Bank Pekao

Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period from 1 January 2018 to 30 June 2018

Warsaw, August 2018

This document is a free translation of the Polish original. Terminology current in Anglo-Saxon countries has been used where practicable for the purposes of this translation in order to aid understanding. The binding Polish original should be referred to in matters of interpretation.

Table of content

Consolidated income statement

(in PLN thousand)

	NOTE	II QUARTER 2018 PERIOD FROM 01.04.2018 TO 30.06.2018	I HALF 2018 PERIOD FROM 01.01.2018 TO 30.06.2018	II QUARTER 2017 PERIOD FROM 01.04.2017 TO 30.06.2017	I HALF 2017 PERIOD FRO7M 01.01.2017 TO 30.06.2017
Interest income	9	**1 515 910**	**2 994 474**	**1 392 566**	**2 767 533**
Financial assets measured at amortised cost		1 299 482	2 559 363	X	X
Financial assets measured at fair value through other comprehensive income		176 523	365 174	X	X
Financial assets measured at fair value through other profit or loss		39 905	69 937	X	X
Interest expense	9	**(280 373)**	**(553 247)**	**(256 384)**	**(516 324)**
Net interest income		**1 235 537**	**2 441 227**	**1 136 182**	**2 251 209**
Fee and commission income	10	707 067	1 382 495	659 104	1 301 078
Fee and commission expense	10	(89 794)	(177 168)	(76 818)	(145 310)
Net fee and commission income		**617 273**	**1 205 327**	**582 286**	**1 155 768**
Dividend income	11	**19 623**	**19 780**	**19 269**	**19 418**
Result on financial assets and liabilities measured at fair value through profit or loss	12	**16 539**	**35 664**	**858**	**8 873**
Result on fair value hedge accounting	30	**662**	**1 999**	**1 334**	**3 047**
Result on derecognition of financial assets and liabilities not measured at fair value through profit or loss	13	**27 245**	**51 077**	**X**	**X**
Gains (losses) on disposal of financial assets and liabilities	14	**X**	**X**	**5 118**	**5 942**
Operating income		**1 916 879**	**3 755 074**	**1 745 047**	**3 444 257**
Net impairment losses on financial assets and off-balance sheet commitments	15	**(123 932)**	**(250 893)**	**(114 848)**	**(229 974)**
Net result on financial activity		**1 792 947**	**3 504 181**	**1 630 199**	**3 214 283**
Administrative expenses	16	**(980 579)**	**(2 056 893)**	**(865 632)**	**(1 901 992)**
Personnel expenses		(554 827)	(1 055 173)	(482 349)	(952 318)
Other administrative expenses		(425 752)	(1 001 720)	(383 283)	(949 674)
Depreciation and amortization	17	**(89 893)**	**(177 673)**	**(85 225)**	**(169 567)**
Net result on other provisions		**(13 768)**	**(14 067)**	**(8 467)**	**(14 002)**
Net other operating income and expenses	18	**12 095**	**25 720**	**12 153**	**47 892**
Operating costs		**(1 072 145)**	**(2 222 913)**	**(947 171)**	**(2 037 669)**
Gains (losses) on subsidiaries and associates	19	**-**	**-**	**10 444**	**20 554**
Gains (losses) on disposal of property, plant and equipment and intangible assets	20	**(6 863)**	**(3 940)**	**(59)**	**66**
Profit before income tax		**713 939**	**1 277 328**	**693 413**	**1 197 234**
Income tax expense	21	**(173 962)**	**(345 026)**	**(158 214)**	**(312 243)**
Net profit		**539 977**	**932 302**	**535 199**	**884 991**
1. Attributable to equity holders of the Bank		539 815	932 140	535 069	884 778
2. Attributable to non-controlling interests		162	162	130	213
Earnings per share (in PLN per share)					
basic for the period	22	2.06	3.55	2.04	3.37
diluted for the period	22	2.06	3.55	2.04	3.37

Notes to the financial statements presented on pages 11 - 124 constitute an integral part of the consolidated financial statements.

Consolidated statement of comprehensive income

(in PLN thousand)

	NOTE	II QUARTER 2018 PERIOD FROM 01.04.2018 TO 30.06.2018	I HALF 2018 PERIOD FROM 01.01.2018 TO 30.06.2018	II QUARTER 2017 PERIOD FROM 01.04.2017 TO 30.06.2017	I HALF 2017 PERIOD FROM 01.01.2017 TO 30.06.2017
Net profit		**539 977**	**932 302**	**535 199**	**884 991**
1. Attributable to equity holders of the Bank		539 815	932 140	535 069	884 778
2. Attributable to non-controlling interests		162	162	130	213
Other comprehensive income					
Item that are or may be reclassified subsequently to profit or loss:					
Change in fair value of financial assets measured at fair value through other comprehensive income		(51 033)	58 259	X	X
Change in fair value of available-for-sale financial assets		X	X	94 566	266 965
Change in fair value of cash flow hedges	30	(3 531)	(20 854)	(27 607)	(32 098)
Tax on items that are or may be reclassified subsequently to profit or loss	21	10 367	(7 107)	(12 721)	(44 624)
Items that will never be reclassified to profit or loss:					
Investment in equity instruments designated at fair value through other comprehensive income		(13 940)	(19 371)	X	X
Remeasurements of the defined benefit liabilities		-	-	-	-
Share in remeasurements of the defined benefit liabilities of associates		-	-	-	-
Tax on items that will never be reclassified to profit or loss	21	2 649	3 681	-	-
Other comprehensive income (net of tax)		**(55 488)**	**14 608**	**54 238**	**190 243**
Total comprehensive income		**484 489**	**946 910**	**589 437**	**1 075 234**
1. Attributable to equity holders of the Bank		484 327	946 748	589 307	1 075 021
2. Attributable to non-controlling interests		162	162	130	213

Notes to the financial statements presented on pages 11 - 124 constitute an integral part of the consolidated financial statements.

Consolidated statement of financial position

(in PLN thousand)

	NOTE	30.06.2018	31.12.2017
ASSETS			
Cash and due from Central Bank	24	8 014 221	5 236 318
Loans and advances to banks	25	3 480 658	2 627 327
Financial assets held for trading	26	1 327 945	1 730 416
Derivative financial instruments (held for trading)	27	1 236 083	1 349 047
Loans and advances to customers	28	117 839 500	127 949 307
1. Measured at amortised cost		116 301 044	X
2. Measured at fair value through profit or loss		335 242	X
3. Measured at fair value through other comprehensive income		1 203 214	X
Receivables from finance leases	29	4 671 461	4 351 352
Hedging instruments	30	144 476	259 396
Investments (placement) securities	31	41 712 770	36 905 822
1. Measured at fair value through profit or loss		65 386	X
2. Designated at fair value through profit or loss		-	-
3. Measured at fair value through other comprehensive income (debt securities)		30 755 181	X
4. Designated at fair value through other comprehensive income (equity instruments)		244 337	X
5. Measured at amortised cost		10 647 866	X
6. Available for sale		X	33 424 031
7. Held to maturity		X	3 481 791
Assets held for sale	32	48 207	65 565
Investments in associates		-	-
Intangible assets	33	1 491 109	1 525 645
Property, plant and equipment	34	1 366 616	1 425 469
Investment properties		11 315	22 167
Income tax assets		1 139 269	960 754
1. Current tax assets		323	9 959
2. Deferred tax assets		1 138 946	950 795
Other assets		1 019 869	1 056 985
TOTAL ASSETS		**183 503 499**	**185 465 570**
EQUITY AND LIABILITIES			
Liabilities			
Amounts due to Central Bank	24	6 028	6 079
Amounts due to other banks	36	5 458 120	4 981 291
Financial liabilities held for trading	26	425 903	469 448
Derivative financial instruments (held for trading)	27	1 450 668	2 030 103
Amounts due to customers	37	142 933 248	146 186 268
Hedging instruments	30	1 012 635	862 331
Debt securities issued	38	3 882 304	2 771 399
Subordinated liabilities	39	1 257 013	1 257 188
Income tax liabilities		161 946	237 885
1. Current tax liabilities		128 750	200 201
2. Deferred tax liabilities		33 196	37 684
Provisions	40	659 685	602 622
Other liabilities		4 804 494	2 793 142
TOTAL LIABILITIES		**162 052 044**	**162 197 756**
Equity			
Share capital		262 470	262 470
Other capital and reserves		20 855 492	20 561 177
Retained earnings and net profit for the period		322 483	2 444 167
Total equity attributable to equity holders of the Bank		**21 440 445**	**23 267 814**
Non-controlling interests		11 010	-
TOTAL EQUITY		**21 451 455**	**23 267 814**
TOTAL LIABILITIES AND EQUITY		**183 503 499**	**185 465 570**

Notes to the financial statements presented on pages 11 - 124 constitute an integral part of the consolidated financial statements.

Consolidated statement of changes in equity

(in PLN thousand)

For the period from 1 January 2018 to 30 June 2018

	EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK									NON - CONTROLLING INTERESTS	TOTAL EQUITY
	SHARE CAPITAL	OTHER CAPITAL AND RESERVES						RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK		
		TOTAL OTHER CAPITAL AND RESERVES	SHARE PREMIUM	GENERAL BANKING RISK FUND	OTHER RESERVE CAPITAL	REVALUATIO N RESERVES	OTHER				
Equity as at 1.01.2018	**262 470**	**20 561 177**	**9 137 221**	**1 982 459**	**9 099 775**	**(56 528)**	**398 250**	**2 444 167**	**23 267 814**	**-**	**23 267 814**
Initial application of IFRS 9	-	236 085	-	-	-	236 085	-	(956 518)	(720 433)	-	(720 433)
Equity as at 1.01.2018 - restated	**262 470**	**20 797 262**	**9 137 221**	**1 982 459**	**9 099 775**	**179 557**	**398 250**	**1 487 649**	**22 547 381**	**-**	**22 547 381**
Management options	-	-	-	-	-	-	-	-	-	-	-
Options exercised (share issue)	-	-	-	-	-	-	-	-	-	-	-
Revaluation of management options	-	-	-	-	-	-	-	-	-	-	-
Comprehensive income	**-**	**15 448**	**-**	**-**	**840**	**14 608**	**-**	**932 140**	**947 588**	**162**	**947 750**
Remeasurements of the defined benefit liabilities (net of tax)	-	-	-	-	-	-	-	-	-	-	-
Revaluation of debt financial instruments measured at fair value through other comprehensive income (net of tax)	-	47 189	-	-	-	47 189	-	-	47 189	-	47 189
Revaluation or sale of investments in equity instruments designated at fair value through other comprehensive income (net of tax)	-	(14 850)	-	-	840	(15 690)	-	-	(14 850)	-	(14 850)
Revaluation of hedging financial instruments (net of tax)	-	(16 891)	-	-	-	(16 891)	-	-	(16 891)	-	(16 891)
Net profit for the period	-	-	-	-	-	-	-	932 140	932 140	162	932 302
Appropriation of retained earnings	**-**	**23 793**	**-**	**-**	**15 583**	**-**	**8 210**	**(2 097 306)**	**(2 073 513)**	**-**	**(2 073 513)**
Dividend paid	-	-	-	-	-	-	-	(2 073 513)	(2 073 513)	-	(2 073 513)
Profit appropriation to other reserves including consolidation adjustments	-	23 793	-	-	15 583	-	8 210	(23 793)	-	-	-
Other	**-**	**18 989**	**-**	**-**	**20 664**	**(1 675)**	**-**	**-**	**18 989**	**10 848**	**29 837**
Changes in non-controlling interests	-	(3 491)	-	-	(3 513)	22	-	-	(3 491)	10 848	7 357
Transfer of management of Pekao OFE and DFE Pekao funds	-	22 680	-	-	22 680	-	-	-	22 680	-	22 680
Other	-	(200)	-	-	1 497	(1 697)	-	-	(200)	-	(200)
Equity as at 30.06.2018	**262 470**	**20 855 492**	**9 137 221**	**1 982 459**	**9 136 862**	**192 490**	**406 460**	**322 483**	**21 440 445**	**11 010**	**21 451 455**

Notes to the financial statements presented on pages 11 - 124 constitute an integral part of the consolidated financial statements.

Consolidated statement of changes in equity (cont.)

(in PLN thousand)

For the period from 1 January 2017 to 31 December 2017

	EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK									NON - CONTROLLING INTERESTS	TOTAL EQUITY
	SHARE CAPITAL	OTHER CAPITAL AND RESERVES						RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK		
		TOTAL OTHER CAPITAL AND RESERVES	SHARE PREMIUM	GENERAL BANKING RISK FUND	OTHER RESERVE CAPITAL	REVALUATION RESERVES	OTHER				
Equity as at 1.01.2017	**262 470**	**20 375 527**	**9 137 221**	**1 982 324**	**9 092 735**	**(223 394)**	**386 641**	**2 259 022**	**22 897 019**	**14 924**	**22 911 943**
Management options	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Options exercised (share issue)	-	-	-	-	-	-	-	-	-	-	-
Revaluation of management share options	-	-	-	-	-	-	-	-	-	-	-
Comprehensive income	**-**	**166 866**	**-**	**-**	**-**	**166 866**	**-**	**2 475 129**	**2 641 995**	**579**	**2 642 574**
Remeasurements of the defined benefit liabilities (net of tax)	-	6 932	-	-	-	6 932	-	-	6 932	-	6 932
Revaluation of available-for-sale investments (net of tax)	-	186 780	-	-	-	186 780	-	-	186 780	-	186 780
Revaluation of hedging financial instruments (net of tax)	-	(26 846)	-	-	-	(26 846)	-	-	(26 846)	-	(26 846)
Net profit for the period	-	-	-	-	-	-	-	2 475 129	2 475 129	579	2 475 708
Appropriation of retained earnings	**-**	**11 744**	**-**	**135**	**-**	**-**	**11 609**	**(2 289 984)**	**(2 278 240)**	**-**	**(2 278 240)**
Dividend paid	-	-	-	-	-	-	-	(2 278 240)	(2 278 240)	-	(2 278 240)
Profit appropriation to other reserves including consolidation adjustments	-	11 744	-	135	-	-	11 609	(11 744)	-	-	-
Other	**-**	**7 040**	**-**	**-**	**7 040**	**-**	**-**	**-**	**7 040**	**(15 503)**	**(8 463)**
Acquisition of non - controlling interests	-	7 040	-	-	7 040	-	-	-	7 040	(15 503)	(8 463)
Equity as at 31.12.2017	**262 470**	**20 561 177**	**9 137 221**	**1 982 459**	**9 099 775**	**(56 528)**	**398 250**	**2 444 167**	**23 267 814**	**-**	**23 267 814**

Notes to the financial statements presented on pages 11 - 124 constitute an integral part of the consolidated financial statements.

Consolidated statement of changes in equity (cont.)

(in PLN thousand)

For the period from 1 January 2017 to 30 June 2017

	EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK										
		OTHER CAPITAL AND RESERVES									
	SHARE CAPITAL	TOTAL OTHER CAPITAL AND RESERVES	SHARE PREMIUM	GENERAL BANKING RISK FUND	OTHER RESERVE CAPITAL	REVALUATION RESERVES	OTHER	RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK	NON - CONTROLLING INTERESTS	TOTAL EQUITY
Equity as at 1.01.2017	**262 470**	**20 375 527**	**9 137 221**	**1 982 324**	**9 092 735**	**(223 394)**	**386 641**	**2 259 022**	**22 897 019**	**14 924**	**22 911 943**
Management options	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Options exercised (share issue)	-	-	-	-	-	-	-	-	-	-	-
Revaluation of management options	-	-	-	-	-	-	-	-	-	-	-
Comprehensive income	**-**	**190 243**	**-**	**-**	**-**	**190 243**	**-**	**884 778**	**1 075 021**	**213**	**1 075 234**
Remeasurements of the defined benefit liabilities (net of tax)	-	-	-	-	-	-	-	-	-	-	-
Revaluation of available-for-sale investments (net of tax)	-	216 242	-	-	-	216 242	-	-	216 242	-	216 242
Revaluation of hedging financial instruments (net of tax)	-	(25 999)	-	-	-	(25 999)	-	-	(25 999)	-	(25 999)
Net profit for the period	-	-	-	-	-	-	-	884 778	884 778	213	884 991
Appropriation of retained earnings	**-**	**11 744**	**-**	**135**	**-**	**-**	**11 609**	**(2 289 984)**	**(2 278 240)**	**-**	**(2 278 240)**
Dividend paid	-	-	-	-	-	-	-	(2 278 240)	(2 278 240)	-	(2 278 240)
Profit appropriation to other reserves including consolidation adjustments	-	11 744	-	135	-	-	11 609	(11 744)	-	-	-
Other	**-**	**-**	-	-	-	-	-	-	-	-	-
Other	-	-	-	-	-	-	-	-	-	-	-
Equity as at 30.06.2017	**262 470**	**20 577 514**	**9 137 221**	**1 982 459**	**9 092 735**	**(33 151)**	**398 250**	**853 816**	**21 693 800**	**15 137**	**21 708 937**

Notes to the financial statements presented on pages 11 – 124 constitute an integral part of the consolidated financial statements.

Consolidated cash flow statement

(in PLN thousand)

	NOTE	I HALF 2018 PERIOD FROM 01.01.2018 TO 30.06.2018	I HALF 2017 PERIOD FROM 01.01.2017 TO 30.06.2017
Cash flow from operating activities – indirect method			
Net profit for the period		**932 140**	**884 778**
Adjustments for:		**(7 252 705)**	**(8 096 876)**
Depreciation and amortization	17	177 673	169 567
Share of profit (loss) of associates	19	-	(20 554)
(Gains) losses on investing activities		(37 521)	(5 779)
Net interest income	9	(2 441 227)	(2 251 209)
Dividend income	11	(19 780)	(19 418)
Interest received		3 095 511	2 805 729
Interest paid		(526 371)	(552 601)
Income tax		345 026	312 243
Income tax paid		(462 674)	(150 267)
Change in loans and advances to banks		968	114 003
Change in financial assets held for trading		398 355	(1 477 361)
Change in derivative financial instruments (assets)		112 964	553 863
Change in loans and advances to customers		(3 733 461)	(2 946 802)
Change in receivables from finance leases		(323 606)	(121 681)
Change in investment (placement) securities		(481 576)	(85 851)
Change in other assets		245 666	(22 368)
Change in amounts due to banks		393 619	(258 748)
Change in financial liabilities held for trading		(43 545)	(383 357)
Change in derivative financial instruments (liabilities)		(579 435)	(458 211)
Change in amounts due to customers		(3 261 095)	(3 180 530)
Change in debt securities issued		4 026	(19 036)
Change in subordinated liabilities		(175)	-
Change in provisions		(3 797)	14 234
Change in other liabilities		(112 250)	(112 742)
Net cash flows from operating activities		**(6 320 565)**	**(7 212 098)**
Cash flow from investing activities			
Investing activity inflows		**75 257 886**	**20 085 862**
Sale of investment securities		74 794 295	19 709 272
Sale of intangible assets and property, plant and equipment		14 585	307
Dividend received		940	1 173
Transfer of management funds		22 680	-
Other investing inflows		425 386	375 110
Investing activity outflows		**(66 476 229)**	**(11 609 855)**
Acquisition of investment securities		(66 388 104)	(11 497 502)
Acquisition of intangible assets and property, plant and equipment		(88 125)	(112 353)
Net cash flows from investing activities		**8 781 657**	**8 476 007**

Notes to the financial statements presented on pages 11 - 124 constitute an integral part of the consolidated financial statements.

Consolidated cash flow statement (cont.)

(in PLN thousand)

	NOTE	I HALF 2018 PERIOD FROM 01.01.2018 TO 30.06.2018	I HALF 2017 PERIOD FROM 01.01.2017 TO 30.06.2017
Cash flows from financing activities	42		
Financing activity inflows		**3 095 259**	**-**
Due to loans and advances received from banks		1 261 076	-
Issue of debt securities		1 834 183	-
Financing activity outflows		**(1 920 412)**	**(255 300)**
Repayment of loans and advances received from banks		(1 179 198)	(67 963)
Redemption of debt securities		(741 214)	(187 337)
Net cash flows from financing activities		**1 174 847**	**(255 300)**
Total net cash flows		**3 635 939**	**1 008 609**
including: effect of exchange rate fluctuations on cash and cash equivalents held		99 328	(122 993)
Net change in cash and cash equivalents		**3 635 939**	**1 008 609**
Cash and cash equivalents at the beginning of the period	42	**7 345 040**	**8 666 090**
Cash and cash equivalents at the end of the period	42	**10 980 979**	**9 674 699**

Notes to the financial statements presented on pages 11 – 124 constitute an integral part of the consolidated financial statements.

Notes to financial statements

(in PLN thousand)

The accompanying notes to the financial statements constitute an integral part of the condensed consolidated interim financial statements.

1. General information

Bank Polska Kasa Opieki Spółka Akcyjna (hereafter 'Bank Pekao S.A.' or 'the Bank'), with its headquarters in Warsaw 00-950, Grzybowska Street 53/57, was incorporated on 29 October 1929 in the Commercial Register of the District Court in Warsaw and has been continuously operating since its incorporation.

Bank Pekao S.A. is registered in the National Court Registry – Enterprise Registry of the Warsaw District Court, XII Commercial Division of the National Court Registry in Warsaw under the reference number KRS 0000014843.

According to IFRS 10 'Consolidated financial statements', the parent entity of Bank Pekao S.A. is Powszechny Zakład Ubezpieczeń S.A. (hereinafter 'PZU S.A.') with its registered office in Warsaw at Al. Jana Pawła II 24.

The condensed consolidated interim financial statements of Bank Pekao S.A. Group for the period from 1 January 2018 to 30 June 2018 contain financial information of the Bank and its subsidiaries (together referred to as the 'Group'), and the associates accounted for using equity method.

The share ownership structure of the Bank is presented in the Note 5.4 of the Report on the activities of Bank Pekao S.A. Group for the first half of 2018.

2. Group structure

The Group consists of Bank Pekao S.A. as the parent entity and the following subsidiaries

NAME OF ENTITY	LOCATION	CORE ACTIVITY	PERCENTAGE OF THE GROUP'S OWNERSHIP RIGHTS IN SHARE CAPITAL / VOTING	
			30.06.2018	31.12.2017
Pekao Bank Hipoteczny S.A.	Warsaw	Banking	100.00	100.00
Centralny Dom Maklerski Pekao S.A.	Warsaw	Brokerage	100.00	100.00
Pekao Leasing Sp. z o.o.	Warsaw	Leasing services	100.00	100.00
Pekao Investment Banking S.A.	Warsaw	Brokerage	100.00	100.00
Pekao Faktoring Sp. z o.o.	Lublin	Factoring services	100.00	100.00
Pekao Powszechne Towarzystwo Emerytalne S.A. (in liquidation)	Warsaw	Pension fund management	100.00	100.00
Centrum Kart S.A.	Warsaw	Financial support	100.00	100.00
Pekao Financial Services Sp. z o.o.	Warsaw	Transferable agent	66.50	100.00
Centrum Bankowości Bezpośredniej Sp. z o.o.	Cracow	Call-center services	100.00	100.00
Pekao Property S.A., including:	Warsaw	Real estate development	100.00	100.00
FPB - Media Sp. z o.o.	*Warsaw*	*Real estate development*	*100.00*	*100.00*
Pekao Fundusz Kapitałowy Sp. z o.o. (in liquidation)	Warsaw	Business consulting	100.00	100.00
Dom Inwestycyjny Xelion Sp. z o.o.	Warsaw	Financial intermediary	100.00	100.00
Pekao Investment Management S.A.	Warsaw	Asset management	100.00	100.00
Pekao TFI S.A.	*Warsaw*	*Asset management*	*100.00*	*100.00*

As at 30 June 2018, all subsidiaries of the Bank have been consolidated.

Notes to financial statements (cont.)

(in PLN thousand)

Associates

Bank Pekao S.A. Group has an interest in the following associates

NAME OF ENTITY	LOCATION	CORE ACTIVITY	PERCENTAGE OF THE GROUP'S OWNERSHIP RIGHTS IN SHARE CAPITAL / VOTING	
			30.06.2018	31.12.2017
CPF Management	Tortola, British Virgin Islands	Financial brokerage – not operating	40.00	40.00

As at 30 June 2018, the Group held no shares in entities under joint control.

Transfer of management of Pekao OFE and DFE Pekao funds

On 24 April 2018, the Polish Financial Supervision Authority issued a consent for PTE PZU S.A. to take over the management of Pekao Otwarty Fundusz Emerytalny ('Pekao OFE') and Dobrowolny Fundusz Emerytalny Pekao ('DFE Pekao'), previously managed by Pekao PTE S.A. As a result of this decision, from 19 May 2018, PTE PZU S.A. has taken over the management of Pekao OFE and DFE Pekao funds.

The transfer transaction of management of Pekao OFE and DFE Pekao funds was classified as an intra-group transaction. Net result on this transaction in the amount of PLN 22 680 thousand was recognized in the Group's equity.

The above presented accounting treatment of a management transfer transaction is consistent with the accounting policy adopted by the Group and applied to the acquisition and sale of entities under common control.

On 1 June 2018, the Extraordinary General Meeting of Pekao PTE S.A. adopted a resolution to dissolve the Company and to open its liquidation as of that date. Currently, the Company operates under the name Pekao PTE S.A. in liquidation.

Changes in non-controlling interests

On 4 June 2018 an entry was made in the National Court Register regarding the transfer of an organized part of the enterprise, separated from PZU Centrum Operacji S.A. at Pekao Financial Services Sp. z o.o. Thus, the share capital of Pekao Financial Services Sp. z o.o. increased to PLN 6 767 000, and the Company took over full service of PTE PZU S.A. and TFI PZU S.A. within the scope of the transfer agent service and extended the scope of services for PZU Życie S.A. The shares in the increased share capital of the Company in the amount of PLN 4 534 worth PLN 2 267 000 were taken up by PZU S.A. The Bank currently holds 66.5% of shares in the Company's equity, while PZU S.A. - 33.5%.

The effect of changes in the ownership interest of Pekao Financial Services Sp. z o.o. on the equity attributable to equity holders of the Bank during the reporting period is presented in the table below.

	I HALF 2018
Carrying amount of non-controlling interests	(10 848)
Consideration received	7 357
Decrease in equity attributable to equity holders of the Bank	**(3 491)**

3. Business combinations

In the first half of 2018 there were no business combinations in the Group.

In 2017 the Bank acquired 51% shares in Pekao Investment Management S.A. and 50% shares in Dom Inwestycyjny Xelion Sp. z o.o. These transactions were described in the 2017 annual consolidated financial statements of the Bank Pekao S.A. for the year ended 31 December 2017 in Note 2.

4. Statement of compliance

The condensed consolidated interim financial statements of Bank Pekao S.A. Group have been prepared in accordance with International Accounting Standard 34 'Interim Financial Reporting' (IAS 34) as adopted by the European Union and other applicable regulations.

These financial statements do not include all information required for annual financial statements, and shall be read in conjunction with the consolidated financial statements of Bank Pekao S.A. Group for the year ended 31 December 2017, including changes caused by the implementation of International Financial Reporting Standard 9 'Financial Instruments' (IFRS 9) as of 1 January 2018 (described in Note 5.9).

The consolidated financial statements of Bank Pekao S.A. Group as at and for the year ended 31 December 2017 are available at the Bank's website, www.pekao.com.pl

In accordance with the Decree of the Ministry of Finance dated 29 March 2018 on current and periodic information provided by issuers of securities and the conditions for recognition as equivalent information required by the law of a non-Member State (Official Journal from 2018, item 757) the Bank is required to publish the financial report for the six months period ended 30 June 2018, i.e. current interim period.

The condensed consolidated interim financial statements have been prepared in Polish Zloty, and all amounts are stated in PLN thousand, unless indicated otherwise.

These condensed consolidated interim financial statements were authorized for issue by the Management Board on 7 August 2018.

5. Significant accounting policies

5.1 Basis of preparation of Consolidated Financial Statements

General information
Consolidated Financial Statements of the Group for the fist half of 2018 have been prepared based on the following valuation methods:

- at fair value for derivatives, financial assets and liabilities held for trading, financial assets designated as measured at fair value through profit and loss at initial recognition, equity instruments, financial assets classified to business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and financial assets that do not meet SPPI criteria,
- at amortized cost for financial assets, classified to business model whose objective is to hold financial assets in order to collect contractual cash and meeting SPPI criteria at the same time, for other financial liabilities,
- at historical cost for non-financial assets and liabilities,

- non-current assets (or disposal groups) classified as held for sale are measured at the lower of the carrying amount or the fair value less costs to sell.

Comparative data in these Consolidated Financial Statements of the Group have been prepared based on the following valuation methods:
- at fair value for derivatives, financial assets and liabilities held for trading, financial assets recognized initially at fair value through profit or loss and available-for-sale financial assets, except for those for which the fair value cannot be reliably measured,
- at amortized cost for other financial assets, including loans and advances and other financial liabilities,
- at historical cost for non-financial assets and liabilities or financial assets available for sale whose fair value cannot be reliably measured,
- non-current assets (or disposal groups) classified as held for sale are measured at the lower of the carrying amount or the fair value less costs to sell.

The Group has adopted International Financial Reporting Standard 9 ‘Financial Instruments’ with a date of transition of 1 January 2018. The adoption of IFRS 9 has resulted in changes in the accounting policies for recognition, classification and measurement of financial assets and financial liabilities and impairment of financial assets. The impact of the implementation of IFRS 9 has been presented in the Note 5.9.

The Group has taken advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. Differences in the carrying amounts of financial assets and financial liabilities resulting from the adoption of IFRS 9 generally have been recognized in retained earnings as at 1 January 2018.

The Group decided to take advantage of the choice which gives IFRS 9 and continues to apply the hedge accounting requirements of IAS 39. This decision will apply to all hedging relationships, for which the Group applies and will apply hedge accounting in the future.

The following is a summary of the significant accounting policies applicable from 1 January 2018, as well as the accounting policies used to compile the comparative data.

5.2 Consolidation

Consolidation principles
The consolidated financial statements of Bank Pekao S.A. Group include the financial data of Bank Pekao S.A. and its subsidiaries as at 30 June 2018. The financial statements of the subsidiaries are prepared at the same reporting date as those of the parent entity, using consistent accounting policies within the Group in all important aspects.

All intra-group balances and transactions, including unrealized gains, have been eliminated. Unrealized losses are also eliminated, unless there is an objective evidence of impairment, which should be recognized in the consolidated financial statements.

Investments in subsidiaries
Subsidiaries are all entities over which the Group has control. The Group controls an entity when the Group has power over an entity, is exposed to or has rights to variable returns from its involvement with the entity and has the ability to affect these returns through its power over the entity. The subsidiaries are consolidated from the date of obtaining control by the Group until the date when the control ceases.

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred to the former owners of the acquiree and the equity interests issued by the Group. Identifiable assets acquired and liabilities assumed are measured at their fair values at the acquisition date. The Group measures any non-controlling interests in the acquire at fair value or at the present ownership instruments’ proportionate share in the recognized amounts of the acquire's identifiable net assets.

Notes to financial statements (cont.)

(in PLN thousand)

Acquisition-related costs are expenses as incurred (in the income statement under 'Administrative expenses').
If the business combination is achieved in stages, the acquirer remeasures its previously held equity interests in the acquiree at fair value at the acquisition date (date of obtaining control) and recognizes the resulting gain or loss in the income statement.

The excess of the consideration transferred, the amount of any non-controlling interest in the acquiree and the acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the identifiable net assets acquired is recorded as goodwill. If the total of consideration transferred, non-controlling interest recognized and previously held interest measured is less than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognized directly in the income statement.

The above policy does not apply to the business combinations under common control.

The changes in a parent entity's ownership interest in a subsidiary that do not result in the parent entity losing control of the subsidiary are accounted for as equity transactions (i.e. transactions with owners of parent entity). The Group recognizes directly in equity any difference between the amount by which the non-controlling interests are adjusted and the fair value of the consideration paid or received, and attributes it to the owners of the parent entity.

When the Group ceases to have control over the subsidiary, any retained interest in that subsidiary is remeasured to its fair value at the date when control is lost, with the change in carrying amount recognized in the income statement.

Recognition of business combinations under common control at book value
Business combinations under common control are excluded from the scope of IFRS. As a consequence, following the recommendation included in IAS 8 'Accounting Policies, Changes in Accounting Estimates and Errors', in the absence of any specific guidance within IFRS, Bank Pekao S.A. has adopted the accounting policy consistently applied in all business combinations under common and recognizes those transactions using book value.

The acquirer recognizes the assets and liabilities of the acquired entity at their current book value adjusted exclusively for the purpose of aligning the accounting principles. Neither goodwill, nor badwill is recognized.

Any difference between the book value of the net assets acquired and the fair value of the consideration paid is recognized in the Group's equity. In applying this book value method, the comparative periods are not restated.

If the transaction results in the acquisition of non-controlling interests, the acquisition of any non-controlling interest is accounted for separately.

There is no guidance in IFRS how to determine the percentage of non-controlling interests acquired from the perspective of a subsidiary. Accordingly Bank Pekao S.A. uses the same principles as the ultimate parent for estimating the value of non-controlling interests acquired.

Investments in associates
An associate is an entity over which the Group has significant influence, and that is neither a subsidiary nor a joint venture. The Group usually holds from 20% to 50% of the voting rights in an associate. The equity method is calculated using the financial statements of the associates. The balance sheet dates of the Group and its associates are the same.

On acquisition of the investment, any difference between the cost of the investment and the Group's share in the net fair value of the investee's identifiable assets and liabilities is accounted for as follows:
- goodwill relating to an associate is included in the carrying amount of the investment,
- any excess of the Group's share in the net fair value of the investee's identifiable assets and liabilities over the cost of the investment is included as income in the determination of the Group's share in the associate's profit or loss in the period in which the investment is acquired.

The Group recognizes the investments in associates applying the equity method. The investment in associates is initially recognized at cost and the carrying amount is increased or decreased to recognize the Group's share in net assets of the associate after the date of acquisition, net of any impairment allowances.

Notes to financial statements (cont.)

(in PLN thousand)

The Group's share of post-acquisition profit or loss is recognized in the income statement, and its share of post-acquisition movements in other comprehensive income is recognized in other comprehensive income with a corresponding adjustment to the carrying amount of the investment. Distributions received from an associate reduce the carrying amount of the investment.

If the Group's share in the losses of an associate equals or exceeds the Group's share in the associate, the Group ceases to recognize further losses, unless it assumed obligations or made a payment on behalf of the associate.

Unrealized profits or losses from transactions between the Group and associates are eliminated pro rata to the Group's share in the associates.

5.3 Foreign currencies

- Transactions and balances
  Foreign currency transactions are calculated into the functional currency using the spot exchange rate from the date of the transaction. Gains and losses from foreign currency translation differences resulting from settlements of such transactions and from the statement of financial position valuation of monetary assets and liabilities expressed in foreign currencies are recognized in the income statement.
- Foreign currency translation differences arising from non-monetary items, such as equity instruments classified as financial assets measured at fair value through the profit or loss are recognized together with the changes in the fair value of that item in the income statement.
- Foreign currency translation differences arising from non-monetary items such as equity instruments classified as financial assets measured at fair value through other comprehensive income are recognized in the revaluation reserves.

The foreign exchange rate differences from the valuation of foreign entities are accounted for as a separate component of equity.

Goodwill arising on acquisition of the entity operating abroad as well as any adjustments of the balance sheet value of assets and liabilities to fair value arising on the acquisition of the entity are treated as assets and liabilities of a foreign entity i.e. they are expressed in the functional currency of the overseas entity and translated at the closing exchange rate as described above.

