Report of Bank Pekao S.A. Group for the third quarter of 2018

Warsaw, November 2018

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Report on the activities of Bank Pekao S.A. Group for the third quarter of 2018

1 Highlights of Bank Pekao S.A. Group

The Group has adopted International Financial Reporting Standard 9 "Financial Instruments" (IFRS 9) 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.

	3 QUARTERS OF 2018	3 QUARTERS OF 2017	2017	2016
INCOME STATEMENT– SELECTED ITEMS				*(in PLN million)*
Operating income	5,713.5	5,328.0	7,350.4	7,347.2
Operating costs	(2,596.7)	(2,408.8)	(3,263.3)	(3,211.9)
Gross operating profit	3,116.8	2,919.2	4,087.1	4,135.3
Profit before income tax	2,070.6	1,899.2	3,153.0	2,896.5
Net profit for the period attributable to equity holders of the Bank	1,537.9	1,421.0	2,475.1	2,279.3
PROFITABILITY RATIOS				
Return on average equity (ROE)	9.1%	8.5%	11.0%	9.8%
Return on assets (ROA)	1.13%	1.11%	1.44%	1.38%
Net interest margin	2.83%	2.79%	2.78%	2.77%
Non-interest income / operating income	34.9%	35.2%	36.7%	39.6%
Cost / income	45.4%	45.2%	44.4%	43.7%
STATEMENT OF FINANCIAL POSITION – SELECTED ITEMS				*(in PLN million)*
Total assets	183,298.5	171,462.9	185,465.6	174,214.9
Customers' financing(*)	137,428.8	129,429.4	132,300.4	122,663.2
Amounts due to customers(**)	142,854.7	135,222.6	145,397.8	136,379.7
Debt securities issued and subordinated liabilities	6,010.0	2,435.9	4,028.6	1,523.0
Equity	22,000.3	22,268.4	23,267.8	22,911.9
STATEMENT OF FINANCIAL POSITION STRUCTURE RATIOS				
Customers' financing (*) / total assets	75.0%	75.5%	71.3%	70.4%
Securities / total assets	15.6%	15.8%	20.8%	20.6%
Deposits(***) / total assets	81.2%	80.3%	80.6%	79.2%
Customers' financing (*) / deposits(***)	92.3%	94.0%	88.5%	88.9%
Equity / total assets	12.0%	13.0%	12.5%	13.2%
Total capital ratio	17.0%	16.5%	17.1%	17.6%
EMPLOYEES AND NETWORK				
Total number of employees	16,906	17,381	17,339	17,757
Number of outlets	849	917	851	928
Number of ATMs	1,709	1,761	1,745	1,761

(*) Including net investments in financial leases to customers, non-quoted securities and excluding reverse repo transactions.

(**) Excluding repo transactions.

(***) Deposits include amounts due to customers, debt securities issued and subordinated liabilities.

Note: Since 2017, the financial data include results of Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.) and Dom Inwestycyjny Xelion Sp. z o.o. for eleven months of 2017 under the equity method and for December 2017 under full method.

Income statement data included in the table above and other notes to the Report on activities were presented according to income statement in a presentation form, which differs from the long form of the income statement presented in the Financial statements of the Group. Reconciliation of income statement in the presentation form and the long form is in the point 6.8 of the Report on activities.

2 Highlights of Bank Pekao S.A.

The Bank has adopted International Financial Reporting Standard 9 "Financial Instruments" (IFRS 9) with a date of transition of 1 January 2018. The Bank 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.

	3 QUARTERS OF 2018	3 QUARTERS OF 2017	2017	2016
INCOME STATEMENT– SELECTED ITEMS				*(in PLN million)*
Operating income	5,529.8	5,175.9	7,085.3	7,036.0
Operating costs	(2,356.7)	(2,237.1)	(3,024.5)	(2,991.4)
Gross operating profit	3,173.1	2,938.8	4,060.8	4,044.6
Profit before income tax	2,153.2	1,928.2	2,727.8	2,863.2
Net profit	1,650.8	1,472.5	2,088.1	2,278.4
PROFITABILITY RATIOS				
Return on average equity (ROE)	10.2%	9.0%	9.6%	10.1%
Return on assets (ROA)	1.24%	1.18%	1.24%	1.40%
Net interest margin	2.85%	2.79%	2.78%	2.76%
Non-interest income / operating income	30.2%	32.1%	34.0%	37.5%
Cost / income	42.6%	43.2%	42.7%	42.5%
STATEMENT OF FINANCIAL POSITION – SELECTED ITEMS				*(in PLN million)*
Total assets	177,494.5	168,364.1	182,077.0	170,988.9
Customers' financing (*)	131,400.0	126,120.7	128,873.2	119,033.6
Amounts due to customers (**)	143,371.6	135,474.7	146,109.9	136,629.9
Debt securities issued and subordinated liabilities	2,417.9	1,114.1	2,727.2	300.9
Equity	21,094.3	21,689.5	22,258.5	22,282.6
STATEMENT OF FINANCIAL POSITION STRUCTURE RATIOS				
Customers' financing (*) / total assets	74.0%	74.9%	70.8%	69.6%
Securities / total assets	16.0%	15.9%	21.1%	20.8%
Deposits(***) / total assets	82.1%	81.1%	81.7%	80.1%
Customers' financing (*) / deposits(***)	90.1%	92.3%	86.6%	86.9%
Equity / total assets	11.9%	12.9%	12.2%	13.0%
Total capital ratio	18.0%	17.0%	18.4%	18.2%
EMPLOYEES AND NETWORK				
Total number of employees	14,674	15,551	15,316	15,882
Number of outlets	849	917	851	928
Number of ATMs	1,709	1,761	1,745	1,761

(*) Including non-quoted securities and excluding reverse repo transactions.

(**) Excluding repo transactions.

(***) Deposits include amounts due to customers, debt securities issued and subordinated liabilities.

3 Summary of Performance

Net profit of Bank Pekao S.A. Group attributable to equity holders for the three quarters of 2018 amounted to PLN 1,537.9 million and was higher by PLN 83.9 million, i.e. 5.8% than pro-forma net profit(*) in the three quarters of 2017.

Thanks to the effective commercial activity of the Group in the three quarters of 2017, a significant growth in loan volumes in the area of retail loans (an increase of 10.4% year on year) as well as in the area of corporate loans (an increase of 5.3% year on year) was reported. Such increase in lending was financed by higher retail deposits growing by 8.8% year on year and corporate deposits growing by 1.8% year on year.

Total capital ratio (TCR) amounted to 17.0% as at the end of September 2018 and was higher (0.5 p.p.) compared to the end of September 2017.

The solid liquidity structure of Bank Pekao S.A. Group is reflected by net loans to deposits ratio at 92.3% as at the end of September 2018. This, together with high level of capital, enables for further sound and stable development of the Group's activities.

Main P&L items

In the three quarters of 2018, the Group's operating income amounted to PLN 5,713.5 million and was higher by 5.3% year on year than pro-forma operating income in the three quarters of 2017, with the following trends:

– Total net interest income, dividend income and income from equity investments in the three quarters of 2018, amounted to PLN 3,719.2 million and was higher by PLN 293.3 million, i.e. 8.6% compared to pro-forma total net interest income, dividend income and income from equity investments achieved in the three quarters of 2017, mainly driven by higher volumes of loans and deposits as well as higher margin.

– Net non-interest income in the three quarters of 2018, amounted to PLN 1,994.3 million and was lower by PLN 3.4 million, i.e. 0.2% compared to pro-forma net non-interest income in three quarters of 2017, with net fee and commission income (including fees on margins on foreign exchange transactions with clients) lower by 1.9% compared to the three quarters of 2017 mainly due to lower net fee and commission income on loans and cards.

The operating costs amounted to PLN 2,596.7 million in the three quarters of 2018. They were higher by PLN 141.5 million, i.e. 5.8% as compared with pro-forma operating costs in the three quarters of 2017, mainly due to higher personnel costs (mainly due to costs in the amount ca. of PLN 50 million, related to the Program Dobrowolnych Odejść – PDO addressed to Bank's employees obtaining pension right in 2018) and other administrative expenses (including mainly marketing related expenses). Operating costs excluding PDO expenses was higher by PLN 91.9 million, i.e. 3.7% as compared with pro-forma operating costs in the three quarters of 2017.

Guarantee funds charges in the three quarters of 2018, amounted to PLN 234.8 million, a decrease of PLN 11.6 million, i.e. 4.7% in comparison with the three quarters of 2017, due to lower annual contribution to the resolution fund of banks.

On February 1, 2016, tax on certain financial institutions under the Act on tax on certain financial institutions was introduced. In the three quarters of 2018, it amounted to PLN 417.8 million and was higher by PLN 34.4 million, i.e. 9.0% in comparison with the three quarters of 2017.

The Group's net impairment losses on financial assets and off-balance sheet commitments amounted to PLN 406.1 million in the three quarters of 2018, an increase of PLN 37.6 million, i.e. 10.2% as compared with the three quarters of 2017.

(*) For comparability purpose of achieved results income statement data for the third quarter of 2017 was presented as pro-forma, i.e. includes full consolidation of results of Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.) and Dom Inwestycyjny Xelion Sp. z o.o. acquired on December 11, 2017.

The Group decided to take advantage of the provisions of IFRS 9 that allow exemption not to restate comparative information for prior periods with respect to classification and measurement (including impairment) changes.

Report on the activities of Bank Pekao S.A. Group for the third quarter of 2018

Volumes

As at the end of September 2018, loans and advances at nominal value amounted to PLN 143,035.4 million, an increase of PLN 8,774.5 million, i.e. 6.5% in comparison to the end of September 2017 with the volume of retail loans growing by 10.4% and corporate loans growing by 5.3%.

As at the end of September 2018, amounts due to the Group's customers and debt securities issued amounted to PLN 148,864.7 million, an increase of PLN 11,206.2 million, i.e. 8.1% in comparison to the end of September 2017, with retail deposits growing by 8.8% and corporate deposits growing by 1.8% year on year.

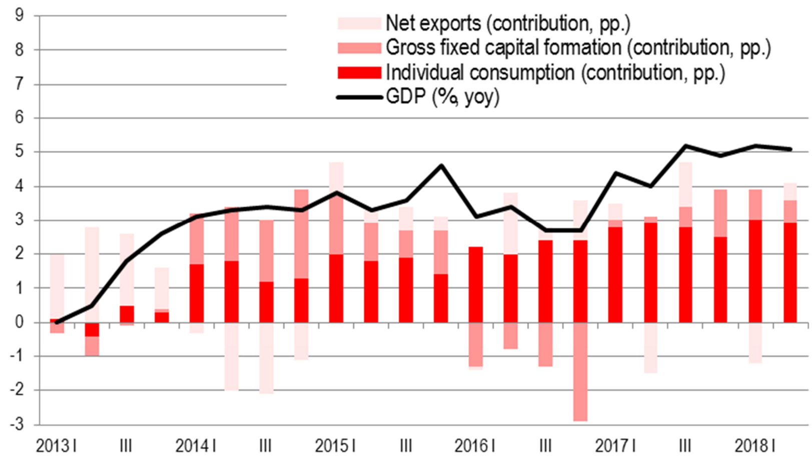
The value of net assets of investment funds managed by Pekao TFI S.A. (ex. Pioneer Pekao TFI S.A.) amounted to PLN 19,534.3 million as at the end of September 2018, an increase of PLN 1,639.0 million, i.e. 9.2% in comparison to the end of September 2017.

4 External Activity Conditions

Economic growth

In the second quarter of 2018, the economic growth amounted to 5.1% year on year as compared with the Gross Domestic Product (GDP) growth of 5.2% year on year in the first quarter of this year. Seasonally adjusted data indicate that in the second quarter of 2018, the GDP slowed to 1.0% quarter on quarter from 1.6% quarter on quarter growth posted in the previous quarter. Domestic demand expanded by 4.6% year on year as compared with 6.8% year on year increase in the first quarter of 2018, while foreign trade contributed 0.5 percentage point to the annual growth rate. Households consumption remained the main engine of economic growth (up by 4.9% year on year vs. 4.8% year on year in the first quarter of 2018). Rapid growth of private consumption growth was still supported by a robust growth of household's disposable income amid rising labour income and high social transfers. Investment activity intensified further in the first quarter of 2018, but the scale of the revival was still moderate. In the second quarter of 2018, gross fixed capital formation growth slowed to 4.5% year on year from an increase of 8.1% year on year in the first quarter of this year. Solid growth of public investments and investment outlays of large and mid-size enterprises was accompanied by mediocre investments of small firms.

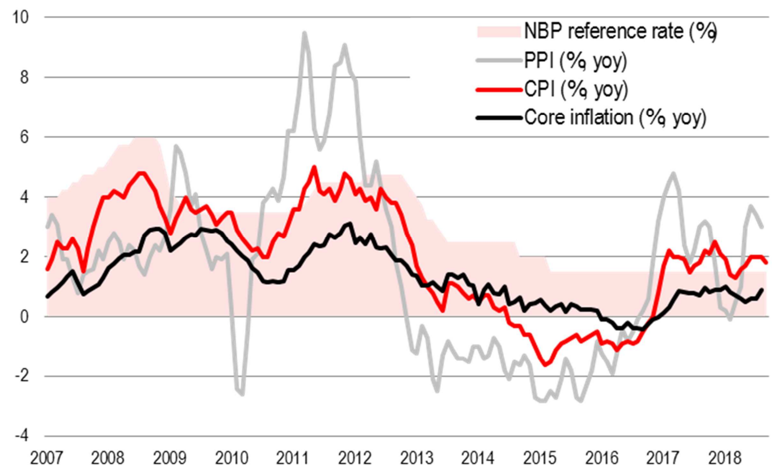
Recent declines of business sentiment indicators point to some slowdown in economic activity growth in the second half of 2018. Manufacturing PMI indicates declines in new orders, particularly export orders, in the Polish industry. In 2018, economic growth is expected of 4.8%.



Inflation and monetary policy

According to the Central Statistical Office (GUS) in September 2018, consumer prices increased by 1.9% year on year and for the tenth consecutive month was below the National Bank of Poland (NBP) target of 2.5% (+/-1 p.p.). In September consumer inflation was predominantly driven by an increase in transport prices (up by 7.0% year on year) and food prices (up by 2.3% year on year) that contributed 0.60 p.p. and 0.52 p.p. respectively to the annual CPI growth. In the third quarter of 2018, consumer prices increased by 2.0% year on year after an increase of 1.8% year on year in the second quarter of 2018.

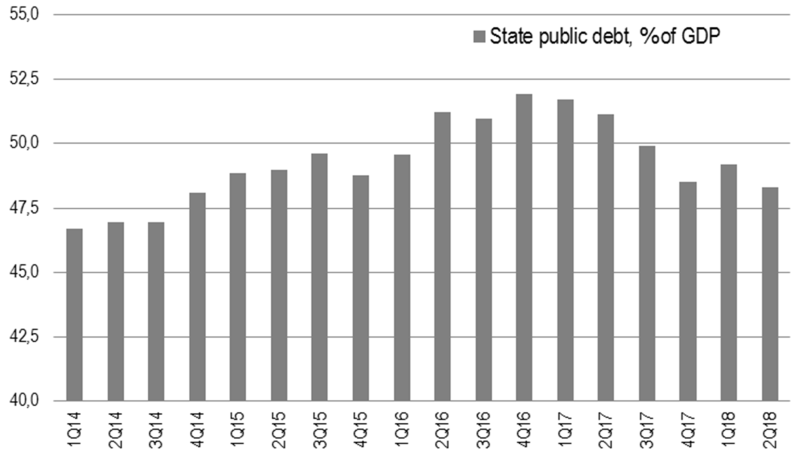
The Monetary Policy Council (MPC) kept the main policy rates unchanged in the third quarter of 2018. The National Bank of Poland reference rate stood at 1.50% and the Lombard rate at 2.50%. According to the MPC in the monetary policy transmission horizon inflation will remain close to the inflation target and the current level of interest rates is conducive to keeping the Polish economy on a sustainable growth path and maintaining macroeconomic stability.



Fiscal policy

After September 2018, the state public debt (cash basis) posted a surplus of PLN 3.2 billion, while the budget act envisages an annual deficit limit of PLN 41.5 billion. In the first nine months of 2018 budget revenues totaled PLN 272.9 billion (76.7% of an annual plan) and were PLN 10.6 billion (4.0%) higher than in the corresponding period of 2017. In the same period budget expenditures amounted to PLN 269.7 billion (67.9% of the annual plan) and were PLN 11.2 billion (4.3%) higher than in the first three quarters of 2017. After September VAT collections were PLN 5.5 billion (4.7%) higher than in the first three quarters of 2017, proceeds from excise duty went up by PLN 2.4 billion (4.7%), revenues from PIT increased by PLN 5.2 billion (13.9%) and CIT collections by PLN 3.7 billion (16.6%). With respect to expenditures, in the first nine months of 2018 subsidy to the Social Security Fund (FUS) was PLN 5.4 billion lower than in the corresponding period of 2017 amid robust growth of contribution collections linked to rising wages and employment. At the same time debt servicing costs increased by PLN 5.9 billion.

