Bank Polski

The PKO Bank Polski SA Group Directors' Report for the year 2016

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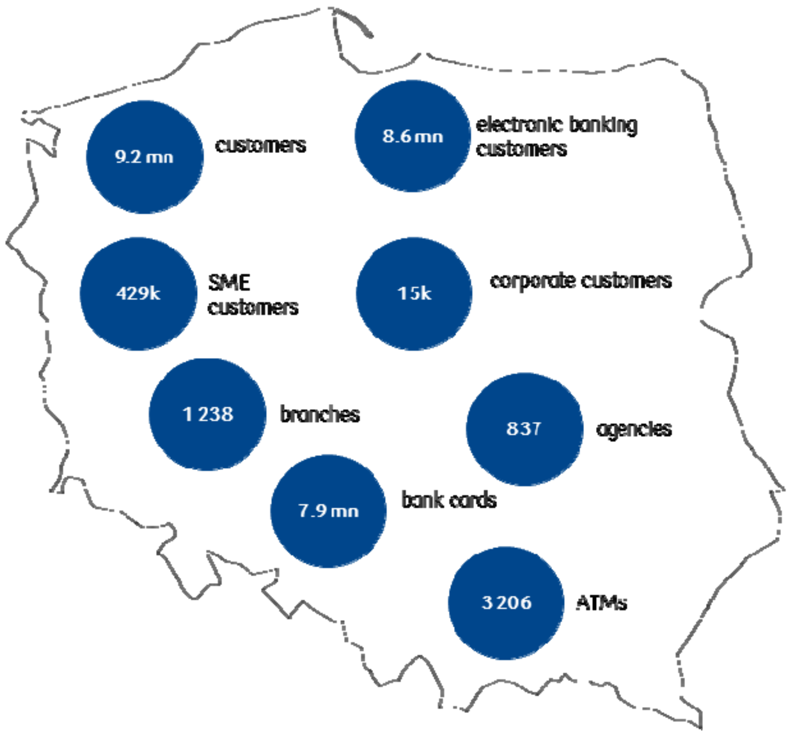
1. INTRODUCTION

1.1 CHARACTERISTICS OF THE PKO BANK POLSKI SA GROUP ACTIVITY

The PKO Bank Polski SA Group (the Bank's Group, the Group) is among the largest financial institutions in Poland and is one of the largest financial groups in Central - Eastern Europe. PKO Bank Polski SA (the Bank), the parent company of the Group, is the largest commercial bank in Poland and a leading bank on the Polish market in terms of scale of operations, equity, loans, deposits, number of customers and the size of the distribution network.

PKO Bank Polski SA is a universal deposit-loan commercial bank offering services to both residents and non-residents retail, corporate and other customers. PKO Bank Polski SA is licensed to hold foreign exchange and currencies and sell/buy them, as well as to perform a full range of foreign exchange services, to open and hold bank accounts abroad and to deposit foreign exchange in these accounts. The Bank stands out on the Polish banking market with high financial results, which ensure stable and safe development of the Bank. PKO Bank Polski SA keeps a leading share in the Polish banking market at the level of 17.3% (deposits) and 17.8% (loans). The Bank is a leader in the Polish market in terms of the number of current accounts, payment cards and the value of mortgage loans.

Apart from the strictly banking and brokerage activities, the PKO Bank Polski SA Group offers a range of specialized services relating to leasing, factoring, investment funds, pension funds and insurance and transfer agent, outsourcing of IT professional, support services in the field of conducting business by other entities, it conducts real estate development and management activities, as well as through its subsidiaries in Ukraine, the Group conducts banking and provides financial services and debt collection.



The Group operates in the Republic of Poland and through its subsidiaries: KREDOBANK SA, 'Inter-Risk Ukraina' Sp. z d.o. (Additional Liability Company), Finansowa Kompania 'Prywatne Inwestycje' Sp. z o.o., Finansowa Kompania 'Idea Kapitał' Sp. z o.o in Ukraine as well as through its subsidiaries PKO Finance AB and PKO Leasing Sverige AB in Sweden and in Germany by a branch of corporate PKO Bank Polski SA (PKO Bank Polski Niederlassung Deutschland) launched in 2015.

During the whole period of activity, the Bank had been consistently developing the prestige of its brand and providing services to many generations of Poles. The long tradition and customers' confidence are the important elements of identification of the PKO Bank Polski SA Group, that's why consistent measures are taken in order to reinforce its perception as a group of institutions:

- secure, strong and competitive,
- modern and innovative, customer-friendly and efficiently managed,
- socially responsible, concerned about the development of the cultural awareness of Poles.

Despite the keen market competition, the PKO Bank Polski SA Group effectively develops its operations not only in its traditional area of operations – serving retail customers. It has also become a leader for corporate customers and small and medium-sized enterprises – especially with regards to financing their operations, and for the market of financial services offered to municipalities, poviats, voivodeships and the public sector. It is also one of the foremost underwriters of municipal bonds.

High standards of customer service and effective procedures for assessing credit risk enabled the PKO Bank Polski SA Group in 2016 to increase gross loan portfolio by over 5% to PLN 200.6 billion and achieve a 22.8% market share in loans to individuals, whereas amounts due to customers as at the end of 2016 reached PLN 205.1 billion thanks to which the Group maintained its leading position in terms of the deposit market share, which amounted to 17.3%.

In 2016, the Group continued its activities concerning the improvement of efficiency of distribution network. As at the end of 2016 the largest network of PKO Bank Polski SA's branches in Poland comprised 1 238 branches and 837 agencies. The Bank's customers can use the systematically enriched electronic banking services offered under the iPKO brand and as a part of Inteligo account and introduced, new standard for mobile payments – IKO. Customers of PKO Bank Polski SA also have an increasing ATMs network at their disposal – as at the end of 2016, there were 3 206 ATMs.

PKO Bank Polski SA Group is one of the largest employers in Poland. As at the end of 2016, the Group employed more than 25 thousand full-time employees. The comprehensive training and education offer served the purpose of building a professional and loyal team of employees able to provide increasingly higher quality customer services and achieve outstanding results.

The Bank's social responsibility is reflected in the operations of PKO Bank Polski SA's Foundation which are performed for the benefit of the public to the widest possible extent.

THE PKO BANK POLSKI SA GROUP IN YEARS 2012-2016

	2016	2015	2014	2013	2012 restated*
Statement of financial position (in PLN million)					
Balance sheet total	285 573	266 940	248 701	199 231	193 151
Total equity	32 569	30 265	27 616	25 154	24 436
Loans and advances to customers	200 607	190 414	179 497	149 623	143 483
Amounts due to customers	205 066	195 759	174 387	151 904	146 194
Profit and loss account (in PLN million)					
Net profit	2 874	2 610	3 254	3 230	3 739
Interest and similar income	7 755	7 029	7 523	6 722	8 089
Fee and commission income	2 693	2 851	2 934	3 006	2 917
Result on business activity	11 791	10 665	11 147	10 707	11 622
Net impairment allowance and write-downs	-1 623	-1 476	-1 899	-2 038	-2 325
Administrative expenses	-5 590	-6 036	-5 245	-4 623	-4 683
Financial ratios					
ROA net	1.1%	1.0%	1.4%	1.6%	2.0%
ROE net	9.1%	9.0%	12.4%	13.2%	16.0%
C/I	47.4%	56.6%	47.1%	43.2%	40.3%
Net interest margin	3.2%	3.0%	3.6%	3.7%	4.7%
Share of impaired loans	5.9%	6.6%	6.9%	8.2%	8.9%
Costs of risk	-0.75%	-0.72%	-0.96%	-1.31%	-1.45%
Total capital ratio	15.81%	14.61%	12.96%	13.58%	12.89%
Client base of the PKO Bank Polski SA (in thousands)	9 199	8 982	8 894	8 451	8 173
Individuals (in thousands)	8 756	8 538	8 431	8 024	7 761
SME (in thousands)	429	430	449	415	401
Corporates (in thousands)	15	14	14	12	12
Operational data					
Branches of the PKO Bank Polski SA (number)	1 238	1 278	1 319	1 186	1 198
Headcount (in FTEs)	29 441	29 221	29 032	27 387	28 556
Current accounts in the PKO Bank Polski SA (in thousands)	6 850	6 621	6 660	6 318	6 220
Stock of shares					
Market capitalization (in PLN million)	35 175	34 163	44 700	49 275	46 125
Number of shares (in million)	1 250	1 250	1 250	1 250	1 250
Share price (in PLN)	28.14	27.33	35.76	39.42	36.90
Dividend per 1 share (in PLN) (paid in current year from the previous year's profit)	0.00	0.00	0.75	1.80	1.27

** Data comparable with 2013*

1.2 Competitive advantages of PKO Bank Polski SA Group

PKO Bank Polski SA Group is distinguished on the Polish financial market with a number of competitive advantages. The key advantages compared with its main competitors include:

The strongest financial brand in Poland

Bank Polski

PKO Bank Polski SA invariably remains the most recognizable bank in Poland. The customers appreciate the brand and associate it not only with a bank that cares for their individual needs but also ensures high security of the entrusted funds. The brand's strength supports the dominating share of PKO Bank Polski SA in the main segments of loan and deposit markets and the share of its subsidiaries which stands out in the investment fund market and lease market. The value of the PKO Bank Polski SA* brand as at the end of 2016 was estimated at PLN 3.6 billion.

* according to *Rzeczpospolita* daily valuation under the ranking of the most valuable Polish brands

The largest distribution network in Poland

The largest multichannel distribution network on the Polish market creates an environment for increasing the revenue not only of PKO Bank Polski SA but also of the entire Group and enables the diversification of revenue sources. The reach of the distribution network enables providing bank products and services in a manner that is the most convenient for the customers. This also applies to persons residing in locations in which the Bank's main competitors do not have their branches.

High quality of customer service

The largest customer base of PKO Bank Polski SA creates an environment for setting the standards of customer service, products and services offered and technological innovations. The potential for setting market standards in association with high strength in the area of enterprise financing provides the bank with a competitive advantage over its largest competitors.

Innovations and payments

PKO Bank Polski SA invests in the development of electronic and mobile banking services, thus dynamically adapting to the changing customer preferences. The project of IKO mobile payments and creating a global scale innovative BLIK payment standard confirmed a high value of the business solutions offered. PKO Bank Polski SA actively cooperates with technological start-ups setting the path for other Polish banks and supports the development of the e-State by using innovative solutions in public administration.

Involvement in the development of Polish entrepreneurship

PKO Bank Polski SA stands out against other banks with a comprehensive product offer addressed to both micro, small and medium and large enterprises. The Bank offers a full range of modern financial solutions: settlement and transaction products, loan and deposit products as well as specialist brokerage and financial services within the scope of leases and factoring. PKO Bank Polski SA follows the needs of Polish entrepreneurs who are open to new development directions and supports them in foreign expansion.

Competent and devoted staff

For many years now PKO Bank Polski SA has belonged to the circle of the most desired employers, both among students and specialists and managers.

Stable base of financing

PKO Bank Polski SA has a secure and stable financing structure based on customer deposits, mainly deposits of retail customers. High assessment of the Bank's financial reliability enables access to financing on the Polish and international bond markets.

1.3 PKO Bank Polski SA Group – historical background

The PKO Bank Polski SA Group strengthens its position as the leader of Polish banking, offering services to retail as well as institutional customers for 98 years.

1919-1938	1. Pocztowa Kasa Oszczędności was established through a decree signed by the Head of the country Józef Piłsudski, prime minister Ignacy Paderewski and Hubert Linde – founder and the first president. 2. Pocztowa Kasa Oszczędności vested with legal personality as a state institution, operating under the supervision and with guarantee of the State. 3. First local branch of Pocztowa Kasa Oszczędności was founded in Poznań. 4. Pocztowa Kasa Oszczędności started to run School Savings Unions (Szkolne Kasy Oszczędności). 5. With the initiative of Pocztowa Kasa Oszczędności, Treasury Ministry has decided to set up Bank Polska Kasa Opieki (today Pekao SA) as a public company to facilitate the Polish Diaspora the transfer of Polish foreign currencies to the country. 6. Pocztowa Kasa Oszczędności strongly contributed to the development of non-cash transactions - every other larger industrial plant and any large company had a cheque account in Pocztowa Kasa Oszczędności, and cheque turnover in Poland was half as much greater than the cash.
1939-1945	Years of war were time of huge losses and standstill in the activity of Pocztowa Kasa Oszczędności.
1946-1987	1. Pocztowa Kasa Oszczędności transformed into Powszechna Kasa Oszczędności. 2. Banking Act introduced privilege of saving deposits held in Powszechna Kasa Oszczędności, they were covered by the State guarantee. 3. Powszechna Kasa Oszczędności introduced a modern product: current account. 4. In years 1975-1987, merged into the structures of the National Bank of Poland (NBP); yet retains its identity.
1991-2000	1. The name Powszechna Kasa Oszczędności – Bank Państwowy, in short PKO BP, appeared in the Articles of Association. The first Supervisory Board of PKO BP was appointed. 2. The Bank became the sole shareholder of the development company Inbudex Sp. z o.o. (currently Qualia Development Sp. z o.o.). 3. The first Internet information portal of the Bank and the first e-PKO Internet branch were launched. 4. PKO Towarzystwo Funduszy Inwestycyjnych SA (PKO TFI) formed by PKO BP and Credit Suisse Asset Management Holding Europe (Luxembourg) SA began its operations. From 2009, the Bank has been the Company's sole owner. 5. PKO BP and Bank Handlowy w Warszawie SA formed PKO BP BANKOWY PTE SA. From 2003, the Bank has been the Company's sole owner. 6. Bankowy Fundusz Leasingowy SA (currently PKO Leasing SA) was formed which provides operating and finance leases of non-current assets and property. 7. PKO BP and Bank Śląski SA formed Centrum Elektronicznych Usług Płatniczych eService SA. From 2001 until 2013, the Bank held 100% shares in the Company. 8. In 2000 the Bank was transformed into a wholly-owned subsidiary of the State Treasury under the name of PKO Bank Polski SA.
2002-2009	1. The Bank acquired Inteligo Financial Services SA, a company providing services within the scope of maintenance and development of ICT systems used in banking systems, also including electronic access to bank accounts (Inteligo account). 2. The Bank acquired 66.65% shares in KREDOBANK SA. The Company is registered and operates in Ukraine. At present, the Bank holds 99.6293% of shares in the Company's share capital. 3. In 2004 Bank's flotation took place - at the end of the first day of quotations, shares reached a price of PLN 24.50 per unit against the issue price fixed at PLN 20.50. 4. PKO BP Faktoring SA began its operations (at present PKO Faktoring SA). 5. The Bank's share capital was increased from PLN 1 000 000 000 to PLN 1 250 000 000 (2009).
2010-2015	1. PKO Bank Polski SA (through its subsidiary PKO Finance AB) issued 5-year Eurobonds with value of EUR 800 million and bonds to the American market in the amount of USD 1.0 billion, which became benchmark securities not only for Polish entities but also for issuers in Central and Eastern Europe. 2. 2013-2015 strategy: 'PKO Bank Polski. Everyday the best' strengthened the Bank's position as a leader in key market segments. 3. In 2013, PKO Bank Polski SA set a new standard for mobile payments – IKO – an innovative solution on the market of mobile payments, transformed in 2015 into the BLIK payment system, which became the Polish market standard.

	4. PKO Bank Polski SA has signed with EVO Payments International Acquisition GmbH an agreement for twenty-year strategic alliance in the electronic payment market and therefore sold a significant portion of shares in eService Sp. z o.o. 5. PKO Bank Hipoteczny SA was formed, the operations of which include issuing long-term mortgage bonds and granting long-term mortgage loans to retail customers. 6. PKO Bank Polski SA acquired shares of Nordea Group, including shares of Nordea Bank Polska SA and a portfolio of amounts due from corporate customers. In October 2014, a legal merger of the banks was carried out. 7. PKO Towarzystwo Ubezpieczeń SA was formed, which provides property insurance services to retail customers of PKO Bank Polski SA. 8. Expansion into foreign markets through actions aimed to establish the first foreign corporate branch of PKO Bank Polski SA abroad (in Frankfurt am Main in the Federal Republic of Germany).
2016	1. Approval of the 2016-2020 strategy: 'We support the development of Poland and the Poles' the objective of which is to continue to strengthen the position of the Bank Group as a leader in key market segments, increase the innovativeness and adapt to customer needs. 2. PKO Leasing SA belonging to the Bank's Group successfully closed the transaction of acquiring Raiffeisen-Leasing Polska SA, thus becoming the main lease provider in Poland with an over 13% market share. 3. PKO Bank Hipoteczny SA effected the issue of mortgage bonds with the highest possible Moody's rating of Aa3 that can be achieved by Polish securities. 4. Continuing the expansion to foreign markets – measures aimed at forming abroad another branch of Bank in the Czech Republic. 5. Starting cooperation with Poczta Polska SA in the scope of payment card handling.

1.4 THE MAIN EVENTS OF 2016

In 2016, the banking sector operated in conditions of historically low levels of interest rates and new regulation burdens, under positive macroeconomic environment. The situation on the loan-deposit market was shaped by the favorable situation on the labor market. The level of domestic demand was supported by the government programme 'Rodzina 500+' and deflation which have been increasing the real purchasing power of households.

In the period under analysis, PKO Bank Polski SA Group continued sustainable growth focused on improving customer service quality by increasing the innovativeness of its products and distribution channels. Initiatives were undertaken to increase the quality of services, among other things, by actions aimed at increasing innovativeness in the area of new financial solutions, both with regards to products and the distribution channels, in particular in the scope of electronic banking and mobile payments.

In 2016, PKO Bank Polski SA introduced a special offer for holders of Karta Dużej Rodziny (Large Family Card) under which the commission for granting housing loans Własny Kąt Hipoteczny was reduced by 50%.

The Group systematically develops electronic banking channels. In 2016, the Bank launched an updated version of the information service which offers more convenient contact with the Bank to the customers and faster access to banking services. The Bank also introduced additional logging security in the form of a security image, which provides customers with a higher level of security when using electronic banking services.

PKO Bank Polski SA offers modern technological solutions to its customers including safe access to banking services available at any place using the telephone. IKO is the most popular and the most developed system of mobile payments in Poland. The aggregate number of IKO activations exceeds one million in 2016. The application is constantly enriched with new functionalities: ability to pay to the telephone number of another IKO user, payments to cash deposit stations using the BLIK code and making payments and transfers using QR codes. The changes have transformed the IKO application used for payments or withdrawals to mobile application being the bank in the phone.

The up-to-date technological solutions of PKO Bank Polski SA have been appreciated by the Chamber of Digital Economy – the Bank was elected the most digitized bank in the competition E-COMMERCE POLSKA AWARDS 2016. The title was granted to Bank in recognition of its involvement in e-administration and cybersecurity projects as well as projects embracing the quality of mobile and electronic banking. This is yet another distinction for the Bank for innovation, implementing leading edge technologies and creating solutions which become a benchmark for other financial institutions.

The development of the product offer was supported by implementing 'Nowy Rytm Sprzedaży' (the New Sales Rhythm) – an innovative sales programme, ensuring wider knowledge about the customers and enabling the presentation of offers to them that are best adapted to their needs, while simplifying the sales processes and formalities. The programme was supported by an integrated incentive system for advisers in the branch network.

In 2016, PKO Bank Polski SA commenced cooperation with Poczta Polska SA (Poczta) within the scope of handling payment cards in Poczta branches. As a result of this cooperation, by the end of 2016, nearly 8 thousand payment terminals were installed in the entire Poczta network thanks to which the customers of more than 4.6 thousand Poczta branches can make card payments for services such as payment of bills or sending parcels.

PKO Bank Polski SA was the first bank to offer its customers the possibility of creating a trusted profile from the level of internet banking. The Trusted Profile enables access to services of various offices through the Internet without leaving home and visiting a given office in person. Thanks to this, customers may electronically register their business activities and at the same time register them with the tax office, the Central Statistical Office and the Social Insurance Office (ZUS, KRUS), and avail themselves of the PUE ZUS function.

In 2016, the Bank strengthened its leading position in the field of services for local governments by signing a contract for complex service for podkarpackie voivodeship and its 23 organizational units. In total, the Bank provides services for 6 voivodeships.

In the third quarter of 2016, PKO Bank Polski SA became a strategic partner of the Polski Fundusz Rozwoju (PFR) Group within the scope of providing the export support offer. PFR will deal with the operational management of financial and advisory products. The value of the support offered by PFR under the Programme of International Expansion of Polish Enterprises may reach up to PLN 60 billion.

In August 2016, the Bank concluded an annex to the agreement for the portfolio guarantee line from the Guarantee Fund of the Innovative Economy Operational Programme (IEOP), thanks to which the Bank obtained the possibility not only of non-revolving working capital loans and investment loans but also BIZNES PARTNER bank overdrafts and working capital revolving loans being covered by guarantees.

The top standards of the procurement processes and business reliability have been confirmed by PKO Bank Polski SA obtaining an international certificate from the Chartered Institute of Procurement and Supply (CIPS). The Bank is the first entity from the financial sector and third in Poland to be thus distinguished.

In June 2016, there has been settlement of acquisition of Visa Europe Limited by the Visa Inc. in which PKO Bank Polski SA was involved. The total amount recognized by the Bank in respect of the settlement of the above-mentioned transaction in the income statement (profit before tax) was PLN 417.6 million, including the amount reflected in other comprehensive income on valuation of shares of Visa Europe Limited of PLN 336.7 million.

In December 2016, PKO Leasing SA belonging to the PKO Bank Polski SA Group successfully closed the transaction of acquiring Raiffeisen-Leasing Polska SA (RLPL), thus becoming the main lease provider in Poland with an over 13% market share. Leasing is the second after loans source of financing of operations of business entities. Already before finalizing the transaction, PKO Leasing SA was the most dynamically developing lease enterprise in Poland. The business models of the companies complement one another. The acquisition of Raiffeisen-Leasing Polska SA will enable increasing the effectiveness of services and ensure a comprehensive offer to enterprises tailored to their needs at each stage of development.

Raiffeisen - Leasing Polska SA acquisition schedule

2016	2 November 2016	Conclusion of the agreement by PKO Bank Polski SA, PKO Leasing SA (PKO Leasing) and Raiffeisen Bank International AG (RBI) on the purchase of 100% of shares in Raiffeisen-Leasing Polska SA (RLPL) by PKO Leasing from RBI.
	10 November 2016	Obtaining the approval of the Antimonopoly Committee of Ukraine
	17 November 2016	Obtaining the approval of the Polish Office of Competition and Consumer Protection (POCCP)
	1 December 2016	Closing of the Transaction, comprising the purchase of 100% of shares in RLPL by PKO Leasing and replacing the financing granted to RLPL by RBI or the RBI Group entities by the PKO Bank Polski SA Group.
	since 1 December 2016	Commencement of operational and IT integration
2017	I half of 2017	Legal merger

In the third quarter of 2016 Qualia Development Sp. z o.o. and its subsidiaries completed two asset sale transactions. As a result, in other net operating income and expenses in the Group's income statement additional income of approx. PLN 114 million was recognized.

In 2016 PKO Bank Hipoteczny SA conducted an issue of mortgage bonds addressed to institutional investors which met with wide interest. The institutions which purchased mortgage bonds included both domestic and foreign investors, including the European Bank of Reconstruction and Development. Mortgage bonds of PKO Bank Hipoteczny SA are one of the safest debt instruments on the Polish financial market. Moody's rating of Aa3, which is the highest rating achievable by Polish securities, attests to this, i.e. in accordance with polish rating.

In October 2016, the Polish Financial Supervision Authority (PFSA) issued a positive opinion on the corporate branch in the Czech Republic. The PFSA studied the Bank's notification application concerning the opening of a corporate branch in Prague and decided to send it over to the competent supervisory authorities in the Czech Republic. Once the notification application is sent by the PFSA, the proceedings before the Polish regulator are completed. The opening of the branch is planned for the 1st half of 2017. The operations of the Czech branch will focus on serving corporate customers.

Actions taken by the PKO Bank Polski SA Group in 2016 despite record low interest rates and significant regulatory changes made it possible to achieve high financial results, allowing the Group to strengthen its position among the largest financial institutions in Poland.

	2016			2015			Change 2016/2015
Net profit	2 874	mn	PLN	2 610	mn	PLN	10.1%
Net interest income	7 755	mn	PLN	7 029	mn	PLN	10.3%
Net fee and commission income	2 693	mn	PLN	2 851	mn	PLN	-5.5%
Result on business activities*	11 791	mn	PLN	10 665	mn	PLN	10.6%
Administrative expenses	(5 590)	mn	PLN	(6 036)	mn	PLN	-7.4%
Tax on certain financial institutions	(829)	mn	PLN	-			x
Net impairment allowance and write-downs	(1 623)	mn	PLN	(1 476)	mn	PLN	9.9%
Total assets	285 573	bn	PLN	266 940	bn	PLN	7.0%
Equity	32 569	bn	PLN	30 265	bn	PLN	7.6%
ROA net	1.1%			1.0%			0.1 p.p.
ROE net	9.1%			9.0%			0.1 p.p.
C/I**	47.4%			56.6%			-9.2 p.p.
Net interest margin	3.2%			3.0%			0.2 p.p.
Share of impaired loans	5.9%			6.6%			-0.7 p.p.
Costs of risk	-0.75%			-0.72%			0 p.p.
Total capital ratio	15.81%			14.61%			1.2 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.

**The ratio of administrative expenses to result on business activities

The net profit of the PKO Bank Polski SA Group generated in 2016 amounted to PLN 2 874.0 million, which represents an increase 10.1%, i.e. by PLN 264.5 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 11 790.7 million (+10.6% y/y) mainly due to:

- an increase in the net interest income of 10.3% y/y, which was achieved thanks to the continuing actions to reduce in the costs of financing of the deposit base and an increase in the amount of interest-bearing assets,

- an increase in other net income of PLN 557.0 million, which was mainly associated with the settlement of the acquisition of Visa Europe Limited by Visa Inc. in June 2016 and sale transaction of asset components of Qualia Development Sp. z o.o. and its related entities in the third quarter 2016,
- at the same time, the net commission income, including, but not limited to, commissions on transactions on securities and loans, decreased by 5.5% y/y,

2) the introduction of tax on certain financial institutions (the bank tax) as of February 2016, which resulted in an additional charge on the financial result of PLN 828.9 million,
3) a decrease in operating expenses of PLN 445.8 million, associated with lower charge due amount of contributions and payments to the Bank Guarantee Fund (BGF) (mainly resulting from the 2015 base effect, i.e. the payment made to the BGF for disbursements of guaranteed funds in respect of deposits with Spółdzielczy Bank Rzemiosła i Rolnictwa in Wołomin[1] and the additional expenses associated with the establishment of the Borrowers' Support Fund). The C/I ratioby the end of 2016 amounted to 47.4% compared with 56.6% at the end of 2015;
4) net impairment allowance and write-downs, which deteriorated by PLN 146.8 million compared with 2015, accompanied by an increase in the gross loan portfolio of 5% and cost of risk at a similar level.

The structure of the statement of financial position of the PKO Bank Polski SA 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, which constitute a further stage in the Bank's development. The loan to deposit ratio (amounts due to customers) as at the end of 2016 amounted to 97.8% (the ratio of loans to stable sources of funding[2] amounted to 83.7%), which proves the very good condition of liquidity of the Group.

As a result of actions taken in 2016 the PKO Bank Polski SA Group:

- increased total assets by almost PLN 19 billion, including portfolio of amounts due from customers by more than PLN 10 billion,
- maintained a high shares of loans and deposits market on the level of 17.8% and 17.3% respectively,
- strengthened the position in the leasing market by acquiring Raiffeisen-Leasing Poland SA,
- was he first on the market with 31.9% share in sales of mortgage loans to individuals[3],
- was the largest lender to small and medium sized enterprises of loans with de minimis guarantees and comprised 22.1% of market share[4],
- significantly improved the quality of the loan portfolio, measured by a ratio of impaired loans,
- increased the number of customers by more than 216 thousand, mainly in the household segment, and increased the number of customers using the IKO mobile banking to more than 1 million at the end of 2016,
- expanded the offer of insurance and investment products, and property insurance for customers, among other things, thanks to starting operating activities by PKO Towarzystwo Ubezpieczeń SA in January 2016,
- strengthened the capital position through action to increase the level of capital base as a result of accumulation of retained earnings for 2015, which resulted in an increase in the total capital ratio of 1.2 p.p. compared to year end of 2015 to a level of 15.8%.

[1] Pursuant to the Resolution of the Management Board of the Bank Guarantee Fund (BGF) No. 87/DGD/2015 of 26 November 2015, banks were obliged to pay a fee within the fund of protection of guaranteed funds (FPOGF) to cover the payments of guaranteed funds to depositors of Spółdzielczy Bank Rzemiosła I Rolnictwa w Wołominie in connection with its bankruptcy.

[2] 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.

[3] The Polish Banks Association Data.

[4] In accordance with data given by the Guarantee Centre of the Bank Gospodarstwa Krajowego as at 31 December 2016.

1.5 DIRECTIONS OF DEVELOPMENT OF THE PKO BANK POLSKI SA GROUP

The development directions of PKO Bank Polski 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

Bank Polski

'WE SUPPORT THE DEVELOPMENT OF POLAND AND THE POLES'

We have provided financial solutions to our customers for more than 100 years; therefore, we understand the needs of the Poles and Polish companies.

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 continue to have a positive impact on Poland – its people, firms, 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 an answer 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:

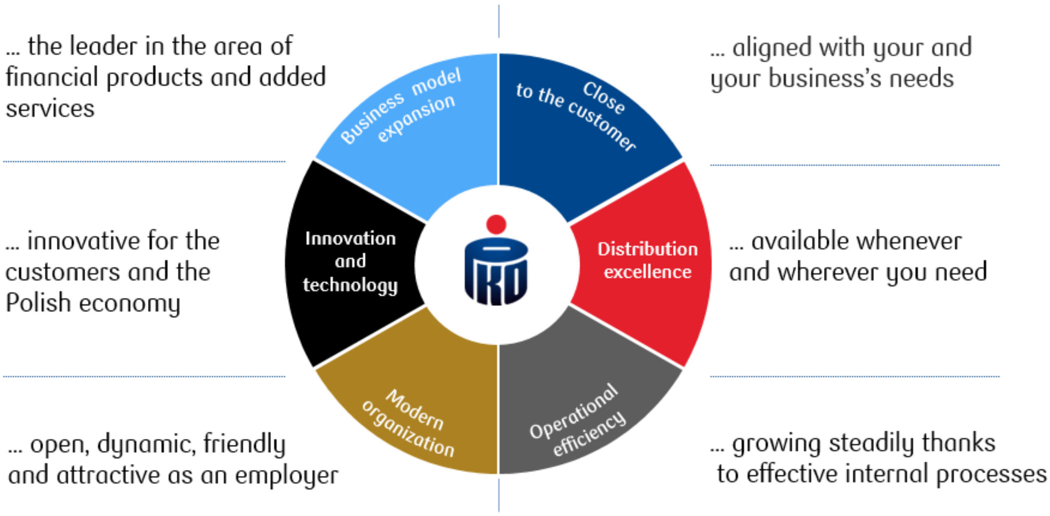
- achieve a return on equity (ROE) of more than 10%,
- reduce the cost to income (C/I) ratio to below 45%,
- maintain the cost of risk within the range of 75-85 b.p.,
- manage its capital adequacy in an efficient and reasonable manner, in order to maintain TCR and CET1 above the regulatory and supervisory 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, 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 strategy based on the levers sustainable growth, in 2020 PKO Bank Polski will be:



Strategy implementation is supported by six sustainable development levers:

1. BEING 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 in 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 customer 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 TECHNOLOGIES

PKO Bank Polski SA will consistently invest in innovative solutions, actively create 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), take part in projects with perspectives and become involved in areas and sectors of the future.

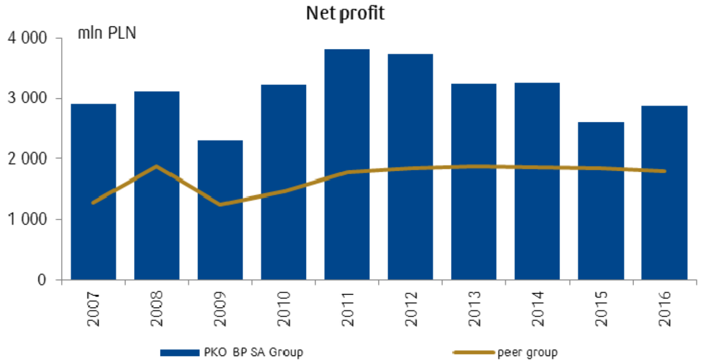
6. BUSINESS MODEL EXTENSION

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 customers, alliances with strategic partners e.g. through loyalty platforms and cooperation with public institutions 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.

1.6 The PKO Bank Polski SA Group against its peer group[5]

The PKO Bank Polski SA Group has the highest net profit in its peer group

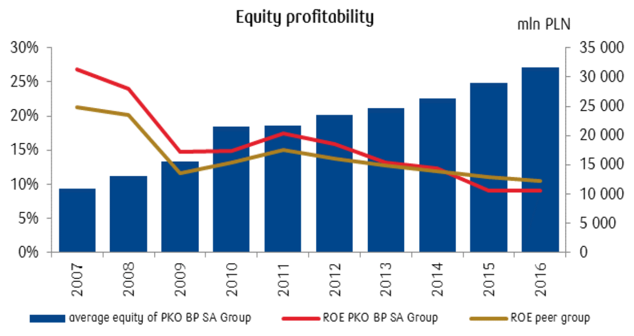


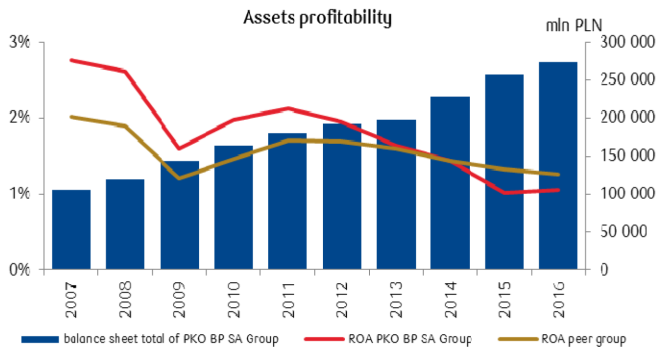
In 2016, the net profits of the PKO Bank Polski SA Group and its peer group were significantly affected by regulatory charges, including mainly the bank tax.

In spite of a significant improvement in interest income and net write-downs achieved under favourable economic conditions, the banks from the peer group did not manage to improve their net profits in relation to the previous year.

In 2016, the PKO Bank Polski SA Group generated the highest net profit among its peer bank groups. At the same time, it achieved a y/y increase.

Profitability of the PKO Bank Polski SA Group and its peer group affected by regulatory factors



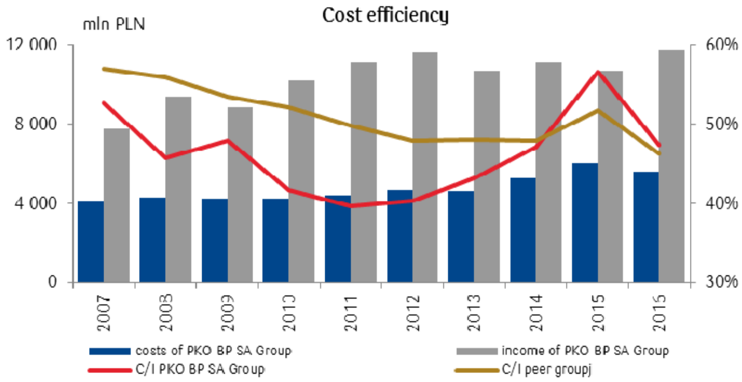


The profitability ratios (ROE, ROA) of the peer group continued to decrease in 2016. It was mainly due to changes in the regulatory environment (including: bank tax and new supervisory recommendations), which affected both the level of equity and income and operating expenses of bank groups.

The profitability of the PKO Bank Polski SA Group improved in the same period.

[5] The peer group consists of the Capital Groups: Pekao SA, mBank SA, ING Bank Śląski SA, BZ WBK SA. The data for the calculation of ratios is from the annual consolidated report and quarter reports of the individual banks.

IMPROVEMENT IN THE COST EFFICIENCY OF THE PKO BANK POLSKI SA GROUP AND ITS PEER GROUP, MAINLY DUE TO A BETTER RESULT ON BUSINESS ACTIVITIES

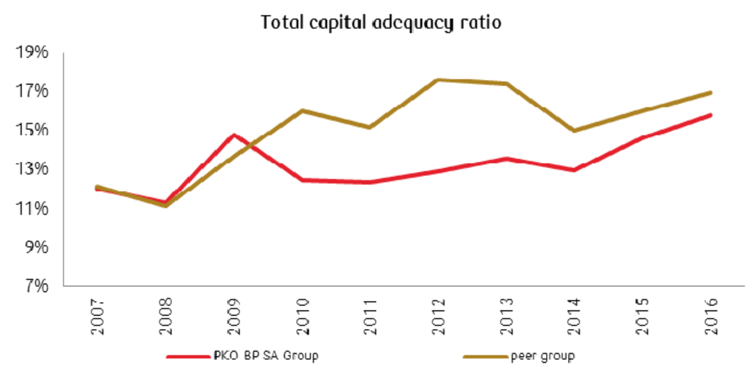


Cost efficiency improved significantly in 2016 (after excluding the costs of bank tax), which was associated with:

- a high base of reference from 2015, associated with additional payments to the Bank Guarantee Fund and Borrowers' Support Fund;
- a significant improvement in the result on business activities (mainly net interest income) compared with 2015;
- cost discipline maintained by banks despite growing spending on digitization and cyber security.

The PKO Bank Polski SA Group improved its cost efficiency position in 2016, getting closer to its peer group.

INCREASE IN THE CAPITAL RATIO OF THE PKO BANK POLSKI SA GROUP AND ITS PEER GROUP DUE TO GROWING REGULATORY AND SUPERVISORY REQUIREMENTS



The capital adequacy of the banking sector increased in 2016. Among other things, it was due to growing minimum requirements defined by the PFSA.

The same trend affected the largest bank groups, including the PKO Bank Polski SA Group.
Actions taken by the PKO Bank Polski SA Group, including mainly the accumulation of profit, allowed the PKO Bank Polski SA Group to improve its capital position in relation to its peer group.

2. EXTERNAL BUSINESS ENVIRONMENT

2.1 MACROECONOMIC ENVIRONMENT

The year 2016 brought a gradual improvement in the situation in the global economy, despite increased uncertainty and many risk factors. The situation of many emerging economies improved due to the discontinuation of the downward trend in raw material prices. An improvement has also been seen in developed economies, in particular in the final months of the year, despite the negative effect of uncertainty associated with the potential effects of Brexit.

Poland experienced a moderate and temporary slowdown in the rate of economic growth in 2016. Its main sources included the end of the EU Financial Perspective 2007-2013 and the associated limitation of investment activities in the public sector, mainly in local administrative units.

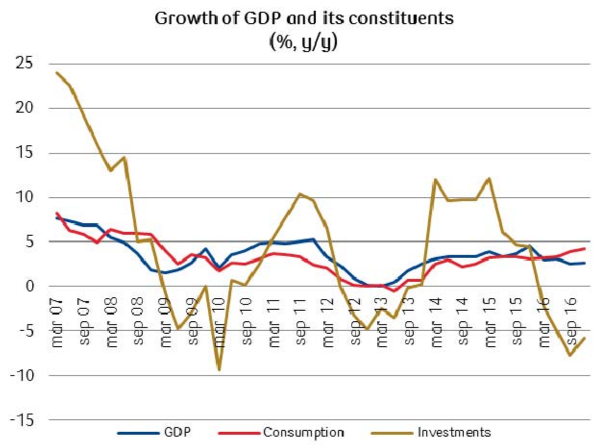
A similar phenomenon ('transition' between EU long-term financial perspectives, resulting in a lower rate of growth of investments and GDP) was observed in other economies of the region (the Czech Republic, Hungary).

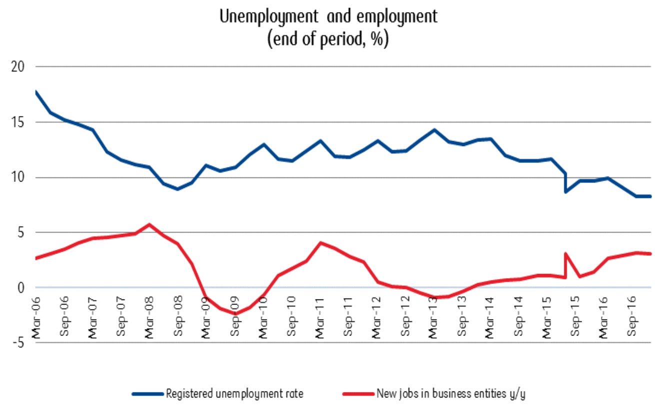
The role of individual consumption in the Polish economic growth structure increased. Accelerated growth of consumption reflected an improvement in the situation on the labour market and the outcome of the 'Rodzina 500+' programme. Gross expenditure on fixed assets had a temporary adverse effect on GDP growth. This was observed mainly in the area of public investment (local authorities' expenditure and expenditure on railway infrastructure were significantly limited) and in part of the private sector (including the power sector, water supply, waste water and solid waste management). The GDP growth amounted to 2.8% in the whole of 2016, compared with 3.9% in the previous year. The economic upturn, which is reflected by the main economic ratios for the final months of 2016, and progress in the absorption of EU funds confirm that the economic slowdown observed last year was temporary.

Positive trends on the labour market throughout 2016 also confirm the temporary nature of the economic slowdown. The employment level increased strongly in the enterprise sector (2.9% compared with 1.3% in the previous year) and registered unemployment dropped to a historic low level (8.3% at the end of the year). The rate of growth of salaries and wages accelerated to 4.1% compared with 3.5% in 2015, and research results indicated exceptionally good moods among households and a growing percentage of firms planning future wage increases.

The annual average inflation rate in 2016 increased to -0.6% from -0.9% in 2015. After a 28-month period of deflation, inflation returned in December 2016 (0.8% y/y), mainly due to the low base effect and an increase in fuel prices associated with an increase in crude oil prices and appreciation of the American dollar.

In view of the lack of negative implications of deflation and the temporary nature of moderate economic slowdown, the Monetary Policy Council maintained the basic interest rates of The National Bank of Poland (NBP) unchanged throughout 2016 (the NBP reference rate amounted to 1.50%). The need to maintain the financial system's stability was also mentioned among the arguments against easing the monetary policy.





2.2 SITUATION ON THE FINANCIAL MARKET

STOCK MARKET

The beginning of 2016 brought deep decreases in the share markets. These were caused by deteriorating assessments of the condition of the global economy (in particular, the Chinese economy). Such assessments caused a drop in raw material prices, which in turn led to concerns not only about the condition of mining companies, but also broader implications for the global economy and financial markets. The raw material prices bounced back later in the year, which was partly due to an economic upturn in China. Together with the more moderate rhetoric of the American Central Bank, it was possible to reverse the negative market trend. The second and third quarter of 2016 brought a side trend, which was temporarily disturbed by the results of the British referendum on EU membership. The end of the year proved to be very important and crucial for the whole picture of the year. A strong growth trend began on the stock markets after Donald Trump's victory in the Presidential elections in the USA. Investors focused on these aspects of the new President's programme that support growth. The year 2016 was quite good for the Polish stock exchange. The main index increased by 11.4% y/y.

It was achieved mainly due to the global trend, the fact that the main concerns associated with the economic situation and regulatory activities affecting the major sectors represented on the WSE did not materialize, and the expected faster GDP growth in 2017.

INTEREST RATES MARKET

The National Bank of Poland kept the interest rates in 2016 and suggested that the monetary policy would not change at least until the end of the following year. As a result, WIBOR3M and WIBOR6M fluctuated within a very narrow range, i.e. 1.67%-1.73% and 1.74%-1.81%, respectively. Despite the fact that the interest rates did not change, the market expectations concerning the monetary policy varied strongly between the valuation of one interest rate decrease of 25 b.p. in 2017 and an interest rate increase of 25 b.p. at the end of the following year. On the Polish interest rate market, Treasury bond yields remained in the side trend over a major part of the year. The situation changed in the last quarter due to rapid changes in the moods on the global market. Donald Trump's victory in the US presidential election was the factor that initiated major changes in bond yields around the world. Concerned about the introduction of a stricter monetary policy in consequence of fiscal easing announced during the presidential campaign, investors were selling American bonds and approached investments on emerging markets, including Poland, with more caution. A drop in the prices of Polish Treasury bonds was visible primarily at the longer end of the profitability curve. Asset swap spreads remained at high levels in 2016. The lower valuation of bonds was mainly a result of: concerns about the rating agencies' decisions, pressure on capital outflow from emerging markets due to the stricter monetary policy of the Fed and big supply of Treasury securities on the primary market.

CURRENCY MARKET

In 2016, the main factors determining changes on the currency market were the following:

- continued quantitative easing policy of the European Central Bank,
- evolution of the expectations concerning potential interest rate increases in the USA,
- economic slowdown in China and the resulting decrease in the exchange rate of the yuan against the American dollar,
- victory of Brexit supporters in the UK referendum,
- a new draft 'Swiss Franc Law' proposed by the Polish President, significantly reducing the burden on the polish banking sector in relation to the previous proposals, and
- Donald Trump's victory in the US presidential election.

The EUR/USD exchange rate was determined mainly by the growing divergence of the monetary policies in the euro zone and in the USA. However, over a major part of the year, due to the cautious approach of the Fed to interest rate increases and their potential impact on the emerging markets, the EUR/USD exchange rate increased from 1.08 at the beginning of the year to around 1.15 at the end of May 2016 (shortly before the British referendum). Further on in the year, concerns associated with Brexit and the growing expectations of interest rate increases in the USA, associated with Trump's victory in the presidential elections (e.g. due to his fiscal expansion programme) resulted in a EUR/USD exchange rate of 1.05 at the end of the year. The year 2016 was a period of significant changes in the EUR/PLN exchange rates. The unexpected decision to decrease the credit rating of Poland, made by S&P in January, resulted in a growth in the EUR/PLN exchange rate of more than 4.50, and then the more moderate position of the Fed on potential further interest rate increases in the USA caused a drop to around 4.20 by the end of the first quarter of 2016. In the second quarter, the victory of Brexit supporters in the UK made the exchange rate exceed 4.50 again; however, the EUR/PLN exchange rate dropped below 4.30 by the end of the third quarter as a result of the 'Swiss Franc Law' draft being more moderate from the banking sector's perspective than expected. At the end of the year the EUR/PLN exchange rate amounted to 4.40 due to the strong depreciation of yuan against the American dollar in the last quarter of the year and growing expectations concerning interest rate increases in the USA after Donald Trump's victory.

2.3 SITUATION IN THE POLISH BANKING SECTOR

Financial result Quality of credit portfolio Statement of financial position

FINANCIAL RESULT

As at the end of 2016, the situation in the banking sector was stable. However, a number of sources of risk remain in the environment of banks, including regulatory risk associated with housing loans in foreign currencies.

In the conditions of stable economic growth, in 2016 the banking sector generated a net profit of PLN 13.9 billion (+24.3% y/y). A high, two-digit rate of net profit growth was caused by one-off events that occurred both in 2016 and in 2015; the most important ones included:

in 2015:

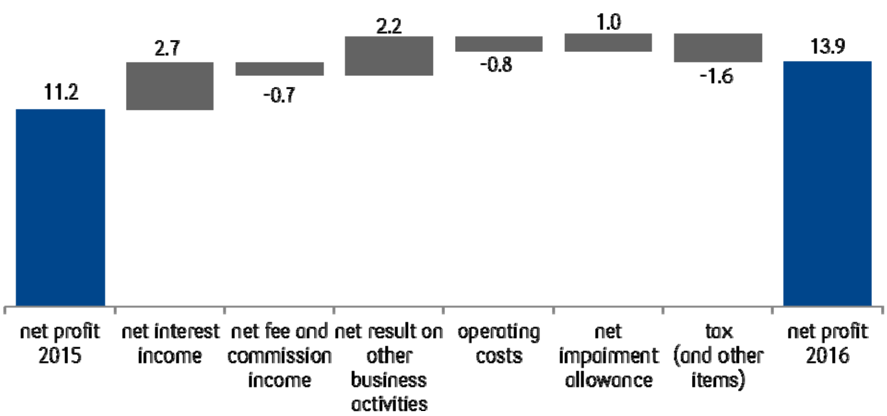
- additional write-downs for the loan portfolio of SK Bank in Wołomin (SK Bank),
- payments made by banks to the guaranteed funds protection fund (FOŚG) in connection with the bankruptcy of SK Bank,
- costs incurred by banks in connection with the establishment of the Borrowers' Support Fund,

in 2016: additional revenue from the settlement of the Visa Europe Ltd. transaction by Visa Inc. (the Visa transaction).

In 2016, in addition to the Visa transaction settlement, the following factors had a positive effect on the banking sector's profit: a noticeable improvement in the net interest income (resulting from both a y/y increase in interest income and a significant decrease in interest expenses) and a relatively stable level of net write-downs (net of the effect of one-off events).

Bank tax charges and a decrease in net fee and commission income had an adverse effect on the net profit.

Chart 1. Change in the net profit of the banking sector (PLN billion)



Source: PFSA, the calculation of PKO Bank Polski SA; operating costs including the tax on certain financial institutions

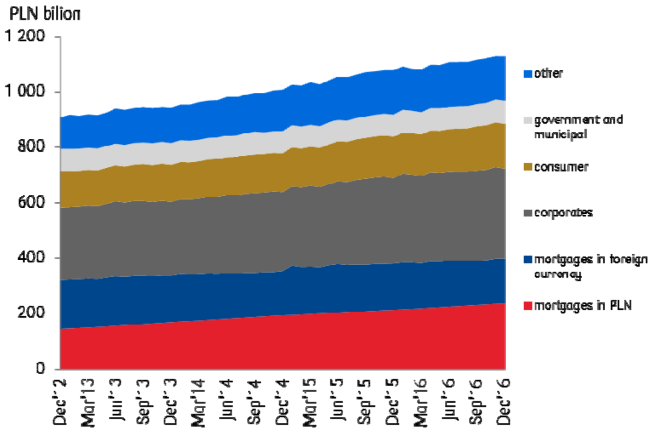
The profitability of the banking sector as at the end of 2016, measured in terms of ROE, increased to 7.7% as compared with the record low level of 6.6% as at the end of 2015.

STATEMENT OF FINANCIAL POSITION

The value of the banks' assets increased due to good economic conditions. The scale of the banking sector's operations increased as at the end of 2016. The sector's total assets increased to PLN 1 711 billion (+7.0% y/y). The assets structure changed as a result of the introduction tax on certain financial institutions; the share of repo transactions decreased and the share of Treasury securities increased (to approx. 15% as compared to 12% before the introduction of the tax on certain financial institutions).

The value of loans granted by the banking sector increased to PLN 1 130 billion as at the end of 2016. The rate of their growth was moderate in 2016 (4.9% y/y). The following factors affected the loan market: (1) the continued significant slow-down in the y/y rate of growth of retail housing loans (+4.9% vs. 7.1% as at the end of 2015; after adjustment for foreign exchange differences, a relative stabilization was observed), (2) the continued slow-down in the y/y growth of corporate loans (5.4% as compared to 8.3% as at the end of 2015), and (3) accelerated y/y rate of growth of consumer loans (7.3% as compared to 6.6% as at the end of 2015). Consumer loans, as well as housing loans in PLN, were among the fastest-growing categories of loans. While interest rates remained low, it was possible due to the banks' focus on more profitable products which at the same time generated relatively low capital requirements.

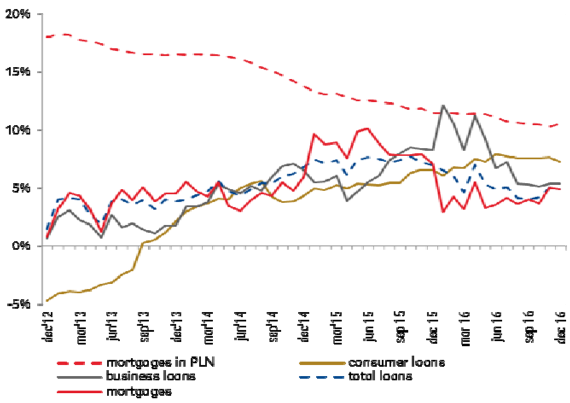
Chart 2. Loan structure of banking sector



* other loans include loans to individual entrepreneurs, non-monetary financial institutions, farmer and non-commercial institutions serving households.

Source: NBP, calculations of PKO Bank Polski SA

Chart 3. The rate change of loans in the banking sector (y/y)

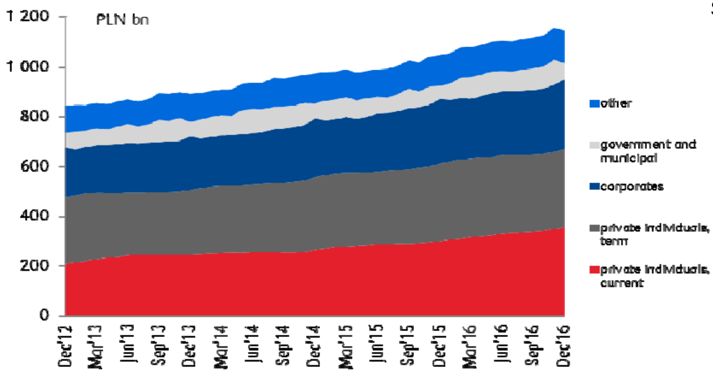


The deposit market in 2016 was affected by better conditions on the labour market and an increase in the income of individuals, as well as a good liquidity position of enterprises, low level of interest rates and the low historical attractiveness of savings and investments treated as alternative products to bank deposits.

The volume of banking sector deposits increased to PLN 1 145 billion as at the end of 2016; its growth accelerated to 9.5% y/y compared to 7.5% as at the end of 2015. It was a result of: (1) continued fast y/y growth of deposits of individuals (9.5% y/y as at the end of 2016 vs. 9.8% as at the end of 2015), (2) slower y/y growth of corporate deposits (8.2% y/y vs. 10.5% y/y as at the end of 2015), and (3) a growth in deposits of the public sector (24.8% y/y vs. a decrease of 16.6% y/y as at the end of 2015).

The high rate of growth of banking sector deposits, which was maintained in 2016, accompanied by a moderate growth of the volume of banking sector loans, resulted in a drop in the loans/deposits ratio to a historical low level of 97.8% as at the end of 2016. Previously, such a low level of the loans/deposits ratio was observed in 2008.

