVE</b>	Mitigate the risk of potential losses arising from market interest rate changes to an acceptable level by appropriate shaping the structure of statement of financial position and off-balance sheet items.
<b>RISK IDENTIFICATION AND MEASUREMENT</b>	The Group utilizes such interest rate risk measures as: <ul style="list-style-type: none"> <li>• sensitivity of interest income,</li> <li>• sensitivity of economic value,</li> <li>• value at risk (VaR),</li> <li>• stress-tests,</li> <li>• repricing gap.</li> </ul>
<b>CONTROL</b>	Control over interest rate risk covers determining interest rate risk limits and thresholds tailored to the scale and complexity of the Group's operations, in particular the strategic limit of tolerance to interest rate risk.
<b>FORECASTING AND MONITORING</b>	The following, in particular, are monitored by the Group on a regular basis: <ul style="list-style-type: none"> <li>• the level of interest rate risk measures,</li> <li>• the degree of utilization of the strategic limit of interest rate risk tolerance,</li> <li>• the degree of utilization of internal limits and threshold values relating to interest rate risk.</li> </ul>
<b>REPORTING</b>	The reports on interest rate risk are developed on a daily, weekly, monthly and quarterly basis.
<b>MANAGEMENT ACTIONS</b>	The main tools used in interest rate risk management in the Group include: <ul style="list-style-type: none"> <li>• procedures for interest rate risk management,</li> <li>• limits and thresholds for interest rate risk.</li> </ul> <p>The Group established limits and thresholds for interest rate risk comprising i.a. the following: interest income sensitivity, sensitivity of the economic value and loss.</p> <p>Methods of managing interest rate risk in Group subsidiaries are determined by internal regulations introduced by the companies for which the interest rate risk measures are significantly high. These regulations are developed after the Bank's opinion has been sought and in consideration of the recommendations addressed to the companies by the Bank.</p>

As at 30 June 2017 and 31 December 2016, the exposure of PKO Bank Polski SA Group to interest rate risk was within the accepted limits. The Group within adopted limits was mainly exposed to PLN interest rate risk. Of all employed by the Group stress-tests involving a parallel shift of interest rate curves, most unfavourable for the Group was the scenario of a parallel shift in PLN interest curves.

Table 27. VaR PKO Bank Polski SA and stress-test analysis of the Group's exposure to interest rate risk

Name of sensitivity measure	30.06.2017	31.12.2016
VaR for a 10-day time horizon*		361 269
Parallel movement of interest rate curves by 200 b.p. (in PLN million) (stress-test)**	2 020	2 059

\* Due to the nature of the activities carried out by the other Group entities generating significant interest rate risk as well as the specific nature of the market on which they operate, the Group does not calculate consolidated VaR. These companies apply their own risk measures in the interest rate risk management. The KREDOBANK SA uses the 10-day interest rate VaR for the main currencies. As at 30 June 2017 the value of VaR in the KREDOBANK SA amounted to approx. PLN 10.0 million and PLN 8.9 million as at 31 December 2016.

\*\* The table presents the value of the most adverse stress-test of the scenarios: movement of interest rate curves in particular currencies by 200 b.p. up and by 200 b.p. down.



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As at 30 June 2017 the Bank's interest rate VaR for a 10-day time horizon (10-day VaR) amounted to PLN 361 million, which accounted for approximately 1.1% of the Bank's own funds. As at 31 December 2016, VaR for the Bank amounted to PLN 269 million, which accounted for approximately 0.9% of the Bank's own funds.

### 8.1.3 CURRENCY RISK

<b>DEFINITION</b>	Currency risk is the risk of incurring losses due to exchange rate changes. The risk is generated by maintaining open currency positions in a given foreign currency.
<b>MANAGEMENT OBJECTIVE</b>	Mitigate the risk of incurring potential losses arising from exchange rate fluctuations to an acceptable level by appropriate shaping the structure of statement of the financial position and off-balance sheet items.
<b>RISK IDENTIFICATION AND MEASUREMENT</b>	The Group utilizes the following currency rate risk measures: <ul style="list-style-type: none"> <li>• value at risk (VaR),</li> <li>• stress-tests.</li> </ul>
<b>CONTROL</b>	Control over currency rate risk covers determining currency risk limits and thresholds tailored to the scale and complexity of the Group's operations, in particular the strategic limit of tolerance to currency risk.
<b>FORECASTING AND MONITORING</b>	The following, in particular, are monitored by the Group on a regular basis: <ul style="list-style-type: none"> <li>• the level of currency risk measures,</li> <li>• the degree of utilization of the strategic limit of currency risk tolerance,</li> <li>• the degree of utilization of internal limits and threshold values relating to currency risk.</li> </ul>
<b>REPORTING</b>	The reports on currency risk are developed on a daily, weekly, monthly and quarterly basis.
<b>MANAGEMENT ACTIONS</b>	<p>Main tools used in currency risk management in the Group include:</p> <ul style="list-style-type: none"> <li>• procedures for currency risk management,</li> <li>• limits and thresholds for currency risk,</li> <li>• defining allowable types of transactions in foreign currencies and the exchange rates used in such transactions.</li> </ul> <p>The Group has set limits and threshold values for currency risk for i.a.: currency positions, Value at Risk calculated for a 10-day time horizon and loss on currency market.</p> <p>Methods of currency risk management in the Group's subsidiaries are defined by internal regulations implemented by these entities, which are characterized by the significant values of currency risk measures. The regulations are developed after consultation with the Bank and taking into account recommendations issued to the entities by the Bank.</p>

Table 28. VaR PKO Bank Polski SA and stress-tests of the Group's exposure to the currency risk, cumulatively for all currencies

Name of sensitivity measure	30.06.2017	31.12.2016
VaR for a 10-day time horizon*	4	9
Change in CUR/PLN by 20% (stress-test)**	63	25

\* Due to the nature of the activities carried out by the other Group entities generating significant interest rate risk as well as a the specific nature of the market on which they operate, the Parent company does not calculate consolidated VaR. These companies apply their own risk measures in the interest rate risk management. KREDOBANK SA uses the 10-day interest rate VaR for the main currencies, which amounted to approx. PLN 0.16 million as at 30 June 2017 and PLN 0.35 million as at 31 December 2016

\*\* The table presents the value of the most adverse stress-test of the scenarios: PLN appreciation by 20% and PLN depreciation by 20%.



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Table 29. The amount of foreign currency positions in the Group

Currency	Currency position as at 30.06.2017	Currency position as at 31.12.2016
EUR	-371	-170
USD	-93	30
CHF	-7	-37
GBP	2	9
Other (global net)	84	89

The amount of foreign currency positions is the key factor (apart from the volatility of foreign exchange rates determining the level of foreign currency risk to which the Group is exposed. All foreign currency transactions, balance-sheet and off-balance sheet have an impact on the foreign exchange position of the Group. Exposure of the Bank's foreign currency risk is low (in respect of own funds, 10-day VaR for the Bank's foreign exchange position as at 30 June 2017 amounted to approx. 0.01%).

### 8.1.4 LIQUIDITY RISK MANAGEMENT

#### DEFINITION

The liquidity risk is defined as the lack of possibility to pay the debts on time due to the lack of liquid assets. Lack of liquidity may arise from inappropriate structure of the statement of financial position, misfit of cash flows, not received payments from counterparties, sudden withdrawal of cash by customers or other market events.

The Bank manages the financing risk, which takes into account the risk of loss of financing sources and the lack of opportunities to renew matured funding, or loss of access to new financing sources.

#### MANAGEMENT OBJECTIVE

Ensure the necessary level the funds to pay present and future debts (also potential) on time, taking into account the nature of performed activities and requirements which may occur due to changes in market environment, by shaping the structure statement of financial position and off-balance sheet liabilities.