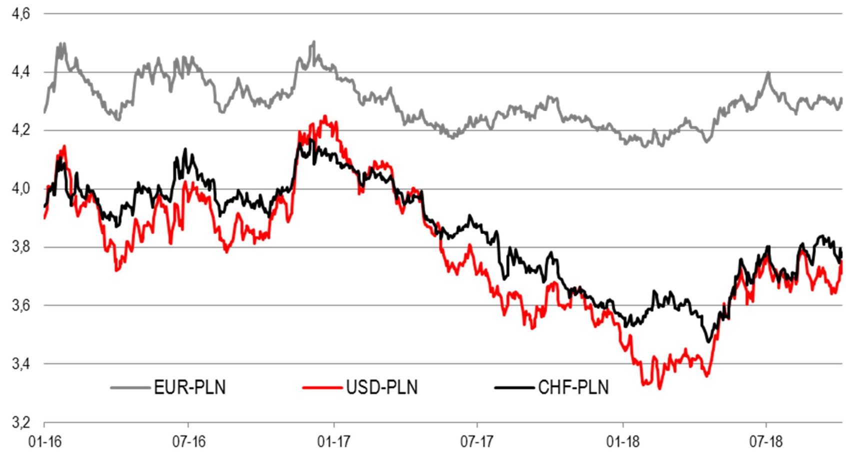
In the second quarter of 2018 the general government deficit amounted to PLN 2.5 billion as compared with a deficit of PLN 8.6 billion in the corresponding quarter of 2017. In cumulative annual terms the deficit moderated to 0.7% of GDP vs. 1.0% of GDP in the first quarter of 2018. At the end of the second quarter of 2018, the state public debt amounted to PLN 985.2 billion and was PLN 4.1 billion lower than at the end of the first quarter of 2018. Domestic debt went down by PLN 3.6 billion in the second quarter of 2018, while foreign debt declined by PLN 0.5 billion. In relation to the GDP the state public debt declined from 49.2% at the end of the first quarter of 2018 to 48.4% at the end of the second quarter of 2018. The general government debt increased from PLN 1,031.4 billion (51.3% of the GDP) at the end of the first quarter of 2018 to PLN 1,032.0 billion (50.7% of the GDP) at the end of the second quarter of 2018.



Currency market

In the third quarter of 2018, the dollar against the euro remained at elevated levels from the end of the previous quarter and the EUR-USD consolidated in a narrow range of 1.1575-1.1750. The main reason for the strong USD was still the increasing risk of faster Fed's monetary policy tightening in comparison to a dovish European Central Bank's stance regarding interest rates normalization. In September the Fed raised interest rates by 25 bps and next rate hike is very likely in December. The economic recovery in the US continues, while leading indicators indicate the gradual slowdown in the euro area. In mid-August, the dollar left the consolidation range for two weeks, strengthening against the euro to the highest level since mid-2017 (1.1340). The reason for the dollar appreciation was the currency crisis in Turkey and the ECB's concern about euro zone banks' exposure to Turkey. After several weeks of improving market sentiment and strengthening of the euro, at the end of the third quarter the single currency was under pressure because of the budget crisis in Italy. It is still expected the EUR-USD to decline towards 1.14 in the perspective of the end of the year, amid the growing divergence of the Fed and ECB interest rates.

In the third quarter of 2018 the zloty was relatively stable despite an unfavorable external environment. After a strong weakening of the zloty at the end of the second quarter of 2018, when the zloty was at the weakest level since January 2017 (4.41/EUR), the zloty took profits, among others, by strengthening of the dollar on the broad market and anchored in the consolidation range of 4.26-4.31/EUR. Due to the strong dollar and still weak market sentiment towards emerging markets, the USD-PLN rate remained at high levels around 3.70 throughout the third quarter of 2018. The zloty will continue to depend on developments in the global markets, but will be supported by still solid prospects of domestic economy.



Banking sector

According to the Financial Supervision Authority (KNF) data, in the first 8 months of 2018 net profit of the banking sector amounted to PLN 10.4 billion and increased 11.7% compared to the corresponding period of 2017.

In January-August 2018 total net operating income of the banking sector increased by 6.2% compared to the same period last year. This was due to an increase in net interest income by 8.6%, a drop in net fee and commission income by 4.2% and an increase in other income by 11.8%.

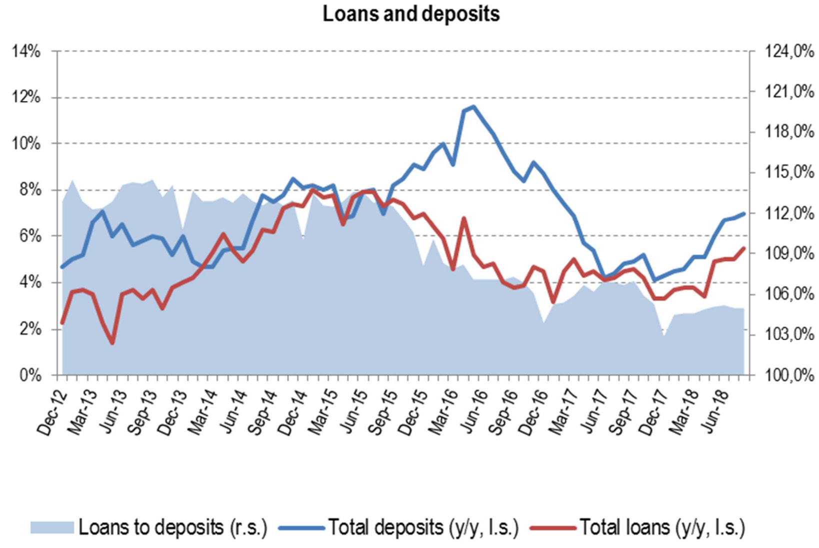
The operating costs of banks increased in January-August by 5.8% y/y, and the cost of risk (provisions and impairment losses on assets) went up by 4.8% y/y.

At the end of August 2018 total assets of the banking sector amounted to PLN 1,846 billion and were 5.8% higher compared to the end of August 2017. The total receivables from the non-financial sector increased by 5.1% y/y, and the total amount of deposits from this sector increased by 7.4%.

According to the NBP, at the end of September 2018 the nominal volume of loans to households was higher by 5.3% compared to the end of September 2017. Pace of growth increased in relation to the levels which were observed at the turn of the year. This was mainly due to relatively high interest in mortgage and consumer loans. It derives from the favorable economic situation of households and their strong sentiment.

The volume of loans and advances to enterprises increased by 5.4% in the same period. The relatively slow growth is due to lack of recovery in the small and medium-sized private companies' investments.

The volume of household deposits at the end of September 2018 increased by 7.8% in comparison to September 2017. Volume of corporate deposits grew at slightly lower pace – 6.0 % year on year. In both cases pace of growth was notably higher compared to the beginning of the year.



5 Internal Factors

5.1 Description of the Group

The Group's structure is presented in the Notes to the Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period of 9 months ended on 30 September 2018.

5.2 Changes in the Group's structure

Change of the Company names

On January 16, 2018, the registry court entered into the KRS register changes of Pekao Pioneer Powszechne Towarzystwo Emerytalne S.A. Statute resulting from the Extraordinary General Meeting of the Company resolution No. 38/2017 on November 9, 2017, including change of the Company's name, which currently is Pekao Powszechne Towarzystwo Emerytalne Spółka Akcyjna (ex. Pekao Pioneer Powszechne Towarzystwo Emerytalne Spółka Akcyjna).

On February 15, 2018, the registry court made an entry in the Register of Entrepreneurs of the National Court Register amending the Statute of Pioneer Pekao Investment Management S.A. resulting from the resolution of the Extraordinary General Meeting of the Company adopted on December 20, 2017, including the change of the Company's name, which currently is Pekao Investment Management S.A.

Transfer of management of Pekao OFE and DFE Pekao funds

On April 24, 2018, the Polish Financial Supervision Authority issued a consents 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 May 19, 2018, PTE PZU S.A. has taken over the management of Pekao OFE and DFE Pekao funds.

On June 1, 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.

Share Capital Increase

On June 4, 2018, the District Court registered the increase of share capital of Pekao Financial Services Sp. z o.o. related to the transaction of the takeover by the Company, pursuant to art. 529 § 1 point 4 of the Code of Commercial Companies (division by separation) of an organized part of the enterprise separated from PZU Centrum Operacji S.A. covering the activities of the transfer agent.

As a result, a new shareholder of the Company PZU SA was disclosed in the National Court Register, which took up shares in the increased share capital in the amount of 4,534 with the total value of PLN 2,267,000. At present, the share capital of the Company amounts to PLN 6,767,000. Bank Pekao S.A. holds 66.50% of votes and capital of the Company, while PZU S.A. holds 33.50%.

5.3 Changes in the Statutory Bodies of the Bank

Supervisory Board

As of September 30, 2018, the composition of the Supervisory Board of Bank Pekao S.A. has not changed in comparison with December 31, 2017 and it was as follows:

SEPTEMBER 30, 2018	DECEMBER 31, 2017
Paweł Surówka Chairman of the Supervisory Board	Paweł Surówka Chairman of the Supervisory Board
Joanna Błaszczyk Deputy Chairman of the Supervisory Board	Joanna Błaszczyk Deputy Chairman of the Supervisory Board
Stanisław Ryszard Kaczoruk Deputy Chairman of the Supervisory Board	Stanisław Ryszard Kaczoruk Deputy Chairman of the Supervisory Board
Paweł Stopczyński Secretary of the Supervisory Board	Paweł Stopczyński Secretary of the Supervisory Board
Sabina Bigos-Jaworowska Member of the Supervisory Board	Sabina Bigos-Jaworowska Member of the Supervisory Board
Justyna Głębikowska-Michalak Member of the Supervisory Board	Justyna Głębikowska-Michalak Member of the Supervisory Board
Grzegorz Janas Member of the Supervisory Board	Grzegorz Janas Member of the Supervisory Board
Michał Kaszyński Member of the Supervisory Board	Michał Kaszyński Member of the Supervisory Board
Marian Majcher Member of the Supervisory Board	Marian Majcher Member of the Supervisory Board

Management Board of the Bank

As of September 30, 2018, the composition of the Management Board of Bank Pekao S.A. has changed in comparison with December 31, 2017 and it was as follows:

SEPTEMBER 30, 2018	DECEMBER 31, 2017
Michał Krupiński President of the Management Board	Michał Krupiński President of the Management Board
Roksana Ciurysek-Gedir Vice President of the Management Board	Andrzej Kopyrski Vice President of the Management Board
Andrzej Kopyrski Vice President of the Management Board	Tomasz Kubiak Vice President of the Management Board
Tomasz Kubiak Vice President of the Management Board	Michał Lehmann Vice President of the Management Board
Michał Lehmann Vice President of the Management Board	Marek Lusztyn Vice President of the Management Board
Marek Lusztyn Vice President of the Management Board	Tomasz Styczyński Vice President of the Management Board
Tomasz Styczyński Vice President of the Management Board	Marek Tomczuk Vice President of the Management Board
Marek Tomczuk Vice President of the Management Board	

5.4 The Bank's shareholding structure

As at September 30, 2018, the share capital of Bank Pekao S.A. amounted to PLN 262,470,034, it was divided into 262,470,034 shares and remained unchanged until the date of submitting the report.

All the existing shares are ordinary bearer shares. There are no special preferences or limitations connected with the shares, or differences in the rights attached to them. The rights and obligations related to the shares are defined by the provisions of the Polish Commercial Companies Code and other applicable law.

Shareholders of Bank Pekao S.A., holding directly or indirectly, through subsidiaries, at least 5% of the total number of votes at the General Meeting of the Bank, are as follows:

SHAREHOLDER'S NAME	NUMBER OF SHARES AND VOTES AT THE GENERAL MEETING	SHARE IN SHARE CAPITAL AND TOTAL NUMBER OF VOTES AT THE GENERAL MEETING	NUMBER OF SHARES AND VOTES AT THE GENERAL MEETING	SHARE IN SHARE CAPITAL AND TOTAL NUMBER OF VOTES AT THE GENERAL MEETING
	AS AT THE DATE OF SUBMITTING THE REPORT FOR THE THIRD QUARTER OF 2018		AS AT THE DATE OF SUBMITTING THE REPORT FOR THE FIRST HALF OF 2018	
Powszechny Zakład Ubezpieczeń S.A.	52,494,007	20.00%	52,494,007	20.00%
Polski Fundusz Rozwoju S.A.	33,596,166	12.80%	33,596,166	12.80%
UniCredit S.p.A.	16,430,000	6.26%	16,430,000	6.26%
Nationale-Nederlanden Powszechne Towarzystwo Emerytalne S.A.	13,357,769	5.09%	13,357,769	5.09%
Other shareholders (below 5%)	146,592,092	55.85%	146,592,092	55.85%
Total	**262,470,034**	**100.00%**	**262,470,034**	**100.00%**

In the current report No. 8/2018, the Management Board of Bank Pekao S.A. informed that on June 8, 2018 the Bank has received notice from Nationale-Nederlanden Powszechne Towarzystwo Emerytalne S.A. (hereinafter NN PTE), about a change in the total number of votes at the General Meeting of the Bank.

According to the information provided in the received notification by NN PTE, as a result of the acquisition of the Bank's shares in transactions on the Warsaw Stock Exchange, settled on June 4, 2018, funds managed by NN PTE: Nationale-Nederlanden Otwarty Fundusz Emerytalny (hereinafter OFE) and Nationale-Nederlanden Dobrowolny Fundusz Emerytalny (hereinafter DFE) increased the ownership of the Bank's shares above 5% of votes at the General Meeting of the Bank.

After the settlement of the transaction on June 4, 2018, the securities accounts of OFE and DFE included 13,357,769 shares of the Bank, which account for 5.09% of the Bank's share capital. These shares entitle to 13,357,769 votes at the General Meeting of the Bank, which constitutes 5.09% of the total number of votes.

5.5 Financial credibility ratings

5.5.1 Bank Pekao S.A. financial credibility ratings

Bank Pekao S.A. co-operates with three leading credit rating agencies: Fitch Ratings, S&P Global Ratings, and Moody's Investors Service. In the case of the first two agencies, the ratings are provided on a solicited basis under relevant agreements and with respect to Moody's Investors Service the ratings are unsolicited and they are based on publicly available information and review meetings.

As of September 30, 2018, Bank Pekao S.A. was assigned following financial credibility ratings:

FITCH RATINGS(*)	**BANK PEKAO S.A.**	**POLAND**
Long-term IDR	A-	A-
Outlook	Negative	Stable
Short-term IDR	F2	F2
Viability Rating	a-	-
Support Rating	5	-
Support Rating Floor	No Floor	-
S&P GLOBAL RATINGS	**BANK PEKAO S.A.**	**POLAND(**)**
Issuer Credit Rating (ICR)		
Long-term ICR in foreign currencies	BBB+	BBB+
Long-term ICR in domestic currency	BBB+	A-
Short-term ICR in foreign currencies	A-2	A-2
Short-term ICR in domestic currency	A-2	A-2
Stand-alone credit profile	bbb	-
Outlook	Stable	Positive
Resolution Counterparty Rating (RCR) (***) (****)		
Long-term RCR in foreign currencies	BBB+	-
Long-term RCR in domestic currency	BBB+	-
Short-term RCR in foreign currencies	A-2	-
Short-term RCR in domestic currency	A-2	-
MOODY'S INVESTORS SERVICE (UNSOLICITED RATING)	**BANK PEKAO S.A.**	**POLAND**
Long-term foreign-currency deposit rating	A2	A2
Short-term deposit rating	Prime-1	Prime-1
Baseline Credit Assessment	baa1	-
Long-term counterparty risk assessment	A1(cr)	-
Short-term counterparty risk assessment	Prime-1(cr)	-
Outlook	Stable	Stable

(*) On October 17, 2018, Fitch Ratings has changed the following ratings of Bank Pekao S.A.:

Long-term Issuer Default Rating (IDR) from "A-" to "BBB+"

Outlook on long-term IDR from "Negative" to "Stable"

Viability Rating (VR) from "a-" to "bbb+";

Other Bank's ratings Fitch Ratings confirmed at the unchanged level.