5.4 Income statement

Interest income and expense – principles applied since 1 January 2018
The Group recognizes in the income statement all interest income and expense related to financial instruments measured at amortized cost using the effective interest rate method, financial assets measured at fair value through other comprehensive income and financial assets and liabilities measured through profit or loss.

The effective interest rate is the discount rate of estimated future cash inflows and payments made during the expected period until the expiry date of the financial instruments, and in justified cases in a shorter time, to the gross carrying amount of such financial asset or to the amortised cost of financial liability. The calculation of the effective interest rate includes all commissions paid and received by parties to the agreement, transaction costs and all other premiums and discounts, comprising an integral part of the effective interest rate.

Interest income includes interest and commission fees received or due from loans, interbank deposits and securities measured at amortised cost recognized in the calculation of effective interest rate of loans and financial assets measured at fair value through other comprehensive income or through profit or loss and hedging derivatives.

Gross carrying amount of the financial asset is the basis for interest income calculation except for credit-impaired financial assets and purchased or originated credit-impaired financial assets (POCI assets). At the recognition of impairment of financial assets measured at amortized cost or financial assets measured at fair value through other comprehensive income, the interest income is still recognized in profit or loss but is calculated by applying the effective interest rate to the gross carrying amount less the impairment charges.

Interest expense related to liabilities associated with client accounts and debt securities issued are recognized in the profit or loss using the effective interest rate.

Interest income and expense – principles applied until 31 December 2017

The Group recognizes in the income statement all interest income and expense related to financial instruments valued at amortized cost using the effective interest rate method, financial assets available for sale and financial assets at fair value through profit or loss.

The effective interest rate is the discount rate of estimated future cash inflows and payments made during the expected period until the expiry of the financial instruments, and in justified cases in a shorter time, to the net carrying amount of such financial assets or liabilities.

The calculation of the effective interest rate includes all commissions paid and received by parties to the agreement, transaction costs and all other premiums and discounts, comprising an integral part of the effective interest rate.

Interest income includes interest and commission fees received or due from credits, interbank deposits and held to maturity securities, recognized in the calculation of effective interest rate, as well as from securities available for sale and measured at fair value through the income statement and hedging derivatives.

At the recognition of impairment of financial instruments measured at amortized cost and of available for sale financial assets, the interest income is accrued based on the carrying amount of the receivable (this is the new, lower value reduced by the impairment charge) using the interest rate used when discounting the future cash flows for impairment calculation.

Interest expense of the reporting period related to interest liabilities associated with client accounts and liabilities from the issue of treasury stock are recognized in the income statement using the effective interest rate.

Fee and commission income and expense

Fee and commission income is generated from financial services provided by the Group. Fee and commission income and expense is recognized in the profit or loss using the following methods:

- fees and commissions directly attributable to financial asset or liability origination (both income and expense) are recognized in the income statement using the effective interest rate method and are described above,
- fees and commissions relating to the loans and advances without a defined repayment schedule and without a defined interest rate schedule e.g. overdraft facilities and credit cards are amortized over the life of the product using the straight line method,
- other fees and commissions arising from the Group’s financial services offering (customer account transaction charges, credit card servicing transactions, bonuses from card providers in order to cover the marketing card cost, brokerage activity and canvassing) as well as the trade margins on foreign exchange transactions with the Bank’s clients are recognized in the income statement up-front when the corresponding service is provided.

Income and expense from bancassurance

The Group splits the remuneration for sale of insurance products linked to loans into separate components, i.e. dividing the remuneration into proportion of fair value of financial instrument and fair value of intermediary service to the sum of those values. The fair values of particular components of the remuneration are determined based on market data to a highest degree.

Notes to the financial statements (cont.)

(in PLN thousand)

The particular components of the Group's remuneration for sale of insurance products linked to loans are recognized in the income statement according to the following principles:

- remuneration from financial instrument – as part of effective interest rate calculation, included in interest income,
- remuneration for intermediary service – upfront at the time when the insurance product in sold, included in fee and commission income.

Additionally the Group estimates the part of the remuneration which will be refunded in the future (eg. due to early termination of insurance contract, early repayment of loan). The estimate of the provision for future refunds is based on the analysis of historical data and expectations in respect to refunds trend in the future.

Result on financial assets and liabilities measured at fair value through profit or loss – principles applied since 1 January 2018

Result on financial assets measured at fair value through profit or loss includes:

- Foreign exchange result
  The foreign exchange gains (losses) are calculated taking into account the positive and negative foreign currency translation differences, whether realized or unrealized from the daily valuation of assets and liabilities denominated in foreign currencies. The revaluation is perform using the average exchange announced by the NBP on the balance sheet date.
  The foreign exchange result includes swap points from derivative transactions, entered into by the Group for the purpose of managing the Group's liquidity in foreign currencies.
  Income from foreign exchange positions includes also foreign currency translation differences from valuation of investments in foreign operations arising on disposal thereof. Until the disposal, foreign currency translation differences from valuation of assets in foreign operations are recognized in 'Other capital and reserves'.
- Result on derivatives, loans and advances to customers and securities measured at fair value through profit or loss.
  The income referred to above includes gains and losses realized on a sale or a change in the fair value of the assets mentioned above.
  The accrued interest and unwinding of a discount or a premium on loans and advances to customers and debt securities measured at fair value through profit or loss is presented in the net interest income.

Result on financial assets and liabilities held for trading – principles applied until 31 December 2017

Result on financial assets and liabilities held for trading include:

- Foreign exchange result
  The foreign exchange gains (losses) are calculated taking into account the positive and negative foreign currency translation differences, whether realized or unrealized from the daily valuation of assets and liabilities denominated in foreign currencies. The revaluation is perform using the average exchange announced by the NBP on the balance sheet date.
  The foreign exchange result includes swap points from derivative transactions, entered into by the Group for the purpose of managing the Group's liquidity in foreign currencies.
  Income from foreign exchange positions includes also foreign currency translation differences from valuation of investments in foreign operations arising on disposal thereof. Until the disposal, foreign currency translation differences from valuation of assets in foreign operations are recognized in 'Other capital and reserves'.
- Income from derivatives and securities held for trading
  The income referred to above includes gains and losses realized on a sale or a change in the fair value of assets and liabilities held for trading.
  The accrued interest and unwinding of a discount or a premium on securities held for trading is presented in the net interest income.

Gains (losses) on financial assets/liabilities designated at fair value through profit or loss

This includes gains and losses realized on a sale or a change in the fair value of assets and liabilities, designated at fair value through profit or loss.

The accrued interest and unwinding of a discount or a premium on financial assets/ liabilities designated at fair value through profit or loss are recognized in the interest result.

Notes to the financial statements (cont.)

(in PLN thousand)

Other operating income/expense
Other operating income includes mainly amounts received for compensation, revenues from operating leases, recovery of debt collection costs, excess payments, miscellaneous income and releases of provision for legal cases. Other operating expenses include mainly the costs of client claims, compensation paid, sundry expenses and costs of provision for litigations.

5.5 Valuation of financial assets and liabilities, derivative financial instruments

Financial assets – principles applied since 1 January 2018
Financial assets are classified into the following categories:

- financial assets measured at amortised cost,
- financial assets measured at fair value through other comprehensive income,
- financial assets measured at fair value through profit or loss.

The above mentioned classification is based on the entity's business model for managing the financial assets and the characteristics regarding the contractual cash flows (i.e. whether the contractual payments are solely payments of principal and interest on the principal amount outstanding 'SPPI').

The financial assets could be classified depending on the Bank's business model to the following categories:

- a business model whose objective is to hold financial assets in order to collect contractual cash flows,
- a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets,
- a business model whose object is to held financial assets for trading and other business models.

The business model assessment
The assessment of the business model is made at the initial recognition of the asset (with the exception of the first adoption of IFRS 9 – when implementing the Standard, the Bank classifies the particular groups of the asset in accordance with the business model applied at the date of the implementation of the IFRS 9 i.e. 1 January 2018, not at the initial recognition of the financial asset.

The business model criteria refers to the way the Bank's managing financial assets in order to generate cash flows.

The Bank evaluates the purpose of the business model, to which the particular financial assets are classified on the level of particular portfolios of the assets – performing the analysis on those portfolio level is a reliable reflection of the Bank's business activities regarding these models and also reflects to information analysis of those activities provided to the Bank's management.

The assessment of the business model is based on the analysis of the following information regarding the portfolio of the financial assets:

- applied policies and business aims for the particular portfolio and its practical implementation. In particular, the management's strategy regarding the acquisition of revenues from contractual interest payments, maintaining a specific interest rate profile of the portfolio, managing the liquidity gap and obtaining cash flows as a result of the sale of financial assets is assessed,
- the manner in which the profitability of the portfolio is assessed and reported to the Bank's Management Board,
- types of risk that affect the profitability and effectiveness of a given business model (and financial assets held under this business model) and the manner of managing the identified types of risk,
- the way in which the managers of business operations are remunerated under a given business model - eg whether the remuneration depends on changes in the fair value of financial assets or the value of contractual cash flows obtained,
- frequency, value and moment of sale of financial assets made in prior reporting periods, the reasons for these sales and expectations regarding future sales activity. However, information on sales activity is analyzed taking into account the overall assessment of the Bank's implementation of the adopted method of managing financial assets and generating cash flows.

Notes to the financial statements (cont.)

(in PLN thousand)

Financial assets held for trading or managed based on their fair value are measured at fair value through profit or loss, as they are not part of the business model, the purpose of which is to benefit from contractual cash flows from held financial assets or the purpose of which is to benefit from acquiring contractual cash flows and from the sale of financial assets.

Before making a decision regarding allocating a portfolio of financial assets to a business model which purpose is to obtain contractual cash flows, the Bank reviews and evaluates significant and objective quantitative data influencing the allocation of asset portfolios to the relevant business model, in particular:

- the value of sales of financial assets made within the particular portfolios,
- the frequency of sales of financial assets as part of particular portfolios,
- expectation analysis regarding the value of planned sales of financial assets and their frequency of the particular portfolios, this analysis is carried out on the basis of probable scenarios of the Bank's business activities in the future.

The portfolios of financial assets from which sales are made that do not result from an increase in credit risk meet the assumptions of the business model, which purpose is to obtain contractual cash flows, provided that these sales:

- are at low volume (even with a relatively high frequency of sales) or
- are made rarely - as a result of one-off events, which the probability to occur again in the future, according to the Bank's professional judgment is rare (even with a relatively high volume) or
- they occur close to the maturity date of the financial assets being sold, and the revenue obtained from such sales is similar to those which could be obtained from remaining contractual cash flows as if the financial asset was held in the Bank's portfolio to the original maturity date.

The following sales are excluded from the analysis of sales value:

- the sales resulting from an increase in the credit risk of financial assets, regardless of their frequency and volume,
- the sales resulting from one-off events, which the probability to occur again in the future, according to the Bank's professional judgment is rare,
- the sales made close to maturity.

A held to obtain contractual cash flows or sale business model includes a portfolio of financial assets whose purpose is, in particular, managing current liquidity levels, maintaining the assumed profitability profile and / or adjust the duration of the asset and financial liabilities, and a level of sales are higher than for those financial assets classified in a model which purpose is to obtain contractual cash flows.

The business model comprising financial assets held for sale and other includes assets that do not meet the criteria to be classified into the business model, which purpose is to obtain contractual cash flows the business model which purpose is to obtain contractual cash flows or sales and also acquiring cash flows from interest and capital is not the main business target.

Assessment, whether the contractual payments are solely payments of principal and interest on the principal amount outstanding (SPPI criteria)

For the purposes of assessing cash flow characteristics, 'principal' is defined as the fair value of a financial asset at the time of initial recognition. 'Interest' is defined as the time value of money and the credit risk related to the unpaid part of principal and also other risks and costs associated with a standard loan agreement (e.g. liquidity risk or administrative costs) and margin.

When assessing whether the contractual cash flows constitute solely payments of principal and interest, the Bank analyzes contractual cash flows. This analysis includes an assessment whether the contractual terms include any provisions that the contractual payments could be changed or the amount of the contractual payments could be changed in a way that from an economic point of view they will not only represent repayments of principal and interest on the outstanding principal. When making this assessment, the Bank takes into account the occurrence of, among others:

- conditional events that may change the amount or timing of the payment,
- financial leverage (for example, interest terms include a multiplier greater than 1),
- terms regarding the extension of the contract or prepayment option,

- terms that the Bank's cash flow claim is limited to a specified assets (eg non-recourse assets),
- terms that modify the time value of money – e.g. mismatch of the frequency of the revaluation of the reference interest rate to its tenor.

The SPPI test is conducted for each financial asset classified into the business model, which purpose is to obtain contractual cash flows or a business model which purpose is to obtain contractual cash flows or sale, as at the initial recognition date or as at the latest significant annex changing the terms of contractual cash flows.

The Bank performs an SPPI test at the level of homogeneous groups of standard products or at the level of a single contract for non-standard products or at the level of ISIN code for debt securities.

In situation when the time value of money is modified for a particular financial asset, the Bank is required to make an additional assessment (i.e. Benchmark Test) to determine whether the contractual cash flows are still solely payments of principal and interest on the principal amount outstanding by determining how different the contractual (undiscounted) cash flows could be from the (undiscounted) cash flows that would arise if the time value of money element was not be modified (the benchmark cash flows). Benchmark Testing is not permitted for situation that some terms modify contractual cash flows, such as the built-in leverage element.

Financial assets measured at amortized cost
Financial assets are measured at amortized cost if at the same time they meet the following two criteria:

- the financial asset is held within a business model whose objective is to hold financial assets in order to collect contractual cash flows, and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Financial assets measured at amortized cost include amounts due from the Central Bank, amounts due from other banks, loans and advances to customers, investment debt securities, receivables reverse-repo and buy-sell-back transactions, meeting the criteria described in the previous paragraph.

Upon initial recognition, these assets are measured at fair value increased by transaction costs that are directly attributable to the acquisition or issue of a financial asset.

After initial recognition, these assets are measured at amortized cost using the effective interest rate. The calculation of the effective interest rate includes all commissions paid and received by the parties, transaction costs and other bonuses and discounts constituting an intergrated part of the effective interest rate.

Interest accrued using the effective interest rate is recognized in net interest income.

At the moment of recognizing the impairment, the interest recognized in the income statement is calculated based on the amount reduced by an allowance for expected credit losses (net carrying amount), whereas in the balance sheet accrued interest is calculated on the gross amount of the exposure. The difference is included in the impairment allowance.

Allowances for expected credit losses reduce the gross carrying amount of assets, on the other hand they are recognized in the income statement under 'Net impairment losses on financial assets and off-balance sheet commitments'.

Financial assets measured at fair value through other comprehensive income
Financial assets (excluding equity instruments) are measured at fair value through other comprehensive income when they simultaneously meet the following two conditions and have not been designated for measurement at fair value through profit or loss:

- the financial asset is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and
- the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

Notes to the financial statements (cont.)

(in PLN thousand)

Financial assets measured at fair value through other comprehensive income include investment debt securities as well as loans and advances to customers that meet the criteria described in the previous paragraph.

Interest accrued using the effective interest rate is recognized in net interest income.

The effects of changes in fair value are recognized in other comprehensive income until the asset is excluded from the statement of financial position, when accumulated profit or loss is recognized in the income statement under 'Result on derecognition of financial assets and liabilities not measured at fair value through profit or loss'.

An allowance for expected credit losses from financial assets that are measured at fair value through other comprehensive income is recognized in other comprehensive income and does not reduce the carrying amount of the financial asset in the statement of financial position. On the other hand, an expected credit risk allowance is recognized in the income statement under 'Net impairment losses on financial assets and off-balance sheet commitments'.

Purchased or originated credit-impaired financial assets (POCI)
The Group distinguishes the category of purchased or originated credit-impaired assets. POCI are assets that are credit-impaired on initial recognition. Financial assets that were classified as POCI at initial recognition should be treated as POCI in all subsequent periods until they are derecognition.

POCI assets may arise through:
a) by purchasing a contract that meets the definition of POCI (e.g. as a result of a merger with another entity or purchase of a portfolio of assets),
b) by concluding a contract that is POCI at the time of original granting (e.g. granting a loan to a customer in a bad financial condition),
c) by modifying the contract (e.g. under restructuring) qualifying this contract to be derecognised, resulting in a recognitionof a new contract meeting the definition of POCI.

Conditions for qualifying a contract to be derecognised are described below.

At initial recognition, POCI assets are recognized in the balance sheet at their fair value, in particular they do not have recognized impairment allowance.

POCI assets do not constitute a separate accounting category of financial assets. They are classified into accounting categories in accordance with the general principles for classification of financial assets. The categories in which POCI assets may exist are a category of financial assets measured at amortized cost and financial assets measured at fair value through other comprehensive income.

Investments in equity instruments
For investments in equity instruments not held for trading, the Group may irrevocably choose to present changes in their fair value in other comprehensive income. The Bank makes a decision in this respect based on an individual analysis of each investment. In sucha a case the amounts presented in other comprehensive income are not subsequently transferred to profit or loss. In case of sale of an equity investment elected to be measured at fair value through other comprehensive income, a result on sale is transferred to the item 'Other reserve capital'.

Equity investments not designated for measurement at fair value through other comprehensive income at the initial recognition are measured at fair value through profit or loss. Changes in the fair value of such investments, as well as the result on sales, are recognized in the income statement under 'Result on financial assets and liabilities measured at fair value through profit or loss'.

Dividends from equity instruments, both measured at fair value through profit or loss and designated for valuation through other comprehensive income, are recognized in the income statement when the Group's right to receive payment is established.

Financial assets at fair value through profit or loss
In this category, the Group qualifies derivatives (non-hedging instruments), debt and equity securities, loans and receivables that were acquired or included in this category with the intention of selling in the short term. In addition, this category includes financial assets not held for trading that are compulsorily measured at fair value through profit or loss for which the SPPI test has not been passed.

Moreover, at initial recognition, the Group may irrevocably designate selected financial assets that meet the amortized cost measurement criteria or at fair value through other comprehensive income for measurement at fair value through profit or loss if it eliminates or significantly reduces the accounting mismatch that would otherwise arise from measuring assets at different methods.

Standardized purchase and sale transactions of financial assets designated at fair value through profit or loss, designated as held for trading (except for derivatives), held to maturity, and available for sale, are recognized and derecognized by the Group on the settlement date of such transaction, i.e. as at the date of receipt or delivery of such assets.

Changes in the fair value of assets, which occur during the period from transaction date to transaction settlement date, shall be recognized similarly as in the case of the asset held.

Credits and loans are recognized on the date of cash disbursement to the debtor.

Derivative instruments are recognized or derecognized on transaction dates.

Reclassification of financial assets - principles applied from 1 January 2018
Financial assets are not reclassified in the reporting periods following the initial recognition, except for the reporting period following the change of the business model for managing financial assets by the Group.

The reclassification of financial assets is applied prospectively from the reclassification date - without restatement of previously recognized gains, losses (including impairment gains or losses) or interest.

The following are not changes in business model:
- a change in intention related to particular financial assets (even in circumstances of significant changes in market conditions),
- the temporary disappearance of a particular market for financial assets,
- a transfer of financial assets between parts of the entity with different business models.

Modifications of financial assets - principles applied from 1 January 2018
If the terms of the financial asset agreement change, the Bank assesses whether the cash flows generated by the modified asset differ significantly from those generated by the asset before modifying the terms of its agreement. If a significant difference is identified, the original financial asset is derecognised, and the modified financial asset is recognized in the books at its fair value.

If the cash flows generated by the modified asset measured at amortized cost are not materially different from the original cash flows, the modification does not result in derecognition of the financial asset. In this case, the Bank recalculates the gross carrying amount of the financial asset.

The assessment whether a given modification of financial assets is significant or insignificant modification depends on the fulfillment of qualitative and quantitative criteria.

The Group has adopted the following quality criteria to determine significant modifications:
- currency conversion, unless it results from existing contractual provisions or requirements of applicable legal regulations,
- change (replacement) of the debtor, excluding the addition / departure of the joint debtor or taking over the loan in inheritance,
- consolidation of several exposures into one under an annex or settlement / restructuring agreement,
- change in the terms of the contract resulting in a change in the result of the SPPI test.

The occurrence of at least one of these criteria results in a significant modification.

The Group has adopted the following quantitative criteria to determine significant modifications:

- extension of the loan term by at least one year and at least a doubling of the residual maturity to the original maturity (meeting both conditions jointly) for Stage 1 and Stage 2, or
- increasing the current loan amount / limit by at least 10% for Stage 1 and Stage 2 or increasing the current loan amount / limit for a contract in Stage 3.

Impairment of financial assets - principles applied from 1 January 2018

A financial asset is credit-impaired when one or more events that have a detrimental impact on the estimated future cash flows of that financial asset have occurred. Evidence that a financial asset is credit-impaired include observable data about the following events:

1) significant financial difficulty of the issuer or the borrower,
2) a breach of contract, such as a default or past due event,
3) the lender(s) of the borrower, for economic or contractual reasons relating to the borrower's financial difficulty, having granted to the borrower a concession(s) that the lender(s) would not otherwise consider,
4) it is becoming probable that the borrower will enter bankruptcy or other financial reorganization,
5) the disappearance of an active market for that financial asset because of financial difficulties, or
6) the purchase or origination of a financial asset at a deep discount that reflects the incurred credit losses.

The Group recognises a loss allowance for expected credit losses on a financial asset that is measured at amortised cost or at fair value through other comprehensive income, a lease receivable, a contract asset or a loan commitment and a financial guarantee contract.

A loss allowance for financial assets that are measured at fair value through other comprehensive income is recognised in other comprehensive income and is not reducing the carrying amount of the financial asset in the statement of financial position.

If, at the reporting date, the credit risk on a financial instrument has not increased significantly since initial recognition, the Group measures the loss allowance for that financial instrument at an amount equal to 12-month expected credit losses.

At each reporting date, the Group measures the loss allowance for a financial instrument at an amount equal to the lifetime expected credit losses if the credit risk on that financial instrument has increased significantly since initial recognition.

The Group recognises in profit or loss, as an impairment gain or loss, the amount of expected credit losses (or reversal) that is required to adjust the loss allowance at the reporting date to the amount that is required to be recognised in accordance with this chapter.

For loan commitments and financial guarantee contracts, the date that the Group becomes a party to the irrevocable commitment shall be considered to be the date of initial recognition for the purposes of applying the impairment requirements.

At the reporting date, the Group only recognises the cumulative changes in lifetime expected credit losses since initial recognition as a loss allowance for purchased or originated credit-impaired financial assets. At each reporting date, the Group recognises in profit or loss the amount of the change in lifetime expected credit losses as an impairment gain or loss. An entity shall recognise favourable changes in lifetime expected credit losses as an impairment gain, even if the lifetime expected credit losses are less than the amount of expected credit losses that were included in the estimated cash flows on initial recognition.

The Group measures the loss allowance at an amount equal to lifetime expected credit losses for:

1) trade receivables or contract assets that result from transactions that are within the scope of IFRS 15,
2) lease receivables that result from transactions that are within the scope of IAS 17.

Expected credit losses are not recognized for impairment of equity instruments.

The methodology for calculating expected credit losses is described in detail in 'The description of the model for impairment allowance' in Note 7.1.

Financial assets – principles applied until 31 December 2017
Financial assets are classified into the following categories:

- Financial assets measured at fair value through profit or loss
  This category comprises two sub-categories: financial assets held for trading and financial assets designated at initial recognition as financial assets measured at fair value through profit or loss.
  Financial assets held for trading include: debt and equity securities, loans and receivables purchased or classified into this category for the purpose of disposal thereof on a short-term basis. The classification also includes derivative instruments (not used as hedging instruments).
  Financial assets classified at the moment of original recognition as financial assets measured at fair value through profit or loss include debt securities acquired by the Group for the purpose of elimination or considerable reduction of inconsistencies in the valuation between these securities and the derivatives, which are economically hedging the interest rate risk of such securities. Otherwise, such securities would have been classified into the available for sale portfolio, with the effect of valuation recognized in revaluation reserves, and valuation of derivatives economically hedging such securities reported in the income statement.

- Held to maturity
  These are non-derivative financial assets with fixed or determinable payments and fixed maturity, for which the entity has an intent and ability to hold to maturity, other than:
  a) those that the entity upon initial recognition designates as at fair value through profit or loss,
  b) those that the entity designates as available for sale, and
  c) those that meet the definition of loans and receivables.
  Financial assets classified into this category are measured at amortized cost using the effective interest rate method. The recognition of amortized cost with the use of effective interest rate is recognized in interest income.

- Loans and receivables
  Loans and receivables are non-derivative financial assets, with fixed or determinable payments, not quoted on active markets, other than:
  a) those that the entity intends to sell immediately or in the near term which are classified as held for trading and those that the entity designates as at fair value through profit or loss upon initial recognition,
  b) those that the Group upon initial recognition designates as available for sale, or
  c) those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration, which are classified as available for sale.
  This category also contains debt securities, purchased from the issuer, for which there is no active market, as well as credits, loans, receivables from reverse repo transactions and other receivables acquired and granted. Loans and receivables are measured at amortized cost using the effective interest rate method and with consideration of impairment.

- Available for sale
  This includes financial assets with an undefined holding period. The portfolio includes: debt and equity securities, as well as loans and receivables not classified into other categories. Interest on assets available for sale is calculated using the effective interest rate method, and recognized in the income statement.
  Available for sale financial assets are measured at fair value, whereas gains and losses resulting from changes in fair value against amortized cost are recognized in the revaluation reserves. Amounts in the revaluation reserves are recognized in the income statement either on the sale of an asset, or its impairment. In case of impairment of an asset, previous increases from revaluation to fair value will decrease the 'Revaluation reserves'. Should the amount of previously recognized increases be insufficient to cover the impairment, the difference will be recorded in the income statement as 'Net impairment losses on financial assets and off-balance sheet commitments'.

Dividends from equity instruments are recognized in the profit or loss at the moment the rights to receive such payments are established.

Standardized purchase and sale transactions of financial assets designated at fair value through profit or loss, designated as held for trading (except for derivatives), held to maturity, and available for sale, are recognized and derecognized by the Group on the settlement date of such transaction, i.e. as at the date of receipt or delivery of such assets.
Changes in the fair value of assets, which occur during the period from transaction date to transaction settlement date, shall be recognized similarly as in the case of the asset held.

Credits and loans are recognized on the date of cash disbursement to the debtor.

Derivative instruments are recognized or derecognized on transaction dates.

Reclassification of financial assets – principles applied until 31 December 2017
The Group may reclassify the financial assets classified as available for sale, which meet the definition of loans and receivables, from the category of available for sale financial assets to the category of loans and receivables, if the Group has the intent and the ability to hold such financial assets in foreseeable future or until their maturity.

If the financial asset with a given maturity is reclassified, prior gains and losses associated with such asset, recognized in other comprehensive income, are amortized in the profit or loss throughout the remaining period until maturity, using the effective interest rate method. Any differences between such new amortized cost and embedded amount is amortized throughout the period remaining until the maturity of such asset using the effective interest rate method, similar to premium or discount amortization.

The Group allows the reclassification of financial assets classified as financial assets measured at fair value through profit or loss, if extraordinary circumstances occur, i.e. events that are unusual and highly unlikely to recur in the near term.

Such financial assets are reclassified at fair value as at reclassification date. The gains or losses recognized in the profit or loss before such reclassification cannot be reversed. The fair value of financial assets, as at reclassification date, is recognized as its new cost or its new amortized cost.

Impairment of financial assets – principles applied until 31 December 2017

Assets measured at amortized cost – loans and advances
At each balance sheet date the Group assesses whether there is any objective evidence ('triggers') that loans and advances or financial assets held-to-maturity measured at amortized cost ('loan exposures') are impaired. In the process of impairment assessment the Group considers all loan exposures, irrespective of the level of risk of particular loan exposures or a group of loan exposures.

The Group splits the loan exposures into individually significant exposures and individually insignificant exposures.
In respect to exposures assessed individually the Group applies the following list of impairment triggers:

- overdue in repayment of principal, interest or credit fees more than 90 days and more than 2 working days in case of exposure towards banks including credit transactions and reverse repo/sell-buy-backs,
- significant financial difficulties of borrower (including loss of job or other events that could impact on ability to repayment in case of individuals). Significant financial difficulties of economic entity mean financial standing that could threaten timely repayment of liabilities towards the Group, especially when incurred losses have consumed equity in 50%, excluding projects where losses have been assumed or where external financial support exists (in form of injections to the equity, granting a loan, warranty/guarantee by related company or other third party, conversion of loan into equity, issuance of shares/bonds),
- restructuring, if it is related with granting an advantage, due to economic or legal reasons resulted from financial difficulties of the borrower, that in other circumstances the Group would not give. The advantage leads to reduction of the Group's loan exposure, and may include: reduction of the interest rate, temporary interest accruing holidays, cancelling a part or total of the exposures, in this interest or principal,

- lowering by the well-known and accepted rating agency a borrower's rating or country's rating – country of domicile or rating of debt securities issued by the borrower by at least 4 notches including modifiers within one year. Decrease in credit rating alone is not an evidence of impairment trigger but could be confirmation of impairment if it is analyzed together with other available information,
- significant worsening of rating or scoring analysis results. It means the decrease in rating by 4 notches in the scale and at the same time move to non-performing category based only on rating criterion, excluding situations of rating deterioration resulted from seasonality of activity and excluding impact of classification in RMT ('Risk Management Tool') on rating. Decrease in rating alone is not an evidence of impairment trigger but could be confirmation of impairment if it is analyzed together with other available information,
- the Group has started an execution process or has been informed about execution towards borrower,
- the debt/loan is questioned by the borrower including commencement of legal proceedings,
- the debt/loan has been due as the credit agreement has been terminated,
- the motion for borrower's bankruptcy has been filled in the court or legal proceedings has been instituted,
- disappearance of active market for given credit exposure resulted from financial difficulties of debtor. This impairment trigger could refer to financial instruments listed on stock exchanges, when due to significant deterioration in financial standing of issuer (eventually bankruptcy), the liquidity of assets trading is so low that reliable price fixing is not possible,
- receivership has been established or debtor has stopped/suspended its activity,
- unknown place of stay and not disclosed assets of the borrower.

In respect to exposures assessed collectively the Group applies the following list of impairment triggers:

- overdue in repayment of principal, interest or credit fees greater or equal to 90 days,
- significant financial difficulties of debtor, including loss of job or other events that could impact on ability to repayment,
- unknown place of stay and not disclosed assets of the retail debtor or sole trader.

The Group classifies the exposure as past due in case the borrower has failed to make payment on the principal and/or interest in the contractual maturity date. The Group presents the whole amount of exposure as past due, regardless of whether the delay of payment affects the whole exposure, or only part of it (installment).

The number of days past due for receivables paid by installments is assumed as the period from the date of maturity of the earliest installment, when the repayment is delayed.

In case of identification of impairment triggers for at least one of loan exposures of the borrower, all loan exposures of such borrower are assessed for impairment.

For all loans exposures, which are impaired, the Group measures the amount of impairment allowance as the difference between the loan exposure's carrying amount and the present value of estimated future cash flows, discounted at the loan exposure's original effective interest rate. The carrying amount of the loan exposure is reduced through use of an allowance account. The amount of the impairment loss is recognized in profit or loss. If, in a subsequent period, the amount of impairment loss decreases, then the previously recognized impairment loss is reversed by adjusting an allowance account. The amount of the reversal is recognized in profit or loss.

For all individually significant exposures, which are impaired as at balance sheet date, the Group measures the impairment allowance (impairment loss) as part of individual assessment. The individual assessment is carrying out by the Group's employees and consists of individual verification of the impairment occurrence and projection of future cash flows from foreclosure less costs for obtaining and selling the collateral or other resources. The Group compares the estimated future cash flows applied for measurement of individual impairment allowances with the actual cash flows on a regular basis.

For all individually insignificant exposures, which are impaired as at balance sheet date, the Group measures the impairment allowance (impairment loss) as part of collective assessment. Each exposure assessed collectively is grouped based on similar credit risk characteristics on the basis of the borrower's type, the product's type, past-due status or other relevant factors impacting on the debtor's ability to pay all amounts due according to the contractual terms. The future cash flows are estimated on the basis of historical data of cash flows and historical loss experience for exposures with credit risk characteristics similar to those in the group (for example, the value of the real estate taken as the collateral for the mortgage). Historical data, when necessary, are adjusted on the basis of current data to remove the effects of conditions in the historical period that do not exist currently. The recovery rates ('RR') and the methodology and assumptions used for estimating future cash flows for particular groups of loan exposures are reviewed regularly.

For all loan exposures, for which no impairment triggers have been identified, the Group measures the allowance for losses incurred, but not reported ('IBNR'). As part of IBNR assessment the Group estimates the loss resulting from events not reported as at balance sheet date and for which no impairment triggers have been identified, but the events occurred prior to balance sheet date and the loss was incurred. While estimating the IBNR, it is assumed that there is a several-months period from the date of emergence of objective impairment trigger to the date of its reporting, i.e. loss identification period ('LIP'). The value of LIP parameter is estimated on the basis of statistical analysis using the historical data. The Group applies different loss identification periods for different groups of loan exposures, taking into account the client's segment, the product's type and the collateral. The update of LIP parameter is carrying out at least once a year.

The IBNR is measured based on the likelihood that the debtor will be unable to meet its obligations during loss identification period ('PD_LIP') multiplied by impairment loss estimated analogously like collective allowance for value of exposure at default ('EAD'). The value of EAD parameter is estimated on the basis of historical data.

The Group estimates the value of PD_LIP parameter using the PD measured by Basel models with relevant transformation taking into account the shortening of loss identification period for applied length of LIP and Point-in-Time adjustment. Within the transformation the Group calibrates the values of PD parameter to the most up to date realized PD_LIP values once a month. The values of PD_LIP as estimated reflect the current economic conditions the best. The model applied to measurement of PD_LIP is of 'Point-In-Time' type.

The values of LIP, PD_LIP, EAD and RR applied for IBNR measurement as well as the methodology and assumptions used for estimating such parameters for particular groups of loan exposures are reviewed regularly.

Financial assets available for sale

When a decline in the fair value of an available for sale financial asset has been recognized directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that has been recognized directly in equity is removed from equity and recognized in the income statement. The amount of the cumulative loss transferred to the income statement is the difference between the acquisition cost (net of any principal repayment and amortization) and the current fair value. If, in a subsequent period, the fair value of a debt instrument classified as available for sale increases and the increase can be objectively related to an event occurring after the impairment loss was recognized in profit or loss, the impairment loss is reversed, with the amount of the reversal recognized in the income statement.

If there is objective evidence that an impairment loss has been incurred on an unquoted equity instrument that is not carried at fair value because its fair value cannot be reliably measured, the amount of the impairment loss is measured as the difference between the carrying amount of the financial asset and the present value of estimated future cash flows discounted at the current market rate of return for a similar financial asset.

Off-balance sheet commitments

The provisions for off-balance sheet commitments is measured as the difference between the expected value of balance sheet exposure arising from granted off-balance sheet commitment and the present value of estimated future cash flows from that balance sheet exposure at the date of impairment identification. The expected value of balance sheet exposure arising from granted off-balance sheet commitment is measured using the credit conversion factor ('CCF'), estimated on the basis of historical data.

The values of CCF applied for measurement of provisions for off-balance sheet commitments as well as the methodology and assumptions used for estimating such parameters for particular groups of loan exposures are reviewed regularly.