#### RISK IDENTIFICATION AND MEASUREMENT

The Group makes use of the following liquidity risk measures:

- the contractual and adjusted liquidity gap in real terms,
- liquidity reserve,
- liquidity surplus,
- ratio of stable funding to illiquid assets,
- liquidity coverage ratio (LCR),
- national supervisory liquidity measures (M1-M4),
- measure of stability of deposit and loan portfolios,
- stress-tests (liquidity stress-tests).

#### CONTROL

Control over liquidity risk covers determining liquidity risk limits and thresholds tailored to the scale and complexity of the Group's operations, in particular the strategic limit of tolerance to liquidity risk.

#### FORECASTING AND MONITORING

The Group regularly monitors:

- the degree of utilization of strategic tolerance risk losses limit,
- the degree of utilization of supervisory liquidity standards,
- the degree of utilization of internal limits and threshold values relating to liquidity risk,
- concentration of financing sources,
- early warning signals - monitoring their level is aimed at the early discovery of unfavourable phenomena which could have a negative on the Bank's or the financial sector's liquidity position (when exceeded, launch liquidity contingency plans).

The Group also performs forecasts of liquidity risk levels, in consideration of the current developments in the Group's operations. Liquidity forecasts account mainly for the level of particular liquidity risk measures in conditions of realizing the Group's balance sheet forecasts and realizing selected stress-test scenarios.



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**REPORTING**

Liquidity reports are developed: on a daily, weekly, monthly and quarterly basis and, once a year, an in-depth long-term liquidity analysis is conducted.

**MANAGEMENT ACTIONS**

The main tools for liquidity risk management in the Group are as follows:

- procedures for liquidity risk management, in particular liquidity emergency plans,
- limits and thresholds mitigating for liquidity risk,
- deposit, investment and derivative transactions, including structural currency transactions and transactions for sale or purchase of securities,
- transactions ensuring long-term financing of the lending activities.

Methods of liquidity risk management in the subsidiaries of the Group are defined by internal regulations implemented by the entities which are characterized by the significant value of liquidity risk measures. These regulations are developed after consultation with the Bank and take into account recommendations issued to the entities by the Bank.

The Group policy concerning liquidity is based on keeping a portfolio of appropriate level of liquidity surplus through an increase in portfolio of liquid securities and stable sources of financing (stable deposit base, in particular). Liquidity risk management also uses money market instruments, including NBP open market operations.

The Group's liquidity reserve and liquidity surplus as at 30 June 2017 and 31 December 2016 are shown in the table below.

Table 30. Liquidity reserve and liquidity surplus of the PKO Bank Polski SA Group (in PLN billion)

	30.06.2017	31.12.2016
Liquidity reserve up to 1 month*	25	31

\* Liquidity reserve equals the gap between the most liquid assets and expected and potential liabilities which mature in a given period of time.

\*\* Liquidity surplus – liquidity surplus determines the Bank's ability to maintain liquidity on each day during the period called the 'horizon of survival' if predefined stress-test scenarios occur.

The Group's supervisory liquidity measures as at 30 June 2017 and 31 December 2016 are shown in the table below. In the period from 31 December 2016 to 30 June 2017 supervisory measures ratios remained above the supervisory limits.

Table 31. Supervisory liquidity measures

Supervisory liquidity measures	30.06.2017	31.12.2016
M1	16 611	24 464
M2	1.49	1.89
M3	12.72	11.63
M4	1.16	1.19
LCR*	118.0%	136.3%

\* The LCR ratio shows the value for the Group

As at 30 June 2017 the level of permanent balances on deposits constituted approx. 93.9% of all deposits in the Bank (excluding interbank market), which means an increase by approximately 0.1 p.p. as compared to the end of 2016.

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## 8.1.5 OTHER MARKET RISKS

Commodity price risk  
Price risk of equity securities  
Derivative instruments risk  
Other price risks

### COMMODITY PRICE RISK

<b>DEFINITION</b>	Commodity price risk is the risk of incurring a loss due to changes in commodity prices, generated by maintaining open positions on particular types of goods.
<b>MANAGEMENT OBJECTIVE</b>	Reduce potential losses resulting from changes in commodity prices to the acceptable level by shaping the appropriate structure of these items.
<b>RISK IDENTIFICATION AND MEASUREMENT</b>	In respect of the measurement of the prices of commodities in the other companies of the Group, information on the positions taken by the company in particular commodities is utilized.
<b>CONTROL</b>	Control of commodity price risk covers determining respective limits and threshold levels tailored to the scale and complexity of the Group's operations.
<b>FORECASTING AND MONITORING</b>	In respect of the commodity price risk for the Group companies it is regularly monitored, in particular open commodity positions.
<b>REPORTING</b>	Reports on commodity price risks are developed on a daily, weekly, monthly and quarterly basis.
<b>MANAGEMENT ACTIONS</b>	Commodity price risk is managed by imposing limits on instruments generating the commodity price risk, monitoring their use and reporting the risk level. The effect of commodity price risk on the PKO Group's financial position is immaterial. Currently, commodity risk in the remaining Group companies is non-existent.

### PRICE RISK OF EQUITY SECURITIES

<b>DEFINITION</b>	The price risk of equity securities is the risk of incurring a loss due to changes in the prices of equity securities on the public market or stock exchange indices, generated by maintaining open positions in instruments sensitive to changes in these market parameters. The price risk of equity securities results from operations conducted as part of trading activities of the Bank's Brokerage House, investing activities and from other operations as part of banking activities generating a position in equity securities.
<b>MANAGEMENT OBJECTIVE</b>	Limiting possible losses due to changes in the prices of equity securities on the public market or stock exchange indices to acceptable level, by optimizing the positions taken in instruments sensitive to changes in these market parameters.
<b>RISK IDENTIFICATION AND MEASUREMENT</b>	For the purpose of equity securities price risk management the Group utilizes: <ul style="list-style-type: none"> <li>analyses of stress-tests, in consideration of changes in market prices of the base instrument and changes in its volatility,</li> <li>information on the utilization of limits of positions taken in the equity securities portfolio.</li> </ul>
<b>CONTROL</b>	Control over equity securities risk covers determining equity securities risk limits and thresholds tailored to the scale and complexity of the Bank's operations.
<b>FORECASTING AND MONITORING</b>	The Group regularly monitors the level of price risk of equity securities and the level of utilization of the limits on positions taken in the equity securities portfolio.



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<b>REPORTING</b>	Reports on the risk of equity securities are prepared on a monthly and quarterly basis.
<b>MANAGEMENT ACTIONS</b>	The risk is managed by imposing limits on the activities of the Bank's Brokerage House and by monitoring the utilization thereof. The effect of the price risk of equity securities on the financial position of the Group was assessed as immaterial. The positions taken in equity securities and index instruments are limited, and are not expected to increase significantly.