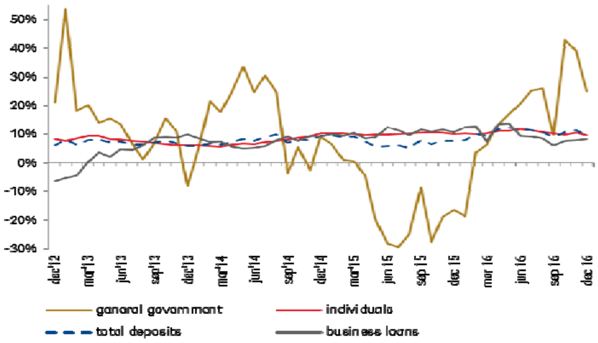
Chart 4. Deposit structure in the banking sector



* Other deposits include loans to individual entrepreneur, non-monetary financial institution, farmers and non-commercial institutions providing services for households.

Source: NBP, calculations of PKO Bank Polski SA

Chart 5. The rate of change of deposits in the banking sector (y/y)



2.4 THE SITUATION OF THE POLISH NON-BANKING SECTOR

INVESTMENT FUND SECTOR

In 2016 the Polish investment fund market continued its growth trend. However, it was much weaker than in the previous year. In 2016, the assets managed by open pension funds' management companies (TFI) increased by 2.6% to PLN 258.6 billion compared with the 20.5% increase in 2015.

In 2016 the relatively small increase in total assets (+PLN 6.4 billion compared with PLN +43 billion in 2015) was accompanied to a large extent by a negative balance of payments made by institutional investors and their surrenders noted in the fourth quarter of 2016 (PLN -10.2 billion). The regulatory changes which have been prepared and which became binding as of 1 January 2017, which resulted in covering part of the entities on the closed-ended investment funds with CIT had a significant impact on this trend.

In 2016 the value of assets of institutional investors managed by TFI dropped by PLN 2.2 billion (-2.0%). Thus, the share of assets of this group of investors dropped to 49.4% of the total investment fund assets.

In 2016 the increase in demand for participation units on the part of individual investors had a positive impact on the increase in investment fund assets, which was particularly visible in the second half of the year. In the second half of 2016 this group of investors paid PLN 4.7 billion net to investment funds (PLN -1.4 billion in a similar period of 2015). As at the end of 2016 assets of individuals increased by 7.1% year on year, to PLN 131 billion compared to the increase in 2015 of 5.2%. In 2016 the largest inflow of new funds from individuals was paid to absolute return funds (PLN 3.4 billion), cash and money funds (PLN 2.6 billion) and debt funds (PLN 1.6 billion). The largest outflow of funds of individual investors was noted in equity and mixed funds of PLN -2.7 billion and PLN -1.9 billion respectively.

The development of investment funds in 2016 was accompanied by the high volatility of returns on Polish Treasury bonds, including strong increases in returns noted in the fourth quarter of 2016, and an improvement in conditions on the equity market on the Warsaw Stock Exchange in the second half of 2016 and the prevailing low base interest rates. This translated into the increase in realized 12M rates of return by funds investing their capital in Polish shares which was visible in the second half of 2016. The rates of return of 12M Polish equity funds and Polish mixed funds which had been negative over the majority of 2016 as at the end of December exceeded the level of interest on new household deposits. This situation contributed to an improvement in the mood of individual investors, and in effect to an increase in demand for investment fund units.

OPEN PENSION FUND MARKET

In 2016 Open Pension Fund (OFE) assets increased by 9.2% (PLN 12.9 billion) y/y to PLN 153.4 billion, compared with the drop of 5.7% (PLN -8.6 billion) y/y in 2015. The OFE market remained influenced by: the improved situation on the labour market, regulatory changes (change in the structure of the OFE investment portfolio) and improved conditions on the Warsaw Stock Exchange (the WIG index increased by 11.4% y/y). Polish shares dominated in the structure of OFE assets. In 2016 the number of OFE participants continued to fall (-107 thousand to 16.4 million).

THE LEASE MARKET

In 2016 the lease industry continued to grow at a two-digit pace. In accordance with the data of the Polish Leasing Association (Związek Polskiego Leasingu) the value of assets financed by lease companies increased by 16.6% y/y reaching the level of PLN 58.1 billion (compared with a 16.3% increase in 2015). Apart from bank loans, leases constituted the second most important external sources of financing investments. As at the end of 2016 the total value of the active lease portfolio amounted to PLN 105 billion compared with the volume of investment loans extended to businesses of PLN 151 billion. The development of the lease market was supported by good market conditions in Poland.

Leases of light vehicles, mainly passenger cars, had the largest positive impact on the development of the lease market. The value of assets leased out in this segment amounted to PLN 24.4 billion (+30.9% y/y), which constituted 42% of total leases granted by lease companies.

Leases of heavy vehicles developed robustly. The value of leased assets in this segment amounted to PLN 17.2 billion (+27.7% y/y), to which the stable rate of growth of the economy in the Euro Area, and the replacement of used fleets with new Euro 6 standard vehicles contributed.

The lease market noted a drop in the segment of plant and machinery (-3.5% y/y). Lease companies financed plant and machinery with a value of PLN 14.6 billion. In this segment leasing agricultural machines dropped most significantly (-22.6% y/y). One of the factors which contributed to the drop in leases of plant and machinery despite the good and stable economic position of enterprises and the relatively high level of use of production capacity and relatively good availability of loans was ending the financing with funds from the EU financial perspective 2007-2013 with a simultaneous weak absorption of funds from the 2014-2020 perspective. In the period under analysis leases of property dropped strongly to PLN 719 million (-49.6% y/y), and its share in the market was further marginalized.

THE INSURANCE MARKET

During the three quarters of 2016 assets of insurance companies increased by PLN 5.0 billion (2.8%). This was the effect of a slight increase in life insurance assets (0.6%) and stronger growth in personal and property insurance assets (+5.7%).

The net profit of the life insurance sector generated in a period covering three quarters of 2016 decreased to PLN 1.7 billion (-26.3% y/y), which was mainly due to a strong decrease in deposit income (-14.9%). A decrease in the costs of insurance activities (-14.2% y/y) and a decrease in the amount of loss payments made (of 6.6% y/y) had a positive effect on this result. The gross written premium decreased by 14.5% y/y, which was mainly due to the fact that insurance companies ceased offering agreements with an insurance capital fund (Group 3 in Section I).
Non-life insurance companies recorded a y/y decrease in profit of 37.3% which amounted to PLN 196 million as at the end of the 3rd quarter of 2016. The value of losses paid and the costs of insurance activities increased (9.44% y/y and 2.2% y/y, respectively). At the same time, the value of gross written premium increased significantly (14.2% y/y) mainly in automotive insurance (Group 3 and 10 in Section II), which will have a positive effect on the results in future periods due to the manner of recording provisions.
Costs of tax on some financial institutions binding as of February 2016 had a strong impact on the profits of insurance companies. According to the estimates of the Polish Chamber of Insurance, the respective costs incurred in the period February-September 2016 by insurers amounted to approx. PLN 450 million.

THE FACTORING MARKET

In 2016, the factoring market continued to grow dynamically. This is confirmed by the factoring companies which report to the Polish Factors Association (Polski Związek Faktorów). Their revenue reached PLN 158.2 billion, which translated into an acceleration of the growth rate to 20.6% y/y compared to 17.6% y/y in 2015. The growing demand for factoring companies is also reflected in the number of customers serviced (an increase of 11% y/y to 7.9 thousand) and invoices (an increase of 16% y/y to PLN 7.5 million).

In 2016 domestic factoring was the driver of growth of the factoring market (an increase in revenues of 23% y/y to PLN 124.9 billion), including both recourse and non-recourse factoring. Recourse export factoring also developed very dynamically (an increase in transaction volumes of approx. 27% y/y to PLN 18.8 billion), which supports the foreign expansion of enterprises. The share of import factoring in the market structure remained marginal, and amounted to 1.0% compared with 1.3% in a similar period of the previous year.

2.5 THE UKRAINIAN MARKET

The year 2016 brought Ukraine a long-awaited economic upturn. GDP growth rate was positive for the first time since 2012, exceeding 2% (estimation based on the preliminary GDP measurement for the 4th quarter of 2016: 4.7% y/y). However, the improvement in the GDP growth rate was largely due to a low base (in 2015, GDP decreased by 9.9%). In 2017, the GDP growth should accelerate moderately to approx. 2.5%). Inflation showed a downward trend (base inflation decreased from 34.7% y/y as at the end of 2015 to 5.8% y/y in December 2016), and major changes in the main price index reflected mainly administrative actions (including utility price increases from April 2015 and October 2016). In previous years, export was a major driver of economic growth. Its competitive advantage grew rapidly after the depreciation of the hryvnia exchange rate. In 2016, wages and salaries started to grow in real terms (on average by 7.9% y/y in the discussed period) due to a decrease in inflation and a relatively stable growth in nominal wages and salaries (on average 23.4% y/y in the whole year). It had a positive effect on consumption and internal demand.

After the significant weakening of the hryvnia exchange rate in February 2016, the exchange rate stabilized only to undergo significant depreciation at the end of the year. As a result, at the end of 2016, 27.1 hryvnia had to be paid for one dollar compared with 24.0 in the previous year. The stabilization of the exchange rate of the hryvnia during the year and the drop in inflationary pressure enabled the Central Bank to reduce rates six times during the year (to 14% in December 2016 from 22% as at the end of 2015). The situation in public finance deteriorated after a rapid increase in the public sector deficit in December. At the end of 2016 the debt of the public finances sector reached 73.8% of GDP compared with 67.4% GDP in 2015.

The banking sector remained unprofitable. In the period from January to November ROA was -1.63% compared with -5.46% in 2015, and ROE was -15.05% compared with -51.91% in 2015. Bankruptcies and mergers led to a decrease in the number of banks from 117 as at the end of 2015 to 98 as at the end of November 2016. The announcement of the nationalization of Private Bank on 18 December (20.9% of the sector's assets) was a significant event in the sector. The share of foreign capital in the sector increased to 55.5% in the period under discussion from 43.3% as at the end of 2015. The banks managed to improve their equity position. The equity to asset ratio increased from 8.3% as at the end of December 2015 to 11.4% in November 2016. Nevertheless, the volume of loans did not increase. The increase in the volume of deposits led to a drop in the loans to deposits ratio to 120.3% as at the end of 2016 from 134.2% in December 2015.

The increased share of the banks in the structure of Treasury securities holders from 16.1% to 38.3% in 2016 indicates that free cash flows were mainly invested in safe Treasury assets.
The value of total assets in the Ukrainian banking sector increased slightly in 2016 (by UAH 9 billion until November 2016). A slight increase in the loan volume of UAH 10.4 billion was recorded in 2016, despite a decrease in the volume of foreign currency loans (of UAH 57.8 billion), including household loans. An increase in the volume of loans denominated in UAH, which could be noticed during the year, suggests a reversal of the downward trend in lending activity, which should bring positive effects in 2017. The share of non-performing loans increased from 22.1% of total loans as at the end of 2015 to 24.2% in November.

In the period under discussion deposits increased by UAH 96.5 billion, and the growth related both to foreign currency deposits and to UAH deposits, and both household and corporate deposits. The drop in inflation (increase in the real payroll budget) and acceleration of economic growth should translate into a further increase in the volume of deposits in consecutive quarters.

2.6 REGULATORY ENVIRONMENT

The financial and organizational situation of the PKO Bank Polski SA Group was affected i.e. by the following:

TAX ON CERTAIN FINANCIAL INSTITUTIONS (BANK TAX)

Act of 15 January 2016 on tax on certain financial institutions (Journal of Laws of 2016, item 68 with amendments) obliging banks, insurance companies and other financial market participants to pay tax on adjusted assets since 1 February 2016.	Impact on the financial results, profitability of commercial and mortgage banks and insurance companies

DEPOSIT GUARANTEE SYSTEM FEES

- Resolution No. 25 and 26 of the Bank Guarantee Fund ('BGF') Council of 25 November 2015 setting out bank's fees for the deposit guarantee system for 2016: decreasing rate to calculate the annual fee (from 0.189% to 0.167%) and increasing ratio used to calculate prudential fee (from 0.050% to 0.079%), - Amendment of the law on the Bank Guarantee Fund (Journal of Laws of 2016, item 381) amending the frequency of determining the rates of mandatory and prudential fees from annually (based on total risk exposure as at 31 December of prior year) to quarterly (based on data as at the end of the last quarter), - Resolution No. 15, 16, 18, 19 and 36, 37, 48 and 49 of 2016 of BGF Council setting rules for bank's fees in favour of the deposit guarantee system in the first and second quarter of 2016 (annual fee of 0.04175%, prudential fee of 0.01975 of the total amount of risk exposure), - Resolution No. 308/DGD/2016 of the BGF Management dated 28 October 2016, specifying the amount of payments to be made by banks due to the bankruptcy of the Cooperative Bank in Nadarzyn.	Impact on the banks' operating expenses and tax burden

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, and recommendations of the Polish Financial Supervision Authority (PFSA), in particular to increase the short-term liquidity rate LCR to 70%.	Impact on the capital base of banks, supervisory prudential standards, business activity of banks, implementation costs

CAPITAL BUFFERS – PFSA ADDITIONAL REQUIREMENTS

- The Act on macroprudential supervision over the financial system and crisis management (Journal of Laws of 2015, item 1513 as amended) in particular, introducing in the period from 1 January 2016 to 31 December 2017 a capital conservation buffer of 1.25%, and from 10 October 2016 - a capital buffer for other systemically important institutions of 0.75% of the total risk exposure calculated in accordance with Art. 92, clause 3 of the Regulation (EU) No.575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms, amending the Regulation (EU) No 648/2012,	Impact on the capital requirements for banks on the separate and consolidated level

- PFSA recommendations for individual banks concerning additional equity requirements to hedge the risk resulting from mortgage loans in foreign currencies granted to households.

TIGHTENING REQUIREMENTS ON GRANTING OF HOUSING LOANS	
Recommendation S of the PFSA on good practice in the management of mortgage secured credit exposures (PFSA Official Journal of 2013, item 23) increasing the requirement for own contribution from 10% to 15% since 1 January 2016.	Impact on the level of lending, interest income, fee and commission income of banks
LIQUIDITY RISK MANAGEMENT	
Recommendation P of the PFSA concerning financial liquidity risk management in banks (PFSA Official Journal of 2015, item 14), changing the rules of liquidity risk management since 1 January 2016.	Impact on the measurement and management of liquidity risk
MODEL RISK MANAGEMENT	
Recommendation W of the PFSA concerning model risk management (PFSA Official Journal of 2015, item 49), from the date of implementation by the banks to 30 June 2016.	Impact on the model risk management process: model constructions and evaluation of their performance
MAXIMUM NON-INTEREST CHARGE	
Amendment to the law on consumer loan (Journal of Laws of 2015, item 1357 with amendments) that specifies the maximum level of non-interest expenses since 11 March 2016.	Impact on the level of non-interest income of banks
'RODZINA 500+' PROGRAMME	
Act on state assistance in raising children (Journal of Laws of 2016, item 195 with amendments) introducing since 1 April 2016 an allowance of PLN 500 a month for each second and subsequent child in a family.	Impact on the level of individuals deposits, credit standing (consumer loans), inflow of funds from individuals to the investment fund market
CHANGE IN THE TRADE OF AGRICULTURAL REAL ESTATE	
Act of 14 April 2016 on cease of real estate sale of Agricultural Property Stock of the Treasury, and on change of some Acts (including Act on land registers and mortgages) effective since 30 April 2016 (Journal of Laws of 2016, item 585) and amendment of the Act on the Agricultural System and the Act on Land and Mortgage Register (Journal of Laws of 2016, item 1159) effective from 16 August 2016.	Impact on the loan policy, the level of lending
FACILITATION OF THE TERMS OF ISSUE OF MORTGAGE BONDS	
Amendment to the law on mortgage bonds and mortgage banks (Journal of Laws of 2015, item 1259) changing the principles of mortgage bonds issuance from 1 January 2016 (among other things, higher limits for issues of mortgage bonds, the possibility of exempting mortgage bonds from withholding tax)	Greater opportunities for financing loan business
BANKING ENFORCEMENT DOCUMENT	
Amendment of the Banking Law (Journal of Laws of 2015, item 1854) cancelling bank enforcement title as of 27 November 2016.	Impact on risk management by banks, increase in the cost of risk, increase in operating expenses
DORMANT ACCOUNTS	
Amendment of the Banking Law (Journal of Laws of 2015, item 1864) defining the treatment of inactive accounts, including accounts of deceased persons, by banks as of 1 July 2016.	Impact on the bank's costs and expenditure

BANKING SUPERVISION COSTS	
Decree of the Prime Minister (Journal of Laws of 2016, item 1371) changing the principles for calculating and paying fees to cover the costs of banking supervision.	Impact on the bank's costs
THE COST OF CAPITAL MARKET SUPERVISION	
Amendment of the law on Capital Market Supervision (Journal of Laws of 2015, item 1260) requiring, among others, banks, insurance companies and investment fund companies to participation in the costs of capital market supervision; effective from 1 January 2016.	Impact on the level of costs and earnings of investment fund companies
MANAGEMENT POLICIES RELATING TO INVESTMENT FUNDS' OPERATIONS	
Amendment to the Act on the investment funds (Journal of Laws of 2016, item 615) stipulating amendments to the information policy and remuneration policy of Investment Fund Management Companies by the end of 2016.	Impact on the level of costs of investment funds
TAXATION OF CLOSED END INVESTMENT FUNDS (FIZ)	
Amendment of the Act on income tax of 29 November 2016 (Journal of Laws of 2016, item 1926) introducing changes which result in covering part of the entities on the closed end investment funds market with CIT as of 1 January 2017.	In the fourth quarter of 2016 the outflow of funds from some FIZ, which resulted in a drop in managed assets of Investment Fund Companies
RESTRICTIONS FOR OPEN PENSION FUNDS (OFE)	
Amendment of the law on Capital Market Supervision (Journal of Laws of 2013, item 1717) changing the rules for payment of pensions from the open pension funds - allowing since 1 January 2016 increased involvement of OFE in shares of companies listed abroad (over 20%) and limiting the involvement of OFE in shares of domestic companies (35%)	Impact on the level of open pension fund (OFE) assets, financial results of general pension society (GPS)
CHANGES IN THE CONDUCT OF INSURANCE BUSINESS	
Amendment to the law on activities of insurance and reinsurance (Journal of Laws of 2015, item 1844), in force since 2016.	changes in the standards of capital and prudential requirements
PFSA RECOMMENDATIONS FOR INSURANCE COMPANIES	
PFSA recommendations dated 22 March 2016 relating to checking the adequacy of insurance products for the customer's needs and abilities, and to the product management system; they should be implemented by the insurance companies by 1 July 2016.	Impact on the costs of insurance companies

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

- Resolutions of the National Bank of Ukraine (NBU) reducing the discount rate – by Resolution No. 278 of 2016 as of 22 April 2016 the NBU reduced the discount rate from 22% to 19%, by Resolution No. 88 as of 24 June 2016 the NBU reduced the discount rate from 19% to 16.5%, by Resolution No. 172 as of 29 July 2016 the NBU reduced the discount rate from 16.5% to 15.5%, by Resolution No. 277 as of 16 September 2016 the NBU reduced the discount rate from 15.5% to 15%; by Resolution No. 372 of 2016 as of 28 October 2016 the NBU reduced the discount rate from 15% to 14%;
- order No. 140, 192, 341, 386, 402 and 410 from year 2016 of the Management Board of the National Bank of Ukraine (NBU) introducing a number of changes in conducting transactions on money-lending and currency market, including the transfer of dividends to foreign investors;
- order No. 338 from year 2016 of the NBU specifying inclusion to the bank's share capital of the financial aid provided by shareholders after obtaining permission of the NBU);
- order No. 341 of the NBU changing polices in determining exchanges rates by banks since 15 June 2016;
- Resolution of the Council of Ministers No. 662 of 2016 preventing paying out pensions, allowances and wages of budget-sector institutions by banks whose share in the banking sector assets market is lower than 1%.

THE REGULATORY SOLUTIONS WHICH WILL AFFECT THE FINANCIAL POSITION OF BANKS AND THEIR GROUPS IN POLAND OVER THE FOLLOWING QUARTERS INCLUDE

The following new regulatory solutions may affect the financial results of the sector in the perspective of the nearest quarters:

- the required own contribution increase from 15% to 20% from 1 January 2017, resulting from recommendation S of the PFSA concerning mortgage secured credit exposures (PFSA Official Journal of 2013, item 23) (an impact on housing loans),
- amendment to recommendation S (under preparation), increasing the risk weight for foreign currency loans (impact on adequacy ratio),
- extension of the *de minimis* Programme for 2017 (amendment of the Decree of the Minister of Finance on granting *de minimis* aid by Bank Gospodarstwa Krajowego in the form of loan repayment guarantees, Journal of Laws of 2016, item 1471),
- increase in the short-term liquidity ratio to 80% as of 1 January 2017 (from 70% in 2016) in accordance with Regulation (EU) No 575/2013 of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms and PFSA recommendations,
- decrease in the limit of the value of transactions between entrepreneurs as of 1 January 2017 that must be settled through a bank account from EUR 15 thousand to PLN 15 thousand (in accordance with the Act on Freedom of Economic Activity, Journal of Laws of 2015, item 584 as amended), which should affect the amount of funds on bank accounts,
- including a free basic payment account in the banks' offer from 8 February 2017,
- a change in the loan concentration risk management principles for universal and mortgage banks as of 1 January 2017, resulting from recommendation C of the PFSA (PFSA Official Journal of 2016, item 15),
- implementation of the Mortgage Loan Act, which is aimed at improving borrower protection and reducing asymmetry in the level of knowledge of the customer and the bank (currently a draft is under preparation),
- changed principles for supporting renewable energy generators (Journal of Laws of 2016, item 925) and a change in the principles for property tax assessment for wind power plants (Journal of Laws of 2016, item 961), which shall affect the financial condition of entities that took bank loans,
- covering part of the entities on the closed end investment funds market with CIT as of 1 January 2017.

2.7 TENDENCIES IN THE POLISH AND GLOBAL ECONOMIES IN 2017 AND THEIR EFFECT ON THE GROUP'S RESULTS[6]

FAVOURABLE EXTERNAL CONDITIONS OF THE POLISH ECONOMIC ENVIRONMENT WITH NUMEROUS RISK FACTORS

The external environment of the Polish economy in 2017 should favour continuing Group development, but numerous risk factors will still play a significant role. The improvement in economic ratios recorded at the end of 2016 in Germany and other major European countries indicates possibility of sustaining solid GDP growth in the Euro area at a level of approx. 1.5%. Maintaining a moderate ECB monetary policy and weaker EUR/USD exchange rate will support continued moderate economic expansion to Poland's main export market. The recovery of commodity prices (and general inflation) will act as a negative factor which will curb the real purchasing power of consumers and increase cost pressure on enterprises. The main risk factors for the Euro area are: a very tight election calendar (among others, the Netherlands, France and Germany), the difficult position of banks and uncertainty related to the start of the Brexit procedure. In the USA, improved economic ratios in industrial processing and the perspective of a new government loosening fiscal policy augur the acceleration of economic growth. The risk factor lies in the potentially excessive scale of USD reinforcement and/or an excessive growth rate of the Fed's interest rates. The rebounding commodity prices constitute a positive factor for many emerging economies. In China, the structural deceleration of economic growth will continue, but the good condition of the world economy and reserves in terms of fiscal and monetary policy should allow it to avoid a 'hard landing'. The last months of 2016 and beginning of 2017 were marked with an apparent rebound of the inflation ratios both in mature economies (USA, Euro area), and in developing ones (China). The change in the inflation environment (abating the threat of deflation) and the improved market environment will result in

[6] Internal forecasts of PKO Bank Polski SA

changes in the monetary policy of central banks. In the USA, a continued increase in interest rates is expected, and the Euro area may decide, at the end of 2017, to gradually withdraw from quantitative mitigation of the monetary policy in the following year.

Acceleration of economic growth

According to forecasts in 2017, economic growth in Poland may reach the level greater than 3%, following a temporary slow-down in 2016. The faster absorption of EU funds, high utilization of industrial capacity, good financial standing and improvement in economic ratios (an evaluation of the future potential demand) result in the revival of investment activities. The good situation on the labour market and best consumer mood ever will encourage a high growth rate of private consumption. Nevertheless, the expiration of the effect of the 'Rodzina 500+' programme and the considerable growth of inflation could lead to a moderate slow-down of consumption growth during the year. Thriving global trade, good economic conditions in the Euro area and the relatively weak PLN which supports the competitiveness of Polish goods, will stimulate exports. The net export contribution to the GDP dynamics should be slightly positive.

The favorable situation on the labor market

In 2017, the situation on the labour market should be continued to improve. Despite the strong growth of demand for labour, the growth of employment will still be restricted by supply factors (the resources of the available workforce running down). These factors, along with inflation (including an increase in food, fuel and energy prices), could lead to increased payroll pressure and accelerated nominal growth in wages and salaries. The unemployment rate should continue its downward trend, and at the end of 2017 it may reach approx. 7.5% compared with 8.3% at the end of 2016.

Increase in CPI inflation rate

Following an over 2-year long deflation period which ended in the last months of 2016, the beginning of 2017 should bring a quick increase in the CPI inflation rate within the admissible variation bracket in respect of the Central Bank's target (2.5% +/-1 p.p.). Accoridng to the forecasts, in 2017, the average annual CPI inflation rate will amount to 2% compared with -0.6% in 2016. In the first half of 2017, inflation will increase mainly due to external factors (rebound of energy and commodity prices) and the effect of the low base, and in the subsequent part of the year, the 'fundamental' price pressure will become increasingly important (closing the negative demand gap, labour market tension, growing costs).

Interest rates unchanged

Despite the accelerated GDP growth rate and CIP inflation rate returning within its target brackets, the Monetary Policy Council will leave NBP interest rates unchanged over the entire 2017. The lack of any threat to the inflation target in mid-term and striving to reinforce the stability of the financial system will be arguments in favour of the stabilization of interest rates.

Steady growth in loans and slowdown of growth in deposits

In the banking sector a steady growth in loans should be visible (approx. 5% y/y in Q4 2017 and in Q4 of 2016, adjusted for exchange rates) as a result of the increase in supply of credit (the effect of partial reconstruction of regulatory capital by banks) and as a result of the increase in demand on credit under record-low interest rates of the NPB and revival of the domestic demand, in particular in respect of investments. In 2017 there will be a slowdown of growth in deposits (up to approx. 7.8% y/y in Q4 2017 of 8.8% y/y in Q4 2016 adjusted by exchange rate), with a weaker growth rate of deposits of non-financial entities and the weakening of the dynamics in personal deposits (stronger interest in alternative forms of saving then deposits, in conditions of record low interest rates).

3. Financial results of the PKO Bank Polski SA Group[7]

Key indicators Consolidated income statement Consolidated statement of financial position

[7] In this chapter, any differences in total balances, percentages and growth rates result from rounding the amounts to PLN million and rounding percentages to one decimal place.

3.1 KEY FINANCIAL INDICATORS

The results achieved by the PKO Bank Polski SA Group in 2016, is represented by the following key financial efficiency indicators, which are shown in the table below.

Table 1. Financial indicators of PKO Bank Polski SA Group

	31.12.2016	31.12.2015	Change 2016-2015
ROA net (net profit/average total assets)*	1.1%	1.0%	0.1 p.p.
ROE net (net profit/average total equity)*	9.1%	9.0%	0.1 p.p.
C/I (cost to income ratio)*	47.4%	56.6%	-9.2 p.p.
Net interest margin (net interest income/average interest–bearing assets)*	3.2%	3.0%	0.2 p.p.
Share of impaired loans**	5.9%	6.6%	-0.7 p.p.
Costs of risk***	-0.75%	-0.72%	0 p.p.
Total capital ratio (own funds/total capital requirement*12,5)	15.81%	14.61%	1.2 p.p.

** 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.*

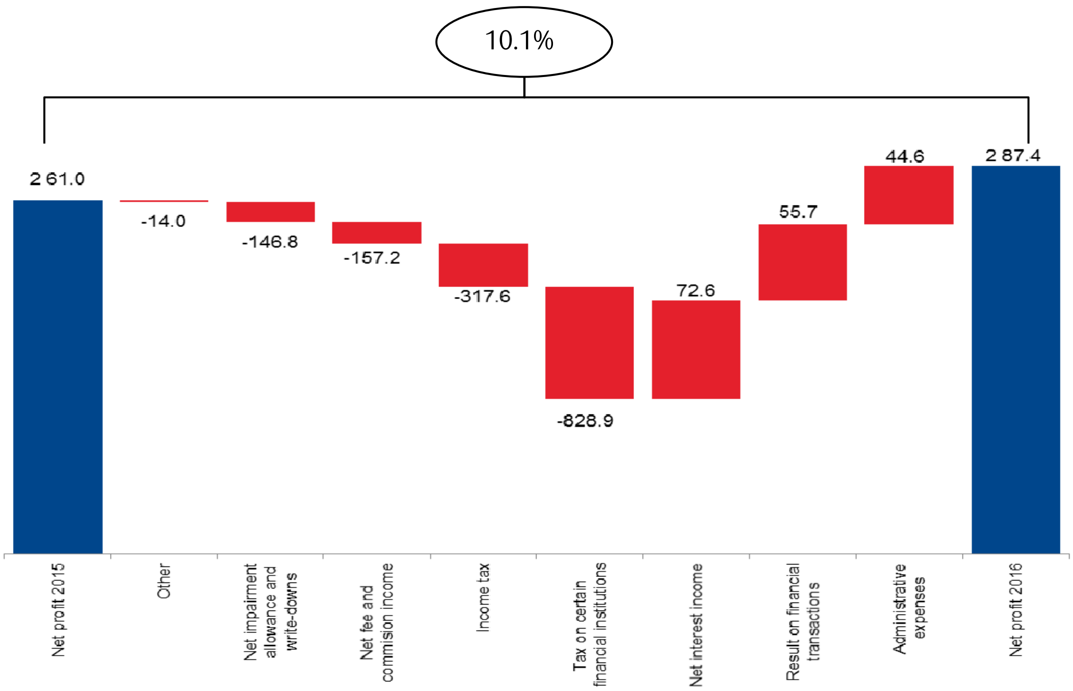
*** Calculated by dividing the gross carrying amount of impaired loans and advances by the gross carrying amount of loans and advances to*

**** Calculated by dividing the balance of impairment allowances on loans and advances to customers over period of 12 months by average 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
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 2016 amounted to PLN 2 874.0 million and was higher by PLN 264.5 million (by 10.1%) than in 2015.



In the PKO Bank Polski SA Group's income statement in 2016, the sum of revenue positions amounted to PLN 11 790.7 million and was by PLN 1 126.0 million, i.e. by 10.6% higher than in 2015, mainly in effect of the growth of net interest income and remaining income.

Table 2. Income statement of PKO Bank Polski SA Group (in PLN million)

	2016	2015	CHANGE (PLN millions)	CHANGE (in %)
Interest and similar income	9 964.4	9 657.8	306.6	3.2%
Interest expense and similar charges	-2 209.6	-2 629.2	419.6	-16.0%
Net interest income	**7 754.8**	**7 028.6**	**726.2**	**10.3%**
Fee and commission income	3 579.6	3 598.3	-18.7	-0.5%
Fee and commission expense	-886.2	-747.7	-138.5	18.5%
Net fee and commission income	**2 693.4**	**2 850.6**	**-157.2**	**-5.5%**
Dividend income	10.3	10.7	-0.4	-3.7%
Net income from financial instruments measured at fair value	4.4	40.6	-36.2	-89.2%
Income from investment securities	506.1	87.7	418.4	5.8x
Net foreign exchange gains (losses)	503.2	369.0	134.2	36.4%
Other net operating income and expense	318.5	277.5	41.0	14.8%
Net impairment allowance and write-downs	-1 622.7	-1 475.9	-146.8	9.9%
Administrative expenses	-5 590.4	-6 036.2	445.8	-7.4%
Tax on certain financial institutions	-828.9	0.0	-828.9	x
Operating profit	**3 748.7**	**3 152.6**	**596.1**	**18.9%**
Share of profit (loss) of associates and joint ventures	34.5	38.1	-3.6	-9.4%
Profit (loss) before income tax	**3 783.2**	**3 190.7**	**592.5**	**18.6%**
Income tax expense	-907.1	-589.5	-317.6	53.9%
Net profit (including non-controlling shareholders)	2 876.1	2 601.2	274.9	10.6%
Profit (loss) attributable to non-controlling shareholders	2.1	-8.3	10.4	x
Net profit (loss)	**2 874.0**	**2 609.5**	**264.5**	**10.1%**

After eliminating from the 2016 results the charges associated with tax on certain financial institutions and major one-off events, such as:

- the settlement of the acquisition of Visa Europe Limited by Visa Inc., in which PKO Bank Polski SA took part; its effect on the Bank's result amounted to PLN 417.6 million,
- the effect of the settlement of the sale of assets of Qualia Development Sp. z o.o. and its subsidiaries; as a result of this transaction, the Group recognized additional income of approx. PLN 114 million in net other operating income and expenses

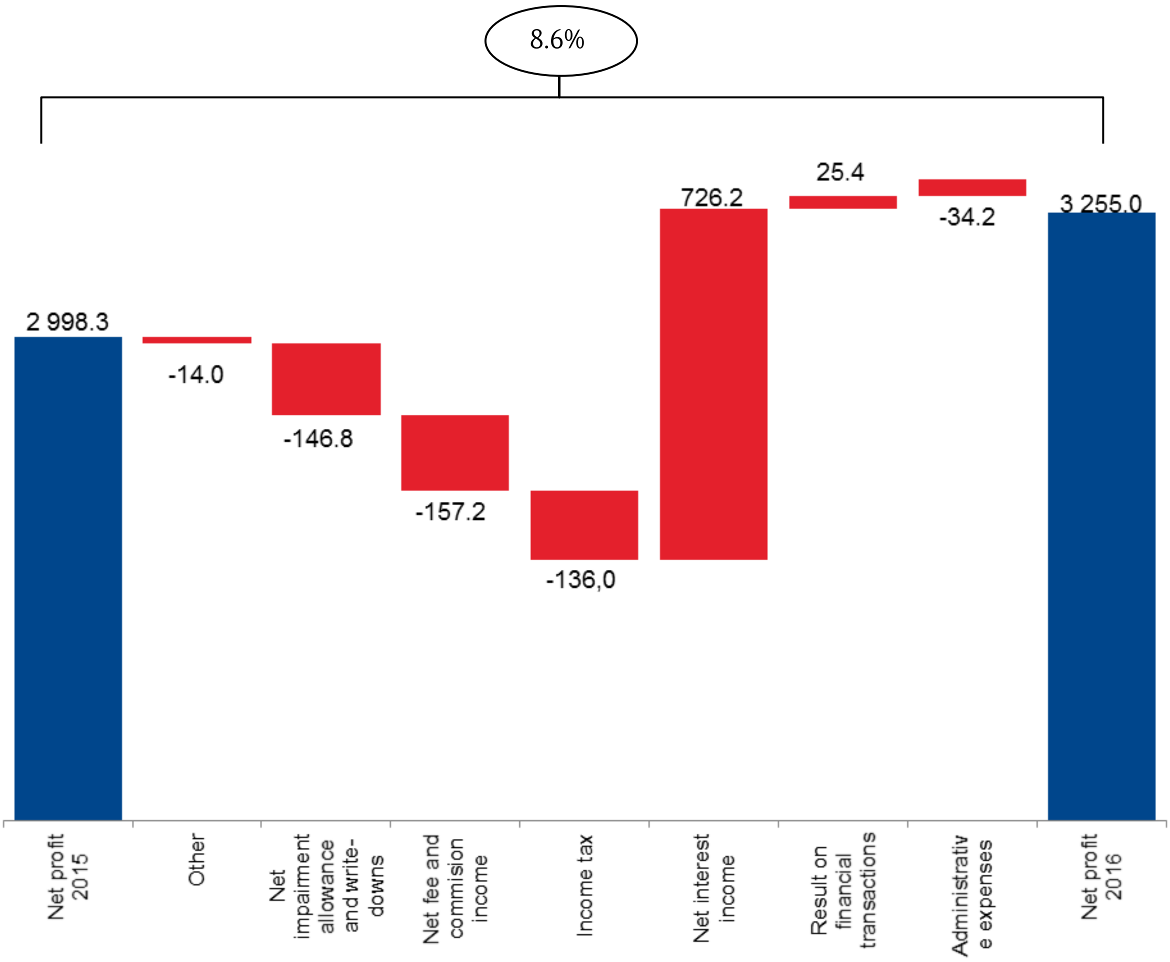
and the events from 2015:

- payments in the amount of PLN 337.9 million made to the Bank Guarantee Fund (BGF) as part of the guaranteed funds protection fund (FOŚG) for the payment of guaranteed funds to holders of deposits with Spółdzielczy Bank Rzemiosła i Rolnictwa in Wołomin after its bankruptcy,
- payments to the Borrowers' Support Fund in the amount of PLN 142 million

the comparable net profit for 2016 amounted to PLN 3 255.0 million and was 8.6% higher than in 2015.

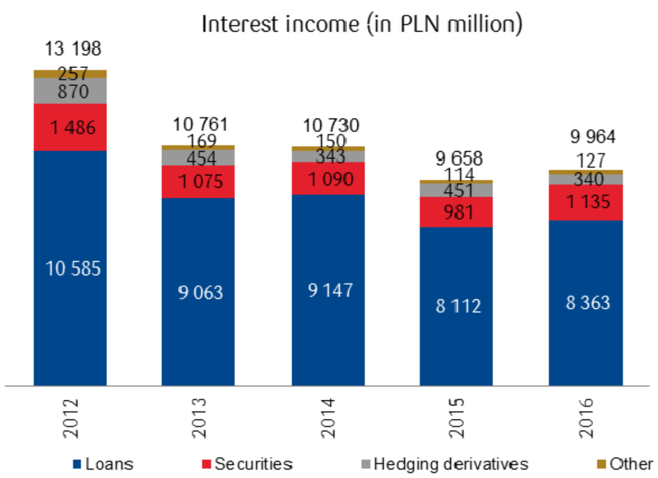
Table 3. Income statement of PKO Bank Polski SA Group (in PLN million) excluding oneoffs

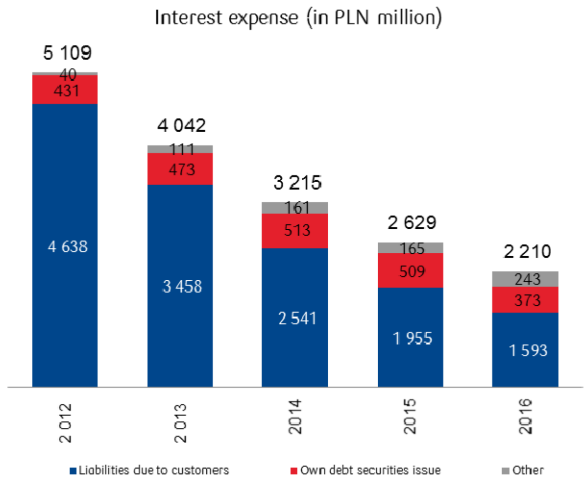
	2016	one-offs	2016 excluding one-offs	2015	one-offs	2015 excluding one-offs	Change (in PLN mn)	Change (in %)
Net interest income	**7 754.8**	**0.0**	**7 754.8**	**7 028.6**	**0.0**	**7 028.6**	**726.2**	**10.3%**
Net fee and commission income	**2 693.4**	**0.0**	**2 693.4**	**2 850.6**	**0.0**	**2 850.6**	**-157.2**	**-5.5%**
Dividend income	10.3	0.0	10.3	10.7	0.0	10.7	-0.4	-3.7%
Net income from financial instruments measured at fair value	4.4	0.0	4.4	40.6	0.0	40.6	-36.2	-89.2%
Gains less losses from investment securities	506.1	417.6	88.5	87.7	0.0	87.7	0.8	0.9%
Net foreign exchange gains (losses)	503.2	0.0	503.2	369.0	0.0	369.0	134.2	36.4%
Net other operating income and expense	318.5	114.0	204.5	277.5	0.0	277.5	-73.0	-26.3%
Net impairment allowance and write-downs	-1 622.7	0.0	-1 622.7	-1 475.9	0.0	-1 475.9	-146.8	9.9%
Administrative expenses	-5 590.4	0.0	-5 590.4	-6 036.2	-480.0	-5 556.2	-34.2	0.6%
Bank on certain financial institutions	-828.9	-828.9	0.0	0.0	0.0	0.0	0.0	x
Operating profit	**3 748.7**	**-297.3**	**4 046.0**	**3 152.6**	**-480.0**	**3 632.6**	**413.4**	**11.4%**
Share in profit (loss) of associates and joint ventures	34.5	0.0	34.5	38.1	0.0	38.1	-3.6	-9.4%
Profit before income tax	**3 783.2**	**-297.3**	**4 080.5**	**3 190.7**	**-480.0**	**3 670.7**	**409.8**	**11.2%**
Income tax expense	-907.1	-83.6	-823.5	-589.5	91.2	-680.7	-142.8	21.0%
Net profit (including non-controlling shareholders)	2 876.1	-381.0	3 257.1	2 601.2	-388.8	2 990.0	267.1	8.9%
Profit (loss) attributable to non-controlling shareholders	2.1	0.0	2.1	-8.3	0.0	-8.3	10.4	x
Net profit	**2 874.0**	**-381.0**	**3 255.0**	**2 609.5**	**-388.8**	**2 998.3**	**256.7**	**8.6%**



NET INTEREST INCOME

Obtained in 2016 net interest income amounted to PLN 7 754.8 million and was PLN 726.2 million higher than last year. The improvement in the net interest resulted from an increase in revenue connected with an increase in the loan portfolio and securities portfolio, as well as a significant reduction in financing costs.





Interest income in 2016 amounted to PLN 9 964.4 million in compared to 2015 was higher by 306.6 million, which is mainly the result of growth:

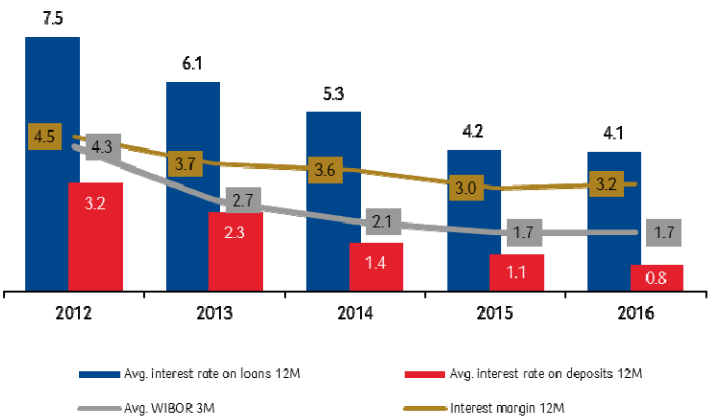
- income from loans and advances to customers of PLN 251.5 million y/y – the drop in income resulting from the drop in market interest rates for PLN and EUR was fully offset by an increase in the average volume of loan receivables, mainly housing and consumer loans,
- income from securities by PLN 153.4 million y/y determined by an increase in the average volume of securities (mainly Treasury Bonds),
- with a decrease in income from hedging derivatives (PLN -110.8 million y/y), mainly due to IRS transactions in PLN matured in 2016.

Interest costs in 2016 amounted to PLN 2 209.6 million in compared to 2015 was lower by 16.0%, which is mainly the result:

- a decrease in the cost of liabilities to customers of PLN 362.4 million y/y, resulting from a lower average interest rate on deposits – the effect of adapting the pricing offer of deposit products to decreasing market rates and the expiry of long-term deposits also resulted from changes in the deposit structure which involved an increase in the share of current deposits in total deposits,
- PLN 101.7 million lower costs of external financing y/y, which was determined by a drop in the level of bonds issued under the EMTN programme, which are gradually replaced with cheaper financing in the form of mortgage bonds,

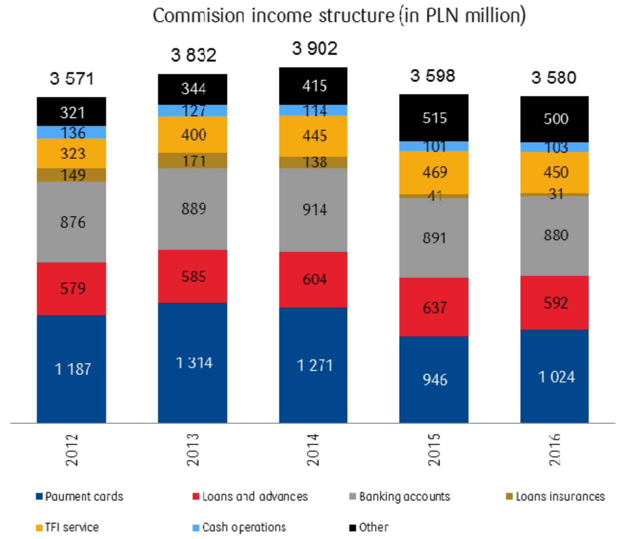
The interest margin increase by approx. 0.2 p.p. y/y to 3.2% at the end of 2016. Average interest-earning assets increased by 6.3% y/y (Mainly the portfolio of amounts due from customers and the securities portfolio), and the annualized net interest income increased by 10.3%, mainly as a result of lower interest expense, with a simultaneous increase in interest income on loans and securities (the effect of an increase in volume).

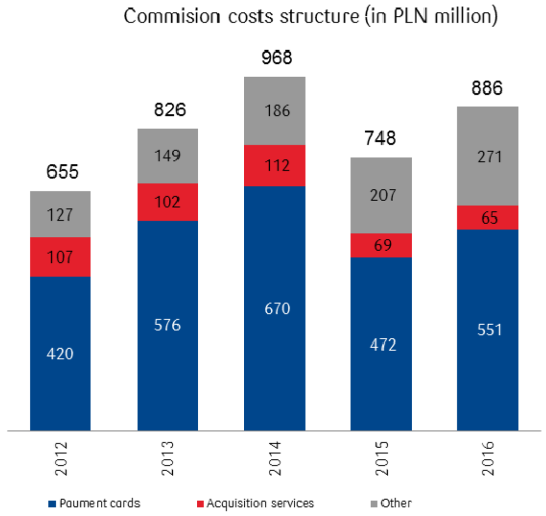
In 2016, the average interest rate on loans of PKO Bank Polski SA amounted to 4.1% and the average interest rate deposits in total stood at 0.8% against, respectively 4.2% and 1.1% in 2015.



NET FEE AND COMMISSION INCOME

Net fee and commission income amounted to PLN 2 693.4 million in 2016 and was PLN 157.2 million lower than in the previous year as a result of commission expenses which were PLN 138.5 million higher accompanied by stable commission income at a level of PLN 3 579.6 million.





The level of net commission income was mainly determined by:

- a lower net commission income on loan insurance (PLN -9.4 million y/y), which was due to, among other things, a decrease in commissions on housing loans insurance; in addition, the sales of insurance products offered by the PKO Bank Polski SA Group entities increased in 2016, and the results on such sales on the Group level are presented under other results on insurance activities,
- a decrease in income on maintaining bank accounts (PLN -11.2 million y/y),
- a decrease in net commission income on maintaining investment funds and pension funds (including management fees) of PLN 18.2 million y/y due to a decrease in management fees and commissions for sale and repurchase, which was a result of adjusting the offer to the market conditions; at the same time, the value of assets under management increased,
- a decrease in income from brokerage activities (PLN -12 million y/y) due to a decrease in the commissions on bond issue arrangement,
- a PLN 6.0 million y/y increase in the costs of maintaining control over construction projects and property valuation, associated with an increase in the sales of housing loans,
- a lower level of income on loans and advances granted (PLN -44.7 million y/y), mainly in respect of business loans,
- a stable result on payment cards (-0.2% y/y). The relatively lower income growth was mainly a result of a high reference level (in the 2nd quarter of 2015, the Bank received payments from payment organizations due to renegotiation of the agreements with such organizations). After eliminating this one-off event, the Group's result on payment cards was PLN 53 million higher than as at the end of 2015, which was partly due to an increase in the income from issue and renewal of cards.

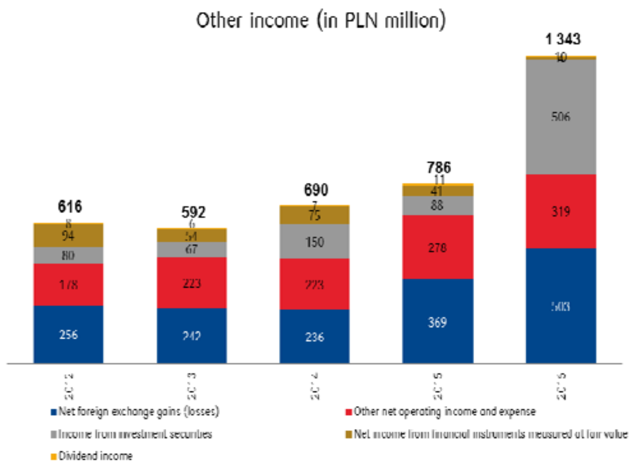
OTHER INCOME

In 2016 other income amounted to PLN 1 342.5 million and increase by PLN 557.0 million compared to the previous year. Level of the other result was mainly determined by the following:

- an increase in gains less losses on investment securities of PLN 418.4 million y/y, which was caused by the settlement, in June 2016, of the acquisition of *Visa Europe Limited* by *Visa Inc.*, in which PKO Bank Polski SA participated; the Bank recognized PLN 417.6 million in this respect,
- an increase in net foreign exchange gains (losses) by PLN 134.2 million, connected mainly with an increase in customer interest in structured deposits based on exchange rate indices,

- an increase in net other operating income of PLN 40.0 million, mainly in consequence of two sales transactions in the third quarter of 2016 of the assets of Qualia Development Sp. z o.o. and its subsidiaries; in this respect the Group recognized additional income of approx. PLN 114 million in other operating income and expenses, given the adverse effect of higher costs of donations,
- accompanied by the result on instruments measured at fair value lower by PLN 36.2 million in total, in consequence of the situation on the Polish debt market, in particular the revaluation of Treasury bonds observed at the end of 2016.

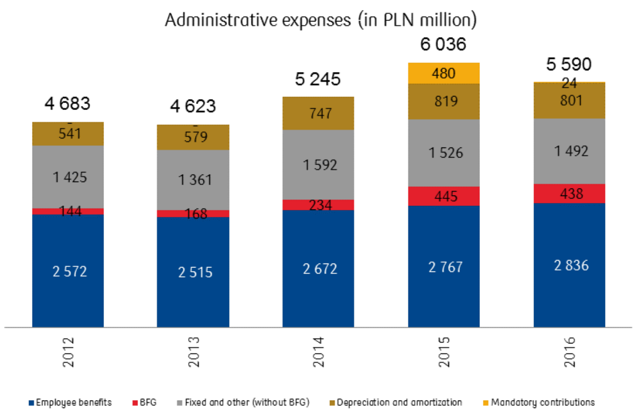
After eliminating one-off events, the other income would amount to approx. PLN 810.9 million, i.e. +3.2% y/y.



Administrative expenses

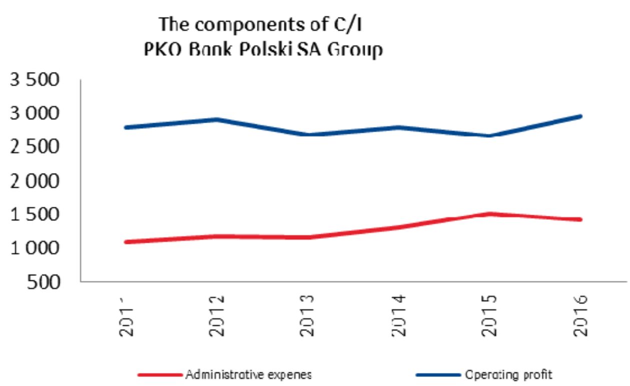
In 2016, administrative expenses amounted to PLN 5 590.4 million and was lower by 7.4% compared to the same period of previous year.

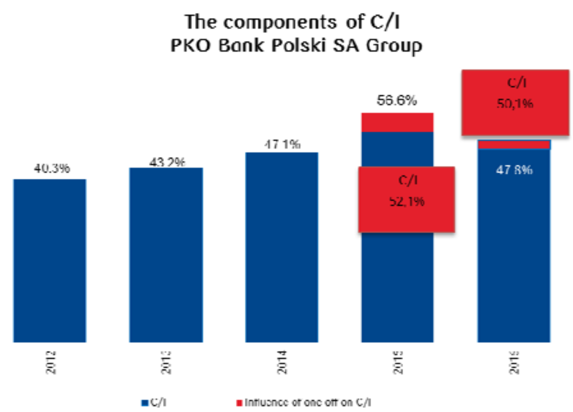
After eliminating the one-off events that occurred in 2015 (the BGF payment to the guaranteed funds protection fund of PLN 337.9 million and payment to the Borrowers' Support Fund of PLN 142.0 million), general administrative expenses were 0.6% higher than in the previous year. Their amount was mainly determined by an increase in the costs of employee benefits of PLN 69.3 million, i.e. 2.5%, which was accompanied by a decrease in material costs of PLN 40.8 million y/y, i.e. 2.8%, and a decrease in amortization and depreciation of PLN 17.9 million y/y, i.e. 2.2%.



As at 31 December 2016, employment in the PKO Bank Polski SA Group amounted to 29 441 full-time positions, which is an increase by 220 positions y/y. Change in employment in subsidiaries y/y is a result of business development and the acquisition of RLPL in December 2016.

The effectiveness of PKO Bank Polski SA Group's performance measured by annualized C/I ratio reached 47.4%.





TAX ON CERTAIN FINANCIAL INSTITUTIONS

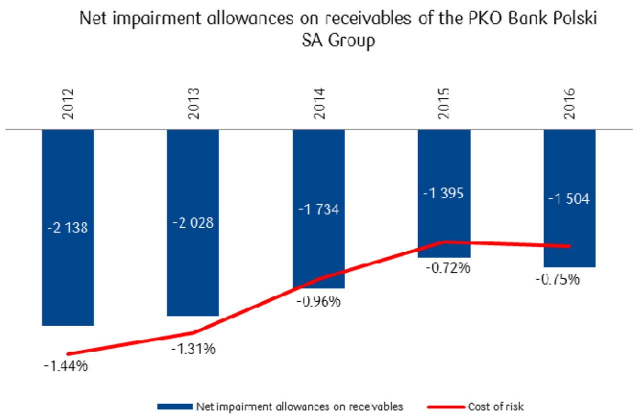
Starting from February 2016 banks and other financial institutions are obliged to pay tax on certain financial institutions. Tax burden on the Group in 2016 amounted to PLN 828.9 million, of which the majority was attributable to PKO Bank Polski SA (PLN 820.2 million).