(**) On October 12, 2018, S& P Global Ratings changed following ratings of Poland:

Long-term in foreign currencies from "BBB +" to "A-"

Long-term in the national currency from "A-" to "A"

Outlook on the long-term domestic and long-term ratings from "Positive" to "Stable"

(***) On July 16, 2018 S&P Global Ratings introduced a new rating category Resolution Counterparty Rating (RCR)

(****) On October 15, 2018 S&P Global Ratings confirmed the Issuer Credit Rating of Bank Pekao S.A. and at the same time upgraded Bank's RCR long-term rating from "BBB+" to "A-". The short-term RCR was confirmed at the "A-2" level.

5.5.2 Pekao Bank Hipoteczny S.A. financial credibility ratings

As the end of September Fitch Ratings agency assigned the “A” rating to the covered bonds issued by Pekao Bank Hipoteczny S.A., a 100% subsidiary of Bank Pekao S.A.

The high rating assigned to the covered bonds confirms Pekao Bank Hipoteczny’s ability to issue securities offering a high level of security and raise long-term capital to fund its lending activity. On October 18, 2018 agency updated long term IDR rating from A- to BBB+ and changed outlook from Negative to Stable. As a result of the lower rating of the Bank, Bank Hipoteczny S.A. on October 22, 2018, the rating of mortgage bonds was updated from A - the new rating for the letters is A-.

5.6 Achievements of Bank Pekao S.A.

Bank Pekao S.A. is a universal commercial bank providing a full range of banking services to individual and institutional clients, mainly in Poland. Bank Pekao S.A. Group includes financial institutions operating in banking, asset management, pension funds, brokerage services, transactional advisory, leasing and factoring markets.

Distribution channels
The Bank offers to its clients a broad distribution network with ATMs and outlets conveniently located throughout Poland.

	30.09.2018	30.09.2017
Total number of outlets	849	917
Total number of own ATMs	1,709	1,761

As at the end of September 2018, the Bank maintained 5,876.4 thousand PLN-denominated current accounts, 373.9 thousand mortgage loan accounts and 669.6 thousand “Pożyczka Ekspresowa” (Express Loan) loan accounts.

(in thousand)

	30.09.2018	30.09.2017
Total number of PLN current accounts(*)	5,876.4	5,582.0
of which packages	4,309.0	4,143.4
Number of mortgage loans accounts(**)	373.9	349.2
of which PLN mortgage loans accounts	341.4	315.6
Number of “Pożyczka Ekspresowa” loan accounts(***)	669.6	619.0

(*) Number of accounts including accounts of prepaid cards.
(**) Retail customers accounts.
(***) “Pożyczka Ekspresowa”, Pożyczka Ekspresowa Biznes.

Individual clients

Individual clients service
In the third quarter of 2018, Bank Pekao S.A. continued realization the new strategy of development for 2018-2020 "Strength of the Polish Bison". The basis for the Bank's growth in the area of individual customer is a significant increase in account numbers thanks to, among others, a new offer and outstanding quality.

In the third quarter of 2018, the sale of Konto Przekorzystne introduced to its offer at the beginning of the year was higher by 39% compared to the same period of 2017. After three quarters of 2018 the total number of sales of ROR accounts was higher by 35% in comparison with the same period of 2017. The Bank continued promotion of Konto Przekorzystne with multicurrency card addressed to the persons traveling abroad. As at the end of September 2018, the sale of multicurrency card amounted to 324 thousand numbers of cards and was five times higher in comparison with the same period of 2017.

Bank Pekao S.A. strengthens its leading position among banks acquiring young customers. In 2018, the Bank recorded double-digit growth dynamics in the number of customers aged up to 26 (13.9% year on year). The largest growth in the number of customers concerned young people aged 13-17 (24.4% year on year). The Bank provides services for nearly 200 thousand students, which translated into a 14% market share. In September 2018 the Bank started the next edition of over 1 thousand of education events in schools and universities that promote personal finance management with the use of digital banking service.

From July 2018 the Bank allowed customers of the Pekao24 Internet banking system to submit application within the framework of the government “Dobry start” – program PLN 300 for a school layette as well as application in Family 500 plus Government Program for new period.

Bank Pekao S.A. is a leading bank in providing services for foreigners with over 25% market share in this area. The largest group among foreigners using banking services in Poland are Ukrainian citizens, therein almost every fourth is a customer of Bank Pekao S.A. In July 2018 the Bank's offer for the Ukrainian citizen was extended by mobile application PeoPay and mobile service m.pekao24.pl in Ukrainian language. Within the framework PeoPay mobile banking application Bank provides customers solution such as checking balance accounts, payment transfer and FX conversion with a preferential rate 24/7. In addition Bank's offer for the Ukrainian citizens free of charge transfers in EUR and USD to Ukraine.

Within the new legal regulations, the Bank's offer was extended to "Basic Account". The offer is addressed to people who did not have any bank account so far. The Bank offers free account maintenance, free access to electronic banking and service of payment card.

In July 2018, the Bank introduced to its offer for affluent client a new Konto Świat Premium account, which replaced previous existing line of Premium account. Konto Świat Premium account is the account of the Bank with full range of products and banking services such as: a high interest of Konto Oszczędnościowe Premium saving account, gold payment card, free of charge foreign currency accounts in thirteen currencies, no fees for SMS notifications and balance confirmation as well as free opening and maintenance account in Dom Maklerski. An additional advantage of the offer is free of charge cash withdrawals from all domestic and abroad ATMs, as well as cash payment in branch office by consultant or via electronic banking services.

In the third quarter of 2018, the Bank promoted also credit cards. Customers received new cards without an annual fee, and current users could take advantage of purchases with a zero interest rate and attractive discounts on card payments. Bank Pekao S.A. serves over 700, thousand credit cards and cards with deferred payment dates, issued to individual customers.

Lending products

The Bank continues activities aimed at building leading position on consumer goods financing market. As at the end of September 2018 increase of cash loans portfolio for individual clients amounted to 19% year on year. Sale of cash loans was supported by competitive offer of Pożyczka Ekspresowa (Express Loan), individual loan offers with the use of CRM tools as well as active use of electronic channels including the PeoPay mobile banking and the Pekao24 Internet banking system.

Loan offer within the framework of process „na klik" ("by click") with fast and fully automated loan granting procedure in the Internet service and mobile applications on phone and tablet regularly attracted new customers. In 2018 the Bank granted loans within framework of process "na klik" higher by 72% in comparison in the same period of 2017. In the third quarter of 2018, almost every third loan was granted in this process and the customer may receive funds on their account within 30 seconds after loan approval.

The Bank conducted an advertising campaign of cash loan on the Internet, social media, countrywide radio channels, the largest shopping centers, public transportation and in the Bank's outlets and ATMs was launched.

In the third quarter of 2018 the Bank once again time achieved a record-high result in a sale of mortgage loans, granting loans for the amount of nearly PLN 2.3 billion (increase by 10% year on year). Market share in sale of new mortgage loans amounted to over 19%.

The Bank's offer in the field of housing loans was adjusted to the changing market conditions and customer needs. In the third quarter of 2018, the mortgage loan offered by the Bank was recognized and honored in many publications and rankings. The Bank took the second place in the category: mortgage loan in the largest Plebiscite "Golden Banker", and 1st place in the "Friendly Bank NEWSWEEK 2018" ranking in the mortgage loan category.

Savings, investment and Insurance products

In the third quarter of 2018 within the scope of savings products The Bank actively promoted the new "Konto Oszczędnościowe" account and introduced to its offer "Konto Oszczędnościowe Premium" account dedicated to the customers to Bankowości Premium. The Banks' customers could take an advantage from promotional interest rate of 3.0% on a "Konto Oszczędnościowe" account up to the amount of PLN 20 thousand for a period of 12 months, and 3.0% on "Konto Oszczędnościowe Premium" account up to the amount of PLN 100 thousand for a period of 6 months.

In the 2018, individual customer's deposits increased by PLN 4.9 billion and were higher by 7.4% in comparison to December 2017, while in comparison to the September of 2017 increased by PLN 6.8 billion (10.5% year on year).

In the third quarter of 2018 the Bank introduced to its offer new investment products. Structured products was enhanced by Certificates financial companies 2 (based on the change in prices of the basket of financial companies) as well as Certyfikat Silny Złoty EUR/PLN (based on currency rates EUR/PLN). As part of pension programs, IKZE DFE PZU (Indywidualne Konto Zabezpieczenia Emerytalnego) was introduced, managed by Powszechne Towarzystwo Emerytalne PZU S.A. (PTE PZU), the aim of which is to achieve stable growth in the long term.

In the area of investment insurance, the offer was extended to include voluntary life insurance with insurance capital funds prepared by PZU Życie S.A. – Świat Inwestycji Premium. The new proposal has made the offer more attractive by extending the diversification of investment portfolios and products. After three quarters of 2018, total sales of investment products net amounted to over PLN 1.4 billion (increase by 70% year on year).

In the third quarter of 2018, the Bank actively promoted the PZU travel insurance campaign in the electronic channels offered by the Moje PZU portal.

Brokerage activity

Bank Pekao S.A. Group offers a wide range of capital market products and services through retail brokerage entities: Dom Maklerski Pekao (Dom Maklerski), a subsidiary Centralny Dom Maklerski Pekao S.A. (CDM) and since December 11, 2017 a subsidiary Dom Inwestycyjny Xelion Sp. z o.o. (DI Xelion).

As at the end of September 2018, the retail brokerage entities of the Group maintained 273.1 thousand investment accounts. The Group's brokerage entities were serving 171.5 thousand accounts with an active access to services through remote channels, in particular through the Internet and mobile applications. As at the end of September 2018, direct service of individual customers was conducted through nationwide network of 452 points of brokerage services.

As of September 30, 2018, the total value of assets deposited on investment accounts run by the Group's retail brokerage entities amounted to PLN 21.7 billion.

In the third quarter of 2018, activities of the Group's brokerage entities focused on clients service on the secondary market, acquisition of new customers through public offers as well as development of tools and scope of services rendered through remote channels.

The Group's brokerage entities, depends on individual business decisions, served:

– sales offers of three Structured Certificates of Deposit under Third Program of Issuance of Structured Certificates of Deposit issued by Bank Pekao S.A., registering records for the total amount of PLN 127 million (Dom Maklerski),
– three sales offers of Structured or Investments Certificates for the total amount of PLN 11.8 million (CDM),
– one public bond offers, registering records for the total amount of nearly PLN 10.6 million (Dom Maklerski)

Additionally, Dom Maklerski acted as the Offering entity for the issue of Investment Certificates of PZU FIZ Akord for the U series.

Within the framework of strategic "Siła Polskiego Żubra" the Group is planning to the integration of the activities within all the Group's brokerage entities. The aim of these activities is to increase the quality and comprehensiveness of the products and services offered and to improve the effectiveness of the entities' operations. The implementation of the planned activities is conditioned by obtaining the required corporate and regulatory approvals. The entire process is planned to be completed by the end of the first half of 2019.

Business clients - micro enterprises

In the third quarter of 2018, the Bank dynamically increased share in the segment of micro enterprises thanks to the introduction of an attractive new account offer and the optimization of service processes. In the first half of 2018 the Bank for micro enterprises implemented one account Konto Przekorzystne Biznes instead of seven accounts. In the third quarter of 2018, the acquisition of micro customers increased by 50% compared to the first quarter of 2018. In the third quarter of 2018 business customers' deposits increased by PLN 0.4 billion. In comparison to December 2017, the increase amounted to PLN 0.6 billion (9.3%).

In September 2018, the Bank provided a special offer for micro enterprises, which during the last year did not have POS terminal. Within the framework enterprises can be provided with three terminals free of charge in the period of 18 months as well as free additional services such as terminal installation, staff training and service. In addition, a new customer who will open a Konto Przekorzystne Biznes account with the POS terminal will provide a voucher worth 100 PLN.

Sales of POS terminals in the third quarter of 2018 were more than three times higher than in the first quarter of 2018 and 6% higher than sales in the second quarter of 2018.

Private Banking

In the third quarter of 2018 in Private Banking activities aimed at new clients acquisition and asset management optimization by existing customers were continued. As a result of these activities, the value of assets increased in the quarter of 2018 by over PLN 250 million and total value of assets covered by Investment Advisory services amounted to PLN 3.2 billion. The Bank consistently expands its product offer In the third quarter of 2018, the customer were offered a subscriptions for six certificates based on four different underlying assets were carried out - Autocall certificates without a capital guarantee based on the following companies: AXA (certificates in PLN and USD), ArcelorMittal S.A. (PLN), Adidas AG (PLN) and certificates with a 100% capital guarantee based on the STOXX HealthCare index (in PLN and USD).

In addition the customers were offered a specialized investment program Sejf + with Golden Capital Protection offered by TFI PZU S.A. and distributed by CDM. This program allows investing in the PZU Sejf+ Subfund, which is capital-protected in case of maintaining the investment for 12, 25 or 38 months from the acquisition of units.

In September 2018, the Bank extended offer by a Multi-Allocation Investment Program - life insurance with insurance capital funds. The new product was prepared jointly with PZU Życie S.A. The investment offer includes 83 funds in PLN, EUR and USD selected from the domestic investment fund companies and foreign investment companies and 3 model strategies, available in PLN, managed by TFI PZU S.A.

Sales targets are supported by initiatives with participation of affluent customers both existing and potential clients’ as well as Private Banking representatives, during which the acquisition and relational activities are conducted. Private Banking customers had the opportunity to participate in events sponsored by the Bank such as the Pekao Szczecin Open Tennis Tournament and the 12th Film and Art Festival “Dwa Brzegi”. In addition, representatives of Private Banking participated in the 23rd Silesian BCC Gala - a cyclical meeting of opinion makers, outstanding personalities of world culture, art and science, managers contributing to the development of the Polish economy. In September 2018, Bank has once again participated in the Economic Forum in Krynica, recognized as the largest and most important annual meeting of political, economic and social life leaders in Central Europe, during which there were also a number of meetings with Private Banking Customers of Bank Pekao S.A. Also, initiatives and events of a relational and educational nature were organized for clients. The aim is to broaden the knowledge in the field of alternative investments and non-financial services - customers had the opportunity to attend a meeting at the LAPADA Art & Antiques Fair in London.

Electronic banking for Individuals

The Bank's individual clients are provided with the Pekao24 Internet system that enables remotely to realize almost all operations available in the Bank's outlet. The Internet service and mobile application also offer access to brokerage accounts held by Dom Maklerski.

The Bank's customer may use the Pekao24 system also through mobile service available on phones. The system in addition to user-friendly navigation and intuitive interface, offers functions well known from mobile application on tablets and the Internet service – expenses reporting by category, possibility to use loan offer "na klik" ("by click"), foreign currency payments and FX conversion with a preferential rates. User can view currency rates and use a convenient calculator in order to determine quickly currency conversion value. A new service provides also the possibility to reschedule the debt of Elastyczna credit card.

The Bank released the most modern in the country mobile banking application PeoPay which is both an application for banking operations and payments. The PeoPay application offers innovative solution in the market such as biometric technology for payments authorization: fingerprint and Face ID, payments for online shopping in mobile phone without logging into Internet banking, scanning banking account number directly from invoice instead of rewrite it to the application. In addition, the application gives the opportunity to pay by mobile phone also abroad (or a foreign online store) directly from the account held in the foreign currency without any additional fees and commissions for currency conversion. New PeoPay application, enables execution of transactions in PLN as well as in selected foreign currencies without FX conversion thanks to connection with corresponding currency accounts. The PeoPay application is available for devices with Android and iOS operational systems. Thanks to the PeoPay application it is possible to make payments in over 647 thousand of terminals in Poland (NBP data as at the end of the first quarter of 2018) i.e. ca. 98% of total number of POS as well as at all terminals accepting contactless payment abroad, with Masterpass logo.

Individual clients may also use innovative mobile application dedicated for tablets – "Pekao24 na tablety". The application, apart from main transactional functions known from the Pekao24 Internet system was equipped with a tool of financial analysis that helps clients to overview revenue and expenditure on their account. A new, simplified form of transfer and advanced search transactions history facilitate day-to-day usage of bank account. The "Pekao24 na tablety" application is available on devices with Android and iOS operating systems.

The Bank regularly expands the scope of functions available for execution through remote access channels. In third quarter of 2018, the Bank allowed customers of the Internet banking system to submit application within the framework of the government "Dobry start" – program PLN 300 for a school layette as well as application in Family 500 plus Government Program for new period. In addition, customers with individual and company account at the Bank, thanks to the connection of accounts in online banking, have access to these accounts at the same login.

The number of individual clients actively using mobile banking increased by 35% year on year.

(in thousand)

	30.09.2018	30.09.2017
Number of individual clients actively using electronic banking Pekao24 as at the end of period (*)	1,998.0	1,803.5
Number of individual clients with an access to mobile banking as at the end of period (**)	1,722.0	1,385.3
Number of individual clients actively using mobile banking as at the end of period (***)	1,179.3	876.6

(*) Unique user actively using electronic banking is a user who logged in to the system at least once during the last quarter.