**DERIVATIVE INSTRUMENTS RISK**

<b>DEFINITION</b>	The risk of derivative instruments is a risk resulting from the Bank's taking up a position in financial instruments.
<b>MANAGEMENT OBJECTIVE</b>	Limiting potential losses in respect of changes in factors specific for derivatives (other than foreign currency rates or interest rates) to acceptable levels by appropriate formation of the structure of positions taken in those instruments.
<b>RISK IDENTIFICATION AND MEASUREMENT</b>	<p>For the purpose of measuring derivatives risk, the Group uses:</p> <ul style="list-style-type: none"> <li>• the Value at Risk (VaR) model,</li> <li>• analyses of stress-tests, in consideration of changes in market prices of the base instrument, changes in its volatility, and changes in interest rates,</li> <li>• sensitivity ratios of options.</li> </ul> <p>Information on the positions taken by the companies in particular derivative instruments indicated by the Bank is used in respect of the measurement of derivatives risk in the Group's other companies.</p>
<b>CONTROL</b>	Control over derivatives risk covers determining derivatives risk limits and thresholds tailored to the scale and complexity of the Group's operations.
<b>FORECASTING AND MONITORING</b>	Monitoring the risk of derivative instruments takes place as part of monitoring of other types of financial and credit risk. The Bank puts particular emphasis to monitor financial risk related to the maintenance of currency options portfolio and customer credit risk resulting from amounts due to the Bank in respect of derivative instruments.
<b>REPORTING</b>	In the Group, the reports on risk are developed on a daily, weekly, monthly and quarterly basis.
<b>MANAGEMENT ACTIONS</b>	<p>The main tools used in derivative risk management are as follows:</p> <ul style="list-style-type: none"> <li>• written procedures for derivative risk management,</li> <li>• limits and thresholds set for the risk related to derivative instruments,</li> <li>• master agreements specifying, i.a. settlement mechanisms,</li> <li>• collateral agreements, under which selected customers of the Bank are required to establish a collateral on exposures due to derivative instruments.</li> </ul> <p>Risk management is carried out by imposing limits on the derivative instruments, monitoring limits and reporting risk level.</p> <p>The derivative risk management process is integrated with management of the following types of risk: interest rate, currency, liquidity and credit risk. However, due to the specific nature of derivatives it is subject to special control specified in the internal regulations of the Bank.</p> <p>Master agreements concluded by the Bank with the major business partners based on the standards developed by the Polish Banks Association (domestic banks) and ISDA (foreign banks and credit institutions), which allow offsetting mutual liabilities, both due (mitigation of settlement risk) and not yet due (mitigation of pre-settlement risk), are particularly important for mitigating the risk associated with derivative instruments. Additional collateral for exposures, resulting from derivative instruments are collateral deposits escrowed by counterparties as a part of CSA agreement (Credit Support Annex).</p> <p>Methods of derivative risk management in the Group's subsidiaries are defined by internal regulations implemented by these entities which take up positions in derivative instruments or plan to take positions in</p>



such instruments. These regulations are developed after consultation with the Bank and take into account the recommendations issued to entities by the Bank.

Positions taken by the other Group entities in particular derivative instruments are determined in a similar manner to positions taken by the Bank in such instruments, taking into account the specified economic activity of the entities.

## OTHER PRICE RISKS

Taking into consideration other price risks, in the first half of 2017, the Bank was exposed to price risk of investment fund participation units in collective investment funds. Influence of this risk to the Bank's financial situation is immaterial.

### 8.1.6 OPERATIONAL RISK MANAGEMENT

#### DEFINITION

Operational risk is defined as the risk of occurrence of a loss due to non-compliance or unreliability of internal processes, people and systems or external events. Operational risk takes into account legal risk, and does not include reputational risk and business risk.

#### MANAGEMENT OBJECTIVE

The objective of operational risk management is to enhance collateral of the operational activity pursued by the Bank by improving the efficient, tailored to the profile and the scale of operations mechanisms of identification, assessment and measurement, controlling, monitoring reduction and reporting of operational risk.

The Group companies manage operational risk in accordance with the management risk policies binding in PKO Bank Polski SA, taking into account the scope and type of relations between the entities comprising the Group, the specific nature and scale of operations of particular companies.

#### RISK IDENTIFICATION AND MEASUREMENT

Operational risk management comprises the identification of operational risk in particular through:

- collecting data about the operational risk,
- the self-assessment of operational risk.

In order to manage the operational risk, the Bank gathers internal and external data about operational events and the causes and consequences of their occurrence, data on the factors of the business environment, results of operational risk self-assessment, data on KRI and data related to the quality of internal functional controls.

The operational risk self-assessment comprises identification and assessment of operational risk for Bank's products, processes and applications as well as organizational changes and it is conducted cyclically and before the introduction of new or changed Bank's products, processes and applications.

The measurement of operational risk comprises:

- calculation of Key Risk Indicators (KRI),
- requirement calculation of own funds for operational risk under the AMA (the Bank) and BIA (Branch in Germany, Branch in Czech Republic and companies of the Group covered by prudential consolidation),
- stress-tests,
- calculation of Group's internal capital.

#### CONTROL

Control of operational risk includes setting tailored to the scale and complexity of the Bank's and the Group's activities risk controls in the form of limits on operational risk, in particular the strategic limits of tolerance and operational risk, losses limits, KRI with thresholds and critical values.

#### FORECASTING AND MONITORING

The Bank regularly monitors:

- utilization level of strategic tolerance and operational risk losses limits for the Bank,
- operational events and their consequences,
- results of operational risk self-assessment,
- requirement in respect of own funds as regards to operational risk in accordance with the BIA approach in respect of the operations of the Bank's branch in Germany, in Czech Republic and the AMA approach in respect of the Bank's remaining operations, and the BIA approach in respect of the Group companies covered by prudential consolidation,
- stress-tests results,



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- Key Risk Indicators (KRI), in relations to threshold and critical values,
  - the level of risk in the Bank and the Group, areas and tools for operational risk management in Bank,
  - effectiveness and timeliness of actions undertaken to reduce or transfer the operational risk,
  - management activities, related to the presence of elevated or high levels of operational risk and their effectiveness in reducing the level of operational risk.
- 

#### REPORTING

Information relating to the Group's operational risk is reported for the purpose of senior management, the Operational Risk Committee, the Risk Committee, the Management Board and the Supervisory Board.

Quarterly reports include in particular information on:

- the Bank's operational risk profile,
- the level of operational risk for the Bank, and the areas and tools for managing operational risk,
- the results of measuring and monitoring operational risk,
- the actions taken to limit operational risk and assessing the effectiveness of the actions taken to lower the level of operational risk,
- recommendations, decisions and suggestions of the Operational Risk Committee or the Management Board.

Information on operational risk is prepared in monthly cycles and addressed to senior management, organizational units of the Head Office and specialist organizational units responsible for systemic management of operational risk. The scope of information is diversified and adapted to the scope of responsibilities of particular addressees.

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#### MANAGEMENT ACTIONS

Management actions are taken in the following cases:

- on ORC's initiative or Management Board,
- on the initiative of organizational units and cells of the Bank managing operational risk,
- when operational risk exceeded levels described by Management Board or ORC.

Especially when the risk level is elevated or high, the Bank uses the following approach and instruments of operational risk management:

- 1) risk reduction – mitigating the impact of risk factors or the consequences of its materialization by introducing or strengthening various types of instruments for managing operational risk such as:
    - control instruments (i.a. authorization, internal control, separation of function),
    - human resources management instruments (human resources selection, employees qualification development, motivating system)
    - determination or verification of threshold values and critical KRIs,
    - determination or verification of operational risk levels,
    - contingency plans.
  - 2) risk transfer – transfer of responsibility for covering potential losses on a third-party:
    - insurance,
    - outsourcing.
  - 3) risk avoidance – resignation from activity that generates risk or elimination the probability of the occurrence of a risk factor.
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### 8.1.7 OTHER RISK

Detailed information on how to manage risks of: compliance and conduct, business, loss of reputation, models, macroeconomic changes, capital, insurance and excessive leverage have been described in the PKO Bank Polski SA Group Directors' Report for the year 2016 and in the Report on capital adequacy and other information subject to publication of the Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna Group as at 31 December 2016.

### 8.1.8 COMPLEX STRESS-TESTS

Complex stress-tests are an integral part of the Bank's risk management and are complementary to stress-tests specific to particular types of risks. They collectively include the types of risk considered by the Bank to be material. They include an analysis of the impact of changes in the environment and the functioning of the Bank on the Bank's financial position, in particular: report on the financial situation, the income statement, own funds, capital adequacy and selected liquidity measures.



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Complex stress-tests for the Bank's own use are carried out once every six months in a three-year horizon, taking into account changes in the value and structure of report on the financial situation and income statement items (dynamic tests). Supervisory tests are carried out at the request of the supervisory authorities in accordance with the assumptions provided by the supervisory authorities.

### 8.1.9 CAPITAL ADEQUACY<sup>15</sup>

Managing of capital adequacy is a process whose objective is to ensure that the level of risk which the Bank and the Group takes in connection with the development of its business activities may be covered with its capital, taking into account a specific risk tolerance level and time horizon. The process of managing capital adequacy comprises, in particular, compliance with the applicable regulations of the supervisory and control authorities, as well as the risk tolerance level determined within the Bank and the Group of the capital planning process, including the policy concerning the sources of acquisition of capital.