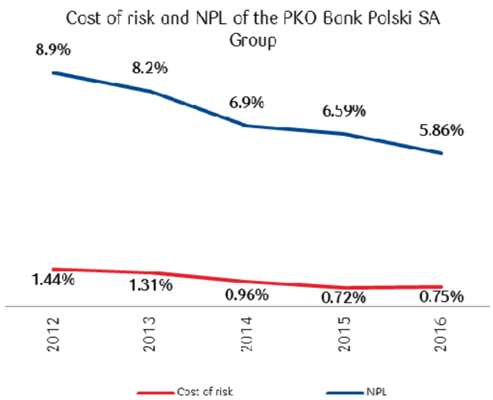
NET IMPAIRMENT ALLOWANCE AND WRITE-DOWNS

The amount of net impairment write-downs and provisions reflects the conservative approach of the PKO Bank Polski SA Group to recognizing and measuring credit risk. The net write-downs deteriorated (9.9% y/y) due to an increase in write-downs recorded by the Bank on corporate customer portfolios.

The share of loans with recognized impairment and coverage of loans with recognized impairment as at the end of 2016 amounted to 5.9% (a decrease of 0.7 p.p. in relation to 2015) and 65.5% (an increase of 2.2 p.p. in relation to 2015), respectively. The improvement was due to an improvement in the quality of business loans and the consistent policy of selling irregular receivables.

The cost of risk[8] at the end of 2016 amounted to 0.75% and has not changed significantly compared to 2015.





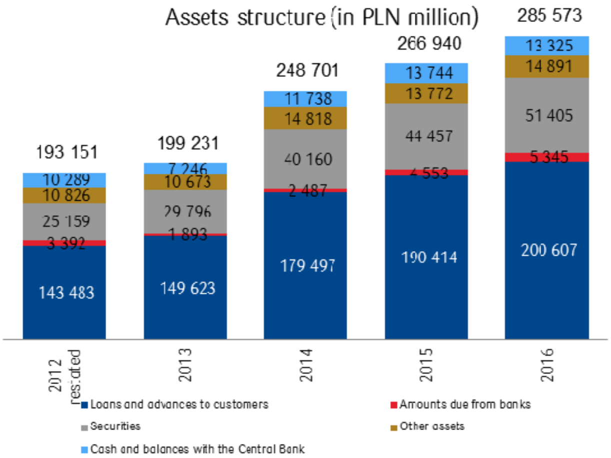
3.3 CONSOLIDATED STATEMENT OF FINANCIAL POSITION

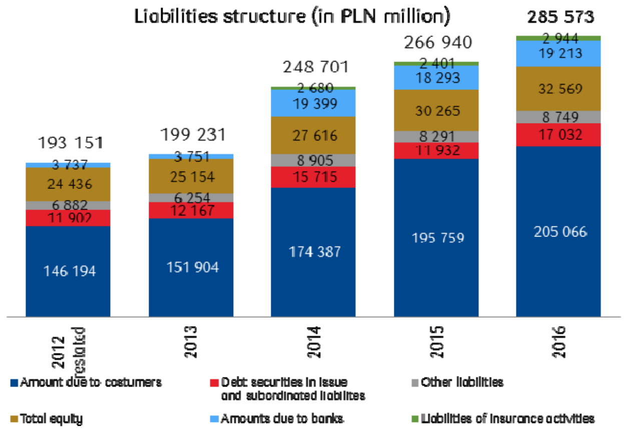
The main items of the statement of financial position
Loans and advances to customers
Securities
Amounts due to customers
External financing
Equity and capital adequacy ratio

THE MAIN ITEMS OF THE STATEMENT OF FINANCIAL POSITION

The statement of financial position of the PKO Bank Polski SA Group is most influenced by the statement of financial position of the parent entity. It determines both the size of total assets and the structure of assets and liabilities. The total assets of the PKO Bank Polski SA Group amounted to PLN 285.6 billion as at the end of 2016, which means an increase by 7.0% y/y.

[8] Calculated by division of net impairment allowance and write-downs of loans and advances to customers for 12 month period ended 31 December 2016 and 2015 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





The increase in the volume of loans and advances to customers of PLN 10.2 billion y/y and of the securities portfolio of PLN 6.9 billion y/y had the key impact on the increase in assets of the PKO Bank Polski SA Group. The increase in assets was financed mainly with an increase in amounts due to customers of PLN 9.3 billion y/y and an increase in liabilities in respect of securities issued of PLN 5.1 billion y/y.

Table 4. Main items of the statement of financial position of the PKO Bank Polski SA Group (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)
Cash and balances with the central bank	13 325	13 744	-419	-3.0%
Amounts due from banks	5 345	4 553	792	17.4%
Loans and advances to customers	200 607	190 414	10 193	5.4%
Securities	51 405	44 457	6 948	15.6%
Other assets	14 891	13 772	1 119	8.1%
Total assets	**285 573**	**266 940**	**18 633**	**7.0%**
Amounts due to banks	19 213	18 293	920	5.0%
Amount due to costumers	205 066	195 759	9 308	4.8%
Debt securities in issue and subordinated liabilites	17 032	11 932	5 100	42.7%
Liabilities of insurance activities	2 944	2 401	543	22.6%
Other liabilities	8 749	8 291	458	5.5%
Total liabilities	**253 004**	**236 675**	**16 329**	**6.9%**
Total equity	32 569	30 265	2 304	7.6%
Total liabilities and equity	**285 573**	**266 940**	**18 633**	**7.0%**
Loans/Deposits	97.8%	97.3%		0.6 p.p.
Loans/Stable sources of funding*	83.7%	85.0%		-1.3 p.p.
Interest bearing assets/Assets	90.1%	89.7%		0.4 p.p.
Interest paying liabilities/Liabilities	84.5%	84.7%		-0.2 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 generic structure of the net credit portfolio consisted mainly of housing loans (52.9% of the portfolio as at the end of 2016); their volume increased by PLN 5.5 billion during the year. In 2016 an increase in the most profitable consumer loans of PLN 1.3 billion and of lease receivables (PLN +6.6 billion y/y) was also noted, which was related to the acquisition of RLPL by PKO Leasing SA.

Table 5. Loans and advances to customers of PKO Bank Polski SA Group – structure by type (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)
Loans and advances to customers net	**200 607**	**190 414**	**10 193**	**5.4%**
Loans	182 258	175 163	7 095	4.1%
Mortgages	106 121	100 669	5 453	5.4%
Business	52 915	52 535	380	0.7%
Consumer	23 222	21 960	1 262	5.7%
Debt securities	4 871	5 285	-414	-7.8%
Debt securities (corporate)	2 283	2 592	-309	-11.9%
Debt securities (municipal)	2 588	2 693	-105	-3.9%
Repurchase agreements	1 339	4 432	-3 093	-69.8%
Receivables from financial leases	12 139	5 534	6 605	2.2x

The maturity structure of loans and advances to customers, which increased by 7.2% y/y compared with 2015 in effect of the increase in the portfolio of housing loans, plays a dominant role in long-term loans (76.9% of the portfolio). Short-term loans with a share of 24.0% noted negative growth at a level of -1.6% y/y.

Table 6. Loans and advances to customers of PKO Bank Polski SA Group – term structure (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)	Structure 2016
Loans and advances to customers (gross), in this:	208 609	198 701	9 908	5.0%	100.0%
Short-term	48 222	49 020	-799	-1.6%	23.1%
Long-term	160 388	149 681	10 707	7.2%	76.9%
Total impairment allowances	-8 003	-8 287	284	-3.4%	x
Total	**200 607**	**190 414**	**10 193**	**5.4%**	x

Securities

As at the end of 2016, the securities portfolio of the PKO Bank Polski SA Group amounted to PLN 51.4 billion and recorded an increase by PLN 6.9 billion compared with the end of 2015. In the structure of the portfolio by type, the main items were debt securities issued by State treasury and issued by the central banks.

Table 7. Securities portfolio of the PKO Bank Polski SA Group (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)
Financial instruments designated at fair value through profit or loss account	13 937	15 154	-1 217	-8.0%
Available for sale investment securities	36 676	28 310	8 366	29.6%
Investment securities held to maturity	466	210	255	2.2x
Trading assets	326	783	-457	-58.3%
Total	**51 405**	**44 457**	**6 948**	**15.6%**

Amounts due to customers

The generic structure of amounts due to customers, the main item amounts to the individuals (72.2% of the portfolio as at the end of 2016), along with an decrease in share of amounts due to corporate entities and liabilities of the budgetary unit.

Table 8. Amounts due to customers of the PKO Bank Polski SA Group structure by type (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)	Structure 2016
Amounts due to individuals	148 000	135 410	12 590	9.3%	72.2%
Amounts due to enterprises	48 657	51 214	-2 557	-5.0%	23.7%
Amounts due to budget entities	8 409	9 134	-725	-7.9%	4.1%
Total amounts due to customers	**205 066**	**195 759**	**9 308**	**4.8%**	x

In 2016, the term structure of amounts due to customers changed. The share of liabilities with maturity up to 1 month increased by PLN 9.4 billion and amounted to 63.9% of all amounts due to customers as at 31 December 2016. An increased share was also noted in liabilities maturing after one year, associated with the migration of funds from short-term term deposits (up to 1 year) to new long-term structured deposits sold in 2016 as part of the Bank's offer and to previously offered long-term (over 1 year) savings products. These movements in funds also contributed to the decrease in liabilities maturing from 1 to 3 months.

Table 9. Amounts due to customers of the PKO Bank Polski SA Group – term structure (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)	Structure 2016
Up to 1 month	135 960	126 532	9 428	7.5%	63.9%
1 month - 3 months	19 168	21 868	-2 700	-12.3%	9.0%
3 months - 1 year	35 334	34 840	494	1.4%	16.6%
1 year - 5 years	13 863	10 565	3 298	31.2%	6.5%
over 5 years	8 296	6 192	2 104	34.0%	3.9%
Adjustment of the value and interest	-7 555	-4 238	-3 317	78.3%	x
Total amounts due to customers	**205 066**	**195 759**	**9 308**	**4.8%**	**x**

EXTERNAL FINANCING

The PKO Bank Polski SA Group is an active participant in the market of debt security issues, both local and international. These actions are intended to diversify the sources of financing of operations and to adapt them to regulatory requirements.
As at the end of 2016 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).
Another important category of long-term financing were liabilities in respect of securities in issue. The increase in these liabilities is mainly the effect of:

- issue of mortgage bonds by PKO Bank Hipoteczny SA, which increased by PLN 4.3 billion in 2016 compared with the previous year,
- acquisition of securitization bonds by the PKO Leasing SA Group under the acquisition transaction of RLPL, which enabled increasing liabilities related to issues by PLN 1.4 billion,

with a simultaneous drop in bonds in issue under the EMTN programme by PLN 0.6 billion y/y.
The volume of subordinated liabilities, which include a subordinated loan in CHF of acquired Bank, remained stable.
Detailed information on the issues carried out by the PKO Bank Polski SA Group is described in note 35 of the Consolidated Financial Statements of the PKO Bank Polski SA Group for the year ended 31 December 2016.

Table 10. External financing of the PKO Bank Polski SA Group (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)
Debt securities in issue	14 493	9 433	5 060	53.6%
Subordinated liabilities	2 539	2 499	40	1.6%
Loans and borrowings received - monetary institutions*	17 567	16 418	1 149	7.0%
Loans and borrowings received - non-monetary institutions**	4 662	3 924	738	18.8%
Total	**39 262**	**32 274**	**6 987**	**21.6%**

** In the Statement of financial position of PKO Bank Polski SA Group carried in a position "amounts due to banks".*

*** In the Statement of financial position of PKO Bank Polski SA Group carried in a position "amounts due to customers".*

4. EQUITY AND CAPITAL ADEQUACY RATIO

Equity and its profitability
The capital adequacy measures
Dividend

4.1 EQUITY AND ITS PROFITABILITY

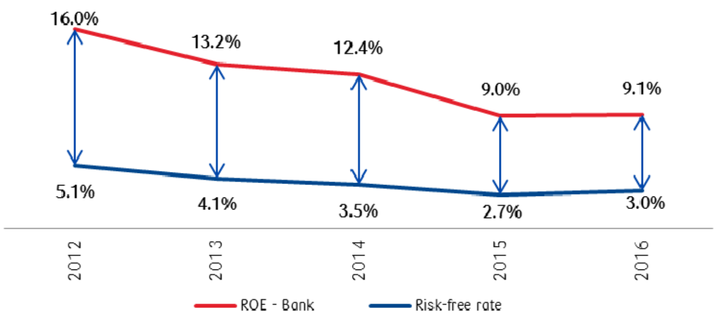
Equity of the PKO Bank Polski SA Group increased by 7.6% per annum and accounted for 11.4% of liabilities as at the end of 2016.

Table 11. Equity and total capital ratio of the PKO Bank Polski SA Group (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)
Equity, including:	**32 569**	**30 265**	**2 304**	**7.6%**
Share capital	1 250	1 250	0	0.0%
Reserve capital	24 491	20 711	3 779	18.2%
The general banking risk fund	1 070	1 070	0	0.0%
Other reserve capital	3 608	3 536	71	2.0%
Financial assets available for sale	-347	171	-518	x
Share in other comprehensive income of the associated entities	-1	0	-1	4x
Cash flow hedges	-109	-58	-51	88.0%
Actuarial gains and losses	-11	-13	2	-16.0%
FX differences arising from translation of the result of foreign entities	-222	-217	-5	2.3%
Undistributed profits	-19	1 222	-1 241	x
Net profit for the year	2 874	2 610	265	10.1%
Non-controlling interests	-16	-18	2	-11.5%
Own funds	**30 873**	**27 091**	**3 782**	**14.0%**
Capital adequacy ratio	**15.81%**	**14.61%**		**1.2 p.p.**

Significant reinforcement of the capital base (an increase in average equity of 9.2% y/y), with the profit dynamics of 10.1% y/y translated into increase of the return on equity ratio (ROE) to the level of 9.1 p.p.

ROE PKO Bank Polski SA Group/risk-free rate*



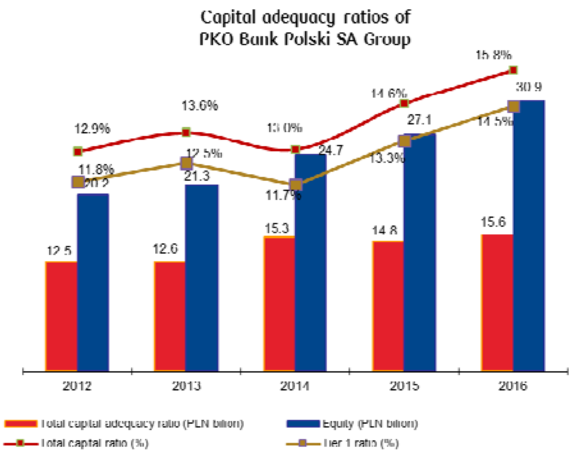
* risk-free rate is calculated as an average yearly return from 10-years State Treasury Bonds.

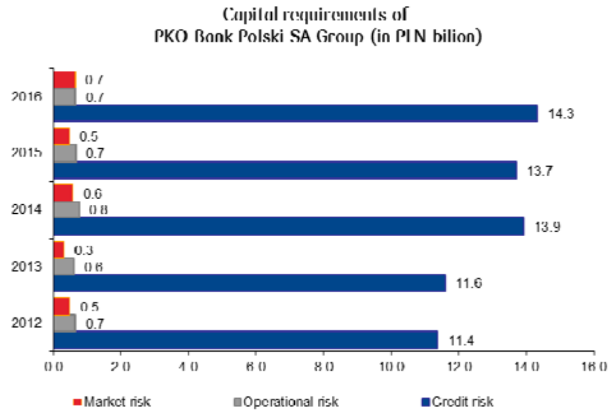
4.2 THE CAPITAL ADEQUACY MEASURES

The level of the PKO Bank Polski SA Group's capital adequacy in 2016 remained at a safe level, significantly above the supervisory limits. On 31 December 2016 the capital adequacy measures have been calculated based on the provisions of the CRR Regulation.

In 2016 PKO Bank Polski SA Group continued efforts to provide adequate capital buffer, as well strengthen its capital position.

As at 31 December 2016 compared with 31 December 2015, the Group's capital ratio increased by 1.2 p.p. to the level of 15.81%, basic capital ratio Tier 1 by 1.2 p.p. to the level of 14.51%.





The increase in the adequacy ratios in 2016 was mainly determined by an increase in own funds of approx. PLN 3.8 billion as a result of retaining all profit of 2015, and allocating part of the 2016 profit of PLN 1.6 billion to own funds, upon the consent of the Financial Supervision Authority.

The increase in the own funds requirement in respect of risk in 2016 of approx. PLN 0.8 billion compared with 31 December 2015 had an impact on the development of business activity of the PKO Bank Polski Group and the acquisition of RLPL by PKO Leasing SA.

4.3 DIVIDEND

On 30 June 2016 the Ordinary General Shareholders' Meeting of the Bank adopted resolution (No. 7/2016, Resolution on the distribution of profit) on distribution of the net profit for the period from 1 January 2015 to 31 December 2015 (PLN 2 571.1 million) and retained earnings from previous years (PLN 1 250.0 million), in the total amount of PLN 3 821.1 million as follows:

- dividend for shareholders PLN 1 250.0 million (which represents PLN 1.00, gross, per share),
- reserve capital in the amount of PLN 2 500.0 million,
- other reserve in the amount of PLN 71.1 million.

The distribution of the profit described above was dependent on meeting, incluging, the following conditions ('Meeting the Conditions for the Dividend Payment'), by 8 December 2016:

- PKO Bank Polski SA shall not take over control of a bank or other entity of the financial sector by a direct or indirect acquisition of a block of shares and shall not acquire a right or incur an obligation to take over control in the manner specified above, and
- there shall not occur any regulatory changes or changes of the supervisory recommendations affecting the requirements for the Bank's own funds that – according to the level of capital adequacy ratios recognized in the financial statements of the Bank for Q3 2016 – would cause a lack of possibility to pay dividend in accordance with the regulatory requirements and supervisory recommendations.

The Bank's Management Board was put under an obligation to pass, no later than by 9 December 2016, a resolution on Meeting the Conditions for the Dividend Payment or failure to meet them.

On 1 December 2016, a transaction comprising the acquisition of 100% of shares in RLPL by PKO Leasing was closed. Furthermore, the Bank's Management Board passed a resolution stating a failure in Meeting the Conditions for the Dividend Payment. In consequence, the Bank's profit earned in 2015 and undistributed profits from previous years were distribution in the manner specified in § 2 of the Resolution on the Distribution of Profit, which assumes that the entire profit be earmarked for transfer to the supplementary capital and the reserve capital, without providing for the payment of a dividend.

Therefore, in 2016 the Bank retained the entire undistributed profits from previous years (PLN 1 250 millions worth of the undistributed profits from 2014) and the entire profit earned in 2015 (in the amount of PLN 2 571.1 millions), which brought about an increase in the Bank's equity of PLN 3 821.1 millions thousand in total.

According to the Financial Supervision Authority's position of 6 December 2016 on dividend policy, the required level of capital ratios for Bank Polski SA to be allowed to pay dividend out of profit of 50%, is, respectively:

- Total capital ratio TCR = 14.83%
- Capital ratio T1 = 14.62%.

In accordance with the PFSA guidelines, the Bank should meet the criteria for dividend distribution both at the standalone and consolidated level, as at the last reporting date before the decision on the payment.

Moreover, the PFSA indicated that the banks which are significantly engaged in currency housing loans for households (which have receivables from the non-financial sector of over 5% of the share in currency housing loans for households) adjust the dividend rate based on two additional criteria:
1) Criterion 1 (K1) – which relies on the share of currency housing loans for households in the entire portfolio of receivables from the non-financial sector;
2) Criterion 2 (K2) – based on the share of currency housing loans granted in the years 2007-2008 (loans decisive for the amounts of bank losses in the case of implementing potential statutory solutions) in the portfolio of currency housing loans of households.

The PFSA recommended applying respective adjustments depending on the portfolio held by the Bank:
1) Criterion 1:
   a) banks with a share of over 10% - adjustment of the dividend rate of 20%,
   b) banks with a share of over 20% - adjustment of the dividend rate of 30%,
   c) banks with a share of over 30% - adjustment of the dividend rate of 50%.
2) Criterion 2:
   a) banks with a share of over 20% - adjustment of the dividend rate of 30%,
   b) banks with a share of over 50% - adjustment of the dividend rate of 50%.

As at 31 December 2016, the share of currency housing loans for households in the entire portfolio of amounts due from the non-financial sector of the PKO Bank Polski SA amounts to approx. 20%, and the share of the currency portfolio granted in the years 2007-2008 – to approx. 44%.

The general principle of the Bank's dividend policy is the stable execution of dividend payments over a long period in keeping 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 Financial Supervision Authority in respect of dividend policy.

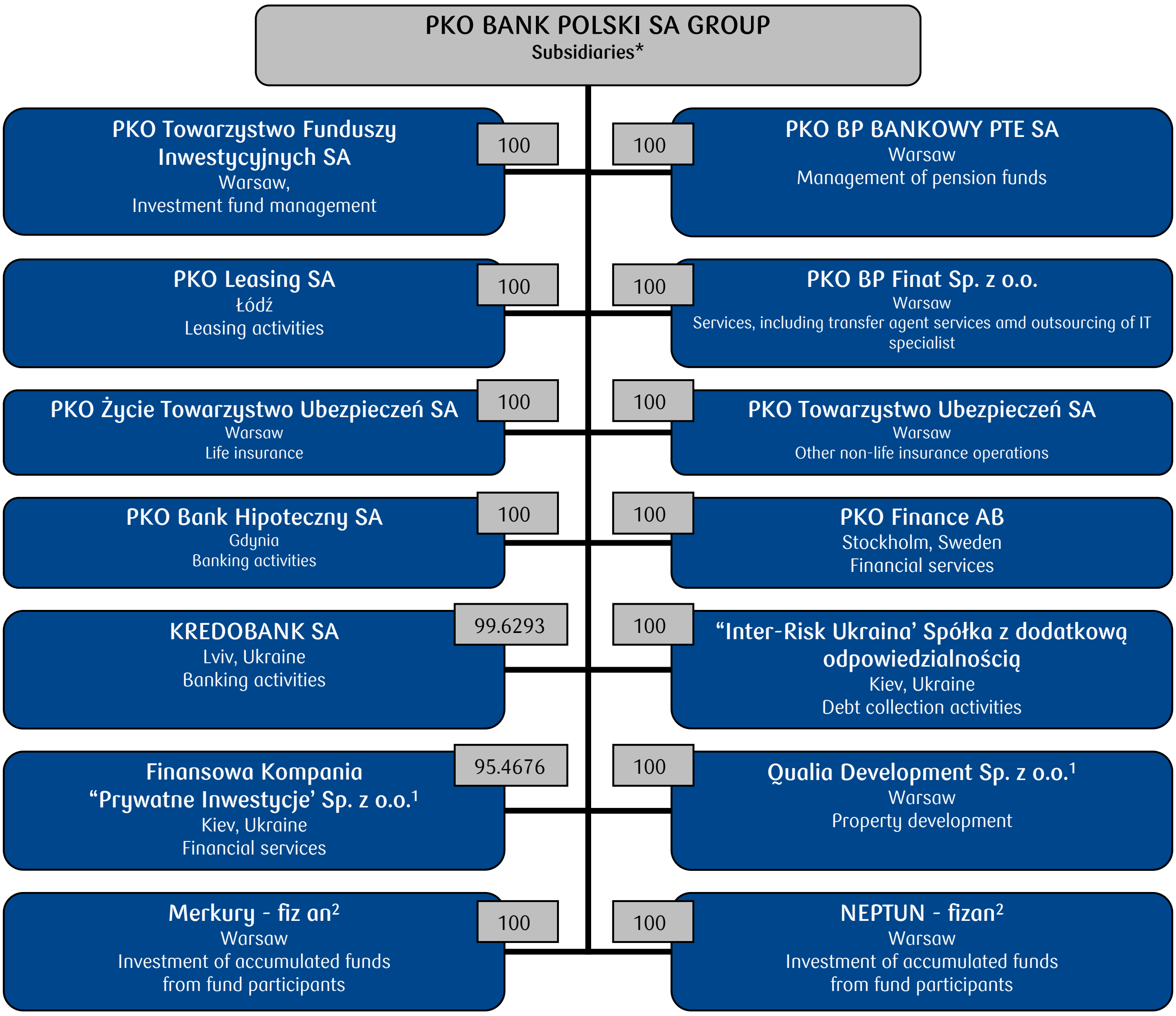
5. ORGANIZATION OF THE PKO BANK POLSKI SA GROUP

Entities included in the financial statement
Organization of the PKO Bank Polski SA Group
Key changes in the structure of the Bank's Group in 2016

5.1 ENTITIES INCLUDED IN THE FINANCIAL STATEMENT

As at 31 December 2015, the PKO Bank Polski SA Group consisted of the Bank, as the parent company and the 42 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 acquisition method.
1) The second shareholder of the Company is 'Inter-Risk Ukraina' Spółka z dodatkową odpowiedzialnością (a company with additional liability); in the Bank's financial statements the Company is recognized under 'non-current assets held for sale'.
2) PKO Bank Polski SA holds the Fund's investment certificates; the Fund's investment certificates held are presented as the share in equity.

The full description of the Group is included in the financial Statements of the PKO Bank Polski SA Group for the year ended 31 December 2016.

5.2 KEY CHANGES IN THE STRUCTURE OF THE BANK'S GROUP IN 2016

ACQUISITION OF RAIFFEISEN-LEASING POLSKA SA BY PKO LEASING SA

On 2 November 2016, PKO Bank Polski SA (as the guarantor), Raiffeisen Bank International AG (as the seller) and PKO Leasing SA (as the purchaser) signed an agreement on the sale of 100% of shares in Raiffeisen-Leasing Polska SA by Raiffeisen Bank International AG to PKO Leasing SA. The transaction was closed on 1 December 2016 after the conditions precedent had been met, including, among other things, gaining the required anti-monopoly consents in Poland and Ukraine.

As a result of the aforementioned transaction, PKO Leasing SA purchased 1 500 038 ordinary shares in Raiffeisen-Leasing Polska SA with a nominal value of PLN 100 each, representing 100% of the Company's share capital and entitling to 100% of the voting rights at the General Meeting of the Company. The purchase price amounted to PLN 850 million. The purchase of the shares was financed entirely with a loan granted by PKO Bank Polski SA.

The business operations of the purchased company consist of conducting leasing activities and granting loans.

As part of the transaction, PKO Bank Polski SA replaced the financing granted to Raiffeisen-Leasing Polska SA and its subsidiaries by Raiffeisen Bank International AG or the entities in its Group, totalling PLN 2 412 million and PLN 255.6 million. The transaction was financed with PKO Bank Polski SA's own funds.

In 2017, both companies, i.e. PKO Leasing and Raiffeisen-Leasing Polska SA, are planned to be merged, including the performance of a legal merger in April 2017.

Full information about this transaction and other changes in the structure of the Bank's Group in the reporting period is included in the Financial Statements of PKO Bank Polski SA for the year ended 31 December 2016.

6. ACTIVITIES OF PKO BANK POLSKI SA GROUP[9]

Activities of PKO Bank Polski SA Market position of PKO Bank Polski SA Group International cooperation Activities of other entities of the PKO Bank Polski SA Group Sponsorship activities Charity activities Prizes and awards

6.1 ACTIVITIES OF PKO BANK POLSKI SA – THE PARENT COMPANY OF THE PKO BANK POLSKI SA GROUP[10]

Retail segment Corporate and investment segment

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

[9] Financial information of members of the PKO Bank Polski SA Group is presented in accordance with the Companies' financial statements prepared in line with IAS/IFRS.
[10] In this sub-chapter the Bank's management information is presented; any differences in total balances, shares and growth rates result from rounding.

RETAIL SEGMENT

The retail segment offers a full range of services for individuals as part of retail and private banking. Moreover, it comprises transactions conducted with legal persons, i.e. 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: 9.2 MN

LOANS VOLUME: 146 BN

DEPOSITS VOLUME: 162 BN

CORPORATE AND INVESTMENT SEGMENT

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

NUMBER OF CUSTOMERS: 15 K

LOANS VOLUME: 52 BN

DEPOSITS VOLUME: 38 BN

6.1.1 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 2016, PKO Bank Polski SA continued sustained development in the area of retail segment customers, focused on identifying and satisfying the needs of its customers with whom it builds strong, long-term relations. It initiated initiatives aimed at increasing service quality, among other things, by activities leading to increased innovation in respect of new financial solutions, both in respect of products and distribution channels, in particular with regard to electronic banking and mobile payments.

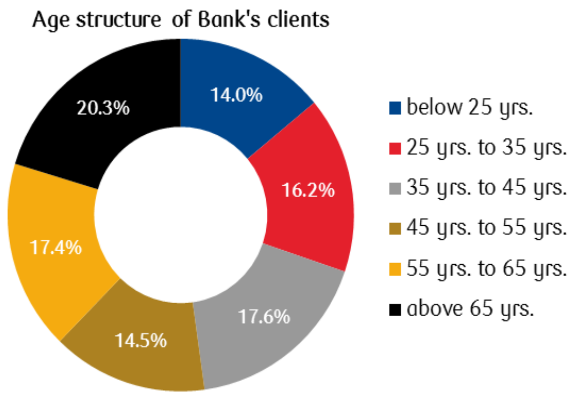
In the period discussed, in all branches of PKO Bank Polski SA the New Sales Rhythm programme was launched. Thanks to this programme, the Bank became even more clearly a multi-channel institution with fast processes, innovative products and personalized offers for customers.

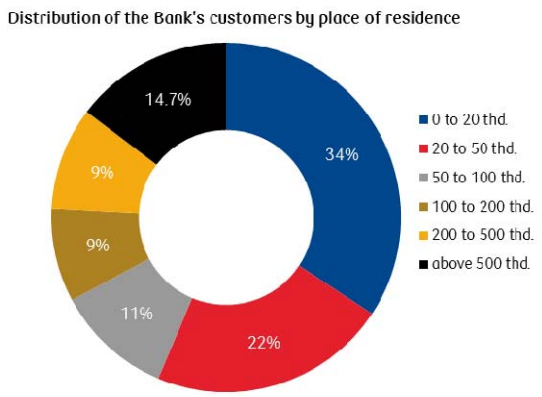
The New Sales Rhythm programme provides modern tools and functionalities of bank applications which – due to the ergonomic support of the Platin CRM (Customer Relationship Management) system – ensure more complete knowledge of the customer and allow to present the customer with the most suitable offer of cash advances tailored to their needs. Also the processes and formalities connected with the consumer finance products have been significantly simplified. All the implemented features are supported with an integrated motivation system with new tools for consultants across the network of branches.

CUSTOMERS OF THE SEGMENT

At the end of 2016 number of serviced customers in retail segment reached 9.2 million, in which 8.8 million were individuals. More than a half of retail segment customers regularly use electronic banking. The most active group of users are customers aged between 18 and 35.

Due to the wide range of distribution channels most of Banks customers (approx. 67%) lives in municipality under 100 thousand citizens. Trustworthy bank's brand, ability in combining tradition with modernity and transparent product offer, which includes time-varying customer preferences, makes bank recognizable not only in urban centers. What is more, due to the demographic profile c.a. 48% of customer base are aged under 45.





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 (over 87%) and by consumer loans (over 12%).

THE LOAN OFFER IN THE RETAIL SEGMENT

The PKO Bank Polski SA offer covers a wide range of credit products. Individuals can take advantage of the financing offered under loans:

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

Offer for small and medium-sized enterprises is available in the form:

- of investment and investor,
- working capital loans.

By the end of 2016 gross loans of retail segment of PKO Bank Polski SA amounted to PLN 146 billion and since the beginning of the year increased almost by PLN 6 billion (i.e. by 4%). Mainly due to growth in mortgage portfolio (PLN +5.4 billion since the beginning of the year) and retail and private banking (PLN +0.9 billion).

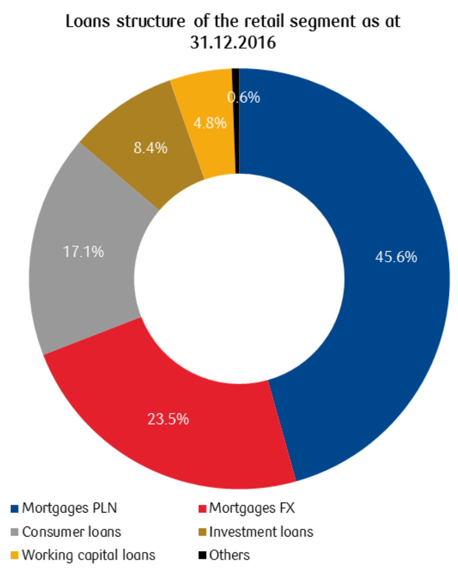


Table 12. Loan balances in the retail segment (in PLN million)

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015	Change (in PLN million)
Gross loans and advances granted, of which:							
retail and private banking	24 280	23 340	21 455	20 399	21 601	4.0%	940
mortgage banking including PKO Bank Hipoteczny SA loans	101 303	95 936	90 623	68 795	63 815	5.6%	5 366
small and medium enterprises	20 571	21 313	21 504	21 632	20 930	-3.5%	-742
Total	**146 154**	**140 589**	**133 582**	**110 827**	**106 347**	**4.0%**	**5 564**

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.

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

- 'Mini Ratka z gwarantowaną stałą ratą' - promoting the sale of short-term cash loan for up to 6 months. The offer was addressed to customers looking for short-term financing, rapid credit decision and a minimum of formalities.
- 'Mini Ratka na pierwszy dzwonek' – an offer with attractive pricing for a maximum of 9 months.
- 'Mini Ratka łączy na święta' – promoting the possibility of consolidation of existing debts and obtaining additional financing even up to 25 percent of the consolidated amount.

PKO Bank Polski SA systematically takes measures to increase effective access to credit offer for retail customers and private banking, regardless of distribution channel. As part of the activities performed:

- the text of the credit application and agreement has been simplified,
- the waiting time for the credit decision and disbursement of funds was shortened,
- the offer has been simplified – irrespective of the customer segment, one product, cash advance with an individually agreed price has been made available.
- 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,
- The new sales process for renewal loans new service One Click was introduced, owner of saving account can sent request via iPKO transaction system or Contact Center (CC) and accept agreement with authorization tool,
- in December 2016, the remote iPKO and CC channels launched a process which allows to grant or extend a limit of admissible negative balance without the need to visit the branch.

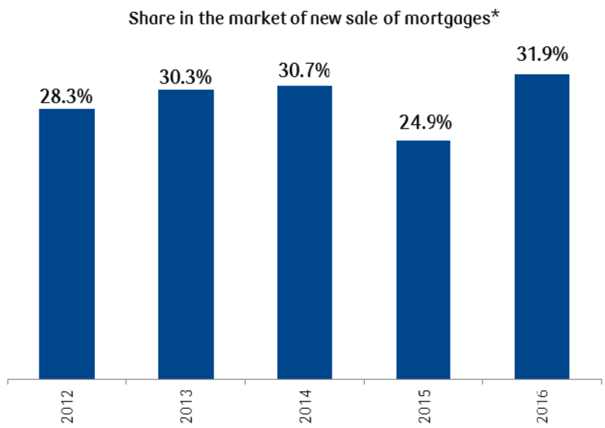
Mortgage banking loans

PKO Bank Polski SA has been a long-term leader in financing the housing needs of people in Poland.

According to the data presented by the Polish Bank Association it shows that at the end of 2016 PKO Bank Polski SA was the first on the market with 31.9% share in sales of mortgage loans for individuals. In 2016 a total amount of granted loans equalled to approx. PLN 12.5 billion.

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

PKO Bank Polski SA strives to provide customers not only with the widest range of credit products, but also to offer attractive prices of mortgage products available in the Banks offer. In promotional periods 'Mortgage Loans' Open Days' it introduced a periodic decrease in margins.



*source: ZBP, share of PKO Banku Polskiego SA and PKO Banku Hipotecznego SA

PKO Bank Polski SA granted under the 'Mieszkanie dla Młodych' programme more than 8.5 thousand loans for a total amount of PLN 1.4 billion. The programme consists of subsidies from the state budget to own contribution and additional financial support in the form of repayment of part of the loan.

In 2016, a special offer for owners of Large Family Card was introduced, valid until 31 August 2020, in which commission for granting the 'Własny Kąt Hipoteczny' housing loan was reduced to 50% of the standard commission for granting loans.

PROCESSES AND ACTIONS IN SUPPORT OF BORROWERS WITH HOUSING LOANS

In connection with the entry into force on 19 February 2016 the law on support for borrowers in a difficult financial situation, the Bank implemented the process of granting support. The new solution is dedicated to borrowers in a difficult financial situation, who have a mortgage loan - either in local currency or in foreign currency, secured by mortgage on the credited property.

From the support will benefit those who on the day of submission of the application fulfil, among others, the following conditions:

- they will have the status of unemployed,
- the monthly cost of servicing the loan exceeds 60% of monthly household income,
- monthly household income net of loan instalment does not exceed the thresholds entitling to benefit from social assistance.

The solutions enable financial support by the Bank Gospodarstwa Krajowego for a period not longer than 18 months, the equivalent of mortgage loan installments (principal and interest), but no more than PLN 1.5 thousand per month. As at 31 December 2016 there were 146 requests for support registered in the Bank's system.

According to a previous declaration the Bank continued to apply operations to compensate customers for an increase in loan installments due to the strengthening of the Swiss franc, including:

- 1% spread in handling mortgage loans in this currency,
- taking into account the negative rate of LIBOR CHF in the cost of a mortgage loan,
- extending the repayment date within the maximum term of the loan without charging a fee for extension of the term of the loan.

In addition, the Bank provided customers with the opportunity to apply for change of collateral of the loans in CHF in order to allow the sale of real estate secured with mortgage, associated with the granting of a new loan in PLN and the establishment of a mortgage on a newly purchased property. In the last quarter of 2016, the validity of the offer supporting borrowers with CHF mortgage loans was extended until 30 June 2017.

LOANS FOR SMALL AND MEDIUM ENTERPRISES

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

As at 31 December 2016, the value of loans granted under the '*De minimis* Guarantee Portfolio Line' programme totalled PLN 4.0 billion. PKO Bank Polski SA was the largest lender of the twenty-one banks providing loans with de minimis guarantees and held 22.1% market share (according to the data provided by the Center of Sureties and Guarantees in Bank Gospodarstwa Krajowego, as at 31 December 2016). Guarantee limit currently granted to PKO Bank Polski SA was risen by PLN 2.5 billion and amounts now PLN 7.3 billion. As at 31 December 2016 the exposure measured by the value of active signed contracts amounted to PLN 2.2 billion. In turn, the value of loans granted under 'COSME Portfolio Guarantee Line' as at 31 December 2016 totalled over PLN 155 million, and guarantees granted amounted to PLN 124 million. In the fourth quarter of 2016, the value of the guarantee limit under the PLG COSME programme was increased to PLN 250 million for the period to 28 September 2017.

On 24 February 2016, PKO Bank Polski SA and Bank Gospodarstwa Krajowego signed an annex to the portfolio guarantee de minimis agreement, on the basis of which innovative entrepreneurs will be granted de minimis guarantees financed from by the Operational Programme Innovative Economy (OPIE) Guarantee Fund. The pool of available funds in PKO Bank Polski SA is PLN 55 million.

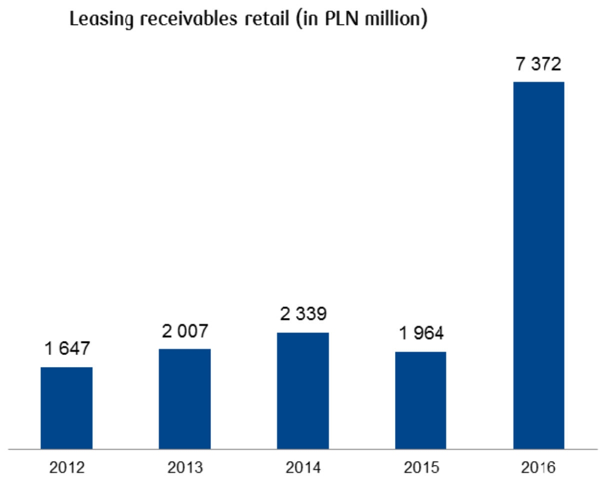
In the period discussed, PKO Bank Polski SA addressed several promotions to small- and middle-sized enterprises, in order to support their investments and business goals financially. Moreover, the multi-channel sale of working capital loans and an SME advances functionality was introduced. Thanks to the new and simplified process, customers can purchase products even up to PLN 50 thousand without leaving their office, without submitting financial documents or security. The loan agreement is concluded online through the electronic banking functionality (iPKO) and authorized using a text message (SMS).

LEASING FOR SMES

Under the Group offer, customers from the small and medium enterprise sector may use lease products and services. Practically any fixed asset may be financed in the form of a lease, depending on the customer needs, including:

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

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



In 2016 the offer of Car Assistance were extended and GAP was reinforced, which increased the attractiveness of the products for the Customers. Additionally, a new product was introduced, Loss of Profits Insurance, which guarantees the Customers the refund of the difference in income before tax in the event of a total loss or theft.

As a result of purchasing the RLPL company, the lease receivables portfolio in the retail segment increased by PLN 4.7 billion.

DEPOSIT AND INVESTMENT OFFER

In 2016 PKO Bank Polski SA continued activities aimed at offering more attractive deposits and investments for changing retail segment customer's needs, taking into account current market conditions and competitive position. At the same time, activities aimed at diversifying sources of financing were carried out.

As at 31 December 2016 the deposits of the retail segment of PKO Bank Polski SA amounted to PLN 162 billion and from the beginning of the year increased by PLN 14 billion (i.e. 9.5%). The increase in deposits of retail and private banking and deposits from SMEs contributed to this, due to growth of current and term deposits volume, with current deposits growing apparently faster.

Table 13. Deposit balances in the retail segment (in PLN million)

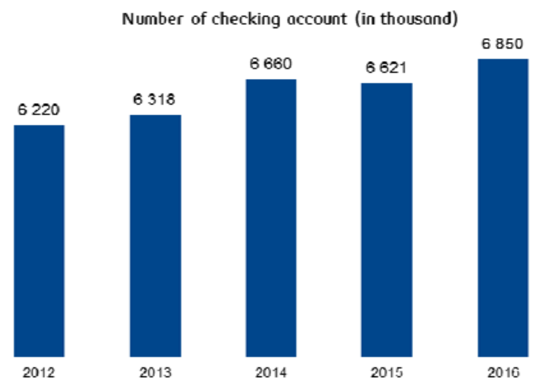
	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015	Change (in PLN milion)
Customer deposits, of which:							
retail and private banking	139 423	127 833	121 893	110 608	105 799	9.1%	11 590
small and medium enterprises	22 243	19 803	17 213	14 757	13 413	12.3%	2 440
Total	**161 666**	**147 636**	**139 106**	**125 365**	**119 212**	**9.5%**	**14 030**

CURRENT AND SAVING ACCOUNTS

PKO Bank Polski SA is the market leader in terms of the number of current accounts, which at 31 December 2016 amounted to 6.9 million.

The present level of accounts is derived from the varied offer in terms of customer preferences, which can be distinguished among others: 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+'. Using an account is free of charge. In 2016, 17.5 thousand of this type of accounts were opened.



What is more bank extended 'PKO Konto dla Młodych' offer. As for now not only students and graduates aged between 18 and 26 can participate in the offer but everyone in specified age group.

Small and medium enterprises interested in complex, modern and price attractive PKO Bank Polski SA services are offered with two packages:

- PKO Corporate Account for individuals running one-man business, freelancers and professional farmer who appreciate support of their finances with modern banking services, as well as with individual advisor in bank branch,
- PKO Business Account was created for enterprises with larger requirements which needs offer perfectly suited to their needs and appreciate the cooperation with individual bank advisor. Bank offers to PKO Business Account owners access to advanced online banking iPKO business, all *cash-management* services, low transaction costs realized via Internet 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.

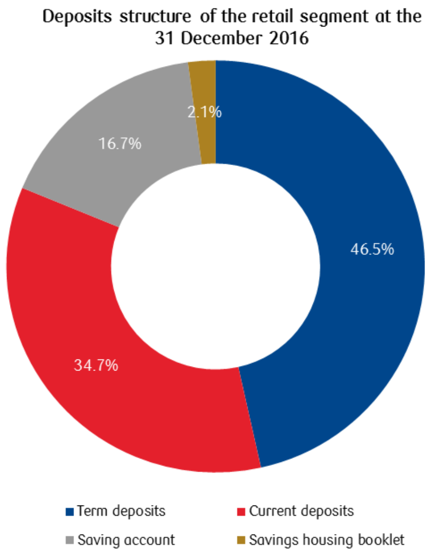
Account maintenance fees depend on customer activity and cash flow.

TERM DEPOSITS AND REGULAR SAVING PRODUCTS

The dominant share of deposits in the retail market are deposits of retail and private banking. Customers in this segment allocated their resources primarily in term deposits. In the first half of 2016, the Bank offered to individual customers, among others, deposits with progressive interest rate and standard and structured deposits.

The most popular term deposits among customers in e Bank's retail and private banking offer in 2016 were:

- 24M term deposits with negotiated interest rates,
- 6M internet deposit available in the electronic banking system,
- term deposit account 3+3 for new funds, deposit 3+3 with negotiated interest rate,
- 1M special term deposits available via online transaction services iPKO and Inteligo.



The Bank's offer dedicated to individual customers also includes structured instruments. In 2016 the Bank has conducted 24 subscriptions of structured deposits, including deposits based on:

- USD/PLN exchange rate (9- and 15-month with guaranteed 1% interest rate and 36-month with guaranteed 2.25% interest rate)
- EUR/PLN exchange rate (9-month, 15-month and 15-month with 1% guaranteed interest rate and 36-month with guaranteed 2.25% interest rate).

The attractiveness of offered products provide achieved results: structured deposit based on basket of shares of new technology companies, which PKO Bank Polski SA offered to customers in 2014, at the end of investment period, which fell on 30 May 2016 brought to investors 10% profit for the wholes investment period, which is c.a. 5% annually.

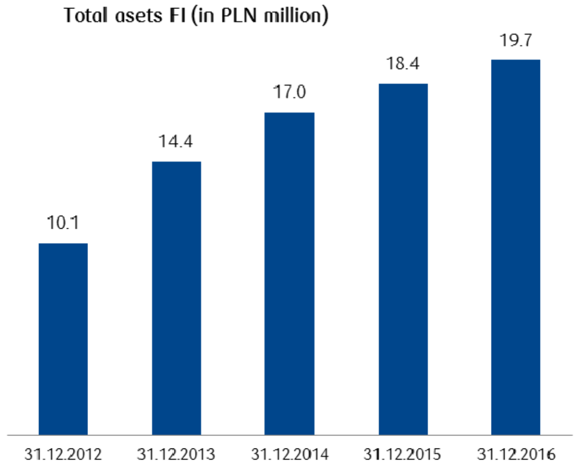
Bank extended its product range of term deposit to encourage customers to regular savings by:

- introducing to the offer a term deposit 'Kapitał na Własny Kąt' as a product which is designed for customers, who are planning to take out a mortgage in the future, the possibility of regular saving for their own contribution,
- introducing to the offer a term deposit 'Kapitał dla Dziecka' addressed to customers receiving 'Rodzina 500+' programme benefits as well as those not covered by the programme, who want to build financial security of their children from earliest years.

INVESTMENT FUNDS

As a result of cooperation with PKO Towarzystwo Funduszy Inwestycyjnych SA (TFI) customers of retail and private banking are offered 40 non dedicated funds, with total assets of PLN 19 billion[11].

PKO Bank Polski SA constantly extends offer in the area of investment funds. In 2016, PKO Bank Polski SA carried out, among other things, an issue of investment certificates of Fundusze Inwestycyjne Zamknięte PKO Globalnej Strategii, PKO Absolutnej Stopy Zwrotu Europa Wschód – Zachód, PKO Strategii Obligacyjnych closed-end investment funds.



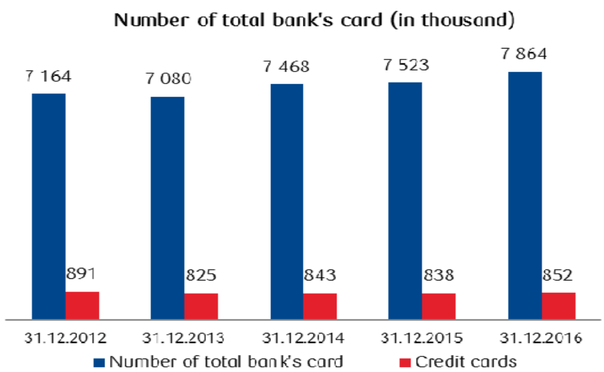
SALES OF STATE TREASURY BONDS

PKO Bank Polski SA possess exclusive rights 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 expansive sales network of PKO Bank Polski SA, which is a great convenience for all persons who wish to invest in bonds. In 2016, almost 46 million of bonds were sold (in 2015, the sale of bonds reached 32 million bonds).

OTHER PRODUCTS AND SERVICES IN THE RETAIL SEGMENT

BANKING CARDS

As at 31 December 2016 the number of PKO Bank Polski SA bank cards amounted to approx. 7.9 million, including 0.9 million credit cards.



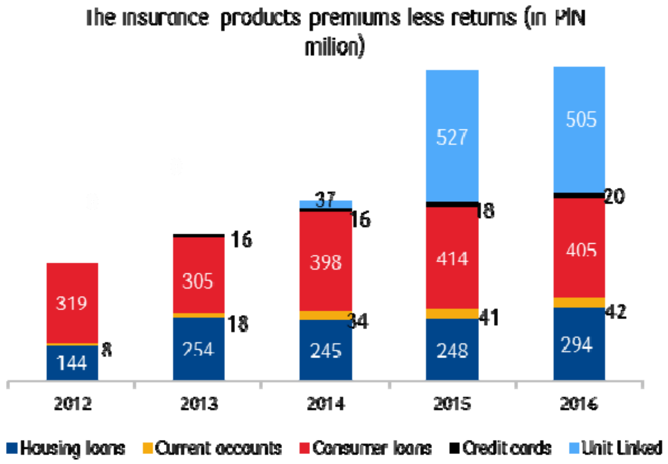
Activities performed in 2016, as part of the card business:

- in the first half of the year, the consortium comprising PKO Bank Polski SA and eService won a tender for handling payment cards in Postal facilities, as a result of which nearly 8 thousand ATMs were installed in the Poczta Polska network, and customers of over 4.6 thousand Postal facilities can pay by card for services such as: paying bills or sending parcels,
- introduced the possibility to order a credit card through the Contact Center and iPKO online banking,
- reduced sales process of credit cards called 'one-click' has been implemented,
- the offer included Przejrzysta (Transparent) credit card endorsed by MasterCard, to supplement the existing bank offer comprising the Przejrzysta credit card endorsed by Visa,
- implemented free of chargé 3D-Secure service, due to payments realized in online shops marked with 'MasterCard Secure Cod' or 'Verified by VISA' are additionally secured by single use code,
- the possibility of ordering in the online service a 'multi-currency' debit card for currency accounts with the VISA brand, which can be attached to all currency accounts held by the customer,
- a promotion of Diners Club cards was addressed to small- and middle-sized enterprises, which involved reducing the annual fee for a newly issued PKO Standard Diners Club card to PLN 0 in the first year and for PKO Executive Diners Club card to PLN 120 in the first year.

[11] Source: Report of the Chamber of Fund and Asset Managers as at 31 December 2016

INSURANCE PRODUCTS

PKO Bank Polski SA 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 due to accident. PKO Bank Polski SA offers insurance products to retail and private banking as well as to the small and medium enterprises segment connected with products such as:



- consumer and mortgage loans (Life and unemployment insurance, Real property insurance, Movables insurance, Third-party liability (OC) insurance, Assistance insurance, Low contribution insurance and Bridge insurance, as well as SME advance repayment insurance),
- current accounts (ROR) (i.a. life and accident insurance, property insurance, civil liability insurance, assistance insurance),
- bank cards (i.a. security package to credit cards, Travel insurance, Loan repayment insurance).

PKO Bank Polski SA concentrates on cooperation with PKO Życie Towarzystwo Ubezpieczeń SA and PKO Towarzystwo Ubezpieczeń SA, thus maximizing the value for the customer and other stakeholders.

In 2016, Bank's offer has been enriched with new insurance products:

- loss of income source or hospital treatment due to accident insurance for credit card holders,
- other retail insurance:
  - loss of income insurance for 'Pożyczka Gotówkowa',
  - property insurance for loans or mortgages loans,
  - loss of income 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
  - Endowment insurance: 'Bezpieczny Kapitał +' ('Safe Capital +').
- uniform security to the Cash Advance addressed to customers in the Base Customer and Private Banking segments,

PRIVATE BANKING

PKO Bank Polski SA was consistently developing Private Banking segment, focusing on close cooperation within the Group, allowing customers access to a wide range of products and financial instruments. During the period under analysis eight closed-end investment funds issues were offered to Private Banking customers – four issues of PKO Corporate bonds and two each issues: PKO Eastern-Western Europe and PKO Global Macroeconomic. Customers participated as well in issue of corporate bonds of: Best SA, Ghelamco SA and Kruk SA.

The team that provides services to the most affluent customers consists of 62 counselors and 29 business analysts. Private Banking offices are located in 9 major cities in Poland: Warsaw, Gdansk, Krakow, Katowice, Poznan, Wroclaw, Lodz, Szczecin and Bydgoszcz (institution was launched as a part of the Private Banking Office in Gdansk).

Private Banking Center of PKO Bank Polski SA manages assets portfolio worth PLN 15.8 billion.

DISTRIBUTION NETWORK AND ACCESS CHANNELS

As at 31 December 2016, the retail branch network of PKO Bank Polski SA consisted of 1 179 branches grouped in 11 regional divisions and 8 retail banking offices. Compared with the end of 2015 the total number of retail branches decreased by 40. The development of the multi-channel distribution model has a considerable impact on the optimization of the branch sales network. The optimization of fixed branches is carried out continuously, and the final decisions on leaving a given facility on a particular micro-market are made based on the economic rationale for its operations, taking into account the development potential of that micro-market. This optimization is of a multi-faceted character, which comprises activities such as changing the character of facilities or reducing their number.

The process of reducing large branches is accompanied by the universalization of smaller branches and transformation of small branches into agencies in justified cases.