The Group estimates the future cash flows as part of individual assessment or collective assessment depending on classification of particular off-balance sheet commitments as individually significant exposures or individually insignificant exposures.

Derivative financial instruments and hedge accounting

The Group acquires the derivative financial instruments: currency transactions (spot, forward, currency swap and currency options, CIRS), exchange rate transactions (FRA, IRS, CAP), derivative transactions based on security prices, indices of stocks and commodities. Derivative financial instruments are initially recorded at fair value as at the transaction date and subsequently re-measured at fair value at each balance sheet date. The fair value is established on the basis of market quotations for an instrument traded in an active market, as well as on the basis of valuation techniques, including models using discounted cash flows and options valuation models, depending on which valuation method is appropriate.

Positive valuation of derivative financial instruments is presented in the statement of financial position in the line 'Derivative financial instruments (held for trading)' or 'Hedging instruments' on an asset side, whereas the negative valuation - 'Derivative financial instruments (held for trading)' or 'Hedging instruments' on a liabilities side. For financial instruments with an embedded derivative component, if the whole or part of the cash flows related to such a financial instrument changes in a way similar to what would be the case with the embedded derivative instrument on its own, then the embedded derivative instrument is reported separately from the basic contract.

This occurs under the following conditions:

- the financial instrument is not included in assets held for trading or in assets designated at fair value through the profit or loss the revaluation results of which are reflected in the financial income or expense of the reporting period,
- the nature of the embedded instrument and the related risks are not closely tied to the nature of the basic contract and to the risks resulting from it,
- a separate instrument characteristics of which correspond to the features of the embedded derivative instrument would meet the definition of the derivative instrument,
- it is possible to reliably establish the fair value of the embedded derivative instrument.

In case of contracts that are not financial instruments with a component of an instrument meeting the above conditions the built-in derivative instrument is classified in accordance with assets or liabilities of derivatives financial instruments with respect to the income statement in accordance with derivative financial instruments valuation principles.

The method of recognition of the changes in the fair value of an instrument depends on whether a derivative instrument is classified as held for trading or is designated as a hedging item under hedge accounting.

The changes in fair value of the derivative financial instruments held for trading are recognized in the income statement.

The Group designates some of its derivative instruments as hedging items in applying hedge accounting. The Bank decided to take advantage of the choice which gives IFRS 9 and continues to apply the hedge accounting requirements of IAS 39. This decision will apply to all hedging relationships, for which the Bank applies and will apply hedge accounting in the future. The Group implemented fair value hedge accounting as well as cash flow hedge accounting.

Fair value hedge accounting principles

Changes in the measurement to fair value of financial instruments indicated as hedged positions are recognized - in the part ensuing from hedged risk - in the income statement. In the remaining part, changes in the carrying amount are recognized in accordance with the principles applicable for the given class of financial instruments.

Changes in the fair market valuation of derivative financial instruments, indicated as hedging positions in fair value hedge accounting, are recognized in the profit or loss in the same caption, in which the gains/losses from change in the value of hedged positions are recognized.

Notes to the financial statements (cont.)

(in PLN thousand)

Interest income on derivative instruments hedging interest positions hedged is presented as interest margin.

The Group ceases to apply hedge accounting, when the hedging instrument expires, is sold, dissolved or released (the replacement of one hedging instrument with another or extension of validity of given hedging instrument is not considered an expiration or release, providing such replacement or extension of validity is a part of a documented hedging strategy adopted by given unit), or does not meet the criteria of hedge accounting or the Group ceases the hedging relation.

An adjustment for the hedged risk on hedged interest position is amortized in the income statement at the point of ceasing to apply hedge accounting.

Cash flow hedge accounting principles

Changes in the fair value of the derivative financial instruments indicated as cash flow hedging instruments are recognized:

- directly in the caption ‘Revaluation reserves’ in the part constituting the effective hedge,
- in the income statement in the line ‘Result on financial assets and liabilities held for trading’ in the part representing ineffective hedge.

The amounts accumulated in the ‘Revaluation reserves’ are transferred to the income statement in the period, in which the hedge is reflected in the income statement and are presented in the same lines as individual components of the hedged position measurement, i.e. the interest income from hedging derivatives in cash flow hedge accounting is recognized in the interest result, whereas gains/losses from foreign exchange revaluation are presented in the foreign exchange gains (losses).

The Group ceases to apply hedge accounting when the hedging instrument expires or is sold, or if the Group revokes the designation. In such cases, the accumulated gains or losses related to such hedging item, initially recognized in ‘Revaluation reserves’, if the hedge was effective, are still presented in equity until the planned transaction was closed and recognized in the income statement.

If the planned transaction is no longer probable, the cumulative gains or losses recognized in ‘Revaluation reserves’ are transferred to the income statement for the given period.

Financial liabilities

The Group classifies financial liabilities other than financial guarantee contracts and loan commitments, as measured at amortized cost or at fair value through profit or loss.

Financial liabilities valued at amortized cost include liabilities to banks and customers, loans taken by the Group and issued own debt securities.

Subordinated liabilities

Subordinated liabilities are measured at amortized cost using the effective interest rate method.

De-recognition of financial instruments from the statement of financial position

Financial assets are derecognized when the contractual rights to the cash flows from the financial assets expire or when the Group transfers the contractual rights to receive the cash flows in a transaction in which substantially all risk and rewards of ownership of the financial asset are transferred.

The Group derecognizes a credit or a loan receivable, or its part, when it is sold. Additionally, the Group writes-off a receivable against the corresponding impairment provision (completely or partially) when the debt redemption process is completed and when no further cash flows from the given receivable are expected. Such cases are documented in compliance with the current tax regulations.

Accumulated profits and losses that have been recognized in other comprehensive income from equity instruments designated to be measured at fair value through other comprehensive income are not recognized in the profit and loss account when these financial instruments are removed from the balance sheet.

The Group derecognizes a financial liability, or its part, when the liability expires. The liability expires when the obligation stated in the agreement is settled, redeemed or the period for its collection expires.

Repo and reverse-repo agreements
Repo and reverse-repo transactions, as well as sell-buy back and buy-sell back transactions are classified as sales or purchase transactions of securities with the obligation of repurchase or resale at an agreed date and price.

Sales transactions of securities with the repurchase obligation granted (repo and sell-buy back) are recognized as at transaction date in amounts due to other banks or amounts due to customers from deposits depending upon the counterparty to the transaction. Securities purchased in reverse-repo and buy-sell back transactions are recognized as loans and receivables from banks or as loans and receivables from customers, depending upon the counterparty to the transaction.

The difference between the sale and repurchase price is recognized as interest income or expense, and amortized over the contractual life of the contract using the effective interest rate method.

5.6 Valuation of other items in the Group's consolidated statement of financial position

Intangible assets

Goodwill
Goodwill is defined as a surplus of the purchasing price over the fair value of the assets, liabilities and contingent liabilities of the acquired subsidiary, associate or a unit under joint control. Goodwill at initial recognition is carried at purchase price reduced by any accumulated impairment losses. Impairment is determined by estimating the recoverable value of the cash generating unit, to which given goodwill pertains.

If the recoverable value of the cash generating unit is lower than the carrying amount an impairment charge is made. Impairment identified in the course of such tests is not subject to subsequent adjustments.

Goodwill on acquisition of subsidiaries is presented in intangible assets and goodwill on acquisition of associates is presented under the caption 'Investments in associates'.

Other intangible assets
Intangible assets are assets controlled by the Group which do not have a physical form which are identifiable and represent future economic benefits for the Group directly attributable to such assets.
These assets include:

- computer software licenses,
- copyrights,
- costs of completed development works.

Intangible assets are initially carried at purchase price. Subsequently intangible assets are stated at cost less accumulated amortization and accumulated impairment losses.

Intangible assets with a definite useful life are amortized over their estimated useful life. Intangible assets with indefinite useful life are not amortized.
All intangible assets are reviewed on a periodical basis to verify if any significant impairment triggers occurred, which would require performing a test for impairment and a potential impairment charge.

As far as intangible assets with indefinite useful life and those still not put into service are concerned, impairment test is performed on a yearly basis and additionally when impairment triggers are identified.

Property, plant and equipment
Property, plant and equipment are defined as controlled non-current assets and assets under construction. Non-current assets include certain tangible assets with an expected useful life longer than one year, which are maintained for the purpose of own use or to be leased to other entities.

Property, plant and equipment are recognized at historical cost less accumulated depreciation and accumulated impairment write downs. Historical cost consists of purchase price or development cost and costs directly related to the purchase of a given asset.

Notes to the financial statements (cont.)

(in PLN thousand)

Each component of property, plant and equipment, the purchase price or production cost of which is significant compared to the purchase price or production cost of the entire item is a subject to separate depreciation. The Group separates the initial value of property, plant and equipment into its significant parts.
Subsequent expenditures relating to property plant and equipment are capitalized only when it is probable that such expenditures will result in future economic benefits to the Group, and the cost of such expenses can be reliably measured.

Service and maintenance costs of property, plant and equipment are expensed in the reporting period in which they have been incurred.

Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset form part of the cost of that asset. Other borrowing costs are recognized as an expense.

Depreciation and amortization
Depreciation expense for property, plant and equipment and investment properties and the amortization expense for intangible assets are calculated using straight line method over the expected useful life of an asset. Depreciated value is defined as the purchase price or cost to develop a given asset, less residual value of the asset. Depreciation rates and residual values of assets, determined for balance-sheet purposes, are subject to regular reviews, with results of such reviews recognized in the same period.

The statement of financial position depreciation and amortization rates applied to property, plant and equipment, investment properties and intangible assets are as follows:

a) depreciation rates applied for non-current assets

Buildings and structures and cooperative ownership rights to residential premises and cooperative ownership rights to commercial premises	1.5% – 10.0%
Technical equipment and machines	4.5% – 30.0%
Vehicles	7% – 20.0%

b) amortization rates for intangible assets

Software licenses, copyrights	12.5% – 50.0%
Costs of completed development projects	33.3%
Other intangibles	20% – 33.3%

c) depreciation rates for investment properties

Buildings and structures	1.5% – 10.0%

Land, non-current assets under construction and intangible assets under development are not subject to depreciation and amortization.
Depreciation and impairment deductions are charged to the income statement in the item ‘Depreciation and amortization’.

Investment properties
Investment properties assets are recognized initially at purchase cost, taking the transaction costs into consideration. Upon initial recognition, investment property assets are measured using the purchasing price model.

Investment property assets are derecognized from the statement of financial position when disposed of, or when such investment property is permanently decommissioned and no future benefits are expected from its sale. Any gains or losses resulting from de-recognition of an investment property are recognized in the income statement in the period when such de-recognition occurred.

Notes to the financial statements (cont.)

(in PLN thousand)

Non-current assets held for sale and discontinued operations
Non-current assets held for sale include assets, the carrying amount of which is to be recovered by way of resale and not from their continued use. The only assets classified as held for sale are those available for immediate sale in their present condition, and the sale of which is highly probable, i.e. when the decision has been made to sell a given asset, an active program to identify a buyer has been launched and the divestment plan is completed. Moreover, such assets are offered for sale at a price which approximates its present fair value, and it is expected that the sale will be recognized as completed within one year from the date of such asset is reclassified into this category.

Non-current assets held for sale are recognized at the carrying amount or at fair value reduced by the cost of such assets, whichever is lower. Assets classified in this category are not subject to depreciation.

A discontinued operation is a component of the Group's business which constitutes a separate line of business or a geographical area of operations, which was sold, made available for sale or to be disposed, or is a subsidiary acquired exclusively with a view to re-sale. Classification as a discontinued operation occurs on disposal or when the operation meets the criteria to be classified as held for sale. When an operation is classified as held for sale, the comparative figures in the income statement are represented as if the operation had been discontinued from the beginning of the comparative period.

Leases
The Group is a party to leasing contracts on the basis of which it grants a right to use a non-current asset or an intangible asset for an agreed period of time in return for payment.

The Group is also a party to leasing contracts under which it receives a right to use a non-asset or an intangible asset for an agreed period of time from another party in return for a payment.

Operating leases
In the case of leasing contracts entered into by the Group acting as lessor, the leased asset is presented in the Group's statement of financial position, since there is no transfer to the lessee of essentially all risks and benefits resulting from the asset.

In the case of lease agreements, entered into by the Group as lessee, the leased asset is not recognized in the Group's statement of financial position.

The entire amount of charges from operating leases is recognized in the profit or loss on a straight line basis, throughout the leasing period.

Finance leases

The Group as lessor
In the lease agreements, where essentially all risks and benefits relating to the ownership of an asset are transferred, the leased asset is no longer recognized in the statement of financial position of the Group. However, receivables are recognized in the amount equal to the present value of the minimum lease payments. Lease payments are split into the financial income and the reduction of receivables balance in order to maintain a fixed interest rate on the outstanding liability.

Lease payments from agreements, which do not meet the conditions of finance lease agreements are recognized as revenues in the income statement using the straight-line method over the life of the lease.

The Group as lessee
For lease agreements in which in principle all risks and benefits relating to ownership of the leased assets are transferred to the Group, the leased asset is recognized as a non-current asset and simultaneously a liability is recognized in the amount equal to the present value of minimum lease payments as at the date of commencement of the lease. Lease payments are split into costs of lease charges and a reduction of liabilities in order to maintain a fixed interest rate on the outstanding liability. Financial costs are recognized directly in the income statement.

Non-current assets subject to finance lease agreements are depreciated in the same way as other non-current assets. However, if it is uncertain whether the ownership of the asset subject of the contract will be transferred then the asset is depreciated over the shorter of the expected useful life or the initial period of lease.

Lease charges from agreements that do not fulfill the criteria for finance lease agreements are recognized as costs in the income statement on a straight line basis over the lease period.

Provisions

The provisions are recognized when the Group has a present obligation (legal or constructive) resulting from the past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation and a reliable estimate can be made of the amount of the obligation.

If the effect of the time value of money is material, the amount of a provision is established by discounting forecasted future cash flows to the present value, using the discount rate reflecting current market estimates of the time value of money and the possible risk associated with the obligation.

The provisions include the provisions relating to long-term employee benefits, in this those measured by an actuary and provisions for restructuring costs. The provision for restructuring costs is recognized when the general recognition criteria for provisions and detailed criteria for recognition of provisions for restructuring cost under IAS 37 'Provisions, contingent liabilities and contingent assets' are met. The amount of employment restructuring provision is calculated by the Group on the basis of the best available estimates of direct outlays resulting from restructuring activities, which are not connected with the Group's current activities.

The provisions are charged to the income statement, except for actuarial gains and losses from the measurement of the defined benefit plans obligations, which are recognized in other comprehensive income.

Deferred income and accrued expenses (liabilities)

This caption includes primarily commission income settled using the straight line method and other income charged in advance, that will be recognized in the income statement in the future periods.

Accrued expenses include accrued costs resulting from services provided for the Group by counterparties which will be settled in future periods, accrued payroll and other employee benefits (including annual and Christmas bonuses, other bonuses and awards and accrued holiday pay).

Deferred income and accrued expenses are presented in the statement of financial position under the caption 'Other liabilities'.

Government grants

The Group recognizes government grants when there is reasonable assurance that it will comply with any conditions attached to the grant and the grant will be received. Government grants are recognized in profit or loss in the periods in which the related expenses are recognized which the grants are intended to compensate. For the settlement of the grant, the Group uses the income method. Government grants related to assets are presented in the statement of financial position of the Group as a reduction in the carrying value of the asset.

Equity of the Group

Equity is comprised of the capital and funds created by the companies of the Group in accordance with the binding legal regulations and the appropriate laws and Articles of Association. Equity also includes retained earnings. Subsidiaries' equity line items, other that share capital, are added to the relevant equity line items of the parent company, in the proportion of the Group's interest.

The equity of the Group includes only those parts of the subsidiaries' equity which were created after the date of purchase of shares or stocks by the parent entity.

The Group equity consists of the following:

a) share capital - applies only to the capital of the Bank as the parent entity and is presented at nominal value specified in the Articles of Association and in the entry in the Enterprises Registry,
b) 'issue premium' - surplus generated during share issues over the nominal value of such issues, remaining after the issue costs are covered. Moreover, this item also includes a change in the value of minority shares, ensuing from an increase of the share of the Parent entity in Bank's share capital,

c) the general banking risk fund is established at Bank Pekao S.A. in keeping with the Banking Act dated 29 August 1997 from profit after tax,

d) other reserve capital utilized for the purposes defined in the Statute is created from appropriations of profits,

e) revaluation reserve includes the impact of revaluation of debt financial instruments measured at fair value through other comprehensive income, revaluation or sale of investments in equity instruments designated at fair value through other comprehensive income, revaluation of derivative instruments hedging cash flows, remeasurements of the defined benefit liabilities and the value of deferred tax for items classified as temporary differences, recognized as valuation allowance. In the statement of financial position, the valuation allowance is presented as net value,

f) other capital:
- other supplementary capital, established in keeping with provisions under the Articles of Association of companies from profit appropriations,
- capital components:
  - bonds convertible to shares - includes the fair value of financial instruments issued as part of transactions settled in equity instruments,
  - provision for purchase of parent entity stocks,
- brokerage activity fund for stock broking operations, carried out by Bank Pekao S.A.,
- retained earnings from prior periods includes undistributed profit and uncovered losses generated/incurred in prior periods by subsidiaries consolidated full method,
- net profit/loss which constitutes profit/loss presented in the income statement for the relevant period. Net profit is after accounting for income tax.

Non - controlling interests

Non - controlling interests are defined as the equity in a subsidiary not attributable, directly or indirectly, to the Bank.

Bank's Pekao S.A. phantom shares-settled share-based payment transaction

The cost of transactions settled with employees in phantom shares is measured by reference to the fair value of the liability as of the balance sheet date.

The fair value of the liability is estimated based upon the Bank's shares price on the (WSE) as of the balance sheet date and expected number of phantom shares to which full rights will be acquired.

The cost of phantom share-based payments is recognized in personnel expenses together with the accompanying increase in the value of liabilities towards employees presented in 'Provisions'.

The accumulated cost recognized for transactions settled in phantom shares for each balance sheet date until the vesting date reflects the extent of elapse of the vesting period and the number of rights to shares the rights to which – in the opinion of the Bank's Management Board for that date based on best available estimates of the number of phantom shares – will be eventually vested.

5.7 Income tax

Income tax expense comprises current and deferred tax. The income tax expense is recognized in the income statement excluding the situations when it is recognized directly in equity. The current tax is the tax payable of the Group entities on their taxable income for the period, calculated based on binding tax rates, and any adjustment to tax payable in respect of previous years. The receivables resulting from taxes are disclosed if the Group's companies has sufficient certainty that they exist and that they will be recovered.

Deferred tax assets and deferred tax liabilities are calculated, using the balance sheet method, on temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes. Deferred income tax is determined using tax rates based on legislation enacted or substantively enacted at the balance sheet date and expected to apply when the deferred tax asset or the deferred tax liability is realized.

A deferred tax asset is recognized for negative temporary differences to the extent that it is probable that taxable profit will be available against which the deductible temporary difference can be utilized.

A deferred tax liability is calculated using the balance sheet method based on identification of positive temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for tax purposes.

5.8 Other

Contingent liabilities and commitments

The Group enters into transactions which are not recognized in the statement of financial position as assets or liabilities, but which result in contingent liabilities and commitments. Contingent liabilities are characterized as:

- a potential obligation the existence of which will be confirmed upon occurrence or non-occurrence of uncertain future events that are beyond the control of the Group (e.g. litigations),
- a current obligation which arises as a result of past events but is not recognized in the statement of financial position as it is improbable that it will result in an outflow of benefits to settle the obligation or the amount of the obligation cannot be reliably measured (mainly: unused credit lines and guarantees and letters of credit issued).

Financial guarantees

Financial guarantees are measured at the higher of:

- the amount of the loss allowance or
- the amount initially recognised less the cumulative amount of income recognised in accordance with the principles of IFRS 15.

5.9 New standards, interpretations and amendments to published standards that have been approved and published by the European Union and are effective on or after 1 January 2018

IFRS 9 'Financial Instruments' and other changes

The Bank has adopted International Financial Reporting Standard 9 'Financial Instruments' with a date of transition of 1 January 2018.

Set out below are disclosures relating to the impact of the adoption of IFRS 9 and other changes on the Bank as at 1 January 2018.

Notes to financial statements (cont.)

(in PLN thousand)

The table below discloses at the time of the first application of IFRS 9 comparison of categories for the measurement of financial assets and their carrying amounts in accordance with IAS 39 and new categories of measurement of financial assets and their carrying amounts in accordance with IFRS 9.

	IAS 39 MEASUREMENT CATEGORY	IFRS 9 MEASUREMENT CATEGORY	IAS 39 CARRYING AMOUNT	IFRS 9 CARRYING AMOUNT
Cash and due from Central Bank	Loans and advances (Amortised cost)	Amortised cost	5 236 318	5 236 107
Loans and advances to banks	Loans and advances (Amortised cost)	Amortised cost	2 627 327	2 627 117
Financial assets held for trading	Held for trading (Fair value through profit or loss)	Fair value through profit or loss (mandatory)	1 730 416	1 730 416
Derivative financial instruments	Held for trading (Fair value through profit or loss)	Fair value through profit or loss (mandatory)	1 349 047	1 349 047
Hedging derivatives	Held for trading (Fair value through profit or loss)	Fair value through profit or loss (mandatory)	259 396	259 396
Loans and advances to customers	Loans and advances (Amortised cost)	Amortised cost	113 330 806	112 284 080
Loans and advances to customers	Loans and advances (Amortised cost)	Fair value through profit or loss (mandatory)	363 079	365 137
Loans and advances to customers	Loans and advances (Amortised cost)	Fair value through other comprehensive income	1 597 449	1 555 964
Receivables from finance leases	Loans and advances (Amortised cost)	Amortised cost	4 351 352	4 347 855
Investments (placement) securities – debt securities	Loans and advances (Amortised cost)	Amortised cost	7 550 390	7 543 879
Investments (placement) securities – debt securities	Loans and advances (Amortised cost)	Fair value through other comprehensive income	5 107 583	5 096 743
Investments (placement) securities – debt securities	Held to maturity (Amortised cost)	Amortised cost	1 620 367	1 620 237
Investments (placement) securities – debt securities	Held to maturity (Amortised cost)	Fair value through other comprehensive income	1 861 424	1 887 731
Investments (placement) securities – debt securities	Available for sale (Fair value through other comprehensive income)	Amortised cost	2 229 193	2 336 021
Investments (placement) securities – debt securities	Available for sale (Fair value through other comprehensive income)	Fair value through other comprehensive income	31 047 397	31 047 397
Investments (placement) securities – equity instruments	Available for sale (Fair value through other comprehensive income)	Fair value through profit or loss (mandatory)	52 376	52 376
Investments (placement) securities – equity instruments	Available for sale (Fair value through other comprehensive income)	Fair value through other comprehensive income	95 065	264 444
Other assets	Loans and advances (Amortised cost)	Amortised cost	948 231	941 722
FINANCIAL ASSETS			**181 357 216**	**180 545 669**

The application of IFRS 9 for the first time by the Bank had no impact on the classification and measurement of financial liabilities.

Notes to financial statements (cont.)

(in PLN thousand)

The table below presents the reconciliation of the carrying amounts of financial assets by category of measurement under IAS 39 with the carrying amounts of these items according to the category of their measurement under IFRS 9, on the date of the first application of IFRS 9, taking into account other changes introduced from 1 January 2018.

		CARRYING AMOUNT 31.12.2017 IAS 39	RECLASSIFICATIONS	REMEASUREMENTS	CARRYING AMOUNT 01.01.2018 IFRS 9
	FINANCIAL ASSETS				
	AMORTISED COST				
	Cash and due from Central Bank				
	Opening balance	5 236 318			
	Remeasurement			(211)	
	Closing balance				**5 236 107**
	Loans and advances to banks				
	Opening balance	2 627 327			
	Remeasurement			(210)	
	Closing balance				**2 627 117**
	Loans and advances to customers				
	Opening balance	127 949 307			
	Remeasurement			(1 046 726)	
A	Reclassification to fair value through other comprehensive income		(1 597 449)		
B	Reclassification to fair value through profit or loss		(363 079)		
C	Reclassification to investments (placement) securities at fair value through other comprehensive income		(5 107 583)		
D	Reclassification to investments (placement) securities at amortised cost		(7 550 390)		
	Closing balance				**112 284 080**
	Receivables from finance leases				
	Opening balance	4 351 352			
	Remeasurement			(3 497)	
	Closing balance				**4 347 855**
	Investments (placement) securities				
	Opening balance	3 481 791			
	Remeasurement			100 187	
D	Reclassification from loans and advances to customers		7 550 390		
E	Reclassification from available for sale		2 229 193		
F	Reclassification to fair value through other comprehensive income		(1 861 424)		
	Closing balance				**11 500 137**
	Other assets				
	Opening balance	948 231			
	Remeasurement			(6 509)	
	Closing balance				**941 722**
	MEASURED AT AMORTISED COST TOTAL				**136 937 018**

Notes to financial statements (cont.)

(in PLN thousand)

		CARRYING AMOUNT 31.12.2017 IAS 39	RECLASSIFICATIONS	REMEASUREMENTS	CARRYING AMOUNT 01.01.2018 IFRS 9
	AVAILABLE FOR SALE				
	Investments (placement) securities				
	Opening balance	33 424 031			
E	Reclassification to amortised cost		(2 229 193)		
G	Reclassification to fair value through other comprehensive income – debt securities		(31 047 397)		
H	Reclassification to fair value through other comprehensive income – equity instruments		(95 065)		
I	Reclassification to fair value through profit or loss – equity instruments		(52 376)		
	Closing balance				**-**
	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME				
	Investments (placement) securities (debt securities)				
	Opening balance	-			
	Remeasurement			15 467	
G	Reclassification from available for sale		31 047 397		
C,F	Reclassification from amortised cost		6 969 007		
	Closing balance				**38 031 871**
	Investments (placement) securities (equity instruments)				
	Opening balance	-			
	Remeasurement			169 379	
H	Reclassification from available for sale		95 065		
	Closing balance				**264 444**
	Loans and advances to customers				
	Opening balance	-			
	Remeasurement			(41 485)	
A	Reclassification from amortised cost		1 597 449		
	Closing balance				**1 555 964**
	MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME TOTAL				**39 852 279**

Notes to financial statements (cont.)

(in PLN thousand)

		CARRYING AMOUNT 31.12.2017 IAS 39	RECLASSIFICATIONS	REMEASUREMENTS	CARRYING AMOUNT 01.01.2018 IFRS 9
	FAIR VALUE THROUGH PROFIT OR LOSS				
	Financial assets held for trading	1 730 416			**1 730 416**
	Derivative financial instruments (held for trading)	1 349 047			**1 349 047**
	Hedging instruments	259 396			**259 396**
	Loans and advances to customers				
	Opening balance	-			
	Remeasurement			2 058	
B	Reclassification from amortised cost		363 079		
	Closing balance				**365 137**
	Investments (placement) securities – equity instruments				
	Opening balance	-			
I	Reclassification from available for sale		52 376		
	Closing balance				**52 376**
	FAIR VALUE THROUGH PROFIT OR LOSS TOTAL				**3 756 372**

The following explains how the application of the new requirements for the classification of IFRS 9 led to the changes in the classification of certain financial assets held by the Bank as shown in the table above.

Loans and advances to customers

A) Certain loans and advances to customers (syndicated loans) are measured at fair value through other comprehensive income because they are classified into a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets. Before applying the requirements of IFRS 9, these loans were measured at amortized cost, in accordance with IAS 39.

B) Some of the loans and advances to customers are classified as measured at fair value through profit or loss, as their contractual cash flows failed to meet the ‘solely payments of principal and interest’ (SPPI) requirement, due to the leverage that increases the volatility of the contractual cash flows. This applies mainly to student loans, loans with subsidies of the Agency for Restructuring and Modernization of Agriculture and several corporate exposures. Before applying the requirements of IFRS 9, these items were measured at amortized cost, in accordance with IAS 39.

The remaining loans and advances to customers held to collect contractual cash flows and meeting the SPPI criteria are still measured at amortized cost.

Corporate and municipal debt securities

C) The Bank assessed the business model for corporate and municipal securities and identified that part of the portfolio of these securities meets the criteria of the business model, whose objective is achieved by both collecting contractual cash flows and selling financial assets. Therefore, certain securities from this portfolio were classified as measured at fair value through other comprehensive income. Before applying the requirements of IFRS 9, these items were measured at amortized cost, in accordance with IAS 39 and presented as loans and advances to customers.

D) The remaining part of the portfolio, which is held to collect contractual cash flows, has been reclassified to the item Securities and is measured at amortized cost. Before applying the requirements of IFRS 9, these items were presented as Loans and advances to customers, as they were classified in the loans and receivables category in accordance with IAS 39.

Investments (placement) securities

E) The Bank assessed the business model for investment securities, which are mostly held to collect cash flows and sell, and identified that in relation to certain of these securities its past practice has been to hold to collect the contractual cash flows and the intention of the Bank remains unchanged. Therefore, the Bank assessed that the appropriate business model for these securities is a model whose objective is to hold to collect contractual cash flows and reclassified them to the amortized cost measurement. Previously, these securities were classified as available for sale and measured at fair value through other comprehensive. As at 30 June 2018, the fair value of securities reclassified from measured at fair value through equity to those measured at amortized cost amounted to PLN 2 242 291 thousand. If these securities had not been reclassified, the Group would have recognized in other comprehensive income a net profit of PLN 22 481 thousand in the first half of 2018.

F) The Bank assessed the business model for held-to-maturity securities and, due to the intention to sell certain securities in this portfolio, reclassified securities to be measured at fair value through other comprehensive income, because it assessed that the appropriate business model for these securities is the model whose objective is achieved by both collecting contractual cash flows and selling financial assets. Before applying the requirements of IFRS 9, these items were measured at amortized cost, in accordance with IAS 39. Other securities previously classified as held to maturity were classified as amortized cost.

G) Other securities previously classified as available for sale were classified as at fair value through other comprehensive income, without the change in the measurement method.

Equity instruments

H) Certain long-term equity instruments in the Bank's portfolio have been irrevocably designated in accordance with IFRS 9 to measure at fair value through other comprehensive income. Prior to the application of IFRS 9, these instruments were measured at fair value through other comprehensive income or at cost, as the Bank stated that it was not possible to reliably measure their fair value. IFRS 9 abolished the possibility of measuring them at cost. Changes in the fair value of such securities will no longer be reclassified to profit or loss when they are disposed of.

I) Other equity instruments that, in accordance with IAS 39, were classified as available for sale and were measured at fair value through other comprehensive income, and were not irrevocably designated for measurement at fair value through other comprehensive income, were reclassified to fair value through profit or loss.

Notes to financial statements (cont.)

(in PLN thousand)

The following table reconciles the prior period's closing impairment allowance measured in accordance with the IAS 39 and provisions for off-balance sheet liabilities calculated in accordance with IAS 37 as at 31 December 2017 to the opening balance of expected credit losses in accordance with IFRS 9 as at 1 January 2018

	IAS 39 MEASUREMENT CATEGORY	IFRS 9 MEASUREMENT CATEGORY	IMPAIRMENT ALLOWANCE IAS 39/IAS 37 31.12.2017	RECLASSIFICATIONS (*)	REMEASUREMENTS	IMPAIRMENT ALLOWANCEIFRS 9 01.01.2018
Cash and due from Central Bank	Loans and advances (Amortised cost)	Amortised cost	-	-	211	211
Loans and advances to banks	Loans and advances (Amortised cost)	Amortised cost	16 637	4 494	210	21 341
Loans and advances to customers	Loans and advances (Amortised cost)	Amortised cost	5 247 726	3 222 963	794 084	9 264 773
Loans and advances to customers	Loans and advances (Amortised cost)	Fair value through profit or loss (mandatory)	4 057	3 869	(7 926)	-
Loans and advances to customers	Loans and advances (Amortised cost)	Fair value through other comprehensive income	8 901	-	9 258	18 159
Receivables from finance leases	Loans and advances (Amortised cost)	Amortised cost	173 715	-	3 497	177 212
Investments (placement) securities – debt securities	Loans and advances (Amortised cost)	Amortised cost	84 535	(31 680)	4 517	57 372
Investments (placement) securities – debt securities	Loans and advances (Amortised cost)	Fair value through other comprehensive income	12 979	-	9 209	22 188
Investments (placement) securities – debt securities	Held to maturity (Amortised cost)	Amortised cost	-	-	130	130
Investments (placement) securities – debt securities	Held to maturity (Amortised cost)	Fair value through other comprehensive income	-	-	179	179
Investments (placement) securities – debt securities	Available for sale (Fair value through other comprehensive income)	Amortised cost	-	-	196	196
Investments (placement) securities – debt instruments	Available for sale (Fair value through other comprehensive income)	Fair value through other comprehensive income	-	-	1 944	1 944
Investments (placement) securities – equity instruments	Available for sale (Fair value through other comprehensive income)	Fair value through profit or loss (mandatory)	-	-	-	-
Investments (placement) securities – equity instruments	Available for sale (Fair value through other comprehensive income)	Fair value through other comprehensive income	1 119	(1 119)	-	-
Other assets	Loans and advances (Amortised cost)	Amortised cost	95 992	5 926	6 509	108 427
Provisions for undrawn credit facilities and guarantees issued	Provisions	Provisions	236 909	-	35 837	272 746
		IMPAIRMENT ALLOWANCES TOTAL	**5 882 570**	**3 204 453**	**857 855**	**9 944 878**

(*) The item 'Reclassifications' includes changes in the level of impairment allowance that occurred in correspondence with the corresponding change in the gross carrying amount, including: (1) increase in impairment allowances as a result of adjusting the gross carrying amount to IFRS 9 (presentation change resulting in increase in the gross carrying amount by recognition of contractual interest accrued in full against receivables in Stage 3 and, as a consequence, an analogous increase in the level of impairment allowance) and (2) a decrease in impairment allowance for loans and advances classified as POCI, which as at the initial recognition are recognized at fair value and do not show impairment allowance. As a result, the changes described above did not affect the level of the Bank's retained earnings.

Notes to financial statements (cont.)

(in PLN thousand)

The table below presents the net impact (gross impact less tax effect) of the first application of IFRS 9 and other changes on the equity

	IMPACT OF FIRST TIME ADOPTION OF IFRS 9 AT 01.01.2018		
	BEFORE TAX	DEFERRED TAX	NET
REVALUATION RESERVES			
Revaluation reserves at 31.12.2017 under IAS 39	**(69 788)**	**13 260**	**(56 528)**
Remeasurement of debt securities / loans and advances to customers reclassified from Amortised cost to Fair value through other comprehensive income	(47 899)	9 101	(38 798)
Remeasurement of debt securities reclassified from available for sale to amortised cost	105 030	(19 956)	85 074
Reclassification of equity instruments from available for sale to fair value through profit or loss	(3 232)	614	(2 618)
Remeasurement of equity instruments reclassified from available for sale to fair value through other comprehensive income	192 999	(34 973)	158 026
Recognition of ECL for debt securities / loans and advances to customers at fair value through other comprehensive income	42 470	(8 069)	34 401
Revaluation reserves at 01.01.2018 under IFRS 9	**219 580**	**(40 023)**	**179 557**
RETAINED EARNINGS			
Retained earnings at 31.12.2017 under IAS 39	**(38 225)**	**7 263**	**(30 962)**
Reclassification of equity instruments from available for sale to fair value through profit or loss	3 232	(614)	2 618
Remeasurement of equity instruments reclassified from available for sale to fair value through other comprehensive income	(23 619)	2 791	(20 828)
Remeasurement of loans and advances to customers mandatory at fair value through profit or loss	(5 868)	1 115	(4 753)
Recognition of ECL for financial assets and off-balance sheet commitments	(857 855)	152 352	(705 503)
Other changes	(277 665)	49 613	(228 052)
Retained earnings at 01.01.2018 under IFRS 9 and other changes	**(1 200 000)**	**212 520**	**(987 480)**
TOTAL IMPACT OF FIRST TIME ADOPTION OF IFRS 9 AND OTHER CHANGES ON EQUITY	**(872 407)**	**151 974**	**(720 433)**

Other changes presented in the table above result from changes made by the Group in the first half of 2018 in the method of recognizing selected commissions and provisions for holiday leave and recognition of the impact of these changes in the scope relating to previous years as a retained earnings as at 1 January 2018. The comparative data have not been restated due to the insignificant impact of the introduced changes on the Group's financial results.