The objective of capital adequacy management is to maintain own funds at a level that is adequate to the scale and profile of the risk relating to the Group's activities continuously.

The process of managing the Group's capital adequacy comprises:

- specifying and pursuing the Group's capital objectives,
- identifying and monitoring material types of risk,
- assessing internal capital to cover the individual risk types and total internal capital,
- establishing internal capital adequacy limits,
- forecasting, monitoring and reporting the level and structure of equity and capital adequacy,
- managing the structure of the statement of financial situation to optimize the quality of the Group's own funds,
- capital emergency action,
- allocating own funds and internal capital requirements to business areas and customer segments in the Bank and particular companies of the Group,
- assessing the profitability of the individual business areas and customer segments.

The main capital adequacy measures are:

- capital adequacy ratio,
- the relation of own funds to internal capital,
- Tier 1 core capital ratio,
- Tier 1 capital ratio,
- leverage ratio.

Pursuant to Article 92 of the CRR, the minimum capital ratios maintained by the Group and the Bank amount to:

- 1) capital adequacy ratio (TCR) – 8.0%,
- 2) Tier 1 capital ratio (T1) – 6.0%,
- 3) Tier 1 core capital ratio (CET1) – 4.5%.

At the same time, the Group and the Bank are obliged to abide by additional requirements imposed by the PFSA and requirements resulting from the Act on macroprudential supervision.

Pursuant to the CRR, for the purposes of prudential consolidation the Group is composed of: PKO Bank Polski SA, the PKO Leasing SA Group, PKO BP BANKOWY PTE SA, PKO Towarzystwo Funduszy Inwestycyjnych SA, the KREDOBANK SA Group, PKO Finance AB, Finansowa Kompania 'Prywatne Inwestycje' Sp. z o.o., PKO BP Finat Sp. z o.o., PKO Bank Hipoteczny SA, Bankowe Towarzystwo Kapitałowe SA and 'Inter-Risk Ukraina' Sp. z d.o.

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<sup>15</sup> Own funds for the purposes of capital adequacy are calculated in accordance with the provisions of the Banking Act and Resolution (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012.





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As at 30 June 2017, the capital adequacy ratio (TCR) of the Group amounted to 16.85%, and the Tier1 core capital ratio (CET1) amounted to 16.00%. The capital adequacy ratio (TCR) of PKO Bank Polski SA amounted to 18.82% and the Tier1 core capital ratio (CET1) amounted to 17.92%. The Group and the Bank maintained a safe capital base above the supervisory and regulatory limits.

In the first half of 2017, the Group maintained a safe capital adequacy level, above supervisory and regulatory levels.

Table 32. Capital adequacy in the PKO Bank Polski SA Group

	30.06.2017	31.12.2016
<b>Total own funds</b>	<b>31 877</b>	<b>30 873</b>
<b>Tier 1 capital</b>	<b>30 276</b>	<b>28 350</b>
Tier 1 capital before regulatory adjustments and reductions, of which:	33 448	32 060
Share capital	1 250	1 250
Other reserves	30 891	27 970
General banking risk fund for unidentified banking risk	1 070	1 070
Retained earnings	237	1 770
(-) Goodwill	(1 160)	(1 160)
(-) Other intangible assets	(1 683)	(1 821)
Accumulated other comprehensive income	(305)	(709)
Deferred income tax assets, dependent on future profitability, not derived from temporary differences	-	(1)
Adjustments in Tier 1 basic capital due to prudential filters	36	30
Other adjustments in transitional period in Tier 1 basic capital	(60)	(49)
<b>Tier 2 capital</b>	<b>1 601</b>	<b>2 523</b>
Equity instruments and subordinated loans eligible as Tier 2 capital	1 601	2 523
<b>Requirements as regard own funds</b>	<b>15 134</b>	<b>15 626</b>
Credit risk	14 008	14 271
Operational risk	619	657
Market risk	486	651
Credit valuation adjustment risk	21	47
<b>Total capital adequacy ratio</b>	<b>16.85%</b>	<b>15.81%</b>
<b>Tier 1 capital ratio</b>	<b>16.00%</b>	<b>14.51%</b>

The Regulation of the Minister of Development and Finance increasing the risk weights for exposures secured with mortgages on properties whose purchase was financed with foreign currency loans was published in the Journal of Laws on 1 June 2017. The risk weight for exposures secured with a mortgage on a residential property amounts to 150% if the amount of a principal or interest instalment depends on changes in the exchange rate(s) of a currency or currencies other than the currency in which the borrower earns income. The Regulation will enter into force on 1 December 2017.

In connection with a recommendation of the Financial Stability Committee, a draft Regulation of the Minister of Development and Finance on the systemic buffer is being analysed. Imposing a systemic risk buffer of 3% on all exposures in the territory of Republic of Poland is planned. The systemic risk buffer will be maintained by all institutions which have received the approval of the Polish Financial Supervision Authority for conducting banking operations.

## 9. INFORMATION FOR INVESTORS

Share capital and shareholding structure of PKO Bank Polski SA  
Share price of PKO Bank Polski SA at the Warsaw Stock Exchange  
Limitations on the shares of PKO Bank Polski SA  
Assessment of financial credibility of PKO Bank Polski SA  
Investor relations

### 9.1 SHAREHOLDERS THAT HOLD DIRECTLY, INDIRECTLY OR THROUGHOUT SUBSIDIARIES SIGNIFICANT BLOCK OF SHARES AT LEAST 5% OF THE TOTAL NUMBER OF VOTES AT THE GENERAL SHAREHOLDERS' MEETING

To the best knowledge of PKO Bank Polski SA, as at 30 June 2017 the shareholders holding, directly or indirectly, considerable block of shares (at least 5%) were three entities: the State Treasury, Aviva Otwarty Fundusz Emerytalny and Nationale-Nederlanden Otwarty Fundusz Emerytalny.

Table 33. Shareholding structure of PKO Bank Polski SA

	As at 30.06.2017		As at 31.03.2017		Change in the number of votes at GSM (p.p.)
	Number of shares	Share in the total number of votes at the GSM	Number of shares	Share in the total number of votes at the GSM	
The State Treasury	367 918 980	29.43%	367 918 980	29.43%	-
Aviva Otwarty Fundusz Emerytalny <sup>1)</sup>	83 952 447	6.72%	83 952 447	6.72%	-
Nationale-Nederlanden Otwarty Fundusz Emerytalny (until 23.06.2015 ING Otwarty Fundusz Emerytalny) <sup>2)</sup>	64 594 448	5.17%	64 594 448	5.17%	-
Other shareholders <sup>3)</sup>	733 534 125	58.68%	733 534 125	58.68%	-
<b>Total</b>	<b>1 250 000 000</b>	<b>100.00%</b>	<b>1 250 000 000</b>	<b>100.00%</b>	<b>-</b>

1) Number of shares held as at 29 January 2013, reported by Aviva OFE after exceeding the threshold of 5% share in PKO Bank Polski SA's shareholding structure after settlement the transaction of sale of 153.1 million of PKO Bank Polski SA's shares by BGK and the State Treasury.

2) Number of shares held as at 24 July 2012, reported by ING OFE (currently Nationale-Nederlanden OFE) after exceeding the threshold of 5% share in PKO Bank Polski SA's shareholding structure after settlement the transaction of sale of 95 million shares of PKO Bank Polski SA by the State Treasury.

3) including Bank Gospodarstwa Krajowego, which, at the publication date of this report, held 24 487 297 shares, constituting 1.96% share in the number of votes at the General Shareholders' Meeting

There are no special control rights resulting from PKO Bank Polski SA shares for their holders.

### 9.2 SHARES OF PKO BANK POLSKI SA HELD BY MEMBERS OF THE BANK'S AUTHORITIES

The Bank's shares held by the members of the Management Board and the Supervisory Board of PKO Bank Polski SA as at 30 June 2017 are presented in the table below. The nominal value of each share is PLN 1.