Table 14. Operating data of the retail segment

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015	Change 2016-2015
Number of branches in the retail segment:	1 198	1 238	1 280	1 147	1 134	-3.2%	-40
retail branches	1 179	1 219	1 261	1 130	1 120	-3.3%	-40
regional retail branches	11	11	11	11	11	0.0%	0
private banking branches	8	8	8	6	3	0.0%	0
Number of ATMs	3 206	3 196	3 065	2 992	2 803	0.3%	10
Number of agencies	837	881	1 001	1 074	1 208	-5.0%	-44

Branch network and agencies

The Bank is constantly improving conditions for customers in the branch network. In 2016 these activities focused on the modernization of branches and moving them to the new attractive locations. 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 optimal 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.

Essential complement to the network of branches and ATMs is a network of agencies. As at 31 December 2016 PKO Bank Polski SA collaborated with 837 agencies and in comparison to 31 December 2015 the number of agencies has decreased by 44 units. 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. In addition to small and medium-sized enterprises there is a possibility of using electronic banking services under the name iPKO business. These services provide customers with access to information about their accounts and products, as well as allows them to make transactions through: Internet, self-service terminals, telephone.

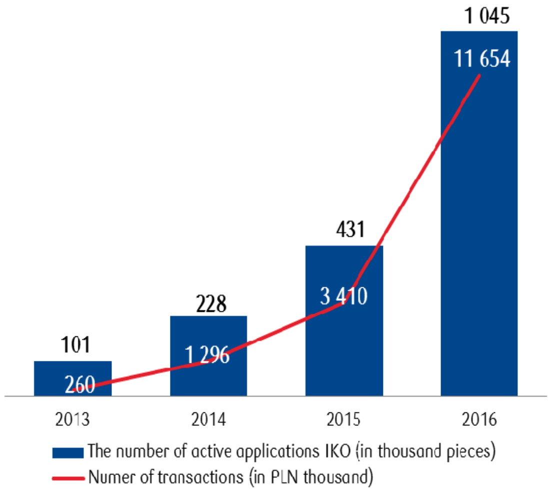
Bank systematically promotes the remote use of the Internet account, separate account management and banking products in the transaction service, which allows customers faster and easier access to their products, as well as lowering the cost of using banking services. One of the campaign popularizing modern banking channels was conducted in the first quarter of 2016 to promote 'Replace scratch card for 10 PLN', which the aim was encouraging customers to use other authorization tools than the transaction authentication codes, such as SMS or token.
PKO Bank Polski SA was the first bank to become involved in the government programme 'Rodzina 500+'. The relevant agreement was signed between the Ministry of Family, Labor and Social Policy and PKO Bank Polski SA. As a result, the Bank's customers with access to the Internet service both iPKO and Inteligo can apply for the benefit of programme 'Rodzina 500+' electronically.

The participation of PKO Bank Polski SA in the programme 'Rodzina 500+' is just one of the signs of the Bank's involvement in the construction of e-state. Thanks to an agreement signed with the Social Insurance Institution, through which the Bank's customers from 13 May 2016 are able to set up a profile on Electronic Services Platform (ESP) of Social Insurance Institution from banking services level or online via iPKO or Inteligo.

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.

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 IKO activations has exceeded one million. 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. 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 31 December 2016 the network of acceptance of mobile payments (IKO, BLIK) included more than 175 thousand devices (eService terminals and First Data) throughout the country. W In connection with the implementation of the BLIK system, IKO application now enables cash withdrawal from more than 15.5 thousand of PKO Bank Polski SA ATMs and Bank Millennium SA, Bank Zachodni WBK SA, ING Bank Śląski SA, Euronet ATMs (about 6 thousand) and IT Card (about 1.8 thousand). At the end of June 2016 PKO Bank Polski gave new option to customers in 'Płace z iPKO' method – transaction authorization through entering BLIK code generated in IKP application. Thanks to implemented method payments can be performed in most of online shops in Poland, including the biggest integrator PayU. Change appeared as well in the biggest Polish e-commerce bidding platform – Allegro.
What is more Bank allowed its youngest customers – under 13, using PKO Konto Dziecka and PKO Junior transaction service, access to 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.

THE PKO BANK POLSKI SA CONTACT CENTER

Contact Center 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.

The tasks of the Contact Center are in particular:

- sale of banking products during incoming and outgoing calls,
- supporting remote sales 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 via customers infosite and iPKO service,
- internal customer service (professional helpdesk for branch employees),
- early monitoring of receivables.

Apart from that, the Contact Center actively participates in many new processes, such as a project aimed at increasing the safety of transactions ordered by the Bank customers, which directs potentially suspicious transfers for additional verification with the customer.

6.1.2 CORPORATE AND INVESTMENT SEGMENT

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

In 2016 PKO Bank Polski SA as in previous years based the development of corporate business on building stable relationships with customers through high quality services, cooperation based on partnership and specialized competence of the sales network. Current business financing (through working capital loans), as well as openness to participation in the implementation of their future projects (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.

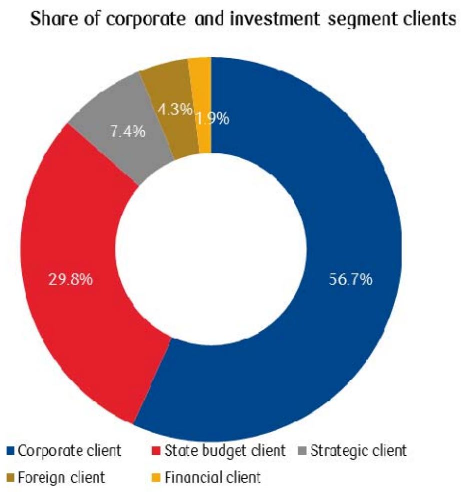
The Bank analyzed market expectations systematically and, in order to meet customer expectations, tailored its current product and service offer so as to cope with increasing competitive pressure. As a result, a broad range of transaction products and products mitigating financial risks (liquidity, settlement, interest rate, currency and commodity price risks) were being developed consistently, and financing structure needs were addressed in a flexible manner.

A parallel international trade financing offer has been 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

At the end of December 2016, the Corporate and Investment segment provided services to nearly 15 thousand customers, including 1.1 thousand strategic customers, over 0.6 thousand foreign customers, and over 4.3 thousand self-government and central government units together with budget-related and associated entities. In 2016, the number of customers served in this segment increased by 0.4 thousand.

In 2016 the Bank strengthened its position as an undisputed leader in providing services for local governments, by participating in local projects with custom character and by winning a tender for providing services to the Podkarpackie Voivodeship. In total, the Bank provides services for 6 from 16 voivodeships in Poland.



LENDING ACTIVITY AND STRUCTURED FINANCING

As at 31 December 2016 gross corporate loans amounted to PLN 52 billion and from the beginning of the year, the balance went up by PLN 5 billion, total financing provided to corporate customers including bonds issued amounted to over PLN 65 billion and in the year increased by almost PLN 6 billion (i.e. by 9.3%).

Table 15. Financing of corporate customer (in PLN million)

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015	Change (in PLN milion)
Corporate loans gross	52 158	46 774	46 257	38 947	39 273	11.5%	5 384
Debt securities*	13 318	13 132	13 064	6 292	6 330	1.4%	186
municipal	7 148	7 309	7 303	4 419	3 955	-2.2%	-161
corporate	6 171	5 823	5 761	1 873	2 375	6.0%	347
Financing total	**65 476**	**59 906**	**59 321**	**45 238**	**45 603**	**9.3%**	**5 570**

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

In 2016 in the corporate and investment segment new loan products were launched that allow customers adjusting their *pre-approved* credit limits to their working capital and investment financing needs in the certain moment and specialized loan and treasury products for agricultural industry reducing market risk.

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.

PKO Bank Polski SA is a strategic partner in investment projects of corporate customers and local self-government units not only by supplying appropriate financing and flexible repayment terms, but also by making it possible to conclude transactions to hedge financial risk. In 2016, the Bank signed:

- 17 loan agreements in a banking consortium for a total of over PLN 12 billion, where the Bank's share amounted to nearly PLN 4 billion,
- 1 investment loan agreement for an entity not related to the Bank for the amount of PLN 0.6 billion and 1 loan promise for the amount of PLN 3.2 billion,
- 3 agreements on bond issues for a total of over PLN 29 million and 1 corporate bond issue in the form of bank consortium for a total of PLN 1.1 billion in which the Bank's share amounted to approx. PLN 90 million,

- 178 municipal bond issues and annexes extending the period of previously concluded issue agreements totalling PLN 1.2 billion;
- 3 bond issue agreements without guarantee of closing the issue, totalling nearly PLN 5 billion.

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.

DEPOSIT ACTIVITIES AND TRANSACTION BANKING

The level of deposits at the end of 2016 amounted to PLN 38 billion and decreased by PLN 4.9 billion as compared to the end of the last year. This resulted from the liquidity policy followed by the Bank and obtaining long-term financing from the wholesale market.

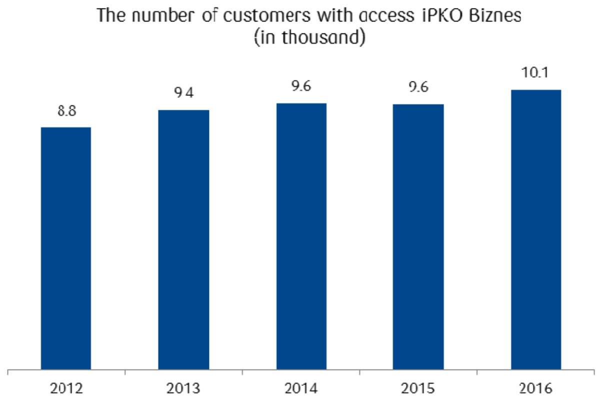
Table 16. Corporate deposits (in PLN million)

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015	Change (in PLN milion)
Corporate deposits	38 025	42 908	30 907	21 336	23 968	-11.4%	-4 883

PKO Bank Polski SA is constantly enhancing the quality of its transaction banking services, which is proved, among other things, by an increase in the number of customers who use iPKO Business.

In 2016 the Bank developed services dedicated to entities characterized by extensive organizational structure (e.g. capital groups), allowing customers to use various kinds of products and services to facilitate settlement of transactions with domestic and foreign partners.

In case of electronic services provided by PKO Bank Polski SA for customers, the leading product for corporate banking is the iPKO Business banking system. In 2016, the iPKO Business 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 Business application allows customers to monitor and manage accounts, payment cards and loans and to submit orders for all kinds of transfers.



In 2016, the Bank enhanced its offer for corporate customers with complex organizational structures by developing dedicated products based on '*cash pooling*' arrangements. In particular, in connection with the operations of a bank in Germany and the launch of a branch in the Czech Republic planned for the first half of 2017, it was possible to use this tool to manage financial resources in a cross-border context.

FINANCIAL INSTITUTIONS

Currently PKO Bank Polski SA holds a leading position in the field of foreign banking in Poland. It has a broad and efficient network of nostro accounts in banks around the world, has more than 1 400 SWIFT established relationships with banks in different countries and in different markets. The Bank provides approx. 200 loro accounts for foreign banks, which are utilized to settle transactions of banks, both in Poland and in other markets.
The Bank actively cooperates with market participants supporting their customers' activities on foreign markets and extends the range of currencies available to the Bank's customers, for example, by including the NZD (New Zealand Dollar) in the Bank's offer.
Such actions are focused on implementing optimum methods of foreign settlements realization, introducing new solutions in international banking and seeking new appealing markets (f.e. Persian Bay, South-East Asia, South Africa).

INTERNATIONAL BANKING

PKO Bank Polski SA participates actively in the development of the international expansion of its customers, offering them support in foreign markets. International activities of the Bank take place on various levels. Initiatives are taken to facilitate financial support for Polish companies operating on the international markets. One of them was the opening of a corporate branch in Federal Republic of Germany. The branch offers 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.

Another Bank branch abroad will be a facility in the Czech Republic operating under the name PKO Bank Polski, Czech Branch. Launch of that branch is scheduled for the first half of 2017. The activities of the branch will focus on servicing corporate customers, i.e. it will be analogous to the operations of the Bank branch in Federal Republic in Germany.

The launch of a Bank branch in the Czech Republic is an element of the international expansion strategy of the Bank according to which it will follow its customers. 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.

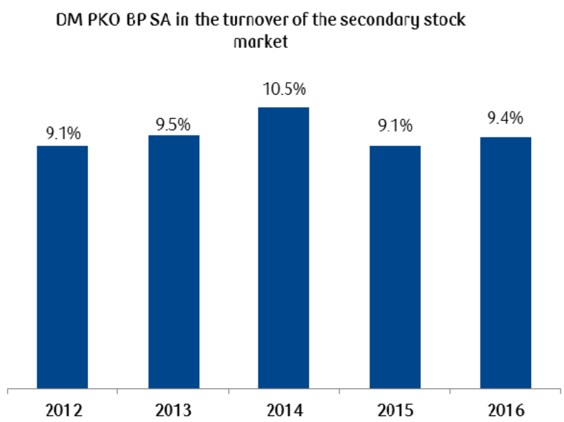
For the entities operating in the territory of Ukraine banking services are being provided via KREDOBANK SA which is a part of the PKO Bank Polski SA Group.

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 appointed, which favors 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, Brokerage House, the Office) is the leader on the brokerage services market not only with regard to the share in turnover on the secondary market, but also the organization of issues on the primary market.

At the end of 2016 BH provided 157.4 thousand securities accounts and cash accounts and had 170.4 thousand active accounts in the registry. BH, in terms of securities accounts, ranks in the fourth position among 38 participants in the market.



In 2016, the value of the Office turnover on the secondary market of shares exceeded PLN 39 billion, which accounted for nearly 10% of the market and allowed to be classified in second place. The Brokerage House plays the role of an agent for the issue of retail bonds and actively participates in the turnover in bonds on the Warsaw Securities Exchange, has nearly half of the share in turnover and for many years has been ranked first among the market participants.

The Brokerage House is also an active participant of the NewConnect market. The value of realized turnover of nearly PLN 250 million gives the Office fourth place on the market and third place in terms of the number of animated companies (48).

The most important transactions in which BH intermediated on the capital market, include, among other things:
- stock sales of Alior Bank SA - value of papers issued amounted to PLN 2.2 billion,
- private offering of shares of Kruk SA – the transaction value exceeded PLN 200 million, and co-arrangement of the issue of corporate bonds of KRUK SA – two issue programmes with a total value of PLN 800 million,
- participation in the sale of the bonds of Ghelamco Invest Sp. z o.o. where the total value of sales of all series amounted to PLN 155 million,
- service of call to sell of Rovese SA shares announced by FTF Galleon SA,
- entity intermediating in the call for the sale of shares in Asseco Central Europe a.s. Announced by Asseco Poland SA – the value of the transaction amounted to nearly PLN 30 million,

In 2016, the Brokerage House introduced the possibility of concluding and settling transactions on foreign markets in foreign currencies. Apart from settlements in PLN, it is possible to settle transactions in: EUR, CHF, GBP, USD NOK, HUF, SEK, CZK, and DKK.

TREASURY PRODUCTS

The Bank undertakes various efforts aimed at improving the product offer and focuses on the development of cutting edge distribution channels.
In the prior year, following the modification of its transactional platform, the Bank provided its customers with several new functionalities, including, among other things, the possibility of signing remotely financial market cooperation agreements.
Foreign exchange SPOT transactions have the largest share in sales of treasury products. In 2016 the number of such transactions increased by approx. 10% and turnover by approx. 5%. It is also worth noting an increase in the result of the sale of interest rate derivatives. In 2016, the realized result was approx. 60% higher.

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 2017 the Bank took third place and second place in the contest for the Money Market Dealer.
Funds not allocated to the lending activities are invested by the Bank on the Treasury securities market. The function of portfolio is related to the current liquidity management of the Bank and the function of the investment portfolio.

FIDUCIARY SERVICES

The Bank maintains security accounts and facilitates domestic and foreign market transactions, provides fiduciary services and acts as a depositee for pension and investment funds. As at the end of 2016 assets held by the customers on fiduciary accounts maintained by the Bank amounted to PLN 68.8 billion and was higher by circa 5% as compared to the value noted as at the end of 2015 The amount of security accounts maintained amounted to 2.0 thousand of unique accounts.
In 2016, the Bank started the project of implementing '*indirect clearing*' services which involve intermediation in the settlement of derivative transactions – subject to the EMiR regulations – for the Bank's customers.

SALES NETWORK

The sales network of the corporate segment includes 32 Regional Corporate Centers concentrated in seven Corporate Macroregions and Branch in Federal Republic of Germany, which serves corporate customers of PKO Bank Polski SA in Germany.

In 2016, the Bank continued to implement a strategic programme for the development of corporate sales successfully based on modern mechanisms of planning the development of customer relations, cooperation in the designing of strategies and financial support.

Table 17. Operating data of the corporate segment

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015	Change 2016-2015
Number of branches in the corporate segment:	**40**	**40**	**39**	**39**	**64**	**0.0%**	**0**
regional corporate branches	7	7	7	7	13	0.0%	0
corporate centres	32	32	32	32	51	0.0%	0
branch of PKO Bank Polski SA in Germany	1	1	x	x	x	0.0%	0

6.2 MARKET POSITION OF PKO BANK POLSKI SA GROUP

In 2016, the Bank maintained its leading position in terms of the share in the loan market and in the deposit market. Also in particular sectors of the financial services market the Group companies hold the lead and key positions.

Table 18. Market share

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change 2016/2015
Loans for:*	**17.8%**	**17.9%**	**17.9%**	**16.1%**	**16.1%**	**-0.1 p.p.**
private individuals, of which:	22.8%	22.9%	22.9%	19.1%	19.0%	-0.1 p.p.
housing	25.7%	25.5%	25.8%	20.6%	20.0%	0.2 p.p.
PLN	28.6%	28.7%	29.6%	28.4%	28.6%	-0.1 p.p.
foreign curency	21.4%	21.5%	21.5%	12.8%	12.9%	-0.1 p.p.
consumptional and other	15.8%	16.1%	15.6%	15.4%	16.6%	-0.3 p.p.
institutional entities	12.9%	13.0%	13.1%	13.1%	13.2%	-0.1 p.p.
Deposits for:	**17.3%**	**17.9%**	**17.3%**	**16.3%**	**16.8%**	**-0.6 p.p.**
private individuals	20.7%	20.7%	21.7%	21.7%	21.8%	0 p.p.
institutional entities	12.4%	14.0%	11.5%	9.4%	10.2%	-1.6 p.p.
Lease	**7.5%**	**6.1%**	**6.4%**	**7.2%**	**6.6%**	**1.4 p.p.**
TFI assets	**7.6%**	**7.3%**	**8.1%**	**7.6%**	**6.9%**	**0.3 p.p.**
Non-Treasury debt securities (indebtedness)	**29.1%**	**28.8%**	**31.5%**	**20.1%**	**23.4%**	**0.3 p.p.**
Brokerage activities						
trading in the secondary market	9.4%	9.1%	10.5%	9.5%	9.1%	0.3 p.p.

Source: NBP, GWP, Związek Polskiego Leasingu
* Data according to Webis, the National Bank of Poland's reporting system. Market shares were updated in Q3 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 under "Other receivables" classified as consumer loans, are now presented under "Housing loans to households".

6.3 INTERNATIONAL COOPERATION

In the PKO Bank Polski SA Group, funds to cover the needs arising from the development of business operations, including the financing of projects relating to the small and medium enterprises segment, are also raised via international cooperation.

The Group raises funds on foreign financial markets, i.a. through loans from international financial institutions (i.a. the Council of Europe Development Bank and the European Investment Bank).
In 2016, PKO Leasing SA used the funds from loans from the Council of Europe Development Bank (CEB) and from the European Investment Bank (EIB) to finance the development of small and medium enterprises. Loan agreements were signed totalling EUR 40 million, and the value of the funds launched in 2016 (also the agreements in 2015) amounted to PLN 132 million and EUR 75 million. In 2016 RLPL signed two loan agreements with international institutions – the European Bank for Restructuring and Development (EBRD) and the International Finance Corporation (IFC) which are part of the World Bank Group. The agreement with EBRD was concluded for PLN 255 million, and the credit limit with IFC amounted to USD 75 million. Under the above financing facilities, in 2016 loans were launched of PLN 170 million in respect of EBRD and EUR 65.7 million in respect of IFC.

As at the end of 2016 total financing of the Bank in the form of loans received from financial institutions amounted to approx. PLN 22.4 billion and included funds denominated in PLN, EUR, CHF and USD.

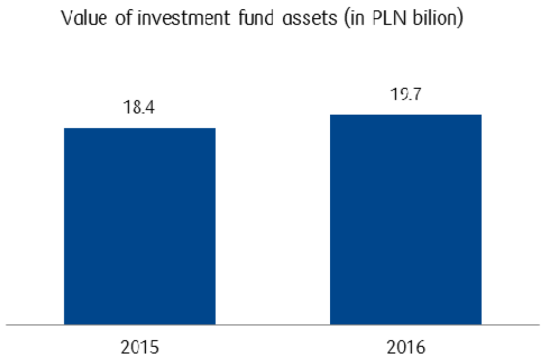
PKO Bank Polski SA participates in The 2020 European Fund for Energy, Climate Change and Infrastructure (the 'Marguerite Fund') project, capital involvement in the above mentioned fund in 2016 amounted to EUR 54.6 million. PKO Bank Polski SA takes part in the above mentioned project as the only Bank operating in one of the new European Union members which was awarded the status of 'Core sponsor'. The 'Marguerite Fund' was established in 2009 for 20 years and currently implements investment projects such as green-field and brown-field in the energy and the road sector in Poland and other European Union countries.

6.4 ACTIVITIES OF OTHER ENTITIES OF THE PKO BANK POLSKI SA GROUP[12]

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

GENERAL INFORMATION ON THE SELECTED PKO BANK POLSKI SA GROUP ENTITIES

PKO TOWARZYSTWO FUNDUSZY INWESTYCYJNYCH SA

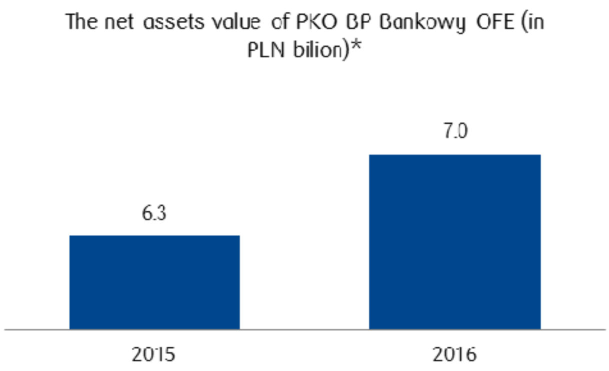


In 2016 Company generated a net profit in amount of PLN 59.8 million (in 2015 net profit amounted to PLN 56.5 million).
The value of fund assets under management of the Company as the end of 2016 amounted to PLN 19.7 billion which represents an 6.8% increase in the value of assets compared to the end of 2015. The increase in the value of assets was mainly associated with the significant net profit from sales and the result from assets management.
PKO Towarzystwo Funduszy Inwestycyjnych SA ranks 3rd in terms of the net assets value with a 7.6% share in the investment funds market and the first place with a 14.4% share in managed assets of non dedicated funds*.

As of 31 December 2016, the Company was managing 42 investment funds and subfunds.
In 2016 the Company's offer was expanded by two investment funds: PKO Absolutnej Stopy Zwrotu Europa Wschód - Zachód – a closed end investment fund, and Subfundusz PKO Medycyny i Demografii Globalny under the umbrella fund Fundusz PKO Parasolowy – open end fund.
In 2016 the Company performed 29 issues of investment certificates of closed end funds, under which it obtained assets with a total gross value of PLN 993.7 million.
In 2016 44 thousand customers acceded the Pension Programme 'Pakiet Emerytalny PKO TFI' which is 56% of all customers of the Programme in the Company's offer since 2012. As at 31 December 2016 PKO Towarzystwo Funduszy Inwestycyjnych SA managed 23 Group Pension Funds. Additionally, in 2016 the Company participated in over a dozen tenders relating to Group Pension Programmes which will be resolved in 2017.
* *Source: The Chamber of Fund and Asset Managers (Izba Zarządzających Funduszami i Aktywami).*

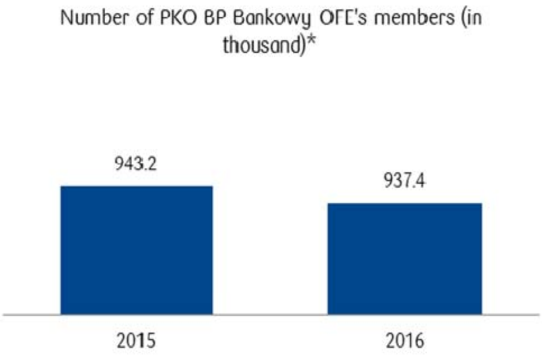
PKO BP BANKOWY PTE SA

Company in 2016 induced net profit amounting to PLN 5.2 million (vs PLN 7.9 million in 2015).



Results of the Open Pension Fund (OFE)*:
As at the end of December 2016 the net asset value of PKO BP Bankowy OFE managed by PKO BP BANKOWY PTE SA amounted to PLN 7.0 billion, which is an increase of 10.6 % compared with the end of 2015. The increase in the net asset value was related mainly to the rate of return on Fund's assets.
As at the end of December 2016 PKO BP Bankowy OFE had over 937 thousand members. PKO BP Bankowy OFE ranks 8th on the pension fund market in terms of OFE net asset value and 9th in terms of the number of OFE members.

[12] 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.



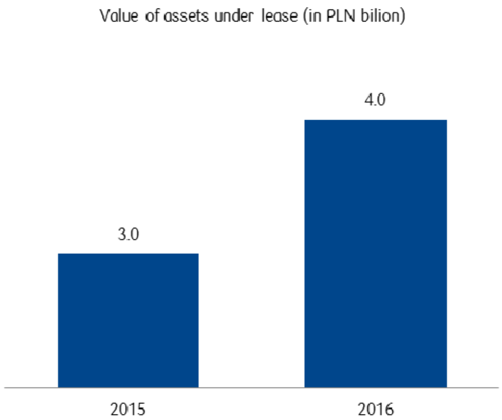
In 2016 the Polish Financial Supervision Authority announced the rates of return of OFE as at the end of March and September, for a period of 36 months. In accordance with the PFSA announcement PKO BP Bankowy OFE earned a rate of return of 9.074% from 29 March 2013 to 31 March 2016 compared with the weighted average rate of return for all funds of 6.344%, ranking first among the pension funds operating on the market. In the second listing which accounted for the period from 30 September 2013 to 30 September 2016 the Fund earned a rate of return of 3.073% with the weighted average for all funds at 0.133%, coming second in the ranking of open pension funds.

* Source: www.knf.gov.pl

PKO Leasing SA Group

On 1 December 2016 PKO Leasing SA acquired Raiffeisen-Leasing Polska SA. As a result of this transaction the PKO Leasing SA Group was expanded by the said company and the companies under the control of Raiffeisen-Leasing Polska SA, in accordance with IFRS, i.e. Raiffeisen-Leasing Real Estate Sp. z o.o., 'Raiffeisen Insurance Agency' Sp. z o.o., Raiffeisen-Leasing Service Sp. z o.o. and ROOF Poland Leasing 2014 DAC.

In 2016, the PKO Leasing SA Group (i.e. PKO Leasing SA and its subsidiaries) earned a net profit of PLN 19.9 million. This result also includes the financial result of the Raiffeisen-Leasing Polska SA Group earned in December 2016.



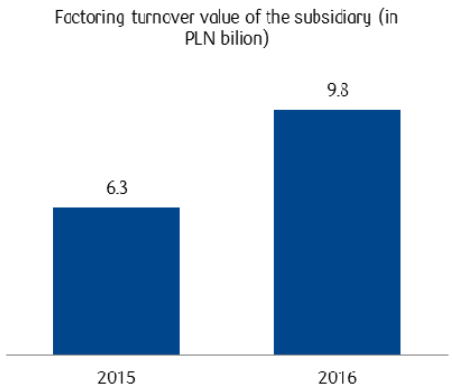
Leasing activities:

At the end of 2016 the total carrying amount of the lease investments of the PKO Leasing SA Group entities amounted to PLN 11.4 billion, including of the Raiffeisen-Leasing Polska SA Group – PLN 5.3 billion.

In 2016 the PKO Leasing SA Group (net of the Raiffeisen-Leasing Polska SA Group companies) transferred leased assets totalling PLN 4.0 billion for use, i.e. 32% more than in 2015. This increase is the result of organic development and using the sales network of PKO Bank Polski SA.

In 2016 the Raiffeisen-Leasing Polska Group companies launched leased assets and loan agreements totalling PLN 3.7 billion for use, including in December 2016 – with a value of PLN 0.37 billion.

In terms of the value of assets leased the PKO Leasing SA Group (without Raiffeisen-Leasing Polska SA Group) at the end of June 2016 ranked 4th position with a leasing services market share of 6.9%, and the Raiffeisen-Leasing Polska SA Group ranked 6th position on the lease services market, with a 6.4% share in the market*, giving a total market leadership.



Factoring activity:

In 2016 the company has been providing domestic and export factoring services with both takeover of the risk and no risk taken, reverse factoring and factoring programme service for counterparties.

In 2016 the value of factoring turnover amounted to PLN 9.8 billion (in 2015 the value of factoring turnover amounted to PLN 6.3 billion); at the end of 2016 the number of customers amounted to 355.

PKO Faktoring SA as at 31 December 2016 ranked 9 place among factoring companies associated in the Polish Factors' Association with a market share of 6.2%.

** Source: Company's calculations and Polish Leasing Association data*

PKO Życie Towarzystwo Ubezpieczeń SA Group

In 2016, the PKO Życie Towarzystwo Ubezpieczeń SA Group (i.e. PKO Życie Towarzystwo Ubezpieczeń SA and its subsidiary, Ubezpieczeniowe Usługi Finansowe Sp. z o.o.) generated a net profit of PLN 7.2 million (in 2015, the Group closed the year with a net loss of PLN 9.9 million). The result of 2016 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 members of the Bank's Group.

PKO Życie Towarzystwo Ubezpieczeń SA offers a wide range of insurance products: from protection products to investment 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 assigned contributions from insurance contracts as at 31 December 2016 amounted to PLN 900.6 million.

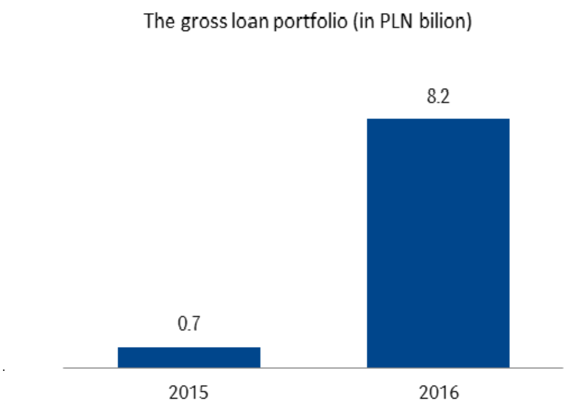
PKO TOWARZYSTWO UBEZPIECZEŃ SA

PKO Towarzystwo Ubezpieczeń SA began their operating activity in January 2016 and closed its first year of operations with a loss of PLN 6.6 million.

The company offers group insurance against loss of income or hospital treatment following a misadventure for the customers of PKO Bank Polski SA, who are holders of credit and individual insurance: cash loan repayment insurance against loss of income or disability following a misadventure for PKO Bank Polski SA borrowers, mortgage payment insurance, mortgage loan insurance in case of loss of income, disability following an misadventure and hospital treatment for customers of PKO Bank Polski SA or PKO Bank Hipoteczny SA and property insurance for customers of PKO Bank Polski SA and PKO Bank Hipoteczny SA who have entered into credit agreements or have loans secured with a mortgage.

The value of gross written premiums from insurance contracts concluded by the company as at 31 December 2016 amounted to PLN 365.7 million.

PKO BANK HIPOTECZNY SA



PKO Bank Hipoteczny SA started its operational activity In April 2015. The principal purpose of the Bank 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.

PKO Bank Hipoteczny SA in 2016 achieved net profit in the amount of PLN 13.2 million.

loans portfolio as at 31 December 2016 amounted to PLN 8.2 billion, ased under the agreement concluded with PKO Bank Polski SA.

On 28 September 2016 Commission de Surveillance du Secteur Financier in Luxembourg approved the Base Prospectus of PKO Bank Hipoteczny SA relating to the programme for issuing mortgage bonds on the European market. Under the programme the Company may conduct issues of mortgage bonds in any currency. The total value of outstanding mortgage bonds issued under the programme cannot exceed EUR 4 billion. The programme stipulates that mortgage bonds issued under it may be quoted in parallel on exchanges in Luxembourg and Warsaw.

In 2016 the Company carried out two issues of covered bonds, including:

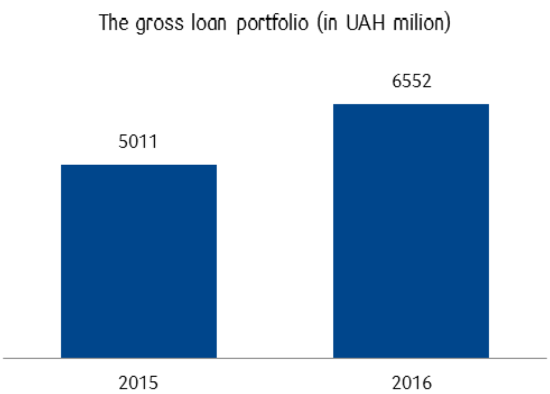
a) two issues denominated in PLN, targeting institutional investors with the total nominal value of PLN 1 billion maturing under the period of 5 years and one day from the issuance date. Interest rate based on variable yield equalled to respectively WIBOR 3M + 0.65 p.p. margin and WIBOR 3M + 0.59 p.p. margin; the bonds are admitted to trading on the Catalyst regulated over-the-counter market maintained by BondSpot SA and the parallel market of the Warsaw Stock Exchange in Warsaw,
b) one foreign issue denominated in EUR, targeting institutional investors with the total nominal value of EUR 500 million maturing under the period of 5 years and 8 months; the fixed interest rate during the term of issue amounts to 0.125%, and the yield at the pricing day was 0.178%; the mortgage bonds were purchased by investors at a price constituting 99.702% of their nominal value and are quoted in parallel on the exchanges in Luxembourg and in Warsaw.

The total value of mortgage bonds issued (at the nominal value) as at the end of 2016 amounted to PLN 3.24 billion.

PKO BP FINAT SP. Z O.O.

PKO BP Finat Sp. z o.o. in 2016 generated net profit in the amount of PLN 45.7 million (in 2015 net profit of the Company was calculated at PLN 16.2 million).
The Company provides complex services for the financial sector firms – such as transfer agent services, bookkeeping for funds and companies. It specializes also in outsourcing of IT specialists, project teams and IT processes. In 2016 the Company started providing group insurance dedicated to products offered by PKO Bank Polski SA.
In February 2016 the Company has been accepted as one the supporting bodies for Chamber of Fund and Asset Management.
In April 2016 the Company successfully passed a supervision audit and kept the Certificate of Registration - Information Security Management System valid, in line with requirements of ISO/IEC 27001:2013.
In September 2016 the Company became a member of the Association of Business Service Leaders in Poland, ABSL, i.e. the organization which associates Shared Service Centers (SSC), Business Process Outsourcing (BPO), Information Technology Outsourcing (ITO), Research&Development (R&D) and companies supporting the development of the business services sector.
In 2016 the Company extended cooperation by five Investment Fund Companies in the area of valuation of open end and closed ended funds, transfer agent and supporting services for closed ended funds. In total, the Company acquired 81 closed ended and open end investment funds to service, signing new Agreements and acquiring an organized part of the enterprise dedicated to valuing investment funds.

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



In 2016 the KREDOBANK SA Group (i.e. KREDOBANK SA and its subsidiary Finansowa Kompania 'Idea Kapitał' Sp. z o.o.) generated net profit of UAH 224 million (PLN 34 million). In 2015 net profit of the KREDOBANK SA Group was UAH 110 million (PLN 19 million). 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 2016 increased by UAH 1 540 million, i.e. by 30.7% and at 31 December 2016 amounted to UAH 6 552 million (loan portfolio gross expressed in PLN at the end of 2016 was equal to PLN 1 010 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 2016 increased by UAH 1 081 million, i.e. by 36.8 % and at 31 December 2016 amounted to UAH 4 020 million (term deposits expressed in PLN as of the end of 2016 amounted to PLN 620 million). Increase of the deposit value is the effect of credibility increase and the position of KREDOBANK SA on the Ukrainian banking market.
As at 31 December 2016 ranch office network of KREDOBANK SA comprised the Central Branch in Lviv and 111 subordinated branches in 22 out of 24 Ukrainian districts. In 2016 location of the 6 subordinated branch was changed, 5 new branches were opened and 4 branches were closed.

QUALIA DEVELOPMENT SP. Z O.O. GROUP

Qualia Development Sp. z o.o. Group (i.e. Qualia Development Sp. z o.o. and its subsidiaries) in 2016 generated net profit in the amount of PLN 30.8 million (the Group closed 2015 with net loss of PLN 22.4 million). The net profit for 2016 is primarily the effect of final completion of the project Royal Park in Warsaw and transferring the apartments to customers, hotel business and selling selected properties and companies.
In 2016 the Group was focused on:
• completion of the final stage of the Royal Park investment implemented at part of the Nowy Wilanów project in Warsaw, obtaining perpetual usufruct and handover of units to customers,
• completion of the fourth stage of the project Neptun Park in Gdańsk,

- selling premises in investment projects accomplished in Warsaw, Międzyzdroje, Sopot and Gdańsk,
- running hospitality business on the basis of completed projects in Gdańsk and Międzyzdroje,
- Continuing the process of selling selected real properties and companies in the Qualia Development Sp. z o.o. Group; real properties located in the area of Żwirki i Wigury Street and Racławicka Street in Warsaw, land properties and a development project in Jurata (transactions were completed in the 3rd quarter of 2016).

6.5 SPONSORSHIP ACTIVITIES REALIZED BY PKO BANK POLSKI SA

Sponsorship of culture and arts Education, Science and Innovation Sports sponsorship Business supporting projects

Sponsorship activities realized by PKO Bank Polski SA are aimed at building the image of the Bank as a reliable financial institution, socially engaged, modern and open to the needs of its customers. By almost century-long history, the Bank is particularly predestined to participate in projects that promote the common good, make closer to the society our heritage, culture, art. The experience and leadership in the financial market obliges also to help young people to face the future challenges and achieving success in the implementation of innovative projects, determining the directions of development of Polish science and entrepreneurship.

In 2016, Bank completed 348 projects of different scale: national - communicated in the media, supported by promotional activities, but also smaller, dedicated to local communities, which is difficult to obtain funds for the organization of meetings with culture, exhibitions, Science Picnics.

The largest share of Bank sponsorship budget is being spent on support of culture and the organization of the sports project, 'PKO biegajmy razem' ('PKO let's jog together').

One of the most important sponsorship projects in 2016 was endorsing the 2016 World Youth Days. The Bank assumed the title of Strategic Sponsor for this exceptional event which attracted 3 million participants from 187 countries.

SPONSORSHIP OF CULTURE AND ARTS

Supporting culture and art is a significant tool for managing corporate social responsibility. It creates the image of the institution and provides operational satisfaction.

The Bank engages in interesting cultural events and supports numerous cultural institutions throughout the country. Activities include establishing sponsorship cooperation, patronage of the exhibition, festivals or support of literary contests. The Bank strives to ensure that the projects pursued have an impact on promoting patriotic attitudes in our society, reinforce ties with our Polish heritage and deepen knowledge about Polish history. Key sponsorship actions in this area:

COOPERATION WITH CULTURAL INSTITUTES

Bank provides support to numerous cultural institution in Poland such as museums, theatres, opera theatres, concert halls. Repertoire events of individual institutions attracts large audience of music lovers and art lovers among local, national and international communities.

- National Museum in Warsaw

  In 2016, the Bank continued patronage of modernized Gallery of Medieval Art, and engaged in preparing a modern application 'Gallery of Medieval Art' with multimedia VR goggles. The application had its premiere at the Polish Pavilion of PAIiZ during the World Youth Days. Additionally, the Bank sponsored the temporary exposition 'Brescia. Renaissance of Northern Italy. Moretto-Savoldo-Moroni, Raphael-Titian-Lotto'.
- The National Museum in Gdańsk

  An exhibition was organized in the National Museum in Gdańsk 'New Gallery of Polish Rulers. Świerzy versus Matejko' which presented a collection of portraits by Professor Waldemar Świerzy, who is sponsored by the Bank. Due to their nature, the collection of 49 portraits is considered to be a practical history lesson, appealing to the imagination of modern recipients, including school youth.
- Collaboration with the National Philharmonic Hall

  Last year the Bank continued cooperation with the National Philharmonic Orchestra, in particular sponsoring the symphonic concert to commemorate the jubilee of Jerzy Maksymiuk, or the Carol Concert.

- National Music Forum in Wrocław

  The National Music Forum in Wrocław is another prestigious institution supported by the Bank. In 2016 NFM hosted all music projects related to the initiative 'Wrocław – European Capital of Culture'.

Opera theatres and philharmonics are also on the list of cultural institutions cooperating with the Bank, such as: the Kraków Opera, Opera Nova in Bydgoszcz, the Podlasie Opera and Philharmonic Theatre – the European Centre of Arts in Białystok, the Centre for the Meeting of Cultures in Lublin, the Raczyńskis Library in Poznań, the Feliks Nowowiejski Warmińsko-Mazurska Philharmonic Theatre in Olsztyn. The sponsored theatres include: the Arnold Szyfman Polish Theatre in Warsaw, the Stefan Jaracz Theatre in Łódź, the Summer Stage of the W. Gombrowicz Theatre in Gdynia, the Musical Theatre in Poznań.

Support organization of music festivals

The Bank actively supports important musical events in the country. Classical music teaches sensitivity, inspires and influences shaping the tastes of Poles. It is also an important part of life, an effective antidote to the noisy everyday life. Bank patronized many festivals with the participation of world-class artists acclaimed by crowds of music lovers. The most important of them include:

- Bydgoszcz Opera Festival - organized since 1994 by Opera Nova in Bydgoszcz,
- Summer Opera Festival Krakow which attracts the audience also to plays performed outdoors,
- the Traveling Festival of the Łódź Philharmonics 'Colours of Poland' – the largest enterprise in Poland connecting high culture with tourism and marketing of particular places,
- the International Festival of the Wieniawski Brothers, organized by the H. Wieniawski Philharmonic Orchestra in Lublin,
- the Music Festival in Łańcut, known for 55 years.

Supporting projects which promote patriotic attitudes

Historical education and forming patriotic attitudes are significant aspects of the Bank's sponsoring activities. In 2016 the Bank engaged in projects related to celebrating the memory of the Cursed Soldiers, the most important of which are: the film Festival NNW 'Niepokorni, Niezłomni, Wyklęci', during which a special show of the documentary sponsored by the Bank 'The Wrocław Battle' was held, the concert 'Honour to the Enduring' – a show celebrating the National Commemoration Day of the Cursed Soldiers, a concert of the Enduring entitled: 'Wilczy ślad' in Warsaw, interactive history lesson about the Cursed Soldiers addressed to senior students, a recording of 50 thousand audiobooks with the novel: 'Klamra-mój ojciec?' commemorating the fate of Major Adam Lazarowicz pseudo. 'Klamra' and support for placing the statue of Danuta Siedzikówna, pseudo. Inka, a nurse in the 5th Vilnius Brigade of the Home Army, in Miłomłyn.

Supporting the organization of film festivals

Since 2011 the Bank has been the patron of projects aimed at consolidating, promoting and popularizing Polish cinema. In 2016 support was continued for the 41st Film Festival in Gdynia, the Gdynia Film Academy, the Film Festival NNW 'Niepokorni, Niezłomni, Wyklęci' and the 34th International Festival for the Young Viewer ALE KINO! organized by the Children's Centre of Arts in Poznań.
The Bank engages in competitions and festivals, promoting new creative talents. In 2016 the Bank for the second time was the sponsor of the event 'FRAZY. Festival of the Word in Songs' ('Festiwal Słowa w piosence FRAZY') organized by the Raczyńskis Library in Poznań, and sponsored the 4th International Theatre Festival of World Classics organized by the Stefan Jaracz theatre in Łódź.

Education, Science and Innovation

Support for science and education is the natural direction of Bank sponsorship, the Bank cooperates with universities and educational institutions across the country. The main projects in this area: valued by students of higher-than-secondary schools Contest on Poland and The Modern World, Polish Academic Championships in Team Programming which qualify students for the Europe and World Championships, Mars Rover RED – constructed by students of the Białystok Technical University.

Projects aimed at building awareness of the huge potential of startups and coaching of the most promising young entrepreneurs, such as Startup Weekend Warsaw and Acceleration Programme MIT Enterprise Forum Poland, which connects the potential of beginning creative entrepreneurs with the infrastructure, experience and resources of large companies, are also important.

Similarly as other large Polish companies, PKO Bank Polski SA is interested in acquiring valuable human resources from among Poles studying in prestigious foreign colleges, in particular British ones. To this end, the Bank engages in initiatives organized by Polish academic and business circles in London: LSE SU Polish Economic Forum and the Poland 2.0 Summit, which present the manner in which innovation and technological progress form the future of startups, business and public policy, with special emphasis on the role of Poland as a player achieving the lead position.

In 2016 the Bank sponsored many educational projects addressed to young students from schools at over-elementary levels throughout Poland. These initiatives promoted creativity, entrepreneurship, mathematical sciences and the economy. The most important of them include: 'My first business before 20', addressed to young students from schools at over-elementary levels in Wrocław and Opole, 'Decius' Ducats' in Kraków, Mathematical Conference for the Young TriMAT in Tricity, Warmia and Masuria Mathematical Competition, Ambassador of School Inventiveness organized by the Patent Office of the Republic of Poland, Colourful University organized by the Adam Mickiewicz University in Poznań, or the Bydgoszcz Science Festival organized by the Kazimierz Wielki University in Bydgoszcz.

SPORTS SPONSORSHIP

IMPLEMENTATION OF THE BANK'S OWN PROGRAMME 'PKO RACE ALONG'

Under the 'PKO race along', which has been organized since 2013, the Bank encourages Poles to common activity. The aim of the programme is to promote the message that running is the best deposit interest rate that a lifetime is expected to generate profits in the form of well-being. Running, especially long distance, shapes the character, developing the condition, it teaches humility and perseverance in the pursuit of the goal. Running can also provide help to the needy, through participation in charity events organized by the Bank during each sponsored runs.

In 2016, the programme held dozens of running events throughout the country, among which the most important were:

- PKO Wroclaw Marathon, Half Marathon PKO Night Wroclaw, PKO Silesia Marathon, PKO Poznan marathon and cross-country series: PKO Rzeszow Runs and PKO Grand Prix of Gdynia. Special attention deserves those commemorating historical events for example Warsaw Triad Race 'Zabiegaj o pamięć', which consists of three runs: Constitution of May 3 Run, the Warsaw Uprising Run and Independence Run,
- PKO Run charity - the second edition of the course organized by the Bank, in 12 Polish cities in the same time. Participants ran for malnourished children,
- SportGeneracja – a project for the youngest whose strategic sponsor is the Bank. Finals of children's eliminations entitled PKO Charity Run of the Young took place during the 2nd PKO Charity Run.

The Bank not only sponsors the largest running events but also enables appropriate preparation for the runs. The Bank once again became the strategic partner in the educational action 'BiegamBoLubię' (I run because I like to). By November free-of-charge running meetings took place in almost 80 athletic stadiums.

The slogan of the events sponsored by the Bank is 'We aid each step'; therefore, by taking part, the participants could join the charity, 'I'm running for...' for people in need of support in saving the life or health. After finishing - a set number of participants - running with pinned card 'I'm running for...' Foundation PKO Bank Polski SA donated money to the designated target.

SPONSORSHIP PARTICIPATION IN OTHER SPORTS INITIATIVES

Besides running events, which definitely dominated in the category of sports sponsorship, the Bank also supported other prestigious sporting events such as:

- Piast Race - already for the 40 time. in Szklarska Poręba - Jakuszyce there was an annual Piast Race - the oldest and most popular ski run in Poland, which was attended by almost 5500 runners; the Piast Race is open to international participants; competitors from 27 countries of Europe and North America took part in it,
- Cavaliada - is a series of International Horse Jumping Contest, enjoying immense popularity among the audience. It is the largest event of its kind in Poland. In 2016, the Bank was the main sponsor of the event, which took place in Poznań, Lublin and the finals in Warsaw; additionally, the event Cavaliada Summer Jumping in Kołobrzeg was organized as part of the horse riding celebration,
- Sea Days in Szczecin – it is one of the largest outdoor events in Poland. Exceptional yachts and sailing boats were moored at the representative pier in Szczecin in 2016. one hundred and twenty five people participated in the event. Szczecin once again was the sailing capital of Poland and Europe.

BUSINESS SUPPORTING PROJECTS

The Bank engages in sponsorship of material events which promote business patriotism, national business and innovativeness in the area of finance.

In 2016 the Bank was the Strategic Partner of the first edition of Congress 590 organized under the slogan: 'We are freeing Polish potential'. The purpose of the Congress was to share the ideas and experiences of representatives of the circles which have an impact on the development of business and entrepreneurship. The Bank also engaged in the new economics congress IMPACT'16, during which global experts pondered over how the Fourth Industrial Revolution may impact the development of the economy, technology and society in Poland.

Due to increasing the digitization of financial services, the threat of cyber-attacks is growing. Ensuring cyberspace security in the financial sector, protecting banks and their customers from losses became the key issue which requires innovative solutions and the use of state-of-the-art technology. Those were the topics of the conferences organized by the Kościuszko Institute: the 1st Polish Cybersecurity Forum in Warsaw and the European Cybersecurity Forum in Kraków. The Bank participated in the Forums not only as a sponsor, but also technically, through the active participation of its experts.

The Bank strongly engages in conferences during which actions to stimulate the security and financial stability of Poland and the European Union are discussed, and in industry conferences and competitions which promote the activity of Polish companies on global markets, the use of new technologies and the presentation of new strategies in industries which may be profitable to the Bank. The examples of such projects include: the 26th Economic Forum in Krynica, Polish Entrepreneur of 2015 of Gazeta Polska Codziennie, Entrepreneur of the Year – organized by EY, Polish Firm – International Champion, or the Congress 'Polish Chemistry'.

The Bank also engaged in initiatives organized by regional chambers of commerce which associate representatives of local business. The Bank's participation in projects which are important for local communities is aimed at integrating various circles, building a platform for sharing experiences, developing entrepreneurship among citizens. The actions taken contribute to reinforcing the Bank's image as an institution engaged in the development of communities and care for the Customers' needs.

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

OBJECTIVES OF THE FOUNDATION

The aim of the PKO Bank Polski Foundation (Foundation) is to deepen customer relationships, understood as the co-financing of projects aimed at building social solidarity. The Foundation sees the common good in building civil society and participates in projects, often initiated by the employees of the Bank - Volunteers, supports, substantively and financially numerous projects of environments and societies that are important for the development of the Poland.

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.

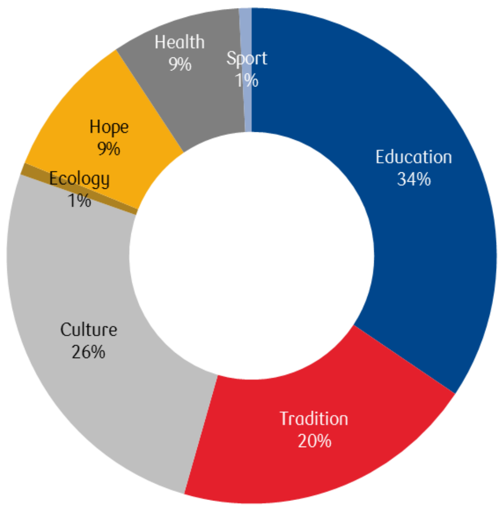
ACTIVITIES OF THE FOUNDATION

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 two affinity cards: 'Good brings profit' ('Dobro procentuje') (since 2013). PKO Bank Polski SA divided profit from each transaction conducted using the charity cards.

During the six years since the start of operation, the Foundation has allocated more than PLN 74.5 million for social activities. Subsidized initiatives are part of one of the seven programme areas: EDUCATION, TRADITION, HOPE, HEALTH, CULTURE, ECOLOGY and SPORT.

In 2016, the implementation of 42 strategic projects, including 5 special strategic projects (which do not require to establish a partnership with an external organization): Banking blood donation, Integrative Meetings with Santa Claus, Banking Collection, Banking and Gift John Weber Collection, the foundation donated PLN 17.8 million. The Foundation makes every effort to ensure that the strategic projects evolve and reach the largest possible number of Beneficiaries. In 2016 the Absolvent – Driver project was launched addressed to handicapped students of college-level schools (Wrocław University of Technology).

Foundation's engagement in the implementation of projects in particular areas as a share of budget



In a partnership at the local level for the implementation of 402 projects the Foundation provided PLN 2.4 million. At local level, a special project, the PKO Charity Run, was conducted for the second time. As in 2015, the project took place in 12 stadiums throughout Poland at the same time.

Individual help, both for children and adults amounted more than PLN 1.5 million. Number of individual beneficiaries amounted to 116, among which 31 persons are employees of PKO Bank Polski SA or their families. Help for 83 individuals was granted by the Charity Action running as part of a special project of the Foundation at the individual level.

The Foundation also mediates in the process of making donation in the form of informatic equipment and furniture withdrawn from use of the branches of PKO Bank Polski SA. In 2016 computers with a total value of PLN 5 350 went to 9 organizations. Furniture worth PLN 99 315 was handed to 59 beneficiaries.

CORPORATE VOLUNTEERING

Since 2013 the Corporate Volunteering system has been functioning in the Bank and 1176 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.

At the same time, the Foundation aims to activate the Foundation Volunteers system and enable involvement in all types of initiatives; in 2016 it organized a country-wide help action among employees, dedicated to children in orphanages. The efforts of the Bank Group's Volunteers enabled packaging and sending the presents collected to 120 children's homes and orphanages. The action was entitled 'Package for Teenagers' ('Paczka dla nastolatka') as a special local project. The involvement of all people in the action proved that the Volunteers' work is a driver of permanent change. Anyone who selflessly takes up new challenges, improves communication and cooperation within the group and gains knowledge about project work. Volunteers reinforce their self-esteem and their attitudes are an inspiration to others.

6.7 PRIZES AND AWARDS GRANTED TO ENTITIES OF THE GROUP

In 2016 PKO Bank Polski SA Group was awarded numerous prizes and awards. We have been recognized for innovative products and services, excellent customer service, management staff of the Bank, excellent financial results and the overall business of the Group.