Impact of IFRS 9 on capital adequacy

The Bank has decided to apply transitional arrangements specified in art. 473a of 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 as amended Regulation (EU) 2017/2395 of the European Parliament and of the Council of 12 December 2017 amending Regulation (EU) No 575/2013 as regards transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds and for the large exposures treatment of certain public sector exposures denominated in the domestic currency of any Member State.

The following table presents the impact of the adoption of IFRS 9 for the first time on capital adequacy with and without transitional arrangements:

	IMPACT OF IFRS 9 WITH TRANSITIONAL ARRANGEMENTS	IMPACT OF IFRS 9 WITHOUT TRANSITIONAL ARRANGEMENTS
Total capital requirement	9 552 335	9 540 398
Total own funds (Tier 1 and Tier 2)	20 637 781	19 795 360
Total Capital Ratio (%)	17.3%	16.6%

IFRS 15 'Revenue from Contracts with Customers'

IFRS 15 'Revenue from Contracts with Customers' has been approved for application in the European Union by the Regulation of the European Commission No. 2016/1905 of 22 September 2016 and applies to financial statements issued for financial periods beginning on 1 January 2018 or later.

IFRS 15 shall be applied to all contracts with customers, except lease contracts within the scope of IAS 17 'Leases', financial instruments and other contractual rights or obligations within the scope of IFRS 9 Financial Instruments, IFRS 10 'Consolidated Financial Statements', IFRS 11 'Joint Arrangements', IAS 27 'Separate Financial Statements' and IAS 28 'Investments in Associates and Joint Ventures', insurance contracts within the scope of IFRS 4 'Insurance Contracts'.

The core principle of this Standard is that the Group shall recognise revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the Group expects to be entitled in exchange for those goods or services.

In accordance with IFRS 15, the transfer of goods and services is based on the concept of transferring control to the customer, which may occur at a point in time (delivery of goods, service) or over time (for example during the service or during the creation of the ordered goods).

IFRS 15 defines a five-step revenue recognition model:

Step 1: Identifying the contract with a client

This step consists in making sure that contracts concluded with clients (in writing, orally or in accordance with other customary business practices) are valid and constitute actual transactions. According to IFRS 15, a contract with a client is a contract if it creates enforceable rights and obligations and the following criteria are met:

- the parties to the contract have approved the contract and are committed to perform their respective obligations,
- each party's rights regarding the goods or services to be transferred can be identified,
- the payment terms for the goods or services to be transferred can be identified
- the contract has commercial substance,
- it is probable that the Group will collect the consideration to which it will be entitled in exchange for the goods or services that will be transferred to the customer. In evaluating whether collectability of an amount of consideration is probable, the Group shall consider the customer's ability and intention to pay that amount of consideration when it is due.

In some cases the Group shall combine two or more contracts entered into at or near the same time with the same customer (or related parties of the customer) and account for the contracts as a single contract if one or more of the following criteria are met:

- the contracts are negotiated as a package with a single commercial objective,
- the amount of consideration to be paid in one contract depends on the price or performance of the other contract,
- the goods or services promised in the contracts (or some goods or services promised in each of the contracts) are a single performance obligation.

Step 2: Identifying performance obligations

The performance obligation corresponds to the promised goods or services (or their package), which may be perceived as 'distinct' from other goods or services promised in the contract.

A good or service that is promised to a customer is distinct if both of the following criteria are met:

- the customer can benefit from the good or service either on its own or together with other resources that are readily available to the customer (the determinant of this criterion is regular sale by the Group of goods or services separately),
- the entity's promise to transfer the good or service to the customer is separately identifiable from other promises in the contract.

Notes to financial statements (cont.)

(in PLN thousand)

Step 3: Determining the transaction price
The transaction price is the amount of consideration which the Group expects to receive in exchange for the transfer of goods or services. Determining the transaction price can be complicated if the contract provides for variable consideration (eg bonuses, penalties, refunds, clauses assuming price change, etc.), significant share of financing costs, non-cash consideration or amounts due to the buyer.

Variable consideration is included in the transaction price only when there is a high probability that its inclusion will not result in a 'significant reversal of revenue' in the future as a result of revaluation. A significant reversal of the revenue approach takes place when the subsequent change in the estimated amount of variable consideration results in a significant decrease in the accumulated value of recognized revenues from a given customer. The variable remuneration includes each variable contractual amount, including for example performance bonuses, penalties, discounts, rebates.

Step 4: Allocating the transaction price to distinct performance obligations
If the contract contains more than one distinct performance obligation, the Group allocates the transaction price to individual obligation based on their stand-alone selling prices.

If the transaction price includes a variable consideration, it should be analyzed whether this amount applies to all or only certain performance obligations contained in the contract. If the criteria included in the standard do not meet the variable consideration as referring only to certain obligations, it should be allocated to all performance obligations included in the contract.

Step 5: Revenue recognition
Revenue is recognised revenue when (or as) the Group satisfies a performance obligation by transferring a promised good or service (ie an asset) to a customer. An asset is transferred when (or as) the customer obtains control of that asset. Therefore revenues are recognized either at a point in time or over time.

Control of an asset refers to the ability to direct the use of, and obtain substantially all of the remaining benefits from, the asset (ie good or service).

The Group transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognises revenue over time, if one of the following criteria is met:
- the customer simultaneously receives and consumes the benefits provided by the Group's performance as the Group performs,
- the Group's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced,
- the Group's performance does not create an asset with an alternative use to the Group and the Group has an enforceable right to payment for performance completed to date.

If a performance obligation is not satisfied over time the following indicators of the transfer of control should be considered to determine the point in time at which a customer obtains control of a promised asset:
- The Group has transferred physical possession of the asset,
- The Group has a present right to payment for the asset,
- The customer has accepted the asset,
- The customer has the significant risks and rewards of ownership of the asset,
- The customer has legal title to the asset.

The Group applies IFRS 15 from 1 January 2018. The Group analyzed the impact of implementing IFRS 15.

The analysis covered the following types of contracts with clients:
1. Agreements with card organizations regarding marketing and promotional activities and related to the development of card activities,
2. Lease agreements in which the Bank is the lessor and, in addition to the rental rent, agree with the client (tenant) how to settle the maintenance fees for maintenance of the property. In such contracts, the Bank buys and resells, for example, municipal services and electricity,
3. Contracts for cash transport services for clients,

Notes to financial statements (cont.)

(in PLN thousand)

4. Bank accounts contracts, in relation to fees and commissions that are not included in effective interest rate,
5. Credit and loan agreements, in relation to fees and commissions that are not included in effective interest rate,
6. Agreements regarding the intermediation in the sale of insurance products,
7. Agreements regarding the investment funds management.

The Group did not identify agreements with a variable uncertain consideration components or contracts for which the implementation of IFRS 15 could have a significant impact on the financial statements.

Other standards, interpretations and amendments to published standards that have been approved and published by the European Union and entered into force from or after 1 January 2018

STANDARD / INTERPRETATION	DESCRIPTION	IMPACT ASSESSMENT
IFRS 2 (amendment) 'Share-based Payment'	The amendments provide requirements on the accounting for: (a) the effects of vesting and non-vesting conditions on the measurement of cash-settled share-based payments, (b) share-based payment transactions with a net settlement feature for withholding tax obligations, and (c) a modification to the terms and conditions of a share-based payment that changes the classification of the transaction from cash-settled to equity-settled.	The standard's amendments did not have a material impact on its financial statements in the period of its first application.
IFRS 4 (amendment) 'Insurance Contracts'	The amendments address concerns arising from implementing the new financial instruments standard, IFRS 9, before implementing the replacement standard that the Board is developing for IFRS 4.	The standard's amendments did not have a material impact on its financial statements in the period of its first application.
IAS 40 (amendment) 'Investment Property'	Amendments to IAS 40 'Investment Property' - Transfers of Investment Property state that an entity shall transfer a property to, or from, investment property when, and only when, there is evidence of a change in use. A change of use occurs if property meets, or ceases to meet, the definition of investment property. A change in management's intentions for the use of a property by itself does not constitute evidence of a change in use. Amendments also state that the list of evidence in paragraph 57 was designated as non-exhaustive list of examples instead of the previous exhaustive list.	The standard's amendments did not have a material impact on its financial statements in the period of its first application.
IFRIC 22 'Foreign Currency Transactions and Advance Consideration'	Interpretation states that the date of the transaction, for the purpose of determining the exchange rate, is the date of initial recognition of the non-monetary prepayment asset or deferred income liability. If there are multiple payments or receipts in advance, a date of transaction is established for each payment or receipt.	The interpretation did not have a material impact on its financial statements in the period of its first application.
Improvements to IFRS 2014-2016	Amendments result from the annual improvement project of IFRS. Amendments relate to IFRS 1, IFRS 12 and IAS 28 and were introduced primarily with a view to removing inconsistencies and clarifying wording.	The standard's amendments did not have a material impact on its financial statements in the period of its first application.

Notes to financial statements (cont.)

(in PLN thousand)

5.10 New standards, interpretations and amendments to published standards that have been published by the International Accounting Standards Board (IASB) and approved by the European Union but are not yet effective

STANDARD / INTERPRETATION	DESCRIPTION	IMPACT ASSESSMENT
IFRS 9 (amendment) 'Financial Instruments'	Amendments to IFRS 9 - Prepayment Features with Negative Compensation – modify the existing requirements regarding termination rights in order to allow measurement at amortised cost (or, depending on the business model, at fair value through other comprehensive income) even in the case of negative compensation payments. Under the amendments, the sign of the prepayment amount is not relevant, i. e. depending on the interest rate prevailing at the time of termination, a payment may also be made in favour of the contracting party effecting the early repayment. The calculation of this compensation payment must be the same for both the case of an early repayment penalty and the case of an early repayment gain. Date of application: annual periods beginning on or after 1 January 2019.	The Group claims that the standard's amendments will not have a material impact on its financial statements in the period of its first application.
IFRS 16 'Leases'	Under IFRS 16 a lessee recognises a right-of-use asset and a lease liability. The right-of-use asset is treated similarly to other non-financial assets and depreciated accordingly. The lease liability is initially measured at the present value of the lease payments payable over the lease term, discounted at the rate implicit in the lease if that can be readily determined. If that rate cannot be readily determined, the lessee shall use their incremental borrowing rate. IFRS 16 defines a lease term as the noncancellable period for which the lessee has the right to use an underlying asset including optional periods when an entity is reasonably certain to exercise an option to extend (or not to terminate) a lease. As with IFRS 16's predecessor, IAS 17, lessors classify leases as operating or finance in nature. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of an underlying asset. Otherwise a lease is classified as an operating lease. For finance leases a lessor recognises finance income over the lease term, based on a pattern reflecting a constant periodic rate of return on the net investment. A lessor recognises operating lease payments as income on a straight-line basis or, if more representative of the pattern in which benefit from use of the underlying asset is diminished, another systematic basis. Date of application: annual periods beginning on or after 1 January 2019. Earlier application is permitted for entities that apply IFRS 15 Revenue from Contracts with Customers at or before the date of initial application of this Standard.	The Group did not use the option of early application of IFRS 16 and will apply the standard from 1 January 2019. As part of the implementation of the new standard, the Group commenced the assessment of contracts to identify whether the contract meets the definition of leasing and estimate of the leasing period. The new requirements eliminate nearly all off balance sheet accounting for lessees. The new standard requires lessees to recognise nearly all leases on the balance sheet which will reflect their right to use an asset for a period of time and the associated liability for payments. This will redefine many commonly used financial metrics. The Group plans to elect not to apply the new requirements to short-term leases and leases for which the underlying asset is of low value. In relation to the Group as a lessor - the accounting largely remains unchanged. However the Group might see an impact to its business model and lease products due to changes in needs and behaviours.

(in PLN thousand)

5.11 New standards, interpretations and amendments to published standards that have been published by the International Accounting Standards Board (IASB) and not yet approved by the European Union

STANDARD / INTERPRETATION	DESCRIPTION	IMPACT ASSESSMENT
IFRS 17 'Insurance Contracts'	The new standard requires insurance liabilities to be measured at a current fulfillment value and provides a more uniform measurement and presentation approach for all insurance contracts. These requirements are designed to achieve the goal of a consistent, principle-based accounting for insurance contracts. IFRS 17 supersedes IFRS 4 'Insurance Contracts' and related interpretations while applied. Date of application: annual periods beginning on or after 1 January 2021.	The Group claims that the new standard will not have a material impact on its financial statements in the period of its first application.
IAS 19 (amendment) 'Employee Benefits'	Amendments to IAS 19 'Employee Benefits' - Plan Amendment, Curtailment or Settlement – require to use the updated assumptions from this remeasurement to determine current service cost and net interest for the remainder of the reporting period after the change to the plan. Date of application: annual periods beginning on or after 1 January 2019.	The Group is currently analyzing the impact of those changes on the financial statements.
IAS 28 (amendment) 'Investments in Associates and Joint Ventures'	Amendments to IAS 28 - Long-term Interests in Associates and Joint Ventures - were introduced to clarify that an entity applies IFRS 9 including its impairment requirements, to long-term interests in an associate or joint venture that form part of the net investment in the associate or joint venture but to which the equity method is not applied. Amendments also delete paragraph 41 because the Board felt that it merely reiterated requirements in IFRS 9 and had created confusion about the accounting for long-term interests. Date of application: annual periods beginning on or after 1 January 2019.	The Group is currently analyzing the impact of those changes on the financial statements.
IFRIC 23 'Uncertainty over Income Tax Treatments'	It may be unclear how tax law applies to a particular transaction or circumstance, or whether a taxation authority will accept a company's tax treatment. IAS 12 Income Taxes specifies how to account for current and deferred tax, but not how to reflect the effects of uncertainty. IFRIC 23 provides requirements that add to the requirements in IAS 12 by specifying how to reflect the effects of uncertainty in accounting for income taxes. Date of application: annual periods beginning on or after 1 January 2019.	The Group is currently analyzing the impact of those changes on the financial statements.
Improvements to IFRS 2015-2017	Amendments to various standards resulting from the annual improvement project of IFRS (IFRS 3, IFRS 11, IAS 12 and IAS 23) primarily with a view to removing inconsistencies and clarifying wording. The amendments clarify that: a company remeasures its previously held interest in a joint operation when it obtains control of the business (IFRS 3), a company does not remeasure its previously held interest in a joint operation when it obtains joint control of the business (IFRS 11), a company accounts for all income tax consequences of dividend payments in the same way (IAS 12), and a company treats as part of general borrowings any borrowing originally made to develop an asset when the asset is ready for its intended use or sale (IAS 23). Date of application: annual periods beginning on or after 1 January 2019.	The Group is currently analyzing the impact of those changes on the financial statements.

(in PLN thousand)

6. Accounting estimates

The preparation of interim financial statements in accordance with IFRS requires the Management Board of the Bank to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expenses.

The estimates at balance sheet day reflect market conditions on that date (e.g. market prices, interest rates, exchange rates).

Although the estimates are based on the best knowledge concerning current conditions and activities of the Group, the actual results may differ from those estimates.

During the six months period ended 30 June 2018 the most significant estimates are as follows:

- impairment of financial assets and off-balance sheet commitments,
- fair value measurement for derivative financial instruments and unquoted debt securities.

In connection with the implementation of IFRS 9, the principles of estimating the impairment of financial assets and off-balance sheet liabilities have changed in relation to the principles used in the financial statements for the year ended 31 December 2017. The new rules are described in Note 7.1 'Credit risk'.

The principles of estimating fair value of derivative instruments and unquoted debt securities measured at fair value did not change.

7. Risk management

7.1 Credit risk

The process of credit risk management, credit risk mitigation methods and rating models did not change significantly compared to those described in the consolidated financial statements of Bank Pekao S.A. Group for the year ended on 31 December 2017. The selected quantitative data in these areas are presented below. More extensive information regarding the impairment allowance is presented additionally in connection with the implementation of IFRS9 from the beginning of 2018.

Rating models – data as at 30 June 2018
The distribution of rated portfolio for individual client segment – mortgage loans

RATING CLASS	RANGE OF PD	30.06.2018						
		CARRYING AMOUNT						%PORTFOLIO
		STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	
				INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
1	0.00% <= PD < 0.06%	8 599 405	1 951 612	-	3 241	-	10 554 258	20.4%
2	0.06% <= PD < 0.19%	3 984 848	1 462 949	-	2 263	-	5 450 060	10.5%
3	0.19% <= PD < 0.35%	17 882 592	5 445 492	-	5 010	-	23 333 094	45.2%
4	0.35% <= PD < 0.73%	6 366 793	3 039 057	-	4 355	-	9 410 205	18.2%
5	0.73% <= PD < 3.50%	552 467	1 051 763	-	12 709	-	1 616 939	3.1%
6	3.50% <= PD < 14.00%	121 893	468 982	-	25 885	-	616 760	1.2%
7	14.00% <= PD < 100.00%	12 366	639 517	-	88 674	-	740 557	1.4%
Total		**37 520 364**	**14 059 372**	**-**	**142 137**	**-**	**51 721 873**	**100.0%**

(in PLN thousand)

The distribution of rated portfolio for individual client segment – consumer loans

RATING CLASS	RANGE OF PD	30.06.2018						
		CARRYING AMOUNT						%PORTFOLIO
		STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	
				INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
1	0.00% <= PD < 0.09%	716 806	98 032	-	255	-	815 093	7.5%
2	0.09% <= PD < 0.18%	1 489 862	148 178	-	301	-	1 638 341	15.0%
3	0.18% <= PD < 0.39%	2 487 209	236 681	-	1 900	-	2 725 790	25.0%
4	0.39% <= PD < 0.90%	2 357 673	169 991	-	3 546	-	2 531 210	23.2%
5	0.90% <= PD < 2.60%	1 514 934	167 892	-	4 697	-	1 687 523	15.5%
6	2.60% <= PD < 9.00%	766 750	153 111	-	8 584	-	928 445	8.5%
7	9.00% <= PD < 30.00%	220 972	135 277	-	12 630	-	368 879	3.4%
8	30.00% <= PD < 100.00%	52 342	123 028	-	26 788	-	202 158	1.9%
Total		**9 606 548**	**1 232 190**	**-**	**58 701**	**-**	**10 897 439**	**100.0%**

The distribution of rated portfolio for non-financial corporate client segment

RATING CLASS	RANGE OF PD	30.06.2018						
		CARRYING AMOUNT						%PORTFOLIO
		STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	
				INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
1	0.00% <= PD < 0.15%	348 099	6 513	-	-	-	354 612	1.7%
2	0.15% <= PD < 0.27%	1 801 305	90 775	-	-	-	1 892 080	9.2%
3	0.27% <= PD < 0.45%	2 481 811	269 030	-	-	-	2 750 841	13.4%
4	0.45% <= PD < 0.75%	4 153 414	195 645	-	-	-	4 349 059	21.1%
5	0.75% <= PD < 1.27%	4 437 862	319 741	-	-	-	4 757 603	23.1%
6	1.27% <= PD < 2.25%	2 399 921	618 408	-	-	-	3 018 329	14.7%
7	2.25% <= PD < 4.00%	616 352	472 121	-	-	-	1 088 473	5.3%
8	4.00% <= PD < 8.50%	1 140 792	846 358	-	-	-	1 987 150	9.7%
9	8.50% <= PD < 100.00%	150 595	186 876	38 278	125	-	375 874	1.8%
Total		**17 530 151**	**3 005 467**	**38 278**	**125**	**-**	**20 574 021**	**100.0%**

For specialized lending, the Bankadopts slotting criteria approach within internal rating method which uses supervisory categories in the process of assigning risk weigh category.

Notes to financial statements (cont.)

(in PLN thousand)

Distribution of the portfolio exposure to specialized lending

SUPERVISORY CATHEGORY	30.06.2018						
	CARRYING AMOUNT						%PORTFOLIO
	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
High	1 081 044	51 570	-	-	-	1 132 614	20.9%
Good	3 649 019	-	-	-	-	3 649 019	67.5%
Satisfactory	614 942	12 323	-	-	-	627 265	11.6%
Low	-	-	-	-	-	-	0.0%
Total	**5 345 005**	**63 893**	**-**	**-**	**-**	**5 408 898**	**100.0%**

Division of loans and advances to customers for covered and not covered by internal rating models

	30.06.2018
Covered by internal rating model:	83 193 333
Mortgage loans	51 721 873
Consumer loans	10 897 439
Corporate loans	20 574 021
Specialized lending exposures	5 408 898
Other, not covered by internal rating model	28 902 027
Total loans and advances to customers subject to impairment (*)	**117 504 258**

(in PLN thousand)

Classification of exposures to debt securities according to Fitch ratings as at 30 June 2018

RATING	CARRYING AMOUNT						%PORTFOLIO
	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
DEBT SECURITIES MEASURED AT AMORTISED COST							
A+ to A-	4 290 163	-	-	-	-	4 290 163	40.0%
No rating	6 386 137	-	31 143	-	5 669	6 422 949	60.0%
Gross carrying amount	**10 676 300**	**-**	**31 143**	**-**	**5 669**	**10 713 112**	**100.0%**
Impairment allowance	(34 103)	-	(31 143)	-	-	(65 246)	-
Carrying amount	**10 642 197**	**-**	**-**	**-**	**5 669**	**10 647 866**	**-**
DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME							
AAA	936 219	-	-	-	-	936 219	3.0%
A+ to A-	21 396 408	-	-	-	-	21 396 408	69.6%
BBB+ to BBB-	50 952	-	-	-	-	50 952	0.2%
No rating	8 371 602	-	-	-	-	8 371 602	27.2%
Carrying amount	**30 755 181**	**-**	**-**	**-**	**-**	**30 755 181**	**100.0%**
Impairment allowance (*)	(29 671)	**-**	**-**	**-**	**-**	(29 671)	**-**
DEBT SECURITIES HELD FOR TRADING							
A+ to A-						1 251 579	94.8%
BBB+ to BBB-						6 141	0.5%
No rating						61 730	4.7%
Carrying amount						**1 319 450**	**100.0%**

(*) The impairment allowance for debt securities measured at fair value through other comprehensive income is included in the 'Revaluation reserve' item and does not reduce the carrying amount.

(in PLN thousand)

Classification of exposures to derivative financial instruments according to Fitch ratings as at 30 June 2018

	DERIVATIVES HELD FOR TRANDING			HEDGING DERIVATIVES			TOTAL	%PORTFOLIO
	BANKS	OTHER FINANCIAL INSTITUTIONS	NON-FINANCIAL ENTITIES	BANKS	OTHER FINANCIAL INSTITUTIONS	NON-FINANCIAL ENTITIES		
AA+ to AA-	33 017	-	-	-	-	-	33 017	2.4%
A+ to A-	343 774	48 963	-	33 112	-	-	425 849	30.8%
BBB+ to BBB-	188 915	41	13 734	4 764	-	-	207 454	15.0%
BB+ to BB-	1 391	-	-	-	-	-	1 391	0.1%
B+ to B-	1 402	-	-	-	-	-	1 402	0.1%
No rating	129 531	233 267	242 048	3 397	103 203	-	711 446	51.6%
Total	**698 030**	**282 271**	**255 782**	**41 273**	**103 203**	**-**	**1 380 559**	**100.0%**

Rating models – comparative data as of 31 December 2017 IAS 39

The Group has adopted International Financial Reporting Standard 9 'Financial Instruments' with a date of transition of 1 January 2018. The Group decided to take advantage of the exemption allowing it not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes. IFRS 9 also significantly amended other standards dealing with financial instruments such as IFRS 7 'Financial instruments: Disclosures'. Disclosures for the comparative period are a repetition of disclosures made in previous periods.

The distribution of rated portfolio for individual client segment (excluding impaired loans) – mortgage loans

RATING CLASS	RANGE OF PD	31.12.2017	
		CARRYING AMOUNT	%PORTFOLIO
1	0.00% <= PD < 0.06%	10 308 122	21.1%
2	0.06% <= PD < 0.19%	5 220 016	10.7%
3	0.19% <= PD < 0.35%	21 828 654	44.8%
4	0.35% <= PD < 0.73%	8 464 383	17.4%
5	0.73% <= PD < 3.50%	1 553 153	3.2%
6	3.50% <= PD < 14.00%	627 941	1.3%
7	14.00% <= PD < 100.00%	722 811	1.5%
Total		**48 725 080**	**100.0%**

The distribution of rated portfolio for individual client segment (excluding impaired loans) – consumer loans

RATING CLASS	RANGE OF PD	31.12.2017	
		CARRYING AMOUNT	%PORTFOLIO
1	0.00% <= PD < 0.09%	763 055	7.4%
2	0.09% <= PD < 0.18%	1 597 102	15.5%
3	0.18% <= PD < 0.39%	2 555 301	24.7%
4	0.39% <= PD < 0.90%	2 423 887	23.5%
5	0.90% <= PD < 2.60%	1 603 023	15.5%
6	2.60% <= PD < 9.00%	854 202	8.3%
7	9.00% <= PD < 30.00%	335 767	3.2%
8	30.00% <= PD < 100.00%	194 236	1.9%
Total		**10 326 573**	**100.0%**

Notes to financial statements (cont.)

(in PLN thousand)

The distribution of rated portfolio for non-financial corporate client segment (excluding impaired loans)

RATING CLASS	RANGE OF PD	31.12.2017	
		CARRYING AMOUNT	%PORTFOLIO
1	0.00% <= PD < 0.15%	618 103	3.0%
2	0.15% <= PD < 0.27%	1 400 964	6.9%
3	0.27% <= PD < 0.45%	2 802 868	13.7%
4	0.45% <= PD < 0.75%	6 073 391	29.7%
5	0.75% <= PD < 1.27%	3 468 286	17.0%
6	1.27% <= PD < 2.25%	2 494 294	12.2%
7	2.25% <= PD < 4.00%	1 244 813	6.1%
8	4.00% <= PD < 8.50%	2 246 694	11.0%
9	8.50% <= PD < 100.00%	84 549	0.4%
Total		**20 433 962**	**100.0%**

For specialized lending, the Groupadopts slotting criteria approach within internal rating method which uses supervisory categories in the process of assigning risk weigh category.

Distribution of the portfolio exposure to specialized lending (excluding impaired loans)

SUPERVISORY CATHEGORY	31.12.2017	
	CARRYING AMOUNT	%PORTFOLIO
High	1 105 911	15.3%
Good	4 863 113	67.1%
Satisfactory	1 271 661	17.5%
Low	7 080	0.1%
Total	**7 247 765**	**100.0%**

Division of loans and advances to customers for covered and not covered by internal rating models

	31.12.2017
Loans with no impairment:	**129 764 165**
Loans to individuals:	**62 073 320**
Covered by internal rating model:	59 051 653
Mortgage loans	48 725 080
Consumer loans	10 326 573
Other, not covered by internal rating model	3 021 667
Loans to corporates:	**67 690 845**
Covered by internal rating model:	20 433 962
Specialized lending exposures	7 247 765
Debt securities, not covered by internal rating model	12 657 973
Repo transactions, not covered by internal rating model	-
Other, not covered by internal rating model	27 351 145
Impaired loans	**2 536 250**
Total loans and advances to customers (*)	**132 300 415**

(*) Loans and advances to customers include receivables from financial leases.

Notes to financial statements (cont.)

(in PLN thousand)

Classification of exposures to debt securities according to Standard & Poor's ratings as at 31 December 2017

RATING	DEBT SECURITIES				
	HELD FOR TRADING	AVAILABLE FOR SALE	HELD TO MATURITY	REPO TRANSACTIONS (***)	TOTAL
AA+ to AA-	-	722 151	-	-	722 151
A+ to A-	1 646 758	20 835 674	3 450 338	492 419	26 425 189
no rating	79 100	11 718 765 (*)	31 453 (**)	-	11 829 318
Total	**1 725 858**	**33 276 590**	**3 481 791**	**492 419**	**38 976 658**

(*) Including NBP bills in an amount of PLN 11 066 168 thousand.
(**) Including NBP bills in an amount of PLN 31 453 thousand.
(***) Fair value of debt securities purchased in the reverse repo transactions.

Classification of exposures to derivative financial instruments according to Standard & Poor's ratings as at 31 December 2017

RATING	DERIVATIVES HELD FOR TRANDING			HEDGING DERIVATIVES			TOTAL
	BANKS	OTHER FINANCIAL INSTITUTIONS	NON-FINANCIAL ENTITIES	BANKS	OTHER FINANCIAL INSTITUTIONS	NON-FINANCIAL ENTITIES	
AAA	129	-	-	-	-	-	129
AA+ to AA-	59 784	-	-	-	-	-	59 784
A+ to A-	588 677	102 882	-	40 143	-	-	731 702
BBB+ to BBB-	40 019	-	-	-	-	-	40 019
no rating	224 868	66 941	265 747	36 653	182 600	-	776 809
Total	**913 477**	**169 823**	**265 747**	**76 796**	**182 600**	**-**	**1 608 443**

The description of the model for impairment allowance

Since 1 January 2018, the Group has recognized impairment allowance in accordance with the International Financial Reporting Standard no. 9 Financial Instruments. IFRS 9 assumes the calculation of impairment losses based on expected credit losses and taking into account forecasts and expected future economic conditions in the context of credit risk exposure assessment.

Expected credit loss model

The impairment model applies to financial assets classified, in accordance with the IFRS 9, as financial assets at amortized cost or at fair value through other comprehensive income, with the exception of equity instruments.

The impairment model in accordance with IFRS 9 is based on the allocation of exposure to one of the three stages, depending on credit quality changes compared to the initial recognition of assets in the accounting records. How to calculate the impairment loss depends on the stage:

STAGE	CLASSIFICATION CRITERION TO THE STAGE	THE METHOD OF CALCULATING THE IMPAIRMENT ALLOWANCE
Stage 1	Exposures for which no significant increase in credit risk has been identified since the initial recognition until the balance sheet date and no impairment was identified	12-month expected credit losses
Stage 2	Exposures for which a significant increase in credit risk has been identified since the initial recognition until the balance sheet date and no impairment was identified	Lifetime expected credit losses
Stage 3	Exposures for which impairment has been identified	

In addition, financial assets that were classified as POCI at the time of initial recognition are treated as POCI (i.e. purchased or originated credit-impaired) in all subsequent periods until they are derecognised. This rule applies even if, in the meantime, the asset has been healed. In other words, assets once recognized as POCI remain in this status regardless of future changes in estimates of their cash flows.

In the case of instruments with the POCI status, life-time expected credit losses are recognized throughout the lifetime of these instruments.

Calculation of expected credit losses
Calculation of expected credit losses in a lifetime horizon requires the application of multi-annual risk parameters.

For the purpose of calculating the credit loss in accordance with IFRS 9, the Group compares the cash flows that it should receive pursuant to the agreement with the borrower and the flows estimated by the Group that it expects to receive. The difference is discounted by the original effective interest rate, and in the case of POCI assets - the original effective interest rate adjusted for credit risk.

Expected credit losses are determined in the contractual maturity period with the exception of products meeting the criteria of IFRS 9 para. 5.5.20, for which the Group determines the expected losses in the period in which it is exposed to credit risk (ie in the economic maturity).

Methodology for calculating group parameters - PD, RR and EAD.
Multi-annual PD parameters are an assessment of the probability of a default event in the next annual intervals in the lifetime. The PD long-term curve for a given exposure depends on the current value of the 12M PD parameter (and the appropriate rating class) determined based on the internal PD models of the Group. In the estimation, the Group:

a) estimates unbiased PD parameters without taking into account additional margins of conservatism (IFRS 9, paragraph 5.5.17 (a)),
b) takes into account current and forecasted macroeconomic conditions (IFRS 9, paragraph 5.5.17 (c)).

The calculation of expected recovery rates (RR) is based on the ‘pool’ model, in which, within homogeneous groups, average monthly recoveries are calculated conditionally against the months since default (MSD). Homogeneous groups of accounts were separated on the basis of the following characteristics:

- the type of borrower,
- product type,
- ranges of the LTV parameter (for mortgages and housing loans).

As part of defined homogeneous groups, average monthly recovery rates are calculated, which consist of repayments and recoveries resulting from both the secured part and the unsecured exposure, weighted by the value of outstanding capital observed at the beginning of a given MSD.

For products for which a repayment schedule is available, the Group sets the exposure value at the moment of default (EAD, Exposure at Default) and principal at the moment of default (PAD, Principal at Default) in the lifetime (ie for future repayments) based on contractual payment schedules and taking into account the following effects:

- the effect of arrears on principal and interest installments related to the expected non-payment of the last installments prior to the occurrence of the default,
- the effect of arrears of payments (principal and interest) on the date of calculation of the,
- the effect of settlement of the EIR adjustment over time.

For products for which a repayment schedule is not available, the Group sets the long-term EAD and PAD using the CCF (Credit Conversion Factor) and PADf (PAD factor) parameters. The CCF parameter, which estimates the percentage utilization of the remaining part of the limit in the period of 12 months before the expected moment of the default event, is used to determine the expected value of PAD and EAD parameters in the 12M period from the reference date. The PADf parameter is used to determine the expected value of PAD and EAD parameters from 12M after the reference date to the maturity date of the account.

For exposures for which it is not possible to determine risk parameters based on internal models, the Group adopts an approach based on using parameters from other portfolios with similar characteristics.

The models and parameters used to calculate impairment allowance are periodically validated.

The low credit risk criterion
According to par. 5.5.10 IFRS 9 exposures that are considered as low risk credit exposures at the reporting date may remain in Stage 1, regardless of the scale of the relative credit deterioration from the initial recognition. According to par. B.5.5.22 of IFRS 9, the credit risk of a financial instrument is considered low when:

- the financial instrument has a low risk of default,
- the borrower has a strong capacity to meet its contractual cash flow obligations in the near term,
- adverse changes in the economic and business conditions in the long term may, but will not necessarily, reduce the ability of the borrower to fulfil its contractual cash flow obligations.

The Group applies a low credit risk criterion for three portfolios: exposures to banks, exposures to local government units and exposures to the State Treasury and the National Bank of Poland.

Financial assets with an identified significant increase in credit risk
Financial assets for which at the balance sheet date the Bank will identify a significant increase in credit risk from the initial recognition are classified in Stage 2. The Bank recognizes that for a given asset a significant increase in credit risk has been identified if a quantitative or qualitative criterion is met or if contractual payments are more than 30 days past due, where the occurrence of a given criterion is verified at the exposure level.

Quantitative criteria
Taking into account the requirements of the standard, the Group defined three basic characteristics of the quantitative model:

- the measure on the basis of which the allocation is made to stages,
- the significance of the deterioration of the credit quality,
- quantification of the level of significant deterioration.