(**) Unique user using at least one of the following mobile solutions: the mobile service m.pekao24.pl, the Pekao24 mobile banking application or the PeoPay application.

(***) Unique users of the Bank's mobile applications and the mobile service light m.pekao24.pl who logged in to the mobile baking in the fourth quarter (when using different mobile channels, the customer counts only once).

Electronic banking for SME customers

SME customers of the Bank use the PekaoBiznes24 system (with extensive Internet banking and fully transactional mobile application) and the Pekao24 dla firm system (the Pekao24 system for entrepreneurs) with the PeoPay application. Both systems are an integral part of Konto Przekorzystne Biznes and Pakiety Mój Biznes (My Business Packages).

Within the framework of Pekao24 electronic banking system for businesses, business customers have access to the most modern in the country mobile application PeoPay, which is both an application for banking operations and payments. The PeoPay application offers innovative solution in the market such as biometric technology for payments authorization, payments for online shopping in mobile phone without logging into Internet banking, scanning banking account number directly from invoice instead of rewrite it to the application. In addition, the application gives the opportunity to pay by mobile phone also abroad (or a foreign online store) directly from the account held in the foreign currency without any additional fees and commissions for currency conversion.

From July 2018, a mechanism of a shared payment has been made available in electronic banking systems, which enables the execution of transfers using funds on the VAT account. From September, customers with a private and company account in the Bank or having several companies have the opportunity to view these accounts in online banking during a single login.

As at the end of September 2018, 189 thousand business users had an access to the electronic banking, and 133 thousand are active users.

As at the end of September 2018, 44 thousand business users had an access to the mobile banking application for SME clients, and 27 thousand were active users. The number of business users with an access to the mobile banking application increased by 20 thousand compared to the end of September 2017.

Small and micro enterprises (SME)

Since the beginning of 2018, the Bank has been consistently implementing the growth strategy in the Small and Medium Enterprises segment. In order to achieve this goal the SME Banking Division has been created with dedicated Business Centers where SME client receives the support of qualified Advisors supported by Product Specialists (FX, leasing, factoring, EU Funds). Thanks to this we offer our clients modern products, solutions and specialist knowledge which supports their development at every stage of their business.

In the third quarter, Bank has implemented the SME Universal Agreement, which is the basis of a comprehensive offer in the area of transactional banking and allows to build a multi-dimensional relationship with clients. The SME Universal Agreement was developed taking into account modern trends in the corporate banking where client receives a wide range of products and services.

In the third quarter, the Bank extended the loan offer by a Mortgage Loan taking into account the needs of SME clients. The new loan allows to finance both trading and investments needs. In addition, it enables to refinance and consolidate loans taken in other banks. The important thing to improve the effectiveness of work is introducing of simplified credit documentation, which allows to offer an unified standard of service for all clients.

Other services (Cash Management, Leasing, Factoring, Foreign Trade Products) are offered depending on the clients needs. The enterprises engaged in export receives services supporting foreign trade (guarantee, letter of credit). The Bank has provided the Pekao Collect service. This service is dedicated for enterprises which cooperate with a wide group of recipients and contractors and helps them to identify mass payments.

In September, Bank Pekao S.A introduced a unique solution for companies - loans with the EFI COSME guarantee. This is the result of an agreement between the Bank and the European Investment Fund signed in July 2018 regarding a portfolio guarantee line for loans with a record value of PLN 1.2 billion. EFI COSME guarantees secure 50% of the capital and interests of investment or revolving loans and they are free of charge. This offer is dedicated to companies operating for up to 3 years and make the access to finance easier. For companies operating longer, the Bank is able to lower a required own contribution. In addition, Bank Pekao S.A. is the only bank which signed this type of contract directly with the European Investment Fund.

The second unique product has been introduced in the Bank is the ESIF Silesia. The program is dedicated to companies operating in the Silesia region and offers preferential investment and revolving loans. Half of the loan capital comes from EU funds and is interest and commissions free. Bank Pekao S.A. is the only bank which signed the contract with the EIF under this program.

In September, the SME Division launched a free of charge direct consultancy for companies wishing to use the EU Grant and Technological Credit under the 2014-2020 Funds, within the EU Funds Office.

Corporate customers

Market position and main directions of the activities

The Bank maintains its position of a leading corporate bank and the leader in innovative product solutions for enterprises and institutions. A wide range of products, innovative solutions and an individual approach ensure comprehensive financial services to enterprises, institutions and public sector units.

The Bank's services are used by every second large company in Poland. The Corporate Banking and MIB Division serviced ca. 14 thousand of entities, including nearly 3 thousand foreign customers and 3 thousand local government units and municipal companies.

The Bank maintains its position of a leading corporate bank and the leader in innovative product solutions for enterprises and institutions. A wide range of products, innovative solutions and an individual approach ensure comprehensive financial services to enterprises, institutions and public sector units.

The Bank is available to clients at every stage of their business activity. The Bank supports the financial management processes of the production and sales network, automation of service processes, finances the development of products and services and provides advisory and funds for investments and international expansion. "Tailor-made" solutions of Bank Pekao S.A. for corporate banking are recognized both in Poland and internationally. Specialized knowledge and experience in the arrangement and financing of investments, trading in Treasury securities, custodian business and a depository bank, trade finance or real estate finance are the areas of corporate banking appreciated by clients and a group of independent, national and international experts.

In September 2018 the Bank Pekao S.A. opened first foreign representative office in London. The London branch is to support business relations in the areas of corporate and private banking, including Polish companies planning to expand abroad and interested in Polish private equity funds.

Transactional services

The Bank strengthens a leading market position within the scope of the comprehensive transactional products offer for corporate clients. Apart from the PekaoBiznes24 Internet platform, which offers the widest range of products and financial services, and is the most commonly chosen electronic banking system for companies in Poland, the Bank provides also the Pekao Connect - a high-tech solution integrating financial-accounting systems of client with the Bank system, which enables automation of payment orders process and receiving feedback information on banking operations.

Key achievements in the area of the Bank's transactional banking in the third quarter of 2018 include:

- an increase in the number and volume of domestic transfers by 15% and 4% year on year, respectively,
- an increase in the number and volume of cash deposits in closed form by 9% and 14% year on year respectively,
- an increase in the number and volume of transaction within the Pekao Collect service (mass payments identification) by nearly 3% and 15% year on year respectively,
- an increase in the number of foreign incoming and outgoing payments by 17% and 12% year on year respectively, and volume by ca 20% and 15% year on year respectively.

Trade finance

In the third quarter of 2018, in the area of trade finance the Bank recorded increase in export LCs by almost 9% and purchased receivables in eFinancing model by over 14% year on year.

In September 2018, the Bank provided possibility issue e-bank guarantees in the pdf form with a qualified electronic signature. E-guarantees are equivalent to guarantees issued in the form of a traditional paper document. The new form of the document is a significant facilitation for entities taking part in tenders for public procurement.

Investment banking, structured finance and commercial real estates

The Bank consistently supports the development of enterprises and infrastructure through financing, organizing and securing the transactions. It offers clients a wide range of services in the field of project financing, structured financing and commercial real estate project financing.

The Bank finances projects aimed at redevelopment of brownfield sites in order to improve common space. The Bank provides financing allowing the activity and development of enterprises operating on the Polish market, and at the same time, participates in transactions executed abroad by companies from Poland.

The Bank has expertise and experience to service every, even the most complex and innovative type of transactions.

In the third quarter of 2018, the Bank participated, among others, in the following investment projects of institutional clients:

- granting of investment loan for expansion of production capacity in the chemical and food industry, syndicated financing in the amount of EUR 73 million,
- financing of the development of market leaders in inspection, and certification in Poland, the total amount of loan PLN 235 million,
- financing of one of the leaders in the telecommunications services industry, the total amount of loan PLN 200 million,
- financing of development of the online flight ticket sector leader, the total amount of loan over PLN 60 million,
- financing of activities of one of Polish leader on the design and manufacture of machinery and equipment for the energy and fuel sector, the total amount of loan PLN 50 million,
- financing of activity of one of the leaders in poultry farming, the total amount of loan PLN 50 million.

In the first nine months 2018, the value of new loan agreements on commercial real estate financing amounted to PLN 2.7 billion, and included, among others, the following transactions:

- granting of loans for innovative form of financing housing transaction, in the total amount of loan PLN 258 million,
- financing of an office building complex in Łódź, in the amount PLN 230 million,
- financing of the logistics park near Szczecin, in the amount nearly PLN 130 million.

Issuance of debt instruments

In the area of arrangement and management of commercial debt securities, Bank Pekao S.A. has 19% market share (the 2nd place), as of September 30, 2018, including 20% market share in organization of corporate bonds issues, 23% market share of the bank debt security and 28% market share in organization of municipal bonds issues.

In the three quarters of 2018, the Bank ranks first position in the medium-term corporate bonds issue segment (37% market share) and in the debt securities segment issued by banks (32% market share).

In the third quarter of 2018, the Bank issued debt securities (corporates, banks and local governments) for the total amount of ca. PLN 4.6 billion, including in particular the following transactions:

- the issue of 3 – years bonds for a financial institution (the largest transaction on the Polish market carried out by one dealer), for the total amount of PLN 2.5 billion,
- the issue of 7 - year cover bonds for mortgage bank for the total amount of PLN 350 million,
- the issue of 1 - year bonds for mortgage bank for the amount of PLN 300 million,
- the issue of 3 series of 2-year bonds for a leasing company for the total amount of over PLN 75 million,
- the issue of 5-year unsecured bonds for a company from developers sector for the amount of PLN 60 million.

Cooperation with international and domestic financial institutions
Bank Pekao S.A. maintains correspondent relations with 1.6 thousand Polish and foreign banks (according to the number of swift keys).

As of September 30, 2018, the Bank maintains 74 nostro accounts with 47 banks in 26 countries; it runs 223 loro accounts for 204 foreign clients (banks and other financial institutions) from 48 countries and 45 current accounts for 41 foreign financial institutions.

The Bank also intermediates in the execution of transactions on behalf of clients of other domestic banks, running 35 loro accounts for 13 Polish banks and maintaining 6 nostro accounts with one Polish bank.

The Bank renders also services for Polish banks and branches of foreign banks in Poland in terms of purchase and sale of foreign and domestic currency.

Comprehensive services for the public finance sector
Bank Pekao S.A. consistently developed cooperation with municipal companies and public sector entities and operated in the area of servicing and financing of the public sector, in particular in financing of the Polish infrastructural projects.

In the third quarter of 2018, Bank in cooperation with Pekao TFI implemented the first on Polish market government investment funds Pekao Samorząd Plus FIZ. The fund's assets include bonds of local government units and municipal companies which implemented investment projects financed by the Bank. The fund is very important for the development of the municipal bond market in Poland.

Implementing the new strategy of development for 2018-2020 Strength of the Polish Bison which assumes an increase in cooperation within the Bank Pekao SA Capital Group, in the third quarter of 2018 the Bank introduced to its offer a public issue of mortgage bonds issued by Pekao Bank Hipoteczny SA - a subsidiary of Bank Pekao SA. This is the first issue of mortgage bonds in the public market in Poland for over 5 years. Local government loans in the amount of PLN 350 million are a security of the issue.

The most important transactions concluded with public finance sector clients in the third quarter of 2018 include:

In the third quarter of 2018, the Bank participated, among others, in the following transactions:

– loan for financing of current activities for one of largest of municipal companies in the area of waste management, the total amount of loan PLN 60 million,

– purchase by company owned by State Treasury, bonds issued by Pekao Leasing for amount PLN 100 million. The customer used a wide range of the Bank's offer and invested in Pekao Leasing bonds with the guarantee of Bank Pekao S.A. as an alternative to deposit products.

5.7 Factors which will affect the results of the Group

The activity of Bank Pekao S.A. and the Group's companies is in majority conducted on the Polish territory, hence the Group's performance will be mainly affected by economic situation in the country and international events that have influence on domestic economy. In the context of the latter one cannot rule out a new wave of tensions related to the situation in some countries (e.g. Italy) or in the face of significant events (Brexit), which may affect into higher market volatility. With regard to the domestic market, tensions in the labor market (visible in the form of increasing wage pressure and shortages of employees) may negatively affect financial situation of enterprises and their propensity to investments, translating into weaker results of the banking sector.

In 2018, the activity and financial results of the banking sector remains under influence of tax and regulatory environment, including among others tax on certain financial institutions, high requirements in terms of banks' equity (including the newest accounting standards IFRS 9), and liquidity, contributions to the BFG and costs of adjustment to a number of regulatory solutions (MIFID II, RODO, PSD II).

It is worth noting that a portion of commission and dividend income that is not directly related to banking activity is influenced by changes taking place in other financial market segments (investment funds, brokerage) resulting from the market situation, competitive dynamics or regulatory changes.

In the following months of 2018 one can expect a high growth rate of the zloty housing loans as well as consumer loans. It is a derivative of a favorable economic situation of households and their high level of optimism. As the scale of recovery in investments - especially in the segment of small and medium-sized enterprises - remains moderate, it translates into relatively low dynamics of corporate loans growth.

Good situation on labour market (increasing employment and wages) and growing risks associated with the alternative forms of saving (due to global liquidity changes stemming from the monetary policy movements in the US and euro zone) should be supportive for the relatively high growth pace in household deposits. Stronger pace of growth should be expected in case of corporate deposits, driven most of all by low base from 2017.

Monetary policy should remain supportive for credit expansion, constraining attractiveness of bank deposits. According to recent comments from members of the MPC, no interest rate changes should be expected in 2018.

In 2018 the banks' results are negatively affected by the level of interest on reserve requirement, which is set by the Monetary Policy Council. Since the beginning of the year, this interest rate has been lowered to 0.50% (from 1.35%).

Right now the Polish Parliament is working on two draft bills related to the portfolio of mortgage loans denominated in foreign currencies. First project provides on returns for some receivables resulting from the loans agreements. It assumes, that in case of FX loans banks will have to return to the clients the difference between acceptable spread (the difference between the rate of buying and selling of the currency set by the law) and the one actually charged. Estimates point out, that if the law is passed the cost for the banking sector may amount to couple of billions of the złoty. Second project proposes special fund to help troubled borrowers. The contribution to the funds would cost banks up to PLN 3.2 billion per year. The entry into force of any of these solutions may have a strong negative impact on the financial performance of banks with significant portfolio of foreign currency denominated mortgages. However, taking into account the relatively minor share of these loans in the total assets of the Bank (almost entirely acquired as a result of the merger of the spun-off part of Bank BPH SA in 2007), Bank Pekao S.A. assesses that potentially taken solutions should not materially affect the financial standing of the Group.

6 Statement of Financial Position and Financial Results

Consolidated income statement containing cumulated items for the period from 1 January to 30 September, 2018 and 2017 respectively is presented in the Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period of 9 months ended on 30 September 2018.

The Report on activities of Bank Pekao S.A. Group for the third quarter of 2018 includes statement of financial position in a short form and income statement in a presentation form as well as the key, selected items from these statements are discussed.

6.1 Structure of the consolidated statement of financial position – short form

The balance sheet of Bank Pekao S.A. determines the amount of total assets in balance sheet and the structure of the assets and liabilities of the Group. As at the end of September 2018, the total assets of Bank Pekao S.A. constitutes 96,8% of the total assets of the whole Group.

The table below presents the Group's statement of financial position – short form.

ASSETS	30.09.2018		30.09.2017		CHANGE
	PLN MILLION	STRUCTURE	PLN MILLION	STRUCTURE	
Cash and due from Central Bank	5,720.3	3.1%	6,106.1	3.6%	(6.3%)
Loans and advances to banks(*)	4,762.6	2.6%	2,926.7	1.7%	62.7%
Customers' financing (**)	137,428.8	75.0%	129,429.4	75.5%	6.2%
Reverse repo transactions	-	x	-	x	x
Securities(***)	28,546.6	15.6%	27,058.9	15.8%	5.5%
Investments in associates	0.0	0.0%	167.9	0.1%	(100.0%)
Property, plant and equipment and intangible assets	2,826.3	1.5%	2,039.8	1.2%	38.6%
Other assets	4,013.9	2.2%	3,734.1	2.1%	7.5%
Total assets	**183,298.5**	**100.0%**	**171,462.9**	**100.0%**	**6.9%**

(*) Including net investments in financial leases to banks.

(**) Including net investments in financial leases to customers and non-quoted securities.

(***) Including financial assets held for trading, other financial instruments at fair value through profit and loss and excluding non-quoted securities.

