Bank Hipoteczny

SELECTED FINANCIAL DATA RELATING TO THE FINANCIAL STATEMENTS

SELECTED FINANCIAL DATA	in PLN '000		in EUR '000	
	period from 01.01.2019 to 30.06.2019	period from 01.01.2018 to 30.06.2018	period from 01.01.2019 to 30.06.2019	period from 01.01.2018 to 30.06.2018
Net interest income	150,318	119,501	35,056	28,188
Net fee and commission income	(2,416)	(2,314)	(563)	(546)
Operating profit	52,179	60,832	12,167	14,349
Profit before income tax	**52,179**	**60,832**	**12,167**	**14,349**
Net profit	**30,629**	**42,588**	**7,143**	**10,046**
Net earnings per share - basic (in PLN/EUR)	**0.02**	**0.04**	**0.01**	**0.01**
Net earnings per share - diluted (in PLN/EUR)	**0.02**	**0.04**	**0.01**	**0.01**
Total net comprehensive income	**118,773**	**82,894**	**27,699**	**19,553**
Net cash used in operating activities	(3,357,285)	(3,119,372)	(782,943)	(735,796)
Net cash used in investing activities	(307,953)	(1,759)	(71,817)	(415)
Net cash used in financing activities	3,665,287	3,237,410	854,771	763,639
Total net cash flows	**49**	**116,279**	**11**	**27,428**

SELECTED FINANCIAL DATA	in PLN '000		in EUR '000	
	as at 30.06.2019	as at 31.12.2018	as at 30.06.2019	as at 31.12.2018
Total assets	25,955,030	22,103,134	6,104,193	5,140,264
Total equity	1,855,897	1,487,883	436,476	346,019
Share capital	1,526,500	1,295,000	359,008	301,163
Number of shares (in thousands)	1,526,500	1,295,000	1,526,500	1,295,000
Book value per share (in PLN/EUR)	1.22	1.15	0.29	0.27
Diluted number of shares (in thousands)	1,526,500	1,295,000	1,526,500	1,295,000
Book value per share (in PLN/EUR)	1.22	1.15	0.29	0.27
Total capital ratio (TCR)	15.2%	15.2%	15.2%	15.2%
Common equity Tier 1 (CET1)	1,685,910	1,393,847	396,498	324,150
Own funds	1,685,910	1,393,847	396,498	324,150

Selected financial statement items have been translated to EUR at the following foreign exchange rates		
items of the income statement, statement of comprehensive income and statement of cash flows – the average of the NBP exchange rates prevailing as at the last day of each month of the reporting period	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
	4.2880	4.2395
items of the statement of financial position – the average NBP exchange rate as at the last day of the reporting period	30.06.2019	31.12.2018
	4.2520	4.3000

Bank Hipoteczny

Condensed interim financial statements of PKO Bank Hipoteczny SA for the six-month period ended 30 June 2019

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INCOME STATEMENT

INCOME STATEMENT	Note	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Interest income, including:	5	404,237	306,882
Interest income recognized under the effective interest rate method		403,457	306,414
Income similar to interest income on instruments measured at fair value through profit or loss		780	468
Interest expense	5	(253,919)	(187,381)
Net interest income		**150,318**	**119,501**
Fee and commission income	6	7,836	6,916
Fee and commission expense	6	(10,252)	(9,230)
Net fee and commission income		**(2,416)**	**(2,314)**
Net gain / (loss) on financial instruments measured at fair value through profit or loss	7	33	24
Net foreign exchange gains / (losses)	8	(1,895)	3,990
Net gain / (loss) on modification	10	370	(257)
Net credit losses	11	(5,680)	(4,445)
Other operating income	12	324	302
Other operating expenses	12	(306)	(301)
Net other operating income and expense		**18**	**1**
Administrative expenses	13	(25,037)	(21,856)
Regulatory charges	14	(24,483)	(6,385)
Tax on certain financial institutions		(39,049)	(27,427)
Operating profit		**52,179**	**60,832**
Profit before income tax		**52,179**	**60,832**
Income tax expense	15	(21,550)	(18,244)
Net profit		**30,629**	**42,588**
Earnings per share - basic (PLN)	16	0.02	0.04
Earnings per share - diluted (PLN)	16	0.02	0.04
Weighted average number of ordinary shares during the period (in thousands)		1,400,243	1,200,000
Weighted average diluted number of ordinary shares during the period (in thousands)		1,400,243	1,200,000

(IN PLN THOUSANDS)

STATEMENT OF COMPREHENSIVE INCOME

STATEMENT OF COMPREHENSIVE INCOME	Note	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Net profit		**30,629**	**42,588**
Other comprehensive income		**88,144**	**40,306**
Items which may be reclassified to profit or loss		**88,144**	**40,306**
Cash flow hedges (gross)		110,925	47,051
Deferred tax		(21,076)	(8,940)
Cash flow hedges (net)	19	89,849	38,111
Remeasurement of financial assets measured at fair value through other comprehensive income (gross)		(2,105)	2,710
Deferred tax		400	(515)
Remeasurement of financial assets measured at fair value through other comprehensive income (net)		(1,705)	2,195
Total net comprehensive income		**118,773**	**82,894**

STATEMENT OF FINANCIAL POSITION

STATEMENT OF FINANCIAL POSITION	Note	30.06.2019	31.12.2018
ASSETS			
Cash and balances with the Central Bank	17	22	6
Amounts due from banks	18	55	22
measured at amortized cost		55	22
Derivative hedging instruments	19	173,484	168,289
Securities	20	1,158,142	842,965
measured at fair value through other comprehensive income		1,158,142	842,965
Loans and advances to customers	21, 22	24,599,196	21,070,469
measured at amortized cost		24,599,196	21,070,469
Intangible assets	23	3,241	4,165
Property, plant and equipment	23	5,953	449
Other assets	24	14,937	16,769
TOTAL ASSETS		**25,955,030**	**22,103,134**
LIABILITIES AND EQUITY			
Liabilities			
Amounts due to banks	25	4,137,637	4,292,286
measured at amortized cost		4,137,637	4,292,286
Derivative hedging instruments	19	48,539	15,254
Amounts due to customers	26	3,378	4,359
measured at amortized cost		3,378	4,359
Mortgage covered bonds issued	27	15,965,585	12,841,500
measured at amortized cost		15,965,585	12,841,500
Unsecured bonds issued	28	3,830,751	3,311,148
measured at amortized cost		3,830,751	3,311,148
Other liabilities	29	51,787	121,974
Current income tax liabilities	15	9,947	3,159
Deferred income tax provision	15	51,096	25,303
Provisions	30	413	268
TOTAL LIABILITIES		**24,099,133**	**20,615,251**
Equity			
Share capital	31	1,526,500	1,295,000
Supplementary capital		146,735	54,932
Accumulated other comprehensive income		152,033	63,889
Retained earnings		-	(11,787)
Net profit for the period		30,629	85,849
TOTAL EQUITY		**1,855,897**	**1,487,883**
TOTAL LIABILITIES AND EQUITY		**25,955,030**	**22,103,134**
Total capital ratio (TCR)	52	15.2%	15.2%
Book value (in PLN '000)		1,855,897	1,487,883
Number of shares (in thousands)	31	1,526,500	1,295,000
Book value per share (in PLN)		1.22	1.15
Diluted number of shares (in thousands)		1,526,500	1,295,000
Diluted book value per share (in PLN)		1.22	1.15

(IN PLN THOUSANDS)

STATEMENT OF CHANGES IN EQUITY

FOR THE PERIOD ENDED 30 JUNE 2019	Note	Share capital	Supplementary capital	Accumulated other comprehensive income		Retained earnings	Net profit for the period	Total equity
				Cash flow hedges	Financial assets measured at fair value through other comprehensive income			
As at 1 January 2019		1,295,000	54,932	59,462	4,427	(11,787)	85,849	1,487,883
Issue of I series shares	31	100,000	-	-	-	-	-	100,000
Issue of J series shares	31	131,500	17,741	-	-	-	-	149,241
Transfer of profit to retained earnings		-	-	-	-	85,849	(85,849)	-
Transfer of profit to equity		-	74,062	-	-	(74,062)	-	-
Total comprehensive income, of which:		-	-	89,849	(1,705)	-	30,629	118,773
Net profit		-	-	-	-	-	30,629	30,629
Other comprehensive income		-	-	89,849	(1,705)	-	-	88,144
As at 30 June 2019	31	**1,526,500**	**146,735**	**149,311**	**2,722**	-	**30,629**	**1,855,897**

FOR THE PERIOD ENDED 30 JUNE 2018	Note	Share capital	Supplementary capital	Accumulated other comprehensive income		Retained earnings	Net profit for the period	Total equity
				Cash flow hedges	Financial assets measured at fair value through other comprehensive income			
As at 31 December 2017		1,200,000	-	(31,372)	2,480	(749)	51,419	1,221,778
Changes due to IFRS 9 implementation		-	-	-	-	(11,787)	-	(11,787)
As at 1 January 2018		1,200,000	-	(31,372)	2,480	(12,536)	51,419	1,209,991
Transfer of profit to retained earnings		-	-			51,419	(51,419)	-
Transfer of profit to equity		-	50,670			(50,670)	-	-
Total comprehensive income, of which:		-	-	38,111	2,195	-	42,588	82,894
Net profit		-	-	-	-	-	42,588	42,588
Other comprehensive income		-	-	38,111	2,195	-	-	40,306
As at 30 June 2018	31	**1,200,000**	**50,670**	**6,739**	**4,675**	**(11,787)**	**42,588**	**1,292,885**

(IN PLN THOUSANDS)

STATEMENT OF CASH FLOWS

STATEMENT OF CASH FLOWS	Nota	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Cash flows from operating activities			
Profit before income tax		**52,179**	**60,832**
Total adjustments:		**(3,409,464)**	**(3,180,204)**
Amortization and depreciation		1,637	1,122
Interest on mortgage-covered bonds issued, bonds issued and loans obtained		94,587	54,478
Change in derivative financial instruments (asset)		(5,195)	(214,382)
Change in loans and advances to customers (gross)		(3,534,161)	(3,042,265)
Change in other assets and right-of-use		1,076	(7,704)
Change in amounts due to banks		(26,931)	(197,029)
Change in derivative financial instruments (liability)		33,285	(217,531)
Change in amounts due to customers		(981)	952
Change in liabilities in respect of mortgage covered bonds issued		(130,571)	366,217
Change in liabilities in respect of bonds issued		35,374	27,575
Change in allowances for expected credit losses and provisions		5,579	4,474
Change in other liabilities, excluding liabilities in respect of unregistered issues of own shares		24,920	10,552
Income tax paid		(9,645)	(13,712)
Other adjustments (including changes in the measurement of securities and derivative instruments recognized in other comprehensive income)		101,562	47,049
Net cash used in operating activities		**(3,357,285)**	**(3,119,372)**
Cash flows from investing activities			
Inflows from investing activities		**584,752**	**187,777**
Disposal of and interest on securities measured at fair value through other comprehensive income		584,752	187,777
Outflows on investing activities		**(892,705)**	**(189,536)**
Acquisition of securities measured at fair value through other comprehensive income		(892,670)	(189,251)
Acquisition of intangible assets and property, plant and equipment		(35)	(285)
Net cash used in investing activities		**(307,953)**	**(1,759)**
Cash flows from financing activities			
Proceeds from issue of own shares and payments towards issue of own shares		149,241	-
Proceeds from issue of mortgage covered bonds		3,254,656	2,918,510
Proceeds from issue of bonds		4,034,729	3,751,378
Redemption of bonds issued		(3,550,500)	(3,308,000)
Proceeds from loans obtained		3,061,074	1,778,736
Proceeds from loans repaid		(3,188,793)	(1,848,736)
Repayment of interest on mortgage covered bonds issued, bonds issued and loans obtained		(94,587)	(54,478)
Payments of lease liabilities (IFRS 16)		(533)	
Net cash used in financing activities		**3,665,287**	**3,237,410**
Total net cash flows		**49**	**116,279**
Cash and cash equivalents at the beginning of the period		28	5,911
Cash and cash equivalents at the end of the period	35	**77**	**122,190**

NOTES TO THE CONDENSED INTERIM FINANCIAL STATEMENTS – CONTENTS

(IN PLN THOUSANDS)

NOTES TO THE INTERIM CONDENSED FINANCIAL STATEMENTS

1. General Information

Banking Activities

PKO Bank Hipoteczny Spółka Akcyjna ("PKO Bank Hipoteczny SA", "Bank") with its registered office in Gdynia, ul. Jerzego Waszyngtona 17, 81-342 Gdynia, was entered in the Register of Businesses maintained by the District Court Gdańsk-Północ in Gdańsk, 8th Business Department of the National Court Register, with the number KRS 0000528469, on 24 October 2014. The Bank was assigned the statistical number REGON 222181030. Its share capital as at 30 June 2019 was PLN 1,526,500,000 and was fully paid up.

PKO Bank Hipoteczny is a specialized bank that operates on the basis of the Polish Mortgage Covered Bonds and Mortgage Banks Act dated 29 August 1997, the Banking Act of 29 August 1997, the Commercial Companies Code and other generally applicable provisions of the law, the principles of good banking practice and the Bank's Articles of Association.

The Bank specializes in granting residential mortgage loans for individuals and acquires receivables following from such loans from PKO Bank Polski SA. The Bank acquires loans for its portfolio based on its strategic cooperation with PKO Bank Polski SA.

The Bank's principal financial objective, in terms of financing, is to issue mortgage covered bonds, which are to serve as the primary source of long-term financing for the residential mortgage loans.

Indication as to whether the Bank is a Parent or Key Investor and whether it prepares consolidated financial statements

PKO Bank Hipoteczny SA is not a parent or a significant investor in associates and jointly-controlled entities. Therefore, PKO Bank Hipoteczny SA does not prepare consolidated financial statements.

The Parent of PKO Bank Hipoteczny SA is PKO Bank Polski SA, which prepares consolidated financial statements for the PKO Bank Polski Group.

Information on the composition of the Bank's Supervisory Management Boards

The following table presents the composition of the Supervisory Board of PKO Bank Hipoteczny SA during the period covered by the interim financial statements:

No.	Name and surname	Position	Date of appointment	Date of dismissal/ resignation/ end of term
1	Jakub Papierski	Chairman of the Supervisory Board	06.10.2014	-
2	Piotr Mazur	Deputy Chairman of the Supervisory Board (to 29.03.2019)	06.10.2014	29.03.2019
3	Rafał Kozłowski	Deputy Chairman of the Supervisory Board (from 17.04.2019) / Member of the Supervisory Board (to 17.04.2019)	09.02.2018	-
4	Justyna Borkiewicz	Member of the Supervisory Board	28.10.2016	-
5	Artur Kluczny	Member of the Supervisory Board (independent)	18.10.2017	-
6	Mieczysław Król	Member of the Supervisory Board	28.10.2016	29.03.2019
7	Piotr Kwiecień	Member of the Supervisory Board (independent)	18.10.2017	-
8	Paweł Metrycki	Member of the Supervisory Board	30.03.2019	-
9	Jan Emeryk Rościszewski	Member of the Supervisory Board	18.10.2017	-
10	Ilona Wołyniec	Member of the Supervisory Board	30.03.2019	-

Due to the end of the term of office of the Supervisory Board on 29 March 2019, on that same day the General Shareholder's Meeting appointed the members of the Supervisory Board for a further four-year term of office.

The following table presents the composition of the Management Board of PKO Bank Hipoteczny SA during the period covered by the condensed interim financial statements:

No.	Name and surname	Position	Date of appointment	Date of dismissal/ resignation
1	Paulina Strugała	President of the Management Board	16.04.2018	-
2	Piotr Kochanek	Vice-President of the Management Board	01.01.2019	-
3	Agnieszka Krawczyk	Vice-President of the Management Board	01.01.2018	-
4	Jakub Niesłuchowski	Vice-President of the Management Board	01.04.2015	28.02.2019

On 12 December 2018, the Supervisory Board of PKO Bank Hipoteczny SA appointed Piotr Kochanek Vice President of the Management Board with effect from 1 January 2019. On 26 February 2019 the Polish Financial Supervision Authority (PFSA) granted its consent to entrusting Piotr Kochanek with the function of Member of the Management Board of PKO Bank Hipoteczny SA responsible for the supervision of material risks in the Bank's operations.

2. Basis of preparation of the condensed interim financial statements

The condensed interim financial statements of PKO Bank Hipoteczny SA cover the six-month period ended 30 June 2019 and contain comparative data for the six months ended 30 June 2018 (comprising the income statement, statement of comprehensive income, statement of cash flows and statement of changes in equity) as well as comparative data as at 31 December 2018 (comprising the statement of financial position). The financial data is presented in thousands of Polish zlotys (PLN), rounded to a thousand, unless otherwise indicated.

2.1 Statement of compliance

These condensed interim financial statements have been prepared in accordance with the requirements of the International Accounting Standard 34, „Interim Financial Reporting", endorsed by the European Union.

The accounting principles and calculation methods applied in the preparation of these condensed interim financial statements are consistent with the principles applicable in the financial year ended 31 December 2018, except changes resulting from the implementation of IFRS 16 "Leases" as of 1 January 2019, described accordingly in chapter 3.1.

The principles that did not change are described in the annual financial statements of PKO Bank Hipoteczny SA for the year ended 31 December 2018.

The condensed interim financial statements for the six months of 2019 do not contain all the information and disclosures that are required in the annual financial statements and they should be read together with the annual financial statements of PKO Bank Hipoteczny SA for the year ended 31 December 2018 prepared in accordance with the International Financial Reporting Standards endorsed by the European Union.

2.2 Approval of the condensed interim financial statements

These condensed interim financial statements, having been reviewed with an opinion issued by the Audit and Finance Committee of the Supervisory Board on 6 August 2019, were approved by the Bank's Management Board for publication on 8 August 2019.

3. Changes to accounting policies

3.1 IFRS 16 Leases

The standard was published by the International Accounting Standards Board on 13 January 2016 and has been endorsed by the European Union. IFRS 16 is binding for the annual periods beginning on or after 1 January 2019. The new standard replaced IAS 17 Leases, which were effective until the end of 2018, and Interpretation of the International Financial Reporting Interpretations Committee ("IFRIC") no. 4 and Interpretations of the Standing Interpretations Committee ("SIC") nos. 15 and 27.

The new standard introduces one model for accounting for leases in the lessee's accounts, consistent with the accounting for financial leases under IAS 17. According to IFRS 16, a contract is a lease or contains a lease if it transfers the right to use an identified asset for a given period in exchange for consideration.

The key difference between the definitions of a lease in IAS 17 and IFRS 16 is the requirement of control over the use of a specific asset, identified in a contract in a direct or implied manner. A transfer of right of use takes place where we have an identified asset from which a lessee has the right to practically all economic benefits, and where the lessee has control over the use of the asset in a given period.

If the definition of a lease is met, a right-of-use asset with the corresponding lease liability determined in the amount of discounted future payments over the lease term are recognized, except for short-term lease contracts up to 12 months and lease contracts relating to assets immaterial in terms of their amounts.

Expenses relating to the use of leased assets which were previously charged to non-personnel costs are currently classified as depreciation and interest expense.

Right-of-use assets are depreciated on a straight line basis, while lease liabilities are accounted for using the effective interest rate.

Impact of IFRS 16 on the financial statements

In the fourth quarter of 2018, the Bank finalized the IFRS 16 implementation project.

Analyses were conducted of all operating lease, rent and hire agreements. In addition, agreements for the purchase of services (external services costs incurred as part of operating activities) were analysed for the existence of the right of use of an identified asset.

As part of the project, the Bank amended its accounting policies and operational procedures as appropriate. Methodologies were developed and implemented for the correct identification of lease contracts and for collecting the data necessary to accurately account for such transactions.

The Bank introduced the standard as of 1 January 2019. In accordance with the transitional provisions of IFRS 16, the New principles were applied retrospectively. Consequently, the comparative data for the financial year 2018 will not be restated (modified retrospective approach).

Specific adjustments resulting from the implementation of IFRS 16 are described below.

Recognition of lease liabilities

In accordance with IFRS 16, the Bank recognizes lease liabilities on contracts previously classified as operating leases in accordance with IAS 17. Such liabilities have been measured at the present value of the remaining lease payments at the date of initial application of IFRS 16, discounted using the interest rate as at 1 January 2019 calculated based on the Bank's incremental interest rate.

As at the date of initial recognition, lease payments taken into account in the measurement of the lease liability include the following types of payments for the right to use the underlying asset over the lease term:

- fixed lease payments less any lease incentives due;
- variable lease payments that depend on market indices;
- amounts expected to be paid in respect of the guaranteed residual value of a leased asset;
- the exercise price of a purchase option if it may be reasonably assumed to be exercised;
- payments of penalties for terminating the lease, if the lessee is able to exercise an option to terminate the lease.

In order to calculate discount rates for the purposes of IFRS 16, the Bank assumed that the discount rate should reflect the cost of financing which would have been incurred to purchase the leased asset. In order to estimate the discount rate, the Bank took into account the following parameters: the lease term and contractual currency, and the profitability of own debt securities.

At 1 January 2019, the discount rates calculated by the Bank ranged from 2.07% to 4.21% (depending on the length of the lease term). All lease contracts concluded by the Bank are in PLN.

The Bank availed itself of the option to simplify the recognition of short-term lease contracts (below 12 months) and lease contracts with low value underlying assets (below PLN 20 thousand) and it does not recognize financial liabilities and right-of-use assets for such contracts. The respective lease payments are charged to costs on a straight-line basis over the period of the lease.

Recognition of the right-of-use assets

Right-of-use assets are measured at cost and presented in the statement of financial position together with assets owned by the Bank, including presentation of additional information in the notes to the financial statements.

The cost of the right-of-use asset includes:

- the initial value of the lease liability;
- all lease payments made at or before the inception date, net of all lease incentives received;

(IN PLN THOUSANDS)

- any initial direct costs incurred by the lessee in connection with concluding the lease contract;
- an estimate of costs to be incurred by the lessee in dismantling and removing the underlying asset or restoring the underlying asset.

APPLICATION OF ESTIMATES

IFRS 16 requires certain estimates and calculations which affect the measurement of the finance lease liabilities and right-of-use assets. They include, among other things:

- identifying contracts covered by IFRS 16;
- identifying the lease term (including for contracts with an unspecified term or with an extension option);
- determining the interest rate applied for discounting future cash flows;
- determining depreciation rates.

APPLICATION OF PRACTICAL EXPEDIENTS

Upon first-time application of IFRS 16, the Bank applied practical expedient permitted by the standard by applying a single discount rate to a portfolio of lease contracts with similar characteristics.

IMPACT ON THE STATEMENT OF FINANCIAL POSITION

The impact of IFRS 16 as at 1 January 2019 on the recognition of additional financial liabilities and right-of-use assets is presented in the table below:

IMPACT ON THE STATEMENT OF FINANCIAL POSITION	As at 31.12.2018 (IAS 17)	Effect of IFRS 16 implementation	As at 01.01.2019 (IFRS 16)
ASSETS			
Property, plant and equipment, including:	449	5,427	**5,876**
right-of-use assets		5,427	**5,427**
LIABILITIES AND EQUITY			
Other liabilities, including:	121,974	5,427	**127,401**
lease liabilities		5,427	**5,427**

Reconciliation of the difference between amounts of future lease payments under irrevocable operating leases disclosed in accordance with IAS 17 as at the end of 2018 and the lease liabilities recognized as at 1 January 2019, i.e. as at the date of the first application of IFRS 16, is presented below:

OPERATING LEASE LIABILITIES AS AT 31 DECEMBER 2018 (NOT DISCOUNTED)	5,297
Agreements whose assessment changed and are treated as service contracts since 1 January 2019	(56)
Impact of discount	(486)
Adjusted for the difference in the recognition of the extension/termination option, including notice period	672
LEASE LIABILITIES AS AT 1 JANUARY 2019	5,427

IMPACT ON EQUITY

The implementation of IFRS 16 had no impact on retained earnings and equity as at 1 January 2019 due to the fact that the right-of-use assets and lease liabilities were recognized in the same amounts.