The measure, on the basis of which the allocation to stages is made, was set by the Group as the ratio of:

- current credit risk assessment defined as lifetime PD in the horizon from the reporting date to the maturity date determined on the basis of the characteristics effective as at the reporting date,
- the original credit risk assessment defined as lifetime PD in the period from the reporting date to the maturity date determined on the basis of the characteristics applicable as at the date of initial recognition.

The assessment of a significant credit risk deterioration is carried out by comparing the observed value of a relative change in the risk assessment with the theoretical value, which is the threshold above which the Group considers that a significant deterioration in credit risk occurred.

The allocation threshold at the single exposure level is determined by a statistical model based, among others, on information on the credit risk assessment as of the date of the initial recognition and the time from the date of the initial recognition of the exposure.

Quality criteria
As a result of the monitoring process carried out by the Group, the qualitative criteria for the allocation to Stage 2 are identified, such as:

- a delay in repayment over 30 days (30 DPD),
- occurrence of forbearance status,
- exposure is on the Watchlist.

In addition to the above, the Group has defined a number of specific quality criteria for various types of portfolios, such as, inter alia, changes in the Group's internal rating specific to customers in a given segment, changes in supervisory classes for selected segments (eg specialized financing), warning signals identified in the monitoring system and credit risk management or the results of individual monitoring.

Financial assets with identified impairment

Financial assets for which at the balance sheet date the Group has identified occurrences of the default event are classified in Stage 3. The Group recognizes that for a given asset a default was identified if at least one of the following occurred:

- amount of arrears above the set materiality threshold for over 90 days,
- exposure during the restructuring process,
- individual impairment trigger.

For SME and corporate segments, default is identified at the customer level, whereas for the retail segment at the customer / product group level. The criterion of days and amounts of delays is also defined at the level of identification. Similarly, if for any of the contracts under the aggregated group there is a default condition, all contracts in this group are treated as default.

The Group applies a six-month quarantine period effective from the moment all defaults cease to exist.

Taking into account expectations regarding future macroeconomic conditions

IFRS 9 requires the Group to take into account expectations regarding the macroeconomic situation in the calculation of expected credit losses. As required by IFRS 9, par. 5.5.4, the Group adjusts risk parameters to take into account forecasted forward-looking macroeconomic information (such as: GDP, unemployment rate, WIBOR, foreign exchange rates, inflation), for portfolios for which it has identified a dependency. The source of information on the values of macroeconomic factors are forecasts prepared by the Group's analysts.

Notes to the financial statements (cont.)

(in PLN thousand)

The tables below present the changes in impairment allowances and gross carrying amount of financial assets not measured at fair value through profit or loss by class of financial assets:

	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT		
LOANS AND ADVANCES TO BANKS MEASURED AT AMORTISED COST						
GROSS CARRYING AMOUNT						
GROSS CARRYING AMOUNT AS AT 1.01.2018	**2 626 260**	**1 071**	**21 014**	**113**	**-**	**2 648 458**
Transfer to Stage 1	150	(149)	-	(1)	-	-
Transfer to Stage 2	(141)	179	-	(38)	-	-
Transfer to Stage 3	(3)	(48)	-	51	-	-
New / purchased / granted financial assets	1 471 046	-	-	-	-	1 471 046
Financial assets derecognised, other than write-offs	(872 888)	(288)	-	(31)	-	(873 207)
Financial assets written off (*)	-	-	(4 943)	-	-	(4 943)
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	256 962	(7)	(6 723)	(10)	-	250 222
GROSS CARRYING AMOUNT AS AT 30.06.2018	**3 481 386**	**758**	**9 348**	**84**	**-**	**3 491 576**
IMPAIRMENT ALLOWANCE						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**213**	**-**	**21 127**	**-**	**-**	**21 340**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	361	-	-	-	-	361
Financial assets derecognised, other than write-offs	(171)	-	-	-	-	(171)
Financial assets written off (*)	-	-	(4 943)	-	-	(4 943)
Changes in level of credit risk (excluding the transfers between the Stages)	235	-	-	-	-	235
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	932	-	(6 836)	-	-	(5 904)
IMPAIRMENT ALLOWANCE AS AT 30.06.2018	**1 570**	**-**	**9 348**	**-**	**-**	**10 918**

(*) Including the value of contractual interest subject to partial write-off in the amount of PLN 4 943 thousand.

Notes to the financial statements (cont.)

(in PLN thousand)

	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT		
LOANS AND ADVANCES TO CUSTOMERS MEASURED AT AMORTISED COST						
GROSS CARRYING AMOUNT						
GROSS CARRYING AMOUNT AS AT 1.01.2018	**89 734 902**	**20 981 569**	**7 423 047**	**3 327 030**	**82 304**	**121 548 852**
Transfer to Stage 1	2 159 178	(2 154 384)	(525)	(4 269)	-	-
Transfer to Stage 2	(4 872 016)	5 080 423	(4 495)	(203 912)	-	-
Transfer to Stage 3	(264 821)	(429 197)	274 291	419 727	-	-
New / purchased / granted financial assets	15 119 037	-	-	-	-	15 119 037
Financial assets derecognised, other than write-offs	(9 167 812)	(2 119 511)	(165 443)	(123 363)	-	(11 576 129)
Financial assets written off (*)	-	-	(2 702 760)	(1 207 865)	(7)	(3 910 632)
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	615 810	59 303	673 892	(80 994)	4 288	1 272 299
GROSS CARRYING AMOUNT AS AT 30.06.2018	**93 324 278**	**21 418 203**	**5 498 007**	**2 126 354**	**86 585**	**122 453 427**
IMPAIRMENT ALLOWANCE						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**352 945**	**647 779**	**5 433 356**	**2 793 537**	**37 157**	**9 264 774**
Transfer to Stage 1	66 984	(64 765)	(51)	(2 168)	-	-
Transfer to Stage 2	(25 468)	123 793	(478)	(97 847)	-	-
Transfer to Stage 3	(24 440)	(55 040)	23 207	56 273	-	-
New / purchased / granted financial assets	85 743	-	-	-	-	85 743
Financial assets derecognised, other than write-offs	(49 149)	(24 501)	(24 811)	(1)	-	(98 462)
Financial assets written off (*)	-	-	(2 702 760)	(1 207 865)	(7)	(3 910 632)
Changes in level of credit risk (excluding the transfers between the Stages)	(67 083)	100 397	107 025	134 672	(7 444)	267 567
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	15 859	15 665	565 117	(47 040)	(6 208)	543 393
IMPAIRMENT ALLOWANCE AS AT 30.06.2018	**355 391**	**743 328**	**3 400 605**	**1 629 561**	**23 498**	**6 152 383**

(*) Including the value of contractual interest subject to partial write-off in the amount of PLN 3 694 252 thousand.

Notes to the financial statements (cont.)

(in PLN thousand)

	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT		
RECEIVABLES FROM FINANCE LEASES						
GROSS CARRYING AMOUNT						
GROSS CARRYING AMOUNT AS AT 1.01.2018	**4 090 628**	**208 808**	**51 859**	**173 772**	-	**4 525 067**
Transfer to Stage 1	125 306	(123 648)	-	(1 658)	-	-
Transfer to Stage 2	(85 815)	88 210	(1 668)	(727)	-	-
Transfer to Stage 3	(9 749)	(23 438)	14 283	18 904	-	-
New / purchased / granted financial assets	987 997	21 661	145	303	-	1 010 106
Financial assets derecognised, other than write-offs	(626 271)	(15 576)	(6 061)	(4 900)	-	(652 808)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	(14 660)	(8 164)	-	(6 537)	-	(29 361)
GROSS CARRYING AMOUNT AS AT 30.06.2018	**4 467 436**	**147 853**	**58 558**	**179 157**	**-**	**4 853 004**
IMPAIRMENT ALLOWANCE						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**4 342**	**3 125**	**26 966**	**142 779**	**-**	**177 212**
Transfer to Stage 1	2 154	(1 910)	-	(244)	-	-
Transfer to Stage 2	(189)	433	(181)	(63)	-	-
Transfer to Stage 3	(19)	(324)	-	343	-	-
New / purchased / granted financial assets	1 851	1 639	3 341	5 480	-	12 311
Financial assets derecognised, other than write-offs	(1 436)	(240)	(511)	(602)	-	(2 789)
Financial assets written off	-	-	-	-	-	
Changes in level of credit risk (excluding the transfers between the Stages)	(1 623)	(1 376)	(531)	(1 577)	-	(5 107)
Changes in models and risk parameters	-	-	-	(2 464)	-	(2 464)
Other, in this changes resulting from exchange rates	(1 229)	1 162	34	2 413	-	2 380
IMPAIRMENT ALLOWANCE AS AT 30.06.2018	**3 851**	**2 509**	**29 118**	**146 065**	**-**	**181 543**

Notes to the financial statements (cont.)

(in PLN thousand)

	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT		
LOANS AND ADVANCES TO CUSTOMERS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME						
CARRYING AMOUNT						
CARRYING AMOUNT AS AT 1.01.2018	**1 555 964**	**-**	**-**	**-**	**-**	**1 555 964**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	-	-	-	-	-	-
Financial assets derecognised, other than write-offs	(402 349)	-	-	-	-	(402 349)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	49 599	-	-	-	-	49 599
CARRYING AMOUNT AS AT 30.06.2018	**1 203 214**	**-**	**-**	**-**	**-**	**1 203 214**
IMPAIRMENT ALLOWANCE (*)						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**18 159**	**-**	**-**	**-**	**-**	**18 159**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	-	-	-	-	-	-
Financial assets derecognised, other than write-offs	(1 305)	-	-	-	-	(1 305)
Financial assets written off	-	-	-	-	-	-
Changes in level of credit risk (excluding the transfers between the Stages)	(3 022)	-	-	-	-	(3 022)
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	1	-	-	-	-	1
IMPAIRMENT ALLOWANCE AS AT 30.06.2018	**13 833**	**-**	**-**	**-**	**-**	**13 833**

(*) The impairment allowance for loans and advances to customers measured at fair value through other comprehensive income is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

Notes to the financial statements (cont.)

(in PLN thousand)

	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT		
DEBT SECURITIES MEASURED AT AMORTISED COST						
GROSS CARRYING AMOUNT						
GROSS CARRYING AMOUNT AS AT 1.01.2018	**11 527 804**	**-**	**30 031**	**-**	**-**	**11 557 835**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	711 909	-	-	-	-	711 909
Financial assets derecognised, other than write-offs	(1 634 843)	-	-	-	-	(1 634 843)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	71 430	-	1 112	-	5 669	78 211
GROSS CARRYING AMOUNT AS AT 30.06.2018	**10 676 300**	**-**	**31 143**	**-**	**5 669**	**10 713 112**
IMPAIRMENT ALLOWANCE						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**27 667**		**30 031**			**57 698**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	1 923	-	-	-	-	1 923
Financial assets derecognised, other than write-offs	(191)	-	-	-	-	(191)
Financial assets written off	-	-	-	-	-	-
Changes in level of credit risk (excluding the transfers between the Stages)	4 474	-	-	-	(5 669)	(1 195)
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	230	-	1 112	-	5 669	7 011
IMPAIRMENT ALLOWANCE AS AT 30.06.2018	**34 103**	**-**	**31 143**	**-**	**-**	**65 246**

Notes to the financial statements (cont.)

(in PLN thousand)

	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT		
DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME						
CARRYING AMOUNT						
CARRYING AMOUNT AS AT 1.01.2018	**38 031 871**	**-**	**-**	**-**	**-**	**38 031 871**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	65 678 117	-	-	-	-	65 678 117
Financial assets derecognised, other than write-offs	(73 535 055)	-	-	-	-	(73 535 055)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	580 248	-	-	-	-	580 248
CARRYING AMOUNT AS AT 30.06.2018	**30 755 181**	**-**	**-**	**-**	**-**	**30 755 181**
IMPAIRMENT ALLOWANCE (*)						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**24 311**					**24 311**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New / purchased / granted financial assets	11 831	-	-	-	-	11 831
Financial assets derecognised, other than write-offs	(803)	-	-	-	-	(803)
Financial assets written off	-	-	-	-	-	-
Changes in level of credit risk (excluding the transfers between the Stages)	(5 694)	-	-	-	-	(5 694)
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	26	-	-	-	-	26
IMPAIRMENT ALLOWANCE AS AT 30.06.2018	**29 671**	**-**	**-**	**-**	**-**	**29 671**

(*) The impairment allowance for debt securities measured at fair value through other comprehensive income is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the securities.

Noty objaśniające (cd.)

(in PLN thousand)

Forbearance measures

The identifying process of forborne exposures has not changed in relation to the one described in the consolidated financial statements of Bank Pekao S.A. Group for the year ended 31 December 2017.

Share of forborne exposures in the Group's loan portfolio

	30.06.2018						31.12.2017
	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
Loans and advances measured at amortised cost, including:	**92 968 889**	**20 674 874**	**2 097 401**	**496 793**	**63 087**	**116 301 044**	**127 949 307**
Forborne exposures gross	491 419	204 562	3 183 983	354 960	23 442	4 258 366	3 987 737
Loss allowance	(6 543)	(19 698)	(1 810 677)	(188 526)	(194)	(2 025 638)	(1 786 125)
Forborne exposures net	484 876	184 864	1 373 306	166 434	23 248	2 232 728	2 201 612
Loans and advances measured at fair value through other comprehensive income, including:	**1 203 214**	**-**	**-**	**-**	**-**	**1 203 214**	**X**
Forborne exposures	-	-	-	-	-	-	X
Loss allowance (*)	-	-	-	-	-	-	X
Loans and advances measured at fair value through profit or loss, including:						**335 242**	**X**
Forborne exposures						1 898	X
Leasing exposure measured at amortised cost, including:	**4 463 585**	**145 344**	**29 440**	**33 092**	**-**	**4 671 461**	**4 351 352**
Forborne exposures gross	4 152	5 243	28 961	4 912	-	43 268	49 104
Loss allowance	(10)	(64)	(6 646)	(3 110)	-	(9 830)	(9 079)
Forborne exposures net	4 142	5 179	22 315	1 802	-	33 438	40 025

(*) The impairment allowance for loans and advances to customers measured at fair value through other comprehensive income is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

CHF loans to individuals

Since 2003, Bank Pekao S.A. has not granted CHF loans for individuals. Almost the entire portfolio of CHF loans for individuals was granted before August 2006 by Bank BPH S.A. and then taken over by Bank Pekao S.A. as a result of the merger.

Notes to financial statements (cont.)

(in PLN thousand)

The table below presents the structure and quality of CHF loans for individuals.

Structure of CHF loans to individuals

	30.06.2018						31.12.2017
	STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED)		PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	TOTAL
			INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT			
Gross carrying amount, of which:	**224 845**	**3 021 053**	**71 275**	**130 944**	**737**	**3 448 854**	**3 467 081**
denominated in CHF	224 845	3 003 767	71 275	130 161	737	3 430 785	3 447 189
indexed to CHF	-	17 286	-	783	-	18 069	19 892
Impairment allowances, of which:	**(148)**	**(40 818)**	**(16 759)**	**(64 380)**	**(178)**	**(122 283)**	**(77 018)**
denominated in CHF	(148)	(40 716)	(16 759)	(64 052)	(178)	(121 853)	(76 732)
indexed to CHF	-	(102)	-	(328)	-	(430)	(286)
Carrying amount, of which:	**224 697**	**2 980 235**	**54 516**	**66 564**	**559**	**3 326 571**	**3 390 063**
denominated in CHF	224 697	2 963 051	54 516	66 109	559	3 308 932	3 370 457
indexed to CHF	-	17 184	-	455	-	17 639	19 606

As of 31 June 2018 the average LTV for CHF loans to individuals granted by the Group amounted to 45.4% (46.3% as at 31 December 2017), with an average LTV for the whole portfolio of 62.5% (64.3% as at 31 December 2017).

Offsetting financial assets and financial liabilities

The disclosures in the tables below include financial assets and financial liabilities that are subject to an enforceable master netting agreements or similar agreements, irrespective of whether they are offset in the statement of financial position.

The netting agreements concluded by the Group are:

- ISDA agreements and similar master netting agreements on derivatives,
- GMRA agreements on repo and reverse-repo transactions.

The netting agreements do not meet the criteria for offsetting in the statement of financial position. This is because they create for the parties to the agreement a right of set-off of recognized amounts that is enforceable only following an event of default, insolvency or bankruptcy of the one of the counterparty. At the balance day, there were no cases of offsetting financial assets and financial liabilities for these netting agreements.

The Group receives and gives collateral in the form of cash and marketable securities in respect of the following transactions:

- derivatives,
- repo and reverse-repo transactions.

Such collateral is subject to standard industry terms. The collateral in the form of cash stems from an ISDA Credit Support Annex (CSA).

The securities received/given as collateral on repo and reverse-repo transaction can be pledged or sold during the term of the transaction but have to be returned on maturity of the transaction. The terms also give each party the right to terminate the related transactions on the counterparty's failure to post collateral.

Financial assets and financial liabilities subject to enforceable master netting agreements and similar agreements and which may be potentially offset in the statement of financial position.

Notes to financial statements (cont.)

(in PLN thousand)

30.06.2018	CARRYING AMOUNT OF FINANCIAL ASSETS PRESENTED IN THE STATEMENT OF FINANCIAL POSITION	AMOUNT OF POTENTIAL OFFSETTING		NET AMOUNT
		FINANCIAL INSTRUMENTS (INCLUDING RECEIVED COLLATERAL IN THE FORM OF SECURITIES)	CASH COLLATERAL RECEIVED	
Financial assets				
Derivatives	1 175 159	(798 230)	(226 796)	150 133
Total	**1 175 159**	**(798 230)**	**(226 796)**	**150 133**

30.06.2018	CARRYING AMOUNT OF FINANCIAL LIABILITIES PRESENTED IN THE STATEMENT OF FINANCIAL POSITION	AMOUNT OF POTENTIAL OFFSETTING		NET AMOUNT
		FINANCIAL INSTRUMENTS (INCLUDING PLEDGED COLLATERAL IN THE FORM OF SECURITIES)	CASH COLLATERAL PLEDGED	
Financial liabilities				
Derivatives	2 181 527	(1 106 029)	(965 764)	109 734
Total	**2 181 527**	**(1 106 029)**	**(965 764)**	**109 734**

31.12.2017	CARRYING AMOUNT OF FINANCIAL ASSETS PRESENTED IN THE STATEMENT OF FINANCIAL POSITION	AMOUNT OF POTENTIAL OFFSETTING		NET AMOUNT
		FINANCIAL INSTRUMENTS (INCLUDING RECEIVED COLLATERAL IN THE FORM OF SECURITIES)	CASH COLLATERAL RECEIVED	
Financial assets				
Derivatives	1 328 535	(902 102)	(265 808)	160 625
Total	**1 328 535**	**(902 102)**	**(265 808)**	**160 625**

31.12.2017	CARRYING AMOUNT OF FINANCIAL ASSETS PRESENTED IN THE STATEMENT OF FINANCIAL POSITION	AMOUNT OF POTENTIAL OFFSETTING		NET AMOUNT
		FINANCIAL INSTRUMENTS (INCLUDING RECEIVED COLLATERAL IN THE FORM OF SECURITIES)	CASH COLLATERAL RECEIVED	
Financial liabilities				
Derivatives	2 575 961	(1 476 984)	(954 537)	144 440
Total	**2 575 961**	**(1 476 984)**	**(954 537)**	**144 440**

The carrying amount of financial assets and financial liabilities disclosed in the above tables have been measured in the statement of financial position on the following bases:

- derivatives – fair value,
- assets and liabilities resulting from repo and reverse-repo transactions – amortized cost.

Reconciliation of the carrying amount of financial assets and financial liabilities subject to enforceable master netting agreements and similar agreements to the amounts presented in the statement of financial position.

Notes to financial statements (cont.)

(in PLN thousand)

30.06.2018	NET CARRYING AMOUNT	ITEM IN STATEMENT OF FINANCIAL POSITION	CARRYING AMOUNT IN STATEMENT OF FINANCIAL POSITION	CARRYING AMOUNT OF TRANSACTIONS NOT IN SCOPE OF OFFSETTING DISCLOSURES	NOTE
Financial assets					
Derivatives	1 133 886	Derivative financial instruments (held for trading)	1 236 083	102 197	27
	41 273	Hedging instruments	144 476	103 203	30
Financial liabilities					
Derivatives	1 174 576	Derivative financial instruments (held for trading)	1 450 668	276 092	27
	1 006 951	Hedging instruments	1 012 635	5 684	30

31.12.2017	NET CARRYING AMOUNT	ITEM IN STATEMENT OF FINANCIAL POSITION	CARRYING AMOUNT IN STATEMENT OF FINANCIAL POSITION	CARRYING AMOUNT OF TRANSACTIONS NOT IN SCOPE OF OFFSETTING DISCLOSURES	NOTE
Financial assets					
Derivatives	1 251 739	Derivative financial instruments (held for trading)	1 349 047	97 308	27
	76 796	Hedging instruments	259 396	182 600	30
Financial liabilities					
Derivatives	1 717 556	Derivative financial instruments (held for trading)	2 030 103	312 547	27
	858 405	Hedging instruments	862 331	3 926	30

7.2 Market risk

Market risk of the trading book

The model of market risk measurement has not changed in relation to the one described in the consolidated financial statements of Bank Pekao S.A. Group for the year ended 31 December 2017.

The table below presents the market risk exposure of the trading portfolio of the Group measured by Value at Risk in the period from 1 January to 30 June 2018 and in 2017:

	30.06.2018	MINIMUM VALUE	AVERAGE VALUE	MAXIMUM VALUE
foreign currency exchange risk	33	9	164	1 232
interest rate risk	815	472	1 033	1 722
Trading portfolio	820	526	1 041	2 362

	31.12.2017	MINIMUM VALUE	AVERAGE VALUE	MAXIMUM VALUE
foreign currency exchange risk	739	13	364	1 918
interest rate risk	791	496	1 013	1 925
Trading portfolio	975	614	1 152	3 046

(in PLN thousand)

Interest rate risk of the banking book

The banking book interest rate risk management process has not changed significantly in relation to the one described in the consolidated financial statements of Bank Pekao S.A. Group for the year ended on 31 December 2017. Selected amendments have been introduced. The risk profile of own funds and additional interest rate risk scenarios considering tilts and changes in the shape of the yield curve have been accounted for in the EVE measures applied for the ongoing internal management. The aggregation rules have also been altered assuming no or partial compensation of the results for specific currencies.

The following table presents contractual NII sensitivity to the change of interest rates by 100 basis points and the EVE sensitivity to the change of interest rates by 200 basis points (standard scenario not accounting for risk profile of own funds) as at 30 June 2018 and as at 31 December 2017.

SENSITIVITY IN %	30.06.2018	31.12.2017
NII	(8.66)	(8.14)
EVE	(4.27)	0.79

Currency risk

The foreign currency exchange risk management process has not changed significantly in relation to the one described in the consolidated financial statements of Bank Pekao S.A. Group for the year ended 31 December 2017.

The tables below present the Group's foreign currency risk profile measured by Value at Risk and currency position.

Value at Risk

CURRENCY	30.06.2018	31.12.2017
Currencies total (*)	377	727

(*) VaR presented in 'Currencies total' is VaR for the whole portfolio, and includes correlations among currencies.

Currency position

30.06.2018	BALANCE SHEET OPERATIONS		OFF-BALANCE SHEET OPERATIONS-DERIVATIVES		NET POSITION
	ASSETS	LIABILITIES	LONG POSITION	SHORT POSITION	
EUR	21 466 169	19 599 399	11 099 085	12 914 659	51 196
USD	4 953 086	8 446 898	8 131 487	4 639 323	(1 648)
CHF	3 566 093	909 244	3 298 740	5 960 237	(4 648)
GBP	269 593	944 810	895 688	219 777	694
HUF	281 514	308 751	155 378	128 241	(100)
NOK	200 161	42 706	30 935	188 928	(538)
CZK	56 428	41 529	149 057	164 059	(103)
Other currencies	159 277	239 716	223 332	141 303	1 590
TOTAL	**30 952 321**	**30 533 053**	**23 983 702**	**24 356 527**	**46 443**

Notes to financial statements (cont.)

(in PLN thousand)

31.12.2017	BALANCE SHEET OPERATIONS		OFF-BALANCE SHEET OPERATIONS-DERIVATIVES		NET POSITION
	ASSETS	LIABILITIES	LONG POSITION	SHORT POSITION	
EUR	19 567 142	20 121 199	12 724 337	12 223 771	(53 491)
USD	4 773 014	8 156 208	9 025 991	5 582 828	59 969
CHF	3 646 120	931 055	3 212 318	5 928 833	(1 450)
GBP	267 038	945 805	786 010	104 930	2 313
CZK	188 269	336 573	158 242	9 956	(18)
Other currencies	326 179	229 077	147 429	243 119	1 412
TOTAL	**28 767 762**	**30 719 917**	**26 054 327**	**24 093 437**	**8 735**

7.3 Liquidity risk

The liquidity risk management process has not changed significantly in relation to the one described in the consolidated financial statements of Bank Pekao S.A. Group for the year ended 31 December 2017.

The tables below present adjusted liquidity gap and structure of financial liabilities maturity.

Adjusted liquidity gap

30.0.2018	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
Balance sheet assets	38 830 073	5 316 801	24 672 739	58 212 803	56 471 083	183 503 499
Balance sheet liabilities	15 567 000	7 910 100	21 714 077	19 844 025	118 468 297	183 503 499
Off-balance sheet assets/liabilities (net)	(5 178 955)	(1 007 539)	(550 780)	2 794 410	3 190 213	(752 651)
Periodic gap	**18 084 118**	**(3 600 838)**	**2 407 882**	**41 163 188**	**(58 807 001)**	**(752 651)**
Cumulated gap	**-**	**14 483 280**	**16 891 162**	**58 054 350**	**(752 651)**	**-**

31.12.2017	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
Balance sheet assets	44 331 276	5 616 950	24 338 476	55 530 078	55 648 790	185 465 570
Balance sheet liabilities	19 514 831	10 388 117	23 351 313	22 738 502	109 472 807	185 465 570
Off-balance sheet assets/liabilities (net)	(5 931 269)	97 029	(410 093)	2 359 200	3 209 552	(675 581)
Periodic gap	**18 885 176**	**(4 674 138)**	**577 070**	**35 150 776**	**(50 614 465)**	**(675 581)**
Cumulated gap	**-**	**14 211 038**	**14 788 108**	**49 938 884**	**(675 581)**	**-**

Notes to financial statements (cont.)

(in PLN thousand)

Structure of financial liabilities by contractual maturity

30.06.2018	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
BALANCE SHEET LIABILITIES (*)						
Amounts due to banks (**)	1 991 267	57 387	968 932	2 004 303	509 651	5 531 540
Amounts due to customers	109 454 711	14 455 222	18 935 091	499 670	91 190	143 435 884
Debt securities issued	547 834	852 708	1 103 736	1 388 061	107 052	3 999 391
Subordinated liabilities	-	-	41 612	203 837	1 527 848	1 773 297
Financial liabilities held for trading	-	-	11 119	38 432	376 352	425 903
Total	**111 993 812**	**15 365 317**	**21 060 490**	**4 134 303**	**2 612 093**	**155 166 015**
OFF-BALANCE SHEET COMMITMENTS (*)						
Financial liabilities granted	34 218 276	-	-	-	-	34 218 276
Guarantees issued	12 943 316	-	-	-	-	12 943 316
Total	**47 161 592**	**-**	**-**	**-**	**-**	**47 161 592**

31.12.2017	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
BALANCE SHEET LIABILITIES (*)						
Amounts due to banks (**)	1 864 915	17 813	172 101	1 950 047	984 629	4 989 505
Amounts due to customers	112 901 631	14 836 699	18 398 928	398 424	41 901	146 577 583
Debt securities issued	162 660	363 837	1 056 673	1 140 615	159 958	2 883 743
Subordinated liabilities	-	-	35 606	180 573	1 526 158	1 742 337
Financial liabilities held for trading	-	-	-	309 328	160 120	469 448
Total	**114 929 206**	**15 218 349**	**19 663 308**	**3 978 987**	**2 872 766**	**156 662 616**
OFF-BALANCE SHEET COMMITMENTS (*)						
Financial liabilities granted	33 879 984	-	-	-	-	33 879 984
Guarantees issued	11 498 681	-	-	-	-	11 498 681
Total	**45 378 665**	**-**	**-**	**-**	**-**	**45 378 665**

(*) Exposure amounts from balance liabilities, financing-related off-balance sheet commitments granted and guarantee liabilities granted have been allocated to earliest tenors, for which an outflow of assets from the Group is possible based on contracts entered into by the Group. However, outflows expected by the Group are actually significantly lower than those indicated by the specification presented above. The above is a consequence of considerable diversification of amounts due to customers and stages of life of individual contracts. Risk monitoring and management in relation to the outflow of assets are provided by the Group on continuous basis. The Group estimates also more probable flows that are reflected in Tables 'Adjusted liquidity gap'.

(**) Including Central Bank.

Notes to financial statements (cont.)

(in PLN thousand)

The financial cash flows associated with off-balance sheet derivative transactions
The following are the liabilities and financial cash flows associated with off-balance sheet derivative transactions, settled, respectively in net and gross amounts.

Off-balance sheet derivative transactions settled by the Group in net amounts include:
- Interest Rate Swaps (IRS),
- Forward Rate Agreements (FRA),
- Foreign currency options and options for gold,
- Interest rate options (Cap/Floor),
- Transactions based on equity securities and stock indexes,
- Transactions based on commodities and precious metals.

Off-balance sheet derivative transactions settled by the Group in gross amounts include:
- Cross-Currency Interest Rate Swaps (CIRS),
- Foreign currency forward contracts,
- Foreign currency swaps (FX-Swap),
- Forward contracts based on securities.

Liabilities from off-balance sheet derivatives transactions settled in net amounts

	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
30.06.2018	64 744	122 523	324 702	598 154	223 759	**1 333 882**
31.12.2017	32 892	27 031	649 423	834 010	285 318	**1 828 674**

Cash flows related to off-balance sheet derivative transactions settled in gross amounts

	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
30.06.2018						
Inflows	21 023 143	4 946 924	8 658 370	4 892 463	2 212 821	**41 733 721**
Outflows	21 123 488	5 014 710	8 959 529	5 126 926	2 377 658	**42 602 311**
31.12.2017						
Inflows	20 996 756	8 816 296	6 701 443	5 583 512	2 601 848	**44 699 855**
Outflows	21 001 290	8 855 192	6 812 448	5 992 032	2 657 321	**45 318 283**

7.4 Operational risk

There have been no significant changes in the operational risk management process in relation to the one described in consolidated financial statements of Bank Pekao S.A. Group for the year ended 31 December 2017.

7.5 Fair value of financial assets and liabilities

Financial instruments that are measured at fair value in the consolidated statement of financial position of the Group

The measurement of fair value of financial instruments, for which market values from active markets are available, is based on market quotations of a given instrument (mark-to-market).

The measurement of fair value of Over-the-counter ('OTC') derivatives and instruments with limited liquidity (i.e. for which no market quotations are available), is made on the basis of other instruments quotations on active markets by replication thereof using a number of valuation techniques, including the estimation of present value of future cash flows (mark-to-model).

As of 30 June 2018 and 31 December 2017, the Group classified the financial assets and liabilities measured at fair value into the following hierarchy of three categories based on the following hierarchy:

- Level 1: mark-to-market, applies to securities quoted on active markets,
- Level 2: mark-to-model valuation with model parameterization, based on quotations from active markets for given type of instrument, applies to illiquid government, municipal, corporate and central bank debt securities, linear and non-linear derivative instruments of interest rate markets (including forward transactions on debt securities), equity, commodity and foreign currency exchange markets, except for those cases that meet the criteria of Level 3,
- Level 3: mark-to-model valuation with partial model parameterization, based on estimated risk factors, applicable to loans and advances, corporate and municipal debt securities and for linear and non-linear derivative instruments of interest rate, equity, commodity and foreign currency exchange markets for which unobservable parameters (e.g. credit risk factors) are recognized as significant.

The measurement at fair value is performed directly by an organizational unit within Risk Management Division, independent of front-office units. The methodology of fair value measurement, including the changes of its parameterization, is subject to approval of Assets and Liabilities Committee (ALCO). The adequacy of measurement methods is subject to on-going analysis and periodical reviews in the framework of model risk management. The same Risk Management Division unit performs the assessment of adequacy and significance of risk factors and assignment of valuation models to appropriate method class, according to established hierarchy of classification.

Notes to financial statements (cont.)

(in PLN thousand)

Assets and liabilities measured at fair value in breakdown by fair value hierarchy levels

30.06.2018	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Assets:	**20 147 727**	**8 601 120**	**6 497 631**	**35 246 478**
Financial assets held for trading	1 159 134	142 083	26 728	1 327 945
Derivative financial instruments, including:	-	1 234 444	1 639	1 236 083
- Banks	-	696 391	1 639	698 030
- Customers	-	538 053	-	538 053
Hedging instruments, including:	-	144 476	-	144 476
- Banks	-	41 273	-	41 273
- Customers	-	103 203	-	103 203
Securities measured at fair value through other comprehensive income	18 988 593	7 080 117	4 930 808	30 999 518
Loans and advances to customers measured at fair value through other comprehensive income	-	-	1 203 214	1 203 214
Loans and advances to customers measured at fair value through profit or loss	-	-	335 242	335 242
Liabilities:	**425 944**	**2 463 262**	**-**	**2 889 206**
Financial liabilities held for trading	425 903	-	-	425 903
Derivative financial instruments, including:	41	1 450 627	-	1 450 668
- Banks	-	616 790	-	616 790
- Customers	41	833 837	-	833 878
Hedging instruments, including:	-	1 012 635	-	1 012 635
- Banks	-	1 006 951	-	1 006 951
- Customers	-	5 684	-	5 684

31.12.2017	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Assets:	**19 838 234**	**16 173 785**	**750 871**	**36 762 890**
Financial assets held for trading	1 629 449	86 756	14 211	1 730 416
Derivative financial instruments, including:	19	1 347 810	1 218	1 349 047
- Banks	-	912 259	1 218	913 477
- Customers	19	435 551	-	435 570
Hedging instruments, including:	-	259 396	-	259 396
- Banks	-	76 796	-	76 796
- Customers	-	182 600	-	182 600
Securities available for sale	18 208 766	14 479 823	735 442	33 424 031
Liabilities:	**456 512**	**2 905 370**	**-**	**3 361 882**
Financial liabilities held for trading	456 510	12 938	-	469 448
Derivative financial instruments, including:	2	2 030 101	-	2 030 103
- Banks	-	815 493	-	815 493
- Customers	2	1 214 608	-	1 214 610
Hedging instruments, including:	-	862 331	-	862 331
- Banks	-	858 274	-	858 274
- Customers	-	4 057	-	4 057

Notes to financial statements (cont.)