DYNAMIC DEVELOPMENT AND EXCELLENT FINANCIAL RESULTS

200 GREATEST POLISH FIRMS 2015	PKO Bank Polski SA was awarded in the second edition of the Weekly 'Wprost' ranking of 200 the greatest polish firms. Position in the ranking was determined by sales revenue induced in the previous year. With the revenue amounting to circa PLN 15 billion PKO Bank Polski SA was the 1st amongst banks in the ranking and preserved last year's 8th position in the whole ranking.
50 LARGEST BANKS IN POLAND	PKO Bank Polski SA won, in another consecutive year, the ranking of the Financial Monthly BANK - '50 largest banks in Poland.' The Bank was the best in terms of total assets, which last year amounted to nearly PLN 267 billion. In this year's 21st edition of the ranking the Bank got a prize in the category Consumer Finance. Moreover, Adam Marciniak, the Director of the Development and Maintenance Application Division, was honoured with the title of 'Banking Market Innovator 2015'. The ranking is prepared by independent market analysts based on financial data of banks for the previous year.
STARS OF BANKING 2016	In the second edition of 'Stars of Banking' ranking created by Dziennik Gazeta Prawna PKO Bank Polski SA was awarded with the second place prize for business structure standing out in terms of loans and deposits. In 2015 loans granted to the Bank's customers increased by 6.1 percent, to PLN 190.4 billion, and the value of deposits to PLN 195.8 billion, i.e. by 12.3%. The ranking was evaluating development pace, profitability and efficiency as well and business structure and levels of innovation. Ranking methodology was developed in collaboration with PwC Advisory Poland.
BOOK OF LISTS	According to the Book of Lists 2016/2017 ranking prepared by the 'Warsaw Business Journal' magazine, PKO Bank Polski SA and the Brokerage Office came first in the Book of Lists 2016/2017 ranking. Once again they were best in the following categories: banks in Poland and brokerage houses. The Book of Lists is the largest and most long-lasting ranking on the Polish market which presents the best companies from various business sectors in Poland. Each year it awards the best, largest and most dynamic enterprises.
PEARLS OF THE POLISH ECONOMY	In the fourteenth edition of the ranking of Polish enterprises PKO Bank Polski SA earned the title of Pearl of the Polish Economy in the category 'pearls of the financial sector'. It was awarded for consistent pursuit of its strategy, dynamic development and strengthening its lead position. The ranking was prepared by the 'Polish Market' in collaboration with the Warsaw School of Economics. The effectiveness and growth dynamics of enterprises are decisive for the place of a company in this ranking.
BANK OF THE YEAR ACCORDING TO THE MONTHLY 'THE BANKER'	For the fourth time, PKO Bank Polski SA was honoured with the 'Bank of the Year in Poland' award. The strengthening of the lead market position of the Bank and significant improvement in the quality of the credit portfolio were appreciated, as well as its maintaining high operating effectiveness, robust liquidity and strengthening of the capital strength. This prestigious award in the financial industry confirms that the Polish Bank's effective strategy is also appreciated abroad. The 'Bank of the Year' competition is organized each year by the monthly 'The Banker' which is owned by 'The Financial Times'. The magazine analyses the financial results of banks, their development strategies and projects completed in particular years in the context of the position of the financial sector of a given country.

Golden Laurel in the 'Super Bizness' competition	In the third edition of the competition organized by 'Super Ekspres' PKO Bank Polski SA earned the 'Super Biznes' Golden Laurel Award in the banking and finance category. The jury also appreciated the Bank's dynamic development, its activity in developing mobile and internet banking, and commitment to developing the e-state. The Bank's market position and constant progress and expanding the areas of operation also gained recognition, e.g. establishment of PKO Bank Hipoteczny SA. The 'Super Business' Golden Laurel competition is organized by the editors of 'Super Biznes' a business supplement to the 'Super Express' daily, in cooperation with the Polish Chamber of Commerce, Business Center Club and the Employers of the Republic of Poland.

Actions awarded in the area of Corporate Social Responsibility (CSR)

Ethical Company 2015	PKO Bank Polski SA in the second edition of the 'Ethical Company' was awarded for responsibility and organizational culture. This distinction is granted to companies that comprehensively and systematically carry out activities to build and enhance an organizational culture based on ethics and values in the most comprehensive and systemic way, showing the highest activity in this area compared to other companies in Poland. The competition is organized by 'Puls Biznesu' with substantial support of PwC Poland, responsible for controlling the audit of processes and procedures of participants.
Odpowiadam Polsce	The journalists of 'Gazeta Bankowa' distinguished PKO Bank Polski SA in the Ranking of Socially Responsible Companies 'Odpowiadam Polsce' in Health and Society for popularizing the idea of blood donation as part of the Bank since 2009. Banking shares Honorary Blood Donation. The 'Odpowiadam Polsce' Ranking is a new initiative, in which the jury distinguished projects that support the development of the country. For the jury also the scale of commitment was important - in the winning projects employees of the winning companies were actively involved.
The Best Annual Report	For the fourth time already the Annual Report of PKO Bank Polski SA was honoured with the special award 'The Best of The Best' in the competition for The Best Annual Report organized by the Institute of Accounting and Taxation. This award is proof of professionalism. The Competition's jury recognized the high quality of financial reporting and its image value. The completeness, consistency and clear and logical presentation of data gained recognition. In 2016 PKO Bank Polski SA issued the Social Report for 2015, which apart for business information presents actions conducted by the Bank in the area of Corporate Social Responsibility.
The Best Employer 2016	PKO Bank Polski SA was found to be one of 25 Best Employers in 2016, according to the ranking conducted by 'Gazeta Finansowa'. The Best Employer title is awarded to companies which above all care for a good working atmosphere, the development of employees and satisfaction level. The Bank was awarded for comprehensive actions aimed at the construction of an attractive work environment and career development, and facilitating achieving the professional/private life balance, addressed to employees, and for activity on the external labour market.
Reliable Employer of 2015	Zbigniew Jagiełło, President of the Management Board of PKO Bank Polski SA was awarded in the XIII edition of the national contest organized within the framework of the Programme of Reliable Employer of the 2015 for effective personnel policy of the Bank, which is reflected in the quality of our products and services. Especially appreciated was the modernization of the structure of HR in a large and stable organization in a manner corresponding to the latest global trends and implement a human capital management system SAP. PKO Bank Polski SA was also recognized for actions in the field of CSR: linking business goals with social commitment. The Company was the only financial institution which received two awards.
PKO Bank Polski SA, the Ideal Employer	In the 8th edition of students' ranking of the most desirable polish employees Trendence Graduate Barometer 2016 PKO Bank Polski took the 4th position in the category *Business* improving previous year's position. The Bank was only outwent by such international giants as Google, Apple and the National Bank of Poland. The position in TOP 100 rendence Graduate Barometer ranking is determined by students' choice who pick the most wanted employees. In this year's polish edition there was over 20 thousand students voting from 53 universities, mostly providing business, technical and IT studies.

CIPS CERTIFICATE FOR PKO BANK POLSKI SA	As the first financial sector firm and the third in Poland, PKO Bank Polski SA received an international certificate confirming the highest procurement process standards. The certificate was awarded to the largest global organization in the procurement industry, the Chartered Institute of Procurement and Supply (CIPS). It documents the Bank's business reliability vis-a-vis its customers and counterparties.
THE BANK RECOGNIZED FOR THE HIGHEST SAFETY STANDARDS	PKO Bank Polski SA was awarded in the competition BIG DATA: Think Big CEE in the category of Solution of the Year, for raising the level of security in cyberspace and minimizing the risks to which consumers may be exposed on the network. This is the result of the bank participation in the Microsoft Enterprise Customers Cyber Threat Intelligence Programme (ECCTIP). PKO Bank Polski SA was the first bank in Europe to begin working with Microsoft on the programme ECCTIP. Its aim is to raise the level of security in cyberspace through the exchange of information on potential risks.
TRUSTWORTHY BRAND	PKO Bank Polski SA was given the title of 'Trustworthy Brand 2016' in the category of loans and advances for enterprises in the ranking of the Monthly 'My Company Polska' created by the research institute Millward Brown. Almost 12 percent of the respondents spontaneously indicated the PKO Bank Polski SA brand. The purpose of the survey was determining the brands most trusted by Polish entrepreneurs.
PKO BANK POLSKI SA –APPRECIATED EDUCATOR	Two PKO Bank Polski SA projects were listed in the first ranking in Poland covering 10 projects 'Educational business activities. List of most significant initiatives' – School Savings Associations (Szkolne Kasy Oszczędności) and PKO Charity Run (PKO Bieg Charytatywny). From among the 271 initiatives evaluated by the jury 51 advanced to the third level. Five of them were PKO Bank Polski SA's: SKO, PKO Bieg Charytatywny, educational action #cyberstrażnik (cyberguard), free-of-charge training for entrepreneurs and supporting startups. The final selection of initiatives was made by internet users. The List was made on the initiative of the Responsible Business Forum.
SKO IN THE CHILD & YOUTH FRIENDLY BANKING AWARD FINALS	PKO Bank Polski SA became the finalist of the international competition The Global Inclusion Awards 2016. The educational programme which has been conducted by the Bank for over 80 years, the School Savings Association (SKO) became one of the six best initiatives awarded in the category Child & Youth Friendly Banking Award. The international jury recognized the wide scale of the programme (almost 5 thousand schools involved, 6 thousand teachers), the variety and innovativeness of the solutions applied and the constant development of SKO in respect of the educational programmes made available.

PKO BANK POLSKI SA – LEADER OF MODERN TECHNOLOGIES

MOST DIGITAL BANK	The Bank was selected as the most digital bank in the e-Commerce Polska Awards 2016 competition organized by the e-Commerce Chamber (Izba Gospodarki Elektronicznej). PKO Banku Polski's SA commitment to e-administration, cyber security projects, and to the quality of mobile and electronic banking decided on its being awarded the title. This is a subsequent award for innovativeness, implementing modern technologies and developing solutions which become the model for other financial institutions. The purpose of the e-Commerce Polska Awards is to reward and promote companies which best and most quickly adapt to changes occurring on the modern market. In this year's edition banks and insurance companies participated for the first time.
EDUKAT 2016 FOR CONTACTLESS PAYMENTS HCE	The jury of eDukat 2016 4th International Congress of Non-cash Payments awarded the PKO Bank Polski SA in the category: Event of the year of the non-cash world for implementing contactless payments to mobile application HCE IKO. The recognition gained scale, on which users of IKO use this method of transaction and benefit form the convenience and safety solutions. eDukat symbolizes the evolution of money to its electronic form.
ERGONOMICS OF ELECTRONIC CHANNELS RANKING	PKO Bank Polski SA was announced the winner of the ergonomics of electronic channels ranking and awarded for the best mobile application. Throughout the audit done by 'Puls Biznesu' and Bankier.pl very high notes were given to PKO Bank Polski SA electronic channels - IKO i iPKO. Regarding ergonomics, comfort and usability of the main processes with the result of 71.9 points PKO Bank Polski SA has outdistanced its competitors by nearly 10 points. Mobile application IKO was recognized as the best one on the market!

IT Leader 2016	PKO Bank Polski SA was a winner in the category of Banking and Finance in the 20th edition of the competition 'IT Leader' organized by 'Computerworld'. The jury recognized the Bank's project enabling customers filing applications for the 'Rodzina 500+' programme and using the Electronic Services Platform (PUE) of the Social Insurance Institute (ZUS).
Leader of 2015	Implemented by PKO Bank Polski SA IT solution adjusting to the Bank requirements of EU Regulation EMIR won in the category 'Banking and Finance' in the 'Gazeta Bankowa' competition. The aim of this comprehensive software is to reduce credit and operational risk in derivatives market. The Leader 2015 competition identifies companies and financial institutions, which are distinguished by special achievements in the field of modern and innovative technologies.
PKO Bank Polski SA, Partner of the Year 2015	The contest jury of 11th Electronic Economy Convention organized under the auspices of The Polish Bank Association, chosen PKO Bank Polski SA as the Partner of the Year 2015. The victory was earned with the Bank's involvement and contribution to the sector's integration around digital economy, support for innovative solutions enabling access to important services and benefits improving comfort of everyday life of millions of Polish citizens.

The best of Products and services

Złoty Bankier of 2015	In the seventh 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 its access to financing also in the case of low own contribution, as well as the conditions for early repayment and promotional reducing the margin in the first year of the contract. Złoty Bankier is the highest ranking assessed banking services and products in Poland. For seven years the Bank determine the direction for Polish banking indicating the best offer on the market. The organizers of the ranking are: Bankier.pl and the 'Puls Biznesu'.
PKO Bank Polski SA the best bank for individual customer	In the Portfolio contest of 'Wprost' the Bank became the winner in one of the main categories – 'Bank for individual customer'. The leader's position was ensured by modern and transparent product offer, tailored to meet customers' needs. The purpose of the contest 'Wprost' Portfolio is to promote financial institutions with the most attractive offer, new financial products and services on the market as well as to honour leaders of the sector.
Comperia Stars statuette for 'Własny Kąt Hipoteczny'	The WŁASNY KĄT Hipoteczny mortgage loan offered by PKO Bank Polski SA triumphed in the listing of mortgage loans prepared by the editors of Comperia.pl in July. Analysts checked the offers of banks dedicated to those who wish to take out loans of PLN 250 thousand with a 20-year repayment period. The offer of PKO Bank Polski SA proved the most favourable for the selected parameters. This is the third time the Bank's Kredyt WŁASNY KĄT Hipoteczny loan won the competition this year, and the product also received statuettes in February and June 2016.
The best Contact Center	The Contact Center of PKO Bank Polski SA declassed its rivals for the tenth time in the cyclic study conducted by ARC Rynek i Opinia (11th time on the podium). The Bank's helpline earned a total score of 97.1 points, with the average for the market at 82.5. Both its email and telephone contacts were appreciated. The auditors evaluated the availability of the helpline, the quality of the connection and conversation, including politeness, commitment and professionalism of the consultants. In respect of email contacts, the Bank also received maximum scores for the speed of response and competencies and politeness of the staff.

Strong Brand

Superbrands	In the 11th edition of the Superbrands Polska poll, PKO Bank Polski SA, was awarded the Superbrands 2016/17 and Created in Poland Superbrands 2016/17 titles. They attest to the brand's strength, its reliability and confidence of respective customers in the brand. The winners of the poll are selected by the expert Brands Council consisting of over 50 experts in the area of marketing, research, strategy, branding, advertising and PR, based on the poll conducted by the research institute ARC Rynek i Opinia. Over 15 thousand consumers participated in the poll, and gave their opinions on over 2000 brands.

LEADER OF TOP MARKA RANKING	PKO Bank Polski SA is the banking institution most frequently and best described in the media – as follows from the seventh 'Top Brand' ranking. It gained the most points for the number and scope of publications. The analysis covered information in the press, on the internet, and in social media. The advertising equivalent for all publications in which references were made to PKO Bank Polski SA proved the highest among the banks and amounted to over PLN 190 million. The purpose of the listing prepared by the 'Press' monthly and Press-Service Monitoring Mediów is selecting brands which are the most popular in the press and in the internet media. In the period under analysis – July 2015 - June 2016 – on average during one month approx. 4.2 thousand pieces of information were published about our Bank in the media and on internet portals.
LAMPARTY	PKO Bank Polski SA was awarded with 'Lampart 2016' statuette with the contest for most admired development of banking and insurance branding. It gained appreciation for brand image rejuvenation, consistence and coherent marketing message. In this year's edition the Bank took the 3rd place. The main idea behind award from Polish research agency TNS is to distinguish those banks and insurance agencies, which most effectively developed their brand during the given year. Winners are selected in TNS Polska survey among the representatives of the banking and insurance industry.
PKO BANK POLSKI SA, ONE OF THE MOST RECOGNIZABLE AND ACTIVE BRANDS	The Bank was awarded the prize 'Global Poland' in the category 'Polish brand with a tradition that still have a strong tradition'. The aim of the competition was to honour the most recognizable and active in foreign markets Polish brands. Plebiscite 'Global Poland' is this year's initiative of monthly management magazine 'Manager'.

BROKERAGE ACTIVITY

BULLS AND BEARS	The Brokerage House of PKO Bank Polski SA has won the title of 'Brokerage House of the Year' in the 22nd edition organized by the newspaper 'Parkiet' in the Bulls and Bears competition. The purpose is to honour companies, institutions and people who have most distinguished themselves in the capital market contributing to its development. Last year, the Brokerage House was the most active on the stock market and bonds. It was the leader in terms of number and value of transactions carried out on the capital market. Offer for individual customers expanded to include modern and comfortable tool to invest in foreign markets.
LEADER OF THE NATIONWIDE INVESTOR SURVEY	Dom Maklerski PKO Banku Polskiego SA (the Bank's Brokerage House) came first in the ranking prepared by the Association of Private Investors (SII) and Bankier.pl. This is proof of effectiveness in its building the lead position among brokerage houses in Poland. During the past six years the Brokerage House rose in the SII ranking from 13th position to being the leader. It gained top scores in six out of seven categories assessed by the investors in the Nationwide Investors Survey for 2016. It was also the sole brokerage house which scored more than 4 points in all categories. The investors appreciated mainly the professionalism of the staff and the quality of service. The transactional platform, the quality of analyses and the educational offer gained the highest scores.

AWARDS GRANTED TO OTHER ENTITIES OF THE GROUP

KREDOBANK RANKS FIRST IN RELIABILITY OF DEPOSITS	KREDOBANK SA, belonging to the PKO Bank Polski SA Group, won in the 15th edition of the ranking of reliability of deposits in Ukraine, prepared by the Ukrainian rating agency 'Standard-Rating'. During the assessment of reliability of deposits, the Agency's analysts took into consideration several factors, including the financial results and the dynamics of other indices subject to publication. Sixty-six Ukrainian banks were classified in the ranking.
KREDOBANK WINS THE RANKING OF FAIR TAXPAYERS IN THE UKRAINE	KREDOBANK SA topped the ranking of 'Fair Taxpayers – 2015' in the Ukraine in the category of 'financial and insurance activities' organized among large taxpayers by the Association of Ukraine Taxpayers. The ranking evaluated fiscal discipline, the number of employees and social programmes.
PKO FAKTORING SA	The product called 'faktoring z przejęciem ryzyka i bez przejęcia ryzyka dla Małych i Średnich Przedsiębiorstw' ('factoring for SMEs with and without assumption of risk'), offered by PKO Faktoring SA, was recognized by Gazeta Finansowa in the poll for the '2016 Best Product for SMEs'.

PKO LEASING SA	PKO Ekspres Leasing offered by PKO Leasing SA was distinguished by Gazeta Finansowa in the poll for the 'Best Business-oriented Product'.
IKZE FROM THE OFFER OF PKO TFI IS BEST	IKZE (an individual pension insurance account) offered as part of the Pension Package by PKO TFI (IKZE+IKE) ranked first in the Ranking of TFI which also offer IKZE in the form of an investment fund prepared by the 'Rzeczpospolita' daily. The ranking took into consideration three factors, i.e. the rates of return on investments in four periods, a diversified offer and fees collected from customers.
2ND PLACE FOR IKE IN THE PKO TFI OFFER	IKE offered under the pension package Pakiet Emerytalny PKO TFI (IKE + IKZE) was awarded second place in the ranking organized by Analizy Online research centre. The programme was awarded the highest score, among other things, for its high management effectiveness, the lowest costs among all IKEs, interesting offer and offering the product in a Package which allows customers to also invest in IKZE.

7. RISK MANAGEMENT

7.1 PRINCIPLES OF RISK MANAGEMENT

Risk management is one the most important internal processes in PKO Bank Polski SA, including in abroad branch and as well as in other companies of the PKO Bank Polski SA Group. Risk management aims at ensuring profitability of business activity, with ensuring control of risk level and maintaining it within the risk tolerance and limits system applied by the Bank, in the changing macroeconomic and legal environment. The level of the risks plays an important role in the planning process.

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[13]): <u>credit</u>, credit risk concentration currency mortgage loans risk, , <u>interest rate</u>, <u>currency</u>, <u>liquidity (including financing risk)</u>, commodity price, price equity securities, other price risk, <u>derivative</u>, <u>operational</u>, lack of <u>compliance and conduct risk</u>, <u>macroeconomic changes</u>, <u>models</u>, <u>business (including strategic risk)</u>, <u>loss of reputation</u>, conduct risk, capital, <u>excessive leverage</u> and insurance[14].

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 Bank 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.

[13] The significance of the individual types of risk is established at the Bank's level. When determining criteria of classifying a given type of risk as significant, an influence of the significance of the risk on the Bank's activities is taken into account, whereas risk are recognized 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 Bank 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 Bank 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 Bank changed.

[14] The risk relates to the Bank Group's companies.

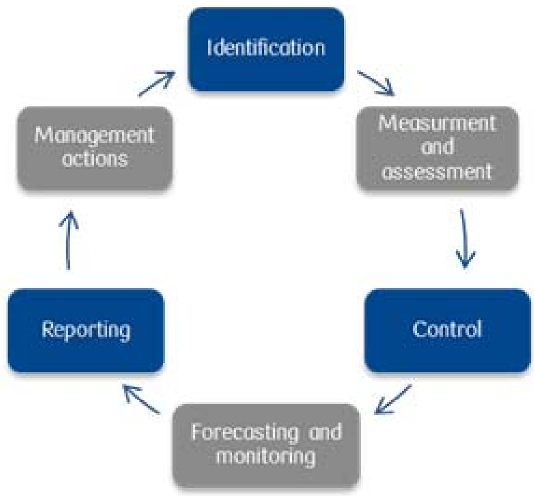
MAIN PRINCIPLES OF RISK MANAGEMENT

Risk management in PKO Bank Polski SA Group is based especially on the following principles:

1) the Group manages all of the identified types of risk,
2) the risk management process 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 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 process supports the implementation of the Group's strategy in compliance with the risk management strategy, in particular with regard to the level of tolerance of the risk.

THE RISK MANAGEMENT PROCESS

The process of risk management in Group consists of the following stages:



- **RISK IDENTIFICATION**

Identification of risk is 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 Bank (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 (defined, among other things, by the GDP, inflation level, unemployment rate, foreign exchange rates, interest rates) on the Bank's financial position.

- **RISK CONTROL**

Risk control is to determination of tools used for measuring or reducing the level of risk in specific areas of the Bank'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.

- **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,

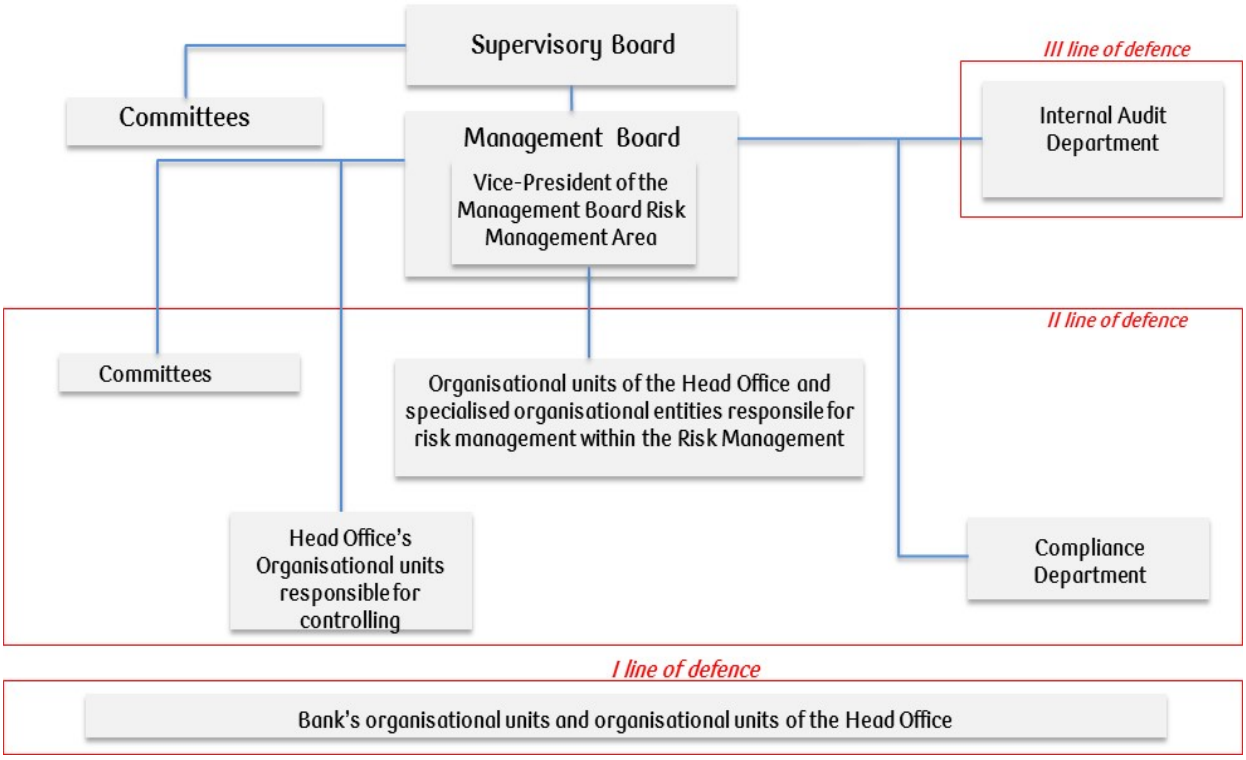
- **MANAGEMENT ACTIONS**

Management actions consist particularly, issuing internal regulations affecting the management process of different types of risk, establishing the level of risk tolerance, establishing limits and thresholds, issuing recommendations, 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.

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 process is supervised by the Supervisory Board of the Bank, which is informed on a regular basis about the risk profile of the Bank as well as of the PKO Bank Polski SA Group and the most important activities taken in the area of risk management. The Bank's Supervisory Board is supported, among other things, by the following committees: the 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 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 regulations concerning risk management. The Supervisory Board is supported by the following committees:

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 process is carried out in three, mutually independent lines of defence:

- **THE FIRST LINE OF DEFENCE** is being performed particularly in the organizational units of the Bank, the organizational units of the Head Office and the external entities to which the Bank outsourced other banking activities and concerns the activities of those units', cells and entities which may generate risk. The units and entities are responsible for identifying risks, designing and implementing appropriate controls, including in the external entities, unless controls have been implemented as part of the measures taken in the second line of defence.

- THE SECOND LINE OF DEFENCE the risk management system, in particular the measurement or assessment, control, monitoring and reporting particular risks important to the Bank, reporting identified threats and irregularities, preparing the Bank's internal regulations determining the risk management principles, methods, tools and procedures, and measuring operating effectiveness. The function is being performed, in particular, in the Risk Management Area, Compliance Department, Planning and Controlling Department, relevant committees, as well as the other organizational units of the Head Office responsible for controlling.
- THE THIRD LINE OF DEFENCE is being performed as part of internal audit, including the audit of the effectiveness of the system of managing the risk.

The independence of the lines of defence consists of preserving organizational independence in the following areas:

- the function of the second line of defence as regards creating system solutions is independent of the function of the first line of defence,
- the function of the third line of defence is independent of the functions of the first and second lines of defence,
- the function of managing the compliance risk reports directly to the President of the Management Board.

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. The Bank also supervises the entities' risk management systems and provides support in the development of these systems. Additionally, 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 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.

The risk management in the Group entities is carried out in particular by:

- involving the units in the Bank's Risk Management Area or the Bank's relevant committees in evaluating large transactions of the Group entities,
- giving opinions and reviewing internal regulations concerning risk management in the individual Group entities, carried out by the units in the Bank's Risk Management Area,
- reporting on the Group entities' risks to the Bank's relevant committees or the Management Board,
- monitoring of strategic risk tolerance limits for the Group.

SPECIFIC ACTIVITIES IN THE AREA OF RISK MANAGEMENT IN THE BANK, UNDERTAKEN IN 2016

PKO Bank Polski SA's priority is to maintain its strong equity position, including effective capital adequacy management, supporting Polish entrepreneurship, customer satisfaction, engaging in creating new standards on a market scale, counteracting cyberthreats, while maintaining the priorities of efficiency and effective cost control and appropriate risk assessment.

In this respect, the Bank took i.a. the following actions in 2016:

- in 2016 turned the maturing own short-term bonds, on bonds in the amounts PLN 1 billion (in May) and PLN 815 million (in November),
- in April 2016 turned the maturing own short-term bonds, on bonds with a maturity to one year in the amounts EUR 200 million,
- in connection with the acquisition of 100% shares in Raiffeisen-Leasing Polska SA by PKO Leasing on 1 December 2016, a decision was taken not to pay dividend from the Bank's profits earned in 2015 and retained earnings.

In 2016, the Bank conducted operating risk management-related preparatory work for starting operations of the Bank's new branch in the Czech Republic, the opening of which is planned for March 2017.

As part of this work, in November 2016, the Bank filed an application with the Polish Financial Supervision Authority requesting consent for joint application of advanced measurement approach (AMA) and basic indicator approach (BIA) consisting of the Bank's calculating the requirements relating to own funds in respect of operational risk using the BIA method in respect of the operations of the Bank's branch in the Federal Republic of Germany and in the Czech Republic, and using the AMA approach in the remaining operations of the Bank.

In the fourth quarter of 2016, the Bank introduced changes to the process of managing the exposure concentration risk, which constitute the fulfilment of the requirements of Resolution No. 351/2016 of the Polish Financial Supervision Authority dated 24 May 2016 on issuing Recommendation C and include: concentration risk management objectives and process, new measures of tolerance to concentration risk, including internal limits mitigating the risk of excessive concentration and the method of performing stress tests regarding concentration risk.

In the fourth quarter of the year, the Bank updated and considerably simplified the method of assessing credited entrepreneurs in the formula of specialist financing, which allows an adequate credit risk assessment of large projects involving financing income-generating residential and commercial real estate.

In the first half of 2016, the Bank and PKO Bank Hipoteczny SA continued work related to model risk management in the process of adapting to the requirements of Recommendation W on risk management in banks, issued by the Polish Financial Supervision Authority in July 2015. As of 30 June 2016 the process of model risk management in the Bank and in PKO Bank Hipoteczny SA is conducted pursuant to the requirements of Recommendation W.

Within the Group, mortgage loan portfolios which had been extended by PKO Bank Polski SA are gradually transferred to PKO Bank Hipoteczny SA. The nominal value of the portfolio transferred in 2016 amounted to PLN 5.8 billion.

In the first half of 2016, PKO Bank Hipoteczny SA conducted two issues of mortgage bonds addressed to institutional investors, in the total amount of PLN 1 billion, with a maturity period of 5 years and 1 day as of the date of issue. Among the institutions which purchased mortgage bonds are both domestic and foreign investors. Mortgage bonds of PKO Bank Hipoteczny are one of the safest debt instruments on the Polish financial market. Moody's rating of Aa3, which is the highest rating achievable by Polish securities, attests to this.

In the second half of 2016 PKO Bank Hipoteczny SA conducted 1 benchmark foreign issue of mortgage bonds addressed to institutional investors, with a value of EUR 0.5 billion and period to redemption of 5 years and 8 months. The securities bear an interest rate of 0.125 p.p. and yield of 0.178 p.p. Among the institutions which purchased mortgage bonds are both domestic and foreign investors, including the European Bank of Reconstruction and Development.

7.1.1 CREDIT RISK

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 as well as to 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 subsidiaries of the Group are primarily driven by the following principles of credit risk management:

- each 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,
- credit risk assessment of exposures which are significant due to their risk levels or its value is subject to additional verification by credit risk assessment teams, which are independent of the business teams,
- terms of loan transactions that are offered to a customer depend on the assessment of credit risk level or its value 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 in their organizational structures, which are in particular responsible for:

- 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 enforcement 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, which are involved in the case of credit transactions which generate increased credit risk level.

Appropriate organizational 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 Loss (EL),

- Unexpected Loss (UL),
- Loss Given Default (LGD),
- Credit Value at Risk (CVaR),
- share and structure of impaired loans,
- ratio of impaired loans (under IAS) to impairment allowances (coverage ratio),
- cost of credit risk.

The Bank extends 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 the whole 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 Banking Risk Division. 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 assess the credit risk of retail customers in two dimensions: creditworthiness assessed quantitatively and qualitatively. The quantitative assessment of creditworthiness consists of evaluation of the 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: customer's 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.

In other cases, 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 real estate financing (e.g. office space, retail areas, industrial areas) and infrastructure projects (e.g. telecommunications, industrial, public utility infrastructure).

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 in the Recommendation S, relating to best practices for the management of mortgage-secured loan exposures and Recommendation T relating to best practices for the management of retail credit exposures.

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, determining the conditions in which credit assessment services are activated 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:

- supervising the level of the portfolio credit risk on the basis of the adopted tools used for measuring credit risk, taking into consideration the identified sources of credit risk and analyzing the effects and actions taken as part of system management,
- 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.

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 – the limits defined in article 395, item 1 of the CRR Regulation and in the Banking Law,
- 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 and the entities of the Group's 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 ensure the highest possible level of recovery in the event of realization of debt collateral activity

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.

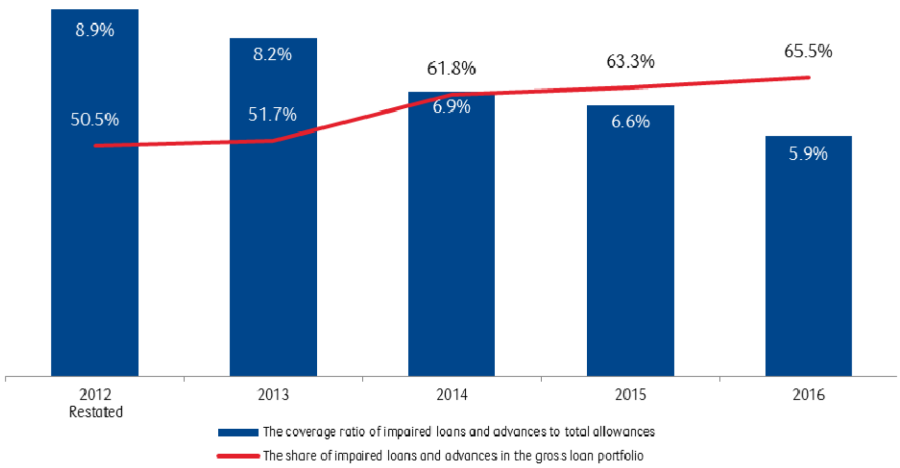
The type of collateral depends on the product and the customer segment. The policy regarding collateral is defined by the internal regulations of the Group subsidiaries.

Table 19. The structure of loan portfolio and impairment allowances of the PKO Bank Polski SA Group (in PLN million)

	31.12.2016			31.12.2015		
	Gross	Write offs	Net	Gross	Write offs	Net
Loans and advances to customers						
individualized method, incuding:	6 551	-2 608	3 942	7 550	-2 896	4 654
impaired	5 049	-2 594	2 455	5 413	-2 882	2 530
no identified impairment	1 502	-14	1 487	2 137	-13	2 124
portfolio method	7 183	-4 766	2 417	7 688	-4 822	2 866
Impaired	7 171	-4 766	2 406	7 688	-4 822	2 866
No identified impairment	12	0	12	0	0	0
group method (IBNR)	194 876	-629	194 247	183 463	-569	182 894
Loans and advances to customers - net	**208 609**	**-8 003**	**200 607**	**198 701**	**-8 287**	**190 414**

In 2016 the gross value of loans extended by the Group, assessed using the individual method decreased by PLN 999 million, and assessed using the portfolio method decreased by PLN 505 million, while those assessed using the group method increased by PLN 11 412 million.

Chart 6. The share of impaired loans and advances in the PKO Bank Polski SA Group and the coverage ratio to total allowances



The share of impaired loans of the PKO Bank Polski SA Group in gross loan portfolio as at 31 December 2016 amounted to 5.8% and dropped by 0.7 p.p. y/y compared with 31 December 2015.

The coverage ratio of impaired loans for the PKO Bank Polski SA Group as at 31 December 2016 amounted to 65.5%, compared with 63.3% as at 31 December 2015.

RISK MANAGEMENT OF FOREIGN CURRENCY MORTGAGE LOANS FOR INDIVIDUALS

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. 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.

Due to the fact that the significant appreciation of the CHF against Polish zloty is 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 Group has taken a number of actions designed to help the customers 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 Group 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.

As at the end of 2016 the value of the Bank's portfolio of loans for denominated in CHF granted to households amounted to PLN 29.8 billion compared to PLN 30.8 billion as at the end of 2015.

7.1.2 Interest rate risk

Definition	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.
Management objective	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.
Risk identification and measurement	The Group utilizes such interest rate risk measures as: • sensitivity of interest income, • sensitivity of economic value, • value at risk (VaR), • stress tests, • repricing gap.
Control	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.
Forecasting and monitoring	The following, in particular, are monitored by the Group on a regular basis: • the level of interest rate risk, • the degree of utilization of the strategic limit of interest rate risk tolerance, • the degree of utilization of internal limits and threshold values relating to interest rate risk.
Reporting	The reports on interest rate risk are developed on a daily, weekly, monthly and quarterly basis.
Management actions	The main tools used in interest rate risk management in the Group include: • procedures for interest rate risk management, • limits and thresholds for interest rate risk. The Group established limits and thresholds for interest rate risk comprising i.a. the following: price sensitivity, sensitivity of the economic value and loss. 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.

As at 31 December 2016, the exposure of PKO Group Polski SA to interest rate risk 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 unfavorable for the Group was the scenario of a parallel shift in PLN interest curves.

The effect of the materialization of this scenario at 31 December 2016 amounted to approx. PLN 1.75 billion, while as at 31 December 2015 this figure amounted to approx. PLN 1.6 billion. Interest rate risk generated by the Group entities with regard to PLN, EUR and CHF did not have a significant effect on the interest rate risk of the entire Group and therefore did not significantly affect its risk profile. Interest rate risk with regard to USD was significantly altered by exposure of the Group entities, in which the biggest part has the exposure of KREDOBANK SA.

Table 20. VaR of PKO Bank Polski SA and stress-tests analysis of the Group's exposure to the interest rate risk

Name of sensitivity measure	31.12.2016	31.12.2015
VaR for a 10-day time horizon (in PLN milion)*	269	272
Parallel movement of the interest rate curves by 200 b.p. (in PLN milion) (stress-test)**	2 059	2 014

* 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 31 December 2016 the value of VaR in the KREDOBANK SA amounted to approx. PLN 8.9 million and PLN 11.5 million as at 31 December 2015.

** 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.

As at 31 December 2016 the Bank's interest rate VaR for a 10-day time horizon (10-day VaR) amounted to PLN 269 million, which accounted for approximately 0.9% of the Bank's own funds. As at 31 December 2015, VaR for the Bank amounted to PLN 272 million, which accounted for approximately 1.00% of the Bank's own funds.

7.1.3 CURRENCY RISK

DEFINITION	Currency risk is the risk of incurring losses due to unfavourable exchange rate changes. The risk is generated by maintaining open currency positions in a given foreign currency.
MANAGEMENT OBJECTIVE	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.
RISK IDENTIFICATION AND MEASUREMENT	The Group utilizes the following currency rate risk measures: • value at risk (VaR), • stress tests.
CONTROL	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.
FORECASTING AND MONITORING	The following, in particular, are monitored by the Group on a regular basis: • the level of currency risk, • the degree of utilization of the strategic limit of currency risk tolerance, • the degree of utilization of internal limits and threshold values relating to currency risk.
REPORTING	The reports on currency risk are developed on a daily, weekly, monthly and quarterly basis.
MANAGEMENT ACTIONS	Main tools used in currency risk management in the Group include: • procedures for currency risk management, • limits and thresholds for currency risk, • defining allowable types of transactions in foreign currencies and the exchange rates used in such transactions. 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 daily loss from transactions on currency market. 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.

Table 21. 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	31.12.2016	31.12.2015
VaR for a 10-day time horizon (in PLN milion)*	10	25
Change in CUR/PLN rates by 20% (in PLN milion) (stress-test)**	25	2

* Due to the nature of the activities carried out by the other Group entities generating significant currency risk as well as the specific nature of the market on which they operate, the Bank does not calculate consolidated VaR. These entities apply their own risk measures in the currency risk management. The KREDOBANK SA Group uses the 10-day VaR, which amounted to approx. PLN 0.35 million as at 31 December 2015 and approx. PLN 4.8 million as at 31 December 2014.
** The table presents the value of the most adverse stress-test of the scenarios: PLN appreciation by 20% and PLN depreciation by 20%.

Table 22. The currency position for particular currencies in the Group

Currencies	The currency position as at 31.12.2016	The currency position as at 31.12.2015
EUR	-170	94
USD	30	-87
CHF	-36	-73
GBP	9	-2
Other (Global Net)	89	171

The amount of foreign currency positions is the key (apart from volatility of foreign exchange rates) factor determining the level of foreign currency risk to which the Group is exposed. All foreign currency transactions concluded, both balance-sheet and off-balance sheet have an impact on the foreign exchange position. The Bank's exposure to foreign exchange risk is low (in respect of the Bank's own funds as at 31 December 2016 10-day VaR for the Bank's foreign exchange position amounted to approx. 0.03%).

7.1.4 LIQUIDITY RISK

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 OF RISK	The Group regularly monitors: • utilization level 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 sources of financing,
- early warning signals – monitoring their level is aimed at the early discovery of unfavourable phenomena which could have a negative impact on the Bank's or the financial sector's liquidity position (which, when exceeded, launch liquidity contingency plans).

The Group also performs cyclic 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.

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 emergency plans,
- limits and thresholds mitigating for liquidity risk,
- deposit, investment, derivative transactions, including structured forex transactions, and purchase and sales transactions 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). In liquidity risk management money market instruments, including NBP open market operations are also used.

The Bank's Group liquidity reserve and excess liquidity as at 31 December 2016 and 31 December 2015 are shown in the Table below.

Table 23. Liquidity reserve and excess liquidity of PKO Bank Polski SA Group (in PLN billion)

Name of sensitivity measure	31.12.2016	31.12.2015
Liquidity reserve up to 1 month*	31	30
Overliquidity in a horizon of up to 30 days**	13	15

* Liquidity reserve equals the gap between the most liquid assets and expected and potential liabilities which mature in a given period of time.
** Excess liquidity – excess liquidity 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 measured as at 31 December 2016 and 31 December 2015 are shown in the Table below.

Table 24. Supervisory liquidity measures

Supervisory liquidity measures	31.12.2016	31.12.2015
M1	24 464	18 907
M2	1.89	1.65
M3	11.63	9.87
M4	1.19	1.15
LCR	136.3%	131.5%

In the period from 31 December 2015 to 31 December 2016 ratios supervisory measures remained above the supervisory limits. Indicated in the table, the LCR indicator shows the value for the Group.

As at 31 December 2016 the level of permanent balances on deposits constituted approx. 93.8% of all deposits in the Bank (excluding interbank market), which means a decrease by approximately 0.3 p.p. as compared to the end of 2015.

7.1.5 OTHER MARKET RISKS

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

COMMODITY PRICE RISK

DEFINITION	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.
MANAGEMENT OBJECTIVE	Reduce potential losses resulting from changes in commodity prices to the acceptable level by shaping the appropriate structure of these items.
RISK IDENTIFICATION AND MEASUREMENT	In respect of the measurement of the prices of commodities in the other companies of the Group, information on the positions taken by the Group in particular commodities is utilized.
CONTROL	Control of commodity prices covers determining respective limits and threshold levels tailored to the scale and complexity of the Group's operations.
FORECASTING AND MONITORING	In respect of the commodity price risk the Group regularly monitors, in particular open commodity positions, if they arise.
REPORTING	Reports on commodity price risks are developed on a daily, weekly, monthly and quarterly basis.
MANAGEMENT ACTIONS	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 Group's financial position is immaterial. Currently, commodity risk in the remaining Group companies is non-existent.

PRICE RISK OF EQUITY SECURITIES

DEFINITION	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.
MANAGEMENT OBJECTIVE	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.
RISK IDENTIFICATION AND MEASUREMENT	For the purpose of equity securities price risk management the Group utilizes: • analyses of stress tests, in consideration of changes in market prices of the base instrument and changes in its volatility, • information on the positions taken in the equity securities portfolio.
CONTROL	Control over equity securities risk covers determining equity securities risk limits and thresholds tailored to the scale and complexity of the Group's operations.
FORECASTING AND MONITORING	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.

Reporting	Reports on the risk of equity securities are prepared on a monthly and quarterly basis.
Management actions	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

Definition	The risk of derivative instruments is a risk resulting from the Bank's taking up a position in financial instruments.
Management objective	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.
Risk identification and measurement	For the purpose of managing derivatives risk, the Group uses: • the Value at Risk (VaR) model, • analyses of stress tests, in consideration of changes in market prices of the base instrument, changes in its volatility, and changes in interest rates, • sensitivity ratios of options. 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.
Control	Control over derivatives risk covers determining derivatives risk limits and thresholds tailored to the scale and complexity of the Group's operations.
Forecasting and monitoring	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.
Reporting	In the Group the reports on risk are developed on a daily, weekly, monthly and quarterly basis
Management actions	The main tools used in derivative risk management are as follows: • written procedures for derivative risk management, • limits and thresholds set for the risk related to derivative instruments, • master agreements specifying, i.a. settlement mechanisms, • collateral agreements, under which selected customers of the Bank are required to establish a collateral on exposures due to derivative instruments. Risk management is carried out by imposing limits on the derivative instruments, monitoring limits and reporting risk level. The derivative risk management process is integrated in the Bank 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. 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).

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 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, at the end of the year 2016, 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.

7.1.6 OPERATIONAL RISK

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 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 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 Group,
- operational events and their consequences,
- results of operational risk self-assessment,
- the operational risk requirement relating to own funds in accordance with the BIA approach in respect of the operations of the Branch in Germany, 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,
- the level of risk in Group, areas and tools for operational risk management in Bank,
- key Risk Indicators (KRI), in relations to threshold and critical values,
- 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.

The following entities had a crucial effect on the Group's operational risk profile: PKO Bank Polski SA, the PKO Leasing SA Group and the KREDOBANK SA Group. Other Group companies, due to the much smaller scale and type of their operations, generate limited operating risk only.

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.

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:

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,
- human resources management instruments,
- 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.

7.1.7 OTHER RISK

Compliance risk and conduct risk Business risk Reputation risk Model risk Macroeconomic changes risk Capital risk Insurance risk Risk of excessive leverage

COMPLIANCE RISK AND CONDUCT RISK

DEFINITION	The non-compliance risk is the risk of legal sanctions, financial losses, or loss of reputation or credibility, if the Group, Group's staff or entities acting on behalf of the Group fail to comply with the universally applicable provisions of law, internal regulations, or market standards adopted by the Group. Conduct risk means a risk which arises on the part of: 1) the customer, 2) the Group, including its credibility, 3) financial markets, with regard to their credibility, as a result of inappropriate action (also unintentional) or any omission by the Group, its staff or related entities, with regard to offering purchase and provision of financial services.
MANAGEMENT OBJECTIVE	• reinforcing among shareholders, customers, the Group's staff, business partners, and other market participants, an image of the Group as an institution which abides by the law and market standards, which is trustworthy, reliable and honest, • countervailing financial losses or legal sanctions, or loss of reputation, which can result from the violation of the law, internal regulations of the Group, and market standards adopted by the Group, • Countervailing losses on the part of the Group, which can result from inappropriate conduct (also unintentional) or omission by the Group, its staff or related entities, with regard to offering purchase and provision of financial services.
RISK IDENTIFICATION AND MEASUREMENT	Identification and asses through information on cases of non-compliance and the reasons for their occurrence, including information as a result of an internal audit, a functional internal control and external controls is used
FORECASTING AND MONITORING	This involves: • an analysis of cases of non-compliance in the Group and in the banking sector, the causes and effects thereof, • evaluation of key provisions of the law affecting the operations of the Group, • evaluation of activities undertaken by the Bank and members of the Group as part of the management of the non-compliance risk, • evaluation of the effectiveness and adequacy of the controls connected with mitigation of the non-compliance risk, • an analysis of information about the status of the major adaptation work performed by the Group to adapt to the universally applicable provisions of law, market standards adopted by the Group and notices of external supervisory and control authorities, • an analysis of information about operating events, security incidents, disputes, including litigation, against the Group, complaints and irregularities connected with the conduct risk.
REPORTING	In the form of quarterly management reports designated for the Risk Committee, the Management Board, the Supervisory Board Risk Committee, and the Supervisory Board, as well as information submitted for the purposes of external supervision and control authorities.
MANAGEMENT ACTIONS	The management comprises, in particular, the following issues: • preventing the Group from engaging in illegal activities, • promoting ethical standards and monitoring them, • managing conflicts of interest, • preventing situations in which the conduct of the Group's employees in official matters could give the

impression of being a private interest,

- professional, reliable, and transparent preparation of the product offer, as well as advertising and marketing messages,
- ensuring the protection of information,
- immediate, fair and professional handling of customer complaints, requests and grievances,
- preventing situations in which a product incompatible with the customer's needs could be offered,
- determining an adequate manner and form of proposing purchases with regard to the nature of the product offered,
- monitoring sales and the reliable performance of agreements concluded with customers.

The Group adopted the policy of 'zero tolerance' for non-compliance which means that the Group focuses its activities on eliminating such risk.

Business risk

Definition	Business risk is the risk of incurring losses due to adverse changes in the business environment, taking bad decisions, the incorrect implementation of decisions taken, or not taking appropriate actions in response to changes in the business environment; this includes in particular strategic risk.
Management objective	Maintaining, on an acceptable level, the potential negative financial consequences resulting from adverse changes in the business environment, making adverse decisions, improper implementation of adopted decisions or lack of appropriate actions, which would be a response to changes in the business environment.
Risk identification and measurement	Identification is to recognize and determine factors both current and potential, resulting from current and planned activities of the Group and which may significantly affect the financial position of the Group, generating or change in the Group's income and expense. Business risk identification is performed by identifying and analyzing the factors that had an impact on the significant deviations of realization of income and expense from their forecasted values. Measurement of business risk is aimed at defining the scale of threats related to the existence of business risk with the use of defined risk measures. The measurement of business risk includes: calculation of internal capital, conducting stress-tests.
Control	Control of the business risk is aimed at striving to maintain the business risk at an acceptable level. Involves setting and periodic review of the risk controls in the form of tolerance limits on the business risk along with its thresholds and critical values, adequate to the scale and complexity of the Group.
Forecasting and Monitoring	Forecasting of the business risk is aimed at determining an anticipated scenario of changes in the income and expense items in the income statement. The forecast is prepared once a quarter on a yearly basis and includes forecasting the level of business risk and internal capital. Once a quarter, the verification of a business risk forecast (so-called backtesting) is performed. Monitoring of the business risk is aimed at diagnosing the areas which require management actions. Monitoring of business risk includes in particular: • strategic levels of business risk tolerance – on a quarterly basis, • stress-tests results – on an annual basis, • internal capital level – on a quarterly basis, • deviations from the implementation of business risk forecast – on a quarterly basis, • results of a survey conducted among senior management staff of the Bank - on an annual basis.
Reporting	Reporting is performed on a quarterly basis. The reports on the business risk level are addressed to the ALCO, the RC, the Management Board, the Risk Committee of the Supervisory Board, and the Supervisory Board.

MANAGEMENT ACTIONS	Management actions consist of, in particular: • verifying and updating quarterly financial forecasts, including actions aimed at lowering the business risk level in accordance with the limits, • monitoring the level of the strategic limit of tolerance to business risk

REPUTATION RISK

DEFINITION	The reputation risk is understood as the risk of deterioration of reputation among customers, counterparties, investors, supervisory and control authorities, and the general public as a result of the Group's business decisions, operating events, instances of non-compliance or other events.
MANAGEMENT OBJECTIVE	Protect the Group's reputation by counteracting the occurrence of reputation and limiting the negative effect of image-related events on the Group's reputation.
MONITORING	Information monitoring of image-related events, taking into account every identified, negative information about the Group, in the form of: information disseminated in the media, information disclosed within the principles of information policy of the Group, evaluation of audits firms, analytical institutions and external supervisory and control authorities, public protests and speeches,
REPORTING	Reporting the risk of loss of reputation is effected by: • management reports for the Risk Committee, the Management Board, the Supervisory Board Risk Committee, and the Supervisory Board, • information submitted on an on-going basis in respect of current events with considerable impact on reputation, to the President of the Management Board Division Director, and the President of the Management Board, • Information included in the Bank's and the Group's financial statements, and submitted on request to external supervisory and control authorities.
MANAGEMENT ACTIONS	These include, among other things: • an analysis of the causes of specific image-related events, • evaluation of the effects thereof, preparing propositions of management activities aimed at mitigating the risk of losing reputation.

MODEL RISK

DEFINITION	Model risk is the risk of incurring negative financial effects or reputation as a result of making incorrect business decisions on the basis of the models functioning. As a part of the Group model risk is managed both at the level of the entity of the Group (the owner of the model), and at the level of the Bank as the parent company of the Group.
MANAGEMENT OBJECTIVE	Mitigate the level of risk of incurring losses as a result of making incorrect business decisions on the basis of existing models in the Group through a well-defined and implemented process of models management. One of the elements of the model management process is to cover all significant models in the Group with regular, independent validation.
RISK IDENTIFICATION AND MEASUREMENT	Identification of the model risk consists of, in particular, collecting information about the existing models and models planned to be implemented as well as determining the materiality of the models on a periodical basis. The model risk evaluation is aimed at determining the scale of the threats associated with the occurrence of the model risk. The evaluation is made at the level of each model as well as on an aggregate basis at the level of the individual Group entities.
CONTROL	Control of the model risk is aimed at maintaining an aggregated evaluation of the model risk at a level which is acceptable to the Group. Control of the model risk consists of determining the mechanisms used to diagnose the model risk level and tools for reducing the level of this risk. The tools used to diagnose the model risk include, in particular, a strategic limit of tolerance to the model risk and the threshold values of the model risk.

MONITORING	Monitoring of the model risk on a periodical basis is aimed at diagnosing the areas requiring management actions and includes, in particular: • updating the model risk level, • evaluating the utilization of the strategic limit of tolerance to the model risk and the threshold values of the model risk, • verifying the stage of implementation and evaluating the effectiveness of the implementation of the activities as part of the mitigation of the model risk.
REPORTING	The results of monitoring the model risk are presented periodically in the reports addressed to the RC, the Management Board, and the Supervisory Board. The reports contain a comprehensive model risk assessment, in particular: information about the degree of utilization of the strategic limit of tolerance to the model risk and about the level of the model risk (from a standalone and consolidated perspective), a model risk map, an evaluation of the effectiveness of the recommendations made to reduce the model risk level, proposed new management actions reducing the model risk (if any).
MANAGEMENT ACTIONS	The purpose of management actions is to form a model risk management process and to affect the level of this risk, in particular by determining acceptable risk levels and making decisions about the use of tools supporting model risk management.