IMPACT ON THE INCOME STATEMENT

Starting from 1 January 2019, there will be a change in the presentation of costs (rent will be replaced by depreciation and interest expense) and the timing of their recognition (costs relating to leases will be recognized faster due to the fact that interest expense will be recognized using the effective interest rate method which has not been applied previously).

(IN PLN THOUSANDS)

3.2 Other amendments to the published standards and interpretations which became binding as of 1 January 2019

The implementation of new standards and interpretations and amendments thereto, which became binding on 1 January 2019, such as, among other things, changes to IFRS 9, IAS 28, IAS 19, apart from IFRS 16, as described in chapter 3.1, did not have a material impact on these financial statements.

3.3 New Standards and Interpretations, and amendments thereto, which have been published and endorsed by the European Union, but are not yet binding and have not been applied by the Bank

The Bank does not identify any new standards or amendments to standards, or interpretations which have been published and endorsed by the European Union, but are not binding for periods beginning on 1 January 2019 and have not been applied to the condensed interim financial statements, but which will have a material impact on the financial statements.

3.4 New standards and interpretations, and the amendments thereto, which were published and have not yet been endorsed by the European Union

Amendments to IFRS 3, IFRS 10, IAS 1, IAS 8 and IAS 28, and the implementation of IFRS 17 will not have a material impact on the Bank's financial statements.

4. Explanation of the differences between previously published financial statements and these financial statements

To better reflect the information in the condensed interim financial statements of PKO Bank Hipoteczny SA for the six-month period ended 30 June 2019 the Bank made the following changes to recognition and presentation:

INCOME STATEMENT	01.01.2018 - 30.06.2018 before restatement	recognition of "regulatory charges" as a separate item	01.01.2018 - 30.06.2018 restated
Administrative expenses	(28,241)	6,385	(21,856)
Regulatory charges	-	(6,385)	(6,385)
Total	**(28,241)**	**-**	**(28,241)**

(IN PLN THOUSANDS)

NOTES TO THE INCOME STATEMENT

5. INTEREST INCOME AND EXPENSES

INTEREST INCOME	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Interest income recognized under the effective interest rate method, including:	**403,457**	**306,414**
on financial instruments measured at amortized cost, including:	394,093	298,361
loans and advances to customers	394,044	298,328
amounts due from banks and on mandatory reserve	49	33
instruments measured at fair value through other comprehensive income, including:	9,364	8,053
debt securities	9,364	8,053
Income similar to interest income on instruments measured at fair value through profit or loss, including:	**780**	**468**
hedging IRS transactions (net)	780	468
Total	**404,237**	**306,882**
including: interest income on impaired financial instruments	233	92

INTEREST EXPENSE	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Interest income on financial instruments measured at amortized cost, including:	**(150,589)**	**(117,603)**
loans received and overdraft facility used	(18,645)	(14,817)
deferred payment for the purchase of receivables	(14,949)	(25,752)
mortgage-covered bonds issued	(77,934)	(49,459)
bonds issued	(38,980)	(27,575)
lease liabilities	(81)	
Interest expense on instruments measured at fair value through profit or loss, including:	**(103,330)**	**(69,778)**
hedging CIRS transactions (net)	(103,330)	(69,778)
Total	**(253,919)**	**(187,381)**

6. FEE AND COMMISSION INCOME AND EXPENSES

FEE AND COMMISSION INCOME	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Fees for property valuation	2,758	2,951
Fees for property inspection	1,340	1,185
Commission for full or partial early repayment of loans	2,872	2,162
Other	866	618
Total	**7,836**	**6,916**

(IN PLN THOUSANDS)

FEE AND COMMISSION EXPENSE	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Preparation by property valuers of appraisal reports on Property Value for Mortgage Lending Purposes (BHWN)	(4,179)	(4,461)
Expenses related to bonds issuance programme	(2,008)	(1,754)
Expenses related to credit lines	(1,528)	(1,106)
Expenses related to mortgage-covered bonds issuance programme	(607)	(599)
Loan insurance costs	(1,794)	(1,234)
Commission on other operating services	(97)	(76)
Costs of debt collection and intermediation in selling collateral	(39)	-
Total	**(10,252)**	**(9,230)**

7. Net gain / (loss) in financial instruments measured at fair value through profit or loss

NET GAIN / (LOSS) IN FINANCIAL INSTRUMENTS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Net gain / (loss) on derivatives	33	24
Net gain / (loss) on IRS derivative instruments related to hedge ineffectiveness	33	24
Total	**33**	**24**

The Bank concludes and maintains IRS derivative instruments solely for hedging purposes.

8. Net foreign exchange gains / (losses)

NET FOREIGN EXCHANGE GAINS / (LOSSES)	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Result on revaluation	13	(879)
Gain / (loss) on derivative instruments (CIRS, FX-Forward) before designation to hedge accounting	(389)	(1,376)
Gain / (loss) on derivative instruments (CIRS, FX-Forward) related to hedge ineffectiveness	(1,519)	6,245
Total	**(1,895)**	**3,990**

The Bank concludes and maintains CIRS and FX Forward derivative instruments solely for hedging purposes.

9. Gains / (losses) on derecognition of financial instruments not measured at fair value through profit or loss

In the first half of 2019 and in the first half of 2018 there were no gains or losses on derecognition of financial assets not measured at fair value through profit or loss.

10. Net gains / (losses) on modification

NET GAIN / (LOSS) ON MODIFICATION	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Financial instruments measured at amortized cost	370	(257)
Total	**370**	**(257)**

(IN PLN THOUSANDS)

11. NET CREDIT LOSSES

NET CREDIT LOSSES	Note	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Net allowances on loans and advances to customers	22	(5,545)	(4,395)
Net provisions for loan commitments	30	(135)	(50)
Total		**(5,680)**	**(4,445)**

12. OTHER OPERATING INCOME AND EXPENSES

OTHER OPERATING INCOME	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Sundry income	317	301
Other	7	1
Total	**324**	**302**

OTHER OPERATING EXPENSES	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Sundry costs	(281)	(268)
Other	(25)	(33)
Total	**(306)**	**(301)**

13. ADMINISTRATIVE EXPENSES

ADMINISTRATIVE EXPENSES	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Employee benefits	(8,705)	(8,007)
Overheads	(14,695)	(12,727)
Amortization and depreciation, including:	(1,637)	(1,122)
property, plant and equipment	(120)	(134)
assets in respect of the right to use, including:	(586)	
real estate	(506)	
cars	(80)	
intangible assets	(931)	(988)
Total	**(25,037)**	**(21,856)**

EMPLOYEE BENEFITS	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Wages and salaries, including:	(7,331)	(6,726)
provision for disability and retirement benefits	(10)	(29)
Salary surcharges	(1,071)	(1,005)
Other employee benefits	(303)	(276)
Total	**(8,705)**	**(8,007)**

(IN PLN THOUSANDS)

OVERHEADS	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Services relating to supporting operations under Outsourcing Agreement [1]	(1,647)	(1,471)
Servicing of loans granted and receivables purchased under Outsourcing Agreement [1]	(9,536)	(7,537)
External services under other contracts	(1,411)	(1,352)
IT costs	(888)	(742)
Non-life insurance costs	(182)	(133)
Rents and service charges		(913)
Car leases		(133)
Costs related to short-term lease contracts	(85)	
Costs related to lease contracts for low-value assets (other than short-term), non-deductible VAT expenses and service charges	(411)	
Other	(535)	(446)
Total	**(14,695)**	**(12,727)**

[1] The Outsourcing Agreement is described in Note 36.1 “Related-party transactions – capital links”

14. Regulatory charges

REGULATORY CHARGES	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Contribution and payments to the Bank Guarantee Fund (BGF), including:	(22,058)	(4,556)
resolution fund	(22,058)	(4,556)
Payments to PFSA	(2,235)	(1,690)
Other taxes and charges	(190)	(139)
Total	**(24,483)**	**(6,385)**

15. Income tax

INCOME TAX EXPENSE	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Current income tax expense	(16,433)	(13,905)
Deferred income tax due to temporary differences	(5,117)	(4,339)
Income tax reported in the income statement	**(21,550)**	**(18,244)**
Income tax reported in other comprehensive income due to temporary differences	(20,676)	(9,455)
Total	**(42,226)**	**(27,698)**

(IN PLN THOUSANDS)

RECONCILIATION OF THE EFFECTIVE TAX RATE	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Profit before income tax	**52,179**	**60,832**
Corporate income tax calculated at the statutory tax rate in force in Poland (19%)	(9,914)	(11,558)
Effect of permanent differences between profit before income tax and taxable income, including:	**(11,636)**	**(6,686)**
tax on certain financial institutions	(7,419)	(5,211)
fees to BGF	(4,191)	(866)
costs exceeding the limit set in Article 15e of the CIT Act	-	(596)
PFRON (State Disabled Persons Fund) costs	(9)	(8)
impact of other permanent differences	(17)	(5)
Income tax reported in the income statement	**(21,550)**	**(18,244)**
Effective tax rate	**41.30%**	**29.99%**
Temporary difference resulting from deferred tax reported in the income statement	(5,117)	(4,339)
Current income tax expense reported in the income statement	(16,433)	(13,905)

TAX GROUP

Based on the contract dated 5 November 2018 PKO Bank Polski SA, as the parent, jointly with its two subsidiaries: PKO Bank Hipoteczny SA and PKO Leasing SA, created the Podatkowa Grupa Kapitałowa Powszechnej Kasy Oszczędności Banku Polskiego Spółki Akcyjnej ("Tax Group", "PGK PKO Banku Polskiego SA"). The contract was registered by the Head of the Second Masovian Tax Office in Warsaw. PGK PKO Banku Polskiego SA was established for three tax years. The first tax year began on 1 January 2019.

A tax group is an institution of the tax law stipulated in the provisions of the Corporate Income Tax Act. Its creation means that the income of the Tax Group companies will be consolidated for corporate income tax purposes and that solutions will be available facilitating the application of other, in particular operational, regulations of the Corporate Income Tax Act, dedicated specifically to Tax Groups.

Due to PKO Bank Hipoteczny SA acceding to the PGK PKO Banku Polskiego SA tax group as of 1 January 2019, the current income tax liability shown in the table below as at 30 June 2019 is a liability to PKO Bank Polski SA.

CURRENT INCOME TAX LIABILITIES	30.06.2019	31.12.2018
Current income tax liabilities	9,947	3,159

Deferred tax assets/provisions

NET DEFERRED TAX ASSETS/PROVISION	31.12.2018	Income statement	Other comprehensive income	30.06.2019
Deferred tax provision				
Interest accrued on loans and advances to customers	7,655	897	-	8,552
Interest accrued and discount on securities	727	573	-	1,300
Adjustment of loan portfolio valuation under the straight-line and effective interest rate methods	19,575	2,813	-	22,388
Adjustment of own issues valuation under the straight-line and effective interest rate methods	3,586	199	-	3,785
Deferred costs	825	(31)	-	794
Difference between carrying amount and tax value of property, plant and equipment and intangible assets	5	(2)	-	3
Valuation of securities	1,038	-	(300)	738
Valuation of derivatives	22,590	120	21,090	43,800
Gross deferred income tax provision	**56,001**	**4,569**	**20,790**	**81,360**
Deferred income tax assets				
Interest accrued on amounts due to banks	5,996	(3,760)	-	2,236
Interest accrued and discount on liabilities in respect of securities issued	11,201	678	-	11,879
Allowances for credit losses	5,132	891	-	6,023
Expenses to be paid	1,639	141	-	1,780
Valuation of securities	-	-	100	100
Valuation of derivatives	6,730	1,488	14	8,232
Difference between depreciation of the right-of-use asset and the cost of lease financing (IFRS 16)	-	14	-	14
Gross deferred income tax assets	**30,698**	**(548)**	**114**	**30,264**
Net deferred income tax assets / (provision) (presented in the statement of financial position)	**(25,303)**	**(5,117)**	**(20,676)**	**(51,096)**

16. Earnings per share

EARNINGS PER SHARE	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Earnings attributable to ordinary shareholders (in PLN '000)	30,629	42,588
Weighted average number of ordinary shares during the period (in thousands)	1,400,243	1,200,000
Earnings per share (in PLN per share)	0.02	0.04

In the first half of 2019 and in the first half of 2018 there were no instruments which would dilute the earnings per share. Therefore, the amount of diluted earnings per share is the same as the amount of basic earnings per share.

(IN PLN THOUSANDS)

NOTES TO THE STATEMENT OF FINANCIAL POSITION

17. Cash and balances with the Central Bank

CASH AND BALANCES WITH THE CENTRAL BANK	30.06.2019	31.12.2018
Current account with the Central Bank	22	6
Total	**22**	**6**

18. Amounts due from banks

AMOUNTS DUE FROM BANKS	30.06.2019	31.12.2018
Measured at amortized cost		
current accounts	55	22
Total	**55**	**22**

Information on exposures to credit risk relating to amounts due from banks is provided in Note 40 “Credit risk management”.

All amounts due from banks were classified to Stage 1 as at 30 June 2019 and 31 December 2018. During the period ended 30 June 2019 and in 2018, there were no transfers between stages for amounts due from banks.

19. Derivative hedging instruments

STRATEGY 1	HEDGING CASH FLOW VOLATILITY FROM MORTGAGE LOANS PLN DUE TO CHANGES IN REFERENCE INTEREST RATES AND FROM CONVERTIBLE CURRENCY MORTGAGE COVERED BONDS RESULTING FROM CHANGES IN THE FOREIGN EXCHANGE RATE, USING CIRS AND FX-FORWARD HEDGING INSTRUMENTS
DESCRIPTION OF THE HEDGING RELATIONSHIP	Elimination of cash flow volatility from mortgage loans in PLN due to changes in reference interest rates and from convertible currency mortgage covered bonds resulting from changes in the foreign exchange rate, using CIRS hedging instruments and a series of FX-Forward transactions in convertible currencies hedging the FX exposures which mature on the dates of payment of coupons from convertible currency mortgage covered bonds.
HEDGED RISK	Currency and interest rate risks.
HEDGING INSTRUMENTS	▪ Cross-Currency Interest Rate Swap (CIRS) transactions in which the Bank pays a coupon based on a variable PLN rate and receives a coupon based on a fixed rate for the convertible currency. If PKO Bank Hipoteczny SA is declared bankrupt by the court, the CIRS transactions will automatically be extended by 12 months on the terms and conditions set on the transaction date; ▪ an optional series of FX-Forward transactions in the convertible foreign currency hedging the FX exposures which mature on the dates of payment of coupons from convertible currency mortgage covered bonds.
HEDGED ITEM	▪ part of the portfolio of the housing loans included in the cover pool of PLN mortgage covered bonds at floating rates. The interest rates on the loans are indexed by the 3M WIBOR rate. The margin on mortgage loans is excluded from hedging; ▪ fixed-rate mortgage covered bonds issued in a convertible currency.
PERIOD IN WHICH CASH FLOWS ARE EXPECTED	Period in which cash flows are expected to occur and when they are expected to affect the financial results: July 2019 – August 2024.

DERIVATIVE HEDGING INSTRUMENTS	NOMINAL VALUE OF DERIVATIVE HEDGING INSTRUMENTS		CARRYING AMOUNT (FAIR VALUE) OF HEDGING INSTRUMENTS		INEFFECTIVE PORTION OF CASH FLOW HEDGES RECOGNIZED IN THE INCOME STATEMENT	CHANGE IN THE FAIR VALUE OF HEDGING INSTRUMENT SINCE DESIGNATION
			Assets	Liabilities		
30.06.2019						
CIRS EUR/PLN	fixed EUR	2,775,514	160,175	47,836	(1,502)	108,882
	float PLN	11,863,682				
FX-Forward	purchase EUR	2,891	332	703	(17)	
	sale EUR	1,817				
31.12.2018						
CIRS EUR/PLN	fixed EUR	2,076,360	162,100	14,786	1,334	143,605
	float PLN	8,858,819				
FX-Forward	purchase EUR	2,173	237	468	(24)	
	sale EUR	1,656				

The average fixed rate weighted with the nominal value for CIRS transactions amounted to 0.504% as at 30 June 2019, and 0.585% as at 31 December 2018.

HEDGED ITEMS	CARRYING AMOUNT OF HEDGED ITEMS	ITEM OF THE STATEMENT OF FINANCIAL POSITION	CHANGE IN THE FAIR VALUE OF HEDGED ITEMS SINCE DESIGNATION
30.06.2019			
floating rate PLN loans	11,863,682	Loans and advances to customers	(119,230)
fixed-rate mortgage covered bonds issued in a convertible currency	11,806,052	Mortgage covered bonds issued	
31.12.2018			
floating rate PLN loans	8,858,819	Loans and advances to customers	(150,942)
fixed-rate mortgage covered bonds issued in a convertible currency	8,930,571	Mortgage covered bonds issued	

STRATEGY 2	HEDGING CASH FLOW VOLATILITY FROM CASH LOANS IN PLN WITH FLUCTUATING INTEREST RATES, RESULTING FROM THE RISK OF FLUCTUATIONS IN INTEREST RATES, USING IRS TRANSACTIONS
DESCRIPTION OF THE HEDGING RELATIONSHIP	Elimination of the risk of cash flow fluctuations from the floating interest rate PLN loan portfolio resulting from the risk of changes in interest rates in the period covered by the hedge using IRS transactions.
HEDGED RISK	Interest rate risk.
HEDGING INSTRUMENTS	IRS transactions where the Bank pays coupons based on the floating 3M WIBOR rate, and receives coupons based on a fixed rate on the nominal value for which they were concluded.
HEDGED ITEM	A part of the portfolio of housing loans in PLN indexed to the WIBOR 3M floating rate. The margin on mortgage loans is excluded from hedging
PERIOD IN WHICH CASH FLOWS ARE EXPECTED	Period in which cash flows are expected to occur and when they are expected to affect the financial results: July 2019 – August 2028.

(IN PLN THOUSANDS)

DERIVATIVE HEDGING INSTRUMENTS	NOMINAL VALUE OF DERIVATIVE HEDGING INSTRUMENTS		CARRYING AMOUNT (FAIR VALUE) OF HEDGING INSTRUMENTS		INEFFECTIVE PORTION OF CASH FLOW HEDGES RECOGNIZED IN THE INCOME STATEMENT	CHANGE IN THE FAIR VALUE OF HEDGING INSTRUMENT SINCE DESIGNATION
			Assets	Liabilities		
30.06.2019						
IRS PLN	PLN	325,000	12,977	-	33	13,190
31.12.2018						
IRS PLN	PLN	325,000	5,952	-	63	6,165

The average fixed rate weighted with the nominal value for IRS transactions amounted to 2.84% as at 30 June 2019 as well as at 31 December 2018.

HEDGED ITEMS	CARRYING AMOUNT OF HEDGED ITEMS	ITEM OF THE STATEMENT OF FINANCIAL POSITION	CHANGE IN THE FAIR VALUE OF HEDGED ITEMS SINCE DESIGNATION
30.06.2019			
floating rate PLN loans	325,000	Loans and advances to customers	(13,258)
31.12.2018			
floating rate PLN loans	325,000	Loans and advances to customers	(6,248)

FINANCIAL INFORMATION:

CARRYING AMOUNT (FAIR VALUE) OF DERIVATIVES USED AS CASH FLOW HEDGES	30.06.2019		31.12.2018	
	Assets	Liabilities	Assets	Liabilities
IRS	12,977	-	5,952	-
CIRS	160,175	47,836	162,100	14,786
FX-Forward	332	703	237	468
Total	**173,484**	**48,539**	**168,289**	**15,254**

The Bank concludes and maintains derivative instruments exclusively for hedging purposes.

NOMINAL VALUE OF HEDGING INSTRUMENTS BY MATURITY AS AT 30 JUNE 2019	up to 1 month	from 1 to 3 months	from 3 months to 1 year	from 1 to 5 years	more than 5 years	Total
IRS						
PLN fixed-float	-	-	-	265,000	60,000	**325,000**
CIRS						
float PLN sale	-	-	-	9,728,941	2,134,741	**11,863,682**
fixed EUR purchase (original currency)	-	-	-	2,275,984	499,530	**2,775,514**
FX-Forward						
PLN sale	-	-	171	11,866	1,978	**14,015**
EUR purchase (original currency)	-	-	39	2,459	393	**2,891**
PLN purchase	-	295	2,847	5,221	-	**8,363**
EUR sale (original currency)	-	66	629	1,122	-	**1,817**

(IN PLN THOUSANDS)

NOMINAL VALUE OF HEDGING INSTRUMENTS BY MATURITY AS AT 31 DECEMBER 2018	up to 1 month	from 1 to 3 months	from 3 months to 1 year	from 1 to 5 years	more than 5 years	Total
IRS						
PLN fixed-float	-	-	-	265,000	60,000	**325,000**
CIRS						
float PLN sale	-	-	-	4,514,349	4,344,470	**8,858,819**
fixed EUR purchase (original currency)	-	-	-	1,052,370	1,023,990	**2,076,360**
FX-Forward						
PLN sale	-	-	-	6,607	4,122	**10,729**
EUR purchase (original currency)	-	-	-	1,340	833	**2,173**
PLN purchase	435	-	1,497	5,731	-	**7,663**
EUR sale (original currency)	101	-	329	1,226	-	**1,656**

CHANGE IN OTHER COMPREHENSIVE INCOME ON CASH FLOW HEDGES AND INEFFECTIVE PORTION OF CASH FLOW HDGES	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
Accumulated other comprehensive income on cash flow hedges at the beginning of the period, gross	73,411	(38,730)
Gains / (Losses) recognized in other comprehensive income during the period	(123,442)	355,793
Amounts transferred from other comprehensive income to the income statement during the period	234,367	308,742
- interest income	(780)	468
- interest expenses	103,330	(69,778)
- net foreign exchange gains/(losses)	131,817	378,052
Accumulated other comprehensive income on cash flow hedges at the end of the period, gross	184,336	8,321
Tax effect	(35,025)	(1,582)
Accumulated other comprehensive income on cash flow hedges at the end of the period, net	**149,311**	**6,739**
Ineffective portion of cash flow hedges recognized in the income statement	**(1,486)**	**6,269**
Impact on other comprehensive income during the period, gross	110,925	47,051
Deferred tax on cash flow hedges	(21,076)	(8,940)
Impact on other comprehensive income during the period, net	**89,849**	**38,111**

20. Securities

SECURITIES	30.06.2019	31.12.2018
Measured at fair value through other comprehensive income, including:	1,158,142	842,965
issued by the State Treasury, PLN Treasury bonds	1,158,142	842,965
Total	**1,158,142**	**842,965**

SECURITIES BY MATURITY	30.06.2019	31.12.2018
Issued by the State Treasury, PLN Treasury bonds		
up to 1 month	-	186,506
from 3 months to 1 year	160,074	-
from 1 to 5 years	703,000	479,474
more than 5 years	295,068	176,985
Total	**1,158,142**	**842,965**

(IN PLN THOUSANDS)

SECURITIES BY NOMINAL VALUE AND AVERAGE YIELD	30.06.2019	31.12.2018
Issued by the State Treasury, PLN Treasury bonds	1,156,480	836,480
Average yield	1.79%	1.78%

Information on credit risk exposure in connection with securities is provided in Note 40 "Credit risk management".

The whole balance of securities as at 30 June 2019 and 31 December 2018 was classified in Stage 1. There were no transfers of securities between the stages in the year ended 30 June 2019 and in 2018.