(in PLN thousand)

Change in fair value of financial assets measured at fair value according to Level 3 by the Group

I HALF 2018	FINANCIAL ASSETS HELD FOR TRADING	DERIVATIVE FINANCIAL INSTRUMENTS (ASSETS)	LOANS AND ADVANCES TO CUSTOMERS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	LOANS AND ADVANCES TO CUSTOMERS MEASURED AT FAIR VALUE THROUGH PROFIT OR LOSS	SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME
Opening balance	**14 211**	**1 218**	**-**	**-**	**735 442**
Initial application of IFRS 9	-	-	1 555 964	365 137	4 336 613
Opening balance - restated	**14 211**	**1 218**	**1 555 964**	**365 137**	**5 072 055**
Increases, including:	197 226	421	58 792	4 786	55 921
Reclassification	392	-	-	-	-
Derivatives transactions made in 2018	-	-	-	1 872	-
Acquisition	196 442	-	-	-	37 940
Gains on financial instruments	392	421	58 792	2 914	17 981
recognized in the income statement	392	421	18 093	2 914	16 966
recognized in revaluation reserves	-	-	40 699	-	1 015
Decreases, including:	(184 709)	-	(411 542)	(34 681)	(197 168)
Reclassification	-	-	-	-	(52 339)
Settlement/redemption	(448)	-	(9 193)	(29 647)	(26 053)
Sale	(183 988)	-	(402 349)	-	(115 000)
Losses on financial instruments	(273)	-	-	(5 034)	(3 776)
recognized in the income statement	(273)	-	-	(5 034)	-
recognized in revaluation reserves	-	-	-	-	(3 776)
Closing balance	**26 728**	**1 639**	**1 203 214**	**335 242**	**4 930 808**
Unrealized income from financial instruments held in portfolio at the end of the period, recognized in:	**(124)**	**421**	**58 792**	**(2 120)**	**9 650**
Income statement:	(124)	421	18 093	(2 120)	11 338
net interest income	146	-	14 363	(5 034)	11 338
net impairment losses on financial assets and off-balance sheet commitments	-	-	3 730	-	-
result on financial assets and liabilities held for trading	(270)	421	-	2 914	-
Other comprehensive income	-	-	40 699	-	(1 688)

Notes to financial statements (cont.)

(in PLN thousand)

Change in fair value of financial assets measured at fair value according to Level 3 by the Group

2017	FINANCIAL ASSETS HELD FOR TRADING	DERIVATIVE FINANCIAL INSTRUMENTS (ASSETS)	SECURITIES AVAILABLE FOR SALE
Opening balance	**66 113**	**-**	**341 199**
Increases, including:	1 388 818	2 353	717 283
Reclassification	-	-	674 519
Acquisition	1 387 394	-	-
Settlement	-	-	-
Derivatives transactions made in 2017	-	2 353	-
Gains on financial instruments	1 424	-	42 764
recognized in the income statement	1 424	-	41 152
recognized in revaluation reserves	-	-	1 612
Decreases, including:	(1 440 720)	(1 135)	(323 040)
Reclassification	-	-	-
Settlement / redemption	(1 020)	-	(290 030)
Sale	(1 439 693)	-	-
Loss on financial instruments	(7)	(1 135)	(33 010)
recognized in the income statement	(7)	(1 135)	(10 054)
recognized in revaluation reserves	-	-	(22 956)
Closing balance	**14 211**	**1 218**	**735 442**
Unrealized income from financial instruments held in portfolio until end of period, recognized in:	**400**	**(1 135)**	**2 853**
Income statement:	400	(1 135)	23 456
net interest income	178	-	23 456
result on financial assets and liabilities held for trading	222	(1 135)	-
Other comprehensive income	-	-	(20 603)

Transfers of instruments between fair value hierarchy levels are based on changes in availability of active market quotations as at the end of the reporting periods.

In the period from 1 January to 30 June 2018 the following transfers of financial instruments between the levels of the fair value hierarchy were made:

- from level 2 to level 1: a government bond denominated in PLN with quotes available on the active market,
- from Level 3 to Level 2: municipal bonds which were valued based on information on the prices of comparable financial instruments and capital market derivative instruments for which impact of the unobservable factor (correlation) on the valuation was immaterial,
- from level 2 to level 3: municipal and corporate bonds, for which impact of estimated credit parameters was material and capital market derivative instruments with material impact of the estimated factor (correlation) on the valuation.

(in PLN thousand)

The impact of estimated parameters on measurement of financial instruments for which the Group applies fair value valuation according to Level 3 as at 30 June 2018 and 31 December 2017 is as follows:

FINANCIAL ASSET/LIABILITY	FAIR VALUE AS AT 30.06.2018	VALUATION TECHNIQUE	UNOBSERVABLE FACTOR	ALTERNATIVE FACTOR RANGE (WEIGHTED AVERAGE)	IMPACT ON FAIR VALUE AS AT 30.06.2018	
					POSITIVE SCENARIO	NEGATIVE SCENARIO
Corporate and municipal debt securities	4 741 972	Discounted cash flow	Credit spread	0.67% - 1.18%	51 192	(51 192)
Government debt securities	17 980	Discounted cash flow	Benchmark bond spread	0.04% - 0.36%	389	(389)
Derivatives	1 639	Black Scholes Model	Correlation	0 - 1	674	(653)
Loans and advances measured at fair value through profit or loss	335 242	Discounted cash flow	Credit spread	0.64% - 1.07%	1 984	(1 964)
Loans and advances measured at fair value through other comprehensive income	1 203 214	Discounted cash flow	Credit spread	2.01% - 2.42%	3 326	(3 077)

FINANCIAL ASSET/LIABILITY	FAIR VALUE AS AT 31.12.2017	VALUATION TECHNIQUE	UNOBSERVABLE FACTOR	ALTERNATIVE FACTOR RANGE (WEIGHTED AVERAGE)	IMPACT ON FAIR VALUE AS AT 31.12.2017	
					POSITIVE SCENARIO	NEGATIVE SCENARIO
Municipal debt securities	652 597	Discounted cash flow	Credit spread	0.45% - 0.87%	3 856	(3 856)
Government debt securities	14 211	Discounted cash flow	Benchmark bond spread	0.09% - 0.46%	448	(448)
Derivatives	1 219	Black Scholes Model	Correlation	0 - 1	966	(578)

Financial instruments that are not measured at fair value in the consolidated statement of financial position of the Group

The Group also holds financial instruments which are not presented at fair value in the financial statements. Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

As of 30 June 2018 and 31 December 2017, the Group classified the financial assets and liabilities not measured at fair value in the consolidated statement of financial position into the following three categories based on the valuation level:

- Level 1: mark-to-market, applies to government securities quoted on the liquid market and cash,
- Level 2: mark-to-model valuation with model parameterization, based on quotations from active markets for given type of instrument, applies to interbank deposits, own issues, illiquid government, municipal, corporate and central bank debt securities,
- Level 3: mark-to-model valuation with partial model parameterization, based on estimated risk factors, is applicable to corporate and municipal debt securities and loans and deposits for which the applied credit risk factor (an unobservable parameter) is recognized significant.

In case of certain groups of financial assets, recognized at the amount to be received with impairment considered, the fair value was assumed to be equal to carrying amount. The above applies in particular to cash and other financial assets and liabilities.

In the case of loans for which no quoted market values are available, the fair values presented are generally estimated using valuation techniques taking into consideration the assumption, that at the moment when the loan is granted its fair value is equal to its carrying amount. Fair value of non-impaired loans is equal to the sum of future expected cash flows, discounted at the balance sheet date, less expected credit loss. The discount rate is defined as the appropriate market risk-free rate plus the liquidity risk margin and current sales margin for the given loan products group. The margin is computed on loans granted broken down by loan product groups and maturity.

(in PLN thousand)

For the purpose of the fair value of foreign currency loans estimation, the margin on PLN loans adjusted by the cross-currency basis swap quotes and FX-Swap is used. The fair value of impaired loans is defined as equal to the sum of expected recoveries, discounted with the use of effective interest rate, since the average expected recovery values take the element of credit risk fully into consideration. In case of loans without repayment schedule (loans in current account, overdrafts and credit cards), the fair value was assumed as equal to the carrying amount.

Since no quoted market prices are available for deposits, their fair values have been generally estimated using valuation techniques with the assumption that the fair value of a deposit at the moment of its receipt is equal to its carrying amount. The fair value of term deposits is equal to the sum of future expected cash flows, discounted at the relevant balance sheet date. The cash flow discount rate is defined as the relevant market risk-free rate, increased by the sales margin. The margin is computed on deposits acquired during last three months broken down by deposit product groups and maturity. In case of short term deposits (current deposits, overnights, saving accounts), the fair value was assumed as equal to the carrying amount.

The fair value of deposits and loans, apart from cash and mortgage loans denominated in PLN and CHF for which prepayment model is used, is calculated based on contractual cash flows.

The mark-to-model valuation of own issue debt instruments is based on the method of discounting the future cash flows. Variable cash flows are estimated based upon rates adopted for specific markets (depending upon issue specifications). Both the fixed and implied cash flows are discounted using interbank money market rates.

Assets and liabilities not measured at fair value in the financial statement in breakdown by fair value hierarchy levels

30.06.2018	CARRYING AMOUNT	FAIR VALUE	OF WHICH:		
			LEVEL 1	LEVEL 2	LEVEL 3
Assets					
Cash and due from Central Bank	8 014 221	8 012 968	2 657 022	5 355 946	-
Loans and advance to banks	3 480 658	3 482 345	-	1 998 500	1 483 845
Loans and advances to customers measured at amortised cost	116 301 044	116 362 530	-	-	116 362 530
Receivables from financial leases	4 671 461	4 745 267	-	-	4 745 267
Debt securities measured at amortised cost	10 647 866	10 679 245	4 101 528	652 960	5 924 757
Total Assets	**143 115 250**	**143 282 355**	**6 758 550**	**8 007 406**	**128 516 399**
Liabilities					
Amounts due to Central Bank	6 028	6 033	-	-	6 033
Amounts due to other banks	5 458 120	5 415 721	-	1 114 846	4 300 875
Amounts due to customers	142 933 248	143 166 919	-	648 905	142 518 014
Debt securities issued	3 882 304	3 898 418	-	3 898 418	-
Subordinated liabilities	1 257 013	1 257 190	-	1 257 190	-
Total Liabilities	**153 536 713**	**153 744 281**	**-**	**6 919 359**	**146 824 922**

Notes to financial statements (cont.)

(in PLN thousand)

Assets and liabilities not measured at fair value in the financial statement in breakdown by fair value hierarchy levels

31.12.2017	CARRYING AMOUNT	FAIR VALUE	OF WHICH:		
			LEVEL 1	LEVEL 2	LEVEL 3
Assets					
Cash and due from Central Bank	5 236 318	5 236 318	2 686 583	2 549 735	-
Loans and advance to banks	2 627 327	2 627 266	-	1 101 422	1 525 844
Loans and advances to customers	127 949 307	127 027 425	-	8 153 945	118 873 480
Receivables from financial leases	4 351 352	4 416 054	-	-	4 416 054
Debt securities held to maturity	3 481 791	3 516 116	3 484 665	31 451	-
Total Assets	**143 646 095**	**142 823 179**	**6 171 248**	**11 836 553**	**124 815 378**
Liabilities					
Amounts due to Central Bank	6 079	6 080	-	-	6 080
Amounts due to other banks	4 981 291	4 909 701	-	671 642	4 238 059
Amounts due to customers	146 186 268	146 367 007	-	788 437	145 578 570
Debt securities issued	2 771 399	2 786 177	-	2 786 177	-
Subordinated liabilities	1 257 188	1 257 349	-	1 257 349	-
Total Liabilities	**155 202 225**	**155 326 314**	**-**	**5 503 605**	**149 822 709**

8. Operating segments

Data reported in the section stem from the application of the management model ('Model') in which the main criterion for segmentation is the classification of customers based on their profile and service model.

Reporting and monitoring of results, for managerial purposes, includes all components of the income statement up to the gross profit level. Therefore, the income from the segment's activities as well as operating costs related to those activities (including direct and allocated costs in line with the allocation model applied) and other components of income statement are attached to each segment.

The Group settles transactions between segments on an arm's length basis by applying current market prices. Fund transfers between retail, private, corporate and investment banking segments, and the assets and liabilities management and other area are based on market prices applicable to the funds' currency and maturity, including liquidity margins.

Operating segments
The operating segments of the Group are as follows:

- Retail banking – all banking activites related to retail customers (excluding private banking customers) and micro companies with annual turnover not exceeding PLN 5 million, as well as results of the subsidiaries, and shares in net profit of associates accounted for using the equity method, that are assigned to the retail banking activity,
- SME banking - all banking activites related to the companies with annual turnover from PLN 5 milion to PLN 50 million and below 5 million in the case of companies conducting full accounting,
- Private banking – all banking activites related to the most affluent individual customers,
- Corporate and Investment banking – all banking activites related to the medium and large companies, interbank market, debt securities and other instruments, and results of the subsidiaries that are assigned to the Corporate and Investment banking activity,
- assets and liabilities management and other – supervision and monitoring of fund transfers, other activities centrally managed as well as the results of subsidiaries and share in net profit of associates accounted for using the equity method that are not assigned to other reported segments.

Notes to financial statements (cont.)

(in PLN thousand)

Operating segments reporting for the period from 1 January to 30 June 2018

	RETAIL BANKING	PRIVATE BANKING	CORPORATE AND INVESTMENT BANKING	SME BANKING	ASSETS AND LIABILITIES MANAGEMENT AND OTHER	TOTAL
Total net interest income	**1 309 840**	**18 674**	**671 636**	**86 870**	**373 987**	**2 461 007**
Non-interest income	**698 235**	**24 737**	**458 694**	**125 508**	**12 613**	**1 319 787**
Operating income	**2 008 075**	**43 411**	**1 130 330**	**212 378**	**386 600**	**3 780 794**
Personnel expenses	(577 827)	(19 744)	(137 716)	(43 153)	(276 733)	(1 055 173)
Other administrative expenses	(557 441)	(19 334)	(187 319)	(116 656)	360 220	(520 530)
Depreciation and amortisation	(68 865)	(1 175)	(11 102)	(9 619)	(86 912)	(177 673)
Operating costs	**(1 204 133)**	**(40 253)**	**(336 137)**	**(169 428)**	**(3 425)**	**(1 753 376)**
Gross operating profit	**803 942**	**3 158**	**794 193**	**42 950**	**383 175**	**2 027 418**
Net impairment losses on financial assets and off-balance sheet commitments	(152 321)	580	(64 412)	(21 647)	(13 093)	(250 893)
Net operating profit	**651 621**	**3 738**	**729 781**	**21 303**	**370 082**	**1 776 525**
Net result on other provisions	335	(2 412)	(465)	-	(11 525)	(14 067)
Guarantee funds charges	(82 783)	(292)	(76 441)	(4 199)	(40 581)	(204 296)
Tax on certain financial institutions	-	-	-	-	(276 894)	(276 894)
Net result on investment activities	12	6	41	-	(3 999)	(3 940)
Profit before tax	**569 185**	**1 040**	**652 916**	**17 104**	**37 083**	**1 277 328**
Income tax expense						(345 026)
Net profit for the period						**932 302**
Attributable to equity holders of the Bank						**932 140**
Attributable to non-controling interests						162
Allocated assets	71 081 597	294 189	100 569 656	3 385 368	(810 121)	174 520 689
Unallocated assets						8 982 810
Total assets						**183 503 499**
Allocated liabilities	79 664 247	8 594 155	59 922 222	10 344 464	(3 529 711)	154 995 377
Unallocated liabilities						28 508 122
Total liabilities						**183 503 499**

Notes to financial statements (cont.)

(in PLN thousand)

Operating segments reporting for the period from 1 January to 30 June 2017

	RETAIL BANKING	PRIVATE BANKING	CORPORATE AND INVESTMENT BANKING	SME BANKING	ASSETS AND LIABILITIES MANAGEMENT AND OTHER	TOTAL
Total net interest income	**1 168 651**	**20 682**	**673 952**	**76 577**	**351 319**	**2 291 181**
Non-interest income	**637 260**	**13 303**	**379 435**	**109 803**	**80 470**	**1 220 271**
Operating income	**1 805 911**	**33 985**	**1 053 387**	**186 380**	**431 789**	**3 511 452**
Personnel expenses	(519 538)	(12 383)	(128 215)	(39 395)	(252 787)	(952 318)
Other administrative expenses	(511 138)	(13 882)	(174 624)	(108 655)	336 222	(472 077)
Depreciation and amortisation	(67 864)	(671)	(10 742)	(9 571)	(80 719)	(169 567)
Operating costs	**(1 098 540)**	**(26 936)**	**(313 581)**	**(157 621)**	**2 716**	**(1 593 962)**
Gross operating profit	**707 371**	**7 049**	**739 806**	**28 759**	**434 505**	**1 917 490**
Net impairment losses on financial assets and off-balance sheet commitments	(109 379)	(383)	(95 372)	(26 710)	1 870	(229 974)
Net operating profit	**597 992**	**6 666**	**644 434**	**2 049**	**436 375**	**1 687 516**
Net result on other provisions	(2 212)	-	239	-	(12 029)	(14 002)
Guarantee funds charges	(76 181)	(314)	(59 607)	(3 618)	(83 941)	(223 661)
Tax on certain financial institutions	-	-	-	-	(252 685)	(252 685)
Net result on investment activities	(150)	-	114	-	102	66
Profit before tax	**519 449**	**6 352**	**585 180**	**(1 569)**	**87 822**	**1 197 234**
Income tax expense						(312 243)
Net profit for the period						**884 991**
Attributable to equity holders of the Bank						**884 778**
Attributable to non-controling interests						213
Allocated assets	64 285 661	254 880	96 760 272	3 129 807	(2 043 638)	162 386 982
Unallocated assets						8 143 121
Total assets						**170 530 103**
Allocated liabilities	72 849 777	8 663 538	56 086 615	9 603 844	(5 444 354)	141 759 420
Unallocated liabilities						28 770 683
Total liabilities						**170 530 103**

Reconciliations of operating income for reportable segments

	I HALF 2018	I HALF 2017
Total operating income for reportable segments	**3 780 794**	**3 511 452**
Share in gains (losses) from associates	-	(20 554)
Net other operating income and expenses	(25 720)	(47 892)
Refunding of administrative expenses	-	1 251
Operating income	**3 755 074**	**3 444 257**

Geographical segment

The operating activity of Bank Pekao S.A. Group is concentrated in Poland through the network of branches and the subsidiaries.

Notes to financial statements (cont.)

(in PLN thousand)

9. Interest income and expense

Interest income

	II QUARTER 2018				II QUARTER 2017
	FINANCIAL ASSETS MEASURED AT AMORTISED COST	FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER PROFIT OR LOSS	TOTAL	
Loans and other receivables from customers	1 205 686	7 094	1 951	1 214 731	1 161 816
Interbank placements	11 885	-	-	11 885	20 316
Reverse repo transactions	7 256	-	-	7 256	6 968
Investment securities	74 655	169 429	-	244 084	164 949
Hedging derivatives	-	-	34 332	34 332	32 338
Financial assets held for trading	-	-	3 622	3 622	6 179
Total	**1 299 482**	**176 523**	**39 905**	**1 515 910**	**1 392 566**

	I HALF 2018				I HALF 2017
	FINANCIAL ASSETS MEASURED AT AMORTISED COST	FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FINANCIAL ASSETS MEASURED AT FAIR VALUE THROUGH OTHER PROFIT OR LOSS	TOTAL	
Loans and other receivables from customers	2 373 555	13 369	3 946	2 390 870	2 283 586
Interbank placements	22 880	-	-	22 880	39 526
Reverse repo transactions	12 076	-	-	12 076	18 715
Investment securities	150 852	351 805	-	502 657	348 629
Hedging derivatives	-	-	61 210	61 210	67 043
Financial assets held for trading	-	-	4 781	4 781	10 034
Total	**2 559 363**	**365 174**	**69 937**	**2 994 474**	**2 767 533**

Interest expense

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Deposits from customers	(232 621)	(466 248)	(224 621)	(452 475)
Interbank deposits	(4 467)	(7 789)	(4 450)	(9 224)
Repo transactions	(10 077)	(17 819)	(17 119)	(33 800)
Loans and advances received	(2 299)	(4 546)	(2 197)	(4 563)
Debt securities issued	(30 909)	(56 845)	(7 997)	(16 262)
Total	**(280 373)**	**(553 247)**	**(256 384)**	**(516 324)**

The amounts shown above contain interest expense relating to the financial liabilities measured at amortised cost.

Notes to financial statements (cont.)

(in PLN thousand)

10. Fee and commission income and expense

Fee and commission income

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Accounts maintenance, payment orders and cash transactions	155 306	305 840	150 075	300 719
Payment cards	145 540	280 999	144 874	282 355
Loans and advances	97 434	181 555	112 278	212 588
Margin on foreign exchange transactions with clients	119 761	224 190	109 897	216 030
Investment products sales intermediation	125 977	257 920	67 404	131 490
Securities operations	16 940	40 702	18 700	45 844
Custody activity	14 229	28 132	16 665	33 293
Pension and investment funds service fees	7 909	15 797	12 960	25 282
Guarantees, letters of credit and similar transactions	13 753	28 055	13 133	26 197
Other	10 218	19 305	13 118	27 280
Total	**707 067**	**1 382 495**	**659 104**	**1 301 078**

Fee and commission expense

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Payment cards	(61 878)	(121 720)	(56 613)	(105 714)
Money orders and transfers	(5 118)	(10 328)	(5 337)	(10 468)
Securities and derivatives operations	(6 998)	(13 736)	(7 123)	(14 680)
Acquisition services	(8 697)	(18 163)	(1 193)	(2 271)
Custody activity	(4 206)	(8 113)	(3 850)	(7 356)
Accounts maintenance	(1 139)	(2 040)	(1 429)	(2 539)
Pension and investment funds management charges	(875)	(1 219)	(572)	(675)
Other	(883)	(1 849)	(701)	(1 607)
Total	**(89 794)**	**(177 168)**	**(76 818)**	**(145 310)**

11. Dividend income

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Issuers of securities held for trading	X	X	16	16
Issuers of securities available for sale	X	X	19 253	19 402
Issuers of securities measured at fair value through profit or loss	7	164	X	X
Issuers of equity instruments designated at fair value through profit or loss	19 616	19 616	X	X
Total	**19 623**	**19 780**	**19 269**	**19 418**

Notes to financial statements (cont.)

(in PLN thousand)

12. Result on financial assets and liabilities measured at fair value through profit or loss

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Gains (losses) on loans and advances to customers measured mandatorily at fair value through profit or loss	(9)	(4 215)	X	X
Gains (losses) on securities measured mandatorily at fair value through profit or loss	6 075	8 485	X	X
Foreign currency exchange result	(12 694)	(15 448)	(16 628)	(23 281)
Gains (losses) on derivatives	17 355	35 612	12 650	22 654
Gains (losses) on securities	5 812	11 230	4 836	9 500
Total	**16 539**	**35 664**	**858**	**8 873**

13. Result on derecognition of financial assets and liabilities not measured at fair value through profit or loss

Realized gains

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Financial assets measured at amortised cost	172	172	X	X
Financial assets measured at fair value through other comprehensive income	27 095	50 948	X	X
Total	**27 267**	**51 120**	**X**	**X**

Realized losses

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Financial liabilities not measured at fair value through profit and loss	(22)	(43)	X	X
Total	**(22)**	**(43)**	**X**	**X**

Net realized profit	**27 245**	**51 077**	**X**	**X**

14. Gains (losses) on disposal of financial assets and liabilities

Realized gains

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Loans and other financial receivables	X	X	27	93
Available for sale financial assets - debt instruments	X	X	4 944	5 753
Held to maturity investments	X	X	176	176
Total	**X**	**X**	**5 147**	**6 022**

Notes to financial statements (cont.)

(in PLN thousand)

Realized losses

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Debt securities issued	X	X	(29)	(80)
Total	**X**	**X**	**(29)**	**(80)**

Net realized profit	**X**	**X**	**5 118**	**5 942**

15. Net impairment losses on financial assets and off-balance sheet commitments

	II QUARTER 2018	I HALF 2018
Loans and other financial assets measured at amortized cost (*)	(118 842)	(259 689)
Debt securities measured at amortized cost	(493)	(536)
Loans measured at fair value through other comprehensive income	(589)	4 326
Debt securities measured at fair value through other comprehensive income	(8 211)	(5 334)
Off-balance sheet commitments	4 203	10 340
Total financial assets and off-balance sheet commitments	**(123 932)**	**(250 893)**

(*) Item includes impairment losses on loans and advances to banks and receivables from financial leases.

	II QUARTER 2017	I HALF 2017
Loans and advances to banks measured at amortized cost	(5)	(22)
Loans and advances to customers measured at amortized cost	(110 728)	(233 759)
Receivables from financial leases	(1 521)	(2 943)
Off-balance sheet commitments	(2 594)	6 750
Total financial assets and off-balance sheet commitments	**(114 848)**	**(229 974)**

16. Administrative expenses

Personnel expenses

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Wages and salaries	(470 393)	(884 258)	(402 854)	(797 292)
Insurance and other charges related to employees	(78 863)	(156 000)	(73 297)	(145 312)
Share-based payments expenses	(5 571)	(14 915)	(6 198)	(9 714)
Total	**(554 827)**	**(1 055 173)**	**(482 349)**	**(952 318)**

(in PLN thousand)

Other administrative expenses

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
General expenses	(247 065)	(486 871)	(223 337)	(440 273)
Taxes and charges	(9 721)	(20 401)	(9 960)	(22 178)
Bank Guarantee Fund fee	(29 983)	(205 025)	(22 213)	(222 717)
Financial supervision authority fee (KNF)	(390)	(12 529)	(242)	(11 821)
Tax on certain financial institutions	(138 593)	(276 894)	(127 531)	(252 685)
Total	**(425 752)**	**(1 001 720)**	**(383 283)**	**(949 674)**

Total administrative expenses	**(980 579)**	**(2 056 893)**	**(865 632)**	**(1 901 992)**

From 1 January 2017 new rules for making contributions to Bank Guarantee Fund (hereinafter 'BGF'), defined in the Act of 10 June 2016 on Bank Guarantee Fund, deposit guarantee schemes and resolution of banks (hereinafter 'BGF Act'), have to be applied.
In accordance with BGF Act, the banks are committed to make quarterly contributions to deposit guarantee fund of banks and annual contribution to resolution fund of banks. Such contributions are expenses not deductible for tax purposes. The obligation to make quarterly contribution to deposit guarantee fund of banks arises at the first day of each quarter, whereas the obligation to make annual contribution to resolution fund of banks arises at 1 January of the year concerned.

As a result of application of the Interpretation IFRIC 21 *Levies* for recognition of the above obligations, the costs of quarterly contribution to deposit guarantee fund of banks in the amount of PLN 60 689 thousand (PLN 44 327 thousand in the first half of 2017) and the costs of annual contribution to resolution fund of banks in the amount of PLN 144 336 thousand (PLN 178 389 thousand in 2017) are charged to the income statement of Bank Pekao Group for the first half of 2018.

17. Depreciation and amortization

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Property, plant and equipment	(43 124)	(85 548)	(42 862)	(85 352)
Investment property	(173)	(395)	(198)	(468)
Intangible assets	(46 596)	(91 730)	(42 165)	(83 747)
Total	**(89 893)**	**(177 673)**	**(85 225)**	**(169 567)**

Notes to financial statements (cont.)

(in PLN thousand)

18. Net other operating income and expenses

Other operating income

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Rental income	5 761	11 221	4 917	10 229
Miscellaneous income	927	5 583	2 770	5 360
Recovery of debt collection costs	3 629	6 383	3 512	6 711
Revenues from sale of products, goods and services	19 797	53 158	18 120	39 818
Excess payments, repayments	688	1 165	643	1 130
Compensation, recoveries, penalty fees and fines received	6 116	12 322	6 874	38 709
Revenues from leasing activity	218	856	1 010	2 074
Refunding of administrative expenses	-	-	571	1 251
Income from written off liabilities	20	29	2	13
Releases of impairment allowances for litigation and other assets	218	472	180	411
Gains on sale of leasing assets for third person and other assets	114	140	-	298
Other	920	1 792	1 357	2 490
Total	**38 408**	**93 121**	**39 956**	**108 494**

Other operating expenses

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Costs related to leasing activity	(249)	(623)	(400)	(1 140)
Credit insurance expenses	(906)	(2 260)	(2 137)	(4 647)
Sundry expenses	(491)	(2 574)	(2 188)	(4 144)
Reimbursement and deficiencies	(237)	(1 127)	(401)	(2 562)
Costs from sale of products, goods and services	(19 108)	(51 156)	(17 373)	(37 134)
Customers complaints expenses	(152)	(376)	(306)	(563)
Impairment allowance for litigations and other assets	(675)	(900)	(641)	(1 406)
Costs of litigation and claims	(466)	(870)	(454)	(1 535)
Compensation, penalty fees and fines paid	(329)	(517)	(115)	(218)
Losses on disposal of leasing assets for third person and other assets	(47)	(260)	(57)	(560)
Other	(3 653)	(6 738)	(3 731)	(6 693)
Total	**(26 313)**	**(67 401)**	**(27 803)**	**(60 602)**

Net other operating income and expenses	**12 095**	**25 720**	**12 153**	**47 892**

Notes to financial statements (cont.)

(in PLN thousand)

19. Gains (losses) on subsidiaries and associates

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Share in gains (losses) from associates				
Dom Inwestycyjny Xelion Sp. z o.o.	-	-	831	1 440
Pekao Investment Management S.A.	-	-	9 613	19 114
Total share in gains (losses) from associates	**-**	**-**	**10 444**	**20 554**
Total gains (losses) from subsidiaries and associates	**-**	**-**	**10 444**	**20 554**

20. Gains (losses) on disposal of property, plant and equipment, and intangible assets

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Gains (losses) on disposal of property, plant and equipment classified as assets held for sale	968	3 820	103	720
Gains (losses) on de-recognition of property, plant and equipment and intangible assets other than classified as assets held for sale	(7 831)	(7 760)	(162)	(654)
Total gains (losses) on disposal of property, plant and equipment and intangible assets	**(6 863)**	**(3 940)**	**(59)**	**66**

21. Basic components of income tax charge in the income statement and equity

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
INCOME STATEMENT				
Current tax	**(250 524)**	**(391 081)**	**(181 171)**	**(274 484)**
Current tax charge in the income statement	(250 400)	(391 503)	(181 016)	(277 544)
Adjustments related to the current tax from previous years	-	601	37	3 298
Other taxes (e.g. withholding tax)	(124)	(179)	(192)	(238)
Deferred tax	**76 562**	**46 055**	**22 957**	**(37 759)**
Occurrence and reversal of temporary differences	76 562	46 055	22 957	(37 759)
Tax charge in the consolidated income statement	**(173 962)**	**(345 026)**	**(158 214)**	**(312 243)**
EQUITY				
Deferred tax	**13 016**	**(3 426)**	**(12 721)**	**(44 624)**
Income and costs disclosed in other comprehensive income:				
revaluation of financial instruments - cash flows hedges	671	3 962	5 246	6 099
revaluation of available for sale financial assets – debt securities	X	X	(21 642)	(40 530)
fair value revaluation through other comprehensive income	9 696	(11 069)	X	X
fair value revaluation through other comprehensive income – equity securities	2 649	3 681	3 675	(10 193)
Tax on items that are or may be reclassified subsequently to profit or loss	**13 016**	**(3 426)**	**(12 721)**	**(44 624)**
Total charge	**(160 946)**	**(348 452)**	**(170 935)**	**(356 867)**

Notes to financial statements (cont.)

(in PLN thousand)

22. Earnings per share

Basic earnings per share

Basic earnings per share are calculated by dividing the net profit attributable to equity holders of the Bank by the weighted average number of the ordinary shares outstanding during the period.

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Net profit	539 815	932 140	535 069	884 778
Weighted average number of ordinary shares in the period	262 470 034	262 470 034	262 470 034	262 470 034
Earnings per share (in PLN per share)	2.06	3.55	2.04	3.37

Diluted earnings per share

Diluted earnings per share are calculated by dividing the net profit attributable to equity holders of the Bank by the weighted average number of the ordinary shares outstanding during the given period adjusted for all potential dilution of ordinary shares.

As at 30 June 2018 there were no diluting instruments in the form of convertible bonds in the Group.

	II QUARTER 2018	I HALF 2018	II QUARTER 2017	I HALF 2017
Net profit	539 815	932 140	535 069	884 778
Weighted average number of ordinary shares in the period	262 470 034	262 470 034	262 470 034	262 470 034
Weighted average number of ordinary shares for the purpose of calculation of diluted earnings per share	262 470 034	262 470 034	262 470 034	262 470 034
Diluted earnings per share (in PLN per share)	2.06	3.55	2.04	3.37

23. Dividend payment

The dividends and other payments to shareholders are recognized directly in equity. The dividend payable is not recognized until the entity has no obligation to pay dividends that is until the payment is approved by the General Meeting.

On 21 June 2018 the Ordinary General Meeting of Bank Pekao S.A. made the resolution regarding the dividend payment for year 2017. The dividend to the shareholders contributed an amount of PLN 2 073 513 268.60, wherein the amount of the dividend per one share was PLN 7.90. The dividend's day was fixed for 6 July 2018.

The payment of the dividend was on 20 July 2018.

24. Cash and balances with Central Bank

Cash and due from Central Bank	**30.06.2018**	**31.12.2017**
Cash	2 657 477	2 686 571
Current account at Central Bank	4 870 541	2 264 688
Other	486 658	285 059
Gross carrying amount	**8 014 676**	**5 236 318**
Impairment allowances	(455)	-
Net carrying amount	**8 014 221**	**5 236 318**

Notes to financial statements (cont.)

(in PLN thousand)

Amounts due to Central Bank	30.06.2018	31.12.2017
Term deposits	6 028	6 079
Amounts due to Central Bank	**6 028**	**6 079**

Receivables and liabilities to the Central Bank are measured at amortized cost.

Cash and balances with Central Bank by currency

30.06.2018	ASSETS	LIABILITIES
PLN	6 921 061	6 028
EUR	511 247	-
USD	355 469	-
CHF	61 683	-
Other currencies	164 761	-
Total	**8 014 221**	**6 028**

31.12.2017	ASSETS	LIABILITIES
PLN	4 352 579	6 079
EUR	463 160	-
USD	168 562	-
CHF	58 882	-
Other currencies	193 135	-
Total	**5 236 318**	**6 079**

25. Loans and advances to banks

Loans and advances to banks by product type

	30.06.2018	31.12.2017
Current accounts	553 879	335 016
Interbank placements	979 081	271 823
Loans and advances	19 989	29 528
Cash collaterals	1 074 079	1 006 332
Reverse repo transactions	465 496	494 706
Cash in transit	399 052	506 559
Total gross amount	**3 491 576**	**2 643 964**
Impairment allowances	(10 918)	(16 637)
Total net amount	**3 480 658**	**2 627 327**

Loans and advances to banks are measured at amortised cost.

(in PLN thousand)

Loans and advances to banks by contractual maturity

	30.06.2018	31.12.2017
Loans and advances to banks, including:		
up to 1 month	3 363 836	2 588 346
between 1 and 3 months	6 009	31 579
between 3 months and 1 year	107 093	7
between 1 and 5 years	183	29
over 5 years	51	50
past due	14 404	23 953
Total gross amount	**3 491 576**	**2 643 964**
Impairment allowances	(10 918)	(16 637)
Total net amount	**3 480 658**	**2 627 327**

Loans and advances to banks by currency

	30.06.2018	31.12.2017
PLN	731 362	702 126
CHF	15 963	23 342
EUR	2 126 127	1 346 256
USD	134 361	209 142
Other currencies	472 845	346 461
Total	**3 480 658**	**2 627 327**

26. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading by product type

	30.06.2018	31.12.2017
FINANCIAL ASSETS		
Debt securities	1 319 450	1 725 858
Equity securities	8 495	4 558
Total financial assets	**1 327 945**	**1 730 416**
FINANCIAL LIABILITIES		
Debt securities	425 903	469 448
Total financial liabilities	**425 903**	**469 448**

Notes to financial statements (cont.)