Table 34. Number of shares held by PKO Bank Polski SA

No.	Name and surname	Number of shares as at 30.06.2017	Acquisition	Disposal	Number of shares as at 31.03.2017
<b>Management Board</b>					
1.	Zbigniew Jagiełło, President of the Management Board	11 000	0	0	11 000
2.	Rafał Antczak*, Vice-President of the Management Board	0	0	0	x
3.	Janusz Derda**, Vice-President of the Management Board	0	0	0	0
4.	Bartosz Drabikowski, Vice-President of the Management Board	0	0	0	0
5.	Maks Kraczkowski, Vice-President of the Management Board	0	0	0	0
6.	Mieczysław Król, Vice-President of the Management Board	5 000	0	0	5 000
7.	Piotr Mazur, Vice-President of the Management Board	4 500	0	0	4 500
8.	Jakub Papierski, Vice-President of the Management Board	3 000	0	0	3 000
9.	Jan Emeryk Rościszewski, Vice-President of the Management Board	0	0	0	0

\*) appointed to the Bank's Management Board on 14 June 2017

\*\*\*) Mr. Janusz Derda resigned from membership in the Bank's Management Board at the end of 9 August 2017



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As at 30 June 2017, the Members of the Supervisory Board of PKO Bank Polski SA did not hold any shares and stocks in PKO Bank Polski SA.

As at 30 June 2017, Members of the Supervisory Board and the Management Board of PKO Bank Polski SA did not hold shares and stocks in companies related to PKO Bank Polski SA defined as subsidiaries, jointly controlled entities and associates.

**9.3 ASSESSMENT OF FINANCIAL CREDIBILITY OF PKO BANK POLSKI SA**

Rating of PKO Bank Polski SA  
Rating of PKO Bank Hipoteczny SA

**RATING OF PKO BANK POLSKI SA**

The rating agencies Moody's Investors Service and Standard and Poor's (which assigns a paid rating to the Bank in accordance with their own procedures for assessing banks), issued financial credibility ratings for PKO Bank Polski SA in the first half of 2017.

Table 35. Ratings of PKO Bank Polski SA as at 30 June 2017 (paid rating)

<b>Moody's Investors Service</b>	
Long-term deposit rating	A2 with a stable outlook
Short-term deposit rating	P-1
Senior unsecured debt rating	A3 with a stable outlook
MTN Programme Liability rating	(P)A3
Short-term liabilities rating	(P)P-2
Long-term counterparty risk assessment	A2(cr)
Short-term counterparty risk assessment	P-1(cr)

On 16 May 2017, Moody's Investors Service informed about an increase in the outlook for the Bank's long-term deposits from negative to stable and about confirmation of the ratings of the Bank's long- and short-term deposits at the A2/P-1 level. Moody's also informed that the other ratings of the Bank remained unchanged.

The increase in the outlook for the Bank's long-term deposits was a result of a similar increase in the outlook for Poland, which was published on 12 May 2017.

In accordance with the Note:

- the rating of long-term deposits was confirmed at the A2 level and the perspective was increased from 'negative' to 'stable',
- short-term deposit rating was confirmed at P-1 level,
- rating for (senior unsecured) liabilities remained unchanged at A3 level, perspective remained unchanged as 'stable',
- MTN Programme liability rating remained unchanged at (P)A3 level,
- rating of other short-term liabilities remained unchanged at (P)P-2 level,
- counterparty risk rating remained unchanged at A2(cr)/P-1(cr) level.

**RATING OF PKO BANK HIPOTECZNY SA**

As at the end of June 2017 PKO Bank Hipoteczny SA had the following ratings granted by Moody's Investors Service (paid rating):

- long-term issuer's rating Baa1 with a stable outlook and short-term issuer rating Prime-2 granted on 7 September 2015 and upheld on 16 May 2016,
- long-term counterparty rating A3(cr) and short-term counterparty rating Prime-2(cr) granted on 7 September 2015 and upheld on 16 May 2016,
- rating for covered bonds issued by PKO Bank Hipoteczny SA and denominated in PLN - Aa3 granted on 11 December 2015,
- rating for covered bonds issued by PKO Bank Hipoteczny SA and denominated in EUR - Aa3 granted on 24 October 2016.



## 9.4 THE RULES FOR CORPORATE GOVERNANCE AND THE SCOPE OF USE

The rules for corporate governance introduced in the form of a document 'Good Practices for Companies Listed on the WSE 2016' Corporate governance principles for supervised institutions, issued by the Polish Financial Supervision Authority

### THE RULES FOR CORPORATE GOVERNANCE INTRODUCED IN THE FORM OF A DOCUMENT 'GOOD PRACTICES FOR COMPANIES LISTED ON THE WSE 2016'

In connection with Good Practices for Companies Listed on the WSE 2016 document, which entered into force on 1 January 2016, the Bank adopted the rules and recommendations contained there, with the reservation that recommendation IV.R.2 concerning the possibility of participating in the General Shareholders' Meeting with the use of the means of electronic communication will not be applied unless the General Shareholders' Meeting makes appropriate amendments to the Bank's Memorandum of Association authorizing the Management Board to organize the General Shareholders' Meeting with the use of electronic communication. Recommendation IV.R.2 is applied by the Bank in the part concerning real-time broadcast of the proceedings of the General Shareholders' Meeting. According to the Bank's experience, its shareholders do not expect more extensive use of the means of electronic communication during General Shareholders' Meetings. PKO Bank Polski SA makes sure that the dates and times of General Shareholders' Meetings are convenient for the shareholders who want to physically participate in such meetings.

Since 1 January 2016 the information about the status of the application by the Bank of recommendations and principles contained in the Best Practices 2016 is available at the Bank's website (<https://www.pkobp.pl/pkobppl-en/investor-relations/corporate-governance/best-practice-of-gpw-listed-companies-2016/>). This information is drawn on the form established by the Warsaw Stock Exchange. It shows the detailed status of compliance or non-compliance with each of the recommendations and principles and is direct settlement of the rule I.Z.1.13.

### CORPORATE GOVERNANCE PRINCIPLES FOR SUPERVISED INSTITUTIONS, ISSUED BY THE POLISH FINANCIAL SUPERVISION AUTHORITY

On 9 December 2014, the Bank's Management Board adopted for use the Corporate Governance Principles for supervised institutions (adopted by the Polish Financial Supervision Authority at the meeting on 22 July 2014) concerning the responsibilities and obligations of the Management Board, i.e. conducting the Bank's affairs and representing it, in compliance with the generally binding laws and the Bank's Memorandum of Association, with the provision that paragraph 8, clause 4 of the Principles, insofar as it relates to allowing the shareholders the possibility to participate in the meetings of the decision-making authority electronically, will not be applied unless the General Shareholders' Meeting makes appropriate amendments to the Bank's Memorandum of Association authorizing the Management Board to organize the General Shareholders' Meeting using electronic means of communication. Chapter 9 of the Principles, concerning the managing of assets at the customer's risk, will not be applied due to the fact that the Bank does not conduct such activities.

On 17 December 2014, the Bank's Supervisory Board adopted for use the Corporate Governance Principles for supervised institutions concerning the responsibilities and obligations of the Supervisory Board, i.e. supervising the conducting of the Bank's affairs in compliance with the generally binding laws and the Bank's Memorandum of Association.

General Shareholders' Meeting convened for 25 June 2015 declared in resolution No. 50/2015 that acting in line with its competencies it will be guided by the principles of corporate governance for supervised institutions issued by the PFSA, however it ruled out the application of the principles set out in:

- § 8 clause 4 Principles for ensuring the possibility of electronic participation of shareholders in meetings of the decision-making body,
- § 10 clause 2 Principles for introduction of personal rights or other special rights for shareholders,
- § 12 clause 1 Principles on responsibility of shareholders for immediate recapitalization of supervised institution,
- § 28 clause 4 Principles of assessing by the decision-making body whether the determined remuneration policy promotes the development and security of the institution supervised.