21. LOANS AND ADVANCES TO CUSTOMERS

LOANS AND ADVANCES TO CUSTOMERS	30.06.2019	31.12.2018
Measured at amortized cost		
Residential mortgage loans, gross, including:	24,632,903	21,098,742
loans granted	10,412,472	8,781,520
receivables acquired	14,220,431	12,317,222
Allowances for expected credit losses	(33,707)	(28,273)
Loans and advances to customers, net	**24,599,196**	**21,070,469**

In the first half of 2019 the Bank purchased, based on the Framework Agreement for the Sale of Receivables signed with PKO Bank Polski SA on 17 November 2015, receivables portfolios relating to residential mortgage loans amounting to PLN 2,519,297 thousand, and in the first half of 2018 amounting to PLN 1,880,968 thousand. The purchase price was determined on an arm's length basis, based on the valuation made by an independent expert. The receivables purchased were recognized on the transfer dates set in the Receivables Sale Agreements, on which the Bank acquired the rights to the cash flows from individual portfolios, and assumed all related liability for costs and economic risks in the constituent receivables. The purchase of the receivable portfolios was financed by the liability, the nature of which is described in Note 25. The Bank ultimately refinances the purchased receivable portfolios primarily through issuing mortgage covered bonds.

Loans granted and receivables purchased that have been entered in the Bank's cover pool represent collateral for mortgage covered bonds issued, as described in Note 27.

Information about the quality of the loan portfolio is also presented in Note 40.4 "Forecasting and monitoring of credit risk".

Information about exposure to credit risk for loans and advances granted measured at amortized cost are described in Note 22 "Expected credit losses".

(IN PLN THOUSANDS)

22. EXPECTED CREDIT LOSSES

GROSS FINANCIAL ASSETS AND ALLOWANCES FOR EXPECTED CREDIT LOSSES AND NOMINAL AMOUNT OF LOAN COMMITMENTS AND PROVISIONS

FINANCIAL ASSETS AND ALLOWANCES FOR EXPECTED CREDIT LOSSES AS AT 30.06.2019	Assets with no significant increase in credit risk since initial recognition, gross (Stage 1)	Allowances for expected credit losses (Stage 1)	Assets with a significant increase in credit risk since initial recognition, but not credit-impaired, gross (Stage 2)	Allowances for expected credit losses (Stage 2)	Credit-impaired assets, gross (Stage 3)	Allowances for expected credit losses (Stage 3)	Total gross amount	Total allowances for expected credit losses
Measured at fair value through other comprehensive income								
securities	1,158,142	-	-	-	-	-	1,158,142	-
issued by the State Treasury, PLN Treasury bonds	1,158,142	-	-	-	-	-	1,158,142	-
Total	1,158,142	-	-	-	-	-	1,158,142	-
Measured at amortized cost								
amounts due from banks	55	-	-	-	-	-	55	-
loans and advances to customers	24,326,926	(9,014)	293,678	(20,290)	12,299	(4,403)	24,632,903	(33,707)
residential mortgage loans	24,326,926	(9,014)	293,678	(20,290)	12,299	(4,403)	24,632,903	(33,707)
loans granted	10,248,890	(4,751)	160,631	(11,014)	2,951	(1,303)	10,412,472	(17,068)
receivables acquired	14,078,036	(4,263)	133,047	(9,276)	9,348	(3,100)	14,220,431	(16,639)
other financial assets	386	-	-	-	-	-	386	-
Total	24,327,367	(9,014)	293,678	(20,290)	12,299	(4,403)	24,633,344	(33,707)

As at 30 June 2019 there were no purchased or originated credit-impaired assets (POCI).

LOAN COMMITMENTS AND PROVISIONS AS AT 30.06.2019	Nominal amount of loan commitments with no significant increase in credit risk since initial recognition (Stage 1)	Provisions for loan commitments (Stage 1)	Nominal amount of loan commitments with a significant increase in credit risk since initial recognition, but not credit-impaired (Stage 2)	Provisions for loan commitments (Stage 2)	Nominal amount of credit-impaired loan commitments (Stage 3)	Provisions for loan commitments (Stage 3)	Total nominal amount	Total provisions for loan commitments
Loan commitments	619,579	(144)	2,219	(135)	-	-	621,798	(279)

(IN PLN THOUSANDS)

FINANCIAL ASSETS AND ALLOWANCES FOR EXPECTED CREDIT LOSSES AS AT 31.12.2018	Assets with no significant increase in credit risk since initial recognition, gross (Stage 1)	Allowances for expected credit losses (Stage 1)	Assets with a significant increase in credit risk since initial recognition, but not credit-impaired, gross (Stage 2)	Allowances for expected credit losses (Stage 2)	Credit-impaired assets, gross (Stage 3)	Allowances for expected credit losses (Stage 3)	Total gross amount	Total allowances for expected credit losses
Measured at fair value through other comprehensive income								
securities	842,965	-	-	-	-	-	842,965	-
issued by the State Treasury, PLN Treasury bonds	842,965	-	-	-	-	-	842,965	-
Total	842,965	-	-	-	-	-	842,965	-
Measured at amortized cost								
amounts due from banks	22	-	-	-	-	-	22	-
loans and advances to customers	20,823,722	(7,108)	266,928	(17,979)	8,092	(3,186)	21,098,742	(28,273)
residential mortgage loans	20,823,722	(7,108)	266,928	(17,979)	8,092	(3,186)	21,098,742	(28,273)
loans granted	8,636,038	(3,480)	143,432	(10,730)	2,050	(922)	8,781,520	(15,132)
receivables acquired	12,187,684	(3,628)	123,496	(7,249)	6,042	(2,264)	12,317,222	(13,141)
other financial assets	449	-	-	-	-	-	449	-
Total	20,824,193	(7,108)	266,928	(17,979)	8,092	(3,186)	21,099,213	(28,273)

As at 31 December 2018 there were no purchased or originated credit-impaired assets (POCI).

LOAN COMMITMENTS AND PROVISIONS AS AT 31.12.2018	Nominal amount of loan commitments with no significant increase in credit risk since initial recognition (Stage 1)	Provisions for loan commitments (Stage 1)	Nominal amount of loan commitments with a significant increase in credit risk since initial recognition, but not credit-impaired (Stage 2)	Provisions for loan commitments (Stage 2)	Nominal amount of credit-impaired loan commitments (Stage 3)	Provisions for loan commitments (Stage 3)	Total nominal amount	Total provisions for loan commitments
Loan commitments	717,808	(103)	1,409	(41)	-	-	719,217	(144)

(IN PLN THOUSANDS)

Transfers between impairment stages for financial assets and loan commitments

FINANCIAL ASSETS AS AT 30.06.2019 – TRANSFERS BETWEEN STAGES in 1H 2019	Gross carrying amount							TOTAL GROSS AMOUNT	Allowances for expected credit losses							TOTAL ALLOWANCES	TOTAL, NET
	AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			
		from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1			from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1		
Measured at fair value through other comprehensive income																	
securities	1,158,142	-	-	-	-	-	-	**1,158,142**	-	-	-	-	-	-	-	-	**1,158,142**
issued by the State Treasury, PLN Treasury bonds	1,158,142	-	-	-	-	-	-	**1,158,142**	-	-	-	-	-	-	-	-	**1,158,142**
Measured at amortized cost																	
amounts due from banks	55	-	-	-	-	-	-	**55**	-	-	-	-	-	-	-	-	**55**
loans and advances to customers	24,302,856	182,005	141,248	4,365	1,015	1,414	-	**24,632,903**	(20,628)	(10,954)	(313)	(1,223)	(167)	(422)	-	**(33,707)**	**24,599,196**
residential mortgage loans	24,302,856	182,005	141,248	4,365	1,015	1,414	-	**24,632,903**	(20,628)	(10,954)	(313)	(1,223)	(167)	(422)	-	**(33,707)**	**24,599,196**
loans granted	10,223,925	105,006	82,638	600	-	303	-	**10,412,472**	(10,790)	(5,828)	(220)	(197)	-	(33)	-	**(17,068)**	**10,395,404**
receivables acquired	14,078,931	76,999	58,610	3,765	1,015	1,111	-	**14,220,431**	(9,838)	(5,126)	(93)	(1,026)	(167)	(389)	-	**(16,639)**	**14,203,792**
other financial assets	386	-	-	-	-	-	-	**386**	-	-	-	-	-	-	-	-	**386**
Total financial assets	**25,461,439**	**182,005**	**141,248**	**4,365**	**1,015**	**1,414**	**-**	**25,791,486**	**(20,628)**	**(10,954)**	**(313)**	**(1,223)**	**(167)**	**(422)**	**-**	**(33,707)**	**25,757,779**

Transfers between impairment stages are presented in the gross carrying amount and amount of allowance as at 30 June 2019. In the case of loans and advances to customers, which changed stages a number of times, the movement was presented as a transfer from the stage to which they belonged as at 1 January 2019 or upon initial recognition to the impairment stage to which they belonged as at 30 June 2019.

LOAN COMMITMENTS AS AT 30.06.2019 – TRANSFERS BETWEEN STAGES in 1H 2019	Nominal value of loan commitments							TOTAL NOMINAL AMOUNT	Provisions for loan commitments							TOTAL PROVISIONS	TOTAL, NET
	AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			
		from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1			from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1		
Loan commitments																	
residential mortgage loans	619,635	1,963	200	-	-	-	-	**621,798**	(152)	(127)	-	-	-	-	-	**(279)**	**621,519**

(IN PLN THOUSANDS)

FINANCIAL ASSETS AS AT 30.06.2018 – TRANSFERS BETWEEN STAGES IN 1H 2018	Gross carrying amount							TOTAL GROSS AMOUNT	Allowances for expected credit losses							TOTAL ALLOWANCES	TOTAL, NET
	AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			
		from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1			from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1		
Measured at fair value through other comprehensive income																	
securities	842,727	-	-	-	-	-	-	**842,727**	-	-	-	-	-	-	-	-	**842,727**
issued by the State Treasury, PLN Treasury bonds	842,727	-	-	-	-	-	-	**842,727**	-	-	-	-	-	-	-	-	**842,727**
Measured at amortized cost																	
amounts due from banks	122,172	-	-	-	-	-	-	**122,172**	-	-	-	-	-	-	-	-	**122,172**
loans and advances to customers	18,880,989	119,375	87,771	1,524	288	-	-	**19,089,947**	(15,253)	(7,577)	(625)	(588)	(59)	-	-	**(24,102)**	**19,065,845**
residential mortgage loans	18,880,989	119,375	87,771	1,524	288	-	-	**19,089,947**	(15,253)	(7,577)	(625)	(588)	(59)	-	-	**(24,102)**	**19,065,845**
loans granted	6,787,818	64,574	34,434	-	-	-	-	**6,886,826**	(6,606)	(4,311)	(278)	-	-	-	-	**(11,195)**	**6,875,631**
receivables acquired	12,093,171	54,801	53,337	1,524	288	-	-	**12,203,121**	(8,647)	(3,266)	(347)	(588)	(59)	-	-	**(12,907)**	**12,190,214**
other financial assets	289	-	-	-	-	-	-	**289**	-	-	-	-	-	-	-	-	**289**
Total financial assets	**19,846,177**	**119,375**	**87,771**	**1,524**	**288**	-	-	**20,055,135**	**(15,253)**	**(7,577)**	**(625)**	**(588)**	**(59)**	-	-	**(24,102)**	**20,031,033**

Transfers between impairment stages are presented in the gross carrying amount and amount of allowance as at 30 June 2018. In the case of loans and advances to customers, which changed stages a number of times, the movement was presented as a transfer from the stage to which they belonged as at 1 January 2018 or upon initial recognition to the impairment stage to which they belonged as at 30 June 2018.

LOAN COMMITMENTS AS AT 30.06.2018 – TRANSFERS BETWEEN STAGES IN 1H 2018	Nominal value of loan commitments							TOTAL NOMINAL AMOUNT	Provisions for loan commitments							TOTAL PROVISIONS	TOTAL, NET
	AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			AMOUNTS NOT SUBJECT TO TRANSFER	Transfers between Stage 1 (S1) and Stage 2 (S2)		Transfers between Stage 2 (S2) and Stage 3 (S3)		Transfers between Stage 1 (S1) and Stage 3 (S3)			
		from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1			from S1 to S2	from S2 to S1	from S2 to S3	from S3 to S2	from S1 to S3	from S3 to S1		
Loan commitments																	
residential mortgage loans	783,271	1,061	327	-	-	-	-	**784,659**	(130)	(28)	-	-	-	-	-	**(158)**	**784,501**

(IN PLN THOUSANDS)

CHANGES IN ALLOWANCES FOR EXPECTED CREDIT LOSSES

CHANGES IN ALLOWANCES FOR EXPECTED CREDIT LOSSES ON FINANCIAL ASSETS IN 1H 2019	As at 31.12.2018	Increase due to granting and purchase of loans	Decrease due to derecognition	Changes due to changes in credit risk (net)	Changes due to lengthening the loss recognition horizon from 12 months to lifetime	Changes due to shortening the loss recognition horizon from lifetime to 12 months	Changes due to modification without derecognition, net	Decrease in impairment allowances due to write-down	As at 30.06.2019
Measured at fair value through OCI									
securities	-	-	-	-	-	-	-	-	-
Total	-	-	-	-	-	-	-	-	-
Measured at amortized cost									
amounts due from banks	-	-	-	-	-	-	-	-	-
loans and advances to customers	28,273	835	(15)	953	10,408	(6,781)	145	(111)	33,707
residential mortgage loans	28,273	835	(15)	953	10,408	(6,781)	145	(111)	33,707
other financial assets	-	-	-	-	-	-	-	-	-
Total	28,273	835	(15)	953	10,408	(6,781)	145	(111)	33,707

CHANGES IN ALLOWANCES FOR EXPECTED CREDIT LOSSES ON FINANCIAL ASSETS IN 1H 2018	As at 01.01.2018	Increase due to granting and purchase of loans	Decrease due to derecognition	Changes due to changes in credit risk (net)	Changes due to lengthening the loss recognition horizon from 12 months to lifetime	Changes due to shortening the loss recognition horizon from lifetime to 12 months	Changes due to modification without derecognition, net	Decrease in impairment allowances due to write-down	As at 30.06.2018
Measured at fair value through OCI									
securities	-	-	-	-	-	-	-	-	-
Total	-	-	-	-	-	-	-	-	-
Measured at amortized cost									
amounts due from banks	-	-	-	-	-	-	-	-	-
loans and advances to customers	19,707	1,242	(270)	3,176	7,311	(7,082)	18	-	24,102
residential mortgage loans	19,707	1,242	(270)	3,176	7,311	(7,082)	18	-	24,102
other financial assets	-	-	-	-	-	-	-	-	-
Total	19,707	1,242	(270)	3,176	7,311	(7,082)	18	-	24,102

(IN PLN THOUSANDS)

CHANGES IN THE GROSS CARRYING AMOUNT OF FINANCIAL INSTRUMENTS

CHANGES IN GROSS CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS BASED ON THE DIFFERENCE BETWEEN THE CARRYING AMOUNTS AS AT 31.12.2018 AND 30.06.2019	Gross carrying amount as at 31.12.2018	Increase due to granting and purchase of loans	Changes due to disbursement of tranches	Decrease due to repayment / redemption	Changes due to modification without derecognition, net	Decrease due to derecognition	Decrease due to impairment in connection with a write-down[1)]	Changes due to lengthening the loss recognition horizon from 12 months to lifetime	Changes due to shortening the loss recognition horizon from lifetime to 12 months	Other changes	Gross carrying amount as at 30.06.2019
Measured at fair value through OCI											
securities	**842,965**	892,670	-	(584,752)	-	-	-	-	-	7,259	**1,158,142**
Total	**842,965**	**892,670**	-	**(584,752)**	-	-	-	-	-	**7,259**	**1,158,142**
including: assets measured on a group basis	**842,965**	892,670	-	(584,752)	-	-	-	-	-	7,259	**1,158,142**
Measured at amortized cost											
amounts due from banks	**22**	55	-	(22)	-	-	-	-	-		**55**
loans and advances to customers	**21,098,742**	3,785,145	593,633	(841,252)	9,243	(3,625)	(111)	(169)	(8,703)	-	**24,632,902**
residential mortgage loans	**21,098,742**	3,785,145	593,633	(841,252)	9,243	(3,625)	(111)	(169)	(8,703)	-	**24,632,902**
other financial assets	**449**	386	-	(449)	-	-	-	-	-	-	**386**
Total	**21,099,213**	**3,785,586**	**593,633**	**(841,723)**	**9,243**	**(3,625)**	**(111)**	**(169)**	**(8,703)**	-	**24,633,343**
including: assets measured on a group basis	**21,098,764**	3,785,200	593,633	(841,274)	9,243	(3,625)	(111)	(169)	(8,703)	-	24,632,958

CHANGES IN GROSS CARRYING AMOUNTS OF FINANCIAL INSTRUMENTS BASED ON THE DIFFERENCE BETWEEN THE CARRYING AMOUNTS AS AT 01.01.2018 AND 30.06.2018	Gross carrying amount as at 01.01.2018	Increase due to granting and purchase of loans	Changes due to disbursement of tranches	Decrease due to repayment / redemption	Changes due to modification without derecognition, net	Decrease due to derecognition	Decrease due to impairment in connection with a write-down[1)]	Changes due to lengthening the loss recognition horizon from 12 months to lifetime	Changes due to shortening the loss recognition horizon from lifetime to 12 months	Other changes	Gross carrying amount as at 30.06.2018
Measured at fair value through OCI											
securities	**830,489**	189,251	-	(187,777)	-	-	-	-	-	10,764	**842,727**
Total	**830,489**	**189,251**	-	**(187,777)**	-	-	-	-	-	**10,764**	**842,727**
including: assets measured on a group basis	**830,489**	189,251	-	(187,777)	-	-	-	-	-	10,764	**842,727**
Measured at amortized cost											
amounts due from banks	**5,350**	122,172	-	(5,350)	-	-	-	-	-		**122,172**
loans and advances to customers	**16,047,682**	3,091,787	530,261	(577,583)	5,452	(3,380)	-	(815)	(3,457)	-	**19,089,947**
residential mortgage loans	**16,047,682**	3,091,787	530,261	(577,583)	5,452	(3,380)	-	(815)	(3,457)	-	**19,089,947**
other financial assets	**99**	289	-	(99)	-	-	-	-	-	-	**289**
Total	**16,053,131**	**3,214,248**	**530,261**	**(583,032)**	**5,452**	**(3,380)**	-	**(815)**	**(3,457)**	-	**19,212,408**
including: assets measured on a group basis	**16,053,032**	3,213,959	530,261	(582,933)	5,452	(3,380)	-	(815)	(3,457)	-	**19,212,119**

[1)] The Bank writes off a part of the penalty interest it does not expect to recover.

In the first half of 2019 the Bank purchased receivables portfolios relating to mortgage covered housing loans amounting to PLN 2,519,297 thousand, and in the first half of 2018 amounting to PLN 1,880,968 thousand.

(IN PLN MILLION)

FINANCIAL ASSETS IMPAIRED UPON INITIAL RECOGNITION – POCI

As at 30 June 2019 and 31 December 2018, the Bank had no purchased or originated credit-impaired assets (POCI).

23. INTANGIBLE ASSETS AND PROPERTY, PLANT AND EQUIPMENT

INTANGIBLE ASSETS	30.06.2019	31.12.2018
Intangible assets under construction	229	229
Software	3,012	3,936
Total	**3,241**	**4,165**

PROPERTY, PLANT AND EQUIPMENT	30.06.2019	31.12.2018
Leasehold improvements	22	23
Plant and machinery	261	312
Assets in respect of the right to use, including:	5,596	
real estate	4,926	
cars	670	
Other	74	114
Total	**5,953**	**449**

The item “Other” comprises mainly the Bank’s furniture.

24. OTHER ASSETS

OTHER ASSETS	30.06.2019	31.12.2018
Prepayments and deferred costs, including:	7,219	7,456
deferred costs relating to the overdraft facility	2,417	2,103
deferred costs relating to bond issuance programmes [1)]	116	290
deferred costs relating to mortgage-covered bonds issuance programmes [1)]	1,643	1,948
other prepayments and deferred costs	3,043	3,115
Deferred costs relating to granting loans in the part corresponding to undrawn principal	7,303	8,829
Settlements relating to appraisal reports on Property Value for Mortgage Lending Purposes (MLV)	378	443
Settlements with the state budget	29	35
Other	8	6
Total	**14,937**	**16,769**
including financial assets	386	449

[1)] Costs associated with issue programmes relate to the issue programmes as a whole and cannot be allocated to the individual issues executed as part of the programmes.

25. AMOUNTS DUE TO BANKS

AMOUNTS DUE TO BANKS	30.06.2019	31.12.2018
Measured at amortized cost		
overdraft within the limit available	5,711	10,513
liabilities in respect of overdraft facilities	1,753,420	1,881,512
liabilities in respect of term loans	100,020	100,007
liabilities in respect of the purchase of receivables	2,278,486	2,300,254
Total	**4,137,637**	**4,292,286**

(IN PLN MILLION)

LIABILITIES IN RESPECT OF OVERDRAFT FACILITIES AND TERM LOANS

LENDER	Effective date of agreement	Maturity date	Amount of loan granted as at 30 June 2019	Amount of loan drawn as at 30 June 2019	Liability as at 30 June 2019
PKO Bank Polski SA	29.10.2015	29.10.2022	2,000,000	2,000,000	800,861
PKO Bank Polski SA	02.02.2017	02.02.2020	1,500,000	1,500,000	802,550
Other bank 1	10.06.2019	12.06.2020	150,000	150,000	150,009
Other bank 2	27.12.2018	28.12.2020	100,000	100,000	100,020
Total			**3,750,000**	**3,750,000**	**1,853,440**

LENDER	Effective date of agreement	Maturity date	Amount of loan granted as at 31 December 2018	Amount of loan drawn as at 31 December 2018	Liability as at 31 December 2018
PKO Bank Polski SA	29.10.2015	29.10.2021	1,500,000	1,400,000	828,580
PKO Bank Polski SA	02.02.2017	02.02.2020	1,500,000	1,500,000	902,924
Other bank 1	05.06.2017	10.06.2019	150,000	150,000	150,008
Other bank 2	27.12.2018	28.12.2020	100,000	100,000	100,007
Total			**3,250,000**	**3,150,000**	**1,981,519**

LIABILITIES IN RESPECT OF THE PURCHASE OF RECEIVABLES

The line “Liabilities in respect of the purchase of receivables” represents the liabilities arising from the transactions of purchase of residential mortgage loans portfolios from PKO Bank Polski SA, as specified in Note 21. The maturity date of the liabilities resulting from the purchase of receivables is each time agreed by the parties in the Receivables Sales Agreement. For receivables acquired in 2019, the parties agreed that the payment would be due no later than 18 months from the date of transfer. If the liability is not settled within 1 month from the date of transfer, the principal amount is subject to interest. The Bank ultimately refinances the purchased receivable portfolios primarily through issuing mortgage covered bonds. The liabilities resulting from the purchase of receivables at 30 June 2019 concern portfolios purchased as of the first half of 2019, whereas as at 31 December 2018 the liabilities concerned portfolios purchased from the second quarter of 2018.