(in PLN thousand)

Debt securities held for trading

	30.06.2018	31.12.2017
FINANCIAL ASSETS		
Debt securities issued by State Treasury	1 175 214	1 646 758
T- bills	-	-
T- bonds	1 175 214	1 646 758
Debt securities issued by banks	33 813	50 258
Debt securities issued by business entities	110 423	28 842
Total financial assets	**1 319 450**	**1 725 858**
FINANCIAL LIABILITIES		
Debt securities issued by State Treasury	425 903	469 448
T- bonds	425 903	469 448
Total financial liabilities	**425 903**	**469 448**

Equity securities held for trading

	30.06.2018	31.12.2017
Shares	2 494	208
Participation units	6 001	4 350
Total	**8 495**	**4 558**

Debt securities held for trading by maturity

	30.06.2018	31.12.2017
FINANCIAL ASSETS		
Debt securities, including:		
up to 1 month	38 778	123 505
between 1 and 3 months	3 010	-
between 3 months and 1 year	52 882	12 605
between 1 and 5 years	921 337	1 461 523
over 5 years	303 443	128 225
unspecified term	-	-
Total financial assets	**1 319 450**	**1 725 858**
FINANCIAL LIABILITIES		
Debt securities, including:		
up to 1 month	-	-
between 1 and 3 months	-	-
between 3 months and 1 year	11 119	-
between 1 and 5 years	38 432	309 328
over 5 years	376 352	160 120
Total financial liabilities	**425 903**	**469 448**

(in PLN thousand)

Debt securities held for trading by currency

	30.06.2018	31.12.2017
FINANCIAL ASSETS		
PLN	1 312 855	1 718 202
EUR	4 566	4 542
USD	2 029	3 114
Total financial assets	**1 319 450**	**1 725 858**
FINANCIAL LIABILITIES		
PLN	425 903	469 448
Total financial liabilities	**425 903**	**469 448**

27. Derivative financial instruments (held for trading)

Fair value of trading derivatives

30.06.2018	ASSETS	LIABILITIES
Interest rate transactions		
Interest Rate Swaps (IRS)	801 123	1 073 071
Forward Rate Agreements (FRA)	954	85
Options	6 171	2 584
Other	782	863
Foreign currency and gold transactions		
Cross-Currency Interest Rate Swaps (CIRS)	33 407	54 360
Currency Forward Agreements	106 846	197 610
Currency Swaps (FX-Swap)	169 298	15 798
Options for currency and gold	50 670	41 506
Transactions based on equity securities and stock indexes		
Options	1 639	1 634
Other	-	41
Transactions based on commodities and precious metals		
Options	30 066	28 444
Other	35 127	34 672
Total	**1 236 083**	**1 450 668**

Notes to financial statements (cont.)

(in PLN thousand)

31.12.2017	ASSETS	LIABILITIES
Interest rate transactions		
Interest Rate Swaps (IRS)	967 627	1 530 119
Forward Rate Agreements (FRA)	176	-
Options	6 161	2 252
Other	461	416
Foreign currency and gold transactions		
Cross-Currency Interest Rate Swaps (CIRS)	54 451	29 255
Currency Forward Agreements	120 428	185 924
Currency Swaps (FX-Swap)	87 603	173 636
Options for currency and for gold	27 932	24 955
Transactions based on equity securities and stock indexes		
Options	10 225	10 219
Other	19	2
Transactions based on commodities and precious metals		
Options	14 739	14 366
Other	59 225	58 959
Total	**1 349 047**	**2 030 103**

Derivative financial instruments are measured at fair value through profit or loss.

28. Loans and advances to customers

Loans and advances to customers by product type

	30.06.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
Mortgage loans	60 352 888	1 203 214	31 190	61 587 292	59 729 689
Current accounts	11 802 647	-	-	11 802 647	11 028 956
Operating loans	12 698 762	-	29 945	12 728 707	12 916 798
Investment loans	18 935 280	-	115 044	19 050 324	18 665 906
Cash loans	12 561 233	-	-	12 561 233	12 190 872
Payment cards receivables	1 110 442	-	-	1 110 442	1 081 499
Factoring	3 572 031	-	-	3 572 031	3 478 545
Other loans and advances	1 377 479	-	159 063	1 536 542	1 386 808
Debt securities	-	-	-	-	12 749 288
Reverse repo transactions	-	-	-	-	-
Cash in transit	42 665	-	-	42 665	79 144
Gross carrying amount	**122 453 427**	**1 203 214**	**335 242**	**123 991 883**	**133 307 505**
Impairment allowances (*)	(6 152 383)	-	-	(6 152 383)	(5 358 198)
Carrying amount	**116 301 044**	**1 203 214**	**335 242**	**117 839 500**	**127 949 307**

(*) The impairment allowance for loans and advances to customers measured at fair value through equity in the amount of PLN 13 545 thousand is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

Notes to financial statements (cont.)

(in PLN thousand)

Corporate and municipal debt securities were transferred to the 'Investment (placement) securities' item. Before applying the requirements of IFRS 9, these items were presented as loans and advances to customers, as they were classified in the Loans and receivables category in accordance with IAS 39.

Due to the classification of some loans and advances to customers (ie loans in the part intended for syndication) to the business model, whose objective is achieved by both collecting contractual cash flows and selling financial assets, these loans are measured at fair value through other comprehensive income.

The Bank identified a portfolio of loans that do not meet the SPPI criterion due to the leverage element in contracts increasing the volatility of cash flows, which includes student loans, loans with subsidies of the Agency for Restructuring and Modernization of Agriculture and several corporate exposures. Therefore, despite the business model, whose objective is to hold financial assets in order to collect contractual cash flows, for these loan portfolios there is a need to measure at fair value through the profit and loss account.

According to IFRS 9 at the moment of recognizing the impairment, the interest recognized in the income statement is calculated based on the amount reduced by an allowance for expected credit losses (net carrying amount), whereas in the balance sheet accrued interest is calculated on the gross amount of the exposure. The difference is included in the impairment allowance. The increase in the amount of impairment allowance, besides the increase resulting from the expected credit losses approach reflected in the Group's retained earnings, includes also changes reflecting the new approach to interest recognition.

Loans and advances to customers by customer type

	30.06.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
Corporate	50 330 296	1 203 214	64 277	51 597 787	58 841 495
Individuals	67 854 598	-	159 063	68 013 661	64 377 510
Budget entities	4 268 533	-	111 902	4 380 435	10 088 500
Gross carrying amount	**122 453 427**	**1 203 214**	**335 242**	**123 991 883**	**133 307 505**
Impairment allowances (*)	(6 152 383)	-	-	(6 152 383)	(5 358 198)
Carrying amount	**116 301 044**	**1 203 214**	**335 242**	**117 839 500**	**127 949 307**

(*) The impairment allowance for loans and advances to customers measured at fair value through equity in the amount of PLN 13 545 thousand is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

Loans and advances to customers by contractual maturity

	30.06.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
Loans and advances to customers, including:					
up to 1 month	15 873 297	-	2 644	15 875 941	14 966 833
between 1 and 3 months	3 698 717	-	15 309	3 714 026	4 657 178
between 3 months and 1 year	9 685 046	121 876	52 995	9 859 917	10 286 555
between 1 and 5 years	36 336 242	440 696	191 767	36 968 705	41 942 265
over 5 years	51 620 469	640 642	61 873	52 322 984	55 962 982
past due	5 239 656	-	10 654	5 250 310	5 491 692
Gross carrying amount	**122 453 427**	**1 203 214**	**335 242**	**123 991 883**	**133 307 505**
Impairment allowances (*)	(6 152 383)	-	-	(6 152 383)	(5 358 198)
Carrying amount	**116 301 044**	**1 203 214**	**335 242**	**117 839 500**	**127 949 307**

(*) The impairment allowance for loans and advances to customers measured at fair value through equity in the amount of PLN 13 545 thousand is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

(in PLN thousand)

Loans and advances to customers by currency

	30.06.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
PLN	98 005 147	49 599	335 242	98 389 988	107 990 654
CHF	3 487 294	-	-	3 487 294	3 561 945
EUR	12 433 889	1 153 615	-	13 587 504	13 688 524
USD	2 053 004	-	-	2 053 004	2 477 434
Other currencies	321 710	-	-	321 710	230 750
Total	**116 301 044**	**1 203 214**	**335 242**	**117 839 500**	**127 949 307**

29. Receivables from financial leases

The Group conducts leasing operations through its subsidiary Pekao Leasing Sp. z o.o.

The value of gross lease investments and minimum lease payments are follows as:

30.06.2018	GROSS LEASING INVESTMENT	PRESENT VALUE OF MINIMUM LEASE PAYMENTS
Up to 1 year	1 905 171	1 765 640
Between 1 and 5 years	2 943 960	2 786 326
Over 5 years	307 627	301 038
Total	**5 156 758**	**4 853 004**
Unearned finance income	(303 754)	
Net leasing investment	**4 853 004**	
Unguaranteed residual values accruing to the benefit of the lessor	-	
Present value of minimum lease payments	4 853 004	
Impairment allowances	(181 543)	
Balance sheet value	**4 671 461**	

31.12.2017	GROSS LEASING INVESTMENT	PRESENT VALUE OF MINIMUM LEASE PAYMENTS
Up to 1 year	1 711 448	1 576 487
Between 1 and 5 years	2 775 224	2 626 222
Over 5 years	335 744	322 358
Total	**4 822 416**	**4 525 067**
Unearned finance income	(297 349)	
Net leasing investment	**4 525 067**	
Unguaranteed residual values accruing to the benefit of the lessor	-	
Present value of minimum lease payments	4 525 067	
Impairment allowances	(173 715)	
Balance sheet value	**4 351 352**	

The Group is acting as a lessor in financial leases mainly for transport vehicles, machines and equipment.

Moreover, when the Group is a lessee in a financial lease contract among the Group entities, the inter-company transactions relating to the financial leases are eliminated in the consolidated financial statements.

(in PLN thousand)

Receivables from financial leases by currency

	30.06.2018	31.12.2017
PLN	2 967 081	2 747 448
CHF	201	467
EUR	1 688 950	1 588 474
USD	15 229	14 963
Total	**4 671 461**	**4 351 352**

30. Hedge accounting

The Group decided to take advantage of the choice given by IFRS 9 and continues to apply hedge accounting procedures according to IAS 39. This decision concerns all hedging relationships, for which the Bank applies and will apply hedge accounting in the future.

As of 30 June 2018 the Group applies fair value hedge accounting and cash flow hedge accounting.

Fair value hedge accounting
The Group applies fair value hedge accounting for fixed coupon debt securities denominated in PLN, EUR and USD, hedged with interest rate swap (IRS) transactions in the same currencies. The Group hedges component of interest rate risk related to the fair value changes of the hedged item resulting exclusively from the volatility of market interest rates (WIBOR, EURIBOR, LIBOR USD). The IRS transactions receive floating-rate flows, and pay fixed-rate flows. In the past, hedged risk component accounted for a significant portion of changes in fair value of the hedged item.

The approach of the Group to market risk managemant, including interest rate risk, is presented in Note 7.2. Details regarding exposure of the Group to interest rate risk is disclosed in Note 7.2.

The use of derivative instruments to hedge the exposure to changes in interest rates generates counterparty credit risk of derivative transactions. The Group mitigates this risk by requiring the counterparties to post collateral deposits and by settling derivative transactions through Central Counterparty Clearing Houses (CCPs) whch apply a number of mechanisms allowing systemic reduction of the risk of default on obligations under concluded transactions.

The Group applies fair value hedge accounting to a hedging relationship if it is justified to expect that the hedge will be highly effective in achieving offsetting fair value changes attributable to the hedged risk in the future and if assessment of hedge effectiveness indicates high effectiveness in all financial reporting periods for which the hedge was designated.

According to the approach of the Group, hedge ratio is determined as ratio of fair value of the hedged item to fair value of the hedging instrument. A hedging relationship is considered effective if all of the following criteria are met:

- high effectiveness of the hedge can be expected on the basis of comparison of critical terms of the hedged item and the hedging instrument,
- in each reporting period, hedge ratio is within 80% - 125% range or relation of inefficiency amount to nominal value of the hedged item is less or equal than the threshold specified in documentation of the hedging relationship, where inefficiency amount is calculated as the sum of cumulative fair value changes of the hedged item and the hedging instrument,
- in each reporting period, simulation of hedge ratio in assumed evoluation of market reference rates scenarios is within 80% - 125% range.

As regards fair value hedge relationships, the main sources of ineffectiveness are:

- impact of the counterparty credit risk and own credit risk of the Group on the fair value of the hedging transactions (IRS), which is not reflected in the fair value of the hedged item,
- differences in maturities of the interest rate swaps and debt securities,
- differences in coupon amounts generated by the hedged item and hedging instruments.

The tables below present interest rate swaps which are used by the Group as instruments hedging interest rate risk in fair value hedge accounting as of 30 June 2018 and 31 December 2017.

(in PLN thousand)

Nominal values and interest rates of hedging derivatives - fair value hedge

30.06.2018	CONTRACTUAL MATURITY					TOTAL
	UP TO 1 MONTH	1 TO 3 MONTHS	3 MONTHS TO 1 YEAR	1 TO 5 YEARS	OVER 5 YEARS	
INTEREST RATE RISK						
Interest rate swaps (IRS) hedging fixed-rate debt securities in PLN						
Nominal value	-	-	-	455 000	200 000	655 000
Average fixed interest rate (%)	-	-	-	1.8	1.8	1.8
Interest rate swaps (IRS) hedging fixed-rate debt securities in EUR						
Nominal value	-	-	266 058	896 309	848 331	2 010 698
Average fixed interest rate (%)	-	-	0.2	0.9	0.1	0.4
Interest rate swaps (IRS) hedging fixed-rate debt securities in USD						
Nominal value	-	-	-	370 656	497 053	867 709
Average fixed interest rate (%)	-	-	-	5.2	3.6	4.3
Total nominal value	**-**	**-**	**266 058**	**1 721 965**	**1 545 384**	**3 533 407**

31.12.2017	CONTRACTUAL MATURITY					TOTAL
	UP TO 1 MONTH	1 TO 3 MONTHS	3 MONTHS TO 1 YEAR	1 TO 5 YEARS	OVER 5 YEARS	
INTEREST RATE RISK						
Interest rate swaps (IRS) hedging fixed-rate debt securities in PLN						
Nominal value	-	115 000	-	510 500	200 000	825 500
Average fixed interest rate (%)	-	1.8	-	1.8	1.8	1.8
Interest rate swaps (IRS) hedging fixed-rate debt securities in EUR						
Nominal value	-	-	-	1 028 127	894 658	1 922 785
Average fixed interest rate (%)	-	-	-	0.6	0.2	0.4
Interest rate swaps (IRS) hedging fixed-rate debt securities in USD						
Nominal value	-	-	-	205 397	601 429	806 826
Average fixed interest rate (%)	-	-	-	5.6	2.7	3.4
Total nominal value	**-**	**115 000**	**-**	**1 744 024**	**1 696 087**	**3 555 111**

Impact of fair value hedge on balance sheet and financial result – hedging instruments (interest rate risk)

30.06.2018	INTEREST RATE RISK		TOTAL
	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT AMORTISED COST	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	
Nominal value	200 000	3 333 407	3 533 407
Carrying amount – assets	-	32 845	32 845
Carrying amount – liabilities	3 106	145 247	148 353
Balance sheet item in which hedging instrument is reported	Hedging instruments	Hedging instruments	Hedging instruments
Amount of changes in fair value of the hedging instrument in the reporting period used for estimating hedge inefficiency	(849)	29 423	28 574
Amount of hedge ineffectiveness recognized in the income statement	463	1 536	1 999
Income statement item in which hedge ineffectiveness is reported	Result on fair value hedge accounting	Result on fair value hedge accounting	Result on fair value hedge accounting

(in PLN thousand)

Impact of fair value hedge on balance sheet and financial result – hedging instruments (interest rate risk)

31.12.2017	INTEREST RATE RISK		TOTAL
	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT AMORTISED COST	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	
Nominal value	255 500	3 299 611	3 555 111
Carrying amount – assets	365	16 131	16 496
Carrying amount – liabilities	2 357	183 745	186 102
Balance sheet item in which hedging instrument is reported	Hedging instruments	Hedging instruments	Hedging instruments
Amount of changes in fair value of the hedging instrument in the reporting period used for estimating hedge inefficiency	40	67 191	67 231
Amount of hedge ineffectiveness recognized in the income statement	20	4 596	4 616
Income statement item in which hedge ineffectiveness is reported	Result on fair value hedge accounting	Result on fair value hedge accounting	Result on fair value hedge accounting

Impact of fair value hedge on balance sheet and financial result – hedged items (interest rate risk)

30.06.2018	INTEREST RATE RISK		TOTAL
	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT AMORTISED COST	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	
Carrying amount – assets	202 239	3 552 356	3 754 595
Accumulated amount of the adjustment to the fair value of the hedged item included in the carrying amount of the hedged item recognized in the balance sheet - assets	2 536	161 648	164 184
Balance sheet item in which hedged item is reported	Investment securities – 5. Measured at amortised cost	Investment securities – 3. Measured at fair value through equity	
Change in the value of hedged item used for estimating hedge inefficiency in the reporting period	1 312	(27 887)	(26 575)
Accumulated amount of the adjustment to the fair value of the hedged item remaining in the balance sheet for those hedged items for which adjustments of the balance sheet item for adjustment to fair value has been discontinued	-	-	-

(in PLN thousand)

Impact of fair value hedge on balance sheet and financial result – hedged items (interest rate risk)

31.12.2017	INTEREST RATE RISK		TOTAL
	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT AMORTISED COST	INTEREST RATE SWAPS (IRS) HEDGING DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	
Carrying amount – assets	257 067	3 607 290	3 864 357
Accumulated amount of the adjustment to the fair value of the hedged item included in the carrying amount of the hedged item recognized in the balance sheet - assets	1 224	220 649	221 873
Balance sheet item in which hedged item is reported	Loans and advances to customers	Investment securities – 6. Available for sale	
Change in the value of hedged item used for estimating hedge inefficiency in the reporting period	(40)	(62 575)	(62 615)
Accumulated amount of the adjustment to the fair value of the hedged item remaining in the balance sheet for those hedged items for which adjustments of the balance sheet item for adjustment to fair value has been discontinued	-	-	-

Cash flow hedge accounting

The Group applies:

- cross-currency interest rate swaps (CIRS) to hedge exposure to interest rate risk related to volatility of market reference rates (WIBOR, LIBOR CHF) and exposure to currency risk. Portfolios of variable-rate loans denominated in CHF and deposits in PLN (which economically reflects to long-term variable-rate liability) are hedged items in this hedging relationship. CIRS transactions are decomposed into the part hedging the portfolio of assets and the part hedging the portfolio of liabilities,
- interest rate swaps (IRS) to hedge the exposure to interest rate risk related to the volatility of market reference rates (WIBOR), generated by portfolios of variable-rate loans denominated in PLN,
- currency swap (FX-Swap) to hedge the exposure to interest rate risk related to the volatility of market reference rates (EURIBOR, LIBOR USD), and the exposure to the currency risk, generated by portfolios of variable-rate of loans denominated in EUR and USD,
- interest rate swaps (IRS) to hedge the exposure to interest rate risk related to the volatility of market reference rates (WIBOR, EURIBOR), generated by portfolio of deposits denominated in PLN and EUR, which economically reflect a long-term, variable-rate liability.

Approach of the Group to hedging interest rate risk through cash flow hedge accounting is the same as the approach applied in the fair value hedge accounting as described above, i.e. only the component of interest rate risk related exclusively to volatility of market reference rates (in the case of cash flows hedge: WIBOR, EURIBOR, LIBOR USD, LIBOR CHF) is hedged. Approach of the Group to market risk management, including interest rate risk and currency risk, is presented in Note 7.2. Details regarding the Group's interest rate risk and currency risk exposure are disclosed in Note 7.2.

As in the case of the fair value hedge, using derivative instruments to hedge the exposure to interest rate risk and currency risk generates counterparty credit risk of the derivative transactions, which is not compensated by the hedged item. The Group manages this risk in a way similar to fair value hedge.

The Group applies cash flow hedge accounting to a hedging relationship if it is justified to expect that the hedge will be highly effective in achieving offsetting cash flow changes attributable to the hedged risk in the future and if assessment of hedge effectiveness indicates high effectiveness in all financial reporting periods for which the hedge was designated. The assessment is conducted using hypothetical derivative method.

Notes to financial statements (cont.)

(in PLN thousand)

According to the approach of the Group, a hedging relationship is considered effective if all of the following criteria are met:

- correlation coefficient between market reference rate of hedged items and market reference rate of hedging instrument is high,
- forecasted interest flows generated by hedged items are not lower than forecasted interest flows generated by hedging instruments,
- in each reporting period, ratio of the fair value of the hedged item to the fair value of the hedging instrument is within 80% - 125% range or relation of inefficiency amount to nominal value of the hedged item is less or equal to the threshold specified in documentation of the hedging relationship, where inefficiency amount is calculated as the sum of cumulative fair value changes of the hedged item and the hedging instrument,
- in each reporting period, ratio of fair value changes of the hedged item to the hedging instrument due to parallel fall or rise in yield curves by 100 basis point is within 80% - 125% range.

In the case of hedging interest rate and currency risk of portfolios of loans and deposits, the manner of managing these portfolios was adopted allowing for regular inclusion of new transactions in the hedging relationship and exclusion of transactions from the hedging relationship as a result of repayment or classification to non-performing category. As a result, the exposure of these portfolios to interest rate and currency risk is constantly changing. Because of frequent changes to term structure of the portfolio, the Group dynamically assigns the hedged items and allows for matching of hedging instruments to these changes.

As regards cash flow hedge relationships, the main sources of ineffectiveness are:

- impact of counterparty and the Group's own credit risk on the fair value of the hedging instruments, i.e. interest rate swap (IRS), cross-currency interest rate swap (CIRS), currency swap (FX swap) which is not reflected in the fair value of the hedged item,
- differences in repricing frequency of the hedging instruments and and hedged loans and deposits.

Nominal values of hedging derivatives – cash flow hedge

30.06.2018	CONTRACTUAL MATURITY					TOTAL
	UP TO 1 MONTH	1 TO 3 MONTHS	3 MONTHS TO 1 YEAR	1 TO 5 YEARS	OVER 5 YEARS	
INTEREST RATE RISK						
Interest rate swaps (IRS) hedging portfolios of variable-rate loans in PLN						
Nominal value	-	-	1 600 000	2 000 000	-	3 600 000
Average fixed interest rate (%)	-	-	3.6	3.7	-	3.7
Interest rate swaps (IRS) hedging portfolios of deposits in PLN economically reflecting long-term variable-rate liability						
Nominal value	-	-	-	150 000	207 000	357 000
Average fixed interest rate (%)	-	-	-	1.8	1.8	1.8
Interest rate swaps (IRS) hedging portfolios of deposits in EUR economically reflecting long-term variable-rate liability						
Nominal value	-	-	-	380 332	-	380 332
Average fixed interest rate (%)	-	-	-	(0.3)	-	(0.3)
INTEREST RATE RISK / CURRENCY RISK						
Cross-currency interest rate swap (CIRS basis swap) hedging portfolios of variable-rate loans in CHF and portfolios of deposits in PLN economically reflecting long-term variable-rate liability						
Nominal value	-	768 458	5 538 409	3 490 105	3 175 560	12 972 532
Average fixed interest rate (%)	-	-	-	-	-	-
Average exchange rate CHF/PLN	-	-	-	-	-	-
Currency swap (FX swap) hedging portfolios of variable-rate loans in EUR						
Nominal value	7 372 273	2 128 564	1 528 664	-	-	11 029 501
Average exchange rate CHF/PLN	4.3	4.3	4.4	-	-	4.3
Total nominal value	**7 372 273**	**2 897 022**	**8 667 073**	**6 020 437**	**3 382 560**	**28 339 365**

Notes to financial statements (cont.)

(in PLN thousand)

Nominal values of hedging derivatives – cash flow hedge

31.12.2017	CONTRACTUAL MATURITY					TOTAL
	UP TO 1 MONTH	1 TO 3 MONTHS	3 MONTHS TO 1 YEAR	1 TO 5 YEARS	OVER 5 YEARS	
INTEREST RATE RISK						
Interest rate swaps (IRS) hedging portfolios of variable-rate loans in PLN						
Nominal value	-	-	-	3 600 000	-	3 600 000
Average fixed interest rate (%)	-	-	-	3.7	-	3.7
Interest rate swaps (IRS) hedging portfolios of deposits in PLN economically reflecting long-term variable-rate liability						
Nominal value	-	-	15 000	-	197 000	212 000
Average fixed interest rate (%)	-	-	1.8	-	1.8	1.8
Interest rate swaps (IRS) hedging portfolios of deposits in EUR economically reflecting long-term variable-rate liability						
Nominal value	-	-	-	363 702	-	363 702
Average fixed interest rate (%)	-	-	-	(0.3)	-	(0.3)
INTEREST RATE RISK / CURRENCY RISK						
Cross-currency interest rate swap (CIRS basis swap) hedging portfolios of variable-rate loans in CHF and portfolios of deposits in PLN economically reflecting long-term variable-rate liability						
Nominal value	-	-	1 635 139	7 842 510	3 431 241	12 908 890
Average fixed interest rate (%)	-	-	-	-	-	-
Average exchange rate CHF/PLN	-	-	-	-	-	-
Currency swap (FX swap) hedging portfolios of variable-rate loans in EUR						
Nominal value	602 846	381 072	1 025 307	-	-	2 009 225
Average exchange rate CHF/PLN	4.4	4.3	4.4	-	-	4.4
Total nominal value	**602 846**	**381 072**	**2 675 446**	**11 806 212**	**3 628 241**	**19 093 817**

Impact of cash flow hedge on balance sheet and financial result – hedging instruments

30.06.2018	INTEREST RATE RISK		INTEREST RATE RISK / CURRENCY RISK		TOTAL
	INTEREST RATE SWAPS (IRS) HEDGING PORTFOLIO OF VARIABLE-RATE LOANS	INTEREST RATE SWAPS (IRS) HEDGING PORTFOLIO OF VARIABLE-RATE DEPOSITS	CROSS-CURRENCY INTEREST RATE SWAP (CIRS BASIS SWAP) HEDGING PORTFOLIO OF VARIABLE-RATE LOANS AND DEPOSITS	CURRENCY SWAP (FX SWAP) HEDGING PORTFOLIO OF VARIABLE-RATE LOANS	
Nominal value	3 600 000	737 332	12 972 532	11 029 501	28 339 365
Carrying amount – assets	111 020	343	-	268	111 631
Carrying amount – liabilities	-	3 492	788 095	72 695	864 282
Balance sheet item in which hedging instrument is reported	Hedging instruments	Hedging instruments	Hedging instruments	Hedging instruments	Hedging instruments
Change in the fair value of the hedging instrument used for estimating hedge ineffectiveness	(22 687)	(1 975)	3 900	(140)	(20 902)
Amount of hedge ineffectiveness recognized in the income statement	(11)	6	5	(27)	(27)
Income statement item in which hedge ineffectiveness is reported	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss

(in PLN thousand)

The effect of the cash flow hedge on balance sheet and financial result – hedging instruments

31.12.2017	INTEREST RATE RISK		INTEREST RATE RISK / CURRENCY RISK		TOTAL
	INTEREST RATE SWAPS (IRS) HEDGING PORTFOLIO OF VARIABLE-RATE LOANS	INTEREST RATE SWAPS (IRS) HEDGING PORTFOLIO OF VARIABLE-RATE DEPOSITS	CROSS-CURRENCY INTEREST RATE SWAP (CIRS BASIS SWAP) HEDGING PORTFOLIO OF VARIABLE-RATE LOANS AND DEPOSITS	CURRENCY SWAP (FX SWAP) HEDGING PORTFOLIO OF VARIABLE-RATE LOANS	
Nominal value	3 600 000	575 702	12 908 890	2 009 225	19 093 817
Carrying amount – assets	199 832	839	-	42 229	242 900
Carrying amount – liabilities	-	1 700	674 529	-	676 229
Balance sheet item in which hedging instrument is reported	Hedging instruments	Hedging instruments	Hedging instruments	Hedging instruments	Hedging instruments
Change in the fair value of the hedging instrument used for estimating hedge ineffectiveness	(59 492)	1 007	23 185	2 207	(33 093)
Amount of hedge ineffectiveness recognized in the income statement	(189)	-	(36)	(2)	(227)
Income statement item in which hedge ineffectiveness is reported	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss	Result on financial assets and liabilities measured at fair value through profit or loss

Impact of cash flow hedge on balance sheet and financial result – hedged items

30.06.2018	INTEREST RATE RISK		INTEREST RATE RISK / CURRENCY RISK		TOTAL
	PORTFOLIO OF VARIABLE-RATE LOANS	PORTFOLIO OF VARIABLE-RATE DEPOSITS	PORTFOLIO OF VARIABLE-RATE LOANS AND DEPOSITS	PORTFOLIO OF VARIABLE-RATE LOANS	
Amount of change in the fair value of a hypothetical derivative representing the hedged item used for estimating the hedge ineffectiveness in the reporting period	22 687	1 975	(12 055)	80	12 687
Revaluation reserve due to cash flow hedge accounting for relationships for which hedge accounting will be continued after the end of the reporting period	78 950	(966)	(91 904)	(353)	(14 273)
Revaluation reserve due to cash flow hedge accounting for relationships for which hedge accounting is no longer applied	-	-	-	-	-

31.12.2017	INTEREST RATE RISK		INTEREST RATE RISK / CURRENCY RISK		TOTAL
	PORTFOLIO OF VARIABLE-RATE LOANS	PORTFOLIO OF VARIABLE-RATE DEPOSITS	PORTFOLIO OF VARIABLE-RATE LOANS AND DEPOSITS	PORTFOLIO OF VARIABLE-RATE LOANS	
Amount of change in the fair value of a hypothetical derivative representing the hedged item used for estimating the hedge ineffectiveness in the reporting period	59 492	(1 007)	(43 838)	(2 191)	12 457
Revaluation reserve due to cash flow hedge accounting for relationships for which hedge accounting will be continued after the end of the reporting period	101 635	1 008	(95 804)	(258)	6 581
Revaluation reserve due to cash flow hedge accounting for relationships for which hedge accounting is no longer applied	-	-	-	-	-

(in PLN thousand)

Changes in the revaluation reserve from the valuation of hedging derivatives in cash flow hedge accounting

	I HALF 2018	2017
Opening balance	**6 581**	**39 724**
INTEREST RATE RISK		
Gains or losses resulting from hedging, recognized in other comprehensive income during the reporting period	(24 659)	(58 480)
Part of the loss transferred to the income statement due to the lack of expectation of materialization of the hedged item	-	(56)
Amount transferred from the revaluation reserves due to cash flow hedge accounting to the income statement as a reclassification adjustment, including:	-	-
Net interest income	-	-
Foreign exchange result	-	-
Amount transferred from the revaluation reserves due to cash flow hedge accounting and recognized as an adjustment to the carrying value of a non-financial asset or liability that is the subject of the hedged transaction	-	-
INTEREST RATE RISK / CURRENCY RISK		
Gains or losses resulting from hedging, recognized in other comprehensive income during the reporting period	3 805	25 393
Part of the loss transferred to the income statement due to the lack of expectation of materialization of the hedged item	-	-
Amount transferred from the revaluation reserves due to cash flow hedge accounting to the income statement as a reclassification adjustment, including:	-	-
Net interest income	-	-
Foreign exchange result	-	-
Amount transferred from the revaluation reserves due to cash flow hedge accounting and recognized as an adjustment to the carrying value of a non-financial asset or liability that is the subject of the hedged transaction	-	-
Closing balance	**(14 273)**	**6 581**

31. Investment (placement) securities

	30.06.2018	31.12.2017
Debt securities measured at amortised cost	10 647 866	X
Debt securities measured at fair value through other comprehensive income	30 755 181	X
Equity instruments designated at fair value through other comprehensive income	244 337	X
Equity instruments mandatorily measured at fair value through profit or loss	65 386	X
Debt securities available for sale (AFS)	X	33 276 590
Equity securities available for sale (AFS)	X	147 441
Debt securities held to maturity (HTM)	X	3 481 791
Total	**41 712 770**	**36 905 822**

The Group transferred Corporate and municipal debt securities from ‘Loans and advances to customers’ to the ‘Investment (placement) securities’ item. Before applying the requirements of IFRS 9, these items were presented as loans and advances to customers, as they were classified in the Loans and receivables category in accordance with IAS 39.

Notes to financial statements (cont.)

(in PLN thousand)

Debt securities measured at amortised cost

	30.06.2018	31.12.2017
Securities issued by State Treasury	4 164 579	X
T-bills	-	X
T-bonds	4 164 579	X
Securities issued by Central Banks	-	X
Securities issued by business entities	3 888 944	X
Securities issued by local governments	2 594 343	X
Total	**10 647 866**	**X**
including impairment of assets	(65 246)	X

Debt securities measured at fair value through other comprehensive income

	30.06.2018	31.12.2017
Securities issued by State Treasury	22 332 627	X
T-bills	-	X
T-bonds	22 332 627	X
Securities issued by Central Banks	2 999 646	X
Securities issued by business entities	1 966 123	X
Securities issued by local governments	3 456 785	X
Total	**30 755 181**	**X**
including impairment of assets (*)	(29 671)	X

(*) The impairment allowance for debt securities measured at fair value through other comprehensive income is included in the 'Revaluation reserve' item and does not reduce the carrying amount.

Debt securities available for sale (AFS)

	30.06.2018	31.12.2017
Securities issued by State Treasury	X	21 557 825
T- bills	X	-
T- bonds	X	21 557 825
Securities issued by Central Banks	X	11 066 168
Securities issued by business entities	X	-
Securities issued by local governments	X	652 597
Total	**X**	**33 276 590**
including impairment of assets	X	-

Debt securities held to maturity (HTM)

	30.06.2018	31.12.2017
Securities issued by State Treasury	X	3 450 338
T- bills	X	-
T- bonds	X	3 450 338
Securities issued by Central Banks	X	31 453
Total	**X**	**3 481 791**
including impairment of assets	X	-

Notes to financial statements (cont.)

(in PLN thousand)

Equity instruments designated at fair value through other comprehensive income

	30.06.2018	31.12.2017
Shares.	244 337	X
Total	**244 337**	**X**

Equity instruments mandatorily measured at fair value through profit or loss

	30.06.2018	31.12.2017
Shares	65 386	X
Total	**65 386**	**X**

Equity securities available for sale (AFS)

	30.06.2018	31.12.2017
Shares	X	147 404
Investment certificates	X	37
Total	**X**	**147 441**
including impairment of assets	X	(1 119)

Investment debt securities according to contractual maturity

	30.06.2018	31.12.2017
Debt securities, including:		
up to 1 month	5 310 770	11 112 757
between 1 and 3 months	78 913	121 753
between 3 months and 1 year	6 440 083	6 054 947
between 1 and 5 years	15 839 672	11 762 697
over 5 years	13 733 609	7 706 227
Total	**41 403 047**	**36 758 381**

Investment debt securities by currency

	30.06.2018	31.12.2017
PLN	36 021 660	32 997 942
EUR	3 191 336	2 091 122
USD	2 190 051	1 669 317
Total	**41 403 047**	**36 758 381**

(in PLN thousand)

32. Assets and liabilities held for sale

According to IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations' the Group identified non-current assets meeting requirements of IFRS 5 (concerning classification of non-current assets as held for sale) in the item 'Assets held for sale'.