EQUITY AND LIABILITIES	30.09.2018		30.09.2017		CHANGE
	PLN MILLION	STRUCTURE	PLN MILLION	STRUCTURE	
Amounts due to Central Bank	5.0	0.0%	6.1	0.0%	(18.0%)
Amounts due to other banks	4,689.3	2.6%	4,371.3	2.5%	7.3%
Amounts due to customers	142,854.7	77.9%	135,222.6	78.9%	5.6%
Debt securities issued	4,742.6	2.6%	2,435.9	1.4%	94.7%
Subordinated liabilities	1,267.4	0.7%	-	x	x
Repo transactions	913.0	0.5%	970.7	0.6%	(5.9%)
Other liabilities	6,826.2	3.7%	6,187.9	3.6%	10.3%
Total equity, including	22,000.3	12.0%	22,268.4	13.0%	(1.2%)
non-controlling interests	11.5	x	15.5	0.0%	(25.8%)
Total equity and liabilities	**183,298.5**	**100.0%**	**171,462.9**	**100.0%**	**6.9%**

Customers' Financing
Customer structure of loans and advances

(in PLN million)

	30.09.2018	30.09.2017	CHANGE
Loans and advances at nominal value(*)	**143,035.4**	**134,260.9**	**6.5%**
Loans (**)	131,890.3	122,238.9	7.9%
Retail	69,311.2	62,793.3	10.4%
Corporate	62,579.1	59,445.6	5.3%
Non - quoted securities	11,145.1	12,022.0	(7.3%)
Other(***)	1,000.5	717.0	39.5%
Nominal value adjustment	x	305.0	x
Impairment allowances	**(6,607.1)**	**(5,853.5)**	**12.9%**
Customers' financing	**137,428.8**	**129,429.4**	**6.2%**
Reverse repo transactions	-	-	x
Gross total customers' financing(****)	**143,035.4**	**134,260.9**	**6.5%**

(*) Excluding reverse repo transactions.

(**) Including net investments in financial leases to customers.

(***) Including interest and receivables in transit.

(****) Gross total customers' financing includes loans and advances at nominal value and reverse repo transactions.

As at the end of September 2018, loans and advances at nominal value amounted to PLN 143,035.4 million, an increase of PLN 8,774.5 million, i.e. 6.5% in comparison to the end of September 2017 with significant growth in key strategic areas.

As at the end of September 2018, the volume of retail loans amounted to PLN 69,311.2 million, an increase of PLN 6,517.9 million, i.e. 10.4% in comparison to the end of September 2017.

As at the end of September 2018, corporate loans amounted to PLN 62,579.1 million, an increase of PLN 3,133.5 million, i.e. 5.3% in comparison to the end of September 2017.

As at the end of September 2018, corporate loans and non - quoted securities amounted to PLN 73,724.2 million, an increase of PLN 2,256.6 million, i.e. 3.2% in comparison to the end of September 2017.

Receivables and impairment losses(*)

(in PLN million)

	30.09.2018	30.09.2017	CHANGE
Gross receivables	**144,035.9**	**135,282.9**	**6.5%**
Stage 1	114,200.4	nd	**x**
Stage 2	21,423.4	nd	**x**
Stage 3	8,412.1	nd	**x**
Impairment allowances	**(6,607.1)**	**(5,853.5)**	**12.9%**
Stage 1	(399.6)	nd	x
Stage 2	(740.2)	nd	x
Stage 3	(5,467.3)	nd	x
Total net receivables	**137,428.8**	**129,429.4**	**6.2%**

(*) Including net investments in financial leases to customers, non-quoted securities, interest and receivables in transit and excluding reverse repo transactions.

As at the end of September 2018 the ratio of impaired receivables (stage 3) to the gross receivables amounted 5.8%.

Loans and advances to customers by currency(*)

	30.09.2018		30.09.2017		CHANGE
	PLN MILLION	STRUCTURE	PLN MILLION	STRUCTURE	
Denominated in PLN	120,332.6	83.5%	111,896.0	82.7%	7.5%
Denominated in foreign currencies(**)	23,703.3	16.5%	23,386.9	17.3%	1.4%
Total	**144,035.9**	**100.0%**	**135,282.9**	**100.0%**	**6.5%**
Impairment allowances	(6,607.1)	,x	(5,853.5)	,x	12.9%
Total net	**137,428.8**	**x**	**129,429.4**	**x**	**6.2%**

(*) Including net investments in financial leases to customers, non-quoted securities, interest and receivables in transit and excluding reverse repo transactions.

(**) Including indexed loans.

The currency structure of loans and advances to customers is dominated by amounts expressed in the Polish złoty; as at the end of September 2018, their share was 83.5%. The largest portion of foreign currency loans and advances to customers were represented by those denominated in EUR (73.3%), CHF (14.8%) and USD (10.4%).

Loans and advances to customers by contractual maturities(*)

	30.09.2018		30.09.2017		CHANGE
	PLN MILLION	STRUCTURE	PLN MILLION	STRUCTURE	
Current and up to 1 month	15,499.5	10.8%	16,701.6	12.3%	(7.2%)
1 to 3 months	4,612.6	3.2%	5,617.7	4.2%	(17.9%)
3 months to 1 year	13,584.1	9.4%	11,735.8	8.7%	15.7%
1 to 5 years	45,757.4	31.8%	42,071.4	31.1%	8.8%
Over 5 years	63,581.8	44.1%	58,439.4	43.2%	8.8%
Other	1,000.5	0.7%	717.0	0.5%	39.5%
Total	**144,035.9**	**100.0%**	**135,282.9**	**100.0%**	**6.5%**
Impairment allowances	(6,607.1)	x	(5,853.5)	x	12.9%
Total net	**137,428.8**	**x**	**129,429.4**	**x**	**6.2%**

(*) Including net investments in financial leases to customers, non-quoted securities, interest and receivables in transit and excluding reverse repo transactions.

As at the end of September 2018, loans and advances with maturity over 5 years represents 44.1% of total loans and advances (mainly attributed to mortgage loans and receivables for which the maturity date already passed).

External sources of financing

(in PLN million)

	30.09.2018	30.09.2017	CHANGE
Amounts due to Central Bank	5.0	6.1	(18.0%)
Amounts due to other banks	4,689.3	4,371.3	7.3%
Amounts due to customers	142,854.7	135,222.6	5.6%
Debt securities issued	4,742.6	2,435.9	94.7%
Subordinated liabilities	1,267.4	-	x
Repo transactions	913.0	970.7	(5.9%)
Total external sources of financing	**154,472.0**	**143,006.6**	**8.0%**

Amounts due to customers amounted to PLN 142,854.7 million, an increase by 5.6% to significant extent contributed to dynamic increase in loans.

The deposit base is widely diversified and is sourced from retail and corporate customers. In addition, the Group uses also funds borrowed on the interbank market. The Group is not dependent on any single customer nor group of customers.

On October 30, 2017, the Bank issued 10 year subordinated bonds with a total nominal value of PLN 1,250.0 million with the maturity date on October 29, 2027. The funds from the issue were designated – after receiving the approval of the KNF on December 21, 2017 – to increase the Bank's supplementary capital, pursuant to art. 127 para. 2 point 2 of the Banking Law and art. 63 of Regulation No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms. The bonds were introduced to trading on the ASO Catalyst market and BondSpot.

Total customer savings

(in PLN million)

	30.09.2018	30.09.2017	CHANGE
Corporate deposits	**62,043.0**	**60,940.2**	**1.8%**
Non-financial entities	45,840.6	42,586.6	7.6%
Non-banking financial entities	5,489.2	8,646.1	(36.5%)
Budget entities	10,713.2	9,707.5	10.4%
Retail deposits	**80,325.8**	**73,823.1**	**8.8%**
Other(*)	485.9	459.3	5.8%
Amounts due to customers(**)	**142,854.7**	**135,222.6**	**5.6%**
Debt securities issued, of which	**6,010.0**	**2,435.9**	**>100%**
Structured Certificates of Deposit (SCD)	468.1	85.4	>100%
Certificates of Deposit	677.0	1,025.0	(34.0%)
Subordinated bonds	1,250.0	-	x
Pekao Bank Hipoteczny S.A. covered bonds	1,519.6	1,315.9	15.5%
Pekao Bank Hipoteczny S.A. bonds	300.0	-	x
Pekao Leasing Sp. z o.o. bonds	1,766.6	-	x
Interest	28.7	9.6	>100%
Amounts due to customers and debt securities issued, total(**)	**148,864.7**	**137,658.5**	**8.1%**
Repo transactions	913.0	970.7	(5.9%)
Investment funds of Pekao TFI S.A. (ex. Pioneer Pekao TFI)	**19,534.3**	**17,895.3**	**9.2%**
Bond and money market funds	15,088.0	12,795.3	17.9%
Balanced funds	2,451.5	2,655.7	(7.7%)
Equity funds	1,994.9	2,444.3	(18.4%)
including distributed through the Group's network	19,252.0	17,558.6	9.6%

(*) Other item includes interest and funds in transit.
(**) Excluding repo transactions.

As at the end of September 2018, amounts due to the Group's customers and debt securities issued amounted to PLN 148,864.7 million, an increase of PLN 11,206.2 million, i.e. 8.1% in comparison to the end of September 2017.

Retail deposits amounted to PLN 80,325.8 million as at the end of September 2018, an increase of PLN 6,502.7 million, i.e. 8.8% in comparison to the end of September 2017.

The total volume of retail customers deposits, Structured Certificates of Deposit and other amounted to PLN 81,238.2 million as at the end of September 2018, an increase of PLN 6,910.9 million, i.e. 9.3% in comparison to the end of September 2017.

Corporate deposits amounted to PLN 62,043.0 million as at the end of September 2018, an increase of PLN 1,102.8 million, i.e. 1.8% as compared to the end of September 2017.

The total volume of corporate deposits, Certificates of Deposit, subordinated bonds, Pekao Bank Hipoteczny S.A. covered bonds and bonds, Pekao Leasing Sp. z o.o. bonds, interest and other amounted to PLN 67,626.3 million as at the end of September 2018, an increase of PLN 4,295.3 million, i.e. 6.8% as compared to the end of September 2017.

Repo transactions amounted to PLN 913.0 million as at the end of September 2018, an increase by PLN 57.7 million, i.e. 5.9% as compared to the end of September 2017.

The value of net assets of investment funds managed by Pekao TFI S.A. (ex. Pioneer Pekao TFI S.A.) amounted to PLN 19,534.3 million as at the end of September 2018, an increase of PLN 1,639.0 million, i.e. 9.2% in comparison to the end of September 2017.

Amounts due to customers by currency(*)

	30.09.2018		30.09.2017		CHANGE
	PLN MILLION	STRUCTURE	PLN MILLION	STRUCTURE	
Denominated in PLN	115,179.3	80.6%	110,557.6	81.8%	4.2%
Denominated in foreign currencies	27,675.4	19.4%	24,665.0	18.2%	12.2%
Total	**142,854.7**	**100.0%**	**135,222.6**	**100.0%**	**5.6%**

(*) Including interest and amounts due in transit and excluding repo transactions.

The bulk of the amounts due to customers are denominated in the Polish currency and its share as at the end of September 2018 amounted to 80.6%. The majority of amounts due to customers denominated in foreign currencies were in EUR (64.0%) and USD (30.3%).

Amounts due to customers by contractual maturities(*)

	30.09.2018		30.09.2017		CHANGE
	PLN MILLION	STRUCTURE	PLN MILLION	STRUCTURE	
Current accounts and overnight deposits	80,132.0	56.3%	81,117.5	60.2%	(1.2%)
Term deposits	62,236.8	43.7%	53,645.7	39.8%	16.0%
Total deposits	**142,368.8**	**100.0%**	**134,763.2**	**100.0%**	**5.6%**
Interest accrued	181.0	x	168.3	x	7.5%
Funds in transit	304.9	x	291.1	x	4.7%
Total	**142,854.7**	**x**	**135,222.6**	**x**	**5.6%**

(*) Excluding repo transactions.

6.2 The consolidated income statement – presentation form

Net profit of Bank Pekao S.A. Group attributable to equity holders for the three quarters of 2018 amounted to PLN 1,537.9 million and was higher by PLN 116.9 million, i.e. 8.2% than net profit reported for the three quarters of 2017. For comparability purpose of achieved results income statement data for the three quarters of 2017 was presented in this chapter as pro-forma, i.e. includes full consolidation of results of Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.) and Dom Inwestycyjny Xelion Sp. z o.o. acquired on December 11, 2017.

Net profit of Bank Pekao S.A. Group attributable to equity holders for the three quarters of 2018 was higher by PLN 83.9 million, i.e. 5.8% than pro-forma net profit in the three quarters of 2017.

Thanks to the effective commercial activity of the Group in the three quarters of 2018, a significant growth in loan volumes in the area of retail loans (an increase of 10.4% year on year) as well as in the area of corporate loans (an increase of 5.3% year on year) was reported. Such increase in lending was financed by higher retail deposits growing by 8.8% year on year and corporate deposits growing by 1.8% year on year.

Total capital ratio (TCR) amounted to 17.0% as at the end of September 2018 and was higher (0.5 p.p.) compared to the end of September 2017.

The solid liquidity structure of Bank Pekao S.A. Group is reflected by net loans to deposits ratio at 92.3% as at the end of September 2018. This, together with high level of capital, enables for further sound and stable development of the Group's activities.

The consolidated income statement – presentation form

(in PLN million)

	3 QUARTERS OF 2018	PRO-FORMA 3 QUARTERS OF 2017	3 QUARTERS OF 2017	CHANGE VS. PRO-FORMA
Net interest income	3,699.2	3,406.2	3,403.3	8.6%
Dividend income and income from equity investments	20.0	19.6	51.3	2.0%
Total net interest income, dividend income and other income from equity investments	**3,719.2**	**3,425.9**	**3,454.6**	**8.6%**
Net fee and commission income	1,824.3	1,859.7	1,735.9	(1.9%)
Trading result	130.4	49.7	49.7	>100%
Net other operating income and expenses	39.6	88.2	87.8	(55.1%)
Net non-interest income	**1,994.3**	**1,997.7**	**1,873.4**	**(0.2%)**
Operating income	**5,713.5**	**5,423.6**	**5,328.0**	**5.3%**
Operating costs	**(2,596.7)**	**(2,455.2)**	**(2,408.8)**	**5.8%**
Gross operating profit	**3,116.8**	**2,968.4**	**2,919.2**	**5.0%**
Net impairment losses on financial assets and off-balance sheet commitments	(406.1)	(368.5)	(368.5)	10.2%
Net operating profit	**2,710.7**	**2,600.0**	**2,550.7**	**4.3%**
Net result on other provisions	(14.4)	(22.3)	(22.0)	(35.3%)
Guarantee funds charges	(234.8)	(246.4)	(246.4)	(4.7%)
Tax on certain financial institutions	(417.8)	(383.4)	(383.4)	9.0%
Net result on investment activities	26.9	0.3	0.3	>100%
Profit before tax	**2,070.6**	**1,948.1**	**1,899.2**	**6.3%**
Income tax expense	(532.0)	(493.5)	(477.6)	7.8%
Net profit	**1,538.6**	**1,454.6**	**1,421.6**	**5.8%**
Attributable to equity holders of the Bank	**1,537.9**	**1,454.0**	**1,421.0**	**5.8%**
Attributable to non-controlling interest	0.7	0.6	0.6	16.7%

Operating income

In the three quarters of 2018, the Group's operating income amounted to PLN 5,713.5 million and was higher by 5.3% year on year than pro-forma operating income in the three quarters of 2017.

Total net interest income, dividend income and income from equity investments

(in PLN million)

	3 QUARTERS OF 2018	PRO-FORMA 3 QUARTERS OF 2017	3 QUARTERS OF 2017	CHANGE VS. PRO-FORMA
Interest income	4,538.5	4,184.5	4,181.6	8.5%
Interest expense	(839.3)	(778.3)	(778.3)	7.8%
Net interest income	**3,699.2**	**3,406.2**	**3,403.3**	**8.6%**
Dividend income	20.0	19.6	19.6	2.0%
Income from equity investments	-	-	31.7	x
Total net interest income, dividend income and income from equity investments	**3,719.2**	**3,425.9**	**3,454.6**	**8.6%**

Total net interest income, dividend income and income from equity investments in the three quarters of 2018, amounted to PLN 3,719.2 million and was higher by PLN 293.3 million, i.e. 8.6% compared to pro-forma total net interest income, dividend income and income from equity investments achieved in the three quarters of 2017, mainly driven by higher volumes of loans and deposits as well as higher margin.