MACROECONOMIC CHANGES RISK

DEFINITION	Risk of macroeconomic changes is a risk of deterioration of the financial situation of the Bank as a result of the adverse impact of changes in macroeconomic conditions.
MANAGEMENT OBJECTIVE	Identify macroeconomic factors having a significant impact on the Group's activities and taking actions to reduce the adverse impact of potential changes in the macroeconomic situation on the financial situation of the Group.
RISK IDENTIFICATION AND MEASUREMENT	Identification of risk of macroeconomic changes is to determine scenarios of the potential macroeconomic changes and to determine risk factors having the greatest impact on the financial situation of the Group. Risk of macroeconomic changes results from interaction of factors dependent and independent of the Group's activities. The Bank identifies the factors affecting the level of risk of macroeconomic changes during carrying out comprehensive stress-tests. The risk of macroeconomic changes materializes indirectly through other risks affecting the Group's operations. For the purpose of measuring the risk of macroeconomic changes the Group uses risk measures based on the results of comprehensive stress-tests, in particular: • financial result and its components, • capital adequacy measures and their components, • selected liquidity measures, • data on the quality of the loan portfolio.
CONTROL	Control of the risk of macroeconomic changes is aimed at striving to mitigate the adverse effect of potential changes in the macroeconomic situation on the financial position of the Group. Control of the risk of macroeconomic changes consists of determining the acceptable risk level tailored to the scale of the Group's operations, with the level of the risk of macroeconomic changes being assessed on the basis of the results of comprehensive stress tests. An acceptable level of the risk of macroeconomic changes is a situation in which stress test results do not point to the need to take any remedial measures.

MONITORING	Monitoring consists of, among other things, analyzing macroeconomic factors and the economic situation on a current basis and includes in particular: • changes in the macroeconomic situation, • the macroeconomic factors to which the Bank is sensitive, • stress test results, • the level of the risk of macroeconomic changes.
REPORTING	Reporting is provided in the form of additional information about the risk of macroeconomic changes which accompanies a quarterly report on capital adequacy, in which the stress tests were conducted. The reports are addressed to the ALCO, the RC, the Management Board, and the Supervisory Board.
MANAGEMENT ACTIONS	Management actions in particular consist of: • issuing internal regulation, • determining acceptable levels of risk, • proposals of actions aimed at reducing the level of risk in the event of elevated or high risk of macroeconomic changes occurrence.

CAPITAL RISK

DEFINITION	Capital risk is the risk of failing to ensure an appropriate level and structure of own funds, with respect to the scale of the Bank operations and risk exposure and, consequently, insufficient for the absorption of unexpected losses, taking into account development plans and extreme situations.
MANAGEMENT OBJECTIVE	Ensure an appropriate level and structure of own funds, with respect to the scale of the operations and risk exposure of the Group, taking into account of the assumptions of the Bank's dividend policy as well as supervisory instructions and recommendations concerning capital adequacy.
CONTROL	The purpose of the capital risk control is to strive to keep the Bank's and the Group's capital risk level low, i.e. below specific thresholds of adequacy measures. The control of the capital risk includes determining risk control measures adapted to the scale and complexity of the Bank's and the Group's operations, in the form of strategic tolerance limits and thresholds for capital adequacy measures. Maintaining the capital adequacy measures above thresholds ensure an appropriate capital buffer above supervisory minimum levels.
RISK IDENTIFICATION AND MEASUREMENT	The capital risk level for the Group is determined based on the minimum, threshold and maximum values of capital adequacy measures, amongst others, the total capital ratio and basic capital (Tier 1) ratio. In addition, threshold and maximum values are determined for capital adequacy measures, as an excess over the minimum values constituting strategic tolerance limits for the capital adequacy measures. The capital risk level is determined as follows: • low level – when all capital adequacy measures exceed the threshold values, • raised level – when at least one adequacy measure is lower than a threshold value and no capital adequacy measure is lower than the strategic tolerance limit, • high level – when at least one capital adequacy measure is lower than the strategic tolerance limit. Should a high level of capital risk be identified, the Bank takes measures to bring capital adequacy measures to a lower level, taking into account of the assumptions of the dividend policy as well as the supervisory instructions and recommendations concerning capital adequacy.
MONITORING AND REPORTING	The Bank regularly monitors and reports the level of capital adequacy measures in order to determine the extent to which the supervisory standards, thresholds and internal strategic limits are met, and to identify cases which require that capital emergency actions be launched. Reporting the levels of capital adequacy measures is performed on a monthly basis for the Management Board and on a quarterly basis for the Supervisory Board.
MANAGEMENT ACTIONS	Capital risk management is performed by: • determining and attaining the capital targets desirable for the Bank, • determining the internal limits for capital adequacy measures, • planning, monitoring and reporting the level and structure of equity, as well as capital adequacy, • allocating the requirement in respect of own funds and internal capital to individual business areas and customer segments in the Bank as well as individual companies in the Group, • evaluation of profitability of individual business areas and customer segments.

The main capital risk management tools include:

- dividend policy,
- issue of shares and share capital increase,
- issue of subordinated debt,
- allocating profits of the current period to own funds,
- loan protection instruments of selected loan receivables portfolios,
- restricting lending activities, including lending activities limits,
- sale of selected financial assets, and
- securitization of portfolio.

INSURANCE RISK

DEFINITION

Insurance risk is a risk of loss or of adverse change in value of insurance liabilities, due to inadequate pricing and provisioning assumptions (in particular for technical provisions).

IDENTIFICATION, MEASUREMENT AND RISK ASSESSMENT

The exposure to insurance risks is monitored and shaped in accordance with the adopted Risk Management Strategy.

In PKO Życie Towarzystwo Ubezpieczeń S.A., the dominant type of insurance risk differs depending on the type of product in the Company's portfolio:

- products with Insurance Capital Funds (UFK) – mainly the contracts withdrawal risk (a relatively short period of time after implementation of the UOKiK decision),
- protection products: mortality and claims risks as well as negative selection (decreasing risk),
- for all products – the risk associated with comparing expenses with income (unit costs).

The Company mitigates its exposure to the risks through:

- reinsurance of the mortality and claims risks in excess of a specified amount per risk and per insurance contract,
- retention campaigns,
- monitoring the quality of sales in order to achieve an improvement in the quality of sales,
- increasing the scope of cover for investment and protection products.

In 2015 and 2016, the risk of changes in the approach to surrender fees materialized partially. As a result of the proceedings of the UOKiK and the agreements concluded in 2015 and 2016 as a result of these proceedings, the Company estimated the changes in the distribution of future withdrawals. The amounts of the future surrender fees were also adjusted in accordance with the above agreement. The decisions made constitute the continuation of activities conducted by the Company so far, with regard to reducing the total surrender value of selected life insurance contracts with insurance capital funds. Up until the date of this report, no increase in contract withdrawals in excess of the assumptions for determining the Best Reserve Estimate was observed.

PKO Towarzystwo Ubezpieczeń SA (which commenced its operating activities in 2016) is exposed to the following types of insurance risk:

- unearned premium and reserve risk – mitigated through proportionate reinsurance, product structure,
- catastrophic risk – mitigated through catastrophic reinsurance,
- contract withdrawal risk – mitigated through retention measures.

The dominant type of risk is dependent on the type of product:

- multi-year loss of source of income insurance contracts – unearned premium and reserve risk,
- property insurance – catastrophic risk (flood).

The measurement of the insurance risk in Insurance Companies is performed, among other things, as part of the analysis of contract withdrawals, claims ratio analysis, the analysis of the amounts of assets to cover technical reserves (APR), and an annual analysis of shock scenarios – stress tests as part of the process of self-assessment of risk and solvency. PKO Życie Towarzystwo Ubezpieczeń SA and PKO Towarzystwo Ubezpieczeń SA have implemented the requirements arising from the new Solvency II system and have been calculating capital ratios under the new regime as from 1 January 2016, maintaining own funds at an adequate level.

MONITORING

As to mitigate the insurance risk exposure, PKO Życie uses among others:

	• reinsurance of risks (mortality, morbidity) • grace periods, • exemptions, • retention activities. Ceded reinsurance of PKO Życie is performed on the basis of: • obligatory-optional, quota share - surplus reinsurance treaties, on the basis of risk – premium, • optional reinsurance treaties, on the basis of risk – premium, • obligatory, proportionate reinsurance treaties, • obligatory catastrophic reinsurance treaties, • obligatory excess of loss reinsurance treaties. Facultative reinsurance is applied for all insurance agreements and risks not covered by obligatory – facultative reinsurance agreements, in which the sum on the gross risk exceeds agreed amount. In case of the new products and the risks, PKO Życie Towarzystwo Ubezpieczeń SA and PKO Towarzystwo Ubezpieczeń SA chose reinsurer, level of protection, conditions of the reinsurance, changes in concluded reinsurance contracts and concluding new reinsurance contracts in relation to the newly introduced to offer or modified insurance products and new risks.
REPORTING	Reporting on insurance risk is provided in the form of periodical reports to the Management Board and for the Asset and Liabilities Committee, the Local Risk Committee, and the Risk Committee of the Supervisory Board.

The assets to cover technical reserves (APR) remained at a sufficient level (over 100%) and had an appropriate structure. As at the end of 2016, the aggregate assets to reserves ratio amounted to 103% for PKO Życie Towarzystwo Ubezpieczeń S.A. and 140% for PKO Towarzystwo Ubezpieczeń SA.

RISK OF EXCESSIVE LEVERAGE

DEFINITION	The risk of excessive financial leverage is the risk resulting from vulnerability to threats due to financial leverage or conditional financial leverage that may require taking unintended action to adjust business plans, including an emergency sale of assets which could result in losses or result in the need for valuation adjustments of other assets.
MANAGEMENT OBJECTIVE	The objective of managing the risk of excessive leverage is to ensure an appropriate relationship between the amount of the core capital (Tier 1) and the total of balance sheet assets and off-balance sheet liabilities granted by the Group.
RISK IDENTIFICATION AND MEASUREMENT	The risk of excessive leverage materializes as a mismatch of scale of activities and structure of the sources of financing and insufficient equipment of Group's own funds. For the purpose of measuring the risk of excessive financial leverage, a leverage ratio is calculated as a measure of Tier 1 capital divided by the measure of total exposure and is expressed as a percentage rate. The leverage ratio is calculated on the reporting reference date. The leverage ratio is calculated both with reference to Tier 1 capital and in accordance with the transitional definition of Tier 1 capital.
CONTROL	The objective of the control of the risk of excessive leverage is to strive to maintain the Bank's risk of excessive leverage at an acceptable level. It covers a periodical review of the risk control mechanisms in the form of a tolerance limit, including its threshold value.
FORECASTING AND MONITORING	The following parameters are in particular subject to monitoring of the risk of excessive leverage: • value of the leverage ratio, • threshold of the risk of excessive leverage, • deviation of the leverage ratio from forecasts.
REPORTING	Reporting is performed on a quarterly basis. The reports on the level of the risk of excessive leverage are addressed to the RC, the Management Board, the Risk Committee of the Supervisory Board, and the Supervisory Board.
MANAGEMENT	The management actions concerning the risk of excessive financial leverage are identical to the

ACTIONS	management actions concerning capital risk. In the event of an increased risk, actions are taken to bring capital adequacy measures to a decreased level, taking into account the assumptions of the dividend policy as well as supervisory suggestions and recommendations concerning capital adequacy.

7.1.8 COMPREHENSIVE STRESS-TESTS

Comprehensive stress-tests are an integral part of the Group'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 Group to be material. They include an analysis of the impact of changes in the environment and the functioning of the Group on the Group's financial position, in particular: the income statement, statement of financial position, own funds, capital adequacy, including own fund requirements, internal capital, capital adequacy measures, and selected liquidity measures.

Comprehensive stress-tests for the Group's own use are carried out at least once a year in a three-year horizon, and for the Bank – every six months in a three-year horizon, taking into account changes in the value and structure of balance sheet 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.

7.1.9 CAPITAL ADEQUACY[15]

Capital adequacy is a process whose objective is to ensure that the level of risk which 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 Group and 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 balance sheet paying attention to optimizing 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 as well as the individual Group companies,
- assessing the profitability of the individual business areas and customer segments.

The main capital adequacy measures are:

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

The objective of monitoring the level of capital adequacy measures is to determine the degree of compliance with supervisory standards and to identify cases which require taking capital emergency action.

[15] Own funds for the purposes of capital adequacy are calculated in accordance with the provisions of the Banking Act and Resolution 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.

The basic regulations applicable in the capital adequacy assessment process are:

- Regulation of the European Parliament and Council (EU) No. 575/2013 dated 26 June 2013 on prudential requirements for credit institutions and investment firms amending Regulation (EU) No. 648/2012 (CRR Regulation),
- the Act of 29 August 1997 on Banking Law,
- the Act of 5 August 2015 on macroprudential supervision over the financial system and crisis management in the financial system (hereinafter referred to as 'the Act on macroprudential supervision').

In 2016, the levels of capital ratios were dependent, among other things, on the following supervisory decisions:

- on 10 October 2016, the Bank received the decision of the Polish Financial Supervision Authority on the identification of the Bank as another systemically important institution (O-SII) on the basis of the assessment of the Bank's systemic importance in accordance with the Act on macroprudential supervision and on the imposition of a buffer on the Bank of 0.75% of its total risk exposure calculated in accordance with Article 92(3) of Regulation (EU) No 575/2013,
- on 18 October 2016, the Bank received the decision of the Polish Financial Supervision Authority on the recommendation to comply with an additional own funds requirement in excess of the value arising from the requirements calculated in accordance with the detailed principles set out in the CRR. The PFSA recommended that the Bank should maintain its own funds to cover the additional capital requirement in order to hedge the risk arising from foreign currency mortgage loans to households, at the standalone level of 0.83 p.p., in excess of the total capital ratio, which should comprise at least 75% of Tier1 capital (which corresponds to a capital requirement of 0.62 p.p. in excess of the value of the Tier 1 capital ratio) and at least 56% of Tier 1 core capital (which corresponds to a capital requirement of 0.46 p.p. in excess of the value of the Tier 1 core capital ratio),
- on 5 December 2016, the Financial Stability Committee passed a resolution on a recommendation concerning maintaining the countercyclical buffer ratio at 0% and also decided to provide the European Systemic Risk Board with appropriate information about this buffer,
- on 30 December 2016 the Polish Financial Supervision Authority sent information to the Bank on the level of the additional requirement in respect of own funds exceeding the value following from the requirements calculated in accordance with the detailed principles specified in CRR. The amount of the additional capital requirement to secure the risk in respect of foreign currency mortgage loans to households, at the consolidated level: 0.79 p.p., for the total capital ratio; 0.59 p.p. for the Tier I capital ratio and 0.44 p.p. for the Tier I core capital ratio.

Pursuant to the CRR, the Group calculates requirements relating to own funds in respect of the following types of risk:

- credit risk – standardized approach,
- operational risk: of the Bank – in accordance with the basic indicator approach (BIA) in respect of the operations of the Bank's branch in the Federal Republic of Germany and the advanced measurement approach (AMA) in respect of the remaining operations conducted by the Bank, and for Group companies covered by prudential consolidation – in accordance with BIA,
- market risk – basic indicator approach.

The total requirement in respect of Bank's own funds comprises the sum of the own funds capital requirements in respect of:

- credit risk, including counterparty credit risk,
- market risk,
- risk of credit valuation adjustment (CVA),
- the risk in relation to exposures to a central counterparty (CCP),
- settlement and delivery risk,
- operational risk.

Table 25. Capital adequacy of PKO Bank Polski SA

	31.12.2016	31.12.2015
Own funds in total	**30 873**	**27 091**
Tier I capital	**28 350**	**24 608**
Tier I capital before regulatory adjustments and reductions, of which:	32 059	27 829
Share Capital	1 250	1 250
Other reserves	27 970	24 119
General banking risk fund	1 070	1 070
Retained earnings	1 770	1 390
(-) Goodwill	(1 160)	(1 102)
(-) Other intangible assets	(1 821)	(1 691)
Accumulated other comprehensive income	(709)	(136)
Deferred tax assets which depend on future profitability but are not related to temporary timing differences	(1)	(2)
Adjustments in Tier I basic capital due to prudential filters	31	(14)
Other adjustments in transitional period in Tier I basic capital	(49)	(275)
Tier II capital	**2 523**	**2 483**
Equity instruments and subordinated loans qualificated as Tier II capital	2 523	2 483
Requirements as regard own funds	**15 626**	**14 837**
Credit risk	14 271	13 658
Operational risk	656	663
Market risk	651	485
Credit valuation adjustment risk	47	32
Total capital adequacy ratio	**15.81%**	**14.61%**
Tier 1 capital ratio	**14.51%**	**13.27%**

In 2016 PKO Bank Polski SA Group maintained a safe capital base which exceeded the supervisory and regulatory limits.

8. REMUNERATION POLICY AND HUMAN RESOURCES MANAGEMENT

Remuneration policy in PKO Bank Polski SA and in the entities of the Group
Number of employees
Incentive system
Benefits for employees
Training policy
Benefits for supervisors and managers
Evaluation of the remuneration policy for the realization of its objectives

8.1 REMUNERATION POLICY IN PKO BANK POLSKI SA AND OTHER GROUP ENTITIES

The basic internal regulation regard of remuneration policy is the Collective Labour Agreement ('Zakładowy Układ Zbiorowy Pracy' - ZUZP) concluded with the company trade union organizations on 28 March 1994 (with subsequent amendments), under which employees of the Bank receive the following remuneration components:

- the base remuneration,
- additional remuneration for working overtime, as well as under conditions which are especially onerous and detrimental to health,
- bonuses and awards for special achievements in professional work.

Base salaries and additional benefits granted to employees are formed on the basis of job grading (grading categories assigned to specific organizational positions) and analysis of market remuneration in the banking sector.

Depending on the size of employment remuneration policy is defined in the rules of remuneration or in contracts of employment or only in contracts of employment. Additionally, the Collective agreement concluded with Committee of Trade Union functions in KREDOBANK SA - in 2015 the new deal for years 2015-2017 was reached.

In 2016 no significant changes were made to the remuneration policy.

8.2 NUMBER OF EMPLOYEES

As at 31 December 2016, the number of employees in the PKO Bank Polski SA Group amounted to 29 441 FTE, which constituted an increase of 220 FTE y/y. The change in the number of employees in the Group y/y resulted from the development of business activities and changes in the structure of the Group (primarily the purchase of RLPL companies).

Table 26. Number of employees in PKO Bank Polski SA and other Group entities (in number of full-time equivalents)

	31.12.2016	31.12.2015	31.12.2014	31.12.2013	31.12.2012	Change of number of employees 2016/2015
PKO Bank Polski SA	25 381	25 909	25 927	24 437	25 399	-529
Other entities of the Group	4 060	3 311	3 105	2 950	3 157	748
Total	**29 441**	**29 221**	**29 032**	**27 387**	**28 556**	**220**

During 2016, 363 employment contracts were terminated for reasons not relating to employees.
Employment was restructured in particular for the following reasons:

- reorganization in respect of the segregation of duties among units,
- an increase in the Bank employees' effectiveness,
- universalization of positions,
- changing the typology of branches,
- centralizing the tasks which had been conducted in field offices.

8.3 INCENTIVE SYSTEM IN PKO BANK POLSKI SA AND IN OTHER GROUP ENTITIES

PKO Bank Polski SA has a remuneration and incentive system, in which the level of variable component of the salary is determined by the degree of achievement of the targets set. It consists of four pillars:

I PILLAR, the so-called Management by Objectives (MbO) covers managerial and expert positions crucial for the Bank's key objectives. The MbO consists of granting bonus which depends on the quality and degree of completion of the tasks.

II PILLAR, the so-called Individual Bonus System (IBS) is the system of bonuses which depends on the degree of completion of specific tasks in the areas of sales and effectiveness. The system covers those employees who are performing business tasks, mainly in corporate and investment banking, as well as in debt collection.

III PILLAR, the so-called Sales Bonus System is aimed to positions in retail branches, which perform the sale of banking products.

IV PILLAR, the so-called Support Bonus System (SBS) includes other employees not covered by the system MbO, IBS and Sales Bonus System.

Regardless of the bonus system there is a system of rewarding employees, under which the Bank creates a prize fund for the purpose of:

- individual discretionary awards to employees of the Bank, deriving outstanding results in their work or for achievements, which led to results important for the Bank, and
- awards in competitions relating to performance.

In addition, in accordance with the Resolution No. 258/2011 of the Polish Financial Supervision Authority, Directive No. 2013/36/EU of the European Parliament and the Council, and delegated Regulation No. 604/2014 of the European Commission, the Bank introduced separate regulations fixing the variable salary components policy, applicable to persons on managerial positions.

The PKO Bank Polski SA Group entities have incentive and remuneration systems in which the degree of achievement of individual targets determines the bonus. The procedure for target setting and belonging to the particular system depends on performed tasks including sales tasks and the size of the Company. Management of most of the entities from the PKO Bank Polski SA Group and the directors of selected Group entities are covered by the Management by Objectives System MbO.

Moreover, in connection with the resolution of the Polish Financial Supervisory Authority No. 258/2011, Directive No. 2013/36/EU of the European Parliament and Council, and Commission Delegated Regulation No. 604/2014 in 2016 rules and regulations were implemented in selected companies of the PKO Bank Polski SA Group which determined policies regarding variable remuneration components. The Regulations on variable remuneration components for members of Management Boards ('Regulaminy zmiennych składników wynagrodzeń dla członków Zarządu') were used in: PKO Leasing SA, PKO Towarzystwo Funduszy Inwestycyjnych SA, PKO BANKOWY PTE SA, PKO Życie Towarzystwo Ubezpieczeń SA, PKO Towarzystwo Ubezpieczeń SA and PKO Bank Hipoteczny SA. Moreover, in PKO Życie Towarzystwo Ubezpieczeń SA, PKO Towarzystwo Ubezpieczeń SA and PKO Bank Hipoteczny SA, the rules for variable remuneration components covered employees in selected management positions.

At the same time, due to the changes in the regulations applicable in investment fund management companies – in particular in connection with the entry into force of Art. 47a (1) of the Act of 27 May 2004 on investment funds and on managing alternative investment funds, as well as the Decree of the Minister of Finance of 30 August 2016 on detailed requirements for remuneration policies in investment fund management companies – on 2 December 2016, the Supervisory Board of PKO Towarzystwo Funduszy Inwestycyjnych SA, adapted the remuneration rules with regard to variable remuneration components for both members of the Management Board and employees of the Management Company to the requirements of the aforesaid Act and Decree.

In 2016, Raiffeisen-Leasing Polska SA applied the rules for variable remuneration components stipulated in the Corporate guidelines - Remuneration rules based on CRD IV Directive, applicable at Raiffeisen-Leasing Polska SA ('Wytyczne korporacyjne – Zasady wynagradzania oparte na dyrektywie CRD IV, Raiffeisen-Leasing Polska SA') in line with the rules applicable in the Raiffeisen Bank International AG Group, based on the EU regulations and Austrian Banking Act. Members of the Company's Management Board were covered by the aforesaid rules.

8.4 BENEFITS FOR EMPLOYEES

Employee Pension Programme Medical care Group insurance My Benefit Social benefits

EMPLOYEE PENSION PROGRAMME

As of July 2013, the Employee Pension Programme (EPP) functions at the Bank. The EPP was introduced in the form of a contract on the Bank making basic and additional contributions on behalf of the employees to investment funds managed by PKO Towarzystwo Funduszy Inwestycyjnych SA.

In 2016 Employee Pension Programmes (PPE) were functional in PKO BP BANKOWY PTE SA, PKO Towarzystwo Funduszy Inwestycyjnych SA, PKO Życie Towarzystwo Ubezpieczeń SA, PKO Leasing SA and PKO BP Finat Sp. z o.o.

MEDICAL CARE

The Bank ensures its employees additional healthcare- besides occupational health services which are compulsory according to the regulations of the Polish Labour Code. Employees are entitled to various packages, addressed to particular groups of jobs. Empoyees may benefit from a health promotion programme called 'Zdrowie jak w Banku', covering, i.a. a preventive health check and activities directed at health-oriented education and promoting a healthy life style.

Most PKO Bank Polski SA Group companies ensure their employees – apart from occupational medicine benefits – additional healthcare benefits according to universal or differentiated benefit packages, depending on the policies adopted by the companies.

Group insurance

Employees are entitled to join the cost-effective group insurance. The fee is being incurred by the Bank.

My Benefit

The Bank gives its employees the possibility of using the cafeteria system called MyBenefit as part of which each employee of the Bank may use the funds allocated to him/her from the Company Social Benefits Fund via an online platform on his/her own. The platform offers a broad range of benefits for the employees to choose from.

The amount of funds received to be spent at the cafeteria is dependent on the amount of gross income per person in a given family.

Social benefits

In accordance with the Act of 4 March 1994 on the Company Social Benefits Fund, the aid granted out of the Company Social Benefits Fund to the Bank's employees and former employees (pensioners, people receiving pre-retirement benefits) and members of their families in 2014 was earmarked for the following purposes:

- various forms of holidays,
- promotion of education, cultural and sport activities,
- day carers or nannies looking after children in day care centers, children's clubs, and kindergartens, and other forms of pre-school education;
- provision of material aid – in-kind or financial aid, as well as aid for housing purposes under terms and conditions set out in agreements.

The purchase of benefits 1-2 is possible through a modern Internet platform.

8.5 Training policy

All actions taken as a part of the training policy support the execution of the Bank's strategy and are adapted to the current needs of the employees and the possibilities of the organization. The training policy implemented in companies in the PKO Bank Polski SA Group is aimed at ensuring the professional development of the staff, including the adaptation of their knowledge and competencies to the changing legal and macroeconomic environment.

Objectives of the training projects executed in PKO Bank Polski SA are especially:

- development of employees' competencies in line with the PKO Bank Polski SA agenda,
- increasing commitment to the performance of business tasks
- improvement of skills associated with selling techniques,
- maintaining the highest possible customer service quality,
- supporting the positive attitude to changes among the Bank's employees,
- advancement of the bank's values.

The Bank offers its employees various forms of improving their professional qualifications. A team of internal trainers provides group, work station training sessions and internal workshops directed at developing sales competencies, product and application knowledge. At the same time, external training firms with which the Bank has signed framework contracts, provide comprehensive development programmes aimed at increasing the level of soft and hard competencies, and increasing specialist knowledge available on the market. In 2016 a total of over 95 796 participants took part in the training organized by PKO Bank Polski SA, which means that one Bank employee on average participated in 4 training sessions.

The internal e-learning platform is actively used by the Bank, mainly for the purpose of training in products, processes and servicing IT platforms. In 2016, 215 920 participants availed themselves of e-learning formula training.

The internal gamification platform, which was implemented in the Bank in 2016, proved to be an additional support in developing employees' knowledge and skills in retail sales. This platform allows employees to increase their product knowledge and develop their sales skills by participating in training exercises prepared for them in the modern and engaging formula of a business game.

The training courses and workshops conducted at the Bank are addressed to the employees of PKO Bank Polski SA and the network of agencies of PKO Bank Polski SA. This allows the employees of the Bank and the agency network to make use of high quality training courses carried out in line with the training methodology and standards of the Bank. Moreover, the framework agreements signed with training companies offer attractive terms and conditions, including training rates.

The Bank provides catalogue training sessions which are available to all the Group's employees using external firms and with the support of the Bank's internal trainers. The said training sessions improve the soft competencies of PKO Bank Polski SA and knowledge from the area of project management and Ms Office tools. In 2016 a total of 1203 PKO Bank Polski SA Group employees availed themselves of catalogue training sessions.

In 2016 two important training/development projects were realized at the Bank:

- New Manager Programme – adaptation programme for new Bank's managers - 182 new managers took part in it,
- The PKO Bank Polski SA Talents Programme – a two-year training and development programme addressed to selected Group employees. In 2016, 126 employees participated in training sessions, workshops and the event summarizing the programme.

Apart from training and development programmes, tailor-made internal workshops are realized at the Bank. They are aimed at building commitment in teams and improving the business activities of individual units (processes, communication, collaboration, business results, etc.). In 2016, a team of internal moderators completed workshops for 523 employees of the Bank.

In connection with the market's business requirements and the Bank's strategy, in 2016 the following training actions were performed:

- adaptation training sessions for employees of the retail sales network in all businesses - 2010 training participants,
- comprehensive training programme for all employees of the retail sales network – New Sales Rhythm,
- implementation of the OFWCA examination allowing to gain the status of an individual person performing agency activities related to the sale of insurance products - employees of the agency network of PKO Bank Polski SA – 640 participants,
- dedicated training programmes for employees from the corporate relations division, such as: recognizing customers' financial needs based on their financial statements, financial analysis of enterprises – advanced level with a final exam, securing the bank's credit receivables – 588 participants,
- dedicated training sessions for employees of the corporate branch in Frankfurt: cross-culture training, compliance with als 1-Mann-Abteilung, foreign banks in Germany, administrator Schulung, administrator Schulung, aufbau Seminar fur Compliance, workshop Geldwasche Fallbeispiele, sales up Training on the Job,
- specialist training in the serviced IT systems – in 2016 a total of 468 persons participated,
- e-learning training sessions for the Bank's auditors: practical aspects of applying the Act on reversed mortgage loans, tax carousel, scope of inspections in branches with reference to FATCA (Foreign Account Tax Compliance). A total of 433 persons participated in those three trainings.

8.6 Benefits for supervisors and managers

Principles of remuneration of the Bank's Management Board members

According to principles of remuneration of the Bank's Management Board members drew by the Supervisory Board, members of the Bank's Management Board are entitled to:

- monthly remuneration at an amount determined by the Bank's Supervisory Board for each member of the Bank's Management Board,
- benefits payable to employees of the Bank (excluding benefits payable to employees under Works Collective Agreements – Zakładowe Układy Zbiorowe Pracy - ZUZP):

- under the common binding laws,
- under the Bank's internal regulations, with standardized or exceptional character, for which the grant basis is not an evaluation of the Member of the Bank's Management Board work effects or the result of the area supervised by him.

- variable remuneration components for the results of work, in particular bonuses, awards for outstanding achievements, severance related to the termination of the employment not higher than 3 times the basic salary, which detailed rules of granting and withdrawal determines the 'Regulations of the variable components of remuneration for the members of the Board' adopted by the resolution of the Supervisory Board - taking into account the requirements of relevant legislation on the variable components of the remuneration of employees in banking institutions in positions that have a significant impact on the risk profile,
- Bank-financed insurance, in particular in respect of death and serious illness, permanent disability, permanent or long-term damage to health, incapacity for work (detailed scope of insurance will result from the insurer's offer and conditions negotiated by the Bank).

Table 27. Remuneration for the Management Board Members paid out in 2016 (in PLN thousand)

No.	Position	Remunaration				Other salary components						Post-employment benefits				Total	
		fixed		variable		additional insurance		PPE		health care and social fund		holiday pay	non-competition	severance fee	PPE+health care		
		2016	2015	2016	2015	2016	2015	2016	2015	2016	2015	2016	2016	2016	2016	2016	2015
1.	**Zbigniew Jagiełło** President of the Management Board in charge of the President of the Management Board Division, Legal Division and Compliance	1 951	1 892	948	875	40	40	88	84	1	1	0	0	0	0	3 029	2 892
2.	**Piotr Alicki** Vice-President of the Bank's Management Board in charge of IT and Services	1 219	1 419	741	651	33	40	60	63	1	1	405	244	366	12	3 081	2 175
3.	**Janusz Derda** Vice-President of the Bank's Management Board in charge of IT and Services	55	0	0	0	0	0	0	0	0	0	0	0	0	0	55	0
4.	**Bartosz Drabikowski** Vice-President of the Bank's Management Board in charge of Finance and Accounting	1 626	1 577	804	742	39	39	74	71	2	1	0	0	0	0	2 544	2 429
5.	**Maks Kraczkowski** Vice-President of the Bank's Management Board in charge of International and Transaction Banking and Cooperation with Self-Government Bodies and Government Agencies	683	0	0	0	14	0	0	0	1	0	0	0	0	0	698	0
6.	**Mieczysław Król** Vice-President of the Bank's Management Board in charge of Insurance Banking	786	0	0	0	18	0	0	0	1	0	0	0	0	0	805	0
7.	**Piotr Mazur** Vice-President of the Bank's Management Board in charge of Risk Management	1 463	1 419	619	532	40	40	64	60	1	1	0	0	0	0	2 187	2 051
8.	**Jarosław Myjak** Vice-President of the Bank's Management Board in charge of Insurance Banking	364	1 400	590	595	9	46	18	57	3	1	609	731	0	29	2 354	2 099
9.	**Jacek Obłękowski** Vice-President of the Bank's Management Board in charge of Retail Market	367	1 419	734	648	10	46	20	63	1	2	825	731	0	39	2 727	2 179
10.	**Jakub Papierski** Vice-President of the Bank's Management Board in charge of Corporate and Investment Banking	1 446	1 419	757	696	43	43	64	65	1	1	0	0	0	0	2 310	2 223
11.	**Jan Emeryk Rościszewski** Vice-President of the Bank's Management Board in charge of the Retail Market	629	0	0	0	0	0	0	0	1	0	0	0	0	0	629	0

VARIABLE COMPONENTS OF REMUNERATION OF BOARD MEMBERS AND KEY MANAGERS WITH A HIGH IMPACT ON THE BANK'S RISK PROFILE (MATERIAL RISK TAKERS - MRT)

In accordance with the requirements of the CRD IV and the Decree No. 604/2014 supplementary to the directive of the European Parliament and the Council 2013/36/EU with regard to regulatory technical standards with regard to quality criteria and appropriate quantitative criteria for determining categories of staff whose professional activities have a material impact on the risk profile of the institution dated March 4, 2014, Bank updated rules, previously implemented in 2012 for determining the variable remuneration components of MRT - through resolutions:

- Supervisory Board - variable components of remuneration policy under the name of 'Rules of the variable components of the remuneration of persons holding managerial positions at the Bank' (which are the basis of further regulation) and 'Rules of the variable components of the remuneration for the members of the Board',
- Board of Managers – 'Rules of the variable components of the remuneration for persons holding managerial positions.'

The rules and derived regulations of remuneration describe the procedure of granting MRT variable components of remuneration related to the results and effect of their work - awards for special achievements in work and bonuses.

The basis for awarding variable remuneration components are primarily premium targets assigned by the Management by Objectives (MbO).

The adopted objectives are to guarantee accounting for the Bank's business cycle and the risk related to its business operations. The risks are accounted for both by determining appropriate risk-sensitive criteria for assessing work effectiveness, and reducing or eliminating bonuses in the event of deteriorating financial results, the Bank's loss or deterioration in other variables (malus).

Variable components of remuneration for the evaluation period (calendar year) are awarded after the settlement of bonus purposes in the form of:

- not deferred – in the amount of 60% of the variable remuneration (in the first year after a period of assessment),
- deferred – 40% of the variable remuneration (in equal instalments over the next three years after the first year after a period of assessment).

wherein both the non-deferred and deferred salary is awarded in equal parts in cash and in the form of a financial instrument, i.e. the phantom shares (whose conversion into cash according to the updated of the prices of shares of the Bank is carried out after a period of retention and in the case of deferred compensation - after a period of deferral).

In case the amount of variable remuneration for the year exceeded PLN 1 million, PLN 400 thousand plus 60% of the excess over the amount of PLN 1 million is subject to deferral.

Variable remuneration may not exceed 100% of the annual fixed salary for managerial positions and 70% for members of the Management Board. At the request of the Supervisory Board the limit of variable remuneration for employees who are not members of the Board can be raised up to 200% of fixed remuneration for investment banking jobs - subject to approval by the General Meeting of Shareholders.

Each of the components of accrued variable compensation may be reduced as a result of the following:

- misconduct,
- failure to observe the law or standards of customer service,
- improper perform their professional duties,
- behaviour in relation to other employees violating the rules of social coexistence.

The bonus amount:

- for member of the Board may be adjusted in minus or in plus by the certain rate - depending on the achieved results of the Bank specified in the Bank's Annual Note (a set of key indicators of management specified for a given calendar year),
- for MRT who is not a member of the Board it may be adjusted in plus by certain rate depending on the results of the Bank specified in the Bank's Annual Note.

In the case of members of the Board granting and payment of variable remuneration is conditional to approval of the financial statements for the period of evaluation by the General Meeting of Shareholders.

In case of:

- significant deterioration in the Bank's results,
- assessment of a significant negative change in equity,
- violation of law or commitment of significant errors by MRT,
- adjustment of implementation and completion degree of results or objectives of MRT,
- performance deterioration of supervised or managed structures,
- granting of variable remuneration on the basis of incorrect, misleading information or MRT fraud it is possible to use - respectively by the Supervisory Board or Board of Directors – malus-type solution reducing the size of the due variable compensation deferred in subsequent accounting periods.

Material Risk Takers may avail themselves of healthcare services financed by the Bank, the social benefit fund, and employee pension programmes (PPE). Additionally, Members of the Bank's Management Board are entitled to insurance financed by the Bank, in particular death insurance, terminal illness insurance, permanent handicap insurance, permanent or long-term detriment to health insurance, inability to work insurance.

In case of granting the MRT severance related to the withdrawal from the function associated with the termination of employment (other than resulting from generally applicable laws) its sum reflects the assessment of the work in the last three years of employment. The Bank's internal regulations stipulate the maximum amount of severance pay.

Members of the Board and selected MRT are additionally covered by non-competition agreements. The agreements provide payment of the required labour law damages for refraining from hiring at competition after the termination of employment at the Bank.

Information on availability of non-monetary remuneration components to individual members of the Board of Directors

Members of the Board and key managers of the Bank are entitled to the non-financial benefits that are available to all employees, i.e.: medical care, PPE, group insurance and cafeteria system - MyBenefit and other benefits from the Company's Social Benefits Fund.

Insurance conditions - Members of the Management Board are entitled to Bank-financed insurance, in particular for the death of serious illness, permanent disability, permanent or long-term damage to health and inability to work.

Members of the management board may also join cost-effective group insurance offered to employees, for a fee paid by employees through the Bank.

Principles of the remuneration of Supervisory Board members

Ordinary General Shareholders' Meeting of PKO Bank Polski SA by the Resolution No. 36/2010 of 25 June 2010 established the monthly salary for members of the Supervisory Board of:

- Chairman of the Supervisory Board – PLN 16 thousand,
- Deputy-Chairman of the Supervisory Board – PLN 14 thousand,
- Secretary of the Supervisory Board – PLN 12 thousand,
- Member of the Supervisory Board – PLN 10 thousand.

Supervisory Board members are entitled to remuneration regardless of the frequency of meetings convened.

Regardless of the remuneration, the Members of the Supervisory Board are entitled to reimbursement of the costs incurred in connection with performing the function, and in particular travel costs from the place of residence to the location of the Supervisory Board's meeting and back, costs of accommodation and board.

Table 28. Supervisory Board members remuneration (PLN thousand)

	2016	2015
Board of Directors		
Remuneration received, due or potentially due from PKO Bank Polski SA	1 267	1 197
Remuneration received, due or potentially due from subsidiaries*	0	0
Total remuneration received, due or potentially due	1 267	1 197

* Other than Treasury of State and its subsidiaries

Short-term benefits include employee benefits, which are fully settled before the elapse of 12 months from the end of the annual reporting period in which the employees performed the work related to them.

Additionally, in 2016 an agreement was concluded for lending cars to Members of the Supervisory Board to enable them to perform their duties and for private purposes.

Full information regarding the remuneration components and other benefits on behalf of the members of the Management Board of PKO Bank Polski SA and the Supervisory Board in the reporting period has been presented in the Financial Statements of PKO Bank Polski SA for the year ended 31 December 2016 (note 49).

AGREEMENTS CONCLUDED BETWEEN THE ISSUER AND MANAGING PERSONS

Within the meaning of § 2 clause 1 item 30a of the Decree of the Minister of Finance of 19 February 2009 on current and periodical information submitted by issuers of securities and the conditions of considering as equivalent the information required by law of a non-member country (Journal of Laws No. 33, item 259 with subsequent amendments), members of the Management Board are persons managing the Bank.

In 2016, two agreements were signed with each of the members of the Management Board of PKO Bank Polski SA:

- an employment contract, providing for severance pay in the event of termination from reasons other than violation of the basic obligations arising from the employment relationship, in the amount of three monthly basic salaries,
- a non-competition agreement, providing for damages for complying with the noncompetition requirement during 6 months after termination of the employment relation, amounting to 100% of the monthly basic salary received before termination of the employment relation, to be paid monthly in arrears during the non-competition period.

8.7 EVALUATION OF THE REMUNERATION POLICY FOR THE REALIZATION OF ITS OBJECTIVES

Fixed remuneration Variable remuneration Non-remuneration benefits

In 2016 in connection with the requirements of the Articles of Association and the 'Principles of Corporate Governance for Supervised Institutions' the 'Assessment of functioning of the remuneration policy in PKO Bank Polski SA' was made and approved by the Supervisory Board. In drawing up the report, an assessment by an external advisor – EY Poland – was used.

The key components of the Bank's assessment are as follows:

1) The Bank's development and safety were ensured by the following actions:
- motivating employees to act in line with the Bank's interests,
- linking the amount of remuneration paid to the Bank's position,
- ensuring an appropriate level of control over the level of fixed and variable remuneration,
- and non-remuneration benefits.

2) The Bank pursued a policy of remunerating Members of the Management and Supervisory Boards, as well as key managers, which was specified in appropriate internal regulations verified in terms of consistency and transparency.
3) Members of the Management Board received remuneration adequate to the functions held and to the scale of the Bank's operations.
4) The Supervisory Board introduced regulations determining the principles for remunerating Members of the Management Board, supervised compliance with those policies and set criteria and conditions justifying the payment of variable remuneration, and verified them before paying it.
5) Variable remuneration of Members of the Management Board and key managers depended on achieving specified goals related to the Bank's strategy. Those goals covered quantitative and qualitative criteria and guaranteed motivating the respective staff to work and forms of behavior which enabled the Bank to achieve the assumed goals.

The amount of variable remuneration of all the employees depended on the level of achieving the said goals.

The Bank as an institution of public confidence conducted operations with utmost diligence and paid special attention to the professionalism and ethical behaviour of its employees. Therefore, the remuneration policy which constituted a significant component of the Bank's development and operating security was pursued by the Bank's Management Board with the active participation of the Supervisory Board.

The policy did not encourage taking excessive risk and – taking into consideration the Bank's financial position – was balanced, supported the pursuit of the Bank's strategic goals and its long-term development. This policy comprised three components described below, each of which met the requirements of the binding regulations.

FIXED REMUNERATION

In the process of awarding fixed remuneration, the Bank acted in accordance with particular internal position grading categories. These categories were determined using an independent and objective grading method. The positions were graded on a current basis, in particular in the case of material organizational changes in the Bank.

The Bank verified the adequacy of fixed remuneration by regular benchmarking of remuneration performed by external specialized entities.

To ensure safety and control over remuneration, the Bank took action to avoid specifying the level of remuneration above market level – at the same time avoiding excessive outflow of staff and increased costs of employee churn which could occur in the event of determining remuneration at a level lower than market level. To ensure the above, the Bank monitored fluctuation ratios in particular positions to potentially adjust the assumptions of the remuneration system should negative HR phenomena occur.

A limited and strictly determined group of employees defined in the Bank's internal regulations was entitled to define and change remuneration amounts.

VARIABLE REMUNERATION

The Bank regulated the process of awarding variable remuneration in: The principles of variable components of remuneration of persons in managerial positions within the Bank, 'Regulations of the variable components of remuneration for Members of the Management Board and MRT', and 'Principles of awarding bonuses to the Bank's employees'.

The process of awarding variable components of remuneration comprised mainly bonus aims specified for particular bonus pillars. The goals adopted were to guarantee accounting for the Bank's business cycle and the risk related to its business operations. All the goals resulted from the networks of goals approved by the Bank's Management Board which were mandatorily cascaded to employees of particular structures. MRT were additionally responsible for special projects aimed at pursuing the Bank's strategy.

MRT – as persons with particular impact on the level of safety and the Bank's stable development were subject to additional restrictions in the area of remuneration. Variable remuneration components were granted to MRT, including the Management Board, for the given evaluation period (calendar year) after settling the deferred and non-deferred bonus goals. To ensure permanency of the results reduction of deferred components of variable remuneration is possible in the event of deteriorated financial results, the Bank's loss or deterioration in other variables (malus).

Additionally, one-half of each component was paid in the form of a financial instrument linked to the Bank's share value. In the event of achieving good and stable results, the Bank's value increases which leads to an increase in the final cash disbursement. In the opposite situation, the cash disbursement may be reduced. This mechanism motivated MRT and Members of the Management Board to care for the results and development of the Group.

Bonuses were parametrized in consideration of the Bank's situation and financial sector market benchmarks. The Supervisory Board was authorized to parametrize bonuses (bonus ratios, bonus adjustment ratios, levels of goals achieved remunerated with bonuses) for the Management Board, and the President of the Management Board is exclusively authorized to parametrize bonuses for MRT.

As part of the completed projects key to the safety and development of the Bank dedicated motivational solutions were introduced on a periodic basis.

NON-REMUNERATION BENEFITS

The Bank offered abundant, comparable to market conditions, additional non-remuneration benefits. The benefits granted on the one hand motivated employees to care for the Bank's results, and on the other, they played a retention function thanks to which the continuity of the Bank's operations was ensured in respect of particular processes. Additionally, educational incentives granted as part of such benefits (training vouchers, additional funds for educational purposes) translated directly to the Bank's development through the development of its employees.

9. CORPORATE GOVERNANCE

Information for investors
Compliance with the rules for corporate governance

9.1 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

9.1.1 SHARE CAPITAL AND SHAREHOLDING STRUCTURE OF PKO BANK POLSKI SA

As at 31 December 2016, the share capital of PKO Bank Polski SA amounted to PLN 1 250 000 thousand and consisted of 1 250 000 thousand shares with a nominal value of PLN 1 each – shares are fully paid. In relation to the end of 2015 there were no changes in the share capital of PKO Bank Polski SA. All issued shares of PKO Bank Polski SA are not preferred shares.

Table 29. Share capital structure of PKO Bank Polski SA

Series	Type of shares	Number of shares	Nominal value of 1 share	Series amount by nominal value (PLN)
Series A	registered ordinary shares	312 500 000	PLN 1	312 500 000
Series A	bearer ordinary shares	197 500 000	PLN 1	197 500 000
Series B	bearer ordinary shares	105 000 000	PLN 1	105 000 000
Series C	bearer ordinary shares	385 000 000	PLN 1	385 000 000
Series D	bearer ordinary shares	250 000 000	PLN 1	250 000 000
		1 250 000 000		**1 250 000 000**

To the best knowledge of PKO Bank Polski SA, as at 31 December 2016 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 30. Shareholding structure of PKO Bank Polski SA

Shareholders	As of 31.12.2016		As of 31.12.2015		Change in the share in the total number of votes at the GSM (pp.)
	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[1)]	83 952 447	6.72%	83 952 447	6.72%	-
Nationale-Nederlanden Otwarty Fundusz Emerytalny (till 23.06.2015 ING Otwarty Fundusz Emerytalny)[2)]	64 594 448	5.17%	64 594 448	5.17%	-
Other shareholders[3)]	733 534 125	58.68%	733 534 125	58.68%	-
Total	1 250 000 000	100.00%	1 250 000 000	100.00%	-

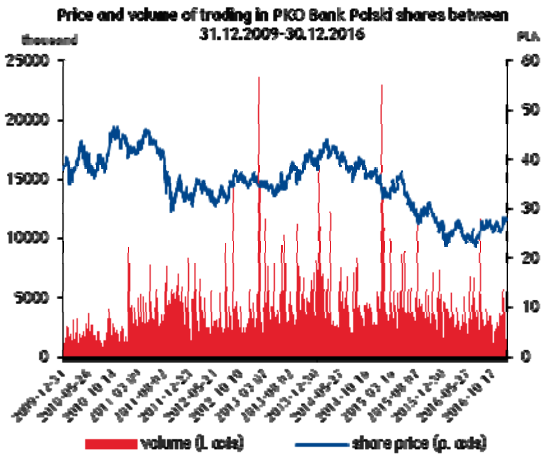
1) holdings of shares as at 29 January 2013, as reported by Aviva OFE after exceeding the threshold of a 5% interest in PKO Bank Polski SA following the settlement of the sale of 153.1 million shares in PKO Bank Polski SA by BGK and the State Treasury.

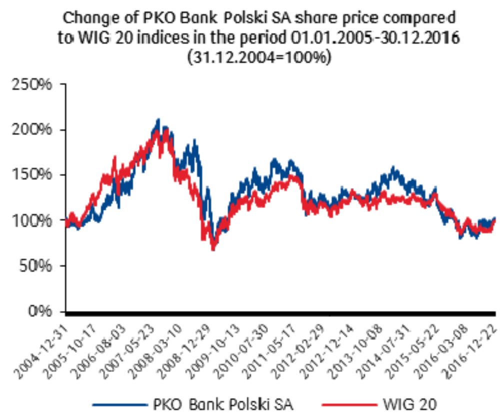
2) holdings of shares as at 24 July 2012, as reported by ING OFE (currently: Nationale-Nederlanden OFE) after exceeding the threshold of a 5% interest in PKO Bank Polski SA following the settlement of the sale of 95 million shares in PKO Bank Polski SA by the State Treasury.

3) including Bank Gospodarstwa Krajowego, which as at 31.12.2015 held 24,487,297 shares representing a 1.96% share in the total votes at the GSM.

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

9.1.2 SHARE PRICE OF PKO BANK POLSKI SA AT THE WARSAW STOCK EXCHANGE





The price of PKO Bank Polski SA's shares increased by 3% in 2016, whereas:

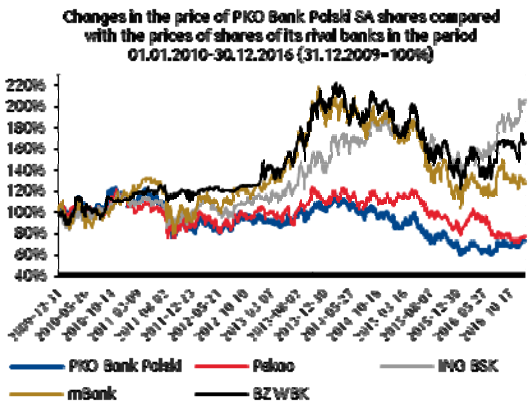
- the prices of: PEKAO SA's shares decreased by 12.3%, ING BSK SA's shares increased by 37.8%, BZ WBK SA's shares increased by 11.3%, mBank's shares increased by 6.8%,
- WIG20 and WIG Banki indices increased by 4.8% and 2.9%, respectively.

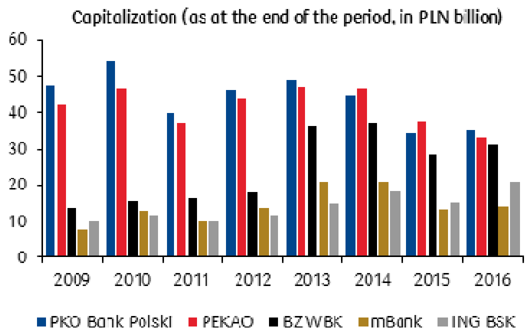
Such changes in the prices of the banks' shares at the WSE, including the prices of PKO Bank Polski SA's shares, were mainly due to:

- regulatory factors - in particular, the introduction of an additional burden, i.e. the bank tax, at the beginning of the year (which imposed a significant burden on the banking sector's profit). On the other hand, the banks' financial results improved as a result of a one-off inflow of funds from the transaction with Visa. The banks' share prices were also affected by the planned regulatory solutions concerning borrowers having housing loans in CHF,
- market factors - in particular, the historically low interest rate levels. Stable economic growth had a positive effect on banking activities.

Despite the prevailing adverse market factors, which have a structural effect on the profitability of the banking sector in Poland, the Bank focuses on achieving business results that are attractive for investors and adjusting its operational model to the new market environment in order to guarantee return on equity that exceeds the cost of equity, and thus to create value for the shareholders.

THE PKO BANK POLSKI SA'S SHARE PRICE AND CAPITALIZATION COMPARED TO COMPETITORS





9.1.3 LIMITATIONS ON THE SHARES OF PKO BANK POLSKI SA

All the shares of PKO Bank Polski SA carry the same rights and obligations. None of the shares are preference shares, in particular in relation to voting rights and dividends. The Memorandum of Association of PKO Bank Polski SA restrict the voting rights of shareholders holding more than 10% of the total number of votes at the General Shareholders' Meeting and forbids those shareholders to execute more than 10% of the total number of votes at the General Shareholders' Meeting. The above limitation does not apply to:

- those shareholders who on the date of passing the resolution of the General Shareholders' Meeting introducing the limitation of the voting rights had rights from the shares representing more than 10% of the total number of votes at the Bank (i.e. the State Treasury and BGK),
- shareholders who have the rights from A-series registered shares (the State Treasury), and
- shareholders acting jointly with the shareholders referred to in point (ii) based on an agreement concerning the joint execution of voting rights from shares. Moreover, limitation of the voting rights shall expire when the share of the State Treasury in the Bank's share capital drops below 5%.

In accordance with § 6 clause 2 of the PKO Bank Polski SA's Memorandum of Association, the conversion of A-series registered shares into bearer shares and the transfer of these shares requires an approval of the Council of Ministers in the form of a resolution. Conversion into bearer shares or transfer of A-series registered shares, after getting the above mentioned approval, results in the expiry of the above mentioned restrictions in respect of shares subject to conversion into bearer shares or transfer, to the extent to which this approval was given.

Pursuant to Art. 13, clause 20 of the Act on Public Property Management, the shares of PKO Bank Polski SA held by the State Treasury cannot be sold. Furthermore, under Art. 14 of the above-mentioned Act, the shares of PKO Bank Polski SA (which has been classified as significant for the Polish economy based on the Decree of the Prime Minister on the list of companies significant for the Polish economy) held by the State Treasury cannot be donated to a local administrative unit or an association of local administrative units.

9.1.4 ASSESSMENT OF FINANCIAL CREDIBILITY OF PKO BANK POLSKI SA

Rating of PKO Bank Polski SA Rating of PKO Bank Hipoteczny SA Rating of KREDOBANK 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 2016.

Moody's Investors Service Rating

On 16 May 2016 rating agency Moody's Investors published at www.moodys.com a press note which confirmed ratings for Bank's both long- and short-term deposits at A2/P-1, liabilities at A3 and corrected perspective of Bank's long-term deposits on negative from stable. At the same time agency has maintained a stable perspective for Bank's long-term liabilities. Perspective correction of Bank's long-term deposits was the consequence of similar correction of rating for Poland. According to notes:

- long-term deposit rating was held at A2 level, perspective was corrected to 'negative' from 'stable',
- short-term deposit rating was held at P-1 level,
- rating for senior unsecured liabilities was held at A3 level, perspective was hold as 'stable',
- MTN programme liability rating was held at (P)A3 level,
- rating of other short-term liabilities was held at (P)P-2 level,
- counterparty risk rating was held at A2(cr)/P-1(cr) level.