As at 30 June 2018 non-current assets classified as held for sale are as follows:

- real estate,
- other property, plant and equipment.

Assets held for sale are presented below:

	30.06.2018	31.12.2017
ASSETS HELD FOR SALE		
Property, plant and equipment	24 897	42 197
Other assets	32 310	23 368
Total assets	**48 207**	**65 565**

The effect of disposal of other assets is as follows:

	I HALF 2018	I HALF 2017
Sales revenues	7 146	911
Net carrying amount of disposed assets (including sale costs)	(3 326)	(191)
Profit/loss on sale before income tax	**3 820**	**720**

33. Intangible assets

	30.06.2018	31.12.2017
Intangible assets, including:	743 461	777 997
research and development expenditures	157	1 073
licenses and patents	494 984	490 762
other	175 239	180 407
assets under construction	73 081	105 755
Goodwill	747 648	747 648
Total	**1 491 109**	**1 525 645**

In the period from 1 January to 30 June 2018 the Group acquired intangible assets in the amount of PLN 51 273 thousand (in 2017 – PLN 230 327 thousand).

In the period from 1 January to 30 June 2018 and in 2017 there have been no intangible assets whose title is restricted and pledged as security for liabilities.

Contractual commitments
As at 30 June 2018 the contractual commitments for the acquisition of intangible assets amounted to PLN 52 313 thousand, whereas as at 31 December 2017 - PLN 33 334 thousand.

(in PLN thousand)

34. Property, plant and equipment

	30.06.2018	31.12.2017
Non-current assets, including:	1 288 647	1 327 191
land and buildings	944 060	972 863
machinery and equipment	236 017	262 673
transport vehicles	47 979	53 983
other	60 591	37 672
Non-current assets under construction and prepayments	77 969	98 278
Total	**1 366 616**	**1 425 469**

In the period from 1 January to 30 June 2018 the Group acquired property, plant and equipment in the amount of PLN 36 853 thousand (in 2017 - PLN 140 311 thousand), while the value of property, plant and equipment sold amounted to PLN 12 663 thousand (in 2017 - PLN 605 thousand).

In the period from 1 January to 30 June 2018 and in 2017 there have been no property, plant and equipment whose title is restricted and pledged as security for liabilities.

Contractual commitments
As at 30 June 2018 the contractual commitments for the acquisition of property, plant and equipment amounted to PLN 11 391 thousand, whereas as at 31 December 2017 - PLN 20 801 thousand.

35. Assets pledged as security for liabilities

As at 30 June 2018 the Group held the following financial assets pledged as security for liabilities

TYPE OF TRANSACTION	SECURITY	CARRYING VALUE OF ASSETS PLEDGED AS SECURITY FOR LIABILITIES	NOMINAL VALUE OF ASSETS PLEDGED AS SECURITY FOR LIABILITIES	VALUE OF LIABILITIES SUBJECT TO SECURITY
Repo transactions	bonds	1 064 603	1 043 885	1 064 944
Coverage of Fund for protection of guaranteed assets to the benefit of the Bank Guarantee Fund	bonds	795 733	730 200	-
Coverage of payment commitments to the guarantee fund for the Bank Guarantee Fund	bonds	52 219	52 000	45 064
Coverage of payment commitments to the resolution fund for the Bank Guarantee Fund	bonds	108 049	107 600	196 740
Lombard and technical loan	bonds	4 582 237	4 472 733	-
Other loans	bonds	259 311	247 800	221 545
Issue of mortgage bonds	receivables backed by mortgage, bonds	1 513 959	1 514 836	1 184 199
Coverage of the Guarantee Fund for the Settlement of Stock Exchange Transactions to Central Securities Depository (KDPW)	bonds, cash deposits	44 593	44 429	-
Derivatives	bonds	379 692	378 099	307 799

(in PLN thousand)

As at 31 December 2017 the Group held the following financial assets pledged as security for liabilities

TYPE OF TRANSACTION	SECURITY	CARRYING VALUE OF ASSETS PLEDGED AS SECURITY FOR LIABILITIES	NOMINAL VALUE OF ASSETS PLEDGED AS SECURITY FOR LIABILITIES	VALUE OF LIABILITIES SUBJECT TO SECURITY
Repo transaction	bonds	1 088 646	1 045 716	1 089 876
Coverage of Fund for protection of guaranteed assets to the benefit of the Bank Guarantee Fund	bonds	763 927	770 200	-
Coverage of payment commitments to the guarantee fund for the Bank Guarantee Fund	bonds	32 488	32 000	26 858
Coverage of payment commitments to the resolution fund for the Bank Guarantee Fund	bonds	63 545	62 600	53 497
Lombard and technical loan	bonds	4 697 247	4 587 519	-
Other loans	bonds	320 074	317 300	234 731
Issue of mortgage bonds	receivables backed by mortgage, bonds	1 576 746	1 574 510	1 211 307
Coverage of the Gurantee Fund for the Settlement of Stock Exchange Transactions to Central Securities Depository (KDPW)	bonds, cash deposit	50 593	50 446	-
Derivatives	bonds	648 671	653 999	574 882

36. Amounts due to other banks

Amounts due to other banks by product type

	30.06.2018	31.12.2017
Current accounts	878 192	995 307
Interbank deposits and other liabilities	835 714	653 917
Loans and advances received	3 258 842	3 006 353
Repo transactions	416 038	301 439
Cash in transit	69 334	24 275
Total	**5 458 120**	**4 981 291**

Amounts due to other banks are measured at amortised cost.

Amounts due to other banks by currency

	30.06.2018	31.12.2017
PLN	1 930 915	1 635 684
CHF	605 535	591 405
EUR	2 817 287	2 654 770
USD	85 730	89 288
Other currencies	18 653	10 144
Total	**5 458 120**	**4 981 291**

(in PLN thousand)

37. Amounts due to customers

Amounts due to customers by entity and product type

	30.06.2018	31.12.2017
Amounts due to corporate, including:	52 280 982	57 397 810
current accounts	34 097 482	38 152 471
term deposits and other liabilities	18 183 500	19 245 339
Amounts due to budget entities, including:	11 001 524	12 192 129
current accounts	6 652 227	9 392 061
term deposits and other liabilities	4 349 297	2 800 068
Amounts due to individuals, including:	78 635 207	75 576 754
current accounts	46 117 301	43 101 222
term deposits and other liabilities	32 517 906	32 475 532
Repo transactions	648 906	788 436
Cash in transit	366 629	231 139
Total	**142 933 248**	**146 186 268**

Amounts due to customers are measured at amortised cost.

Amounts due to customers by currency

	30.06.2018	31.12.2017
PLN	116 966 241	119 945 891
CHF	302 397	336 479
EUR	15 860 334	16 487 441
USD	8 253 397	7 925 639
Other currencies	1 550 879	1 490 818
Total	**142 933 248**	**146 186 268**

38. Debt securities issued

Debt securities issued by type

	30.06.2018	31.12.2017
Liabilities from bonds	1 279 240	90 092
Certificates of deposit	1 418 865	1 470 000
Mortgage bonds	1 184 199	1 211 307
Total	**3 882 304**	**2 771 399**

Amounts debt securities issued are measured at amortised cost.

The Group redeems its own debt securities issued on a timely basis.

(in PLN thousand)

Debt securities issued by currency

	30.06.2018	31.12.2017
PLN	3 548 104	2 410 014
EUR	334 200	361 385
USD	-	-
Total	**3 882 304**	**2 771 399**

39. Subordinated liabilities

As at 30 June 2018

TYPE OF TRANSACTION	NOMINAL AMOUNT	CURRENCY	INTEREST RATE	ISSUE DATE	MATURITY DATE	SPECIAL TERMS	BALANCE SHEET VALUE AS AT 31.03.2018
Subordinated bonds	1 250 000	PLN	variable, WIBOR 6M + margin	30.10.2017	29.10.2027	Call option giving the Bank the right of early redemption within 5 years from the issue date, subject to the approval of the PFSA	1 257 013

As at 31 December 2017

TYPE OF TRANSACTION	NOMINAL AMOUNT	CURRENCY	INTEREST RATE	ISSUE DATE	MATURITY DATE	SPECIAL TERMS	BALANCE SHEET VALUE AS AT 31.12.2017
Subordinated bonds	1 250 000	PLN	variable, WIBOR 6M + margin	30.10.2017	29.10.2027	Call option giving the Bank the right of early redemption within 5 years from the issue date, subject to the approval of the PFSA	1 257 188

40. Provisions

Changes in provisions in the reporting period

I HALF 2018	PROVISIONS FOR LITIGATION AND CLAIMS	PROVISONS FOR DEFINED BENEFIT PLANS	PROVISIONS FOR UNDRAWN CREDIT FACILITIES AND GUARANTEES ISSUED	OTHER PROVISIONS	TOTAL
Opening balance	**17 132**	**300 248**	**236 909**	**48 333**	**602 622**
Initial application of IFRS 9	-	-	35 837	-	35 837
Opening balance - restated	**17 132**	**300 248**	**272 746**	**48 333**	**638 459**
Provision charges/revaluation	14 602	13 816	72 818	16 025	117 261
Provision utilization	(391)	(25 032)	-	(4 793)	(30 216)
Provision releases	(535)	-	(83 158)	-	(83 693)
Foreign currency exchange differences	-	-	1 098	-	1 098
Other changes	16 596	180	-	-	16 776
Closing balance	**47 404**	**289 212**	**263 504**	**59 565**	**659 685**
Short term	2 478	25 034	19 899	3 675	51 086
Long term	44 926	264 178	243 605	55 890	608 599

(in PLN thousand)

Changes in provisions in the reporting period

2017	PROVISIONS FOR LITIGATION AND CLAIMS	PROVISONS FOR DEFINED BENEFIT PLANS	PROVISIONS FOR UNDRAWN CREDIT FACILITIES AND GUARANTEES ISSUED	OTHER PROVISIONS	TOTAL
Opening balance	**8 551**	**294 014**	**220 983**	**36 844**	**560 392**
Provision charges/revaluation	10 428	27 931	71 221	47 861	157 441
Provision utilization	(6 554)	(14 068)	-	(5 644)	(26 266)
Provision releases	(1 329)	(41)	(53 690)	(111)	(55 171)
Foreign currency exchange differences	-	-	(1 605)	-	(1 605)
Business combinations	1 061	974	-	5 382	7 417
Other changes	4 975	(8 562)	-	(35 999)	(39 586)
Closing balance	**17 132**	**300 248**	**236 909**	**48 333**	**602 622**
Short term	4 281	33 893	50 514	9 354	98 042
Long term	12 851	266 355	186 395	38 979	504 580

Provisions for litigation and claims
Provisions for litigation and claims include court, administrative and other legal proceedings. The provisions were estimated in the amount of expected outflow of resources embodying economic benefits**.**

Provisions for defined benefits plans
Provisions for defined benefits plans consist of provisions for retirement benefits and death-in-service benefits.The present value of such obligations is measured by an independent actuary using the projected unit credit method.

Other provisions
Other provisions include in particular provisions for other employee benefits.

41. Contingent commitments

Court litigations

As at 30 June 2018 the Group is involved in the following, major in terms of the litigation value, court proceedings:

1) to be paid (brought against the Group):

- brought by the joint stock company's receiver in liquidation bankruptcy - claim for the payment of damages for the damage incurred as a result of Bank demanding immediate repayment of the balance resulting from the necessity to pay the price set under the debt balance assignment agreement and instigation of the debt enforcement proceedings concerning the remaining part of this price, the value of the litigation is PLN 57 450 130, date the proceedings were instigated – 30 April 2015, in the light of the present legal status of the proceedings, Bank evaluates the risk of the loss of funds as minor,
- brought by a guarantee beneficiary – claim for the payment of the guarantee issued by the Bank, the value of the litigation is PLN 55 996 064.23, date the proceedings were instigated – 20 May 2014, in the light of the present legal status of the proceedings, Bank evaluates the risk of the loss of funds as possible,
- brought by a guarantee beneficiary – claim for the payment of the guarantee issued by the Bank, the value of the litigation is PLN 43 760 219, date the proceedings were instigated – 29 January 2013, in the light of the present legal status of the proceedings, Bank evaluates the risk of the loss of funds as probable. On 27 June 2018 the Appellate Court in Warsaw announced the decision to dismiss the Bank's appeal in which the Bank had questioned in its entirety the decision of the Circuit Court in Warsaw of 23 May 2016 ordering the Bank to pay the amount of PLN 43 760 219. As the decision of the Appellate Court is legally binding and following the plaintiff's call, Bank made the payment of the claimed amount using the provision that had already been set aside. Bank addressed the Appellate Court with a request to be delivered the decision with the justification in order to consider the purposefulness of filing a cassation appeal,

(in PLN thousand)

- brought be an individual – claim for the payment by the Bank of the amount collected as a result of settlement of the forward financial transactions, the value of the litigation is PLN 38 916 555.18, date the proceedings were instigated – 02 October 2016, in the light of the present legal status of the proceedings, Bank evaluates the risk of the loss of funds as possible,
- brought by a guarantee beneficiary – claim for the payment of the guarantee issued by the Bank, the value of the litigation is PLN 32 750 000, date the proceedings were instigated – 14 January 2014, in the light of the present legal status of the proceedings, Bank evaluates the risk of the loss of funds as minor,
- brought by a guarantee beneficiary – claim for the payment of the guarantee issued by the Bank, the value of the litigation is PLN 29 204 684, date the proceedings were instigated – 16 January 2015, in the light of the present legal status of the proceedings, Bank evaluates the risk of the loss of funds as possible.

2) to be received (brought by Group):

- Bank's counterclaim for determination of the expiry of the bank guarantee and payment of the balance due from the debt assignment, value of the litigation is PLN 133 738 104.92, date the proceedings were instigated – 28 February 2013,
- brought by the Bank against the limited debtor (in possession) for the payment of the mortgage securing loan repayment, value of the litigation is PLN 132 877 901, date the proceedings were instigated – 21 January 2016,
- brought by the Bank for the payment of the loan balance and determination of existence of the balance due to the Bank, value of the litigation is PLN 111 165 487, date the proceedings were instigated – 29 January 2013.

None of the litigations pending before courts, authorities competent for arbitration proceedings or public administration authorities in the first half of year 2018 created any threat to the Bank's financial liquidity.

The Group created provisions for litigations against the Group entities which, according to the legal opinion, are connected with a risk of the funds outflow resulting from the fulfillment of the obligation. The value of the provisions as at 30 June 2018 is PLN 47 404 thousand (PLN 17 132 thousand as at 31 December 2017).

Financial commitments granted

Financial commitments granted by entity

	30.06.2018	31.12.2017
Financial commitments granted to:		
financial entities	1 260 244	785 430
non - financial entities	32 036 413	32 495 145
budget entities	921 619	599 409
Total	**34 218 276**	**33 879 984**

Guarantees issued

Guarantees issued by entity

	30.06.2018	31.12.2017
Issued to financial entities:	1 010 019	1 093 608
guarantees	1 004 387	1 093 608
confirmed export letters of credit	5 632	-
Issued to non - financial entities	11 508 552	9 970 336
guarantees	7 921 053	6 726 612
securities' underwriting guarantees	3 464 536	3 070 727
sureties	122 963	172 997
Issued to budget entities:	424 745	434 737
guarantees	21 830	13 186
securities' underwriting guarantees	402 915	421 551
Total	**12 943 316**	**11 498 681**

Notes to financial statements (cont.)

(in PLN thousand)

Off-balance sheet commitments received

Off-balance sheet commitments received by entity

	30.06.2018	31.12.2017
Financial received from:	1 281 141	384 961
financial entities	1 081 141	384 961
non - financial entities	200 000	-
budget entities	-	-
Guarantees received from:	17 112 799	13 871 406
financial entities	3 624 067	3 116 556
non - financial entities	12 512 274	9 824 811
budget entities	976 458	930 039
Total	**18 393 940**	**14 256 367**

Moreover, the Group has the ability to obtain financing from National Bank of Poland secured by government securities.

42. Additional information to the consolidated cash flow statement

Cash and cash equivalents

	30.06.2018	31.12.2017	30.06.2017
Cash and amounts due from Central Bank	8 014 221	5 236 318	6 735 048
Loans and receivables from banks with maturity up to 3 months	2 966 758	2 108 722	2 939 651
Cash and Cash equivalents presented in the cash flow statement	**10 980 979**	**7 345 040**	**9 674 699**

Restricted availability cash and cash equivalents as at 30 June 2018 amounted to PLN 4 991 812 thousand (PLN 4 786 930 thousand as at 31 December 2017, PLN 4 672 732 thousand as at 30 June 2017).

Changes in liabilities arising from financing activities

	BALANCE AS AT 1 JANUARY 2018	CHANGES FROM FINANCING CASH FLOWS	NON-CASH CHANGES				BALANCE AS AT 30 JUNE 2018
			CHANGES ARISING FROM OBTAINING OR LOSING CONTROL OF SUBSIDIARIES OR OTHER BUSINESSES	THE EFFECT OF CHANGES IN FOREIGN EXCHANGE RATES	CHANGES IN FAIR VALUES	OTHER CHANGES	
Debt securities issued	2 771 399	1 092 969	-	-	-	17 936	3 882 304
Subordinated liabilities	1 257 188	-	-	-	-	(175)	1 257 013
Loans and advances received	3 006 353	81 878	-	172 205	-	(1 594)	3 258 842
Total	**7 034 940**	**1 174 847**	**-**	**172 205**	**-**	**16 167**	**8 398 159**

Notes to financial statements (cont.)

(in PLN thousand)

	BALANCE AS AT 1 JANUARY 2017	CHANGES FROM FINANCING CASH FLOWS	NON-CASH CHANGES				BALANCE AS AT 30 JUNE 2017
			CHANGES ARISING FROM OBTAINING OR LOSING CONTROL OF SUBSIDIARIES OR OTHER BUSINESSES	THE EFFECT OF CHANGES IN FOREIGN EXCHANGE RATES	CHANGES IN FAIR VALUES	OTHER CHANGES	
Debt securities issued	1 522 963	(187 337)	-	-	-	(21 139)	1 314 487
Loans and advances received	3 249 417	(67 963)	-	(83 687)	-	(96 198)	3 001 569
Total	**4 772 380**	**(255 300)**	**-**	**(83 687)**	**-**	**(117 337)**	**4 316 056**

43. Related party transactions

The transactions between the Bank and related parties are typical transactions arising from current operating activities conducted by the Bank. Such transactions mainly include loans, deposits, foreign currency transactions and guarantees.

The credit granting process applicable to the Bank's management and entities related to the Bank
According to the Banking Act, credit transactions with Members of the Bank's Management Board and Supervisory Board, persons holding managerial positions at the Bank, with the entities related financially or organizationally therewith, shall be effected according to Regulation adopted by the Supervisory Board of the Bank.

The Regulation provides detailed decision-making procedures, applicable to transactions with such persons and entities, also defining the decision-making levels authorized to take decisions. In particular, the transactions with the Members of the Bank's Management Board or Supervisory Board or with an entity related therewith financially or organizationally, are subject to decisions taken by the Bank's Management Board and Supervisory Board.

Members of the Bank's Management Board and entities related therewith financially or organizationally may take advantage of credit products offered by the Bank on standard terms and conditions of the Bank. In particular, the Bank may not offer more advantageous credit interest rates to such persons or entities.

Credit risk assessment is performed using the methodology applied by the Bank, tailored to the client's segment and type of transaction.

In case of entities related to the Bank, the standard credit procedures are applied, with transaction-related decisions taken exclusively at level of the Bank's Head Office.

Notes to financial statements (cont.)

(in PLN thousand)

Related party transactions

Related party transactions as at 30 June 2018

NAME OF ENTITY	RECEIVABLES FROM LOANS AND PLACEMENTS	SECURITIES	RECEIVABLES FROM REVALUATION OF DERIVATIVES	OTHER RECEIVABLES	LIABILITIES FROM LOANS AND DEPOSITS	LIABILITIES FROM REVALUATION OF DERIVATIVES	OTHER LIABILITIES
PZU S.A. – the Bank's parent entity	-	-	-	4 752	8 408	-	414 838
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	2 719		25 495	4 877	66 055	1 426	1 727
Key management personnel of the Bank Pekao S.A.	466	-	-	-	8 949	-	-
Total	**3 185**	**-**	**25 495**	**9 629**	**83 412**	**1 426**	**416 565**

Receivables from loans and placements by contractual maturity

30.06.2018	CURRENT (*)	UP TO 1 MONTH	BETWEEN 1AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
PZU S.A. – the Bank's parent entity	-	-	-	-	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	1 599	926	32	102	60	-	2 719
Key management personnel of the Bank Pekao S.A.	-	-	-	9	60	397	466
Total	**1 599**	**926**	**32**	**111**	**120**	**397**	**3 185**

(*) Current receivables include Nostro account and cash collaterals.

Liabilities from loans and deposits by contractual maturity

30.06.2018	CURRENT (*)	UP TO 1 MONTH	BETWEEN 1AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
PZU S.A. – the Bank's parent entity	8 408	-	-	-	-	-	8 408
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	29 064	36 991	-	-	-	-	66 055
Key management personnel of the Bank Pekao S.A.	8 949	-	-	-	-	-	8 949
Total	**46 421**	**36 991**	**-**	**-**	**-**	**-**	**83 412**

(*) Current liabilities include Loro account and cash collaterals.

Notes to financial statements (cont.)

(in PLN thousand)

Receivables from loans and placements by currency

30.06.2018	EUR	USD	CHF	PLN	OTHER	TOTAL
PZU S.A. – the Bank's parent entity	-	-	-	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	-	-	2 719	-	2 719
Key management personnel of the Bank Pekao S.A.	-	-	398	68	-	466
Total	**-**	**-**	**398**	**2 787**	**-**	**3 185**

Liabilities from loans and deposits by currency

30.06.2018	EUR	USD	CHF	PLN	OTHER	TOTAL
PZU S.A. – the Bank's parent entity	314	-	-	8 094	-	8 408
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	1 386	6 803	1 834	55 349	683	66 055
Key management personnel of the Bank Pekao S.A.	3 651	453	150	4 689	6	8 949
Total	**5 351**	**7 256**	**1 984**	**68 132**	**689**	**83 412**

Notes to financial statements (cont.)

(in PLN thousand)

Related party transactions as at 31 December 2017

NAME OF ENTITY	RECEIVABLES FROM LOANS, ADVANCES AND PLACEMENTS	SECURITIES	RECEIVABLES FROM REVALUATION OF DERIVATIVES	OTHER RECEIVABLES	LIABILITIES FROM LOANS AND DEPOSITS	LIABILITIES FROM REVALUATION OF DERIVATIVES	OTHER LIABILITIES
PZU S.A. – the Bank's parent entity	-	-	-	1 733	477 485	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	1 463	-	489	824	489 058	5 062	11
Key management personnel of the Bank Pekao S.A.	458	-	-	-	8 118	-	-
Total	**1 921**	**-**	**489**	**2 557**	**974 661**	**5 062**	**11**

Receivables from loans and deposits by contractual maturity

31.12.2017	CURRENT (*)	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
PZU S.A. – the Bank's parent entity	-	-	-	-	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	900	110	-	192	261	-	1 463
Key management personnel of the Bank Pekao S.A.	-	-	-	6	28	424	458
Total	**900**	**110**	**-**	**198**	**289**	**424**	**1 921**

(*) Current receivables includude Nostro accounts and cash collaterals.

Liabilities due to loans and deposits by contractual maturity

31.12.2017	CURRENT (*)	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
PZU S.A. – the Bank's parent entity	3 978	473 507	-	-	-	-	477 485
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	6 249	482 809	-	-	-	-	489 058
Key management personnel of the Bank Pekao S.A.	5 511	-	2 607	-	-	-	8 118
Total	**15 738**	**956 316**	**2 607**	**-**	**-**	**-**	**974 661**

(*) Current liabilities include Loro accounts and cash collaterals.

Notes to financial statements (cont.)

(in PLN thousand)

Receivables from loans and deposits by currency

31.12.2017	EUR	USD	CHF	PLN	OTHER	TOTAL
PZU S.A. – the Bank's parent entity	-	-	-	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	93	-	-	1 370	-	1 463
Key management personnel of the Bank Pekao S.A.	-	-	387	71	-	458
Total	**93**	**-**	**387**	**1 441**	**-**	**1 921**

Liabilities due to loans and deposits by currency

31.12.2017	EUR	USD	CHF	PLN	OTHER	TOTAL
PZU S.A. – the Bank's parent entity	301	-	-	477 184	-	477 485
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	93	1	247	488 717	-	489 058
Key management personnel of the Bank Pekao S.A.	3 483	185	5	4 442	3	8 118
Total	**3 877**	**186**	**252**	**970 343**	**3**	**974 661**

Notes to financial statements (cont.)

(in PLN thousand)

Income and expenses from transactions with related parties for the period from 1 January 2018 to 30 June 2018

NAME OF ENTITY	INTEREST INCOME	INTERES EXPENSE	FEE AND COMMISSION INCOME	FEE AND COMMISSION EXPENSE	POSITIVE VALUATION OF DERIVATIVES AND OTHER INCOME	NEGATIVE VALUATION OFDERIVATIVES AND OTHER EXPENSES
PZU S.A. – the Bank 's parent entity	39	(88)	846	-	211	(3 661)
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities	170	(265)	8 438	(72)	2 227	(264)
Key management personnel of the Bank Pekao S.A.	1	(28)	-	-	-	-
Total	**210**	**(381)**	**9 284**	**(72)**	**2 438**	**(3 925)**

Income and expenses from transactions with related parties for the period from 1 January to 30 June 2017

NAME OF ENTITY	INTEREST INCOME	INTEREST EXPENSE	FEE AND COMMISSION INCOME	FEE AND COMMISSION EXPENSE	POSITIVE VALUATION OF DERIVATIVES AND OTHER INCOME	NEGATIVE VALUATION OF DERIVATIVES AND OTHER EXPENSES
PZU S.A. – the Bank 's parent entity (*)	5	(38)	1 855	-	3	(35)
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities (*)	7	(10)	729	(10)	554	(13)
UniCredit S.p.A. – the Bank's parent entity (**)	154	(153)	391	(1 197)	1 510	(3 825)
Entities of UniCredit Group excluding of Bank Pekao S.A. Group entities (**)	3 275	(1 253)	3 321	(62)	14 472	(1 725)
Associates of Bank Pekao S.A. Group						
Dom Inwestycyjny Xelion Sp. z o.o.	-	(187)	20	-	170	-
Pekao Investment Management S.A.	-	(829)	5	-	-	-
Pekao TFI S.A. (PIM S.A. subsidiary)	-	(715)	98 718	-	8	(3)
Total Associates of Bank Pekao S.A. Group	**-**	**(1 731)**	**98 744**	**-**	**178**	**(3)**
Key management personnel of the Bank Pekao S.A.	93	(163)	1	-	-	-
Total	**3 534**	**(3 348)**	**105 041**	**(1 269)**	**16 717**	**(5 601)**

(*) data from the date of taking control by PZU S.A.
(**) data until the day of loss of control by UniCredit S.p.A.

Notes to financial statements (cont.)

(in PLN thousand)

Off-balance sheet financial liabilities and guarantees as at 30 June 2018

NAME OF ENTITY	GRANTED		RECEIVED	
	FINANCIAL	GUARANTEES	FINANCIAL	GUARANTEE
PZU S.A. – the Bank's parent entity	2 789	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	555	6 000	-	6 000
Key management personnel of the Bank Pekao S.A.	592	-	-	-
Total	**3 936**	**6 000**	**-**	**6 000**

Off-balance sheet financial commitments and guarantees by contractual maturity

30.06.2018	CURRENT	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
FINANCIAL COMMITMENTS GRANTED							
PZU S.A. – the Bank's parent entity		-	-	-	2 789	-	2 789
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	20	-	-	535	-	555
Key management personnel of the Bank Pekao S.A.	10	-	-	31	129	422	592
Total	**10**	**20**	**-**	**31**	**3 453**	**422**	**3 936**
Guarantees issued							
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities	-	-	6 000	-	-	-	6 000
Total	**-**	**-**	**6 000**	**-**	**-**	**-**	**6 000**
Guarantees received							
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities	-	-	6 000	-	-	-	6 000
Total	**-**	**-**	**6 000**	**-**	**-**	**-**	**6 000**

Notes to financial statements (cont.)

(in PLN thousand)

Off-balance sheet financial commitments and guarantees by currency

30.06.2018	EUR	USD	CHF	PLN	OTHER	TOTAL
FINANCIAL COMMITMENTS GRANTED						
PZU S.A. – the Bank's parent entity	-	-	-	2 789	-	2 789
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	-	-	555	-	555
Key management personnel of the Bank Pekao S.A.	-	-	-	592	-	592
Total	**-**	**-**	**-**	**3 936**	**-**	**3 936**
Guarantees issued						
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities	-	-	-	6 000	-	6 000
Total	**-**	**-**	**-**	**6 000**	**-**	**6 000**
Guarantees received						
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities	-	-	-	6 000	-	6 000
Total	**-**	**-**	**-**	**6 000**	**-**	**6 000**

Notes to financial statements (cont.)

(in PLN thousand)

Off-balance sheet financial liabilities and guarantees as at 31 December 2017

NAME OF ENTITY	GRANTED		RECEIVED	
	FINANCIAL	GUARANTEES	FINANCIAL	GUARANTEE
PZU S.A. – the Bank's parent entity	2 509	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	599	-	-	-
Key management personnel of the Bank Pekao S.A.	553	-	-	-
Total	**3 661**	**-**	**-**	**-**

Off-balance sheet financial commitments and guarantees by contractual maturity

31.12.2017	CURRENT	UP TO 1 MONTH	BETWEEN 1 AND 3 MONTHS	BETWEEN 3 MONTHS AND 1 YEAR	BETWEEN 1 AND 5 YEARS	OVER 5 YEARS	TOTAL
FINANCIAL COMMITMENTS GRANTED							
PZU S.A. – the Bank's parent entity	-	-	-	-	2 509	-	2 509
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	20	-	-	579	-	599
Key management personnel of the Bank Pekao S.A.	10	-	-	24	126	393	553
Total	**10**	**20**	**-**	**24**	**3 214**	**393**	**3 661**

Off-balance sheet financial commitments and guarantees by currency

31.12.2017	EUR	USD	CHF	PLN	OTHER	TOTAL
FINANCIAL COMMITMENTS GRANTED						
PZU S.A. – the Bank's parent entity	-	-	-	2 509	-	2 509
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	-	-	599	-	599
Key management personnel of the Bank Pekao S.A.	-	-	-	553	-	553
Total	**-**	**-**	**-**	**3 661**	**-**	**3 661**

(in PLN thousand)

Remuneration expenses of the Bank's Management Board and Supervisory Board Members

	VALUE OF BENEFITS	
	I HALF 2018	I HALF 2017
Management Board of the Bank		
Short-term employee benefits (*)	5 382	6 502
Post-employment benefits	845	-
Long-term benefits (**)	3 207	1 438
Share-based payments (***)	-	5 460
Total	**9 434**	**13 400**
Supervisory Board of the Bank		
Short-term employee benefits (*)	788	445
Total	**788**	**445**

(*) Short-term employee benefits include: base salary, bonuses and other benefits due in next 12 months from the date of the balance sheet.
(**) The item 'Other long-term benefit' includes: provisions for deferred bonus payments.
(***) The value of share-based payments is a part of Personnel Expenses, recognized according to IFRS 2 during the reporting period in the income statement, representing the settlement of fair value of share options and shares, including phantom shares, granted to the Members of the Bank's Management Board.

The Bank's Management Board and Supervisory Board Members did not receive any remuneration from subsidiaries and associates in the period from 1 January to 30 June 2018 and in the period from 1 January to 30 June 2017.

Remuneration expenses of Supervisory Boards and Management Boards of subsidiaries

	VALUE OF BENEFITS	
	I HALF 2018	I HALF 2017
Companies' Management Boards		
Short-term employee benefits	9 897	8 335
Post-employment benefits	138	-
Long-term benefits	1 723	-
Termination benefits	1 603	-
Share-based payments	-	808
Total	**13 361**	**9 143**
Companies' Supervisory Boards		
Short-term employee benefits	480	126
Total	**480**	**126**

44. Subsequent events

Court litigation after the balance sheet day

On 19 July 2018 Bank was delivered a statement of claim brought by a legal person for the payment of EUR 17 521 646 (which at the average NBP rate of 19 July 2018 translated to PLN 75 610 347.81) resulting from an improper performance of the agreement. Bank in the process of preparing the answer to the claim and estimating the probability of funds outflow risk.

Signatures of the Management Board Members

Date	Name/Surname	Position/Function	Signature
07.08.2018	Michał Krupiński	President of the Management Board	
07.08.2018	Roksana Ciurysek-Gedir	Vice President of the Management Board	
07.08.2018	Andrzej Kopyrski	Vice President of the Management Board	
07.08.2018	Tomasz Kubiak	Vice President of the Management Board	
07.08.2018	Michał Lehmann	Vice President of the Management Board	
07.08.2018	Marek Lusztyn	Vice President of the Management Board	
07.08.2018	Tomasz Styczyński	Vice President of the Management Board	
07.08.2018	Marek Tomczuk	Vice President of the Management Board	

Glossary

Glossary

IFRS – International Financial Reporting Standards – the standards, interpretations and their structure adopted by the International Accounting Standards Board (IASB.)

IAS – International Accounting Standards – previous name of the standards forming part of the current IFRS.

IFRIC – International Financial Reporting Interpretations Committee – the committee operating under the International Accounting Standards Board publishing interpretations of IFRS.

CIRS – Currency Interest Rate Swap – the transaction exchange of principal amounts and interest payments in different currencies between two counterparties.

IRS – Interest Rate Swap – the agreement between two counterparties, under which the counterparties pay each other (at specified intervals during the contract life) interest on contractual principal of the contract, charged at a different interest rate.

FRA – Forward Rate Agreement – the contract under which two counterparties fix the interest rate that will apply in the future for a specified amount expressed in currency of the transaction for a predetermined period.

CAP – the financial agreement, which limits the risk borne by lender on a variable interest rate, exposed to the potential loss as a result of increase in interest rates. Cap option is a series of call options on interest rates, in which the issuer guarantees the buyer the compensation of the additional interest costs, that the buyer must pay if the interest rate on loan increases above the fixed interest rate.

FLOOR –the financial agreement, which limits the risk of incurring losses resulting from decrease in interest rates by the lender providing the loan at a variable interest rate. Floor option is a series of put options on interest rates, in which the issuer guarantees the interest to be paid on the loan if the interest rate on the loan decreases below the fixed interest rate.

IBNR – Incurred but Not Reported losses.

PD – Probability Default – the parameter used in Internal Ratings-Based Approach which determines the likelihood that the debtor will be unable to meet its obligation. PD is a financial term describing the likelihood of a default over an one year time horizon.

LGD – Loss Given Default – the percentage of loss over the total exposure when bank’s counterparty goes to default.

EAD – Exposure at Default.

EL – Expected Loss.

CCF – Credit Conversion Factor.

VaR – Value at Risk – the risk measure by which the market value of an asset or portfolio may be reduced for a given assumptions, probability and time horizon.

ICAAP – Internal Capital Adequacy Assessment Process – the process of assessing internal capital adequacy.