26. AMOUNTS DUE TO CUSTOMERS

AMOUNTS DUE TO CUSTOMERS	30.06.2019	31.12.2018
Measured at amortized cost		
amounts due to retail customers- overpaid loans	3,378	4,359
Total	**3,378**	**4,359**

27. MORTGAGE COVERED BONDS ISSUED

MORTGAGE COVERED BONDS ISSUED	30.06.2019	31.12.2018
Measured at amortized cost		
mortgage covered bonds, including issued under:	15,965,585	12,841,500
International Mortgage-Covered Bonds Issue Programme	11,818,575	8,949,417
National Mortgage-Covered Bonds Issue Programme	4,147,010	3,892,083
Total	**15,965,585**	**12,841,500**

(IN PLN MILLION)

REPAYMENT PERIOD OF MORTGAGE COVERED BONDS ISSUED	30.06.2019	31.12.2018
from 1 to 5 years	12,788,592	6,933,749
more than 5 years	3,176,993	5,907,751
Total	**15,965,585**	**12,841,500**

Mortgage covered bonds issued as at 30 June 2019

ISIN	Currency	Nominal amount	Interest as at 30.06.2019	Rate + margin / fixed rate	Issue date	Redemption date	Market
PLPKOHP00017	PLN	30,000	2.47%	WIBOR3M + 0.75 p.p.	11.12.2015	11.12.2020	BondSpot, WSE parallel market
PLPKOHP00025	PLN	500,000	2.37%	WIBOR3M + 0.65 p.p.	27.04.2016	28.04.2021	BondSpot, WSE parallel market
PLPKOHP00033	PLN	500,000	2.31%	WIBOR3M + 0.59 p.p.	17.06.2016	18.06.2021	BondSpot, WSE parallel market
XS1508351357	EUR	500,000	0.13%	fixed rate	24.10.2016	24.06.2022	LuxSE, WSE parallel market
XS1559882821	EUR	25,000	0.82%	fixed rate	02.02.2017	02.02.2024	LuxSE
XS1588411188	EUR	500,000	0.63%	fixed rate	30.03.2017	24.01.2023	LuxSE, WSE parallel market
PLPKOHP00041	PLN	500,000	2.41%	WIBOR3M + 0.69 p.p.	28.04.2017	18.05.2022	BondSpot, WSE parallel market
PLPKOHP00058	PLN	265,000	2.69%	fixed rate in the period	22.06.2017	10.09.2021	BondSpot, WSE parallel market
XS1690669574	EUR	500,000	0.75%	fixed rate	27.09.2017	27.08.2024	LuxSE, WSE parallel market
PLPKOHP00066	PLN	500,000	2.32%	WIBOR3M + 0.60 p.p.	27.10.2017	27.06.2023	BondSpot, WSE parallel market
XS1709552696	EUR	54,000	0.47%	fixed rate	02.11.2017	03.11.2022	LuxSE
XS1795407979	EUR	500,000	0.75%	fixed rate	22.03.2018	24.01.2024	LuxSE, WSE parallel market
PLPKOHP00074	PLN	700,000	2.21%	WIBOR3M + 0.49 p.p.	27.04.2018	25.04.2024	BondSpot, WSE parallel market
PLPKOHP00082	PLN	100,000	2.04%	WIBOR3M + 0.32 p.p.	18.05.2018	29.04.2022	BondSpot, WSE parallel market
PLPKOHP00090	PLN	500,000	2.34%	WIBOR3M + 0.62 p.p.	27.07.2018	25.07.2025	BondSpot, WSE parallel market
PLPKOHP00108	PLN	60,000	3.49%	fixed rate	24.08.2018	24.08.2028	BondSpot, WSE parallel market
PLPKOHP00116	PLN	230,000	2.38%	WIBOR3M + 0.66 p.p.	26.10.2018	28.04.2025	BondSpot, WSE parallel market
XS1935261013	EUR	500,000	0.25%	fixed rate	28.01.2019	23.11.2021	LuxSE, WSE parallel market
XS1935261013 (tranche 2)	EUR	100,000	0.25%	fixed rate	01.03.2019	23.11.2021	LuxSE, WSE parallel market
XS1508351357 (tranche 2)	EUR	100,000	0.13%	fixed rate	08.03.2019	24.06.2022	LuxSE, WSE parallel market
PLPKOHP00132	PLN	250,000	2.32%	WIBOR3M + 0.60 p.p.	10.06.2019	30.09.2024	BondSpot, WSE parallel market

On 10 June 2019 PKO Bank Hipoteczny SA, as the first bank in Poland, issued green mortgage covered bonds to finance residential mortgage loans that meet the energy effectiveness criteria. The energy effectiveness criteria developed by the Bank were approved by the International Climate Bonds Initiative Agency and are recommended as Low Carbon Building Criteria for housing properties in Poland. The Bank's green mortgage covered bonds have been certified by the Climate Bonds Initiative Agency as bonds that meet the highest international standards in terms of positive environmental impact.

(IN PLN MILLION)

In the first half of 2019 the Bank issued the said green mortgage covered bonds in PLN amounting to PLN 250,000 thousand and conducted three issues of mortgage covered bonds in EUR totalling EUR 700,000 thousand, whereas in the first half of 2018, the Bank conducted two issues of mortgage covered bonds in PLN totalling PLN 800,000 thousand and one issue of mortgage covered bonds in EUR of EUR 500,000 thousand. The Bank did not redeem any mortgage covered bonds in the first half of 2019 or in 2018.

As at 30 June 2019 and 31 December 2018 the issued PLN- and EUR mortgage covered bonds were rated by Moody's Investors Service at Aa3, i.e. the highest achievable by Polish securities. The limit for the ratings is the Polish country ceiling for debt instruments (i.e. the highest rating which can be obtained in Poland) is currently at the level of Aa3.

The total nominal value of the issued mortgage covered bonds as at 30 June 2019 amounted to PLN 15,951,308 thousand, and as at 31 December 2018 it amounted to PLN 12,824,700 thousand.

SECURING THE MORTGAGE COVERED BONDS

The mortgage covered bonds are secured by loans secured by the highest priority mortgage. Additionally, the basis for the issue of mortgage covered bonds may also be the Bank's own funds:

- funds invested in securities issued or guaranteed by the National Bank of Poland, the European Central Bank, governments and central banks of members of the European Union and/or the Organization for Economic Cooperation and Development, excluding countries that are restructuring or have restructured their foreign debt in the past 5 years;
- funds deposited with the National Bank of Poland;
- held in cash.

The nominal value of loans included in the cover pool and constituting collateral for issues of mortgage covered bonds as at 30 June 2019 amounted to PLN 18,782,135 thousand, whereas the nominal value of additional collateral in the form of PLN-denominated securities issued by the State Treasury amounted to PLN 250,000 thousand. As at 31 December 2018, these amounts were PLN 16,947,730 thousand and PLN 251,000 thousand, respectively. The Bank's mortgage covered bonds' cover pool also included CIRS and FX-Forward transactions hedging the currency and interest-rate risk of issued mortgage covered bonds denominated in EUR and IRS transactions securing the interest rate risk of fixed rate mortgage covered bonds issued in PLN.

In the first half of 2019 and in previous years, the Bank's cover pool did not include asset-backed securities (ABS) that do not meet the requirements described in paragraph 1 Art. 80 of Guideline (EU) 2015/510 of the European Central Bank of 19 December 2014 on the implementation of the Eurosystem monetary policy framework (ECB/2014/60) (recast).

28. UNSECURED BONDS ISSUED

UNSECURED BONDS ISSUED	30.06.2019	31.12.2018
Measured at amortized cost		
unsecured bonds, including bonds issued under:	3,830,751	3,311,148
Non-Public Bond Issue Programme	3,479,956	2,961,108
an individual agreement	350,795	350,040
Total	**3,830,751**	**3,311,148**

REPAYMENT PERIOD OF UNSECURED BONDS ISSUED	30.06.2019	31.12.2018
up to 1 month	842,213	384,312
from 1 to 3 months	168,407	454,191
from 3 months to 1 year	2,820,131	2,122,605
from 1 to 5 years	-	350,040
Total	**3,830,751**	**3,311,148**

In the first half of 2019 the Bank issued bonds with a total nominal value of PLN 4,072,100 thousand and redeemed bonds of a total nominal value of PLN 3,550,500 thousand, whereas in the first half of 2018 it was PLN 3,783,200 thousand and PLN 3,308,000 thousand respectively.

(IN PLN MILLION)

The total nominal value of the issued bonds as at 30 June 2019 amounted to PLN 3,850,000 thousand, and PLN 3,328,400 thousand as at 31 December 2018.

UNSECURED BONDS ISSUED AS AT 30 JUNE 2019

UNSECURED BONDS	Nominal amount	Currency	Interest rate	Issue date	Redemption date
OW080819-157	14,200	PLN	zero-coupon	08.08.2018	08.08.2019
OW251019-171	4,300	PLN	zero-coupon	26.10.2018	25.10.2019
PLPKOHP00124	350,000	PLN	variable	21.12.2018	21.02.2020
OW230719-183	228,000	PLN	zero-coupon	23.01.2019	23.07.2019
OW050220-186	102,000	PLN	zero-coupon	05.02.2019	05.02.2020
OW100719-188	250,000	PLN	zero-coupon	22.02.2019	10.07.2019
OW100719-189	60,000	PLN	zero-coupon	19.03.2019	10.07.2019
OW021019-190	800,000	PLN	zero-coupon	05.04.2019	02.10.2019
OW230719-191	119,000	PLN	zero-coupon	05.04.2019	23.07.2019
OW230719-192	186,000	PLN	zero-coupon	24.04.2019	23.07.2019
OW080819-193	86,600	PLN	zero-coupon	07.05.2019	08.08.2019
OW061119-194	644,900	PLN	zero-coupon	09.05.2019	06.11.2019
OW230819-195	68,000	PLN	zero-coupon	24.05.2019	23.08.2019
OW061219-196	837,000	PLN	zero-coupon	10.06.2019	06.12.2019
OW301219-197	100,000	PLN	zero-coupon	26.06.2019	30.12.2019

As at 30 June 2019 PKO Bank Polski SA did not hold any bonds under the guarantee described in Note 36.1 (PLN 54,100 thousand as at 31 December 2018).

On 11 April 2019 the Bank established a Public Bond Issue Programme, and as at 31 May 2019, the PFSA approved the Base Prospectus for the Issue of Bonds by PKO Bank Hipoteczny SA. By 30 June 2019 bonds with a total nominal value of PLN 50,000 thousand had been subscribed under the programme. Their issue date was set at 11 July 2019.

29. OTHER LIABILITIES

OTHER LIABILITIES	30.06.2019	31.12.2018
Expenses to be paid	9,237	8,506
Liabilities in respect of contribution to the Bank Guarantee Fund, including:	23,425	1,367
in respect of contribution accrued by BGF / payable to BGF to the resolution fund	22,058	-
maintained in the form of payment commitments to the resolution fund	1,367	1,367
Other liabilities, including:	13,486	12,101
sundry creditors	5,680	5,882
settlements with the state budget, including:	7,806	6,219
liabilities in respect of tax on certain financial institutions	7,006	5,818
Liabilities in respect of payment for shares which have not yet been registered with the National Court Register	-	100,000
Lease liabilities	5,639	
Total	**51,787**	**121,974**
including financial liabilities	20,556	14,388

As at 30 June 2019 and 31 December 2018, the Bank had no overdue contractual liabilities.

(IN PLN MILLION)

30. Provisions

PROVISIONS FOR THE PERIOD FROM 01 January 2019 TO 30 June 2019	Provision for disability and retirement benefits	Provision for loan commitments	Total
As at 01 January 2019, including:	**124**	**144**	**268**
Short-term provision	-	144	144
Long-term provision	124	-	124
Increase/reassessment of provisions	10	205	215
Release/utilization	-	(70)	(70)
As at 30 June 2019, including:	**134**	**279**	**413**
Short-term provision	-	279	279
Long-term provision	134	-	134

PROVISIONS FOR THE PERIOD FROM 1 JANUARY 2018 TO 30 JUNE 2018	Provision for disability and retirement benefits	Provision for loan commitments	Total
As at 31 December 2017, including:	**84**	**-**	**84**
Short-term provision	-	54	54
Long-term provision	84	-	84
Changes due to IFRS 9 implementation	**-**	**54**	**54**
Short-term provision	-	54	54
As at 01 January 2018, including:	**84**	**54**	**84**
Short-term provision	-	54	54
Long-term provision	84	-	84
Increase/reassessment of provisions	29	92	121
Release	-	(42)	(42)
As at 30 June 2018, including:	**113**	**104**	**113**
Short-term provision	-	104	104
Long-term provision	113	-	113

31. Equity and shareholding structure of the Bank

EQUITY	30.06.2019	31.12.2018
Share capital	1,526,500	1,295,000
Supplementary capital	146,735	54,932
Accumulated other comprehensive income, including:	152,033	63,889
cash flow hedges	149,311	59,462
measurement of financial assets measured at fair value through other comprehensive income	2,722	4,427
Retained earnings/accumulated losses (loss resulting from IFRS 9 implementation)	-	(11,787)
Net profit for the period	30,629	85,849
Total equity	**1,855,897**	**1,487,883**

(IN PLN MILLION)

SHAREHOLDING STRUCTURE

Series	Type of shares	Number of shares	Nominal value of 1 share (in PLN)	Series value at nominal value (in PLN)	Date of passing the resolution by GSM	Issue date	Date of registration in the National Court Register
A	ordinary	300,000,000	1	300,000,000	06.10.2014	06.10.2014	24.10.2014
B	ordinary	200,000,000	1	200,000,000	14.03.2016	07.04.2016	22.04.2016
C	ordinary	200,000,000	1	200,000,000	01.07.2016	15.07.2016	28.07.2016
D	ordinary	100,000,000	1	100,000,000	28.10.2016	18.11.2016	01.12.2016
E	ordinary	150,000,000	1	150,000,000	21.03.2017	04.04.2017	12.04.2017
F	ordinary	150,000,000	1	150,000,000	28.06.2017	04.07.2017	11.09.2017
G	ordinary	100,000,000	1	100,000,000	18.10.2017	20.10.2017	16.11.2017
H	ordinary	95,000,000	1	95,000,000	13.08.2018	17.08.2018	08.10.2018
I	ordinary	100,000,000	1	100,000,000	19.12.2018	21.12.2018	21.02.2019
J	ordinary	131,500,000	1	131,500,000	07.03.2019	19.03.2019	16.05.2019
Total		**1,526,500,000**		**1,526,500,000**			

PKO Bank Polski SA was the Bank's sole shareholder as at 30 June 2019 and 31 December 2018.

On 21 February 2019, the issue of 100,000,000 I-series shares (issued on 21 December 2018) was registered with the National Court Register.

In the first half of 2019, 131,500,000 new J-series ordinary registered shares with a nominal value of PLN 1 each were issued. The shares were acquired for the issue price of PLN 1.14 per share. The share premium (less tax on civil law transactions and notarial fees) in the amount of PLN 17,741 thousand was recognized in supplementary capital. The issue was registered with the National Court Register on 16 May 2019.

The Bank's share capital as at 30 June 2019 amounts to PLN 1,526,500,000 and consists of 1,526,500,000 ordinary registered shares, each of PLN 1 nominal value. The PKO Bank Hipoteczny SA shares are non-preference shares and have been paid up in full.

Furthermore, on 27 June 2019 the Extraordinary General Shareholders' Meeting passed a resolution on increasing the share capital of PKO Bank Hipoteczny by PLN 84,800,000 to PLN 1,611,300,000, by issuing 84 800,000 new K-series ordinary registered shares with a nominal value of PLN 1 each. The issue price for each K-series share amounted to PLN 1.18. The K series shares were subscribed and fully paid up by PKO Bank SA on 1 July 2019.

In the first half of 2019 and in 2018 the Bank did not pay any dividends.

(IN PLN MILLION)

OTHER NOTES

32. Contingent liabilities granted and received

32.1 Contractual commitments

As at 30 June 2019 and 31 December 2018 the Bank had no contractual commitments relating to the purchase of intangible assets and property, plant and equipment.

32.2 Financial liabilities granted

LOAN COMMITMENTS (CONTINGENT)	30.06.2019	31.12.2018
Undrawn housing loans (nominal value)		
housing loans to individuals	621,798	719,217
provisions for loan commitments	(279)	(144)
Total, net	**621,519**	**719,073**
including irrevocable loan commitments	-	-

Information on provisions for financial liabilities granted is provided in Note 30 “Provisions”.

32.3 Guarantee commitments granted

PKO Bank Hipoteczny SA does not grant guarantee commitments.

32.4 Contingent liabilities received

CONTINGENT ASSETS AT THE NOMINAL VALUE	30.06.2019	31.12.2018
Contingent assets		
financial	1,899,139	1,171,420
guarantees	2,000,000	1,945,900
Total	**3,899,139**	**3,117,320**

The contingent liabilities received of a financial nature represent initiated and available revolving current account overdraft facilities, while guarantee commitments received represent the available guarantees to underwrite unsecured bond issues.

Right to sell or pledge collateral established for the Bank

As at 30 June 2019 and 31 December 2018 no collateral was established for the Bank, which the Bank would be entitled to sell or re-pledge, in the event of fulfilling all obligations by the owner of the collateral.

33. Legal claims

As at 30 June 2019 and 31 December 2018 there were no legal claims.

34. INFORMATION ABOUT LEASES

LEASE – LESSEE

The Bank classifies contracts to lease contracts or contracts containing a lease if:

- it obtains the right to use an identified asset, and the supplier's right to substitute it with an alternative asset is insignificant; and
- it has the right to substantially all economic rewards from exercising the right over the entire period of use; and
- it has the right to direct the use of an identified asset over the entire period of its use, where:
    - the Bank has the right to direct how and for what purpose the asset is used over the entire period of the lease; or
    - appropriate previous decisions were taken as to how and for what purpose the asset is used.

The Bank applies eliminations and does not recognize right-of-use assets or liabilities in respect of:

- short-term leases to which the Bank classifies contracts without a purchase option, concluded for a period no longer than 12 months from the inception of the lease, in particular contracts concluded for an unspecified period with a short (up to 12-month) notice period, without any significant penalties which are understood in particular as expenses incurred on leasehold improvements or costs of changing the location;
- low-value leases (an asset with a value below PLN 20 000 determined based on the value of a new asset, irrespective of the age of the leased asset), with the exception of leases of space.

The Bank measures its lease liabilities initially at the amount of the present value of outstanding lease payments as at that date.

The Bank does not classify variable fees depending on external factors as elements of lease payments.

After the initial recognition of a lease liability the Bank measures it at amortized cost.

The remeasurement of a lease liability is recognized by the Bank as an adjustment of a right-of-use asset. If as a result of the remeasurement the carrying amount of a right-of-use asset is reduced to nil and the measurement of the lease liability continues to decrease, the remaining amount of the remeasurement is recognized by the Bank as profit or loss.

Right-of-use assets are initially measured by the Bank at cost. After initial recognition the Bank measures the right-of-use asset by reducing its initial value by depreciation (on a straight-line basis) and impairment, and adjusts lease liabilities in accordance with the remeasurement.

In order to discount future lease payments, the Bank uses discount rates:

- calculated based on profitability curves reflecting the cost of financing in the given currency;
- covering the tenor of the longest lease contract measured and reflecting – for the given currency – a fixed market interest rate and the Bank's cost of financing;
- read from the curve for maturities reflecting half of the term to maturity of a lease contract (in connection with the assumption that lease payments will be fixed).

The value of the marginal lending rate for leases is updated by the Bank on a quarterly basis.

The Bank applies the same discount rates to the portfolio of lease contracts for cars and properties, taking into account the impact of the security for the lease on the discount rate applied.

Lease payments in respect of short-term and low-value leases are recognized by the Bank as costs on a straight-line basis over the term of the lease. Differences between the amounts paid and those resulting from the straight-line accounting for costs are recognized in prepayments or accruals.

(IN PLN MILLION)

FINANCIAL INFORMATION:

LEASE AMOUNTS RECOGNIZED IN THE INCOME STATEMENT - LESSEE	01.01.2019 - 30.06.2019
Amortization of the right-of-use assets	(586)
real estate	(506)
cars	(80)
Interest expense	(81)
Costs related to short-term lease contracts	(85)
Costs related to lease contracts for low-value assets (other than short-term), non-deductible VAT expenses and service charges	(411)
Total	**(1,163)**

Right-of-use assets and lease liabilities are also shown in the tables below as recognized upon the implementation of IFRS 16 "Leases", i.e. as at 1 January 2019.

RIGHT-OF-USE ASSETS	30.06.2019	01.01.2019
Real estate	4,926	5,361
Cars	670	65
Total	**5,596**	**5,427**

OTHER LIABILITIES	30.06.2019	01.01.2019
Lease liabilities	5,639	5,427
Total	**5,639**	**5,427**

LEASES – LESSOR

The Bank does not conclude contracts in which it has the role of lessor.

35. NOTES TO THE STATEMENT OF CASH FLOWS

Cash and cash equivalents	30.06.2019	31.12.2018	30.06.2018
Cash and balances with the Central Bank	22	6	18
Amounts due from banks - current accounts	55	22	122,172
Total	**77**	**28**	**122,190**

As at 30 June 2019 and 31 December 2018 there were no cash and cash equivalents with restricted availability for use.

36. RELATED PARTY TRANSACTIONS

36.1 RELATED-PARTY TRANSACTIONS –CAPITAL LINKS

PKO Bank Polski SA and PKO Bank Polski SA Group entities are the Bank's related parties.

(IN PLN MILLION)

Financial information:

As at 30 June 2019

ENTITY	ASSETS	
	Receivables	including derivatives
PKO Bank Polski SA	173,916	173,484
Total	173,916	173,484

ENTITY	LIABILITIES				
	Current account credit limits, overdrafts	Liabilities in respect of the purchase of receivables	Mortgage covered bonds and unsecured bonds	Other liabilities	including derivatives
PKO Bank Polski SA	1,609,122	2,278,486	405,117	61,033	48,539
PKO BP Finat Sp. z o.o.	-	-	-	18	-
PKO Leasing SA	-	-	-	684	-
PKO Towarzystwo Ubezpieczeń SA	-	-	-	228	-
PKO VC -fizan	-	-	33,100	-	-
Total	1,609,122	2,278,486	438,217	61,963	48,539

ENTITY	Loan commitments	Contingent assets
PKO Bank Polski SA	-	3,899,139
Total	-	3,899,139

For the period from 1 January 2019 to 30 June 2019

ENTITY	Total revenues	including interest and commissions	Total costs	including interest and commissions	Net income/ (expense) from financial instruments measured at fair value	Net foreign exchange gains / (losses)
PKO Bank Polski SA	1,041	816	156,320	144,555	33	(133,638)
PKO BP Finat Sp. z o.o.	-	-	101	-	-	-
PKO Leasing SA	-	-	163	6	-	-
PKO Towarzystwo Ubezpieczeń SA	-	-	1,478	1,478	-	-
PKO VC -fizan	-	-	364	364	-	-
Total	1,041	816	158,426	146,403	33	(133,638)

As at 31 December 2018

ENTITY	ASSETS	
	Receivables	including derivatives
PKO Bank Polski SA	168,754	168,289
Total	168,754	168,289

(IN PLN MILLION)

ENTITY	LIABILITIES				
	current account credit limits and overdrafts	Liabilities in respect of the purchase of receivables	Mortgage covered bonds and unsecured bonds	Other liabilities	including derivatives
PKO Bank Polski SA	1,742,017	2,300,254	137,491	122,185	15,254
PKO BP Finat Sp. z o.o.	-	-	-	18	-
PKO Leasing SA	-	-	-	50	-
PKO VC -fizan	-	-	34,675	-	-
Total	**1,742,017**	**2,300,254**	**172,166**	**122,253**	**15,254**

ENTITY	Loan commitments	Contingent assets
PKO Bank Polski SA	-	3,117,320
Total	**-**	**3,117,320**

FOR THE PERIOD FROM 1 JANUARY 2018 TO 30 JUNE 2018

ENTITY	Total revenues	including interest and commissions	Total costs	including interest and commissions	Net income/ (expense) from financial instruments measured at fair value	Net foreign exchange gains / (losses)
PKO Bank Polski SA	712	499	128,615	117,951	24	382,965
PKO BP Finat Sp. z o.o.	-	-	96	-	-	-
PKO Leasing SA	-	-	186	-	-	-
PKO Towarzystwo Ubezpieczeń SA	-	-	680	680	-	-
Total	**712**	**499**	**129,577**	**118,631**	**24**	**382,965**

The Bank held current accounts and made deposits with PKO Bank Polski SA during the reporting period. In addition, the Bank cooperates strategically with PKO Bank Polski SA. Housing loan sales as well as after-sales servicing, excluding risk management, internal audit and control, are carried out within the framework of the Outsourcing Agreement with PKO Bank Polski SA dated 16 January 2015. Assistance is also provided with respect to support activities under this agreement.