In the note Moddy's agency informed that Bank's deposit and liabilities rating were held intact due to agency's expectation of continuous moderate support from the government. Intact ratings for Bank are connected with good quality of assets and adequate level of write-downs of impaired loans, which parameters improved in recent years. At the same time, Moody's indicated that the Bank has strengthened its capital base.

Table 31. Ratings as of 31 December 2016 (paid rating)

Moody's Investors Service	
Long-term deposit rating	A2 with a negative outlook
Short-term deposit rating	P-1
Senior unsecured debt rating	A3 with a stable outlook
Rating of the MTN Program Liabilities	(P)A3
Short-term liabilities rating	(P)P-2
Long-term counterparty risk assessment	A2(cr)
Short-term counterparty risk assessment	P-1(cr)

Standard and Poor's Rating

On 19 January 2016, the rating agency Standard and Poor's withdrew its ratings issued for the Bank at the Bank's request submitted on 17 December 2015. The Bank terminated its agreement with Standard and Poor's and requested the withdrawal of its ratings due to the limitation of its plans concerning bond issues on international markets, in particular in the United States. The agreement was terminated due to the fact that the current structure of the Bank's balance sheet and the related plans for obtaining medium- and long-term financing provide for issues of bonds mainly on the Polish and European markets (primarily in EUR). Therefore, paid ratings issued by just one rating agency are sufficient for the execution of the Bank's financial plans. Another important reason for terminating the agreement with Standard and Poor's in 2015 was the need to reduce the Bank's operating expenses, which was particularly important given the low interest rates and regulatory changes.

In connection with withdrawing its ratings, Standard and Poor's performed a final analysis of the Bank's current situation and its business environment and on 19 January 2016 confirmed the short-term rating 'A-2' and lowered the long-term rating from 'BBB+' to 'BBB'. At the moment of withdrawal of the ratings, the outlook was stable. Standard and Poor's informed that the Bank's long-term rating was lowered due to the fact that the sovereign credit ratings of Poland were lowered on 15 January 2016. In its analysis, the agency stated that the Bank had a strong business position, adequate capital strength and liquidity in the perspective of the following 2 years, appropriate asset quality and a solid financing base, mainly based on retail deposits.

RATING OF PKO BANK HIPOTECZNY SA

As at the end of 2016 PKO Bank Hipoteczny SA had the following ratings granted by Moody's Investors Service (paid rating):

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

RATING OF KREDOBANK SA

As at the end of December 2016 KREDOBANK SA had the following ratings granted by Standard & Poor's on 26 April 2016 (paid):

- long-term international scale credit rating - CCC+,
- positive outlook,
- short-term international scale credit rating - C,
- rating on a Ukrainian scale – uaBB-.

At the same time, on 25 October 2016 KREDOBANK SA filed an application with Standard & Poor's to withdraw the ratings (paid) granted to the Company. The Company's rating was withdrawn by the Agency on 1 February 2017. Upon withdrawing the rating, on 1 February 2017 the Agency confirmed the previous rating of the Company.

9.1.5 INVESTOR RELATIONS

The main goals of investor relations Activities in 2016 Evaluation of investor relation activities

PKO Bank Polski SA maintains regular contact with investors and financial market analysts. For investors and analysts, the main purpose of contact with the Bank's representatives is to receive answers to their questions concerning the Bank's operations in a broad sense, its financial results and the situation in the banking sector. The Bank allows various forms of contact preferred by the investors and analysts.

THE MAIN GOALS OF INVESTOR RELATIONS

In 2016, the Bank's investor relation activities focused on the following areas:

- strengthening a positive image of PKO Bank Polski SA as a reliable and transparent company among the existing and potential investors, financial market analysts and rating agencies, through the use of various market communication tools,
- providing exhaustive information on the Bank's financial results and activities, including changes in the market environment, in order to allow a reliable assessment of the Bank's current situation and perspectives, as well as the correct valuation of its shares,
- fulfilling the information duties of the Company as an issuer of securities, as required by the law,
- organizing the General Shareholders' Meeting and providing information to the Bank's shareholders,
- ensuring the Bank's cooperation with appropriate governmental bodies, organizations and capital market institutions in connection with the Bank's presence on the public securities market,
- adjusting its internal regulations to the MAR Regulation, which regulates the information obligations of public companies.

ACTIVITIES IN 2016

As part of market communication in 2016:

- after each quarter end, the Bank's and the Group's financial performance was presented by the Bank's Management Board in a meeting with capital market and debt securities analysts, organized on the Bank's premises, and during teleconferences in which ca. 65 analysts and representatives of investors participated each time,
- Management Board members and key managers regularly participated in meetings (and conference calls) with investors and analysts, both on the Bank's premises and during investor conferences; in 2016, there were approx. 60 meetings at the Bank and approx. 90 conference calls; additionally, the members of the Bank's Management Board answered the investors' questions during investor conferences organized both in Poland and abroad. In total, approx. 120 meetings took place in 2016 during 13 investor conferences organized in: the Czech Republic (one conference), France (one conference), Poland (three conferences), the United States (three conferences) and the UK (five conferences),
- the Investor Relations Office maintained on-going contacts with analysts and investors, both corporate and individual, by answering many questions asked by telephone or e-mail and relating to business operations and financial performance of PKO Bank Polski SA,
- all information significant for the Bank's investors and shareholders was promptly published on the Investor Relations website www.pkobp.pl/investors; the website was modified further in 2016 - new user-friendly functionalities were introduced, including a portal available in RWD technology, which allows the automatic adjustment of the page view to the device on which it is displayed,
- in 2016, the Bank again provided its online annual report for 2015 in the form of a dedicated website in two language versions: Polish and English (http://www.raportroczny2015.pkobp.pl/pkobppl-en). The annual report published in the form of a separate website fulfils the Bank's needs in the area of information and image: above all, it makes it easier to find key financial and business information on the PKO Bank Polski SA Group, which is provided in a user-friendly form,

- in 2016, the Bank followed the internal Information Policy Rules of PKO Bank Polski SA adopted by Management Board in December 2014 in contacts with investors and customers. In particular, the Rules define the scope and manner of communication, including communication channels and competencies in the area of information activities. In August 2016, the information policy was amended in order to adjust it to the provisions of the MAR, which regulates the information obligations of public companies.

EVALUATION OF INVESTOR RELATION ACTIVITIES

In 2016, for the fourth time in a row, PKO Bank Polski SA received 'The Best of The Best' award in the competition for the best annual report organized by Instytut Rachunkowości i Podatków (Accounting and Tax Institute). The award is granted for high quality of financial reporting. The completeness, consistency, clear and logical presentation of data were recognized.

In accordance with the 'Survey of analysts' satisfaction with cooperation with PKO Bank Polski conducted by Partner in Business Strategies, analysts value their cooperation with the Bank very highly. 94% of the respondents expressed positive opinions. The following elements of this cooperation received the highest evaluations: technical value of presentation for analysts and investors - 88% of positive evaluations, and the technical skills of the employees who contacted the analysts - 82%.

9.2 COMPLIANCE WITH THE RULES FOR CORPORATE GOVERNANCE

9.2.1 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'

In connection with Good Practices for Companies Listed on the WSE 2016, 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 Articles 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.

In 2016, the Bank incidentally violated rule IV.Z.17 contained in Good Practices for Companies Listed on the WSE 2016, 'The General Shareholders' Meeting and Investor Relations', which says that 'A resolution of the General Shareholders' Meeting on the payment of contingent dividend may only contain conditions that will be satisfied before the ex-dividend date.' In the resolution of the Annual General Meeting on distribution of profit for 2015 and unappropriated profit of prior years, dated 30 June 2016, the Bank did not apply this principle, because it contained conditions which could materialize after the dividend date. According to the aforesaid resolution, the decision on profit distribution was supposed to apply, unless the conditions stipulated in the resolution ('Meeting the Dividend Conditions') are met by 8 December 2016.

At the same time, the resolution set out the dividend date for 30 September 2016, and 9 December 2016 was the latest date by which the Management Board was obliged to adopt the resolution on Meeting the Dividend Conditions or failing to meet them. The deadlines set for Meeting the Dividend Conditions were determined taking into account all possible deadlines for presenting new supervisory requirements in respect of own funds and determining their impact on capital adequacy ratios as at 30 September 2016, which was, in turn, necessary to determine whether the Dividend

Conditions were met or not. The dividend payment date could not be earlier than the date of verification of whether the conditions for its payment had or had not been satisfied. Taking above into consideration, the dividend payment date was set on 20 December 2016. The Bank informed about the fact that this rule would not be observed in a report dated 30 June 2016.

The Code of Good Practice 2016 is publicly available at the website:
https://www.gpw.pl/regulations_best_practices.

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 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.

THE MOST IMPORTANT ACTIONS TAKEN BY PKO BANK POLSKI SA TO ENSURE COMPLIANCE WITH THE RULES AND RECOMMENDATIONS CONTAINED IN GOOD PRACTICES 2016 OF WSE LISTED COMPANIES

INFORMATION POLICY AND COMMUNICATION WITH INVESTORS

The Bank took actions aimed at ensuring that the recommendations and rules contained in this section of Good Practices 2016 of WSE listed companies are applied as extensively as possible, both in the area of communication with investors and providing modern communication channels for their use, and in the area of information policy and publication of the required information on the website.
PKO Bank Polski SA regularly contacts investors in various forms preferred by them. They can ask questions by e-mail, by telephone or during face-to-face meetings with the Bank's representatives. The Bank makes every effort to provide the financial results to investors as soon after the end of a reporting period as possible. Moreover, in accordance with the Good Practices 2016 of WSE listed companies, the financial statements of PKO Bank Polski Group contain information on sponsorship and charitable activities.
The Bank has also implemented internal regulations in respect of providing explanations and rectifying untrue, inaccurate or detrimental information published in the media.
In accordance with the Good Practices 2016, the Bank maintains its corporate website in two language versions: Polish and English. All information and corporate documents required by the Good Practices are published on the website, including the information on the application of the recommendations and rules provided in the Good Practices for Companies Listed on the WSE 2016.

MANAGEMENT BOARD AND THE SUPERVISORY BOARD

The rules and recommendations contained in this section were followed. Both the Management Board and the Supervisory Board adopted the Good Practices 2016 of WSE listed companies.
In particular, the members of the Bank's Management Board and Supervisory Board are highly qualified and experienced. The internal division of responsibilities for individual areas of the Company's business between the Management Board members is published on the Bank's website. Performing their functions in the Bank's Management Board was the main professional activity of the Bank's Management Board members in 2016.
The Supervisory Board members devoted a sufficient amount of time to performing their duties in 2016; 12 Supervisory Board meetings were held.
The required number of Supervisory Board members meets the independence criteria in accordance with the rules. In accordance with the Supervisory Board members' declarations, 7 members of the Supervisory Board, which consists of 9 members, are independent.
Furthermore, the Supervisory Board prepared and presented to the Annual General Shareholders' Meeting the required assessment of the Company's condition, the report on the activities of the Supervisory Board, the assessment of the fulfilment of the Bank's information obligations in the area of corporate governance, the assessment of the Bank's policy in the area of sponsoring and charitable activities.

INTERNAL SYSTEMS AND FUNCTIONS

The internal regulations and practices of the Bank satisfied all the requirements provided in this section of Good Practices 2016 of WSE listed companies.
In particular, the Bank's organizational structure is adequate to the scale and nature of its activities and risks. There are separate units dedicated to the individual systems and functions or parts thereof.

The Bank's internal regulations specify: the Management Board's responsibility for the internal control system and risk management system, direct subordination of persons responsible for risk management, internal audit and compliance to the President or another Management Board member, the possibility of reporting directly to the Supervisory Board or the audit committee, the application of independence rules with regard to the manager of the internal audit function and other persons responsible for that function.
In accordance with the Good Practices 2016 of WSE listed companies, the effectiveness of systems and functions is verified and monitored

General Shareholders' Meeting and Investor Relations

With respect to the organization of General Shareholders' Meetings, the Bank decided not to apply the recommendation concerning the opportunity to participate in General Shareholders' Meetings with the use of the means of electronic communication, unless the General Shareholders' Meeting makes appropriate amendments to the Bank's Articles of Association authorizing the Management Board to organize General Shareholders' Meetings with the use of electronic communication. This decision was made taking into account the organizational and legal risks associated with such method of communication.
The Bank also informed about an incidental violation of rule IV.Z.17 contained in Good Practices 2016, which says that 'A resolution of the General Shareholders' Meeting on the payment of contingent dividend may only contain conditions that will be satisfied before the ex-dividend date.'
In other respects the Bank General Shareholders' Meetings were organized in accordance with the requirements of the Good Practices 2016 of WSE listed companies.
In particular, the Bank took actions to ensure that, as far as possible, Annual General Shareholders' Meetings take place within a reasonably short period from the publication of the annual report. The places and dates of the Annual General Shareholders' Meetings (30 June 2016) and the Extraordinary General Shareholders' Meeting (25 February 2016) were set to allow the greatest possible number of shareholders to participate. Draft resolutions of the Annual General Shareholders' Meeting convened for 30 June 2016 were prepared and presented together with statements of grounds. During that General Shareholders' Meeting, no shareholders requested any matters to be put on the agenda or presented any draft resolutions with statements of grounds. The Extraordinary General Shareholders' Meeting was convened for 25 February 2016 at the request of the authorized shareholder - the State Treasury. The said shareholder presented draft resolutions with statements of grounds together with the request for convening the Extraordinary General Shareholders' Meeting.
The Bank also made available a real-time broadcast of both the Annual General Shareholders' Meeting and the Extraordinary General Shareholders' Meeting and allowed the media to be present.

Conflicts of interest and related party transactions

The internal regulations of PKO Bank Polski SA guarantee compliance with the recommendations and rules contained in this section. The Bank has adopted regulations concerning the management of conflict of interest, including the regulations concerning professional or other involvement that could lead to a conflict of interests. The Management Board and Supervisory Board rules and regulations define the principles for excluding their members from participation in matters associated with conflicts of interest. If a situation that could lead to a potential conflict of interest has occurred, the persons concerned are obliged to disclose the situation.
Moreover, the Bank has internal regulations in place for monitoring and restricting the possibilities of receiving benefits or gifts which could affect the independence and objectivity of decision makers or have an adverse effect on the independence of opinions and judgements.
Transactions with related parties and significant shareholders are concluded on an arm's length basis, in accordance with consistent and uniform policies, based on the Bank's internal regulations. Furthermore, at the Annual General Shareholders' Meeting in 2016 some amendments were made to the Articles of Association, in accordance with which the Bank cannot conclude a significant agreement with a shareholder holding at least 5% of the total number of votes at the Bank without the prior approval of the Supervisory Board. This requirement is not applicable to typical transactions or transactions concluded on an arm's length basis in the course of the Bank normal operating activities, if they are concluded with members of the Bank's group.

Remunerations

The Bank follows the principles of the Code of Good Practice of WSE Listed Companies 2016 with regards to remuneration. In accordance with the requirements of the Code, The Bank's Directors' Report includes a report on the remuneration policy with the elements specified in the Code of Good Practice of WSE Listed Companies and in the Decree of the Minister of Finance on current and periodical information submitted by issuers of securities and conditions for considering as equivalent, the information required under the legislation of a non-Member State.
In the Bank's opinion, the remuneration policy is connected with the strategy and short- and long-term goals, long-term interests and financial results, and takes into account solutions aimed at avoiding discrimination for any reason.
Remuneration of the Bank's Management Board members and key managers is directly linked to the Bank's financial situation and the growth of its value through appropriate bonus targets and payment deferral and suspension mechanisms.
In accordance with the Good Practices 2016 of WSE listed companies, the remuneration of the Supervisory Board members is not linked to any options, other derivatives or any other variable factors, nor is it dependent on the Bank's results.

Moreover, the Bank's Supervisory Board has appointed a Remuneration Committee, which applies the principles defined in the Good Practices.

According to the current PKO Bank Polski SA principles of Corporate Governance for supervised institutions, issued by the PFSA, the Supervisory Board will assess the functioning of the company payroll system and the results of this evaluation are presented to the Annual General Meeting.

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 AGM of PKO Bank Polski SA dated 30 June 2011, expressed through the failure to adopt the resolution on amendments to the Statute 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 jeopardize 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

9.2.2 Control systems in financial statements preparation process

Internal control system Control mechanisms concerning the preparation of financial statements Entity authorized to audit financial statements

PKO Bank Polski SA has an internal control system in place, which is aimed at ensuring: effective operation of the Bank, the reliability of financial reporting, compliance with the risk management rules, compliance of the Bank's operations with generally applicable laws, the Bank's internal regulations, supervisory recommendations and market standards adopted by the Bank.

Within the system of internal control the Bank identifies risk: connected with every operation, transaction, product and process, resulting from the organizational structure of the Bank and the Group, it also estimates the risk of not achieving the internal control system goals.

Internal control system

Within internal control system of the Bank distinguished are:

- control function with the task of ensuring that the control mechanisms relating in particular to risk management at the Bank, which covers all units of the Bank and positions within those units,
- compliance organizational unit, which aim it is, in cooperation with Bank's departments and units, to identify, evaluate, control and monitor the risk that Bank's operations do not comply with the generally applicable laws, the Bank's internal regulations, adopted by the Bank market standards, and
- an independent internal audit organization unit with the task of independently and objectively test and evaluate the adequacy and effectiveness of risk management and internal control system, with the exception of the internal audit unit.

In order to limit irregularities and fraud, ensure appropriate quality and correctness of the executed tasks, ensure compliance with risk management policies, generally applicable laws, internal regulations and market standards adopted by the Bank, as well as the reliability of its accounting and financial reporting, the Bank applies control mechanisms adjusted to its operations. The application of control mechanisms by the Bank's employees is verified as part of functional internal controls and internal audits. The issues, operations and transactions that are important for the individual areas of the Bank's operations are identified and subsequently monitored as part of the functional internal control.

Significant issues concerning the performance of functional internal control and control mechanisms are presented in periodical management reports submitted to the Risk Committee, the Bank's Management Board, the Supervisory Board Audit Committee and the Supervisory Board.

Control mechanisms concerning the preparation of financial statements

In order to ensure the accuracy and correctness of preparation of financial statements, the Bank designed and implemented a number of control mechanisms built into the functionality of reporting systems and internal regulations concerning this process. These mechanisms involve among others the use of a continuous verification and reconciliation of reporting data with accounts, analytical data and other documents which are the basis for preparing financial statements as well as with applicable regulations in the field of accounting policies and financial reporting.

The process of financial statements preparing is periodically subjected to a multi-functional internal control, in particular with regard to the correctness of the accounting arrangements, substantive analysis and reliability of the information. According to the internal regulations, financial statements are accepted by the Board of PKO Bank Polski SA and the Audit Committee of the Supervisory Board appointed by the Supervisory Board of PKO Bank Polski SA in 2006.

The tasks of the Audit Committee of the Supervisory Board i.a. monitoring the financial reporting process including the review of individual and consolidated interim and annual financial statements, with particular emphasis on:

- information on substantial changes in accounting and reporting policy and how to make significant for the financial reporting estimates and judgments of management, as well as the compliance of the financial reporting process with the applicable law,
- significant adjustments resulting from the audit and the auditor's opinion on the audit of financial statements, discuss any problems, concerns and doubts resulting from the audit of financial statements and analysis of the external auditor's recommendations addressed to the Management Board and the response of the Management Board in this regard.

Description of cooperation between the Audit Committee and the external auditor and its assessment is drawn up in the annual report on the activities of the Audit Committee annexed to the report of the Supervisory Board on the activities of that body.

ENTITY AUTHORIZED TO AUDIT FINANCIAL STATEMENTS

On 11 March 2015 the Supervisory Board of PKO Bank Polski SA selected KPMG Audyt Spółka z ograniczoną odpowiedzialnością spółka komandytowa as an entity authorized to audit the financial statements of PKO Bank Polski SA and consolidated financial statements of the PKO SA Group. KPMG Audyt Spółka z ograniczoną odpowiedzialnością spółka komandytowa with its registered office in Warsaw, Inflancka 4a Street is entered in the list of entities authorized to audit financial statements run by the National Council of Statutory Auditors under the number 3546. The choice of the entity authorized to audit and review financial statements was made by the Supervisory Board in accordance with applicable regulations and professional standards, on the basis of § 15 clause 1 pt.3 of the Statutes of the Bank.

On 10 April 2015, PKO Bank Polski SA and the entity authorized to audit financial statements KPMG Audyt Spółka z ograniczoną odpowiedzialnością spółka komandytowa concluded an agreement for audit and review of financial statements of the Bank and the PKO Bank Polski SA Group for years 2015-2016.

The total amount of net fees for KPMG Audyt Sp. z o.o. Sp.k for audit of the financial statements and the consolidated financial statements of PKO Bank Polski SA Group in 2016 amounted to PLN 1.25 million (in 2015 PLN 1.25 million). Fees for assurance services, including the review of financial statements amounted in 2016 PLN 2.38 million (in 2015 PLN 0.97 million). Net fee for other services in 2016 amounted to PLN 0.07 million.

9.2.3 THE ARTICLES OF ASSOCIATION OF PKO BANK POLSKI SA

Principles for amending the Articles of Association of PKO Bank Polski SA
Changes to the Statute in 2016

PRINCIPLES FOR AMENDING THE ARTICLES OF ASSOCIATION OF PKO BANK POLSKI SA

Amending the Articles of Association of PKO Bank Polski SA falls within the competence of the General Meeting and requires passing a resolution by a three-fourths majority of votes, the consent of the Polish Financial Supervision Authority in the cases defined in the Banking Act, and making an entry in the Register of Entrepreneurs of the National Court Register.

Moreover, according to Article § 10, clause 4 of the Articles of Association of PKO Bank Polski SA resolutions of the General Meeting relating to share preference and to issues concerning the Bank's merger by transferring all of its assets to another company, its liquidation, a reduction in the share capital by way of redeeming some of its shares without increasing it at the same time or changing the scope of the Bank's operations which would lead to the Bank ceasing its banking activities require a 90% majority of the votes cast.

CHANGES TO THE STATUTE IN 2016

25 FEBRUARY 2016 – EGSM RESOLUTION ON AMENDMENTS TO THE BANK'S ARTICLES OF ASSOCIATION

On 25 February 2016, the Extraordinary General Shareholders' Meeting of PKO Bank Polski SA passed Resolution No. 16/2016 on amendments to the Articles of Association of Powszechna Kasa Oszczędności Bank Polski SA, on the basis of which the following items were amended: § 15, clause 1, point 8 and § 23, clause 3, and the following items were deleted: § 19, clause 4, § 23, clause 1, point 4 and § 23, clause 1, point 7 of the Articles of Association of PKO Bank Polski SA.

The above-mentioned amendments to the Articles of Association of PKO Bank Polski SA were entered in the Register of Entrepreneurs of the National Court Register by virtue of the decision of the District Court for the Capital City of Warsaw in Warsaw, 13th Business Department of the National Court Register dated 19 April 2016 (ref. no. WA.XIII NS-REJ.KRS/016754/16/368).

30 June 2016 – OGSM resolution on amendments to the Bank's Articles of Association

On 30 June 2016, the Ordinary General Shareholders' Meeting of PKO Bank Polski SA passed Resolution No. 26/2016 on amendments to the Articles of Association of Powszechna Kasa Oszczędności Bank Polski SA, on the basis of which the following items were amended: § 1, clause 1, § 9, clause 2, § 15, § 17, clause 4, the first sentence, § 17a, clause 1, the first sentence, § 19, § 22, clauses 2-4, § 23, clauses 4-5, § 25, clause 1, point 3, letters a)-c), the title of Chapter VI, §§ 26-27, § 28, § 29, clause 3, the following items were deleted: § 9, clause 3, § 22, clause 5, § 30, clause 3, and the following items were added: § 5a, § 27a, § 29, clause 1, the second sentence, § 31a of the Articles of Association of PKO Bank Polski SA.

The above-mentioned amendments to the Articles of Association of PKO Bank Polski SA were entered in the Register of Entrepreneurs of the National Court Register by virtue of the decision of the District Court for the Capital City of Warsaw in Warsaw, 13th Business Department of the National Court Register, dated 31 August 2016 (ref. no. WA.XIII NS-REJ.KRS/039167/16/513).

9.2.4 The General Shareholders' Meeting

Fundamental powers of the General Shareholders' Meeting Manner of functioning

The General Shareholders' Meeting of PKO Bank Polski SA is convened as ordinary or extraordinary meeting in accordance with the provisions of the Code of Commercial Companies and the Statute, and based on the policies defined in the by-laws of the General Shareholders' Meeting.

Fundamental powers of the General Shareholders' Meeting

The fundamental powers of the General Shareholders' Meeting, apart from other matters defined in the binding laws, include adopting resolutions concerning the following matters:

- appointment and dismissal of Supervisory Board Members,
- approval of by-laws of the Supervisory Board,
- determining the manner of redemption of shares and the amount of consideration for the shares subject to buyout,
- creation and liquidation of special funds established from net profit appropriation,
- disposal by PKO Bank Polski SA of property items or perpetual usufruct right to property, provided that the value of the real property or the right being subject to such an act exceeds ¼ of the share capital,
- issuance of convertible bonds or other instruments giving the right to acquire or take up PKO Bank Polski SA's shares.

Manner of functioning

Allowed to participate in the General Shareholders' Meeting are holders of registered shares, pledgees and users with the right to vote entered in the share register at the registration date and holders of bearer shares, who have been entered in the Register of Shares at the day of registration and holders of bearer shares, if they were shareholders of the Bank at the day of the registration and they asked, within the act compliant time frame specified in the notification on the call of General Shareholders' Meeting, the entity maintaining their securities accounts for registered certificate on the right to participate in the General Shareholders' Meeting.

The shareholder who is a natural person may participate in the General Shareholders' Meeting and exercise his voting right in person or by proxy. The shareholder who is not a natural person may participate in the General Shareholders' Meeting and exercise his voting right by a person authorized to file declarations of will on his behalf, or by proxy.

A power of attorney should be prepared, under the sanction of nullity, in writing and attached to the minutes of the General Shareholders' Meeting or granted in an electronic form. The right to represent a shareholder who is not a natural person should be specified in the original or copy of the excerpt from the relevant register presented possibly with a power of attorney or sequence of a power of attorney. These documents should be presented at the time of drawing up the attendance register or sent electronically until the day before the day of the General Shareholders' Meeting on an email address indicated on announcement of convening the General Shareholders' Meeting.

The person(s) granting a power of attorney on behalf of a shareholder who is not a natural person should be listed in an up-to-date excerpt from the relevant register of a given shareholder.

Management Board Member and an employee of PKO Bank Polski SA may serve as proxy of shareholders at the General Shareholders' Meeting of PKO Bank Polski SA.

Projects of resolutions proposed by the Management Board are accepted by the General Shareholders' Meeting with justification and opinion of the Supervisory Board and complete text of the documentation, which will be presented to the General Shareholders' Meeting, are published on the Bank's website in the time enabling acquainting with them and evaluating them.

Draft resolutions put forward in accordance with the provisions of the Commercial Companies Code by an authorized shareholder or shareholders before the date of the General Shareholders' Meeting are published on the Bank's website as soon as they are received.

A shareholder or shareholders representing at least one twentieth of the share capital of the Bank may demand that certain matters be included in the agenda of the General Shareholders' Meeting. The demand may be filed in an electronic form.

A shareholder or shareholders of PKO Bank Polski SA representing at least one twentieth of the share capital may, before the date of the General Shareholders' Meeting, put forward to the Bank, in writing or by using electronic means of communication, draft resolutions concerning the matters included in the agenda of the General Shareholders' Meeting or matters which are to be included in the agenda. Moreover, shareholders during the General Shareholders' Meeting have the right to propose projects of resolutions and submit proposals of changes or supplements to the projects of resolutions, included in the agenda of the General Shareholders' Meeting.

Removing from agenda or desisting, at the request of shareholders, from further discussing the matter included in the General Shareholders' Meeting agenda requires that the General Shareholders' Meeting resolution is adopted by the majority of three-quarters votes, after prior consent of all those shareholders present at the General Shareholders' Meeting who applied for including the matter in the agenda.

Resolutions of the General Shareholders' Meeting are adopted by an absolute majority of votes, unless the binding laws or the Memorandum of Association of PKO Bank Polski SA provide otherwise.

The General Shareholders' Meeting adopts resolutions by way of open vote, with the provision that votes by ballot are ordered in the following circumstances:

- elections,
- applications for dismissal of members of PKO Bank Polski SA's authorities or liquidators,
- applications for bringing members of PKO Bank Polski SA's authorities or liquidators to justice,
- in staff matters,
- on demand of at least one shareholder present or represented at the General Shareholders' Meeting,
- in other cases defined in binding law regulations.

A shareholder may not, either personally or by proxy, or while acting as a proxy of another person, vote on resolutions concerning his liability towards PKO Bank Polski SA on whatever account, including the acknowledgement of the fulfilment of his duties, release of any of his duties towards PKO Bank Polski SA, or any dispute between him and PKO Bank Polski SA.

Shareholders have the right to ask questions, through the Chairman of the General Shareholders' Meeting, to the Members of PKO Bank Polski SA's Management or Supervisory Boards and the PKO Bank Polski SA's auditor.

For each of the agenda point, each shareholder has the right to one own speech and one reply. Shareholders may, during the course of discussion on each of the agenda points, apply for closing the list of speakers or closing the discussion on the given agenda point.

9.2.5 THE SUPERVISORY BOARD OF PKO BANK POLSKI SA IN THE REPORTING PERIOD

Composition of the Supervisory Board of PKO Bank Polski SA Changes in the composition of the Supervisory Board in 2016 The Supervisory Board manner of functioning The Supervisory Board competencies Changes in the Internal Regulations of the Supervisory Board Committees of the Supervisory Board

The Supervisory Board of PKO Bank Polski SA is composed of 5 to 13 members appointed for a joint term of office of three years. Members of the Supervisory Board are appointed and dismissed by the General Shareholders' Meeting.

On 26 June 2014 the State Treasury, as the Eligible Shareholder, on the basis of § 11 clause 1 of the Bank's Memorandum of Association determined the number of the Supervisory Board members to include 9 persons, of which the Bank informed in a Current Report No. 53/2014. As at 31 December 2016, the Supervisory Board of the Bank consisted of 9 persons.

The current term of office of all the Supervisory Board members started on 26 June 2014.

COMPOSITION OF THE SUPERVISORY BOARD OF PKO BANK POLSKI SA AS AT 31 DECEMBER 2016

PIOTR SADOWNIK - CHAIRMAN OF THE BANK'S SUPERVISORY BOARD

On 25 February 2016 appointed for the current term of the Supervisory Board, on the same day appointed the Chairman of the Supervisory Board by the Minister of State Treasury.

He is a graduate of the Faculty of Law and Administration at the University of Warsaw and of Pantheon-Assas University in Paris. In 1996, he obtained the title of legal attorney at the District Bar Council in Warsaw. He commenced his professional career in 1993 in the Warsaw office of the law firm Gide Loyrette Nouel. Currently, he is a partner heading the Dispute Resolution, Infrastructure, Public Law and Intellectual Property Departments at the Warsaw office of Gide Loyrette Nouel.
He represents the law firm's customers in court disputes and advises both Polish companies and international investors on infrastructure and public procurement projects. He also specializes in intellectual property law.
He is a lawyer recommended by the Legal 500 EMEA and Chambers Europe in dispute resolution. Moreover, the Legal 500 recommends him in the areas of energy and natural resources as well as intellectual property.
Member of the Supervisory Board of Bank Ochrony Środowiska SA.

GRAŻYNA CIURZYŃSKA- VICE-CHAIRMAN OF THE BANK'S SUPERVISORY BOARD

On 30 June 2016 appointed for the current term of the Supervisory Board, on the same day appointed the Vice-chairman of the Supervisory Board by the Minister of State Treasury.

She graduated from the Foreign Trade Department of the Warsaw School of Economics in Warsaw and Post-graduate Studies in European Banking Law of the Institute of Law Studies of the Polish Academy of Sciences. She started her career in 1991 in government administration, in the Ministry of Ownership Transformations.
Since 1996 she has been working within the banking sector. She held managerial positions in the area of corporate business of PBK SA (currently Bank BPH SA) and Kredyt Bank SA, supervising, among other things, cooperation with strategic customers and the development of enterprise financing programmes. Next, as a director in the retail area of Bank BGŻ SA, she was responsible, among other things, for the creation of the retail activity strategy, sales and pricing policy, bancassurance development, sales network management, designing and implementing products. She also served as an advisor to the President of the Management Board of the Bank.
Since 2007 she has been working within the banking payments and cards market. As a director of the department at Bank BGŻ SA and then at Bank BGŻ BNP Paribas SA, she was responsible for the area of card activity, cooperation with international payment organizations and providers of card technologies and services.
Moreover, she was a member of the Presidium of the Council of Banking Card Issuers and previously the Presidium of the Council of Cash Management at the Polish Bank Association.
For more than 15 years she was involved in teaching and research activity at the Warsaw School of Economics, at the Institute of International Economic Relations.
Currently, she is Director of the Large Investment Support Department at the Ministry of Development, coordinating the investment policy, supervising cooperation with Polish and foreign investors and financial institutions.

ZBIGNIEW HAJŁASZ- SECRETARY OF THE SUPERVISORY BOARD

On 30 June appointed for the current term of the Supervisory Board.
On 14 July 2016 appointed the Secretary of the Supervisory Board.

He is a practitioner and consultant in the field of management and development. He has over 20 years' experience in managing commercial companies and as an analyst and practitioner in the field of planning, management and development of financial institutions, industrial restructuring, privatization and international undertakings.
He took the following academic degrees: MPhil in Economics (London University, 2002) and M.Sc. Eng. in Mathematics (Wrocław University of Technology, 1982).
In 1993-96 and since 2005 – an academic lecturer (Wrocław University of Technology, University of

Wrocław, the Academy of Fine Arts in Wrocław). Since August 2011 – President of the Management Board of Zakład Gospodarki Komunalnej sp. z o.o. in Św. Katarzyna (winner in the Business Gazelles ranking in 2015 and 2016); since January 2016 – Vice-Chairman of the Supervisory Board of Polskie Radio SA.
He has held, among other things, the following positions: Director of the Economic Development Department at the Voivodeship Office in Wrocław (1991-1993); Director of the Regional Privatization Office of Bank BWP SA (1994-1996), Vice-President of the Management Board of Wrocławska Agencja Rozwoju Regionalnego SA – Managing Director, President of the Management Board of PRW SA in Wrocław, President of the Management Board of TBS sp. z o.o. in Głogów, and Director of the OPDRO Project Coordination Office.
He was a member of the Supervisory Boards of state-owned companies and companies with the participation of local government authorities, among other things, Dolnośląskie Konsorcjum Handlowo - Finansowe SA in Wrocław, Polskie Radio Wrocław SA in Wrocław, TBS sp. z o.o. in Lubin (the best TBS (a social building society) in Poland in the BGK ranking), Siechnicka Inwestycyjna Spółka Komunalna sp. z o.o., and Polskie Radio SA.
The author of expert opinions for the Sejm (the Polish Parliament) and the Government of the Republic of Poland and for financial institutions.

Mirosław Barszcz - Member of the Supervisory Board

On 25 February 2016 appointed for the current term of the Supervisory Board.

He graduated from the Catholic University of Lublin, where he took a degree in Master of Laws. He has extensive professional experience which he gained in audit companies (1996-1997 Ernst & Young, 1998-2001 Arthur Andersen, 2001-2004 PricewaterhouseCoopers), law firms (2005 Baker & McKenzie, 2008-2013 GWW Legal) and government administration (2005-2006 Undersecretary of State in the Ministry of Finance, 2007 – Minister of Construction, 2011-2013 advisor to the Minister of Justice). He has participated in more than 30 training courses (organized by Ernst & Young, Arthur Andersen, PricewaterhouseCoopers), including in the field of taxes, finances, human resources management, negotiations, project management, change management, cultural differences, and communication. He has consulting experience in many industries, including financial, information technology, telecommunications, energy, construction, real estate development, pharmaceutical, manufacturing, banking, commerce, logistics, and tourist industries. He has worked on numerous projects on government administration.
In 2013-2014, he was an independent advisor in the areas of strategy, finances, negotiations, project management, and change management.
In 2014-2016, he was an advisor in the Strategy Department at PGNiG SA. Currently, he is President of the Management Board of BGK Nieruchomości SA.

Adam Budnikowski - Member of the Supervisory Board

On 25 February 2016 appointed for the current term of the Supervisory Board.

He completed his M.Sc. studies in 1971 at the Higher School of Economics in Poznań (currently Poznań University of Economics and Business), taking a degree course in the economics of foreign trade. He received his doctoral degree in 1975 at the Faculty of Foreign Trade of the former Main School of Planning and Statistics (currently the Warsaw School of Economics). He obtained his post-doctoral degree at the same faculty in 1983. In 1992, the President of Poland awarded him the title of Professor of Economic Sciences.
He has been with the Warsaw School of Economics ever since the beginning of his professional career. He began working at the School in 1974 as an assistant in the Institute of International Trade Relations. In the following years, as he was granted higher academic degrees, he was promoted to assistant professor, then to associate professor, and finally to full professor. In 1996, he was elected Dean of the World Economy College of the Warsaw School of Economics and held that position for two consecutive terms of office until 2002. He was elected Chancellor of the Warsaw School of Economics in 2005, and on 5 March 2008 he was re-elected for the second term of office for the years 2008-2012. Since 2012 he has yet again been Dean of the World Economy College of the Warsaw School of Economics.
During his professional career, he has also collaborated with other academic and educational institutions, including the Polish Academy of Sciences, the Polish Economic Society, the Institute of Business Cycles and International Trade Prices (he was Deputy Director of the Institute in 1992-1993), the Catholic University of Lublin, Radom Academy of Economics, Academy of Diplomacy in Warsaw, and the National School of Public Administration. Since 2001 he has been a member of the Association of Polish Economists, and since 2012 he has been a member of the Presidium of the Economic Sciences Board of the Polish Academy of Sciences.
During his academic and research career, he has lectured and been a visiting researcher at Western universities many times. He was, among other things, a Fulbright scholar and in 1996 he took part in the World Bank's missions in Turkey and Romania as a World Bank expert.
His main areas of academic interest are related to international business. They include, among other things, international business relations (with a special emphasis on trade policy and international finances), transformation in Central and Eastern Europe, and environmental protection policy.

Wojciech Jasiński - Member of the Supervisory Board

On 25 February 2016 appointed for the current term of the Supervisory Board.	He graduated from the Faculty of Law and Administration at the University of Warsaw (1972). In 1972-1986, he worked in Płock, among other things, at the National Bank of Poland, the Branch in Płock, at the Town Hall, also as legal counsel in the Tax Chamber. In 1990-1991, he organized the local government in the Płockie Voivodeship, as a Representative of the Government Plenipotentiary for Local Government Reform. From 1992 to 1997 he worked in the Supreme Audit Office (NIK), as director of: the NIK Branch Office in Warsaw, Finance and Budget Team, and State Budget Department. In 1997-2000, he was a member and then President of the Management Board of Srebrna, a company with its registered office in Warsaw. He was a member of the Supervisory Board of Bank Ochrony Środowiska in 1998-2000. From September 2000 to July 2001 he held the position of Undersecretary of State at the Ministry of Justice. In 2006-2007, he was Minister of the State Treasury. Since 2001 he has been a member of the Polish Parliament (during the 4th, 5th, 6th, 7th and 8th terms of office) where he performed the following functions: Chairman of the Standing Subcommittee for the Banking System and Monetary Policy, Chairman of the Economy Committee, and Chairman of the Public Finance Committee. He was also a member of the State Treasury Committee at the Parliament. On 16 December 2015, the Supervisory Board of PKN ORLEN SA appointed Mr. Wojciech Jasiński to perform the function of President of the Company's Management Board for a joint three-term of office of the Management Board which ends on the date of the Ordinary General Shareholders' Meeting that will approve the Company's financial statements for 2016.

Andrzej Kisielewicz – Member of the Supervisory Board

On 25 February 2016 appointed for the current term of the Supervisory Board.	He holds a degree of Professor of Mathematical Sciences. He works at the University of Wrocław, at the Faculty of Mathematics and Computer Science. He obtained his post-doctoral degree from the University of Wrocław, and received a doctoral degree in mathematical sciences from the Polish Academy of Sciences. He graduated from the University of Wrocław. He gained his professional experience in such academic centers as: the University of Opole, Vanderbilt University (Nashville, USA), Polish Academy of Sciences, Technische University (Darmstadt, Germany), The University of Manitoba (Winnipeg, Canada), Wrocław University of Technology. He has gained experience as a member of supervisory boards. He is the author of more than 60 academic publications in foreign journals on mathematics, logistics and computer science as well as many books (e.g. 'Sztuczna inteligencja i logika' [*Artificial Intelligence and Logic*], 'Wprowadzenie do informatyki' [*An Introduction to Computer Science*], etc. He is also the author of many opinions, reviews and expert opinions, including for the National Science Centre and the European Commission. His research interests are the application of mathematics, logic and computer science in practice, artificial intelligence, business intelligence, informatization and argumentation theory.

Elżbieta Mączyńska-Ziemacka - Member of the Supervisory Board

On 20 June 2013 appointed to the Supervisory Board. On 26 June 2014 reappointed for the current term of the Supervisory Board	Graduated from the University of Warsaw (Political Economy Department, specialization: econometrics). Prof. PhD in economic sciences, employed at the Institute of Economic Sciences of the Polish Academy of Sciences (since 1990) and the Warsaw School of Economics (since 1998) at the position of the Head of the Department of Research of Enterprise Bankruptcy at the Institute of Corporate Finance and Investments at the Collegium of Business Administration of the Warsaw School of Economics (since 2008) and the Head of the Postgraduate Studies: 'Property Valuation'. Chairman of the Economic Strategic Thinking Committee of the Ministry of Economy (since 14 June 2013), President of the Polish Economic Society (since 2005), and member of the Presidium of the 'Poland 2000 Plus' Forecast Committee and the Committee of Economic Sciences of the Polish Academy of Sciences (since 2011). In 1994-2005, scientific secretary and member of the Presidium of the Social and Economic Strategy Council of the Council of Ministers. In 2005-2007, independent member of the Supervisory Board of BGŻ, in 1996-1998 independent member of the Supervisory Board of Polski Bank Rozwoju, in 1990-1991 advisor and consultant to the Polish-Swedish limited liability company SWEA SYSTEM. Has completed scientific and research internships i.a. in Germany (University of Mannheim) and Austria (WIIW, Wirtschaftsuniversität Wien). Three-time recipient of a DAAD scholarship. Author, co-author and editor of around 200 publications and expert opinions in the area of economic analysis, finance and enterprise appraisal, as well as in the area of economic systems and strategies of social and economic development. Member of the Editorial Committee of the bi-monthly 'Ekonomista' published by the Polish Economic Society and the Committee of Economic Sciences of the Polish Academy of Sciences, member of the Editorial Board of the quarterly 'Kwartalnik Nauk o Przedsiębiorstwie' published by the Collegium of Business Administration of the Warsaw School of Economics, member of the editorial team of the quarterly International Journal of Sustainable Economy (IJSE), Inderscience Publishers Editorial Office, UK.

JANUSZ OSTASZEWSKI - MEMBER OF THE SUPERVISORY BOARD

On 25 February 2016 appointed for the current term of the Supervisory Board.	Director of the Institute of Finance, Head of the Faculty of Finance in 2001-2013, a member of the Senate of the Warsaw School of Economics, an eminent specialist in finance. In 2005-2012, he was Dean of the College of Management and Finance for two terms of office. He graduated from the Main School of Planning and Statistics. He completed his studies in 1978. He took his doctoral degree in 1982 at the Faculty of Domestic Trade. He received his post-doctoral degree at the same faculty in 1990. In 2001, the President of Poland awarded him the tile of Professor of Economic Sciences. He completed his post-graduate studies in finance and management at Scuola Superiore Enrico Mattei in Milan. His main areas of research are issues relating to the operation of businesses, their financial management and strategy. This is reflected in the courses he has taught for many years: corporate finance, finance, management and in numerous teaching aids and books he has published. His considerable academic achievements include over 140 various types of academic papers, including 40 books. So far, 22 scholars have written and defended their PhD theses under his tutelage. His interest in finance was further deepened during his work for several years at the Ministry of Finance, in the position of Director of the Property Matters Department and his subsequent professional activity as an advisor to the President of Kredyt Lease SA – a company in the Kredyt Bank SA Group – and his work in the Finance Office of the Chancellery of the Polish Parliament.

CHANGES IN THE COMPOSITION OF THE SUPERVISORY BOARD IN 2016

On 25 February 2016 the Extraordinary General Shareholders' Meeting dismissed from the Bank's Supervisory Board:

- Jerzy Góra,
- Mirosław Czekaj,
- Piotr Marczak,
- Marek Mroczkowski,
- Krzysztof Kilian,
- Zofia Dzik.

Furthermore, the Extraordinary General Shareholders' Meeting appointed the following persons to the Bank's Supervisory Board:

- Mirosław Barszcz,
- Adam Budnikowski,
- Wojciech Jasiński,
- Andrzej Kisielewicz,
- Janusz Ostaszewski,
- Piotr Sadownik,
- Agnieszka Winnik – Kalemba.

The State Treasury (as the Authorized Shareholder) appointed Piotr Sadownik Chairman of the Bank's Supervisory Board and Agnieszka Winnik-Kalemba Deputy Chair of the Bank's Supervisory Board.

On 30 June 2016 the Ordinary General Shareholders' Meeting of the Bank dismissed members of the Supervisory Board of the Bank:

- Agnieszka Winnik–Kalemba,
- Małgorzata Dec–Kruczkowska.

Furthermore, the Ordinary General Shareholders' Meeting of the Bank appointed the following persons to the Bank's Supervisory Board:

- Grażyna Ciurzyńska,
- Zbigniew Hajłasz.

The State Treasury (as the Authorized Shareholder), based on § 12, clause 1 of the Bank's Articles of Association, appointed Ms. Grażyna Ciurzyńska Deputy Chair of the Bank's Supervisory Board.

According to statements issued by members of the Supervisory Board, Piotr Sadownik, Zbigniew Hajłasz, Mirosław Barszcz, Adam Budnikowski, Andrzej Kisielewicz, Elżbieta Mączyńska – Ziemacka and Janusz Ostaszewski meet the criteria of independency for members of the Supervisory Board set out in the Code of Best Practice for WSE Listed Companies. Other members of the Supervisory Board, i.e. Grażyna Ciurzyńska and Wojciech Jasiński, filed statements on lacking on the criteria of independence of the Bank and entities with significant connections with the Bank.

THE SUPERVISORY BOARD MANNER OF FUNCTIONING

The Supervisory Board acts based on the by-laws passed by the Supervisory Board and approved by the General Shareholders' Meeting. Meetings of the Supervisory Board are convened at least once a quarter.

The Supervisory Board adopts resolutions by an absolute majority of votes with the presence of at least half of the Supervisory Board Members, including the Chairman or Deputy-Chairman of the Supervisory Board, except for resolutions indicated in the Bank's Memorandum of Association concerning those matters that are required to be accepted by, apart from the quorum indicated, the qualified majority of 2/3 of total votes. Excluded from the vote are those members of the Supervisory Board to whom the given voted matter relates.

THE SUPERVISORY BOARD COMPETENCIES

The competencies of the Supervisory Board, apart from the rights and obligations stipulated in generally binding legal regulations and the provisions of the Memorandum of Association of PKO Bank Polski SA, include passing resolutions relating specifically to:

- approving the strategy of PKO Bank Polski SA and the annual financial plan approved by the Management Board,
- approving the risk management strategy adopted by the Management Board and accepting the overall level of tolerance to risk,
- appointing the entity to conduct the audit or review of the financial statements and giving consent to concluding contracts with such entity or its related entities,
- passing the Internal Regulations in regard of:
  - the Supervisory Board,
  - defining the rules of granting loans, advances, bank's guarantees and warranties to a member of the Management Board, the Supervisory Board, to a person holding a managerial position in the Bank and to entities related in terms of capital and organization,
- appointing and dismissing the President of the Management Board and, at the request of the President of the Management Board, also the Vice-Presidents and other Management Board Members, and suspending Members of the Management Board from performing their duties, as well as delegating Members of the Supervisory Board to temporarily perform the duties of Members of the Management Board,
- approving the Internal Regulations passed by the Management Board: of the Management Board, Management of special funds set up from the net profit, the Organizational Regulations of the Bank,
- expressing prior consent to actions which meet specific criteria, including, i.a. things, purchasing and selling fixed assets and real estate, establishing a company, taking up or acquiring shares, concluding transactions between PKO Bank Polski SA with a shareholder holding at least 5% of the total number of votes in the Bank or with a related entity,
- applying to the Polish Financial Supervision Authority for consent to the appointment of the President of the Management Board and a Management Board member supervising the management of risk material to the Bank's activities, and to entrusting the function of the Management Board member supervising the management of risk material to the Bank's activities with a current Management Board member who has not supervised the management of this risk,
- evaluation of the functioning of the remuneration policy of the Bank and submit a report in this regard to the Annual General Meeting,
- opinion on the application by the Bank 'Principles of Corporate Governance for supervised institutions'.

CHANGES IN THE INTERNAL REGULATIONS OF THE SUPERVISORY BOARD

On 30 June 2016, the General Shareholders' Meeting approved the amendments to the Regulations of the Supervisory Board adopted by the Supervisory Board on 2 June 2016.

The amendments related to, among other things:

- the Supervisory Board considering and giving its opinion on matters put on the agenda for the General Shareholders' Meeting. This amendment is associated with the rule set out in point II.Z.11. of the Best Practice for WSE Listed Companies 2016, according to which the Supervisory Board gives its opinion on all matters which are to be the subject of the resolutions of the General Shareholders' Meeting. The amended contents of the

Regulations of the Supervisory Board introduced the possibility of refraining from giving opinions on matters concerning the exclusively of the Supervisory Board or Supervisory Board Members as well as matters put forward by the shareholders after convening the General Shareholders' Meeting. In this situation, the Supervisory Board refraining from giving its opinion on a given matter will be the subject of a respective report on one-time refraining from the application of the rule set out in point II.Z.11. of the Best Practice for WSE Listed Companies 2016,

- authorizing the Chairman directly in the Regulations of the Supervisory Board to represent the Supervisory Board vis-à-vis the Bank's other bodies, the supervisory authorities and other persons,
- deleting the detailed provisions relating to the activities of the committees of the Supervisory Board which should be set out in the respective regulations of the committees of the Supervisory Board,
- specifying in detail the provision of the Regulations of the Supervisory Board with regards to the possibility of abstaining from voting.

COMMITTEES OF THE SUPERVISORY BOARD

According to the Bank's Articles of Association, the Supervisory Board appoints from among its members an Audit Committee, and the Committee for Remuneration. The Supervisory Board may also appoint other committees from among its members.

According to the Internal Regulations of the Supervisory Board, it is entitled to appoint, and in cases, when the provisions of the law require, appoint permanent committees whose members perform functions as members of the Supervisory Board delegated to fulfil selected supervisory activities in the Bank. The Supervisory Board appoints particularly permanent committees:

THE AUDIT COMMITTEE OF THE SUPERVISORY BOARD

TASKS

1) monitoring the process of the financial reporting, including the review of interim and annual financial statements of the Bank and the Group (standalone and consolidated), especially by:

- analyzing:
  – Information on significant changes in the accounting policy and financial reporting and ways of making estimates and judgments of management, when they are essential for the Bank's financial reporting,
  – Bank's financial statements, together with the summary of significant adjustments to the reports, being the result of audit and the opinion of the audit of financial statements,
  – Compliance of the financial reporting process with applicable laws and regulations on accounting,
  – Problems, concerns and doubts that arise from the audit of financial statements of the Bank and the Group,
  – Recommendations of the entity authorized to audit financial statements (auditor) of the Bank and the Group addressed to the Management Board and the Board's reply in this regard,
- presenting to the Supervisory Board recommendations on the opinion of the financial statements of the Bank and the Bank Group examined by the auditor,
- presenting to the Supervisory Board recommendations on the evaluation of the proposal of the Management Board regarding distribution of profit or covering of loss (including, in particular dividend policy) and issuance of securities,

2) monitoring efficiency of the systems of internal control, internal audit and risk management, in particular:

- evaluation of the Bank's activities related to the functioning of the internal control system and an assessment of its adequacy and effectiveness, in particular through:
  – Opinions on the resolutions of the Board of Directors, the approval of which falls within the competence of the Supervisory Board regarding internal control system,
  – Issuing opinions on submitted to the Supervisory Board periodic reports on the internal control system,
  – Review of procedures for the anonymous reporting of infringements of the law and the applicable Bank's procedures and ethical standards to members of the Management Board or the Supervisory Board,
  – A review of the writings of supervisory authorities addressed to the Management Board and the Supervisory Board together with answers,
- Analyzing information gathered from the Risk Committee,
- monitoring the activity of Internal Audit department, in particular through:
  – consulting the plan of internal audits in the Bank and an internal regulations of the Internal Audit Department,
  – performing a periodic review of the execution of the internal audit plan, ad-hoc audits and evaluating activities of the Internal Audit Department within the available resources,

- presenting an opinion to the Supervisory Board as regards appointing and dismissal the head of the Internal Audit Department,
- monitoring of the remuneration levels of a director and employees of the Internal audit Department,

- monitoring activities of the Compliance Department, in particular through:

- analyzing information received from the Compliance Department on the review of the effectiveness of the compliance monitoring,
- opinions on the proposals of the President of the Management Board to the Supervisory Board on the appointment and dismissal of the Director of the Department of Compliance,
- monitoring the level of remuneration of directors and the employees of the Department of Compliance,

3) monitoring the execution of financial audit activities, in particular by means of:

- recommending to the Supervisory Board a registered audit company entitled to perform a financial audit of the Bank together with its evaluation, level of fee and supervision of work performed,
- examining written information submitted by the registered audit company about relevant issues concerning financial audit, of which in particular information concerning material irregularities in the Bank's internal control system as regards financial reporting,
- agree with the entity authorized to audit the financial statements of the Bank and the Bank Group rules of conduct and activities of the proposed plan of action,
- examination of the reasons for termination of the contract with the entity authorized to audit financial statements of the Bank and the Bank Group,

4) monitoring the independence of a registered auditor and a registered audit company and on the services referred to in art. 48, clause 2 of the Act on Registered Auditors, in particular through obtaining:

- statements confirming the independence of a registered audit company and the independence of the registered auditors conducting the financial audit activities,
- information on the services referred to in art. 48, clause 2 of the Act on Registered Auditors, provided to the Bank.

