Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością sp. k.
Rondo ONZ 1
00-124 Warszawa

+48 (0) 22 557 70 00
+48 (0) 22 557 70 01
www.ey.com/pl

INDEPENDENT AUDITOR'S REPORT ON THE AUDIT

To the Shareholders Meeting and Supervisory Board of mBank Hipoteczny S.A.

Audit report on the annual financial statements

Opinion

We have audited the annual financial statements of mBank Hipoteczny (the 'Bank') located in Warsaw at Armii Ludowej 26, containing: the income statement and the statement of comprehensive income for the period form 1 January 2018 to 31 December 2018, the statement of financial position as at 31 December 2018, the statement of changes in equity and the statement of cash flows for the period from 1 January 2018 to 31 December 2018 and the explanatory notes to the standalone financial statements (the 'financial statements').

In our opinion, the financial statements:

- give a true and fair view of the financial position of the Bank as at 31 December 2018 and its financial performance and its cash flows for the period from 1 January 2018 to 31 December 2018 in accordance with required applicable rules of International Financial Reporting Standards approved by the European Union and the adopted accounting policies,

- are in respect of the form and content in accordance with legal regulations governing the Bank and the Bank's Statute,

- have been prepared based on properly maintained accounting records, in accordance with chapter 2 of the Accounting Act dated 29 September 1994 (the 'Accounting Act').

The opinion is consistent with the additional report to the Audit Committee issued on 26 March 2019.

Basis for opinion

We conducted our audit in accordance with the International Standards on Auditing in the version adopted as the National Auditing Standards by the National Council of Statutory Auditors ("NAS") and pursuant to the Act of 11 May 2017 on Statutory Auditors, Audit Firms and Public Oversight (the 'Act on Statutory Auditors') and the Regulation (EU) No. 537/2014 of the European Parliament and of the Council of 16 April 2014 on specific requirements regarding statutory audit of public-interest entities and repealing Commission Decision 2005/909/EC (the 'Regulation 537/2014'). Our responsibilities under those standards are further described in the *'Auditor's responsibilities for the audit of the financial statements'* section of our report.

We are independent of the Bank in accordance with the Code of ethics for professional accountants, published by the International Federation of Accountants (the 'Code of ethics'), adopted by the National Council of Statutory Auditors and other ethical responsibilities in accordance with required applicable rules of the audit of financial statements in Poland. We have fulfilled our other ethical responsibilities in accordance with these requirements and the Code of ethics. While conducting the audit, the key certified auditor and the audit firm remained independent of the Bank in accordance with the independence requirements set out in the Act on Statutory Auditors and the Regulation 537/2014.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period. They include the most significant assessed risks of material misstatement, including the assessed risks of material misstatement due to fraud. These matters were addressed in the context of our audit of the financial statements as a whole, and in forming our opinion thereon, and we have summarized our reaction to these risks and in cases where we deemed it necessary, we presented the most important observations related to these types of risks. We do not provide a separate opinion on these matters.

Key audit matter	How the matter was addressed in our audit
Mortgage loans and advances to customers as at December 31, 2018 amounted to PLN 11,139 million and accounted for the most significant portion of total assets. The amount of PLN 11,139 million included the gross book value of loans and advances to customers in the amount of PLN 11,021 million, provisions for expected credit losses to these exposures in the amount of PLN 90 million (including group model provisions of PLN 21 million and individual provisions of PLN 69 million), and book value of loans and advances to clients valued at fair value through profit and loss amounting to PLN 208 million. In addition, receivables from mortgage loans constituted the basis for the issue of covered bonds, the total value of which amounted to PLN 7 870 million as at December 31, 2018. Determining the amount and the moment of recognizing provision for expected credit losses requires significant judgment and significant and complex estimates of the Management Board regarding, among others, assumptions and judgments built into statistical credit loss models such as: • assessment of significant credit risk growth and definition of default, as well as probability of such an event occurring, • consideration of future information on the calculation of expected credit losses, • calculation of the loss given default parameter and the recovery rates used in the calculation of impairment losses.	As part of the audit procedures, we have carried out, among others, the following procedures for the first application of IFRS 9 as at January 1, 2018: • We analyzed the assumptions adopted by the Bank in the new model in the context of the assumptions applicable in the model according to the International Accounting Standard 39 Financial Instruments: Recognition and Measurement ('IAS 39'), • We analyzed the methodologies of creating collective provisions for expected credit losses in terms of their compliance with the requirements of IFRS 9 as of the date of the first application and we recalculated the provisions for expected credit losses, • We conducted analytical procedures regarding the structure and level of provisioning for expected losses for loans and advances to customers under IFRS 9 as compared to impairment losses under IAS 39 to identify potential inconsistencies in the implementation of IFRS 9. In addition, we have conducted the following audit procedures in the area of impairment provisions for expected credit losses created in the financial year ended December 31, 2018:

The estimates of the Bank's Management Board for the individual method concern, among others: • the value of real estate collateral for loans and advances to clients, including accepted market prices of real estate, rates and levels of renting space and capitalization rates used to determine the value of real estate. In addition, the Bank applied on January 1, 2018 the requirements of International Financial Reporting Standard 9: ‚Financial Instruments' (hereinafter ‚IFRS 9') in the area of impairment of loans and advances to customers. Due to the significance of loans and advances to clients, the receivables of which constitute the basis for the issue of mortgage bonds by the Bank, in relation to total assets, the significant role and complexity of the Bank's Management Board judgments and estimates and the complexity of these judgments and estimates regarding the expected credit losses described above and in connection with the first application of IFRS 9 as at January 1, 2018, we consider loan loss provisions for mortgage loans as a key audit matter.	• We documented our understanding of the Bank's policies and procedures related to the estimation of expected losses of loans and advances to clients, as well as the credit risk management policies in the Bank, and analyzed the design and functioning of control mechanisms in the areas of identification and measurement of credit losses of loans and advances to clients in the reporting period implemented by the Bank. • Tests of control mechanisms performed as a part of audit procedures included the process of granting loans, the process of monitoring the economic and financial situation of customers, valuation of collateral and identification of premises for impairment, as well as the process of calculating write-offs for expected losses of loans and advances to customers • We reconciled a database of loans and advances to customers with accounting records to confirm the completeness of the recognition of loans and advances to customers, being the basis for the calculation of provisions for expected credit losses, as well as the value of these provisions.

Information on the methodology for the valuation of loans and advances to customers, as well as the related judgments and estimates and the impact of the implementation of IFRS 9 as of January 1, 2018 are described in explanatory notes 2.6., 2.8., 2.25. and 5 of the attached financial statements, and detailed information on the value of loans and advances to clients and the value of provisions for expected credit losses are described in explanatory notes 22 and 24 of the attached financial statements.	• We analyzed changes in methodologies and models of creating provisions for expected credit losses in the financial year ended December 31, 2018. We assessed the models, assumptions and completeness of data used by the Bank for the purposes of creating impairment allowances, including assumptions underlying the basis for determining the value of real estate as collateral for loans and advances to clients, the probability of default and loss as a result of default, as well as the results of the Bank's tests of credit risk parameters (so-called 'backtesting'). • On a selected sample, we analyzed loan exposures assessed individually by the Bank. For selected impaired exposures, we assessed the reasonableness of the recovery amount estimated by the Management Board, including the assumptions regarding recoverable amount of collateral and the dates of expected future cash flows, in particular due to repayments and collateral execution, based on available financial and market data and using the work of internal specialists in the area of real estate valuation to evaluate the recoverable value of collateral. For selected exposures without impairment, we analyzed the economic and financial situation of borrowers and fulfillment of the terms of loan agreements in order to identify potential impairment triggers.

	• We also conducted analytical procedures regarding the structure and dynamics of changes in the balance of loans and advances to customers reflecting the quality of the loan portfolio in the light of the impairment provisions for expected credit losses for loans and advances to customers aimed at identifying portfolios of loans and advances to customers with underestimated provisions. In addition, we have carried out an analysis of the premises of a significant increase in credit risk and classification into risk categories (‘stages’), so-called ‘staging’. • Regarding IT systems, in which both the credit risk parameters and the calculation of the provisions for expected credit losses were calculated in the reporting period, our analysis of control mechanisms effectiveness was carried out in cooperation with specialists in the field of IT systems. In addition, we have assessed the disclosures regarding expected credit losses for loans and advances to customers valued at amortized cost included in the financial statements in terms of their completeness and compliance with International Financial Reporting Standards (‘IFRS’).

Other matters

The financial statements for the previous financial year (i.e. from 1 January 2017 to 31 December 2017) were audited by an auditor acting on behalf of another auditing company that issued an unqualified opinion on this report on these financial statements on 2 March 2018.

Responsibilities of the Bank's Management the Supervisory Board for the financial statements

The Bank's Management is responsible for the preparation, based on properly maintained accounting records, the financial statements that give a true and fair view of the financial position and the financial performance in accordance with required applicable rules of International Financial Reporting Standards approved by the European Union, the adopted accounting policies, other applicable laws, as well as the Bank's Statute, and is also responsible for such internal control as determined is necessary to enable the preparation of the financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, The Bank's Management is responsible for assessing the Bank's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless The Bank's Management either intends to liquidate the Bank or to cease operations, or has no realistic alternative but to do so.

The Bank's Management and the members of the Bank's Supervisory Board are required to ensure that the financial statements meet the requirements of the Accounting Act. The members of the Bank's Supervisory Board are responsible for overseeing the Bank's financial reporting process.

Auditor's responsibility for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement due to fraud or error, and to issue an independent auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not guarantee that an audit conducted in accordance with NAS will always detect material misstatement when it exists. Misstatements may arise as a result of fraud or error and are considered material if it can reasonably be expected that individually or in the aggregate, they could influence the economic decisions of the users taken on the basis of these financial statements.

In accordance with International Auditing Standard 320, section 5, the concept of materiality is applied by the auditor both in planning and performing the audit, and in evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements and in forming the opinion in the auditor's report. Hence all auditor's assertions and statements contained in the auditor's report are made with the contemplation of the qualitative and quantitative materiality levels established in accordance with auditing standards and auditor's professional judgment.