Net non-interest income

(in PLN million)

	3 QUARTERS OF 2018	PRO-FORMA 3 QUARTERS OF 2017	3 QUARTERS OF 2017	CHANGE VS. PRO-FORMA
Fee and commission income	2,097.2	2,111.8	1,960.0	(0.7%)
Fee and commission expense	(272.9)	(252.0)	(224.1)	8.3%
Net fee and commission income	**1,824.3**	**1,859.7**	**1,735.9**	**(1.9%)**
Trading result	130.4	49.7	49.7	>100%
of which gains on disposal of AFS assets	65.1	25.8	25.8	>100%
Net other operating income and expense	39.6	88.2	87.8	(55.1%)
Net non-interest income	**1,994.3**	**1,997.7**	**1,873.4**	**(0.2%)**

Net non-interest income in the three quarters of 2018, amounted to PLN 1,994.3 million and was lower by PLN 3.4 million, i.e. 0.2% compared to pro-forma net non-interest income in three quarters of 2017, with net fee and commission income (including fees on margins on foreign exchange transactions with clients) lower by 1.9% compared to the three quarters of 2017 mainly due to lower net fee and commission income on loans and cards.

The Group's net fee and commission income in the three quarters of 2018, amounted to PLN 1,824.3 million and was lower by PLN 35.4 million, i.e. 1.9% in comparison with pro-forma net fee and commission income for the three quarters of 2017, mainly due to lower fees on loans (partially due to presentation shift) and higher commission expenses on cards, partially compensated by higher income on margins on foreign exchange transactions with clients and mutual funds.

The table below presents the Group's net fee and commission income divided according to the main areas of the activity.

(in PLN million)

	3 QUARTERS OF 2018	PRO-FORMA 3 QUARTERS OF 2017	3 QUARTERS OF 2017	CHANGE VS. PRO-FORMA
Net fee and commission income	**1,824.3**	**1,859.7**	**1,735.9**	**(1.9%)**
on loans	335.8	357.4	357.4	(6.0%)
on cards	244.7	270.6	270.6	(9.6%)
on margins on foreign exchange transactions with clients	339.3	330.5	330.5	2.7%
on mutual funds	336.6	322.6	199.0	4.3%
other	567.9	578.7	578.4	(1.9%)

Operating costs

The operating costs amounted to PLN 2,596.7 million in the three quarters of 2018. They were higher by PLN 141.5 million, i.e. 5.8% as compared with pro-forma operating costs in the three quarters of 2017, mainly due to higher personnel costs (mainly due to costs in the amount ca. of PLN 50 million, related to the Program Dobrowolnych Odejść – PDO addressed to Bank's employees obtaining pension right in 2018) and other administrative expenses (including mainly marketing related expenses). Operating costs excluding PDO expenses was higher by PLN 91.9 million, i.e. 3.7% as compared with pro-forma operating costs in the three quarters of 2017.

(in PLN million)

	3 QUARTERS OF 2018	PRO-FORMA 3 QUARTERS OF 2017	3 QUARTERS OF 2017	CHANGE VS. PRO-FORMA
Personnel expenses	(1,545.7)	(1,471.0)	(1,445.5)	5.1%
Other administrative expenses	(780.6)	(728.9)	(709.7)	7.1%
Depreciation and amortization	(270.4)	(255.2)	(253.6)	5.9%
Operating costs	**(2,596.7)**	**(2,455.2)**	**(2,408.8)**	**5.8%**

In the three quarters of 2018, cost / income ratio amounted to 45.4% in comparison with pro-forma cost / income ratio of 45.3% in the three quarters of 2017.

As of September 30, 2018, the Group employed 16,906 employees (in the Bank and the companies consolidated under full consolidation method) as compared to 17,381 employees as at the end of September 2017.

As of September 30, 2018, the Bank employed 14,674 employees as compared to 15,551 employees as at the end of September 2017.

Guarantee funds charges

Guarantee funds charges in the three quarters of 2018, amounted to PLN 234.8 million, a decrease of PLN 11.6 million, i.e. 4.7% in comparison with the three quarters of 2017, due to lower annual contribution to the resolution fund of banks.

Tax on certain financial institutions

On February 1, 2016, tax on certain financial institutions under the Act on tax on certain financial institutions was introduced. In the three quarters of 2018, it amounted to PLN 417.8 million and was higher by PLN 34.4 million, i.e. 9.0% in comparison with the three quarters of 2017.

6.3 The structure of the net profit

The structure of the net profit of the Group is presented in the table below:

(in PLN million)

	3 QUARTERS OF 2018	3 QUARTERS OF 2017	CHANGE
Net profit of Bank Pekao S.A.	**1,650.8**	**1,472.5**	**12.1%**
Entities consolidated under full method			
Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.)(*)	61.5	-	x
Pekao Leasing Sp. z o.o.	30.5	25.4	20.1%
Centralny Dom Maklerski Pekao S.A.	20.8	26.5	(21.5%)
Pekao Faktoring Sp. z o.o.	9.3	8.0	16.3%
Pekao Financial Services Sp. z o.o. (**)	4.0	4.6	(13.0%)
Centrum Bankowości Bezpośredniej Sp. z o.o.	3.6	2.4	50.0%
Dom Inwestycyjny Xelion Sp. z o.o.(*)	3.6	-	x
Pekao Investment Banking S.A.	3.1	6.6	(53.0%)
Pekao Powszechne Towarzystwo Emerytalne S.A. w likwidacji(ex. Pekao Pioneer Powszechne Towarzystwo Emerytalne S.A.)(***)	2.8	1.7	64.7%
Pekao Bank Hipoteczny S.A.	2.1	3.9	(46.2%)
Pekao Fundusz Kapitałowy Sp. z o.o. w likwidacji	0.3	0.3	0.0%
Pekao Property S.A.	0.1	0.2	(50.0%)
Centrum Kart S.A.	(0.2)	0.6	x
FPB "MEDIA" Sp. z o.o.(****)	(15.2)	0.3	x
Entities valued under the equity method			
Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.)(*)	-	29.6	x
Dom Inwestycyjny Xelion Sp. z o.o.(*)	-	2.1	x
Exclusions and consolidation adjustments (*****)	**(239.2)**	**(163.7)**	**46.1%**
Net profit of the Group attributable to equity holders of the Bank	**1,537.9**	**1,421.0**	**8.2%**

(*) On December 11, 2017, the Bank and UniCredit S.p.A. (legal successor of Pioneer Global Asset Management S.p.A.) executed the final sale agreement regarding 14,746 shares in Pioneer Pekao Investment Management S.A. (PPIM) with registered office in Warsaw, constituting 51% stake in share capital and in the overall number of votes in the General Meeting of PPIM. In consequence, the Bank has become a stockholder holding 100% of PPIM shares. Currently PPIM operates under the name Pekao Investment Management S.A.(Pekao IM).Pekao IM owns a 100% stake in Pekao Towarzystwo Funduszy Inwestycyjnych S.A. with registered office in Warsaw (ex. Pioneer Pekao Towarzystwo Funduszy Inwestycyjnych S.A.).

In addition, on December 11, 2017, the Bank acquired 60,050 shares of Dom Inwestycyjny Xelion Sp. z o.o., constituting 50% of voting rights at the General Shareholder Meeting and 50% share in share capital. In consequence, the Bank is the only shareholder with 100% voting rights at the General Shareholders Meeting of Xelion and 100% in equity. Net profit of aforementioned Companies for the free quarters of 2017 was recognized under the equity method and net profit for the free quarters of 2018 under full method.

(**) On June 4, 2018, the District Court registered the increase of share capital of Pekao Financial Services Sp. z o.o. related to the transaction of the takeover by the Company, pursuant to art. 529 § 1 point 4 of the Code of Commercial Companies (division by separation) of an organized part of the enterprise separated from PZU Centrum Operacji S.A. As a result, a new shareholder of the Company, PZU SA, was disclosed in the National Court Register, which took up shares in the increased share capital in the amount of 4,534 with the total value of PLN 2,267,000. At present, the share capital of the Company amounted to PLN 6,767,000. Bank Pekao S.A. holds 66.50% of votes and capital of the Company, while PZU S.A. holds 33.50%.

(***) On October 17, 2017, after receiving regulatory consent, the Bank acquired 7,266 ordinary, registered stocks of Pekao Pioneer Powszechne Towarzystwo Emerytalne S.A. with the nominal value PLN 1,000 per stock representing 35% of voting rights at the General Stockholder Meeting of PTE and 35% share in equity. Following the transaction, the Bank is the only stockholder of PTE with 100% in equity and voting rights at the General Stockholders Meeting of PTE. On April 24, 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 May 19, 2018, PTE PZU S.A. has taken over the management of Pekao OFE and DFE Pekao funds. The transaction was classified as an intra-group transaction and the result of this transaction was recognized in the Group's equity.

On June 1, 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.

(****) The result of FPB "Media" Sp. z o.o. takes into account the effect of dismissing the Company's complaint against the Court's decision regarding the ownership of the property.

(*****) Includes, among others, transactions within the Group (including dividends from subsidiaries for the previous years), gain related to acquisition of shares of Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.) and Dom Inwestycyjny Xelion Spółka z o.o. and net profit attributable to non-controlling interest.

The results of Bank Pekao S.A.

The main items from the Bank's income statement in presentation form are as follows:

(in PLN million)

	3 QUARTERS OF 2018	3 QUARTERS OF 2017	CHANGE
Net interest income	3,606.9	3,324.1	8.5%
Dividend income	255.2	187.9	35.8%
Total net interest income and dividend income	3,862.1	3,512.0	10.0%
Net non-interest income	1,667.7	1,663.9	0.2%
Operating income	**5,529.8**	**5,175.9**	**6.8%**
Operating costs	**(2,356.7)**	**(2,237.1)**	**5.3%**
Gross operating profit	**3,173.1**	**2,938.8**	**8.0%**
Net impairment losses on financial assets and off-balance sheet commitments	(377.9)	(364.0)	3.8%
Net operating profit	**2,795.2**	**2,574.8**	**8.6%**
Net result on other provisions	(14.7)	(19.7)	(25.4%)
Guarantee funds charges	(234.4)	(243.7)	(3.8%)
Tax on certain financial institutions	(417.8)	(383.5)	8.9%
Net result on investment activities	25.0	0.3	>100%
Profit before tax	**2,153.2**	**1,928.2**	**11.7%**
Net profit	**1,650.8**	**1,472.5**	**12.1%**

Net profit of the Bank for the three quarters of 2018 amounted to PLN 1,650.8 million and was higher by PLN 178.3 million, i.e. 12.1% than net profit achieved in for the three quarters of 2017.

The main Bank's financial information are as follows:

	30.09.2018	30.09.2017	CHANGE
STATEMENT OF FINANCIAL POSITION – SELECTED ITEMS (in PLN million)			
Loans and advances at nominal value(*)	136,822.1	130,825.4	4.6%
Amounts due to customers	143,371.6	135,474.7	5.8%
Structured Certificates of Deposit	468.1	85.4	>100%
Certificates of Deposit	677.0	1,025.0	(34.0%)
Subordinated bonds	1,250.0	-	x
Repo transactions	913.0	970.7	(5.9%)
Total assets	177,494.5	168,364.1	5.4%
Investment funds distributed through the Bank's network	18,311.0	16,660.4	9.9%
Total capital ratio in %	18.0%	17.0%	1 p.p.

(*) Including loans and non-quoted securities.

As at the end of September 2018, loans and advances at nominal value amounted to PLN 136,822.1 million, an increase of PLN 5,996.7 million, i.e. 4.6% in comparison to the end of September 2017. As at the end of September 2018, the volume of retail loans amounted to PLN 68,367.2 million and the volume of corporate loans amounted to PLN 57,309.8 million.

As at the end of September 2018, the amounts due to customers, Structured Certificates of Deposit, Certificates of Deposit and subordinated bonds amounted to PLN 145,766.7 million, an increase of PLN 9,181.6 million, i.e. 6.7% in comparison to the end of September 2017.

On October 30, 2017, the Bank issued 10- year subordinated bonds with a total nominal value of PLN 1,250.0 million with the maturity date on October 29, 2027. The funds from the issue were designated – after receiving the approval of the KNF on December 21, 2017 – to increase the Bank's supplementary capital, pursuant to art. 127 para. 2 point 2 of the Banking Law and art. 63 of Regulation No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms. The bonds were introduced to trading on the ASO Catalyst market and BondSpot.

The value of net assets of investment funds managed by Pekao TFI S.A. (ex. Pioneer Pekao TFI S.A.) distributed through the Bank's network amounted to PLN 18,311.0 million as at the end of September 2018, an increase of PLN 1,650.6 million, i.e. 9.9% in comparison to the end of September 2017.

Results of the Bank's major related entities

Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.) – Pekao IM
In the three quarters of 2018, consolidated net profit of Pekao IM amounted to **PLN 61.5** million compared with PLN 60.4 million in the three quarters of 2017. The higher result is related to the increase in net assets of investment funds managed by Pekao TFI S.A. by ca. 9% compared to the end of September 2017.

Pekao Leasing Sp. z o.o. – Pekao Leasing
In the three quarters of 2018, Pekao Leasing reported a net profit of **PLN 30.5 million** compared with PLN 25.4 million in the three quarters of 2017. In the three quarters of 2018, Pekao Leasing signed over 9.2 thousand new agreements, i.e. 14.9% increase year on year, while the value of leased assets was higher by 15.6% year on year and amounted to PLN 1,989.7 million.

Centralny Dom Maklerski Pekao S.A. – CDM
In the three quarters of 2018, net profit of CDM amounted to **PLN 20.8 million** compared with PLN 26.5 million profit earned million in the three quarters of 2017, influenced by lower turnover on the WSE, caused by less favourable situation on capital markets.

Pekao Faktoring Sp. z o.o. – Pekao Faktoring
In the three quarters of 2018, Pekao Faktoring reported a net profit of **PLN 9.3 million** compared with PLN 8.0 million in the three quarters of 2017 influenced by an increasing factoring commitment (increase by 15.9% year on year) and favourable situation on factoring market.

Pekao Financial Services Sp. z o.o. – PFS
In the three quarters of 2018, PFS reported a net profit in the amount of PLN 4.0 million (the Bank's share in the company's was **PLN 3.3 million)** compared with PLN 4.6 million in the three quarters of 2017. In 2018, the acquisition of the PZU Centrum Operacji S.A. was finalized by PFS. This transaction made it possible to take over PTE PZU S.A. and TFI PZU S.A. within the scope of the transfer agent service and extending the scope of service to PZU Życie S.A.

Dom Inwestycyjny Xelion Sp. z o.o. – DI Xelion
In the three quarters of 2018, DI Xelion reported a net profit in the amount of **PLN 3.6 million** compared with PLN 4.2 million in the three quarters of 2017, caused by less favourable situation on capital markets.

Centrum Bankowości Bezpośredniej Sp. z o.o.– CBB
In the three quarters of 2018, CBB reported a net profit in the amount of **PLN 3.6 million** compared with PLN 2.4 million in the three quarters of 2017, influenced by a larger number of marketing and sales campaigns and the implementation of new services provided to the Bank.

Pekao Investment Banking S.A. – PIB
In the three quarters of 2018, PIB reported net profit of **PLN 3.1** million compared with PLN 6.6 million in the three quarters of 2017, as the result of less favourable situation on the capital markets and a lower number of large transactions completed.

Pekao Powszechne Towarzystwo Emerytalne S.A – Pekao PTE
In the three quarters of 2018, Pekao PTE reported net profit of **PLN 2.8** million compared with PLN 1.7 million in the three quarters of 2017, influenced by of the settlement of PTE's participation in the Guarantee Fund and the implementation of the PTE Company's sales contract. The result of Pekao PTE for the current period does not include the result on the PTE sale transaction, because the transaction was classified as a transaction within the group, and the result of this transaction was included in the Group's equity.

Pekao Bank Hipoteczny S.A. – Pekao Bank Hipoteczny
In the three quarters of 2018, Pekao Bank Hipoteczny reported a net profit of **PLN 2.1 million** compared with PLN 3.9 million in the three quarters of 2017, as a result of the impact of a lower average level of assets due to the early repayment of credit exposures.

6.4 Provisions, deferred tax assets and liabilities

(in PLN million)

	GROUP		BANK PEKAO S.A.	
	30.09.2018	30.09.2017	30.09.2018	30.09.2017
Total provisions	**589.8**	**596.5**	**591.2**	**599.6**
of which:				
provisions for off-balance sheet commitments	209.9	222.8	223.4	229.9
provisions for liabilities to employees	333.6	334.3	324.2	330.9
other provisions	46.3	39.4	43.6	38.8
Deferred tax liabilities	**33.2**	**4.1**	**-**	**-**
Deferred tax assets	**1,230.2**	**924.9**	**964.3**	**693.1**

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

(in PLN million)

	GROUP		BANK PEKAO S.A.	
	3 QUARTERS OF 2018	3 QUARTERS OF 2017	3 QUARTERS OF 2018	3 QUARTERS OF 2017
financial assets measured at amortized cost	(403.9)	(365.8)	(375.9)	(359.6)
financial assets measured at fair value through other comprehensive income	2.5	(0.1)	7.5	0.0
financial liabilities measured at amortized cost	(4.7)	(2.6)	(9.5)	(4.4)
Net impairment losses on financial assets and off-balance sheet commitments	**(406.1)**	**(368.5)**	**(377.9)**	**(364.0)**

The Group's net impairment losses on financial assets and off-balance sheet commitments amounted to PLN 406.1 million in the three quarters of 2018, an increase of PLN 37.6 million, i.e. 10.2% as compared with the three quarters of 2017.