Withdrawal from the application of principles set out in § 8 clause 4 was in line with the prior decision of the OGM of PKO Bank Polski SA dated 30 June 2011, expressed through the failure to adopt the resolution on amendments to the



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Memorandum of Association of the Bank, whose aim was to enable participation in the General Meeting through electronic means of communication.

The decision ruling out rule was taken because of legal and organizational-technical risks, which could threaten the proper conduct of the General Meeting. Exclusion of the application of this principle by the AGM was consistent with the opinion of the Management Board not to use it, adopted due to the fact that the current rules of the Bank about participation in General Meetings allow shareholders the effective implementation of all rights from shares and protect the interests of all shareholders.

Withdrawal from other 'Principles of Corporate Governance for supervised institutions', indicated in the resolution of OGM, was due to issuing of these proposals by a qualified shareholder of the Bank - Treasury and then adoption by the OGM through the adoption of resolution no. 50/2015. According to the substantiation presented by the State Treasury along with a proposal for draft resolutions of the OGM, resignation from application of the principles set out in § 10 clause 2 and § 12 clause 1 was justified by unfinished privatization process of the Bank by the Treasury.

Withdrawal from applying of principles set out in § 28 clause 4 was substantiated, according to the request of the Treasury, with too wide range of remuneration policy evaluated by the decision-making body. In the opinion of the above mentioned shareholder, remuneration policy of the employees performing key functions but not being members of the governing body, should be subject to an assessment of their employer or principal, that is the Bank represented by the Management Board and controlled by the Supervisory Board. The text of the Principles can be found on the website of the Polish Financial Supervision Authority at the following address: <https://www.knf.gov.pl/en/regulations/practice/index.html>

## **9.5 THE MEMORANDUM OF ASSOCIATION OF PKO BANK POLSKI SA**

Principles for amending the Memorandum of Association of PKO Bank Polski SA in the first half of 2017

### **PRINCIPLES FOR AMENDING THE MEMORANDUM OF ASSOCIATION OF PKO BANK POLSKI SA IN THE FIRST HALF OF 2017**

#### **13 MARCH 2017 – RESOLUTION OF EGSM IN THE CHANGES OF THE BANKS'S MEMORANDUM OF ASSOCIATION**

On 13 March 2017, the Extraordinary General Shareholders' Meeting of PKO Bank Polski SA passed a resolution no. 4/2017 on the amendments to the Memorandum of Association of PKO Bank Polski SA. The aim of the changes was to allow a Bank Management Board member other than the President to supervise the Bank's operations associated with legal services and compliance risk. It was specified in the Memorandum of Association which areas of the Bank's operations are supervised by the President, taking into account the issues concerning security, strategy and HR management.

On 10 April 2017 the above-mentioned amendments to the Memorandum of Association of PKO Bank Polski SA were entered in the Register of Entrepreneurs of the National Court Register.

#### **14 JUNE 2017 – DRAFT RESOLUTION EGSM IN THE CHANGES OF THE BANKS'S MEMORANDUM OF ASSOCIATION**

On 14 June 2017, the State Treasury represented by the Minister of Development and Finance proposed to the Ordinary General Shareholders' Meeting of PKO Bank Polski SA convened for 22 June 2017 a draft resolution amending the Bank's Memorandum of Association in the area of the powers of the Bank's authorities, the manner of appointing Management Board members and the principles for disposing with fixed assets. The said amendments are aimed at ensuring compliance with the Act on the management of state-owned assets of 16 December 2016. The amendments to the Bank's Memorandum of Association are also aimed at adjusting their content to the requirements of the new laws applicable to the Bank, including in particular the Regulation of the Minister of Finance of 6 March 2017 on risk management and the internal control system, remuneration policy and a detailed method for estimating internal capital at banks, the Regulation of the European Parliament and of the Council (EU) No. 537/2014 on specific requirements regarding the statutory financial statements audit of public-interest entities and the new Act on registered auditors, audit firms and public supervision. Due to a break in the Ordinary General Shareholders' Meeting, a decision concerning the amendments to the Bank's Memorandum of Association was made after the Meeting was resumed, on 20 July 2017. The amendments made to the Memorandum of Association are specified in detail in the resolution of the Ordinary General Shareholders' Meeting No. 50/2017, which is available on the Bank's webpage:

[http://www.pkobp.pl/media\\_files/b21fa41e-d2b2-4bc6-bfa1-ea333c089b8c.pdf](http://www.pkobp.pl/media_files/b21fa41e-d2b2-4bc6-bfa1-ea333c089b8c.pdf).



## 10. OTHER INFORMATION

### Identification data

The authorities of PKO Bank Polski SA in the reporting period

Significant contracts and important agreements with the Central Bank or supervisory authorities

Published forecasts related to financial results for 2017

Loans and advance contracts, warranties and guarantees not related to the Bank's operating activity

Underwriting agreements and guarantees granted to subsidiaries

Benefits for supervisors and managers

Number of employees in PKO Bank Polski SA and in the PKO Bank Polski SA Group

Proceedings pending before the court, arbitration tribunal or public administrative authority

Seasonality or cyclicity of activities in the reporting period

Information on transaction or a number of transactions concluded by the issuer or its subsidiary with related parties, if were concluded not on arm's length

Post balance sheet significant events

Declaration of the Management Board

### IDENTIFICATION DATA

Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna with its registered office in Warsaw at Puławska 15 Street, 02-515 Warsaw, is registered in the District Court for the capital city of Warsaw in Warsaw, XIII Economic Department of the National Court Register, under entry No. KRS 0000026438. The Company's was granted a statistical No. REGON 016298263 and tax identification number (NIP) 525-000-77-38, share capital (the paid share capital) PLN 1 250 000 000.

### THE AUTHORITIES OF PKO BANK POLSKI SA IN THE REPORTING PERIOD

Table 36. The Management Board of PKO Bank Polski SA as at 30 June 2017

#### ZBIGNIEW JAGIEŁŁO

PRESIDENT OF THE MANAGEMENT BOARD

Appointed on 8 January 2014 again to the position of President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board. Appointed on 14 June 2017 again to the position of President of the Management Board of PKO Bank Polski SA for the next joint term of the Management Board, which commenced on 2 July 2017.

IN CHARGE OF THE PRESIDENT OF THE MANAGEMENT BOARD DIVISION

#### JANUSZ DERDA

VICE-PRESIDENT OF THE MANAGEMENT BOARD

Appointed on 3 November 2016 to the position of Vice-President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board as of 1 December 2016. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the next joint term of the Management Board, which commenced on 2 July 2017.

IN CHARGE OF IT AND SERVICE DIVISION

#### BARTOSZ DRABIKOWSKI

VICE-PRESIDENT OF THE MANAGEMENT BOARD

Appointed on 8 January 2014 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the joint term of the Management Board, which commenced on 2 July 2017.

IN CHARGE OF FINANCE AND ACCOUNTING DIVISION

#### MAKS KRACZKOWSKI

VICE-PRESIDENT OF THE MANAGEMENT BOARD

Appointed on 30 June 2016 to the position of Vice-President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board as of 4 July 2016. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the next joint term of the Management Board, which commenced on 2 July 2017.

IN CHARGE OF INTERNATIONAL AND TRANSACTION BANKING AND COOPERATION WITH SELF-GOVERNMENT BODIES AND GOVERNMENT AGENCIES DIVISION





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**MIECZYŚLAW KRÓL**

VICE-PRESIDENT OF THE MANAGEMENT BOARD  
IN CHARGE OF INSURANCE BANKING DIVISION AND LEGAL AND COMPLIANCE DIVISION

Appointed on 2 June 2016 to the position of Vice-President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board as of 6 June 2016. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the next joint term of the Management Board, which commenced on 2 July 2017.