The Bank also obtains financing from PKO Bank Polski SA. On 29 October 2015, PKO Bank Hipoteczny SA concluded with PKO Bank Polski SA a Current Account Revolving Credit Agreement with a limit of PLN 900,000 thousand for a period of 3 years. By annexes to the Agreement, the amount of the limit was increased to PLN 2,000,000 thousand and the lending period was extended until 29 October 2022. As at 30 June 2019, PLN 2,000,000 thousand of the facility was available. Furthermore, on 2 February 2017, PKO Bank Hipoteczny SA concluded with PKO Bank Polski SA a Current Account Revolving Credit Agreement with a limit of PLN 1,500,000 thousand for a period of 3 years in tranches. As at 30 June 2019, PLN 1,500,000 thousand of the facility was available.

On 30 September 2015 the Bank entered into a PKO Bank Hipoteczny Bond Issue Programme Agreement (the "Programme") with PKO Bank Polski SA up to the amount of PLN 2 billion over a period of 4 years as well as an Underwriting Agreement under which the underwriter assumes the obligation to take up the Issuer's Bonds on its own account up to PLN 2,000,000 thousand. As at 31 June 2019 and 31 December 2018 the value of the programme with the annexes amounted to PLN 3,500,000 thousand.

On 17 November 2015 A Framework Agreement for the Sale of Receivables was concluded with PKO Bank Polski SA. Based on the agreement, in 2019 the Bank continued to purchase portfolios of receivables under residential mortgage loans. Further details are available in Notes 21 and 25.

On 9 November 2015 the Bank concluded a Programme Agreement with PKO Bank Polski SA and the Powszechna Kasa Oszczednosci Bank Polski SA Brokerage House Branch of PKO Bank Polski SA. for the National Programme for

(IN PLN MILLION)

Issuing Mortgage Covered Bonds. On 30 August 2017, the parties signed an amendment agreement altering and standardizing the Programme Agreement, under which the Brokerage House of PKO Bank Polski is engaged by the Bank as a Firm Commitment Underwriter.

PKO Bank Polski also acts as Arranger and Dealer under the Programme Agreement of 28 September 2016, under which the Bank conducts international mortgage bond issues within the framework of the PKO Bank Hipoteczny Base Prospectus, approved by the Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg.

On 31 May 2019 the Bank concluded a Programme Agreement with PKO Bank Polski SA and the Powszechna Kasa Oszczednosci Bank Polski SA Brokerage House Branch of PKO Bank Polski SA. concerning the Programme for Issuing Bonds established on 11 April 2019. PKO Bank Polski SA acts as Arranger and Calculation Agent and Dom Maklerski PKO Banku Polskiego SA acts as Dealer and Firm Commitment Underwriter.

Furthermore, as a part of transactions with parties related by equity, PKO BP Finat Sp. z o.o. provides accounting services to the Bank's in respect of general administration, as well as personnel and payroll services, PKO Bank Polski SA leases out office space, PKO Leasing SA provides vehicles under a lease contract, while PKO Towarzystwo Ubezpieczeniowe SA insures the Bank's credit risk.

During the reporting period the Bank did not conclude transactions with related parties other than on an arm's length basis.

36.2 Related-party transactions – personal links

As at 30 June 2019, 10 entities were related to the Bank through key management personnel of PKO Bank Hipoteczny SA or close relatives of key management personnel, whereas at 31 December 2018 it was 12 entities.

In the first half of 2019 and the first half of 2018, no mutual transactions were conducted between the Bank and those entities.

36.3 Benefits for PKO Bank Hipoteczny SA key management personnel

COST OF REMUNERATION OF THE BANK'S MANAGEMENT BOARD AND SUPERVISORY BOARD	01.01.2019 - 30.06.2019	01.01.2018 - 30.06.2018
The Bank's Management Board		
Short-term employee benefits[1]	1,155	1,002
Post-employment benefits	-	-
Long-term benefits[2]	224	253
Share-based payments settled in cash[3]	224	253
Total	**1,603**	**1,508**
The Bank's Supervisory Board (independent Supervisory Board members)		
Short-term employee benefits[1]	69	73
Total	**69**	**73**

[1] Short-term employee benefits comprise remuneration, social insurance contributions and other benefits which were settled or will be settled within 12 months of the end of a reporting period;

[2] Long-term benefits comprise cost of accruals for deferred variable remuneration components granted in cash;

[3] Share-based payments settled in cash comprise cost of accruals for deferred variable remuneration components granted in the form of financial instruments, i.e. phantom shares. Phantom shares are converted into cash after the retention period.

Loans and advances granted by the Bank to its Management

In the first half of 2019 and in 2018 the Bank did not grant any loans or advances to its management.

Under the Framework Agreement Concerning the Sale of Receivables entered into with PKO Bank Polski SA on 17 November 2015, the Bank purchased portfolios of residential mortgage loans comprising two loans granted to one of the members of the Bank's Supervisory Board. As at 30 June 2019 their carrying amount was PLN 639 thousand, and PLN 656 thousand as at 31 December 2018. The interest rate and repayment terms are consistent with the arm's length principle.

(IN PLN MILLION)

37. Fair value of financial assets and liabilities

37.1 Categories of fair-value measurement of financial assets and financial liabilities measured at fair value in the Statement of Financial Position

ASSETS AND LIABILITIES MEASURED AT FAIR VALUE AS AT 30 JUNE 2019	Note	Carrying amount	Level 1 Prices quoted on active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
Derivative hedging instruments	19	173,484	-	173,484	-
CIRS		160,175	-	160,175	-
FX-Forward		332	-	332	-
IRS		12,977		12,977	
Securities	20	1,158,142	1,158,142	-	-
measured at fair value through other comprehensive income		1,158,142	1,158,142	-	-
Total financial assets measured at fair value		**1,331,626**	**1,158,142**	**173,484**	**-**
Derivative hedging instruments	19	48,539	-	48,539	-
CIRS		47,836	-	47,836	-
FX-Forward		703	-	703	-
IRS		-	-	-	-
Total financial liabilities measured at fair value		**48,539**	**-**	**48,539**	**-**

ASSETS AND LIABILITIES MEASURED AT FAIR VALUE AS AT 31 DECEMBER 2018	Note	Carrying amount	Level 1 Prices quoted on active markets	Level 2 Valuation techniques based on observable market data	Level 3 Other valuation techniques
Derivative hedging instruments	19	168,289	-	168,289	-
CIRS		162,100	-	162,100	-
FX-Forward		237	-	237	-
IRS		5,952		5,952	-
Securities	20	842,965	842,965	-	-
measured at fair value through other comprehensive income		842,965	842,965	-	-
Total financial assets measured at fair value		**1,011,254**	**842,965**	**168,289**	**-**
Derivative hedging instruments	19	15,254	-	15,254	-
CIRS		14,786	-	14,786	-
FX-Forward		468	-	468	-
IRS		-	-	-	-
Total financial liabilities measured at fair value		**15,254**	**-**	**15,254**	**-**

In the first half of 2019 and in the first half of 2018 there were no transfers between the different levels of fair value hierarchy.

(IN PLN MILLION)

37.2 Financial assets and liabilities not presented at fair value in the Statement of Financial Position

FINANCIAL ASSETS AND LIABILITIES NOT PRESENTED AT FAIR VALUE AS AT 30 JUNE 2019	fair value hierarchy level	valuation method	30.06.2019	
			carrying amount	fair value
Cash and balances with the Central Bank	N/A	amount of consideration due	22	22
Amounts due from banks	2	discounted cash flows	55	55
Loans and advances to customers, including:			24,599,196	24,216,278
residential mortgage loans	3	discounted cash flows	24,599,196	24,216,278
Other financial assets	3	amount of consideration due taking into account impairment	386	386
Amounts due to banks	2	discounted cash flows	4,137,637	4,137,637
Amounts due to customers	2	discounted cash flows	3,378	3,378
Mortgage covered bonds issued	1.2	discounted cash flows, quotation on a regulated market	15,965,585	16,221,562
Unsecured bonds issued	2	discounted cash flows	3,830,751	3,830,751
Other financial liabilities	3	amount of consideration due	20,556	20,556

FINANCIAL ASSETS AND LIABILITIES NOT PRESENTED AT FAIR VALUE AS AT 31 DECEMBER 2018	fair value hierarchy level	valuation method	31.12.2018	
			carrying amount	fair value
Cash and balances with the Central Bank	N/A	amount of consideration due	6	6
Amounts due from banks	2	discounted cash flows	22	22
Loans and advances to customers, including:			21,070,469	21,026,457
residential mortgage loans	3	discounted cash flows	21,070,469	21,026,457
Other financial assets	3	amount of consideration due taking into account impairment	449	449
Amounts due to banks	2	discounted cash flows	4,292,286	4,292,286
Amounts due to customers	2	discounted cash flows	4,359	4,359
Mortgage covered bonds issued	1.2	discounted cash flows, quotation on a regulated market	12,841,500	12,855,959
Unsecured bonds issued	2	discounted cash flows	3,311,148	3,311,148
Other financial liabilities	3	amount of consideration due	14,388	14,388

38. Operating segments

In the reporting period and in the period ended 30 June 2018, the Bank did not analyse its operations by segments due to the specific nature of its operations.

(IN PLN MILLION)

OBJECTIVES AND PRINCIPLES OF RISK MANAGEMENT

39. Risk management in PKO Bank Hipoteczny SA

Risk management at PKO Bank Hipoteczny SA is aimed at ensuring the financial stability of the Bank, safeguarding the value and security of the mortgage covered bonds issued and to guarantee the safety of funds deriving from the issue of bonds and the other sources of financing the Bank's operations. The assumed level of risk plays an important role in the planning process.

The Bank has identified the following types of risks which are managed:

Type of risk	Section
credit risk	40
concentration risk	41
residual risk	42
liquidity risk	43
interest rate risk	44
foreign exchange risk	45
model risk	46
operational risk	47
business risk	48
compliance risk	49
reputation risk	50
capital risk	51

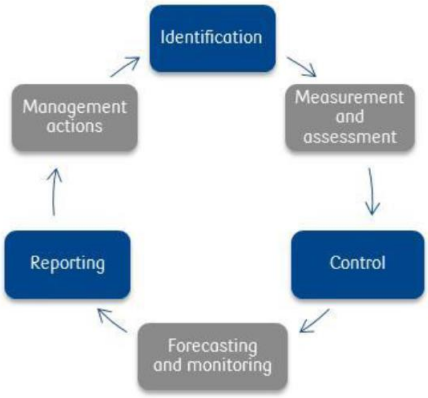
39.1 Main principles of risk management

Risk management in PKO Bank Hipoteczny SA is based in particular on the following policies:

- the risk management process, including the lending process, is defined and regulated by strategies, policies and procedures adopted by the Management Board and approved by the Supervisory Board of PKO Bank Hipoteczny SA;
- the Bank manages all identified types of banking risks and performs an ICAAP (Internal Capital Adequacy Assessment Process), where:
  - 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 of risk as they emerge;
  - the risk management methods, models and their assumptions as well as systems are tailored to the scale and complexity of the risk, and periodically verified and validated;
- the organizational structure of risk management ensures the independence of the risk function, including the real estate valuation and the credit decision making processes from business activities;
- risk management is integrated with the planning and controlling systems and supports the pursuit of the Bank's strategy in compliance with the risk management strategy, in particular in terms of risk tolerance levels;
- the risk management process is consistent with the principles of risk management of the PKO Bank Polski SA Group, including the application of group risk models, modified to reflect the nature of activities of PKO Bank Hipoteczny SA and approved by the competent authorities of PKO Bank Hipoteczny SA.

RISK MANAGEMENT SYSTEM

The risk management system of PKO Bank Hipoteczny SA covers the following components:



39.2 COMPONENTS OF THE RISK MANAGEMENT SYSTEM

The risk management system of PKO Bank Hipoteczny SA comprises the following components:

RISK IDENTIFICATION

Risk identification consists of identifying actual and potential sources of risk and assessing the materiality of their potential influence on the given type of risk and on the financial position of the Bank. As part of the risk identification process, material types of risk for the Bank's activities are identified. The different risks assessments are reviewed at least once a year for their materiality.

RISK MEASUREMENT OR ASSESSMENT

Risk measurement covers defining risk measures adequate to the type and materiality of the risk, data availability and quantitative risk assessment by means of set measures, and risk assessment covers identifying the scale of risk, taking into account risk management goals. Stress tests are carried out as part of risk measurement, with a view to determining the potential impact of adverse changes in the Bank's environment and operations on its financial position.

RISK CONTROL

Risk control consists of determining the tools to be used to diagnose or mitigate the level of risk in specific areas of the Bank's activity. Risk control comprises determining risk controls appropriate for the scale and complexity of the Bank's operations, in particular in the form of strategic tolerance limits for individual types of risks subject to monitoring, and in the event that these are exceeded, management actions are taken.

RISK FORECASTING AND MONITORING

Risk forecasting and monitoring consists of preparing forecasts and monitoring deviations from forecasts or adopted reference points (e.g. limits, thresholds, plans, measures from the previous period, recommendations) and stress testing. Risk monitoring is performed with a frequency appropriate to the materiality and volatility of a specific risk type.

RISK REPORTING

Risk reporting consists of regularly informing the authorities of the Bank about the results of risk measurement, actions taken and recommended actions. The scope, frequency and the form of reporting are adjusted to the management level of the recipients.

MANAGEMENT ACTIONS

The management actions taken by the Bank comprise in particular enacting internal regulations, specifying the risk tolerance level, establishing limits and thresholds, issuing recommendations, taking decisions, including about the use of tools supporting risk management. The objective of management actions is to shape the risk management system and risk levels.

39.3 ORGANIZATION OF RISK MANAGEMENT IN THE BANK

Risk management is overseen by the Bank's Supervisory Board, which is informed on a regular basis about the risk profile of PKO Bank Hipoteczny SA and about the most important actions undertaken with respect to risk management.

The Bank's Management Board is responsible for risk management, including supervising and monitoring actions taken by the Bank concerning risk management. The Bank's Management Board takes key decisions affecting the risk profile of the Bank and adopts internal regulations concerning risk management.

Risk is managed at three mutually complementinv levels:

- the first level consists of organizational structures managing the product, organizing the sale of products and customer service as well as other organizational units carrying out operational tasks generating risk, operating on the basis of internal regulations;
- the second level covers the activity of the compliance unit and the identification, measurement or assessment, control, monitoring and reporting of risk and the identified threats and irregularities - the tasks are carried out by specialized organizational units operating on the basis of the Bank's internal regulations. The purpose of these units is to create internal regulations defining the principles, methods, tools and procedures for risk management as well as measuring the effectiveness of operations;
- the third level is the activity of the internal audit unit performing independent audits of the elements of the Bank's management system, including the risk management system and the internal control system. Internal audit functions separately from the first and second level.

The independence of the abovementioned levels is achieved by preserving organizational independence in the following areas:

- the function of the second level with regard to creating systematic solutions is independent of the function of the first level;
- the function of the third level is independent of the functions of the first and second level.

The following organizational units of PKO Bank Hipoteczny SA are responsible for risk management to the extent of the powers vested in them:

RISK BUREAU

The Risk Bureau is responsible, in particular, for managing the following risks: credit risk, residual risk, concentration risk, liquidity risk, interest rate risk, foreign exchange risk, business risk, and the management of capital adequacy, including:

- identifying risk factors and sources of risk;
- measuring, assessing, as well as periodic monitoring and reporting risk levels;
- measuring and assessing capital adequacy;
- collaboration with the regulator in the risk area (SREP, inspections, clarifications, questionnaires, etc.)
- analysing the property market, principles for property valuation, including the rules for determining the Property Value for Mortgage Lending Purposes;
- managing non-performing receivables and taking effective actions to collect those receivables.

COMPLIANCE TEAM IN THE COMPLIANCE, SECURITY AND LEGAL BUREAU

The Compliance Team, which is a separate internal unit of the Compliance, Security and Legal Bureau, is responsible in particular for developing the compliance risk management system and identifying, controlling and monitoring compliance risk in the Bank, as well as preparing reports and developing a system for managing reputation risk.

VALIDATION AND RISK CONTROL TEAM

The Validation and Risk Control Team is responsible, in particular, for ensuring the effectiveness of the Bank's operating risk management system, which includes the identification, measurement, monitoring, control and reporting of the risk, designing model risk management standards, and assessing the level of model risk, validating the models, cooperating in this respect with the model validations unit in PKO Bank Polski SA and for designing and monitoring the operations of systemic solutions for forming control functions in respect of processes considered to be significant for the internal control system, including maintaining the Control Function Matrix. The Team's responsibilities also include coordinating data quality management processes as well as supervising the security of IT systems.

Risk management is supported by the following committees:

Supervisory Board Audit and Finance Committee ("AFC")

The Committee supports the Supervisory Board in particular by:

- monitoring and expressing periodic opinions on the adequacy and effectiveness of the internal control and risk management systems, the effectiveness of the Bank's compliance risk management, the application of the Corporate Governance Principles for Supervised Institutions, the adequacy and effectiveness of the whistleblowing policy and the ethical procedures and standards in force at the Bank;
- developing a policy for selecting an audit firm, recommending an audit firm to audit the Bank's financial statements to the Supervisory Board;
- monitoring the process of financial reporting, including reviewing the periodic and annual financial statements of the Bank;
- monitoring the audit performance and independence of the registered auditor and the audit firm;
- giving opinions on the resolutions of the Bank's Management Board relating to internal controls, the approval of which is the responsibility of the Supervisory Board.

Supervisory Board Risk Committee ("RC")

The Committee supports the Supervisory Board in particular by:

- giving opinion on the Bank's overall current and future risk appetite, strategic risk directions and tasks in the context of the Bank's strategy and the conditions resulting from the macroeconomic situation and the regulatory environment, and, in particular, the risk management strategy developed by the Management Board and the Bank's acceptable overall risk level;
- monitoring the compliance of the Bank's policy in the area of taking on risk with the strategy and financial plan;
- analysing periodic risk reports, including the utilization of strategic risk tolerance limits and developing relevant guidelines on their basis, as well as periodic reviews of pursuance of the risk management strategy;
- issuing opinions about capital adequacy, the rules of evaluation of creditworthiness, the risk measurement models, the impairment model;
- giving opinions on the principles of the disclosure policy regarding capital adequacy, capital adequacy management, liquidity risk, operational risk, model risk, and impairment measurement risk.
- giving opinions on the draft Rules on Setting the Mortgage Lending Value of Real Estate.

Assets & Liabilities Management Committee ("ALCO")

The Committee supports the Bank's Management Board in particular by:

- supporting the functions managing the liquidity risk, interest rate risk, business risk including macroeconomic changes risk, foreign exchange risk and capital risk including excessive financial leverage risk and respective models risk;
- managing the Bank's capital adequacy;
- examining materials on capital adequacy, equity, internal capital, stress tests, the risks mentioned above, as well as tolerance limits for these risks;
- making decisions regarding the Bank's operations, in particular as regards risk measures and limits as well as the initiation of capital and liquidity contingency actions;
- issuing recommendations for the Bank's competent authorities, organizational units, members of the Bank's Management Board, project teams or task forces – within the scope of their powers.

Credit Committee ("CC")

The Committee supports the Bank's Management Board in particular by:

- supporting the functions that manage credit, concentration and residual risks, as well as the risk of the models measuring such risks;
- examining materials on the risks mentioned above, the profile and quality structure of the loan portfolio, expected credit losses, acquisition of loan portfolios, the housing market;
- making decisions on the Bank's operations, in particular as regards risk measures and limits, risk model validation results, the methodology and models of calculating expected credit losses, cut-offs used as part of credit risk assessment, credit receivables purchased by the Bank, single loan transactions;

- issuing recommendations for the Bank's competent authorities, organizational units, members of the Bank's Management Board, project teams or task forces – within the scope of their powers.

STRATEGY AND BUSINESS INITIATIVES COMMITTEE ("SBIC")

The Committee supports the Bank's Management Board in particular by:

- supporting the operational, reputation, compliance and related model risk management functions;
- examining materials on the risks mentioned above, directions of the Bank's development, the Bank's strategy and IT strategy, initiatives related to the implementation of the Bank's strategy and IT strategy together with the operational risk analysis, product offer, product profitability, credit process;
- making decisions regarding the Bank's operations, in particular as regards managing the risks mentioned above, the related risk measures and limits;
- issuing recommendations for the Bank's competent authorities, organizational units, members of the Bank's Management Board, project teams or task forces – within the scope of their powers.

DATA QUALITY COMMITTEE ("DQC")

The Committee supports the Bank's Management Board in particular by:

- determining the directions of operations in the area of managing the quality of data and data architecture in the Bank, in the context of the Data Management System (DMS);
- oversight over the functioning of the DMS, including evaluation of its effectiveness and the operations of particular organizational units of the Bank.

The Committees, Management Board and Supervisory Board are recipients of regular reports concerning the different types of risk.

39.4 IDENTIFICATION OF MATERIAL RISKS

MATERIALITY OF DIFFERENT RISKS

The materiality of different risks is established on the basis of the review of the Bank's operations.

In determining the materiality criteria for the different risks, the impact of the risk on the Bank's operations is taken into account and three types of risks are recognized:

- material risks – subject to active management;
- risks subject to monitoring– which are monitored for materiality;
- other undefined risks or risks that do not exist in the Bank (immaterial and unmonitored).

The materiality evaluation of the different risks is performed periodically on the basis of quantitative and qualitative data. Above all, the evaluation results in defining all the risks existing in the Bank and then the risks are classified to one of the two categories: material risk or risk subject to monitoring. The materiality evaluation is also performed whenever a major change occurs in the scope or profile of the Bank's operations.

Risk types considered to be material:

- credit risk;
- liquidity risk, including financing risk;
- interest rate risk;
- operational risk, including legal risk and outsourcing risk;
- model risk.

Additionally, the following types of risk are considered by the Bank to require monitoring:

- concentration risk;
- foreign exchange risk;
- residual risk;
- business risk, including risk of macroeconomic changes;
- compliance risk;
- reputation risk;
- capital risk, including risk of excessive leverage.

The Bank has defined and monitors materiality criteria for the risks that are subject to monitoring. The fulfilment of these criteria will result in the recognition of such risk as material to the Bank.

In its Risk Management Strategy, the Bank defined a range of strategic limits defining the appetite for particular types of risk. The limits are regularly monitored. In the first half of 2019 and in 2018 none of the strategic limits was exceeded.

40. CREDIT RISK MANAGEMENT

Credit risk is defined as the risk of the occurrence of losses due to a counterparty's default on obligations to the Bank or as the risk of a decrease in the economic value of the Bank's receivables as a result of a deterioration in a customer's ability to service its obligations. The aim of credit risk management is to minimize losses in the loan portfolio as well as to minimize the risk of occurrence of impairment exposures, while maintaining the expected level of profitability and value of the loan portfolio.

PKO Bank Hipoteczny SA has policies for credit risk management, which are aimed at the proper risk assessment of loan transactions at the loan application stage and throughout the life of the transaction (monitoring), as well as proper safeguarding against risk by applying appropriate credit risk mitigation techniques.