The Bank's net impairment losses on financial assets and off-balance sheet commitments amounted to PLN 377.9 million on the three quarters of 2018, an increase of PLN 13.9 million i.e. 3.8% as compared with the three quarters of 2017.

6.6 Off–balance sheet items

(in PLN million)

	30.09.2018	30.09.2017	CHANGE
Contingent liabilities granted and received	65,306.3	58,496.1	11.6%
Liabilities granted:	46,619.4	45,024.8	3.5%
financial	34,580.6	33,610.8	2.9%
guarantees	12,038.8	11,414.0	5.5%
Liabilities received:	18,686.9	13,471.3	38.7%
financial	900.3	999.5	(9.9%)
guarantees	17,786.6	12,471.8	42.6%
Derivative financial instruments	235,063.6	196,230.2	19.8%
interest rate transactions	136,747.8	92,093.5	48.5%
transactions in foreign currency and in gold	95,486.5	103,240.1	(7.5%)
transactions based on commodities and equity securities	2,829.3	896.6	>100%
Total off-balance sheet items	**300,369.9**	**254,726.3**	**17.9%**

6.7 Capital adequacy

Capital ratios are the basic measure applied for the measurement of capital adequacy according to Regulation of the European Parliament and of the Council (EU) No 575/2013 of June 26, 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (CRR Regulation), which entered into force since January 1, 2014 together with further amendments.

Capital ratios, capital requirements and own funds have been calculated in accordance with the above mentioned CRR Regulation using national options defined in article 171a of The Banking Act, Act of 5 August 2015 on macro-prudential supervision over financial system and crisis management in financial system (Act on macro-prudential supervision), as well as regulations of minister in charge of the finance.

According to law, Group is required to maintain minimal values of capital ratios resulting from Pillar I level (CRR Regulation), capital requirement of Pillar II resulting from The Banking Act and combined buffer requirement resulting from Act on macro-prudential supervision.

Minimal value of capital ratios on Pillar I level are:

- Total capital ratio (TCR) in amount of 8%,
- Tier I capital ratio (T1) in amount of 6%,
- Common Equity Tier I capital ratio (CET 1) in amount of 4.5%.

For Group, capital requirement of Pillar II, resulting from individual requirement imposed on Pekao Bank Hipoteczny, by KNF, amounts to:

- 0.01% for total capital ratio,
- 0.0075% for capital Tier I.

Combined buffer requirement consists of:

- Capital conservation buffer in amount of 1.875%,
- Countercyclical capital buffer in amount of 0.0084%,
- Other systemically important institution buffer in amount of 0.75%,
- Systemic risk buffer in amount of 3%.

In total, Group is required to maintain:

- Total capital ratio (TCR) in amount of 13.64%,
- Capital ratio Tier I (T1) in amount of 11.64%,
- Common Equity Tier (CET 1) in amount of 10.14%.

As of September 30, 2018 for Group, total capital ratio amounted to 17.0% and Tier I ratio amounted to 16.0%. The capital ratios were significantly above the minimum required by the law.

The table below presents the basic information concerning the Group capital adequacy as of September 30, 2018, December 31, 2017 and September 30, 2017 according to regulation which were in force at those dates.

(in PLN thousand)

CAPITAL REQUIREMENT	30.09.2018	31.12.2017	30.09.2017
Credit risk	9,179,444	8,833,498	9,093,274
Exceeding the exposure concentration limit and large exposures limit	-	-	-
Market risk	55,941	48,154	45,670
Counterparty credit risk including CVA	123,354	139,865	144,824
Operational risk	564,145	560,851	489,678
Total capital requirement	**9,922,885**	**9,582,368**	**9,773,446**
OWN FUNDS			
Common Equity Tier I Capital	19,855,913	19,252,010	20,146,611
Tier II Capital	1,250,000	1,250,000	
Own funds for total capital ratio	**21,105,913**	**20,502,010**	**20,146,611**
Common Equity Tier I Capital ratio (%)	**16.0%**	**16.1%**	**16.5%**
Total capital ratio TCR (%)	**17.0%**	**17.1%**	**16.5%**

Total Capital Ratio of the Group as at the end of September 2018 was higher by 0.5 p.p. compared to the end of September 2017 mainly due to higher own funds, partially compensated by higher capital requirement.

Increase in own funds for total capital ratio calculation resulted from including in Tier II capital the amount of PLN 1.25 billion from the issue of subordinated bonds.

Total capital requirement increased by 1.5%, mainly due to higher operational risk capital requirement resulting from purchase of remaining part of Xelion and PPIM and credit risk capital requirement resulting mainly from increase in loan volumes.

6.8 Reconciliation of income statement – presentation form and long form

Consolidated income statement for the three quarters of 2018

(in PLN thousand)

INCOME STATEMENT – PRESENTATION FORM'S ITEMS	LONG FORM'S ITEMS RECLASSIFFIED TO PRESENTATION FORM	3 QUARTERS OF 2018
Net interest income		3,699,216
Dividend income		20,025
	Dividend income	20,025
Total net interest income and dividend income		**3,719,241**
Net fee and commission income	Net fee and commission income	1,824,314
Trading result		130,357
	Net result on other financial instruments at fair value through profit and loss	62,171
	Result on fair value hedge accounting	3,158
	Gains (losses) on derecognition of debt securities not measured at fair value through profit or loss	65,094
	(Gains) losses on derecognition of financial assets and liabilities not measured at fair value through profit or loss	(66)
Net other operating income and expenses		39,604
	Net other operating income and expenses	39,294
	Gains (losses) on derecognition of loans and other financial receivables not measured at fair value through profit or loss	310
Net non-interest income		**1,994,275**
Operating income		**5,713,516**
Operating costs		(2,596,671)
	Personnel expenses	(1,545,699)
	Other administrative expenses	(1,433,263)
	less –Guarantee funds charges	234,808
	less – Tax on certain financial institutions	417,828
	Depreciation and amortization	(270,345)
Gross operating profit		**3,116,845**
Net impairment losses on financial assets and off-balance sheet commitments	Net impairment losses on loans and off-balance sheet commitments	(406,170)
Net operating profit		**2,710,675**
Net result on other provisions	Net result on other provisions	(14,364)
Guarantee funds charges	Guarantee funds charges	(234,808)
Tax on certain financial institutions	Tax on certain financial institutions	(417,828)
Net result on investment activities		26,903
	(Gains) losses on disposal of property, plant and equipment and intangible assets.	26,903
Profit before income tax		**2,070,578**
Income tax expense	Income tax expense	(531,967)
Net profit for the period	**Net profit for the period**	**1,538,611**
Attributable to equity holders of the Bank	**Attributable to equity holders of the Bank**	**1,537,933**
Attributable to non-controlling interest	Attributable to non-controlling interest	678

Consolidated income statement for the three quarters of 2017

(in PLN thousand)

INCOME STATEMENT – PRESENTATION FORM'S ITEMS	LONG FORM'S ITEMS RECLASSIFFIED TO PRESENTATION FORM	3 QUARTERS OF 2017
Net interest income		3,403,330
Dividend income and income from equity investments		51,300
	Dividend income	19,641
	Gains (losses) on subsidiaries and associates	31,659
Total net interest income, dividend income and other income from equity investments		**3,454,630**
Net fee and commission income	Net fee and commission income	1,735,852
Trading result		49,703
	Net result on other financial instruments at fair value through profit and loss	20,119
	Result on fair value hedge accounting	3,966
	Gains (losses) on disposal of available for sale financial assets and held to maturity investments	25,770
	(Gains) losses on disposal of financial liabilities	(152)
Net other operating income and expenses		87,840
	Net other operating income and expenses	87,522
	less - Refunding of administrative expenses	(1,888)
	Gains (losses) on disposal of loans and other financial receivables	2,206
Net non-interest income		**1,873,395**
Operating income		**5,328,025**
Operating costs		(2,408,861)
	Personnel expenses	(1,445,502)
	Other administrative expenses	(1,341,466)
	less –Guarantee funds charges	246,376
	less – tax on certain financial institution	383,480
	Refunding of administrative expenses	1,888
	Depreciation and amortization	(253,637)
Gross operating profit		**2,919,164**
Net impairment losses on loans and off-balance sheet commitments		(368,454)
	Net impairment losses on loans	(365,824)
	Net impairment provision for off-balance sheet commitments	(2,630)
Net operating profit		**2,550,710**
Net result on other provisions	Net result on other provisions	(21,970)
Guarantee funds charges	Guarantee funds charges	(246,376)
Tax on certain financial institution	Tax on certain financial institution	(383,480)
Net result on investment activities		342
	Gains (losses) on disposal of property, plant and equipment and intangible assets.	441
	Net impairment losses: on financial assets available for sale and held to maturity investments	(99)
Profit before income tax		**1,899,226**
Income tax expense	Income tax expense	(477,649)
Net profit for the period	**Net profit for the period**	**1,421,577**
Attributable to equity holders of the Bank	**Attributable to equity holders of the Bank**	**1,420,998**
Attributable to non-controlling interest	Attributable to non-controlling interest	579

7 Quarterly Income Statement

7.1 Consolidated income statement – long form

Consolidated income statement for 2018 and 2017

(in PLN thousand)

	Q3 2018	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017
Interest income	1,544,067	1,515,910	1,478,564	1,459,134	1,414,047	1,392,566	1,374,967
Interest expense	(286,078)	(280,373)	(272,874)	(268,968)	(261,926)	(256,384)	(259,940)
Net interest income	**1,257,989**	**1,235,537**	**1,205,690**	**1,190,166**	**1,152,121**	**1,136,182**	**1,115,027**
Fee and commission income	714,682	707,067	675,428	703,574	658,913	659,104	641,974
Fee and commission expense	(95,695)	(89,794)	(87,374)	(86,381)	(78,829)	(76,818)	(68,492)
Net fee and commission income	**618,987**	**617,273**	**588,054**	**617,193**	**580,084**	**582,286**	**573,482**
Dividend income	**245**	**19,623**	**157**	**131**	**223**	**19,269**	**149**
Result on financial assets and liabilities measured at fair value through profit or loss	**26,507**	**16,539**	**19,125**	**22,873**	**11,246**	**858**	**8,015**
Result on fair value hedge accounting	**1,159**	**662**	**1,337**	**650**	**919**	**1,334**	**1,713**
Result on derecognition of financial assets and liabilities not measured at fair value through profit or loss	**14,261**	**27,245**	**23,832**	**x**	**x**	**x**	**x**
Gains (losses) on disposal of financial assets and liabilities	**x**	**x**	**x**	**159,337**	**21,882**	**5,118**	**824**
Operating income	**1,919,148**	**1,916,879**	**1,838,195**	**1,990,350**	**1,766,475**	**1,745,047**	**1,699,210**
Net impairment losses on financial assets and off-balance sheet commitments	**(155,277)**	**(123,932)**	**(126,961)**	**(152,797)**	**(138,579)**	**(114,848)**	**(115,126)**
Net result on financial activity	**1,763,871**	**1,792,947**	**1,711,234**	**1,837,553**	**1,627,896**	**1,630,199**	**1,584,084**
Administrative expenses	**(922,069)**	**(980,579)**	**(1,076,314)**	**(922,856)**	**(884,976)**	**(865,632)**	**(1,036,360)**
personnel expenses	(490,526)	(554,827)	(500,346)	(504,800)	(493,184)	(482,349)	(469,969)
other administrative expenses(*)	(431,543)	(425,752)	(575,968)	(418,056)	(391,792)	(383,283)	(566,391)
Depreciation and amortization	**(92,672)**	**(89,893)**	**(87,780)**	**(93,701)**	**(84,070)**	**(85,225)**	**(84,342)**
Net result on other provisions	**(297)**	**(13,768)**	**(299)**	**(14,053)**	**(7,968)**	**(8,467)**	**(5,535)**
Net other operating income and expenses	**13,574**	**12,095**	**13,625**	**24,926**	**39,630**	**12,153**	**35,739**
Operating costs	**(1,001,464)**	**(1,072,145)**	**(1,150,768)**	**(1,005,684)**	**(937,384)**	**(947,171)**	**(1,090,498)**
Gains (losses) on subsidiaries and associates	**-**	**-**	**-**	**421,755**	**11,105**	**10,444**	**10,110**
Gains (losses) on disposal of property, plant and equipment, and intangible assets	**30,843**	**(6,863)**	**2,923**	**181**	**375**	**(59)**	**125**
Profit before income tax	**793,250**	**713,939**	**563,389**	**1,253,805**	**701,992**	**693,413**	**503,821**
Income tax expense	(186,941)	(173,962)	(171,064)	(199,674)	(165,406)	(158,214)	(154,029)
Net profit for the period	**606,309**	**539,977**	**392,325**	**1,054,131**	**536,586**	**535,199**	**349,792**
Attributable to equity holders of the Bank	**605,793**	**539,815**	**392,325**	**1,054,131**	**536,220**	**535,069**	**349,709**
Attributable to non-controlling interest	516	162	-	-	366	130	83

(*) Other administrative expenses includes tax on certain financial institutions and guarantee funds charges.

7.2 Consolidated statement of comprehensive income

Consolidated statement of comprehensive income for 2018 and 2017

(in PLN thousand)

	Q3 2018	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017
Net profit for the period	**606,309**	**539,977**	**392,325**	**1,054,131**	**536,586**	**535,199**	**349,792**
attributable to equity holders of the Bank	**605,793**	**539,815**	**392,325**	**1,054,131**	**536,220**	**535,069**	**349,709**
attributable to non-controlling interest	516	162	-	-	366	130	83
Other comprehensive income							
Items 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	(43,432)	(51,033)	109,292	x	x	x	x
Change in fair value of available-for-sale financial assets	x	x	x	(39,359)	2,986	94,566	172,399
Change in fair value of cash flow hedges	(28,960)	(3,531)	(17,323)	(26,332)	25,287	(27,607)	(4,491)
Tax on items that are or may be reclassified subsequently to profit or loss	13,754	10,367	(17,474)	12,482	(5,373)	(12,721)	(31,903)
Items that will never be reclassified to profit or loss:							
Investment in equity instruments designated at fair value through other comprehensive income	1,463	(13,940)	(5,431)	x	x	x	x
Remeasurement of the defined benefit liabilities	-	-	-	8,557	-	-	-
Share in remeasurements of the defined benefit liabilities of associates	-	-	-	-	-	-	-
Tax on items that will never be reclassified to profit or loss	(279)	2,649	1,032	(1,625)	-	-	-
Other comprehensive income (net of tax)	**(57,454)**	**(55,488)**	**70,096**	**(46,277)**	**22,900**	**54,238**	**136,005**
Total comprehensive income	**548,855**	**484,489**	**462,421**	**1,007,854**	**559,486**	**589,437**	**485,797**
attributable to equity holders of the Bank	**548,339**	**484,327**	**462,421**	**1,007,854**	**559,120**	**589,307**	**485,714**
attributable to non-controlling interest	516	162	-	-	366	130	83

7.3 Consolidated income statement – presentation form

Consolidated income statement for 2018 and 2017

(in PLN thousand)

	Q3 2018	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017
Net interest income	1,257,989	1,235,537	1,205,690	1,190,166	1,152,121	1,136,182	1,115,027
Dividend income and income from equity investments	245	19,623	157	7,909	11,328	29,713	10,259
Total net interest income, dividend income and other income from equity investments	**1,258,234**	**1,255,160**	**1,205,847**	**1,198,075**	**1,163,449**	**1,165,895**	**1,125,286**
Net fee and commission income	618,987	617,273	588,054	617,193	580,084	582,286	573,482
Trading result	41,789	44,274	44,294	39,085	31,934	7,283	10,486
Net other operating income and expenses	13,712	12,267	13,625	168,043	41,106	11,609	35,125
Net non-interest income	**674,488**	**673,814**	**645,973**	**824,321**	**653,124**	**601,178**	**619,093**
Operating income	**1,932,722**	**1,928,974**	**1,851,820**	**2,022,396**	**1,816,573**	**1,767,073**	**1,744,379**
Operating costs	**(843,295)**	**(901,896)**	**(851,480)**	**(854,489)**	**(814,899)**	**(800,246)**	**(793,716)**
Gross operating profit	**1,089,427**	**1,027,078**	**1,000,340**	**1,167,907**	**1,001,674**	**966,827**	**950,663**
Net impairment losses on financial assets and off-balance sheet commitments	(155,277)	(123,932)	(126,961)	(152,797)	(138,480)	(114,848)	(115,126)
Net operating profit	**934,150**	**903,146**	**873,379**	**1,015,110**	**863,194**	**851,979**	**835,537**
Net result on other provisions	(297)	(13,768)	(299)	(14,053)	(7,968)	(8,467)	(5,535)
Guarantee funds charges	(30,512)	(29,983)	(174,313)	(22,609)	(22,715)	(22,509)	(201,152)
Tax on certain financial institutions	(140,934)	(138,593)	(138,301)	(138,801)	(130,795)	(127,531)	(125,154)
Net result on investment activities	30,843	(6,863)	2,923	414,158	276	(59)	125
Profit before income tax	**793,250**	**713,939**	**563,389**	**1,253,805**	**701,992**	**693,413**	**503,821**
Income tax expense	(186,941)	(173,962)	(171,064)	(199,674)	(165,406)	(158,214)	(154,029)
Net profit	**606,309**	**539,977**	**392,325**	**1,054,131**	**536,586**	**535,199**	**349,792**
Attributable to equity holders of the Bank	**605,793**	**539,815**	**392,325**	**1,054,131**	**536,220**	**535,069**	**349,709**
Attributable to non-controlling interest	516	162	-	-	366	130	83

Note: The fourth quarter of 2017 net profit includes gain on measurement to fair value of previously held shares, related to the acquisition of remaining shares in Pekao Investment Management S.A. (ex. Pioneer Pekao Investment Management S.A.)and Dom Inwestycyjny Xelion Spółka z o.o. in the amount of PLN 414 million.