**PIOTR MAZUR**

VICE-PRESIDENT OF THE MANAGEMENT BOARD  
IN CHARGE OF RISK MANAGEMENT DIVISION

Appointed on 8 January 2014 again to the position of Vice-President of the Management Board of PKO Bank Polski SA, for the previous joint term of the Management Board. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA, for the joint term of the Management Board, which commenced on 2 July 2017.

**JAKUB PAPIERSKI**

VICE-PRESIDENT OF THE MANAGEMENT BOARD  
IN CHARGE OF CORPORATE AND INVESTMENT BANKING DIVISION

Appointed on 8 January 2014 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the next joint term of the Management Board, which commenced on 2 July 2017.

**JAN EMERYK ROŚCISZEWSKI**

VICE-PRESIDENT OF THE MANAGEMENT BOARD  
IN CHARGE OF THE RETAIL MARKET DIVISION

Appointed on 14 July 2016 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the previous joint term of the Management Board as of 18 July 2016. Appointed on 14 June 2017 again to the position of Vice-President of the Management Board of PKO Bank Polski SA for the next joint term of the Management Board, which commenced on 2 July 2017.

On 14 June 2017, the Supervisory Board of PKO Bank Polski SA appointed Mr Rafał Antczak as Vice-President of the Management Board of PKO Bank Polski SA for a joint term of the Management Board, which commenced on 2 July 2017.

Table 37. Composition of the Supervisory Board of PKO Bank Polski SA as at 30 June 2017

**PIOTR SADOWNIK**

CHAIRMAN OF THE SUPERVISORY BOARD

Appointed to the Supervisory Board on 25 February 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. The entity authorized to exercise rights from shares owned by the State Treasury, as Eligible Shareholder, appointed Piotr Sadownik as the Chairman of the Supervisory Board. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017. The entity authorized to exercise rights from shares owned by the State Treasury, as Eligible Shareholder, appointed Piotr Sadownik as the Chairman of the Supervisory Board.

**GRAŻYNA CIURZYŃSKA**

VICE-CHAIRMAN OF THE SUPERVISORY BOARD

Appointed to the Supervisory Board on 30 June 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. The entity authorized to exercise rights from shares owned by the State Treasury, as Eligible Shareholder, appointed Grażyna Ciurzyńska as the Vice-Chairman of the Supervisory Board. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017. The entity authorized to exercise rights from shares owned by the State Treasury, as Eligible Shareholder, appointed Grażyna Ciurzyńska as the Vice-Chairman of the Supervisory Board.

**ZBIGNIEW HAJŁASZ**

SECRETARY OF THE SUPERVISORY BOARD TILL 22 JUNE 2017  
MEMBER OF THE SUPERVISORY BOARD

Appointed to the Supervisory Board on 30 June 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. On 14 July 2016 elected as Secretary of the Supervisory Board. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

**MARIUSZ ANDRZEJEWSKI**

MEMBER OF THE SUPERVISORY BOARD

Appointed again to the Supervisory Board on 22 June 2017 for the joint term of Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened for 22 June 2017.





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**MIROSLAW BARSZCZ**

**MEMBER OF THE SUPERVISORY BOARD** Appointed to the Supervisory Board on 25 February 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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**ADAM BUDNIKOWSKI**

**MEMBER OF THE SUPERVISORY BOARD** Appointed to the Supervisory Board on 25 February 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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**WOJCIECH JASIŃSKI**

**MEMBER OF THE SUPERVISORY BOARD** Appointed to the Supervisory Board on 25 February 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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**ANDRZEJ KISIELEWICZ**

**MEMBER OF THE SUPERVISORY BOARD** Appointed to the Supervisory Board on 25 February 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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**ELŻBIETA MAĆZYŃSKA-ZIEMACKA**

**MEMBER OF THE SUPERVISORY BOARD** Appointed again to the Supervisory Board on 26 June 2014 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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**JERZY PALUCHNIAK**

**MEMBER OF THE SUPERVISORY BOARD** Appointed to the Supervisory Board on 22 June 2017 for the joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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**JANUSZ OSTASZEWSKI**

**MEMBER OF THE SUPERVISORY BOARD** Appointed to the Supervisory Board on 25 February 2016 for the term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 26 June 2014. Appointed again to the Supervisory Board on 22 June 2017 for the next joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened on 22 June 2017.

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On 22 June 2017, the Ordinary General Shareholders' Meeting of PKO Bank Polski SA dismissed the following persons from the Supervisory Board of PKO Bank Polski SA: Mr Piotr Sadownik, Ms. Grażyna Ciurzyńska, Mr Zbigniew Hajłasz, Mr Mirosław Barszcz, Mr Adam Budnikowski, Mr Wojciech Jasiński, Mr Andrzej Kisielewicz, Ms. Elżbieta Maćzyńska-Ziemacka and Mr Janusz Ostaszewski, and then reappointed the above-mentioned persons to the Supervisory Board of PKO Bank Polski SA for another joint term of the Supervisory Board, which commenced on the day of the Ordinary General Shareholders' Meeting convened for 22 June 2017. Moreover, on 22 June 2017, the Ordinary General Shareholders' Meeting of PKO Bank Polski SA appointed Mr Mariusz Andrzejewski and Mr Jerzy Paluchniak to the Supervisory Board of PKO Bank Polski SA for another joint term, which commenced on the day of the Ordinary General Shareholders' Meeting convened for 22 June 2017.

The entity authorized to exercise the rights carried by the shares held by the State Treasury, as the Eligible Shareholder, decided that the number of members of the Supervisory Board of PKO Bank Polski SA shall be 11.

According to the rule No. 111a point 4 of The Banking Law Act, every person appointed to the Supervisory Board and the Management Board meet the requirements determined in the rule No. 22.aa of this Act.



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### SIGNIFICANT CONTRACTS AND IMPORTANT AGREEMENTS WITH THE CENTRAL BANK OR SUPERVISORY AUTHORITIES

The Bank did not conclude any significant agreements with the Central Bank or the regulatory authorities in the first half of 2017. In the first half of 2017 PKO Bank Polski SA subsidiaries did not conclude any significant contracts and did not conclude material contracts with the Central Bank or with the regulators.

### PUBLISHED FORECASTS RELATED TO FINANCIAL RESULTS FOR 2017

PKO Bank Polski SA did not publish forecasts related to financial results for 2017.

### LOANS AND ADVANCES TAKEN, GUARANTEES AND WARRANTIES AGREEMENTS

In the first half of 2017, PKO Bank Polski SA and the companies of the Group did not take out any loans or advances or receive any guarantees or warranties that were not related to operating activity.

### ENFORCEABLE TITLES ISSUED

As at 30 June 2017 issues of bonds of PKO Bank Hipoteczny SA were regulated by the Agreement for the Bond Issue Programme dated 30 September 2015, pursuant to which the maximum value of bonds issued and not redeemed based on the programme is PLN 3 billion, and the Guarantee Agreement dated 30 September 2015 pursuant to which PKO Bank Polski SA is the underwriter of the bonds issue up to a total value to PLN 2 billion.

The Annex to the Bond Issue Programme Agreement of 3 March 2017 increased the programme issue amount from PLN 2 billion to PLN 3 billion, and the Annex to the Guarantee Agreement signed on 3 March 2017 increased the guarantee amount from PLN 1 billion to PLN 2 billion.

As at 30 June 2017, the company's liability under the bonds issued at the nominal value amounted to PLN 1 920.7 million. The bonds with a nominal value of PLN 51.4 million were acquired by PKO Bank Polski SA. They included bonds with a value of PLN 36.4 million, which were acquired under the Guarantee Agreement.