The scope of the audit does not include assurance on the future profitability of the Bank nor effectiveness of conducting business matters now and in the future by the Bank's Management.

Throughout the audit in accordance with NAS, we exercise professional judgment and maintain professional skepticism and we also:

- identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations or override of internal control,

- obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Bank's internal control,

- evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Bank's Management,

- conclude on the appropriateness of the Bank's Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Bank's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our independent auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our independent auditor's report, however, future events or conditions may cause the Bank to cease to continue as a going concern,

- evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and communicate to them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated to the Audit Committee, we determine those matters that were of most significance in the audit of the financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Other information, including the Directors' Report

The other information comprises the Directors' Report for the period from 1 January 2018 to 31 December 2018 and the representation on the corporate governance, mentioned in article 49b, section 1 of the Accounting Act as a separate element of the Directors' Report (jointly 'Other Information').

Responsibilities of the Bank's Management and the Supervisory Board

The Bank's Management is responsible for the preparation the Other Information in accordance with the law.

The Bank's Management and members of the Bank's Supervisory Board are required to ensure that the Directors' Report (with separate elements) meets the requirements of the Accounting Act.

Auditor's responsibility

Our opinion on the financial statements does not include the Other Information. In connection with our audit of the financial statements, our responsibility is to read the Other Information and, in doing so, consider whether it is materially inconsistent with the financial statements or our knowledge obtained during the audit or otherwise appears to be materially misstated. If, based on the work we have performed, we conclude that there is a material misstatement of this Other Information, we are required to report that fact in our independent auditor's report. Our responsibility in accordance with the Act on Statutory Auditors is also to issue an opinion on whether the Directors' Report was prepared in accordance with relevant laws and that it is consistent with the information contained in the financial statements.

In addition, we are required to issue an opinion on whether the Bank has included the required information in the representation on application of corporate governance.

Opinion on the Directors' Report

Based on the work performed during our audit, in our opinion, the Directors' Report:

- has been prepared in accordance with the article 49 of the Accounting Act and paragraph 70 of the Decree of the Minister of Finance dated 29 March 2018 on current and periodic information published by issuers of securities and conditions for recognition as equivalent the information required by laws of non-EU member states (the 'Decree on current and periodic information') and article 111a, section 1-2 of the Banking Law Act dated 29 August 1997 (the 'Banking Law Act')

- is consistent with the information contained in the financial statements.

Moreover, based on our knowledge of the Bank and its environment obtained during our audit, we have not identified material misstatements in the Directors' Report.

Opinion on the corporate governance application representation

In our opinion, in the representation on application of corporate governance, the Bank has included information stipulated in paragraph 70, section 6, point 5 of the Decree on current and periodic information.

Moreover, in our opinion, the information stipulated in paragraph 70, section 6, point 5 letter c-f, h and i of the Decree included in the representation on application of corporate governance is in accordance with applicable laws and information included in the financial statements.

Report on other legal and regulatory requirements

Banks are obliged to comply with the prudential requirements specified in the Banking Law, resolutions of the National Bank of Poland, resolutions of the PFSA, recommendations of the PFSA and Regulation (EU) No. 575/2013 of the European Parliament and of the EU Council of 26 June 2013 on prudential requirements for credit institutions and investment firms, regarding prudential requirements for credit institutions and investment firms, amending Regulation (EU) No 648/2012 (CRR) and Commission Decisions based on that Regulation concerning:

- concentration of credit risks,
- concentration of equity shares,
- classification of loans and guarantees granted into risk groups,
- liquidity,
- obligatory reserve requirements,
- capital adequacy.

The Bank's Management Board is responsible for compliance with prudential regulations, including in particular, adequate calculation of the capital ratio. Our responsibility was, based on the conducted audit, to provide information whether the Bank complied with the above described prudential regulations. Our responsibility was not to express an opinion on compliance with these regulations.

As part of the audit of the financial statements we have performed the procedures with regards to capital ratios and we have not identified any discrepancies in their calculation which would have a material impact on financial statement as a whole. Therefore, we inform that the Bank's Management Board has correctly calculated the capital requirements in compliance with the rules described above.

Representation on the provision of non-audit services

To the best of our knowledge and belief, we represent that services other than audits of the financial statements, which we have provided to the Bank and its subsidiaries, are compliant with the laws and regulations applicable in Poland, and that we have not provided non-audit services, which are prohibited based on article 5 item 1 of Regulation 537/2014 and article 136 of the Act on Statutory Auditors. The non-audit services, which we have provided to the Bank and its subsidiaries in the audited period, have been disclosed in the financial statements of the Bank.

Building a better working world

Appointment of the audit firm

We were appointed for the audit of the Bank's financial statements initially based on the resolution of the Supervisory Board from 2 March 2018. We are auditing the financial statements of the Bank for the first time.

Warsaw, 26 March 2019

Key Certified Auditor

Maja Mandela
certified auditor
no in the register: 11942

on behalf of:
Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością sp. k.
Rondo ONZ 1, 00-124 Warsaw
no on the audit firms list: 130