The policies are executed by the Bank through the use of advanced credit risk management methods, both at the level of individual credit exposures and at the level of the entire loan portfolio of the Bank. These methods are verified and developed to ensure compliance with internal rating based requirements (IRB), i.e. an advanced credit risk measurement approach.

40.1 CREDIT RISK MEASUREMENT AND ASSESSMENT

PKO Bank Hipoteczny SA measures and assesses credit risk at the level of individual transactions and at the level of the entire portfolio.

The measurement and assessment of the risk of individual loan transactions is performed by PKO Bank Hipoteczny SA with the use of group risk models adapted to the specificity of PKO Bank Hipoteczny's business and approved by the relevant governing bodies of PKO Bank Hipoteczny SA. The group risk models used by PKO Bank Hipoteczny SA are based on application data, behavioural data and data from the Credit Information Bureau. The review (monitoring) of the models and their validation are performed separately based on the Bank's portfolio, PKO Bank Polski SA's portfolio as well as the combined portfolios of both banks.

The detailed principles and scope of cooperation within the PKO Bank Polski Group regarding the group risk models are laid down in the Outsourcing agreement with PKO Bank Polski SA described in Note 36.1.

In the lending process, as part of the risk assessment of an individual loan transaction, the Bank assesses the customer's creditworthiness in a qualitative and quantitative basis as well as evaluating the collateral. The qualitative assessment of creditworthiness means the review of all the available customer information originating from internal and external sources of information, as well as the assessment of certain socio-demographic features describing the customer from the perspective of statistical risk as a debtor. The quantitative assessment consists of investigating the customer's financial position in order to determine if the customer has adequate funds to pay his dues on time, including those arising from the requested loan. Creditworthiness is assessed, among other things, based on the documentation supplied by the customer, which is verified for completeness, authenticity and consistency with the factual and the legal status. The assessment of the collateral, particularly the property value for mortgage-lending purposes, consists of verifying the criteria determining the acceptability and effectiveness of the collateral as a possible source of recovery of the receivables.

When purchasing receivables in respect of residential mortgage loans from PKO Bank Polski SA, the Bank also performs an assessment of the credit risks of the contracts to be purchased, in accordance with the Bank's methodology of assessment of purchased receivables. In particular, the Bank assess: the customer's creditworthiness at the time PKO Bank Polski SA granted the loan to be transferred, the current behavioural scoring PD IRB (based on the Group's scoring model) in accordance with the Internal Ratings-Based Approach – IRB) and the current timeliness of repayments, eliminating from the transfer receivables which do not satisfy the methodology criteria.

In addition, the purchased portfolios are measured by an independent third party to guarantee an unbiased valuation of the portfolios to be acquired. As part of the valuation, the costs of risk anticipated with regard to the given receivables portfolio are also assessed and are reflected in the final price which the Bank pays for the portfolio.

In order to determine the credit risk at portfolio level, the Bank uses the following risk measurement and assessment methods:

- probability of default – "PD";
- loss given default – "LGD";
- expected credit loss – "ECL";
- share and structure of non-performing loans – "NPL";
- coverage ratio – "CR";
- risk costs – "RC";
- vintage analysis.

The portfolio credit risk measurement methods enable, among other things, to determine the level of allowances for expected credit losses.

The Bank performs analyses and stress-tests regarding the influence of potential changes in macroeconomic conditions on the quality of the Bank's loan portfolio. The test results reported to the Bank's governing bodies enable them to identify and take measures to mitigate the risks related to the business conducted.

The loan portfolio structure, taking into account the PD parameters, is presented in the table in Note 40.4.4.

40.2 Credit risk control

The control of credit risk consists of defining tools for measuring the level of credit risks and applying risk controls to mitigate the level of credit risk, both in the lending processes and at portfolio level. The key credit risk control are strategic credit risk tolerance limits. The Bank monitors the level of credit exposure towards its customers or groups of related customers within the meaning of the Banking Act, setting competency limits representing the maximum level of credit decision-making powers.

40.3 Impairment loss on credit exposures

PKO Bank Hipoteczny SA performs monthly reviews of credit exposures in order to identify those that are at risk of impairment or whose credit risk has increased significantly since the initial recognition, to measure the impairment of credit exposures and to set up provisions for expected credit losses.

With regard to impairment, the Bank applies IFRS 9, which is based on the concept of expected losses. The impairment model applies to financial assets which are not measured at fair value through profit or loss, and which comprise:

- debt financial instruments comprising credit exposures and securities;
- off-balance-sheet financial and guarantee exposures.

In accordance with IFRS 9 impairment is measured as 12-month expected credit losses or perpetual expected credit losses. The time horizon of an expected loss depends on whether a significant increase in credit risk occurred since the moment of initial recognition. Therefore, financial assets are allocated to 4 stages.

IFRS 9 portfolio	Period of expected credit losses
Stage 1 (assets whose credit risk has not increased significantly since initial recognition)	12-month expected credit losses
Stage 2 (assets whose credit risk has increased significantly since initial recognition)	perpetual expected credit losses
Stage 3 (impaired assets)	
Stage 4 (purchased or originated impaired assets – POCI)	

The expected loss is calculated as the product of credit risk parameters: probability of default (PD), loss given default (LGD) and exposure at default (EAD).

With regard to exposures classified in Stage 1, the Bank will use a maximum 12-month horizon of estimation of the expected loss, unless the maturity is shorter than 12 months. With Stage 2 exposures, the expected loss will be estimated in the time horizon until maturity. In either case, the expected loss will be the sum total of the losses expected in the individual periods, discounted by the effective interest rate.

To assess the materiality of growth in the risk of mortgage exposures the Bank uses a model based on marginal PD, i.e. probability of default in a given month, calculated as of the moment of the initial recognition of the loan. This allows reflecting the differentiation of the loan quality characteristic for retail customers over the lifetime of the exposure. The Bank identifies material risk increases based on the comparison of probability of default curves over the lifetime of exposure on initial recognition and on a given reporting date. For each reporting date, only those parts of the initial and current PD curve are compared which correspond to the period from the reporting date to the maturity of the loan. The comparison is based on average PD probability values in the given period adjusted for current and forecast macroeconomic ratios.

Additionally, to assess the materiality of credit risk increases the Bank uses full quantitative and qualitative information, including information on:
- payment delinquencies exceeding 30 days;
- forbearance measures due to the borrower's financial distress;
- quarantine for Stage 2 exposures which have not shown premises for impairment in the previous 3 months.

Impairment premises of credit exposures comprise in particular:
- delays in repayment of a material amount of principal or interest exceeding 90 days;
- conclusion of a restructuring agreement or applying a relief in repayment of the debt for economic or legal reasons resulting from the customer's financial distress (until the debt is considered recoverable);
- the Bank giving notice and requesting immediate repayment of the loan;
- petitioning for consumer bankruptcy by at least one of the co-borrowers;
- so-called contamination of the loans, i.e. situations whereby impairment recognized on a loan exposure implicates the necessity of its recognition in all loan exposures in respect of residential loans of the relevant co-debtors – this premise requires checking both the Bank's and PKO Bank Polski SA's exposures.

In order to determine the value of assets at the time of default, the Bank determines the exposure at default parameter on the basis of future payments according to the repayment schedule and potential over- or underpayments.

In calculating the value of the ultimate expected loss, the Bank also considers the impact of macroeconomic scenarios on the respective parameters (PD, LGD). The methodology of calculation of the risk parameters includes back-testing of the dependence of the value of the parameters on macroeconomic conditions. Three macroeconomic scenarios developed on the basis of the Group are used for the purpose of calculating expected loss (as in the identification of an indication of a material increase in credit risk) – a baseline scenario and two alternative scenarios. The scope of projected indicators includes: the GDP growth rate, the unemployment rate, the 3M WIBOR rate, the property price index, and the NBP reference rate. The final expected loss is the average of expected losses in each scenario, weighted by the probability of the scenarios.

The structure of the loan portfolio and the amount of allowances for expected credit losses of PKO Bank Hipoteczny SA are shown in the tables in Note 22 "Expected credit losses".

40.4 Credit risk forecasting and monitoring

Credit risk is monitored at the level of individual transactions and at the level of the entire portfolio.

The monitoring of credit risk at the level of individual loan transactions is governed by the Bank's policies concerning, among other things, the early monitoring of delays in the payment of dues.

The monitoring of credit risk at the portfolio level consists of:
- monitoring the level of the portfolio credit risk taking into account the identified sources of credit risk and an analysis of the consequences and measures applied as part of systemic management;
- recommending preventative measures in the event of identifying an increased level of credit risk.

40.4.1 Maximum exposure to credit risk

The following table presents the maximum exposure to credit risk with respect to financial instruments covered by the provisions of IFRS 7 to which the requirements of IFRS 9 relating to impairment do not apply.

(IN PLN MILLION)

MAXIMUM EXPOSURE TO CREDIT RISK	30.06.2019	31.12.2018
Derivative hedging instruments	173,484	168,289
Total balance sheet exposure	**173,484**	**168,289**

40.4.2 Amounts due from banks

AMOUNTS DUE FROM BANKS	30.06.2019	31.12.2018
Amounts not overdue, not impaired (counterparty rating A2)	55	22
Total, gross	**55**	**22**
Allowances for expected credit losses	-	-
Total, net	**55**	**22**

40.4.3 Securities

SECURITIES	30.06.2019	31.12.2018
Issued by the State Treasury, PLN Treasury bonds (rating A)	1,158,142	842,965
Total, gross	**1,158,142**	**842,965**
Allowances for expected credit losses	-	-
Total, net	**1,158,142**	**842,965**

40.4.4 Loans and advances to customers

The loan portfolio is characterized by low exposure to impairment. At 30 June 2019, 63 impaired loans were recognized, and their share in the total loan portfolio amount was 0.05%, whereas as at 31 December 2018, 42 impaired loans were recognized, and their share in the total loan portfolio amounted to 0.04%.

LOANS AND ADVANCES TO CUSTOMERS	30.06.2019	31.12.2018
Loans not overdue, not impaired	24,444,394	20,998,000
Loans overdue, not impaired	176,210	92,650
Loans impaired	12,299	8,092
Total, gross	**24,632,903**	**21,098,742**
Allowances for loans not overdue, not impaired	(22,248)	(19,205)
Allowances for loans overdue, not impaired	(7,056)	(5,882)
Allowances for loans impaired	(4,403)	(3,186)
Total, net	**24,599,196**	**21,070,469**

LOANS AND ADVANCES TO CUSTOMERS, NOT IMPAIRED	30.06.2019	31.12.2018
not overdue	24,444,394	20,998,000
up to 30 days overdue	167,598	84,269
from 31 to 60 days overdue	5,753	6,922
from 61 to 90 days overdue	2,859	1,459
Total, gross	**24,620,604**	**21,090,650**

Loan portfolio and financial liabilities granted by PD range

(IN PLN MILLION)

The PD parameter presented in the following tables defines the probability of default over a 12-month horizon:

LOANS AND ADVANCES TO CUSTOMERS	30.06.2019				
PD RANGE	Stage 1	Stage 2	Stage 3	POCI	Total, gross
<0,01%	462,054	367	-	-	**462,421**
0,01% - 0,02%	2,690,570	1,126	-	-	**2,691,696**
0,02% - 0,05%	6,741,176	3,464	-	-	**6,744,640**
0,05% - 0,1%	5,758,898	3,040	-	-	**5,761,938**
0,1% - 0,3%	6,802,824	4,004	-	-	**6,806,828**
0,3% - 1,0%	1,651,189	89,219	-	-	**1,740,408**
1,0% - 10%	208,674	152,694	-	-	**361,368**
10% - 100%	11,541	39,764	12,299	-	**63,604**
Total gross amount	**24,326,926**	**293,678**	**12,299**	**-**	**24,632,903**

LOANS AND ADVANCES TO CUSTOMERS	31.12.2018				
PD RANGE	Stage 1	Stage 2	Stage 3	POCI	Total, gross
<0,01%	1,092,324	625	-	-	**1,092,949**
0,01% - 0,02%	2,880,865	1,438	-	-	**2,882,303**
0,02% - 0,05%	5,577,867	2,817	-	-	**5,580,684**
0,05% - 0,1%	4,672,304	2,070	-	-	**4,674,374**
0,1% - 0,3%	5,077,344	3,424	-	-	**5,080,768**
0,3% - 1,0%	1,201,972	74,853	-	-	**1,276,825**
1,0% - 10%	312,451	150,920	-	-	**463,371**
10% - 100%	8,595	30,781	8,092	-	**47,468**
Total gross amount	**20,823,722**	**266,928**	**8,092**	**-**	**21,098,742**

LOAN COMMITMENTS	30.06.2019				
PD RANGE	Stage 1	Stage 2	Stage 3	POCI	Total
<0,01%	25,557	-	-	-	**25,557**
0,01% - 0,02%	84,454	-	-	-	**84,454**
0,02% - 0,05%	133,167	-	-	-	**133,167**
0,05% - 0,1%	264,892	311	-	-	**265,203**
0,1% - 0,3%	89,603	-	-	-	**89,603**
0,3% - 1,0%	21,604	778	-	-	**22,382**
1,0% - 10%	302	930	-	-	**1,232**
10% - 100%	-	200	-	-	**200**
Total nominal amount	**619,579**	**2,219**	**-**	**-**	**621,798**

(IN PLN MILLION)

LOAN COMMITMENTS	31.12.2018				
PD RANGE	Stage 1	Stage 2	Stage 3	POCI	Total
<0,01%	131,526	-	-	-	**131,526**
0,01% - 0,02%	122,745	-	-	-	**122,745**
0,02% - 0,05%	118,025	-	-	-	**118,025**
0,05% - 0,1%	250,835	110	-	-	**250,945**
0,1% - 0,3%	79,044	-	-	-	**79,044**
0,3% - 1,0%	15,633	995	-	-	**16,628**
1,0% - 10%	-	304	-	-	**304**
10% - 100%	-	-	-	-	**-**
Total nominal amount	**717,808**	**1,409**	**-**	**-**	**719,217**

40.4.5 Forbearance practices

The Bank defines forbearance as actions aimed at amending the contractual terms agreed with a debtor or an issuer, forced by the debtor's difficult financial situation (restructuring activities introducing concessions that otherwise would not have been granted). The purpose of forbearance activities is to restore a debtor's ability to fulfil his obligations towards the Bank and to maximize the effectiveness of non-performing loan management, i.e. obtaining the highest recoveries while minimizing their costs.

Forbearance changes in repayment terms may consist in:

- dividing the debt due into instalments;
- changing the repayment scheme (annuities, degressive instalments);
- extending the loan period;
- changing the interest rate;
- changing the margin;
- reducing the debt.

As a result of signing and repaying the amounts due under a forbearance agreement on a timely basis, a non-performing loan becomes performing.

The granting of forbearance concessions recognized as impairment triggers results in the recognition of a default event and the classification of the credit exposure in the non-performing portfolio.

The inclusion of such exposures in the portfolio of serviced exposures (discontinuation of recognition of the forbearance agreement as an impairment trigger) takes place at least 12 months after the introduction of forbearance, provided that all payments in arrears and at least six scheduled payments have been made by the customer and, in the Bank's opinion, the current situation of the customer does not pose a threat to their compliance with the terms of the restructuring agreement.

Exposures cease to meet the criteria of a forborne exposure when all of the following conditions are met:

- at least 24 months have passed from the date of including the forborne exposure in the portfolio of serviced exposures (conditional period);
- as at the end of the conditional period referred to above, the customer has no debt vis-à-vis the Bank overdue for more than 30 days;
- at least 12 instalments have been repaid on a timely basis and in the amounts agreed.

Forborne exposures are monitored on an on-going basis. Due to the impairment trigger or a significant increase in credit risk identified in connection therewith, throughout the whole period of their recognition, allowances are recognized for these exposures in the amount of expected losses over the life horizon of the exposure.

(IN PLN MILLION)

EXPOSURES SUBJECT TO FORBEARANCE IN THE LOAN PORTFOLIO	30.06.2019	31.12.2018
Gross loans and advances to customers, of which:	24,632,903	21,098,742
subject to forbearance	4,305	2,420
Impairment allowances on loans and advances to customers, of which:	(33,707)	(28,273)
subject to forbearance	(1,159)	(801)
Net loans and advances to customers, including:	**24,599,196**	**21,070,469**
subject to forbearance	**3,146**	**1,619**

40.5 Credit risk reporting

Monthly and quarterly credit risk reports are prepared in the Bank. Credit risk reporting involves periodical reporting on the structure and scale of risk exposure of the Bank's loan portfolio. Reports are submitted to the Credit Committee on a monthly basis and to the Bank's Management Board, the Supervisory Board Risk Committee and the Supervisory Board on a quarterly basis.

40.6 Credit risk management actions

The basic credit risk management tools used by PKO Bank Hipoteczny SA comprise in particular:

- strategic and internal (portfolio) risk tolerance limits;
- minimum transaction conditions (i.e. the maximum value of LTV, maximum loan amount, required down payment, required collateral, the amount of a single loan to MLV);
- a scoring system, including specific cut-off points (the minimum number of score points making it possible to accept the loan transaction);
- limits of loan exposures of Bank customers – limits defining the Bank's appetite for credit risk resulting, among other things, from Recommendation S (such as the ratio of the costs of servicing credit and financial liabilities to the customer's income, i.e. Debt-to-Income (DtI) ratio, acceptable to the Supervisory Board);
- competence limits – defining the maximum level of credit decision-making powers concerning the customers of the Bank; the amount of competence limits depends on the authority level at which the credit decision is made (within the Bank's organization);
- minimum loan margins, taking into account the costs of credit risk.

A key role in establishing minimum transaction conditions is played by the collateral policy. It is pursued by setting up mortgages on the financed properties, and its main purpose is to limit credit losses resulting from the customers' inability to repay their liabilities to the Bank. At the same time, the Bank follows the overriding principle that collateral is only accepted as a loan support instrument and may not be used as a substitute for the customer's ability to pay his/her dues.

41. Concentration risk management

Concentration risk is analysed in the Bank in relation to lending and is defined as the threat of the Bank's excessive exposure to:

- customers or groups or related customers;
- common or correlated risk factors;
- characterized by the potential to generate losses large enough to threaten the financial standing of the Bank or the ability to conduct its core operations or to lead to a significant change in the Bank's risk profile.

As part of the management of concentration risk, the Bank performs regular risk identification, measurement, control, monitoring and reporting.

Given the high degree of dispersion of the Bank's portfolio in terms of exposure to individual customers, the Bank identifies and assesses the concentration risk by analysing the structure of the portfolio in relation to significant risk factors (characteristics of exposure) from the point of view of credit risk, and on this basis distinguishes groups of exposures whose excessive concentration is undesirable and could generate losses in excess of the Bank's appetite for credit risk in stress conditions.

(IN PLN MILLION)

The following table presents the concentration ratio of loans and advances portfolio measured with the share of largest exposures in the Bank's total loan portfolio.

GROSS LOANS AND ADVANCES TO CUSTOMERS - CONCENTRATION RATIO	30.06.2019	31.12.2018
10 largest exposures	0.05%	0.06%
20 largest exposures	0.10%	0.10%
50 largest exposures	0.22%	0.24%
100 largest exposures	0.40%	0.45%

Measurement and control of the concentration risk in PKO Bank Hipoteczny SA are performed by determining the amount of exposure, which generates the risk of concentration, and comparing the amount to the set limits resulting from legal regulations and internal limits.

Internal limits of exposure are determined in respect of the Bank's own funds and the Bank's total credit exposure, and reflect the Bank's credit risk appetite taking into consideration both normal and stress conditions.

The Bank mitigates concentration risk by using the following limits, the use of which is monitored and reported on a monthly basis:

- exposure limits to a single entity or group of entities related in terms of capital or organizational links;
- limits of concentration of internal receivables;
- exposure limits to credit exposures for customers generating income from a commercial activity;
- exposure limits to credit exposures for customers with a DtI ratio of over 50%.

In the period ended 30 June 2019 as well as in each of the preceding periods the Bank did not exceed any of the concentration limits.

Monthly and quarterly concentration risk reports are prepared in the Bank. Reports are submitted to the Credit Committee on a monthly basis and to the Bank's Management Board, the Supervisory Board Risk Committee and the Supervisory Board on a quarterly basis.

42. Residual risk management

Residual risk is the risk arising from the effectiveness of the credit risk mitigation techniques used by the Bank being lower than assumed.

The aim of residual risk management is to ensure the effectiveness of the credit risk mitigation techniques and eliminate the risk connected with the use of loan collateral.

In view of the above and considering the specialist nature of its business, the Bank attaches particular importance to monitoring the collateral value. Therefore a key role in determining the minimum transaction conditions is a collateral policy regarding credit risk. The mortgage collateral policy is aimed at properly securing the credit risk to which the Bank is exposed, including the establishment of mortgage collateral affording the highest possible recovery rates in the event of the need for debt recovery activities.

The Bank's policy regarding loan collateral and its valuations takes into the account the provisions of the following acts: the Banking Act, the Mortgage Covered Bonds and Mortgage Banks Act, the Act on Land and Mortgage Registers and Mortgage; In addition, the matter of collateral is also addressed by the guidelines and recommendations of the Polish Financial Supervision Authority, including Recommendations F, S, and J, and the provisions of internal regulations of the Bank.

The Bank has enacted and follows the Regulations for Determining the Property Value for Mortgage Lending Purposes approved by the Polish Financial Supervision Authority, issued on the basis of the Polish Mortgage Covered Bonds and Mortgage Banks Act of 29 August 1997, taking into account Recommendation F concerning the basic criteria applied by the Polish Financial Supervision Authority in approving the rules for determining the property value for mortgage lending purposes enacted by mortgage banks.

The Property Value for Mortgage Lending Purposes is the value determined by the Bank, which in the Bank's opinion reflects the level of risk associated with the property serving as collateral for loans, and is used to determine the ceiling for granting or acquiring mortgage secured loans on a given property or for deciding whether the receivables secured with said property may be acquired by the Bank.

(IN PLN MILLION)

PKO Bank Hipoteczny SA determines the MLV on the basis of expert valuations of the mortgage lending value of property. Such valuations are carried out with due diligence and prudence. They take into account only characteristics of the real estate and investments necessary for its construction that will have a permanent nature and which, assuming rational use, can be realized by any owner of the property. In the expert opinion, prepared as at a specific date, the assumptions and parameters of the analysis are documented, as is the process of setting the MLV and the proposed MLV that results. The expert valuation report takes into account the analyses and forecasts concerning specific parameters for a given property that affect the credit risk assessment, as well as general factors such as: population growth, unemployment rate, and local zoning plans.

The Bank accepts the following as a mandatory legal collateral for loans granted or acquired:

- the highest priority mortgage on the property registered in the land and mortgage register;
- the assignment of rights from the insurance policies against fire and other accidental causes for the mortgaged property underwritten on behalf of the Bank.

The following table presents the concentration ratio for the portfolio of loans and advances measured in terms of LtV based on market valuation.

GROSS LOANS BY LTV BASED ON MARKET VALUATION	30.06.2019	31.12.2018
below 50%	31%	29%
51% - 60%	18%	18%
61% - 70%	23%	23%
71% - 80%	20%	21%
81% - 90%	8%	9%
over 90%	0%	0%
Total	**100%**	**100%**
Average LtV based on market valuation	58.0%	58.7%

The following table presents the concentration ratio for the portfolio of loans and advances by geographical region in which the real estate put up as collateral for the loan is located.