In the first half of 2017, PKO Bank Polski SA issued the following guarantees concerning the subsidiaries, which were open at the end of June 2017:

- a guarantee for up to PLN 36 thousand, securing the liability of PKO Towarzystwo Funduszy Inwestycyjnych SA in respect of a lottery it organized; the guarantee was issued for a period up to 7 September 2018,
- a guarantee for up to EUR 170 thousand, relating to the repayment of liabilities in respect of office space and parking spots leased by PKO Życie Towarzystwo Ubezpieczeń SA; the guarantee was issued for a period up to 28 February 2023,
- a guarantee for up to EUR 326 thousand, relating to the repayment of liabilities in respect of office space and parking spots leased by PKO Leasing SA and a guarantee of up to EUR 27 thousand relating to the repayment of liabilities in respect of office space lease; the guarantees were issued for the periods of up to 31 May 2023 and 31 March 2021, respectively,
- two guarantees for KREDOBANK SA up to a total amount of USD 1 500 thousand, relating to the repayment of loans granted by KREDOBANK SA to customers, four guarantees up to a total amount of USD 279 thousand and one guarantee for up to EUR 81 thousand, relating to a bid bond granted to customers and one guarantee for up to EUR 22 thousand, relating to a performance bond granted to a customer; the guarantees were issued for a period up to May 2018.

### BENEFITS FOR SUPERVISORS AND MANAGERS

Full information on the remuneration and other benefits paid to the members of the Management Board of PKO Bank Polski SA and the Supervisory Board of PKO Bank Polski SA in the reporting period is presented in Note 47 to the condensed interim consolidated financial statements of the PKO Bank Polski SA Group for the six-month period ended 30 June 2017.



## NUMBER OF EMPLOYEES IN PKO BANK POLSKI SA AND IN THE PKO BANK POLSKI SA GROUP

As at 30 June 2017, the number of employees of the PKO Bank Polski SA Group was 28 825 FTEs, which represents a decrease of 42 FTEs y/y. The employment level at PKO Bank Polski SA decreased by 718 FTEs y/y, whereas in the other Group companies (excluding PKO Bank Polski SA) it increased by 676 FTEs y/y. The y/y change in the employment level at the subsidiaries is a result of the development of business activities and changes in the Group structure.

Table 38. Employment in PKO Bank Polski SA and in the PKO Bank Polski SA Group

	As at 30.06.2017	As at 30.06.2016	Change of number of employees
PKO Bank Polski SA	24 725	25 443	-718
Other Group companies	4 100	3 424	676
<b>Total</b>	<b>28 825</b>	<b>28 867</b>	<b>-42</b>

## PROCEEDINGS PENDING BEFORE THE COURT, ARBITRATION TRIBUNAL OR PUBLIC ADMINISTRATIVE AUTHORITY

As at 30 June 2017, the total amount in litigation where the Bank is the defendant, and litigation in which other PKO Bank Polski SA Group companies are defendants (suits) was PLN 373 million, including PLN 19 million in respect of litigation in Ukraine (as at 31 December 2016 the total amount of the said litigation was PLN 449 million), and the total amount of litigation (suits) as at 30 June 2017 where the Bank is the plaintiff and litigation where other PKO Bank Polski SA Group companies are plaintiffs was PLN 1 165 million, including PLN 31 million in respect of litigation in Ukraine (as at 31 December 2016 the total amount under the said litigation was PLN 1 232 million).

The Bank and the Group companies had not been parties to any proceedings before courts, arbitration bodies or public administration bodies relating to liabilities or receivables with a value of at least 10% of the equity of PKO Bank Polski SA.

## SEASONALITY OR CYCLICALITY OF ACTIVITIES IN THE REPORTING PERIOD

PKO Bank Polski SA is a universal bank, which provides services on the territory of Poland, and thus its activities are exposed to similar seasonal fluctuations to those affecting the entire Polish economy. The operations of the other PKO Bank Polski SA Group companies do not show any material traits of seasonality or cyclicity.

## INFORMATION ON THE CONCLUSION BY THE ISSUER OR ITS SUBSIDIARY OF ONE OR MORE TRANSACTIONS WITH RELATED PARTIES, IF THEY WERE CONCLUDED ON OTHER THAN MARKET CONDITIONS

In the first half of 2017, the subsidiaries of PKO Bank Polski SA did not conclude any significant non-arm's length transactions with related parties.

The list of significant transactions between PKO Bank Polski SA and its subsidiaries, including credit debt of these entities to the Bank as at 30 June 2017 was presented in the consolidated condensed interim financial statements of PKO Bank Polski SA Group for the six months period ended 30 June 2017.



## SUBSEQUENT EVENTS

- 1) In the period from 1 July 2017 to 7 August 2017, PKO Bank Hipoteczny SA acquired portfolios of receivables in respect of mortgage-secured housing loans in the amount of PLN 967.6 million under the Framework Agreement for Sale of Receivables signed on 17 November 2015 with PKO Bank Polski SA.
- 2) In the period from 1 July 2017 to 7 August 2017, PKO Bank Hipoteczny SA carried out several issues of bonds with a total value of PLN 772.9 million and at the same time redeemed bonds with a total value of PLN 658.9 million.
- 3) On 18 July 2017 PKO Bank Polski SA issued within eurobonds with the value of EUR 750 million, maturity of 4 years and valuation at the level of 65 basis points above Mid Swap. The bonds will be listed on the Luxembourg Stock Exchange and parallelly on the Warsaw Stock Exchange. This issue is the first one under the new EMTN programme for a total amount of EUR 3 billion, which was opened in May 2017. Under the programme, it will be possible to issue unsecured senior eurobonds and subordinated bonds in euro, US dollars, Swiss francs and Polish zlotys. The funds obtained from the issue will be used for the purposes of the Bank's general business activity. On 20 July 2017 the Moody's Investors Service granted the rating of A3 with a stable outlook for the above-mentioned bonds.
- 4) As of the end of the day of 9 August 2017, Mr Janusz Derda resigned from membership of the Bank's Management Board.
- 5) On 23 August 2017, the Bank has placed an issuance of subordinated bonds with total nominal value amounting to PLN 1 700 million. The issue price of the bonds will be equal to its nominal value and amount to PLN 0.1 million. The bonds will have semi-annual interest period and the interests will be calculated on the basis of nominal value with variable interest rate equal to WIBOR 6M plus 155 b.p. margin during the entire issuance period. Settlement of the issuance will take place on 28 August 2017. Upon the approval of the PFSA, the resources acquired as part of the issuance will be allocated to reserve capital of the Bank. The maturity of issued bonds equals 10 years, however upon the approval of the PFSA, the Bank is entitled to early redemption of aforementioned bonds 5 years after the issue date. The Bank will attempt to introduce the bonds through the multilateral trading facility.



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**DECLARATION OF THE MANAGEMENT BOARD**

The Management Board of PKO Bank Polski SA certifies that, to the best of its knowledge:

- The condensed interim consolidated financial statements of the PKO Bank Polski SA Group for the six-month period ended 30 June 2017 and comparative data have been prepared in accordance with binding accounting and reporting standards and present a true, fair and transparent view of financial condition and results of the PKO Bank Polski SA Group,
- the Directors' Report of the PKO Bank Polski SA Group for the first half of 2017 presents a true view of the development and achievements as well as condition of the PKO Bank Polski SA Group, including a description of the basic risks and threats.

The Management Board of PKO Bank Polski SA certifies that the entity authorized to audit the financial statements and which is performing the audit of annual consolidated financial statements, has been elected in compliance with applicable laws. The entity as well as the certified auditors performing the audit fulfilled all criteria for providing unbiased and independent audit opinion in compliance with applicable laws and professional norms.

The PKO Bank Polski SA Group Directors' Report for the first half of 2017 consists of 90 subsequently numbered pages.

**SIGNATURES OF ALL MEMBERS OF THE BANK'S MANAGEMENT BOARD**

24.08.2017	ZBIGNIEW JAGIEŁŁO	PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	RAFAŁ ANT CZAK	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	BARTOSZ DRABIKOWSKI	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	MAKS KRACZKOWSKI	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	MIECZY SŁAW KRÓL	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	PIOTR MAZUR	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	JAKUB PAPIERSKI	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)
24.08.2017	JAN EMERYK ROŚCISZEWSKI	VICE-PRESIDENT OF THE MANAGEMENT BOARD	..... (SIGNATURE)