COMPOSITION OF THE COMMITTEE AS AT 31 DECEMBER 2016

Zbigniew Hajłasz (President of the Committee),

Grażyna Ciurzyńska (Vice-President of the Committee),

Andrzej Kisielewicz (Member of the Committee),

Janusz Ostaszewski (Member of the Committee),

Piotr Sadownik (Member of the Committee).

THE REMUNERATION COMMITTEE

TASKS

Evaluation and monitoring of a remuneration policy adopted by the Bank and supporting the Bank's governing bodies in shaping and implementing this policy. Committee is responsible in particular for executing the following tasks:

1) providing opinions on general rules approved by the Supervisory Board on the variable salary components policy for persons holding managerial positions, as defined in § 28 clause 1 of the Resolution No. 258/2011 of the Polish Financial Supervision Authority of 4 October 2011 on detailed principles for the functioning of the risk management system and internal control system and detailed terms of estimating internal capital by banks and reviewing the process of estimating and maintaining internal capital, and the principles for determining the variable salary components policy for persons holding managerial positions at the bank, including the amount and components of the salaries, based on prudent and stable risk management, capital and liquidity and special care about the long-term interests of the Bank and the interests of shareholders and the Bank's investors,

2) making a periodical review of general principles of the variable salary components policy for persons holding managerial positions in the Bank and presentation of the results of the review to the Supervisory Board,

3) presentation to the Supervisory Board proposals of principles for remunerating, the variable salary components policy and remuneration of the Management Board members,

4) presentation to the Supervisory Board proposals related to appropriate forms of contracts with the Management Board members of the Bank,

5) giving opinions on motions for approval for a member of the Management Board to become involved in competitive business activities or participate in a competitive company as a shareholder of a civil law company, a partnership or as a member of a body in a corporation, or participate in another competitive legal person as a member of its body,

	6) giving opinions on a review report concerning the implementation of the variable salary components policy carried out by the Internal Audit Department, 7) prepare the draft report evaluating the ongoing functionality of the remuneration policy of the Bank, which is presented to the General Meeting by the Supervisory Board.
Composition of the Committee as at 31 December 2016	Piotr Sadownik (President of the Committee), Grażyna Ciurzyńska (Vice-President of the Committee), Wojciech Jasiński (Member of the Committee), Elżbieta Mączyńska-Ziemacka (Member of the Committee), Janusz Ostaszewski (Member of the Committee).
Risk Committee	
Tasks	1) evaluating the overall current and future readiness of the Bank to take risks, including the risk profile of the Group, in particular giving opinions about adopted by the Board strategic tolerance limits for individual types of risks for the Bank and the Group, the approval of which falls within the competence of the Supervisory Board, 2) evaluation of adopted by the Board risk management strategy in the Bank's ongoing business and submitted by the Board information on the implementation of this strategy and other periodic reports on risk management and capital adequacy, 3) evaluation of other resolutions of the Board in scope of risk management and capital adequacy, approval of which is the competence of the Supervisory Board, 4) supporting the Supervisory Board in overseeing the implementation of the risk management strategy in the Bank's ongoing business by senior management, 5) a review of whether the price of assets and liabilities offered to customers fully envision the Bank's business model and its strategy in terms of risk, and if these prices do not adequately reflect the risks in accordance with this model and this strategy, an indication of directions of corrective measures to restore the adequacy of the price of assets and liabilities to the business model and risk strategy of the Bank; Committee monitors the implementation of these actions by the Board, 6) evaluating solutions for reduction of business risk with the use of bank's non-life insurance and insurance of civil liability of members of the Board and proxies, 7) evaluating proposals of the Chairman of the Board on the appointment or dismissal of a member of the Board to supervise the management of risk material in the Bank's operations for the Supervisory Board, 8) issuing opinions on the information provided by the Bank to the public in relation to risk management strategies and risk management system, 9) performing other tasks assigned by the Supervisory Board on risk management at the Bank.
Composition of the Committee as at 31 December 2016	Andrzej Kisielewicz (President of the Committee), Grażyna Ciurzyńska (Vice-President of the Committee), Adam Budnikowski (Member of the Committee), Elżbieta Mączyńska-Ziemacka (Member of the Committee).
The Strategy Committee (established on 26 August 2016)	
Tasks	1) giving an opinion on the Bank's strategy adopted by the Management Board, whose approval falls within the competence of the Supervisory Board; 2) supporting the Supervisory Board in supervising the implementation of the strategy referred to, in particular by analyzing the periodical information about its implementation, presented by the Management Board; 3) giving opinions on the Bank's strategic activities which require the prior consent of the Supervisory Board, in particular with regards to their consistency with the Bank's strategy in force; 4) performing other tasks entrusted by the Supervisory Board with regards to pursuing the strategic objectives and key projects of the Bank.
Composition of the Committee as at 31 December 2016	Grażyna Ciurzyńska (President of the Committee), Zbigniew Hajłasz (Vice-President of the Committee), Mirosław Barszcz (Member of the Committee), Adam Budnikowski (Member of the Committee), Elżbieta Mączyńska - Ziemacka (Member of the Committee), Janusz Ostaszewski (Member of the Committee), Piotr Sadownik (Member of the Committee).

9.2.6 THE MANAGEMENT BOARD OF PKO BANK POLSKI SA IN THE REPORTING PERIOD

The Management Board of PKO Bank Polski SA Changes in the composition of the Management Board in 2016 Rules of operations of the Bank's Management Board The Bank's Management Board competencies Committees of the Bank's Management Board

Pursuant to § 19 clause 1 and 2 of PKO Bank Polski SA Memorandum of Association, members of the Management Board are appointed by the Supervisory Board for a joint term of office of three years.

The Management Board is composed of 3 to 9 members. Appointment of two members of the Management Board, including the President of the Management Board, requires approval of the Polish Financial Supervision Authority. As at 31 December 2016 the Management Board of the Bank was composed of 8 members.

Current joint term of office of the Bank's Management Board began at the end of the previous joint term of the Management Board started on 30 June 2011.

THE MANAGEMENT BOARD OF PKO BANK POLSKI SA AS AT 31 DECEMBER 2016

ZBIGNIEW JAGIEŁŁO - PRESIDENT OF THE MANAGEMENT BOARD

Member of the Management Board from 1 October 2009. On 8 January 2014 reappointed for the current term of the Management Board.

The President of the Management Board of PKO Bank Polski SA since October 2009, with appointment for new terms in 2011 and 2014. Prior to this he was the Pioneer Pekao TFI SA Management Board President for nearly 9 years. Also, within the global structure of Pioneer Investments he was responsible for the CEE region distribution. In the second half of 90s of the last century he was, i.a. active in establishing PKO/Credit Suisse TFI SA. investment funds company, in the function of its Vice-President. In his more than twenty-year long career in the financial markets he was responsible, i.a. for: (•) successfully steering PKO Bank Polski SA through the critical period of turmoil in the international financial markets, while strengthening the Bank's position of leadership in terms of assets, equity funds and earnings in Poland and the CEE region; (•) development and implementation of the PKO Bank Polski SA's strategy for the years 2010-2012 and 2013-2015, which resulted in significant increase in assets and strong business efficiency gains as well as in increased interest in the company among domestic and international investors; (•) adjustment of PKO Bank Polski SA to the requirements of the ever more competitive financial market through increased attractiveness of its product offer and quality of its customer service; (•) refocusing of the PKO Bank Polski SA Group's operational model toward its core activity of providing financial services.

He is actively involved in development and promotion of the most demanding financial market standards in Poland. He is a member of the Council of the Polish Bank Association and of the prestigious Institute International D'Etudes Bancaires, which brings together the international banking community. His previous functions included, i.a. that of the Chairman of the Chamber of Fund and Asset Management.

A graduate of the Wrocław Technical University, School of Computer Science and Management. He also completed Postgraduate Management Studies at the Gdańsk Foundation for Management Development and the University of Gdańsk, with Executive MBA certified by the Rotterdam School of Management, Erasmus University. The President of the Republic of Poland decorated him with the Officer's Cross of the Order of the Rebirth of Poland and he was awarded the Social Solidarity Medal for promoting the idea of corporate social responsibility. He is the Chairman of the Programme Council of the PKO Bank Polski SA's Foundation, an entity formed at his initiative in the year 2010. Chosen the CEO of the Year 2011 by Parkiet daily; the recipient of the Wektor 2011 granted by the Polish Employers' Chapter and of the Golden Banker in the Personality of the Year 2011 category. He was also lauded the Manager of the Year 2011 and 2014 in a competition ran by Gazeta Bankowa. In year 2012, 2014 and 2015 Bloomberg Businessweek Polska singled him out as one of the Top 20 Managers in Polish Economy. In 2013 he was honoured by Bank – financial monthly – with the title of 'The Innovator of Banking Sector 2012'. He also received the special award of 'Man of the Year 2013' from Brief monthly and 'Visionary 2013' from Dziennik Gazeta Prawna. In 2014, he received an honourable mention from the *Gazeta Finansowa* weekly as one of '25 Most Valuable Managers of the World of Finance'. In 2015, he received a medal from the Polish Chamber of Commerce (KIG) for supporting the development of economic self-government and entrepreneurship, and he was awarded an eDucat statuette by the Foundation for the Development of Non-cash Payments for his vision of the development of non-cash payments and the effective building of a coalition for the mobile payment standard. The industry service Mediarun.com recognized him as the most pro-marketing president, and the Jury of Responsible Business Awards awarded him the title of Outstanding CEO Philanthropist.

Other functions performed:	President of the Assets and Liabilities Management Committee President of the IT Security Committee President of the Risk Committee President of the Strategy Committee

JANUSZ DERDA - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD IN CHARGE OF IT AND SERVICES

On 3 November 2016 appointed for the current term of the Management Board.

He graduated from the Faculty of Mathematics, Physics and Chemistry of the University of Wrocław (field of study: Computer Science, specialization: Numerical Methods Software).
He has many years' experience in managing IT projects in the areas of banking, the development of IT system architecture, creating IT solutions for scoring tools, and the automation of loan request processing.
In 1994-95, he worked at Z.E.T.O. Opole sp. z o.o. as a designer and programmer. In 1997, he was employed at INEKOM s.c. in Opole. In 1998-2000, he was employed at Wielkopolski Bank Kredytowy 1, the Branch in Opole, and since 2000 – at Bank Zachodni WBK SA, at first in the loan team, and then in the CRS. Next, at BZ WBK SA, he worked in the Central System Department, at first as an expert, then as the Process Development and Centralization Team Manager and the Deputy Director of the Development Department. In 2008-2010, he was Deputy Director of the IT Area for Operational Matters. In 2010 – 2016, he performed the function of CIO at Bank Zachodni WBK SA responsible for: designing a strategy for the development of IT system architecture, business support and developing it solutions, supervising the IT investment and operating budget, maintaining the business continuity of IT systems, and ensuring IT operating security. From June to November 2016 he was Programme Director at Fiserv, responsible for the implementation of the central system.

Other functions performed:	President of the IT Architecture Committee Vice-President of the IT Security Committee Member of the Strategy Committee 1st Vice-President of the Operational Risk Committee Member of the Risk Committee Member of the Data Quality Committee

BARTOSZ DRABIKOWSKI - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD IN CHARGE OF FINANCE AND ACCOUNTING

Member of the Management Board from 20 May 2008. On 8 January 2014 reappointed for the current term of the Management Board.

He has been Vice-President of the Management Board in charge of Financial Matters at PKO Bank Polski SA since 20 May 2008.
He is also Chairman of the Supervisory Board of the Polish Association of Listed Companies and Deputy Chairman of the BIAC Finance Task Force – OECD. In 2015-2016, he was a Member of the Board of Directors of Visa Europe and a Member of the Risk, Audit and Finance Committee. In 2006-2008, he was a member of the Management Board of Krajowa Izba Rozliczeniowa SA (National Clearing House) responsible for finance, new products in the area of electronic payments, security and risk management.
In 2006-2008, he was a member of the Management Board of Krajowa Izba Rozliczeniowa SA (National Clearing House) responsible for finance, new products in the area of electronic payments, security and risk management.
He has many years' experience in managing financial institutions. He has chaired the Supervisory Boards of companies in the PKO Bank Polski SA Group: Inteligo Financial Services SA, eService SA, PKO BP Faktoring SA. He was a member of the Supervisory Board of Krajowy Depozyt Papierów Wartościowych SA (Central Securities Depository of Poland), a member of the Council of the Bank Guarantee Fund, and a member of the Supervisory Board of Polska Wytwórnia Papierów Wartościowych SA (Polish Security Printing Works).
He began his professional career at the Ministry of Finance, where he was responsible for, among other things, regulations and supervision over financial market institutions, mainly the banking sector and capital market. He has also prepared strategies for the development of the financial services sector both in Poland and within the common market of the European Union. At the Ministry of Finance, he held the positions of minister counsellor, deputy director and Director of the Financial Institutions Department.
For several years he was a member of the Commission for Banking Supervision, a member of the Securities and Exchange Commission, and a deputy member of the Payment System Board at the National Bank of Poland. He was also a member of many institutions of the European Union: among other things, he was a member of the Financial Services Committee (the European Council), a member of the European Banking Committee and the European Securities Committee (the European Commission). Bartosz Drabikowski graduated from the Harvard Business School where he completed

	an Advanced Management Programme. He is also a graduate of the University of Illinois Executive MBA at Urbana-Champaign, Warsaw School of Economics, Lodz University of Technology, National School of Public Administration, and the Academy of Diplomacy (as part of the Polish Institute of International Affairs). He has undergone professional training in many institutions: Deutsche Bundesbank, Deutsche Börse AG, Deutsche Ausgleichsbank and Rheinische Hypothekenbank. He received a scholarship from The German Marshall Fund of the United States and has participated in many training courses organized by, among other things, the European Commission and International Monetary Fund.
Other functions performed:	President of the Expense Committee President of the Data Quality Committee 1st Vice-President of the Assets and Liabilities Management Committee Member of the Strategy Committee 2nd Vice-President of the Operational Risk Committee Member of the Risk Committee Vice-President of the Bank's Loan Committee in charge of credit risk models

MAKS KRACZKOWSKI - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD SUPERVISING THE AREA OF INTERNATIONAL AND TRANSACTION BANKING AND COOPERATION WITH LOCAL GOVERNMENT AUTHORITIES AND GOVERNMENT AGENCIES

On 30 June 2016 appointed for the current term of the Management Board.	He graduated from the Faculty of Law and Administration of the University of Warsaw. A member of the Polish Parliament for the 5th, 6th, 7th and 8th terms of office: since 2015 – Deputy Chairman of the Commission of Economy and Development of the Polish Parliament, in 2005-2007 – Chairman of the Commission of Economy of the Polish Parliament, as well as: Member of the Legislative Commission of the Polish Parliament, and Chairman of the Standing Subcommission of the Constitutional Tribunal. He has many years' experience in establishing laws and a knowledge of business matters in Poland and abroad. As an MP for four terms of office of the Polish Parliament, in his activities he has focused on economic and financial market matters.
Other functions performed:	Vice-President of the Bank's Loan Committee Member of the Strategy Committee

MIECZYSŁAW KRÓL - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD IN CHARGE OF INSURANCE BANKING

On 2 June 2016 appointed for the current term of the Management Board.	Banker, finance specialist, manager, holder of an MA degree in economics, a graduate of the Warsaw School of Economics (the Faculty of Finance and Statistics) and the International School of Management. He completed his post-graduate studies at the Warsaw School of Economics (Collegium of Management and Finance). He has been working in banking and finance for over thirty years. He has worked, among other things, at the National Bank of Poland. He was a director at PKO Bank Polski SA for many years. In 2006-2010, he was the Director of the Audit Department at PKO Bank Polski SA, then, in 2011-2015, he was the Director of the Audit Department at Bank Ochrony Środowiska SA in Warsaw. In 2006-2007, he was a member of the Supervisory Board of the Financial and Banking Centre in Warsaw. In 2007, he was the Chairman of the Supervisory Board of Zakłady Chemiczne Organika Sarzyna in Nowa Sarzyna and in the Monument Preservation and Conservation Workshops. He has lectured at the Academy of Business Activity in Warsaw. He has authored many articles about banking and economics. In 1998-2002, he was a councillor for the Warsaw County. He was Deputy Chairman of the Budget Commission and a member of the Audit Committee. In 2002-2014, he was a councillor on the Warsaw City Council where he was, among other things, Deputy Chairman of the Budget and Finance Commission and a member of the Health Commission. As part of his social activities, he managed the Social Council of the Priest Jerzy Popiełuszko Hospital in Bielany, Warsaw.
Other functions performed:	Member of the Strategy Committee

PIOTR MAZUR - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD IN CHARGE OF RISK MANAGEMENT

On 8 January 2013 appointed to the Management Board until	He performs the function of Vice-President of the Management Board of PKO Bank Polski SA responsible for Risk Management Area, upon the approval of the Polish Financial Supervision Authority on 8 January 2013. He is a graduate of the Faculty of Organization and Management at the

the end of the previous term. On 8 January 2014 reappointed for the current term of the Management Board.	Academy of Economics in Wrocław (currently, Wroclaw University of Economics). He has over 20 years' experience in banking, including holding managerial positions since 2000 – being mainly responsible for risk management, restructuring and loans. He worked with international financial groups operating in Europe, the USA and South America. He is a member of supervisory boards, creditors' committees, a member and chairman of key risk management committees. He participated in developing Bank Zachodni WBK SA's strategy, he was directly responsible for risk management, the optimization of debt collection and restructuring processes, and he cooperated with the regulators in Poland and abroad. After graduating in 1991, he began his professional career in Bank BPH SA, in the loan area. In 1992, he began working at Bank Zachodni SA, and then, after the merger with Wielkopolski Bank Kredytowy SA he worked for BZ WBK SA. In the years 1992-2000 he was employed In the Department of Capital Investments, and then In the years 2000-2005 he held the position of Director in the Department of Credit Quality Control. In the years 2005–2008 he was the Director of Business Intelligence and Risk Management Area, and in the years 2008–2010 was the Deputy Chief Risk Officer. Since January 2011 he was the Chief Credit Officer and since March 2012 also Deputy Chief Risk Office. Moreover, he was the Chairman of the Credit Committee at BZ WBK SA, Deputy Chairman of the Credit Risk Forum, and Deputy Chairman of the Risk Model Forum.
Other functions performed:	President of the Bank's Loan Committee President of the Operational Risk Committee Vice-President of the Risk Committee 2nd Vice-President of the Assets and Liabilities Management Committee Member of the IT Security Committee Member of the Strategy Committee Member of the Data Quality Committee

JAKUB PAPIERSKI - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD IN CHARGE OF CORPORATE AND INVESTMENT BANKING

Member of the Management Board from 22 March 2010. On 8 January 2014 reappointed for the current term of the Management Board.	He is a graduate of Warsaw School of Economics and a holder of a Chartered Financial Analyst (CFA) license. He commenced his professional career in 1993 in Pro-Invest International, a consulting company. Between 1995 and 1996, he worked for ProCapital Brokerage House and subsequently for Creditanstalt Investment Bank. In March 1996, he started working for Deutsche Morgan Grenfell/Deutsche Bank Research dealing with the banking sector in Central and Eastern Europe. Between November 2001 and September 2003, he worked for Bank Pekao SA as executive Director of the Financial Division, directly supervising financial and fiscal policy of the bank, managerial information systems, as well as the treasury and management of investment portfolios; moreover, he was a member of the Asset and Liability Management Committee in the Bank. He accepted the position of the president of the Management Board for Centralny Dom Maklerski Pekao SA in October 2003. In September 2006, he also took up the position of a deputy-chairman of the Supervisory Board of Pioneer Pekao TFI SA. From May 2009, he served as the president of the Management Board of Allianz Bank Polska SA and in October 2009 he became the Management Board's president. Between 2005 and 2009, Jakub Papierski was a Chairman in the Programme Council of Akademia Liderów Rynku Kapitałowego established at the Lesław Paga Foundation; and now he is a member of the Programme Council.
Other functions performed:	Vice-President of the Bank's Loan Committee Member of the Risk Committee Member of the Strategy Committee Member of the Data Quality Committee

JAN EMERYK ROŚCISZEWSKI - VICE-PRESIDENT OF THE BANK'S MANAGEMENT BOARD, ACTING HEAD OF THE RETAIL BANKING AREA

On 14 July 2016 appointed for the current term of the Management Board.	Polish entrepreneur, manager in the insurance industry. In 1988, he obtained his master's degree in history from the Faculty of Humanities of the Catholic University of Lublin. In 1990, he earned his DEA diploma from Paris Institute of Political Studies (Institut d'Etudes Politiques de Paris). He completed numerous training courses in the fields of finance, insurance and management in France, Great Britain and Poland. In 1996, he earned his insurance broker licence. Since the first half of the 1990s he has been working for international banking and insurance institutions, among other things for AXA and Azur. In 1990-1991, he worked for AXA Banque and AXA International in France, and in 1991-1993 for Groupe Azur. In 1993-1996, he was Management Board Member of TU Azur Ostoja SA and TUnŻ Azur Życie SA. Since 1996 he worked for the BNP Paribas Group. In 1998-2016, he managed – as President of the Management Board – Towarzystwo Ubezpieczeń na Życie Cardif Polska SA, which now belongs to the BNP Paribas. Simultaneously, in 2001-2016 he held the position of Director General of Cardif Assurance Risques Divers in Poland. He has held many additional positions in the industry, such as Chairman of the Supervisory Board of

	Pocztylion-Arka Pension Fund Company (since 1999), Vice Chairman of the Supervisory Board of Postal Financial Services Agency SA (2000-2014), a member of the Audit Committee of the Polish Insurance Association (2012-2016), a member of the Supervisory Board of BBI Development NFI SA (since 2011). In 1981-1983, he was active in the charity organization of the Primate's Committee for Help to People Deprived of Liberty. Since 2009 he has been a Knight of Honour and Devotion of the Sovereign Military Order of Malta, whereas since December 2012 he has held the position of hospitaller of the Polish Association of the Sovereign Military Order of Malta. He is a member of the Management Board of the Page of History Foundation (since 2007) and a member of the Alpine Club of Warsaw, the Polish Heraldic Society, *Domus Polonorum*. In 2010, he was decorated with the Officer's Cross of the Order of Polonia Restituta for outstanding achievement in the development of the insurance market in Poland. He is an author and co-author of historical books and articles on finance and management.
Other functions performed:	Vice-President of the Data Quality Committee Rotary member of the Bank's Loan Committee in charge of credit risk models Member of the Strategy Committee Member of the Data Quality Committee

In addition to those mentioned above, members of the Management Board of the Bank also participated in non-permanent Committees, including the Steering Committees set up as a part of realized projects.

CHANGES IN THE COMPOSITION OF THE MANAGEMENT BOARD IN 2016

- On 21 March 2016, Mr. Jacek Obłękowski resigned as Vice-President of the Bank's Management Board as from 21 March 2016;
- On 22 March 2016, Mr. Jarosław Myjak resigned as Vice-President of the Bank's Management Board as from 22 March 2016;
- On 2 June 2016, the Bank's Supervisory Board appointed Mr. Mieczysław Król Vice-President of the Bank's Management Board as from 6 June 2016 for the current joint term of office of the Bank's Management Board;
- On 30 June 2016, the Bank's Supervisory Board appointed Mr. Maks Kraczkowski Vice-President of the Bank's Management Board as from 4 July 2016 for the current joint term of office of the Bank's Management Board;
- On 14 July 2016, the Bank's Supervisory Board appointed Mr. Jan Emeryk Rościszewski Vice-President of the Bank's Management Board as from 18 July 2016, for the current joint term of office of the Bank's Management Board;
- On 5 October 2016, Mr. Piotr Alicki resigned as Vice-President of the Bank's Management Board as from 30 October 2016;
- On 3 November 2016, the Bank's Supervisory Board appointed Mr. Janusz Derda Vice-President of the Bank's Management Board as from 1 December 2016 for the current joint term of office of the Bank's Management Board.

RULES OF OPERATIONS OF THE BANK'S MANAGEMENT BOARD

Management Board makes decisions as resolutions.

Statements on behalf of the Bank are made by:

- President of the Management Board independently,
- two members of the Management Board together or one member of the Management Board together with a proxy,
- two proxies acting jointly,
- proxies acting independently or jointly within the limits of granted authorization.

THE BANK'S MANAGEMENT BOARD COMPETENCIES

In accordance with § 20 clause 1 of the Memorandum of Association of PKO Bank Polski SA, the competences of the Management Board include all matters associated with the running of PKO Bank Polski SA's business, with the exception of those restricted for the competence of the General Shareholders' Meeting or the Supervisory Board based on generally applicable law or the provisions of the Memorandum of Association of PKO Bank Polski SA, including purchasing and disposing of real properties, shares in real properties or the perpetual usufruct of land not requiring the approval of the General Shareholders' Meeting based on § 9 clause 1 item 5 of the Memorandum of Association of PKO Bank Polski SA.

In accordance with § 20 clause 2 of the Memorandum of Association of PKO Bank Polski SA, the competences of the Management Board include making decisions on incurring liabilities or disposing of assets whose total value, in relation to one entity, exceeds 5% of own funds, with prejudice to the competences of the General Shareholders' Meeting specified in § 9 of the Memorandum of Association of PKO Bank Polski SA or the competences of the Supervisory Board specified in § 15 of the Memorandum of Association of PKO Bank Polski SA.

All matters which are outside the scope of the Bank's ordinary activities require a Management Board resolution. Management Board resolutions are passed by an absolute majority of votes. In the case of a voting tie, the President of the Management Board has the casting vote. The manner of functioning of the Management Board and the matters which require a Management Board resolution are defined in the Regulations of the Management Board.

Committees of the Bank's Management Board

In 2016 there were the following permanent committees in which Members of the Bank's Management Board operated:

The Assets and Liabilities Committee of PKO Bank Polski SA

Purpose

Managing assets and equity and liabilities by influencing the structure of PKO Bank Polski SA statement of financial position and its off-balance sheet items in a manner conducive to achieving the optimum financial result.

Tasks

Supporting the Management Board in the following areas of the Bank's activities:

- shaping the structure of the Bank's statement of financial position,
- capital adequacy management,
- managing profitability, taking into account the specific nature of the individual areas of activity and respective risks,
- managing financial risk, of which market and liquidity risks, the business and credit risk (settlement and pre-settlement) of transaction on the wholesale market.

Making decisions concerning in particular:

- limits related to the financial risks,
- limits related to settlement and credit transaction on the wholesale market,
- investment limits,
- limits specifying the appetite for portfolio credit risk,
- the ratios adjusting the transfer prices including individual rates of these ratios, and the method of their application,
- transfer prices for items classified in the investment bank portfolio in the Treasury Department,
- liquidity profile for the purpose of establishing transfer prices and replicated interest rate risk profiles,
- portfolio models and parameters, used for establishing impairment allowances and write-downs on loan exposures,
- significant financial and business risk models and their parameters.

Issuing recommendations to the Management Board or Management Board members, related especially to:

- shaping the structure of the statement of financial position,
- risk management: financial, settlement and pre-settlement transactions on wholesale and business market,
- launching of capital-related emergency activities and the capital needs,
- pricing policy in the individual business areas and interest rate levels and minimum lending margins,
- the financial model, including the principles for determining the management results and the transfer pricing system,
- hedging strategies as part of hedge accounting,
- taking any reorganization actions after conducted comprehensive stress-tests.

The Risk Committee

Purpose

Design strategic directions and tasks in the scope of banking risk in the context of the Bank's strategy and conditions arising from the macroeconomic situation and the regulatory environment, analyzing periodic reports related to the banking risks and developing appropriate guidance on their basis, as well as preparing the banking risk management strategy and its periodic verification.

TASKS

- monitoring the integrity, adequacy and effectiveness of the banking risk management system, capital adequacy and allocation of internal capital to individual business lines and implementing the risk management policy executed as part of the Bank's adopted Strategy,
- analyzing and evaluating the utilization of strategic risk limits set in the Banking Risk Management Strategy,
- giving opinions on cyclical risk reports submitted for approval to the Supervisory Board and taking into account the information from the reports when issuing opinions.

THE LOAN COMMITTEE OF THE BANK

PURPOSE

Credit risk management and mitigating of credit risk when making lending decisions or decisions concerning the non-performing loans management in PKO Bank Polski SA, and management of risk of occurring negative financial or reputation effects as a result of making incorrect business decisions on the basis of the credit risk models.

TASKS

- making decisions in matters relating to the segregation of competencies for making lending and selling decisions, managing non-performing loans, industry and customer limits, and securing the debt of PKO Bank Polski SA,
- making decisions related to credit risk models, in particular in the range of: models and credit policy parameters used in determining the scoring or rating evaluation, models and credit risk parameters consistent with the internal ratings method, the results of the validation of significant credit risk models and related proposals for changes in models, reports on the status of implementation of recommendations after validation; insignificant credit risk models; from monitoring of significant models and the quality of loan portfolios, for which credit risk models are used.
- issuing recommendations for the Management Board of PKO Bank Polski SA in matters relating to making decisions about lending transactions and changes in the material terms and conditions of these transactions, customer internal limits, non-performing loans management, credit risk models, particularly in the field of credit policy parameters, which, due to external regulations, require the approval of the Management Board or the Supervisory Board.
- issuing an opinion concerning applications of credit transactions, leasing transactions or factoring transactions led by the entities of PKO Bank Polski SA Group, restructuring and debt collection customers of KREDOBANK SA and on significant credit risk models in the companies of the Bank Group.

THE OPERATIONAL RISK COMMITTEE

PURPOSE

Purpose is to effectively manage operational risk, increasing safety of the Bank operating activity.

TASKS

- determining the directions of operational risk management development,
- supervising the operation of the operational risk management,
- coordinating operational risk management,
- determining measures to be taken in case of an emergency which exposes the Bank to reputational risk and results in operating losses.

THE EXPENSE COMMITTEE

TASKS

- granting approval, expressing opinions on overheads and administrative expenses of on-going operations, arising from new agreements or annexes to existing agreements, and granting approval to exceed the budget of overheads and other administrative expenses of on-going operations, in accordance with the Bank's internal cost management regulations,
- granting approval for further actions relating to areas identified as empty and refusing approval for new locations, in accordance with the Bank's internal real estate management regulations,
- making decisions concerning projects, including i.a. the approval of project applications, approval and recommendation of project plans, approval of significant changes in projects, making decisions to suspend project execution or close projects, approval of assessments of the objectives achieved and effects of projects, in accordance with the Bank's internal regulations on project and investment management,

	• transfers of funds between the costs of on-going operations and the costs of projects or investments, • approval of capital expenditure relating to the execution of tasks which do not meet the criteria of projects or investments.

THE STRATEGY COMMITTEE

PURPOSE	Supervise the strategic planning process and to manage the Bank's strategy.
TASKS	• managing the activities related to strategy development and implementation, • approving the strategy development schedule and strategy implementation schedule, • making key decisions necessary to ensuring the strategy's execution, including implementation of strategic programmes, • resolving any disputes arising during the work on individual strategic programmes.

THE IT ARCHITECTURE COMMITTEE OF PKO BANK POLSKI SA

PURPOSE	Develop an IT architecture ensuring the implementation of the Bank's Strategy.
TASKS	• developing the key assumptions of the IT architecture of the Bank (the principles), • evaluating the IT architecture functioning in the Bank on a periodical basis, • developing a target architecture model, • initiating measures aimed at achieving the target architecture model.

THE COMMITTEE FOR IT SAFETY

PURPOSE	Increase the effectiveness of supervision and control over the information system's safety in PKO Bank Polski SA (SIB).
TASKS	Issuing recommendations on the SIB safety, in particular related to: • coordinating and monitoring work related to the SIB safety, • setting the directions for the Bank's activities within the scope of SIB safety, • specifying the desirable activities, which in the Committee's opinion should be undertaken in the event of emergency situations which put the Bank's image at risk and cause operating or financial losses in the area of SIB safety, • monitoring the risk related to SIB safety.

DATA QUALITY COMMITTEE

PURPOSE	Design strategic directions for the activities relating to data quality management and data architecture at the Bank in the context of the Data Management System (DMS), to supervise its operations, and to assess its effectiveness and the activities undertaken by the individual organizational teams and units.
TASKS	Include making decisions about data management at the Bank, in particular those relating to: • directions for the development of the DMS, • recommendations for the organizational teams and units of the Head Office, regarding data management activities, • detailed data management solutions, • assessing the effectiveness of the operations of the DMS, determining priority measures as part of the DMS, and drawing up periodical action plans, • assigning ownership to groups of data, • resolving disputes over the DMS at the request of the Committee members, • accepting – particularly in cases justified by the need to ensure the Bank's continued operations – deviations from data quality criteria and rules as well as data quality solutions standards.

Moreover, in addition to those mentioned above, members of the Bank's Management Board also participated in the non-permanent committees, including steering committees set up as a part of realized projects.

9.3 SHARES OF PKO BANK POLSKI SA HELD BY 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 31 December 2016 are presented in the table below. The nominal value of each share is PLN 1.

Table 32. Shares of PKO Bank Polski SA held by the Bank's authorities

No.	Name and Surname	Number of shares as of 31.12.2016	Acquisition	Disposal	Number of shares as of 31.12.2015
	Management Board of the Bank				
1.	Zbigniew Jagiełło, President of the Management Board	11 000	0	0	11 000
2.	Janusz Derda, Vice-President of the Bank's Management Board*	0	0	0	x
3.	Bartosz Drabikowski, Vice-President of the Bank's Management Board	0	0	0	0
4.	Maks Kraczkowski, Vice-President of the Bank's Management Board*	0	0	0	0
5.	Mieczysław Król, Vice-President of the Bank's Management Board*	5 000	0	0	x
6.	Piotr Mazur, Vice-President of the Bank's Management Board	4 500	0	0	4 500
7.	Jakub Papierski, Vice-President of the Bank's Management Board	3 000	0	0	3 000
8.	Jan Emeryk Rościszewski, Vice-President of the Bank's Management Board*	0	0	0	x

*) members of the Bank's Management Board who did not perform their functions as at 31.12.2015.

As at 31 December 2016, the Members of the Supervisory Board of PKO Bank Polski SA did not hold any shares in PKO Bank Polski SA.

As at 31 December 2016, Members of the Supervisory Board and the Management Board of PKO Bank Polski SA did not hold shares in companies related to PKO Bank Polski SA defined as subsidiaries, jointly controlled entities and associates.

10. OTHER INFORMATION

OFF-BALANCE SHEET LIABILITIES GRANTED

At the end of 2016, guarantees and other financial off-balance sheet liabilities granted with respect to related parties of the PKO Bank Polski SA amounted to PLN 7 776 million and decreased by PLN 5 472 million as compared to the end of 2015.

The largest off-balance sheet liabilities granted are related to the following entities:

- PKO Leasing SA and its subsidiaries – PLN 6 112 million,
- PKO Bank Hipoteczny SA– PLN 1 506 million.

In 2016, the Bank did not conclude any material transactions with its related parties other than on an arm's length basis.

At the end of 2016, guarantees and other financial off-balance sheet liabilities granted with respect to related parties of the PKO Bank Polski SA.

At the end of 2016, guarantees and other financial off-balance sheet liabilities granted with respect to related parties of the PKO Bank Polski SA amounted to PLN 22 million and decreased by PLN 19 million as compared to the end of 2015. The largest amount of off-balance sheet liability granted relates to Centrum Elektronicznych Usług Płatniczych eService Sp. z. o. o. (PLN 21 million).

REACQUISITION OF OWN SHARES

During the period covered by this Report, PKO Bank Polski SA did not re-acquire its shares on its own account.

INFORMATION ABOUT THE ACTIVITIES OF THE PKO BANK POLSKI SA GROUP OUTSIDE THE TERRITORY OF THE REPUBLIC OF POLAND

Data in thousand PLN	Revenue*	Profit (loss) before income tax	Income tax	Net profit (loss)	Headcount (in FTEs)
In the EU Member States					
- Poland	14 047	3 897	-869	3 028	26 741
- Sweden	273	2	0	2	0
- Irleand	35	0	0	0	0
In third countries:					
- Ukraine	259	42	-11	31	2 170

*revenue defined as sum of interest and similar income, fee and commission income and other operating income

The Bank and its' related parties, in principle of Art. 4, clause 1, point 48 of the Regulation of the European Parliament and of the Council no. 575/2013, are based on the territory of Poland, Ukraine, Sweden and Irleand. In accordance with the Regulation, for the purpose of prudential consolidation, the Group consists of: PKO Bank Polski SA, PKO Leasing SA Group, PKO BP BANKOWY PTE SA, PKO Towarzystwo Funduszy Inwestycyjnych SA, KREDOBANK SA Group, PKO Finance AB, Finansowa Kompania 'Prywatne Inwestycje' Sp. z o.o., PKO BP Finat Sp. z o.o. and PKO Bank Hipoteczny SA.

In companies with their headquarters in Sweden and Irleand, members of the Boards hold their functions on the basis of corporate contracts.

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

In 2016 (up until 3 July 2016) SA disclosed in its current reports all the agreements with customers for which the total value of services arising from long-term agreements with the given customer meets the criteria defined in the Decree of the Minister of Finance of 19 February 2009 on current and periodical information submitted by issuers of securities and the conditions of considering as equivalent the information required by law of a non-member country (Journal of Laws No. 33, item 259). Since 3 July 2016 the Bank provided information about the conclusion of significant agreements in accordance with the requirements of Regulation (EU) of the European Parliament and of the Council No 596/2014 on market abuse, which came into force on that date.

On 7 December 2016, the Group issued its customer a promise based on which the Bank undertook to grant the customer a loan of up to PLN 3.2 million intended for financing the customer's investment activities. The Promise agreed by the Bank and the customer provides that the Loan will be granted on the basis of a loan agreement whose contents will be finally negotiated by 30 April 2017. The framework terms of the Loan Agreement were set out in an appendix to the Promise and provide for, among other things, securing the Bank's receivables in the form of financial and registered pledges, as well as the Bank receiving a declaration of submission to enforcement proceedings from the customer.

The principles for issuing the promise and the terms of the loan agreement do not differ from the standard ones used in the Bank or from the arm's length terms used in financing with a comparable credit risk profile. The promise is the Bank's first exposure to the customer and its subsidiaries in respect of agreements concluded over the past 12 months, therefore, the Bank's total exposure (including the value of the loan agreement) is PLN 3 200 million. The Bank will provide information about the conclusion of the Loan Agreement in a separate report.

On 2 November 2016, PKO Bank Polski SA (as the guarantor), Raiffeisen Bank International AG (RBI) (as the seller) and PKO Leasing SA (the Bank's subsidiary) (as the purchasers) signed a Share Purchase Agreement on the sale of

100% of shares of Raiffeisen-Leasing Polska SA by RBI to PKO Leasing SA. The transaction was closed on 1 December 2016.

As a result of the above-mentioned transaction, PKO Leasing SA purchased all of the shares of Raiffeisen-Leasing Polska SA and PKO Bank Polski SA replaced the financing granted to Raiffeisen-Leasing Polska SA and its subsidiaries by Raiffeisen Bank International AG or its Group entities.

In 2016, the Bank did not conclude any significant agreements with the Central Bank or the supervisory authorities. In 2016 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 2016

PKO Bank Polski SA did not publish forecasts related to financial results for 2016.

GUARANTEES AND LOAN COMMITMENTS GRANTED

As at 31 December 2016 the total value of guarantees and loan commitments granted amounted to PLN 58.1 billion with loan commitments making up 79.5% of this amount. Total rate of growth of guarantees and loan commitments granted amounted to 1.8% y/y, mainly in effect of an increase in financial liabilities granted to non-financial entities and a drop in guarantee liabilities granted to non-financial entities.

Table 33. Off-balance sheet liabilities granted (in PLN million)

	31.12.2016	31.12.2015	Change (in PLN million)	Change (%)
Loan commitments	**46 144.6**	**42 544.4**	**3 600.2**	**8.5%**
financial entities	2 763.3	2 306.2	457.1	19.8%
non-financials	39 525.0	36 157.8	3 367.2	9.3%
budgetary entities	3 856.3	4 080.4	-224.1	-5.5%
of which: irrevocable	*31 077.9*	*30 513.9*	*564.0*	*1.8%*
The guarantees granted:	**11 930.5**	**14 527.4**	**-2 596.9**	**-17.9%**
financial entities	304.4	229.1	75.3	32.9%
non-financials	11 264.4	14 231.6	-2 967.2	-20.8%
budgetary entities	361.7	66.7	295.0	5.4x
Total	**58 075.1**	**57 071.8**	**1 003.3**	**1.8%**

LOANS AND ADVANCES TAKEN, GUARANTEES AND WARRANTIES AGREEMENTS

In 2016, 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.

UNDERWRITING AGREEMENTS AND GUARANTEES GRANTED TO SUBSIDIARIES

As at 31 December 2016 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 2 billion, and the Guarantee Agreement dated 30 September 2015 (annexed on 26 October 2016), pursuant to which PKO Bank Polski SA is the underwriter of the bonds issue up to a total value of PLN 1 billion. The annexe signed in 2016 increased the guaranteed amount from PLN 500 million to PLN 1 billion.

As at 31 December 2016 PKO Bank Hipoteczny SA's liability in respect of the bonds issued, in nominal terms, amounted to PLN 1 156 million. All the bonds were taken up by investors other than PKO Bank Polski SA.

As of 26 October 2016 issues of bonds of PKO Leasing SA are regulated by the new Bond Issue Agreement. Issues of bonds issued based on the said Agreement are not covered by guarantees of PKO Bank Polski SA.

In 2016, PKO Bank Polski SA granted the following guarantees relating to its subsidiaries, active as at the end of 2016:

- it issued a guarantee of up to EUR 52 million to the Council of Europe Development Bank (CEB) for the repayment of a loan granted to RLPL; the guarantee was issued for the period to 29 August 2021;
- it issued a guarantee of up to EUR 44 million to the European Investment Bank (EBI) for the repayment of a loan granted to PKO Leasing SA; the guarantee was issued for the period to 25 November 2025;
- it issued a guarantee of up to PLN 1 250 thousand in connection with the lease of office space and parking spaces by RLPL; the guarantee was issued for the period to 31 December 2017;
- it issued four guarantees of up to PLN 261 thousand in total and two guarantees of up to EUR 20 thousand in total and increased the amount of one guarantee by PLN 44 thousand in connection with the lease of office space and parking spaces by PKO Leasing SA; the guarantees were issued for the maximum period to January 2022;
- it issued four guarantees of up to EUR 212 thousand in connection with the lease of office space and parking spaces by PKO Życie Towarzystwo Ubezpieczeń SA; the guarantee was issued for the period to 30 April 2017,
- it issued four guarantees of up to USD 2 130 thousand in total to KREDOBANK SA for the repayment of loans granted by KREDOBANK SA to its customers and one guarantee of up to EUR 49 thousand related to granting a tender bond to a customer; the guarantees were issued for the maximum period to November 2019.

ENFORCEABLE TITLES ISSUED

As from 27 November 2015, the amendment to the Banking Act waived banks' rights to issue bank enforceable titles. The Bank does not issue any other enforceable titles – it only applies for such title (mainly in the form of a court ruling) or it receives it from a customer (a Notarial Deed with a statement of submission to enforcement proceedings)

In the case of KREDOBANK SA, the Ukrainian law does not allow to issue enforceable titles as defined in the Polish Banking Law. In accordance with the Ukrainian law, bank liabilities are pursued in a court of law based on the provisions of the Code of Civil Procedure and Code of Economic Procedure.

DEBT WRITE-OFFS

The PKO Bank Polski SA Group in 2016 reduced a credits and loans impairment write-off to customers amounted to PLN 1 867 million.

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

As at 31 December 2016, 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 448.7 million, including PLN 43.8 million in respect of litigation in Ukraine (as at 31 December 2015 the total amount of the said litigation was PLN 638 million), and the total amount of litigation (suits) as at 31 December 2016 where the Bank is the plaintiff and litigation where other PKO Bank Polski SA Group companies are plaintiffs was PLN 1 232.3 million, including PLN 42.2 million in respect of litigation in Ukraine (as at 31 December 2015 the total amount under the said litigation was PLN 697 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.

PROXIES, MANAGEMENT BOARD MEETINGS AND EXECUTION OF THE RESOLUTIONS OF THE GENERAL SHAREHOLDERS' MEETING

As at 31 December 2016 there were 5 proxies of the Bank.

In 2016:

- two proxies were dismissed – Jarosław Orlikowski and Paweł Borys,
- one proxy was granted – to Justyna Borkiewicz.

In 2016, the Bank's Management Board held 50 meetings and adopted 664 resolutions.

Major actions and decisions of the Management Board, which affected the Bank's financial position and operations, are presented in different parts of this Directors' Report.

FACTORS WHICH WILL AFFECT FUTURE FINANCIAL PERFORMANCE OF THE PKO BANK POLSKI SA

In the near future, the results of the PKO Bank Polski SA Group will be affected by economic processes which will take place in Poland and in the global economy as well as by reactions of the financial markets. The interest rate policy applied by the Monetary Policy Council and key central banks will also have a great impact on future performance. Specific predictions about trends in the economy are covered in section2.7.

REGULATORY RISK

The continued regulatory risk, including the one arising from the resolution of the question of foreign currency loans (including the implementation of the recommendation of the Financial Stability Committee dated 13 January 2017 concerning the restructuring of the housing loans portfolio in foreign currencies), required capital ratios, the amounts of individual fees paid by banks towards a deposit guarantee system in 2017 taking into account, among other things, the exposure on the mortgage loan market, will be a considerable challenge for the Polish banking sector.

BANK TAX

The tax on the assets of certain financial institutions, which came into force as from February 2016, will have a negative effect on the results and profitability of banks. This charge will determine the level of the costs incurred by banks. In the medium term, it will contribute to a reduction in the banks' potential to develop lending activity, constituting a particular challenge for banks with low return on assets and, at the same time, a high financial leverage.

CENTRAL ASSESSMENT MECHANISM OF THE NATIONAL CLEARING CHAMBER

Joining the system of new reporting to the National Clearing Chamber in connection with the Central Assessment Mechanism, which is being prepared, and using this database will be a challenge for banks, including PKO Bank Polski SA.

BANK AS A SYSTEMICALLY IMPORTANT INSTITUTION

The financial results within the following quarters will be affected by the decision of the Polish Financial Supervision Authority dated 10 October 2016, on the identification of the Bank as another systemically important institution and on the imposition of a buffer on the Bank of 0.75% of its total risk exposure calculated in accordance with Article 92(3) of Regulation (EU) No 575/2013. As at the date of preparation of the information about the receipt of the decision, the Bank met the PFSA requirements regarding the minimum capital ratios, both on a standalone and consolidated basis.

On 18 October 2016, it received the decision of the Polish Financial Supervision Authority recommending that the Bank should comply with an additional own funds requirement. The PFSA recommended that the Bank should maintain its own funds to cover an additional capital requirement in order to hedge the risk arising from foreign currency mortgage loans to households, at the standalone level of 0.83 p.p. (vs. 0.76 p.p. to date), in excess of the value of the total capital ratio. According to Article 11, clause 2, point 21 of the Banking Act, the PFSA's decision has the power of a final administrative decision and is subject to immediate execution.

POLITICAL AND ECONOMIC SITUATION OF UKRAINE

The results of the PKO Bank Polski SA Group will be impacted also by the political and economic situation in Ukraine where operate the Group entities: KREDOBANK SA and financial and debt collection companies. It is conducted current analysis of impact of political and economic situation in Ukraine on financial results and on risk of assets deterioration of the PKO Bank Polski SA Group. PKO Bank Polski SA continues its activities to provide safe functioning its subsidiaries in Ukraine i.a. through enhance of their controlling activities, including monitoring of regulatory requirements determined by the National Bank of Ukraine. Information on the economic conditions and the banking sector in Ukraine is presented in the paragraph on international operating conditions – the Ukrainian market.

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 ARE SIGNIFICANT AND WERE CONCLUDED ON OTHER THAN MARKET CONDITIONS

In 2016 PKO Bank Polski SA provided on an arm's length basis the following services to related (subordinated) entities: services regarding maintaining bank accounts, accepting deposits, granting loans and advances, issuing debt securities, granting guarantees and concluding foreign exchange transactions and offering participation units in investment funds, lease products, factoring products and insurance products offered by the PKO Bank Polski SA Group entities. Simultaneously PKO Bank Polski SA provided for PKO Bank Hipoteczny SA services of brokering the sales of mortgage loans to individuals, providing post sales service activities to these loans and support activities within an outsourcing agreement. PKO Bank Hipoteczny SA rented office space to selected entities of Banks Group and along with Centrum Elektronicznych Usług Płatniczych eService Sp. z o.o. provided payment transaction settlement services.

The list of significant transactions between PKO Bank Polski SA and its subsidiaries, including credit debt of these entities to the Bank as at 31 December 2016 was presented in the Standalone financial statements of PKO Bank Polski SA for the year ended 31 December 2016.

SUBSEQUENT EVENTS

1) On 2 January 2017, Raiffeisen-Leasing Polska SA received a call from Raiffeisen Bank Polska SA for the early redemption of the bonds issued by the Company and held in the portfolio of said bank. On 31 January 2017, the Company conducted an early redemption of bonds with a nominal value of PLN 227 million. The redemption was financed from funds received from PKO Bank Polski SA in the form of a loan, based on an agreement signed in December 2016.
2) In January 2017, PKO Bank Polski SA acquired 100% of shares in ZenCard Sp. z o.o. and took up shares in the increased capital of the Company. ZenCard Sp. z o.o. is a technology company which has built a platform for retailers enabling them to create discount and loyalty programmes which also allows the virtualization of loyalty cards. The platform is integrated with a POS terminal and makes it possible to resign from many separate loyalty cards or separate applications installed on a phone and replace them with a single card which is also a payment card. CEUP eService Sp. z o.o., one of the largest clearing agents in Poland, is the Company's strategic partner. The Bank is interested in using the Company's know-how in the area of developing the solutions produced and using the Company's products in the Bank's Group. The acquisition of the Company is an important step towards strengthening relations with the customers and taking advantage of modern tools created by the progressing digitization.
3) On 13 January 2017, the Financial Stability Committee adopted resolution no. 14/2017 on the recommendation for restructuring the portfolio of housing loans in foreign currencies, and issued the following recommendations:
   - to the minister competent for financial institutions:
     - increasing to 150% the risk weight for exposures in foreign currencies which are fully and wholly secured with a mortgage on a residential property;
     - increasing, by banks using IRB, the minimum value of LGD for exposures in foreign currencies secured with a mortgage on a residential property;
     - amending the rules for the functioning of the Borrowers' Support Fund;
     - neutralizing tax effects for borrowers and banks which decided to convert housing loans into PLN;
     - imposing a systemic risk buffer of 3%.
   - to the Polish Financial Supervision Authority:

- updating the SREP methodology and expanding it by including the rules to allow assigning the appropriate level of capital charge
- amending additional capital requirements relating to the operational, market and credit risk currently used as part of Pillar 2
- issuing a supervisory recommendation on good practices when restructuring foreign-currency portfolios of housing loans.

- to the Bank Guarantee Fund – taking into account the risk associated with housing loans in foreign currencies in the methodology of determining contributions to the banks' guarantee fund.

The final impact of the recommendations on the Group will be possible to estimate after the competent bodies have formulated the recommendations.

4) In January 2017, one proxy was cancelled (Błażej Borzym) and one proxy was granted (Maciej Wyszoczarski). The number of proxies did not change (5).
5) On 26 January 2017, the Supervisory Board of PKO Bank Polski SA selected KPMG Audyt Spółka z ograniczoną odpowiedzialnością spółka komandytowa as the entity authorized to audit and review the financial statements of the Bank and consolidated financial statements of the PKO Bank Polski SA Group for 2017 - 2019.
6) On 2 February 2017, PKO Bank Hipoteczny SA issued mortgage bonds denominated in EUR with a value of EUR 25 million and a redemption period of 7 years from the date of issue. Mortgage bonds were taken up under a non-public issue. The mortgage bonds issued will be listed on the Luxembourg Stock Exchange.
7) On 2 February 2017, PKO Bank Hipoteczny SA concluded with PKO Bank Polski SA the Agreement for a revolving working capital loan in the current account up to the limit of PLN 1 500 million, to be made available in instalments. The loan was granted for the period to 2 February 2020. On 2 February 2017, PLN 600 million was made available as part of the loan.
8) On 6 February 2017, PKO Bank Hipoteczny SA acquired another portfolio of receivables from mortgage-secured housing loans of PLN 337.6 million under the Framework Receivables Sale Agreement concluded on 17 November 2015 with PKO Bank Polski SA.
9) An Extraordinary Shareholders Meeting was convened for 13 March 2017 to consider, among other things, draft resolutions submitted by the State Treasury represented by the Minister of Development and Finance, on the following topics:

- the rules for determining the remuneration of the Management Board members;
- determining the rules for remunerating Supervisory Board members.

The Minister of Development and Finance, in execution of the rights from shares in PKO Bank Polski SA held by the State Treasury, submitted a motion to include these resolutions on the agenda of the Extraordinary Shareholders' Meeting, in order to adapt the existing rules for remunerating members of the Bank's Management and Supervisory Boards to the provisions of the Act on determining the remuneration of persons managing certain companies. The proposed remuneration rules are intended to replace the rules for remunerating members of the Management and Supervisory Boards currently applicable in PKO Bank Polski SA. The proposed remuneration of members of the Management and Supervisory Boards of PKO Bank Polski S.A. was determined in accordance with the provisions of the Act on determining the remuneration of persons managing certain companies.

DECLARATION OF THE MANAGEMENT BOARD

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

- the annual financial statements 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 annual Directors' Report of the PKO Bank Polski SA Group 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 year 2016 consists of 144 subsequently numbered pages.

Signatures of all members of the Management Board

21.02.2017	Zbigniew Jagiełło	President of the Management Board	.... (signature)
21.02.2017	Janusz Derda	Vice-President of the Management Board	.... (signature)
21.02.2017	Bartosz Drabikowski	Vice-President of the Management Board	.... (signature)
21.02.2017	Maks Kraczkowski	Vice-President of the Management Board	.... (signature)
21.02.2017	Mieczysław Król	Vice-President of the Management Board	.... (signature)
21.02.2017	Piotr Mazur	Vice-President of the Management Board	.... (signature)
21.02.2017	Jakub Papierski	Vice-President of the Management Board	.... (signature)
21.02.2017	Jan Emeryk Rościszewski	Vice-President of the Management Board	.... (signature)