GROSS LOANS AND ADVANCES TO CUSTOMERS - BY GEOGRAPHICAL REGION	30.06.2019	31.12.2018
mazowiecki	23.6%	24.2%
śląsko-opolski	11.7%	11.3%
dolnośląski	10.6%	10.5%
wielkopolski	9.3%	9.4%
małopolsko-świętokrzyski	8.2%	8.3%
pomorski	8.1%	8.1%
lubelsko-podkarpacki	6.6%	6.8%
zachodnio-pomorski	6.2%	6.2%
łódzki	5.0%	4.8%
kujawsko-pomorski	4.8%	4.7%
warmińsko-mazurski	3.4%	3.3%
podlaski	2.5%	2.4%
Total	**100.0%**	**100.0%**

43. Liquidity risk management

Liquidity risk is the risk of the inability to settle the Bank's obligations when due as a result of the lack of liquid assets. Liquidity risk comprises funding risk, which is a risk of the inability to renew the required funding resources or the loss of access to new sources of funding.

Lack of liquidity may arise from an inappropriate structure of the statement of financial position, mismatch of cash flows, counterparty default, customers' sudden realization of contingent commitments, the inability to roll over bonds or other market events.

The aim of liquidity risk management is to ensure a sufficient level of funds to settle present and future obligations (including potential obligations) when due, taking into account the nature of activities and requirements which may occur due to changes in market conditions. The Bank maintains a proper liquidity level by appropriate structuring of the statement of financial position and financial liabilities granted.

(IN PLN MILLION)

The Bank manages liquidity risk in order to maintain current, short-term, medium-term and long-term liquidity. The fundamental rule of the liquidity policy of PKO Bank Hipoteczny SA is to maintain an appropriate portfolio of liquid securities, to ensure appropriate liquidity supporting tools and to increase stable sources of funding (in particular, from the issue of mortgage covered bonds). Money market instruments and unsecured bonds issued are also used in liquidity risk management.

The liquidity risk management is built into the risk management process described in Note 39.2.

The Bank's Supervisory Board oversees the liquidity management policy and reviews reports concerning the Bank's liquidity, the Bank's liquidity risk exposure, the utilization of internal limits and the consequences of liquidity risk management decisions. The Supervisory Board approves a set of strategic limits which determine liquidity risk tolerance and the rules of stress-testing with regard to liquidity.

The Bank's Management Board supervises liquidity risk management, and at least once a year reviews, evaluates and potentially updates internal regulations (including the policies for stress testing), informing the Supervisory Board about the results of the assessment and the implementation of liquidity risk management policies. The Management Board makes decisions about corrective actions, in particular in a situation of heightened risk of the loss of liquidity and accepts financial plans in accordance with separate internal regulations of the Bank regarding the annual planning process. In the event of potential liquidity problems, the Bank's Management Board promptly informs the Supervisory Board about the level of the Bank's liquidity, threats and actions taken.

The Assets and Liabilities Management Committee (ALCO) establishes internal limits on liquidity risk, verifies, at least once a year, the level of existing internal limits on liquidity risk, issues recommendations for actions for the purpose of maintaining an acceptable level of liquidity risk by the Bank, and monitors liquidity risk on the basis of the reports obtained. The ALCO also initiates action to protect the Bank from liquidity risk, in particular, for the purpose of implementing the banking risk management strategy adopted by the Bank.

The Treasury Bureau is responsible for the operational management of short-term liquidity and the Risk Measurement Bureau deals with overseeing this activity and with developing risk management tools and checking the observance of the limits.

43.1 LIQUIDITY RISK MEASUREMENT AND ASSESSMENT

The Bank applies the following liquidity risk measures:

- contractual, actualized and stress-test liquidity gap;
- liquidity surplus and survival horizon;
- regulatory liquidity measures:
  - M3 – Non-liquid assets to own funds;
  - M4 – Non-liquid assets and assets with limited liquidity to own funds and stable external funds ratio;
- short-term liquidity measure:
  - Liquidity coverage ratio (LCR) - the coverage ratio of net outflows up to 1 month;
- the concentration of funding sources;
- coverage ratio of long-term assets with long-term funding;
- the liquidity stress tests.

The adjusted liquidity gaps as at 30 June 2019 and as at 31 December 2018 are presented below.

LIQUIDITY GAP AS AT 30.06.2019	on demand	0 - 1 month	1 - 3 months	3 - 6 months	6 - 12 months	12 - 24 months	24 - 60 months	more than 60 months
Adjusted periodic gap	1,899,215	581,956	(36,171)	(1,290,237)	(1,573,834)	(4,317,565)	(10,727,551)	14,792,078
Adjusted cumulative periodic gap	1,899,215	2,481,171	2,445,000	1,154,763	(419,071)	(4,736,636)	(15,464,187)	(672,109)

As at 30 June 2019, in the ranges up to 6 months, the cumulative adjusted liquidity gap has positive values, which means a surplus of maturing assets increased by estimated inflows from available overdraft limit over mature liabilities in the short and medium term.

LIQUIDITY GAP AS AT 31.12.2018	on demand	0 - 1 month	1 - 3 months	3 - 6 months	6 - 12 months	12 - 24 months	24 - 60 months	more than 60 months
Adjusted periodic gap	1,171,448	393,495	(45,787)	(1,760,766)	(397,478)	(4,098,827)	(5,517,552)	9,610,867
Adjusted cumulative periodic gap	1,171,448	1,564,943	1,519,156	(241,610)	(639,088)	(4,737,915)	(10,255,467)	(644,600)

The liquidity surplus is determined with account taken of outflows of funds under stress conditions. The survival horizon means the time during which the Bank will see a surplus of inflows over outflows under stress conditions.

A positive liquidity surplus in a one-month time horizon indicates a sufficient level of short-term liquidity.

A liquidity surplus comprises:

- basic liquidity surplus, consisting of items acquirable within 7 days. The basic part of the liquidity surplus comprises:
  - liquid assets;
  - inflows and outflows over a horizon of up to 7 days (inclusive);
  - additional stress-test outflows over a horizon of up to 7 days (inclusive).
- supplementary liquidity surplus, consisting of items acquirable from 8 to 30 days. The supplementary part of the liquidity surplus comprises:
  - inflows and outflows over a horizon of 8 to 30 days;
  - additional stress-test outflows over a horizon of 8 to 30 days.

SENSITIVITY MEASURE	30.06.2019	31.12.2018
Liquidity surplus in the horizon of up to 1 month (in PLN million)	2,004	1,452

Liquidity surplus is defined as the difference between the sum of liquid assets and the unconditional stand-by credit facility, and the expected and potential liabilities which mature in a given time horizon.

The Bank monitors all liquidity standards specified in the Resolution of the PFSA 386/2008 dated 17 December 2008. The values of liquidity standards binding as at the end of the reporting period ended 30 June 2019 and 31 December 2018 and the average, minimum and maximum values during these reporting periods are shown in the following table:

30.06.2019	as at the end of the period	average during the period	minimum for the period	maximum for the period	regulatory minimum
M3	264.69	326.24	145.75	1,807.65	>1.0
M4	1.03	1.03	1.03	1.04	>1.0

31.12.2018	as at the end of the period	average during the period	minimum for the period	maximum for the period	regulatory minimum
M3	1,493.58	921.62	78.48	2,164.57	>1.0
M4	1.03	1.04	1.03	1.05	>1.0

The liquidity coverage ratio (LCR) of net outflows up to 1 month is shown in the following table:

SENSITIVITY MEASURE	30.06.2019	31.12.2018
Liquidity coverage ratio up to 1 month (LCR)	285%	1255%
LCR regulatory limit	100%	100%

43.2 LIQUIDITY RISK CONTROL

The control of liquidity risk consists of determining strategic tolerance limits appropriate for the scale and complexity of the Bank, and internal liquidity risk limits for short-, medium-, and long-term liquidity, which are monitored, and if overrun, the Bank initiates management actions.

(IN PLN MILLION)

43.3 Liquidity risk forecasting and monitoring

The liquidity risk exposure of PKO Bank Hipoteczny SA as at 30 June 2019 and 31 December 2018 was within the strategic and internal limits set. In the period ended 30 June 2019 and 31 December 2018 the Bank did not exceed any of the standards nor any strategic or internal limits.

The Bank regularly reviews the business assumptions which may have a material effect on the projections of liquidity risk measures. Forecasts of the basic liquidity risk measures are prepared periodically and on an on-going basis and these are juxtaposed with the internal limits.

43.4 Liquidity gap in the presentation of contractual cash flows

Liquidity gap in the presentation of contractual cash flows is a mismatch between the inflows and outflows classified in a given range. In the calculation of liquidity gap relating to cash flows the Bank takes into account all instruments concluded as at the balance sheet date. An increase in the amount of loans granted or rolling over of financing for a consecutive period is not taken into account. It is assumed that the funds available under the existing credit lines will be utilized.

30.06.2019	on demand	0 - 1 month	1 - 3 months	3 - 6 months	6 - 12 months	12 - 24 months	24 - 60 months	more than 60 months	Total
Inflows	1,899,216	154,350	288,095	438,161	1,054,997	1,976,584	5,848,769	26,940,599	38,600,771
securities	-	9,071	-	1,280	169,028	190,677	568,738	310,974	1,249,768
loans and advances to customers	-	144,893	288,095	436,881	885,969	1,785,907	5,280,031	26,629,625	35,451,401
credit lines	1,899,139	-	-	-	-	-	-	-	1,899,139
other	77	386	-	-	-	-	-	-	463
Outflows	668	1,025,344	407,544	2,559,455	2,319,325	3,696,506	14,122,473	3,217,910	27,349,225
amounts due to banks	668	5,417	15,377	5,581	1,682,396	2,478,895	2,053,443	-	6,241,777
mortgage covered bonds issued	-	11,602	35,687	29,191	80,444	1,182,381	12,068,178	3,217,910	16,625,393
unsecured bonds issued	-	843,000	170,935	2,388,410	454,254	-	-	-	3,856,599
disbursement of loan commitments	-	161,667	185,545	136,273	102,231	35,230	852	-	621,798
other	-	3,658	-	-	-	-	-	-	3,658
Inflows from derivative hedging instruments	-	-	25,744	7,045	37,976	72,272	9,843,866	2,152,362	12,139,265
Outflows on derivative hedging instruments	-	25,749	47,008	83,921	173,497	371,748	10,472,946	2,167,391	13,342,260
Periodic gap	1,898,548	(896,743)	(140,713)	(2,198,170)	(1,399,849)	(2,019,398)	(8,902,784)	23,707,660	10,048,551
Cumulative gap	1,898,548	1,001,805	861,092	(1,337,078)	(2,736,927)	(4,756,325)	(13,659,109)	10,048,551	

31.12.2018	on demand	0 - 1 month	1 - 3 months	3 - 6 months	6 - 12 months	12 - 24 months	24 - 60 months	more than 60 months	Total
Inflows	1,171,448	314,154	244,439	373,354	760,153	1,694,468	4,852,822	23,000,979	32,411,817
securities	-	191,172	-	1,280	5,985	169,036	335,428	181,920	884,821
loans and advances to customers	-	122,533	244,439	372,074	754,168	1,525,432	4,517,394	22,819,059	30,355,099
credit lines	1,171,420	-	-	-	-	-	-	-	1,171,420
other	28	449	-	-	-	-	-	-	477
Outflows	5,496	641,563	656,458	4,103,379	926,399	2,200,035	8,770,547	5,992,147	23,296,024
amounts due to banks	5,496	10,778	12,120	1,804,054	678,562	1,628,999	1,517,526	-	5,657,535
mortgage covered bonds issued	-	38,803	9,810	23,775	70,874	174,505	7,251,797	5,992,147	13,561,711
unsecured bonds issued	-	386,239	455,400	2,121,798	23,037	352,340	-	-	3,338,814
disbursement of loan commitments	-	186,996	179,128	153,752	153,926	44,191	1,224	-	719,217
other	-	18,747	-	-	-	-	-	-	18,747
Inflows from derivative hedging instruments	-	27,913	882	5,017	27,011	63,510	4,699,897	4,451,008	9,275,238
Outflows on derivative hedging instruments	-	26,465	28,673	61,503	129,001	282,588	5,297,119	4,442,569	10,267,918
Periodic gap	1,165,952	(325,961)	(439,810)	(3,786,511)	(268,236)	(724,645)	(4,514,947)	17,017,271	8,123,113
Cumulative gap	1,165,952	839,991	400,181	(3,386,330)	(3,654,566)	(4,379,211)	(8,894,158)	8,123,113	

(IN PLN MILLION)

43.5 Concentration of funding sources

The Bank recognizes the risk of concentration of funding sources, as an element of liquidity risk, determined by circumstances under which the funding structure becomes susceptible to the occurrence of individual events or single factors, such as sudden significant withdrawal of funds or insufficient access to new funding.

The business model of the Bank assumes that the risk of concentration of funding sources results from:

- a high proportion of mortgage covered bonds in the funding structure (mortgage covered bonds are a stable source of funding, however the balloon nature of their redemption causes further need for a new issue or alternative source of funding to arise at redemption in most cases);
- funding supplied by the parent;
- issue of short-term bonds.

The table below presents the structure of the Bank's funding sources:

STRUCTURE OF THE BANK'S FINANCING	30.06.2019	31.12.2018
Mortgage covered bonds issued	61.5%	58.1%
Unsecured bonds issued	14.7%	15.0%
Funds from the parent entity	15.0%	18.7%
Equity	7.2%	6.7%
Other	1.6%	1.5%
Total	**100.0%**	**100.0%**

The share of funding raised from the parent amounted to 15.0% as at 30 June 2019 (18.7% as at 31 December 2018). Such level of the indicator is consistent with the financial plan at the current stage of the Bank's operations and is expected to gradually decrease with successive issues of mortgage covered bonds and own bonds. The funding concentration risk is assessed as acceptable.

Seeking to reduce the concentration risk of funding sources, the Bank has implemented a system of internal limits, both in short-term and long-term horizons, according to mortgage covered bond issues carried out by the Bank. In the period ended 30 June 2019 and 31 December 2018 none of these limits were exceeded.

43.6 Liquidity stress tests

Liquidity stress tests present the impact of stressed market conditions on the level of the Bank's liquidity. Shock analyses are carried out on the basis of scenarios involving hypothetical changes in the following factors:

- shock changes in market parameters on financial markets;
- the impact of extreme changes in market factors, as well as drops in prices on the property market on the anticipated losses on the housing loan portfolio;
- down rating of the Bank's counterparties and of the Bank;
- deterioration of the creditworthiness of borrowers;
- increased instability of funding sources;
- increased disbursements of mortgage loans granted;
- inability to roll over short-term bond issues or obtain new ones;
- inability to roll over mortgage covered bond issues or obtain new ones.

Stress test results are used in particular in:

- monitoring the Bank's exposure to liquidity risk under stressed conditions;
- the process of setting internal limits for liquidity risk measures;
- controlling liquidity maintenance, for each day of the 30-day time range;
- the process of planning the Bank's statement of financial position;
- the process of determining conditions triggering the implementation of liquidity contingency plans of the Bank.

Test results are presented at the meetings of the Management Board and the Supervisory Board of the Bank.

The stress tests conducted on the basis of the Bank's financial data as at 30 June 2019 and as at 31 December 2018 did not indicate any risk to the Bank's business due to the occurrence of hypothetical stressed market conditions. Owing to the well-balanced funding structure, long maturities of most of its liabilities and a sufficient level of liquid assets, the Bank has a high ability to survive a liquidity crisis.

43.7 Liquidity risk reporting

The Bank prepares reports concerning liquidity risk on a daily, weekly, monthly and quarterly basis. Reports containing information about the exposure to liquidity risk and information about the utilization of the liquidity risk limits are submitted to the ALCO on a monthly basis and to the Management Board and the Supervisory Board of the Bank on a quarterly basis.

43.8 Liquidity risk management actions

The risk management system of PKO Bank Hipoteczny SA comprises the following components:

- procedures for liquidity risk management, including in particular emergency plans;
- internal limits limiting liquidity risk;
- deposit and derivative transactions, including structural currency transactions and transactions for sale or purchase of securities;
- unconditional liquidity support instruments obtained from PKO Bank Polski SA;
- transactions ensuring long-term funding of the lending activity.

The Bank pays particular attention to matching the timing of cash flows upon the maturity of material liabilities (redemption of mortgage covered bonds).

44. Interest rate risk management

The operations of PKO Bank Hipoteczny SA are exposed to interest rate risk, which is defined as the risk of loss on balance sheet items and financial liabilities granted by the Bank, sensitive to movements in the interest rates, as a result of changes in the market interest rates.

The aim of interest rate risk management is to limit any potential losses incurred due to changes in the market interest rates to an acceptable level by the proper shaping of the structure of the balance sheet items and financial liabilities granted, among other things, in terms of the matching of the repricing periods.

44.1 Interest rate risk measurement and assessment

In the process of interest rate risk management, the Bank uses the net interest income sensitivity (NIIS) measure, the Basis Point Value (BPV) measure, stress tests and repricing gap reports.

The net interest income sensitivity (NIIS) measure is a measure determining the change in net interest income arising from a sudden change in the interest rates while the Basis Point Value (BPV) measure is a measure illustrating the impact of such a change on the economic value of capital. The measures allow for the diversification of the repricing periods of individual interest items in each subsequent time range.

Stress tests are used to estimate potential losses resulting from the maintained structure of the statement of financial position and financial liabilities granted in the event of the occurrence of the hypothetical scenarios within which parallel shifts in interest rate curves by ±50 bps, ±100 bps and ±200 bps or changes in the shape of interest rate curves are arbitrarily assumed. Reversed stress test scenarios are also adopted, assuming a drop in the Bank's financial result to PLN 0 and a loss of the Bank's economic value of 1% of its equity. The repricing gap presents the difference between the current value of the assets and liabilities exposed to interest rate risk, which are repriced within the given time range, where positions which are not marked-to-market (e.g. loans) are recognized in the amounts serving as the basis for interest accrual.

The repricing gap report presented below includes assets and liabilities as financial liabilities granted which are sensitive to changes in interest rates. They do not include contingent liabilities which are insensitive to interest rate risk, the Bank's own funds, amounts due from banks in the form of current account balances and current account overdrafts.

(IN PLN MILLION)

30.06.2019	0-1 month	1-3 months	3-6 months	6-12 months	1-2 years	2-5 years	>5 years	Total
Assets, including:	8,800,183	15,981,773	865,362	3,313	8,020	1,037	-	25,659,688
securities	1,013,480	-	143,000	-	-	-	-	1,156,480
loans and advances to customers	7,786,703	15,981,773	722,362	3,313	8,020	1,037	-	24,503,208
Liabilities	(4,888,917)	(4,403,042)	(2,386,200)	(102,000)	-	(9,955,308)	(2,186,000)	(23,921,467)
amounts due to banks	(2,015,917)	(2,104,242)	-	-	-	-	-	(4,120,159)
mortgage covered bonds issued	(2,030,000)	(1,780,000)	-	-	-	(9,955,308)	(2,186,000)	(15,951,308)
unsecured bonds issued	(843,000)	(518,800)	(2,386,200)	(102,000)	-	-	-	(3,850,000)
Derivative hedging instruments - assets	-	295	591	2,421	3,537	9,954,624	2,185,672	12,147,140
Derivative hedging instruments - liabilities	(4,232,131)	(7,956,833)	(586)	(2,262)	(3,288)	(13,350)	(1,978)	(12,210,428)
Periodic gap	(320,865)	3,622,193	(1,520,833)	(98,528)	8,269	(12,997)	(2,306)	1,674,933
Cumulative gap	(320,865)	3,301,328	1,780,495	1,681,967	1,690,236	1,677,239	1,674,933	

31.12.2018	0-1 month	1-3 months	3-6 months	6-12 months	1-2 years	2-5 years	>5 years	Total
Assets, including:	7,606,968	14,063,152	144,045	3,636	7,794	-	-	21,825,595
securities	693,480	-	143,000	-	-	-	-	836,480
loans and advances to customers	6,913,488	14,063,152	1,045	3,636	7,794	-	-	20,989,115
Liabilities	(3,642,594)	(5,357,824)	(2,119,700)	(18,500)	-	(4,797,200)	(4,467,500)	(20,403,318)
amounts due to banks	(1,227,794)	(3,022,424)	-	-	-	-	-	(4,250,218)
mortgage covered bonds issued	(2,030,000)	(1,530,000)	-	-	-	(4,797,200)	(4,467,500)	(12,824,700)
unsecured bonds issued	(384,800)	(805,400)	(2,119,700)	(18,500)	-	-	-	(3,328,400)
Derivative hedging instruments - assets	435	-	1,202	295	2,040	4,799,644	4,466,738	9,270,354
Derivative hedging instruments - liabilities	(4,232,565)	(4,951,687)	(1,128)	(286)	(1,908)	(9,971)	(4,122)	(9,201,667)
Periodic gap	(267,756)	3,753,641	(1,975,581)	(14,855)	7,926	(7,527)	(4,884)	1,490,964
Cumulative gap	(267,756)	3,485,885	1,510,304	1,495,449	1,503,375	1,495,848	1,490,964	

44.2 INTEREST RATE RISK CONTROL

The control of interest rate risk involves determining interest rate risk limits and thresholds appropriate for the scale and complexity of the Bank's operations, in particular strategic tolerance limits for interest rate risk, which are subject to monitoring, and in the event these are exceeded management actions are taken.

44.3 INTEREST RATE RISK FORECASTING AND MONITORING

The interest rate risk exposure of PKO Bank Hipoteczny SA as at 30 June 2019 and 31 December 2018 was within the strategic and internal limits set. Owing to effective mitigating activities, despite dynamically growing total assets, interest rate risk was relatively low and caused by the mismatch between the repricing dates of the interest rates on the Bank's assets and liabilities in the shortest repricing ranges, i.e. up to 3 months.

44.4 INTEREST RATE RISK REPORTING

The Bank prepares reports concerning interest rate risk on a daily, weekly, monthly and quarterly basis. Reports containing information about the exposure to interest rate risk and information about the utilization of the interest rate risk limits are submitted to the ALCO on a monthly basis and to the Management Board and the Supervisory Board of the Bank on a quarterly basis.

44.5 Interest rate risk management actions

The basic interest rate risk management tools used by PKO Bank Hipoteczny SA comprise in particular:

- procedures concerning the management of interest rate risk;
- internal limits on interest rate risk, among other things for basis point value sensitivity and net interest income sensitivity;
- specification of the permitted types of interest-rate based transactions;
- determining acceptable transactions based on interest rate;
- concluding derivative transactions which limit the interest rate risk level;
- the proper selection of transaction parameters and making it possible to apply natural hedges between assets and liabilities.

The Bank manages interest rate risk by matching the repricing structure of the assets and funding sources (natural hedging) and, on an as needs basis, and if necessary enters into hedging transactions (derivative contracts).

45. Foreign exchange risk management

The operations of PKO Bank Hipoteczny SA are exposed to foreign exchange risk, which is defined as the risk of loss due to changes in the foreign exchange rates generated by the maintenance of open positions in various currencies.

The aim of foreign exchange risk management is to limit any potential losses incurred due to changes in the exchange rates to an acceptable level by the proper shaping of the currency structure of the statement of financial positions items and financial liabilities granted, and the use of derivative instruments.

In the process of foreign exchange risk management the Bank uses individual and aggregate FX positions and stress tests. Stress tests are used to estimate the potential loss on the positions taken in foreign currencies in the event of an extraordinary situation in the FX market. The Bank uses hypothetical scenarios – which assume a hypothetical appreciation or depreciation of currency rates (20 per cent and 50 per cent).

FOREIGN CURRENCY POSITION EXPRESSED IN PLN '000	30.06.2019	31.12.2018
EUR	23	78
USD	2	2

The foreign exchange risk exposure of PKO Bank Hipoteczny SA as at 30 June 2019 and 31 December 2018 was within the strategic and internal limits set.

The Bank closes all open FX positions on an ongoing basis, and the control and reporting procedures implemented by the Bank significantly limit the impact of changes in exchange rates on the Bank's financial performance, hence the foreign exchange risk as at 30 June 2019 and as at 31 December 2018 was at a low level.

The Bank prepares reports concerning foreign exchange risk on a daily, weekly, monthly and quarterly basis. Reports containing information about the exposure to foreign currency risk and information about the utilization of the foreign currency risk limits are submitted to the ALCO on a monthly basis and to the Management Board and the Supervisory Board of the Bank on a quarterly basis.

The basic foreign exchange rate risk management tools used by PKO Bank Hipoteczny SA comprise in particular:

- procedures concerning the management of foreign exchange risk;
- limits and thresholds on foreign exchange risk, among others on foreign exchange positions;
- specification of the permitted types of foreign exchange transactions.

46. Model risk management

Model risk is the risk of losses resulting from wrong business decisions made on the basis of the models used.

The aim of the management of model risk is to mitigate the risk of losses resulting from a wrong business decision made on the basis of the models used by way of a properly defined and implemented model management process.

All models of significance for the Bank are subject to a process of regular and impartial validation by the Bank's validation function – The Validation and Risk Control Team.

The model risk management process in PKO Bank Hipoteczny SA is consistent with the solutions of the PKO Bank Polski Group.

46.1 Model risk measurement and assessment

Identification of model risk consists in particular of:

- collecting information about the models in use and those to be implemented;
- periodical determination of the significance of the models.

The assessment of model risk is aimed at determining the scale of threats connected with the existence of model risk. The evaluation is made at the level of each model as well as on an aggregate basis at the level of the Bank.

46.2 Model risk control

The aim of the model risk control is to maintain the aggregate assessment of model risk at a level acceptable to the Bank. The control of model risk consists of defining mechanisms for probing the model risk level and the risk mitigation tools.

The tools used for diagnosing model risk include in particular a strategic limit of model risk tolerance and model risk thresholds.

46.3 Model risk forecasting and monitoring

The aim of model risk monitoring is to diagnose the areas requiring management action. The following in particular are monitored as part of the model risk monitoring process:

- updating the model risk level;
- evaluating the utilization of the strategic limit of model risk tolerance and the values of the model risk thresholds;
- verifying the stage of implementation and evaluating the effectiveness of the implementation of actions intended to mitigate the model risk

46.4 Model risk reporting

The results of monitoring are presented in periodic reports for the Management Board, the Supervisory Board Risk Committee and the Supervisory Board containing a comprehensive assessment of model risk, particularly:

- information about the utilization of the strategic limit of model risk tolerance;
- information about the level of model risk;
- the model risk map;
- the status of implementation of the recommendations issued after model reviews or validation;
- suggested management actions to mitigate the model risk.

46.5 Model risk management actions

The aim of management actions is to develop the model risk management process and shape the risk level, in particular by setting acceptable risk levels and making decisions about the use of risk management supporting tools.

47. Operational risk management

Operational risk is defined as the risk of the occurrence of a loss due to non-compliance or failed internal processes, people and systems or external events. Operational risk includes legal risk, but not reputation risk or business risk. Operational risk is classified as a material risk.

The aim of operational risk management is to enhance the security of the operational activities pursued by the Bank by enhancing effective mechanisms of identification, assessment and measurement, limitation, monitoring of and reporting on operational risk tailored to the profile and the scale of operations.

The process of operational risk management is realized at the level of the entire Bank and at the level of each systemic operational risk management area. Systemic operational risk management involves the creation of solutions which enable the Bank to exercise control over the level of operational risk so that it can accomplish its goals. Ongoing operational risk management is conducted by every employee of the Bank, within their responsibilities and tasks.

For the purpose of managing operational risk, the Bank gathers data on operational incidents, on business environment factors, the results of operational risk self-assessment, data on key risk indicators in respect of operational risk (KRI) and data related to the quality of internal control.

Taking into account the scale of outsourcing and its potential impact on the operational risk profile, the Bank has prepared a risk management process related to the outsourcing of services, including sales and after sales servicing, and IT services. The management of this risk, carried out by different organizational units of the Bank, includes numerous components, such as the introduction of procedures of outsourcing services for the Bank, analysing and assessing the risk associated with the outsourcing of services by the Bank, assessing the reliability and financial position of the service providers, developing contingency plans for the Bank and its service providers (in particular, in the IT field), implementing adequate safeguards of the Bank's interests in outsourcing agreements, requirements for an appropriate insurance coverage by insourcers, monitoring the proper execution of contracts and the insourcers' position, including their periodic verification, recording incidents and losses related to the realization of services by insourcers.

47.1 OPERATIONAL RISK MEASUREMENT AND ASSESSMENT

Operational risk is measured in order to determine the scale of threats connected with the existence of operational risk using set risk measures. Operational risk measurement covers:

- determining the strategic operational risk tolerance limits;
- calculating key risk indicators (KRI);
- calculating the own funds requirement for operational risk under the BIA approach (BIA requirement);
- stress testing;
- calculating internal capital.

The operational risk self-assessment includes the identification and assessment of operational risk in relation to the Bank's processes. The operational risk self-assessment is conducted once a year and before the introduction of new or changed products, processes or applications used by the Bank, with the use of:

- data collected on operational incidents;
- results of inspections, proceedings and functional internal control;
- KRIs.

47.2 OPERATIONAL RISK CONTROL

The aim of operational risk control is to strive to maintain the Bank's operational risk at an acceptable level.

The control of operational risk involves determining the risk limits appropriate for the scale and complexity of the Bank's operations, in particular strategic tolerance limits for operational risk and KRI limits, including threshold and critical values.

The strategic operational risk tolerance limits are set by the Management Board and approved by the Supervisory Board.

47.3 OPERATIONAL RISK FORECASTING AND MONITORING

The aim of operational risk monitoring is to control operational risk and diagnose the areas requiring management action.

In particular, the Bank regularly monitors:

- the utilization of strategic tolerance limits and operational risk loss limits;
- the effectiveness and timeliness of actions undertaken to reduce or transfer the operational risk;
- the values of the KRIs;
- the results of operational risk self-assessment;
- the results of stress tests;

- operational incidents and their consequences.

47.4 Operational risk reporting

Operational risk information is reported for:
- the Bank's internal purposes: in particular, the Management and Supervisory Boards;
- regulatory bodies;
- shareholders and the financial market.

Reporting for the Bank's internal purposes related to operational risk is performed on a quarterly basis. Quarterly reports contain, in particular, information about:
- the results of the measurement and monitoring of operational risk;
- the operational risk profile of the Bank resulting from the process of identifying and assessing the threats to products, processes and applications of the Bank;
- the level of operational risk and the tools applied in operational risk management;
- the actions taken to limit operational risk and the evaluation of the effectiveness of the actions taken to reduce the operational risk level;
- recommendations, decisions and suggestions of the Management Board.

The quarterly reports also include information on operational risks identified in relation to the activities outsourced by the Bank to external entities, including, in particular, PKO Bank Polski SA.

47.5 Operational risk management actions

Management actions are taken when the self-assessed operational risk, KRI or adjusted operational risk reaches an elevated or high level at the Bank.

If the risk level is elevated or high, the Bank uses the following approach:
- risk reduction – mitigating the impact of the risk factors or the consequences of its materialization;
- risk transfer – the transfer of responsibility for covering potential losses to a third-party;
- risk avoidance – discontinuance of activities that generate risk or eliminate the possibility of occurrence of a risk factor.

The operational risk management process is subject to internal control including:
- a review of the strategy and the process of operational risk management;
- internal audit.

47.6 Operational losses incurred

In the first half of 2019, six operational risk incidents were disclosed at the Bank, which involved operational losses for the total net amount of PLN 1 thousand, whereas in the first half of 2018 there was one incident with a financial loss of PLN 5 thousand.

In order to limit losses arising from operational risk, the Bank applies ad hoc and systemic management measures. Ad hoc measures include a direct response to the identified risks, eliminating reversible irregularities and recovering losses.

48. Business risk management

Business risk is a risk of failing to achieve the assumed financial targets, including a risk of losses, resulting from adverse changes in the business environment, wrong decisions made, incorrect implementation of decisions made or failing to take proper action in response to changes occurring in the business environment. It also takes into account a risk of macroeconomic changes (a risk of deterioration in the Bank's financial position due to an adverse effect of changing macroeconomic conditions).

Identification of business risk consists of recognizing and defining actual as well as potential factors which result from the current or contemplated business operations of the Bank and may adversely affect the Bank's financial position, the generation or the amount of the Bank's income and expenses.

Business risk is measured in order to determine the scale of threats connected with the existence of business risk using specified risk measures.

Control of business risk is intended to mitigate the adverse effect of internal and external factors on the financial position of the Bank. The purpose of business risk control is to maintain the Bank's business risk at an acceptable level adapted to the Bank's scale of operations, and its impact on the functioning and financial situation of the Bank in the form of strategic tolerance limits.

The aim of business risk monitoring is to determine whether its level after applying risk controls reflects the admissible level, and diagnosing the necessity of taking management actions and the areas in which it has to be taken.

The strategic business risk tolerance limit is monitored in particular.

Business risk is reported in the form of periodic reports addressed to the ALCO, the Management Board and Supervisory Board of the Bank.

Management actions consist in particular of:

- reviewing and revising the quarterly financial forecasts and financial plan taking into account measures aimed at mitigating the level of business risk in line with the set limits;
- monitoring the level of the strategic business risk tolerance limit.

49. Compliance risk management

Compliance risk is defined at PKO Bank Hipoteczny SA as the risk of legal sanctions, incurring financial losses or the loss of reputation as a result of failure on the part of the Bank, the Bank's employees or entities acting on its behalf to comply with the provisions of the law, internal regulations and the market standards adopted by the Bank.

The aim of compliance risk management is to:

- maintain the Bank's reputation as an institution acting in accordance with the law and the adopted market standards and reliable, fair and honest, among customers, employees, business partners and other market participants;
- prevent the occurrence of financial losses or legal sanctions and cases of loss of reputation on the part of the Bank, which may be a result of a breach of the law, internal regulations or the market standards adopted by the Bank.

The identification and assessment of compliance risk is carried out on the basis of the methodology implemented in the PKO Bank Polski SA Group for identifying and assessment of compliance risk.

Identification of compliance risk covers determining cases of potential non-compliance that may occur in processes and products, divided into compliance risk categories.

The assessment of compliance risk is carried out by way of:

- estimating the potential severity of the consequences of non-compliance cases in the form of:
  - financial losses, particularly in the form of administrative penalties or damages;
  - loss of reputation;
  - other legal sanctions;
- estimating the probability of compliance risk arising.

Based on the compliance risk assessment, by compliance risk category, the overall level of compliance risk for a given process and the related product is determined.

As part of compliance risk control, the Bank protects itself from or mitigates the risk by implementing compliance risk controls and ensuring that they are observed.

The following is covered by compliance risk monitoring:

- the results of compliance risk identification and assessment;
- in the event of non-compliance – the reasons for their arising and the consequences;
- the actions taken by the Bank as part of:
  - compliance risk management;
  - implementing the recommendations issued by internal auditors and external inspectors;

  - bringing the Bank to compliance with new legislation and standards of conduct;
  - implementing of compliance recommendations;
- effectiveness of the controls connected with the mitigation of compliance risk;
- results of compliance tests.

Reporting of information related to compliance risk of the Bank is conducted on a quarterly basis. The recipients of the reports are: the Management Board, the Supervisory Board and the Supervisory Board Audit and Finance Committee. The reports contain, in particular, information about:

- the results of compliance risk identification and assessment;
- the observed cases of non-compliance in the Bank and in the financial sector;
- the most significant changes in the regulatory environment of the Bank, as well as circumstances resulting from the activities of external supervisory and control authorities;
- the results of external inspections carried out within the Bank;
- the most important actions undertaken as part of compliance risk management and the implementation of recommendations arising from external inspections.

The Compliance Team is responsible for managing compliance risk. The activities of the Compliance Team are based on an annual plan approved by the Bank's Supervisory Board. The report on the pursuit of the plan, and supplementary and summary information to the quarterly reports are presented to the Management Board, the Supervisory Board, and the Audit and Finance Committee on an annual basis.

50. REPUTATION RISK MANAGEMENT

Reputation risk is understood as the risk of deterioration of reputation among customers, counterparties, investors, supervisory and control authorities and the public opinion, as a result of business decisions made by the Bank, operating incidents, and issues of non-compliance or other events.

The objective of managing the reputation risk is to protect the Bank's reputation by counteracting reputational losses and limiting the negative impact of image-related events to the Bank's reputation.

Identification of the reputation risks covers the phenomena observed in the Bank's internal processes and its external environment, particularly:

- image-related events;
- factors related to the business environment, i.e. quantitative and qualitative information, including in particular data describing the Bank and its external environment, which have informational value about the existence of reputation risk.

Collecting information about image-related events includes identified negative information content about the Bank, leading to the deterioration of its reputation, such as:

- information disseminated by the mass media;
- information disclosed by the Bank;
- evaluations of auditing firms, analytical institutions and external supervisory and control authorities;
- public protests and public speeches.

An assessment of reputation risk involves evaluating the impact of image-related events on the Bank's reputation, and in particular, quantifying and determining the severity of damages of reputation. The assessment of reputation risk includes the impact, credibility and the opinion-forming potential and scope of the disclosure of an image-related event to the public.

Controlling reputation risk involves determining the risk controls appropriate for the scale and complexity of the Bank's operations, in the form of an internal tolerance limit for reputation risk.

Monitoring reputation risk consists of regular assessments of the values of the reputation risk measures compared with the adopted threshold values.

Information about reputation risk is reported in the form of:

- semi-annual management reports addressed to the Management Board of the Bank;
- information on current events having a material impact on the Bank's reputation, delivered on an ad hoc basis to the President of the Management Board;

Based on the specific level of reputation risk management actions are taken which may cover:

- an analysis of the reasons for the given level of risk occurring;
- assessing the effects of such a level of risk occurring;
- preparation of proposed management actions aimed at reducing the level of reputation risk or grounds for not taking such actions, e.g. in the event of incidental extraordinary events occurring.

51. CAPITAL ADEQUACY AND THE MANAGEMENT OF CAPITAL RISK

Capital adequacy is a process aimed at ensuring that, for a given level of risk tolerance, the level of risk assumed by the Bank associated with the development of its business activities will be covered with capital held within a given time horizon. The process of managing capital adequacy comprises, in particular, compliance with prevailing regulatory standards and the level of risk tolerance determined within the Bank, the process of capital planning, including the policies regarding capital sourcing.

Capital risk is the risk of failing to arrange an adequate level and structure of own funds or the inability to ensure an adequate level of equity given the business risk borne by the Bank, necessary to cover unexpected losses and satisfy regulatory requirements, making it possible for the Bank to continue independent operations. Capital risk includes the risk of excessive leverage, i.e. the risk resulting from vulnerability to threats due to financial leverage or conditional financial leverage, which may necessitate taking involuntary action modifying business plans, including the forced sale of assets which could lead to losses or to the need to adjust the valuation of other assets.

Managing the Bank's capital adequacy covers:

- Pillar I: minimum capital requirements specified in the legislation;
- Pillar II: internal capital, determined by means of the Bank's own models for the risks considered to be material.

The aim of capital adequacy management is to maintain, on a continuous basis, own funds at a level that is adequate to the scale and risk profile of the Bank's activities, with due regard to regulatory requirements.

The following constituted the legal basis of the capital adequacy assessment process as at 30 June 2019:

- Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 ("CRR Regulation");
- The Act of 29 August 1997 "Banking Act";
- The Act of 5 August 2015 on macroprudential supervision over the financial system and crisis management in the financial system ("Macroprudential Act");
- The Regulation of the Minister of Development and Finance of 25 May 2017 in respect of a higher risk weight for exposures secured with mortgages on residential property.

The internal capital adequacy assessment process is described in Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC ("CRD IV"). The CRD Directive has been implemented in Polish law by way of updating the Banking Act.

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

- defining and achieving the capital adequacy targets desired by the Bank;
- identifying and monitoring material risks;
- assessing internal capital to cover the individual risk types and assessing total internal capital;
- establishing internal limits with respect to capital adequacy;
- forecasting, monitoring, and reporting the level and structure of own capital and capital adequacy;
- capital contingency activities.

Capital risk is classified as a risk subject to monitoring. In the first half of 2019 and throughout the Bank's operations, capital adequacy remained at a safe level above the supervisory limits.

At 30 June 2019, the total capital ratio of the Bank amounted to 15.2% (15.2% as at 31 December 2018). Without taking account of the temporary solutions resulting from the implementation of IFRS 9, the total capital ratio of the Bank would have amounted to 15.1% (15.0% as at 31 December 2018).

(IN PLN MILLION)

51.1 Own funds for the purpose of capital adequacy

The Bank's own funds for capital adequacy purposes have been calculated in accordance with the Banking Act and the CRR with implementing legislation.

The Bank's own funds consist entirely of common equity Tier 1 capital (CET 1). In determining its own funds, the Bank makes use of the transitional provisions following from the implementation of IFRS 9.

BANK'S OWN FUNDS	30.06.2019	31.12.2018
Share capital	1,526,500	1,295,000
Supplementary capital	146,735	54,932
Retained earnings	-	(11,787)
Net profit for the period	30,629	85,849
Accumulated other comprehensive income - cash flow hedges	149,311	59,462
Accumulated other comprehensive income - financial assets measured at fair value through other comprehensive income	2,722	4,427
Equity	**1,855,897**	**1,487,883**
Equity adjustments	(169,987)	(94,036)
Net profit for the period	(30,629)	(85,849)
Current profit, included by permission from the PFSA	-	42,588
Accumulated other comprehensive income - cash flow hedges	(149,311)	(59,462)
Intangible assets	(3,241)	(4,165)
Adjustment to assets measured at fair value (AVA)	(1,275)	(949)
Adjustment relating to the transitional period for IFRS 9 implementation	14,469	13,801
Own funds	**1,685,910**	**1,393,847**

At 30 June 2019, the Bank's own funds Tier I common equity capital and Tier I capital, without accounting for transitional solutions following from the implementation of IFRS 9, would have amounted to PLN 1,671,441 thousand and to PLN 1,380,046 thousand as at 31 December 2018.

51.2 Capital buffers

The CRD Directive, in particular the provisions on regulatory capital buffers, has been implemented into national law by adopting the Macroprudential Act and amending the Banking Act. The Macroprudential Act defines capital buffers that are applicable to banks with effect from January 2016.

Due to the fact that 1 January 2018 marked the effective date for the Regulation of the Minister of Development and Finance of 1 September 2017 in respect of the systemic risk buffer (Journal of Laws of 2017, item 1776), in 2019, the banks are required to maintain the equity ratios at the following levels:

- Total capital ratio (TCR) = 8% + an add-on + the combined buffer requirement;
- Tier 1 capital ratio (T1) = 6% + 75%*add-on + the combined buffer requirement;
- Common Equity Tier 1 capital ratio (CET1) = 4.5% + 56%*add-on + the combined buffer requirement,

where the add-on means the requirement specified in Article 138 (1) (2a) of the Banking Act and the combined buffer requirement is the sum total of the mandatory buffers, i.e.

- the conservation buffer of 2.5%;
- the counter-cyclical buffer of 0% for loan exposures on the territory of Poland;
- the buffer of other systemically important institutions set by the PFSA on a case by case basis;
- the systemic risk buffer of 3%.

PKO Bank Hipoteczny SA has not been recognized as another systemically important institution by the PFSA and therefore it is not required to satisfy the applicable additional capital requirements.

The Bank is also not required to satisfy the requirements specified in Article 138 (1) (2a) of the Banking Act (add-on).

(IN PLN MILLION)

51.3 Financial leverage

The risk of excessive leverage is defined as the risk resulting from vulnerability to risks because of financial leverage or conditional financial leverage, which may necessitate taking involuntary action modifying business plans, including forced sale of assets which could result in losses or result in the need to adjust the valuation of other assets.

Financial leverage is defined as the relative size of a Bank's assets, contingent liabilities relating to payments or provision or delivery of collateral, including obligations from received funding, liabilities drawn, derivatives or repurchase agreements, but excluding liabilities which can only be enforced during the liquidation of a Bank, compared to the Bank's own funds.

The Bank calculates financial leverage according to the CRR.

The financial leverage ratio is monitored on a monthly basis, whereas the Bank recognizes a ratio in excess of 5% to be safe and not requiring further action.

LEVERAGE	30.06.2019	31.12.2018
Leverage ratio (LR)	6.5%	6.3%

As at 30 June 2019 and as at 31 December 2018, the Bank's financial leverage ratio was above the 3% level recommended for banks by the Basel Committee.

As at 30 June 2019, the leverage ratio, without taking account of the transitional solutions resulting from the implementation of IFRS 9, would have amounted to 6.4%, whereas it was 6.2% as at 31 December 2018.

51.4 Requirements regarding own funds (Pillar I)

In accordance with the CRR, the Bank calculates requirements in respect of own funds for the following risk types:

- credit risk – according to the standardized approach;
- credit valuation adjustment (CVA) risk – according to the standardized approach;
- settlement and delivery risk – according to the standardized approach;
- operational risk – using the Basic Indicator Approach (BIA);
- market risk (foreign exchange risk only) – according to basic methods.

At 30 June 2019 and as at 31 December 2018, the own fund requirements in respect of the risk of credit valuation adjustment, settlement and delivery, and market risk were nil, therefore, the total requirement in respect of own funds comprised the requirements in respect of credit and operational risk.

OWN FUNDS REQUIREMENTS	30.06.2019	31.12.2018
Credit risk	862,228	718,961
Operational risk	22,695	15,655
Total own funds requirement	**884,923**	**734,616**
Common Equity Tier 1 capital ratio (CET1)	15.2%	15.2%
Tier 1 capital ratio (T1)	15.2%	15.2%
Total capital ratio (TCR)	**15.2%**	**15.2%**

(IN PLN MILLION)

EVENTS AFTER THE END OF THE REPORTING PERIOD

52. EVENTS AFTER THE END OF THE REPORTING PERIOD

In the period from 1 July 2019 to the date of signing these financial statements, PKO Bank Hipoteczny SA acquired another portfolio of receivables of residential mortgage housing loans amounting to PLN 225,911 thousand under the Framework Receivables Sale Agreement concluded on 17 November 2015 with PKO Bank Polski SA.

On 10 July 2019, PKO Bank Hipoteczny SA concluded with PKO Bank Polski SA a current account revolving credit agreement with a limit of PLN 1 billion for a period of 3 years. The loan is earmarked for servicing the redemption of bonds issued under the Non-Public Programme. The Bank acquired the funding due to the duty to register and settle all non-public issues of securities through the National Depository of Securities binding as of 1 July 2019. In effect it is impossible to redeem and receive funds from a new issue (roll-over) on the same day.

On 10 July 2019 PKO Bank Hipoteczny SA issued bonds of PLN 161 500 thousand to be redeemed after six months under the Public Bond Issue Programme as part of the underwriting services provided by Dom Maklerski PKO Banku Polskiego SA. Furthermore, on 11 July 2019 bonds primarily addressed to retail investors with a value of PLN 50 million and two-year period to redemption were issued under the programme.

Signatures of all Members of the Bank's Management Board

08.08.2019	Paulina Strugała	President of the Management Board	*Signed on the Polish original* .... (signature)
08.08.2019	Piotr Kochanek	Vice-President of the Management Board	*Signed on the Polish original* .... (signature)
08.08.2019	Agnieszka Krawczyk	Vice-President of the Management Board	*Signed on the Polish original* .... (signature)

Signature of the person in charge of maintaining the accounting records.

08.08.2019

Tomasz Rynkowski
Director, the Bank's Chief Accountant

Signed on the Polish original

....

(signature)