8 Other Information

8.1 Management Board position regarding the possibility of achieving previously published forecasts

The Bank has not published the forecast of the financial results for 2018.

8.2 The issuer's shares held by the Management and Supervisory Board Members

According to information available to the Bank, as at the date of submitting of Report on the activities of Bank Pekao S.A. Group for the three quarters of 2018 and as at the date of submitting of Report on the activities of Bank Pekao S.A. Group for the three quarters 2018, the Members of the Bank's management and supervisory bodies did not held shares of Bank Pekao S.A.

8.3 Related party transactions

In the third quarters of 2018, the Bank and its subsidiaries have not concluded any significant transactions (single or aggregate) with related entities other than those executed on arm's length.

In the third quarters of 2018, the Bank and its subsidiaries did not provide any sureties in respect of loans or advances or did not provide any guarantees to an entity or a subsidiary of such entity, which the total value would be significant.

Detailed information on related party transactions is included in Note 43 to the Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period of 9 months ended on 30 September 2018.

8.4 Accounting principles adopted in the preparation of the report

Accounting principles adopted in the preparation of the report are described in Note 5 to the Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period of 9 months ended on 30 September 2018.

8.5 Seasonality or cyclical nature of the Bank's activity

The demand for the financial services offered by the Bank is stable with no material impact of seasonal changes. Due to the nature of the Bank's activity, it is not subject to seasonal or cyclical changes.

8.6 Issuance, redemption and repayment of debt securities

Structured Certificates of Deposit
Structured Certificates of Deposit are investment products for the Bank's clients that form an alternative to traditional banks' deposits. The total value of the Bank's liabilities relating to these products amounted to PLN 468.1million (principal value) as at the end of September 2018. There is 9 issuances of Structured Certificates of Deposit open in PLN with the maximum maturity date on August 16, 2021. The liabilities with the maturity date in 2018, 2019, 2020 and 2021 accounts for 34.6%, 36.2%, 18.6% and 10.5% of its total value respectively.

Certificates of Deposit
Certificates of Deposit are investment products denominated in PLN that guarantee 100% protection of invested funds also in case of termination before redemption date. The total value of the Bank's liabilities under these products amounted to PLN 677.0 million (principal value) as at the end of September 2018. There are 4 issuances of Certificates of Deposit. The liabilities with the maturity date up to 1 month and up to 1 year account for 6.1% and 93.9% of its total value respectively.

Subordinated bonds
On October 30, 2017, the Bank issued 10 year subordinated bonds with a total nominal value of PLN 1,250.0 million with the maturity date on October 29, 2027. The funds from the issue were designated – after receiving the approval of the KNF on December 21, 2017 – to increase the Bank's supplementary capital, pursuant to art. 127 para. 2 point 2 of the Banking Law and art. 63 of Regulation No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms. The bonds were introduced to trading on the ASO Catalyst market and BondSpot.

Pekao Bank Hipoteczny S.A. covered bonds
The total value of the company's liabilities due to covered bonds amounted to PLN 1,519.6 million (principal value) as at the end of September, 2018. The liabilities under covered bonds with maturity date up to 1 year account for 14.6%, with maturity date from 1 up to 3 years account for 32.8%, with maturity date from 3 up to 5 years account for 23.0% and with maturity date from 5 up to 10 years account for 29.5% of the total nominal value.

Pekao Bank Hipoteczny S.A bonds
The total value of the company's liabilities under bonds with maturity date to 1 year, amounted to PLN 300.0 million (principal value) as of September 30, 2018,

Pekao Leasing Sp. z o.o. bonds
The total value of the company's liabilities under bonds amounted to PLN 1,766.6 million (principal value) as of September 30, 2018. The liabilities with the maturity date up to 1 months, up to 3 months, up to 6 months, up to 1 year, and up to 3 years accounts for 8.1% , 29.6% , 51.0%, 0.5% and 10.8% of its total value respectively.

8.7 Pending litigations

Information on significant legal proceedings pending before courts, arbitration bodies or public administration authorities in respect of liabilities and receivables of the Bank and its subsidiaries is included in Note 41 to the Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period from 1 January 2018 to 30 September 2018.

8.8 Subsequent events

Issuance of subordinated bonds of Bank Pekao S.A.
On October 4, 2018, in reference to the Current Report No. 20/2018 of September 11, 2018 regarding the consent to the non-public issue of subordinated bonds of Bank Pekao S.A. The Management Board of Bank Pekao S.A . hereby informs that after completion of the book building process, the Bank's Management Board adopted resolutions regarding the issue of two series (series B and series C) of subordinated bonds of the Bank. The total nominal value of both series of the bonds to be issued is PLN 750,000,000 The issue amount reflects situation on the bond market and the current capital requirements of the Bank.

After obtaining the approval of the Polish Financial Supervision Authority, the bonds will be classified as Tier 2 instruments.

The main conditions for the issue of the series B subordinate bonds of the Bank are as follows:

1. Type of bonds: bearer bonds; the bonds will not have a documentary form and the bonds will be registered on the issue date in the deposit of securities maintained by the National Depository for Securities,
2. Total number of bonds to be issued: 1,100,
3. The nominal value of one bond: PLN 500,000,
4. The total nominal value of bonds to be issued: PLN 550,000,000,
5. Interest rate: floating, based on the reference rate of WIBOR for six months deposits (WIBOR 6M) plus a margin of 1.55 percentage points;

6. Format of issue: 10NC5, i.e. bonds with 10- year maturity, with a reserved call option giving the Bank the right to redeem the bonds earlier, after 5 years from the date of issue or in other cases indicated in the terms and conditions of the bonds (no approval by the PFSA for being classified as a Tier 2 instrument, changes in the regulatory classification of bonds, change in taxation of bonds), subject to the approval of the PFSA , if such approval will be required,
7. Issue price: equal to the nominal value,
8. Currency: Polish zloty,
9. Issue date: October 15, 2018,
10. Maturity date: October 16, 2028, subject to the possibility of their early redemption on the terms described in point 6 directly above,
11. Trading: Bonds to be traded on the alternative trading system of debt securities on the Catalyst market maintained by the Bondspot S.A or Warsaw Stock Exchange,
12. Purpose of the issue: the purpose of the issue, within the meaning of Article 32 Section 1 of the Act of January 15, 2015 on bonds, has not been specified.

The main conditions for the issue of the series C subordinate bonds of the Bank are as follows:

1. Type of bonds: bearer bonds; the bonds will not have a documentary form and the bonds will be registered on the issue date in the deposit of securities maintained by the National Depository for Securities,
2. Total number of bonds to be issued: 400,
3. The nominal value of one bond: PLN 500,000,
4. The total nominal value of bonds to be issued: PLN 200,000,000,
5. Interest rate: floating, based on the reference rate of WIBOR for six months deposits (WIBOR 6M) plus a margin of 1.80 percentage points,
6. Format of issue: 15NC10, i.e. bonds with 15-year maturity, with a reserved call option giving the Bank the right to redeem the bonds earlier, after 10 years from the date of issue or in other cases indicated in the terms and conditions of the bonds (no approval by the PFSA for being classified as a Tier 2 instrument, changes in the regulatory classification of bonds, change in taxation of bonds), subject to the approval of the PFSA, if such approval will be required,
7. Issue price: equal to the nominal value,
8. Currency: Polish zloty,
9. Issue date: October 15, 2018,
10. Maturity date: October 14, 2033, subject to the possibility of their early redemption on the terms described in point 6 directly above,
11. Trading: Bonds to be traded on the alternative trading system of debt securities on the Catalyst market maintained by the Bondspot S.A or Warsaw Stock Exchange,
12. Purpose of the issue: the purpose of the issue, within the meaning of Article 32 Section 1 of the Act of January 15, 2015 on bonds, has not been specified.

Confirmation of the Issuer Credit Rating (ICR), maintenance of its stable outlook and upgrade of the long-term Bank's Resolution Counterparty Rating (RCR) by S&P Global Ratings

On October 15, 2018, in the current report No. 23/2018, the Management Board of Bank Pekao S.A. informed that on October 15, 2018 the rating agency S&P Global Ratings ("S&P") informed the Bank about the review of the Bank's ratings.

Bank's ratings were reviewed following the upgrade of the long-term rating on Poland from “BBB+" to “A-“ on October 12, 2018.

As a result of the review, S&P confirmed the Issuer Credit Rating (“ICR") and its stable outlook, upgraded the long-term and confirmed the short-term Resolution Counterparty Rating (“RCR") of the Bank.
The Issuer Credit Rating for the Bank (“ICR") has been maintained at the following levels:

(i) Long-term rating: "BBB+"

(ii) Short-term rating: "A-2"

(iii) Outlook: "Stable"

(iv) Stand-alone: "bbb".

Stable outlook on the Bank's ratings reflects the stable outlook on ratings of PZU S.A., the largest shareholder of Bank and the largest insurer in Poland.

An RCR is a forward-looking opinion of the relative default risk of certain senior liabilities that may be protected from default with an effective bail-in resolution process.

The long-term RCR for the Bank has been upgraded from “BBB+" to “A-“.

The short-term RCR for the Bank has been maintained at “A-2".

Fitch Ratings update of Bank Pekao ratings and outlook

On October 17, 2018, in the current report No. 24/2018, the Management Board of Bank Pekao S.A. informed that on October 17, 2018, informed the Bank about the review of Bank's Long-Term IDR and Viability Ratings and the change of the Long-Term IDR Outlook from Negative to Stable.

As a result of the review, the following rating actions were taken by Fitch: change of Long-Term IDR: from "A-" to “BBB+", change of Outlook: from "Negative" to “Stable", change of Viability Rating: from "a-" to “bbb+", affirmed Short-term IDR: "F2", affirmed Support Rating: "5", affirmed Support Rating Floor: “No Floor"

“The downgrade of Bank's Long-Term IDR is driven by the downgrade of the VR. The downgrade of the Bank's VR reflects the decline of the Bank's core capital ratio measured within Fitch methodology to a level, which is broadly similar to peers also measured by Fitch methodology. In Fitch opinion the level of Bank's capital measured by Fitch methodology is no longer sufficient to support Bank's VR being above most of those peers'. Simultaneously, Fitch highlighted that its assessment of the Bank's regulatory as well as Fitch-based capital position remains strong.“

In Fitch opinion the IDRs of the Bank are driven by the bank's intrinsic strength, which is reflected in its VR. According to Fitch, the Bank's rating strengths include well-established domestic market franchise, stable business model, conservative risk appetite, strong capitalisation, sound asset quality, solid profitability and robust funding and liquidity.

After this decision Bank's rating are as follows: Long-term IDR: "BBB+", Outlook: "Stable", Short-term IDR: "F2", Viability Rating: "bbb+", Support Rating: "5", Support Rating Floor: “No Floor.

Decision of the Polish Financial Supervision Authority on expressing consent to qualify series C of subordinated bonds of the Bank Pekao S.A. as Tier II capital instruments of the Bank

On October 26, 2018, in the current report No. 25/2018, in reference to current report No. 20/2018 on September 11, 2018 and current report No. 22/2018 on October 4, 2018, the Management Board of Bank Pekao S.A. informed that on October 26 2018, received the decision of the Polish Financial Supervision Authority on expressing consent to qualify by the Bank 400 the C series subordinated bonds with a total nominal value of PLN 200,000,000 as instruments in Tier II capital of the Bank as stated in Article 63 of Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26th June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No. 648/2012, on terms specified in the documents submitted by the Bank in Office of the Polish Financial Supervision Authority, i.e. inter alia in Terms and Conditions of Series C Bonds.

Simultaneously with the issuance of Series C Bonds, Bank issued the B series subordinated bonds with a total nominal value of PLN 550,000,000. The application of the Bank to the Polish Financial Supervision Authority for the consent to qualify by the Bank the Series B Bonds as instruments in Tier II capital of the Bank is currently being examined.

2018 EU-Wide Stress Test Results

On November 2, 2018, in the current report No. 27/2018, the Management Board of Bank Pekao S.A. informed that the Bank was subject to the 2018 EU-wide stress test conducted by the European Banking Authority (EBA), in cooperation with the Polish Financial Supervision Authority (KNF), the European Central Bank (ECB), and the European Systemic Risk Board (ESRB), and the results were published by EBA. The tests place Bank Pekao S.A. among the three most resilient European banks (out of 48 included in the sample), with the sensitivity of capital ratios to stress conditions several times below the average of European banks.

The Bank fully acknowledges the outcomes of this exercise.

The 2018 EU-wide stress test does not contain a pass fail threshold and instead is designed to be used as an important source of information for the purposes of the supervisory review and evaluation process (SREP). The results will assist competent authorities in assessing Bank's ability to meet applicable prudential requirements under stressed scenarios.

The adverse stress test scenario was set by the ECB/ESRB and covers a three-year time horizon (2018-2020). The stress test has been carried out applying a static balance sheet assumption as at December 2017, and therefore does not take into account future business strategies and management actions. It is not a forecast of Bank profits.

Based on the results of the exercise and under the supervisor's control, the Bank will assess the impact of the results on the Bank's forward looking capital plans and its capacity to meet applicable prudential requirements; and determine whether any additional measures or changes to the Bank's capital plan are needed.

According to the EU-wide stress test results, the consolidated Common Equity Tier 1 (CET1) ratio of Bank would be in 2020 at the level of 16.50% under the baseline scenario and at 15.47% under the adverse scenario. Consolidated CET1 ratio of Bank reflecting the full IFRS9 effect would be at the level of 16.14% and 14.55% respectively.

Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period of 9 months ended on 30 September 2018

Warsaw, November 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	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Interest income	9	**1 544 067**	**4 538 541**	**1 414 047**	**4 181 580**
Financial assets measured at amortized cost		1 330 570	3 889 933	X	X
Financial assets measured at fair value through other comprehensive income		166 448	531 622	X	X
Financial assets measured at fair value through other profit or loss		47 049	116 986	X	X
Interest expense	9	**(286 078)**	**(839 325)**	**(261 926)**	**(778 250)**
Net interest income		**1 257 989**	**3 699 216**	**1 152 121**	**3 403 330**
Fee and commission income	10	714 682	2 097 177	658 913	1 959 991
Fee and commission expense	10	(95 695)	(272 863)	(78 829)	(224 139)
Net fee and commission income		**618 987**	**1 824 314**	**580 084**	**1 735 852**
Dividend income	11	**245**	**20 025**	**223**	**19 641**
Result on financial assets and liabilities measured at fair value through profit or loss	12	**26 507**	**62 171**	**11 246**	**20 119**
Result on fair value hedge accounting	30	**1 159**	**3 158**	**919**	**3 966**
Result on derecognition of financial assets and liabilities not measured at fair value through profit or loss	13	**14 261**	**65 338**	**X**	**X**
Gains (losses) on disposal of financial assets and liabilities	14	**X**	**X**	**21 882**	**27 824**
Operating income		**1 919 148**	**5 674 222**	**1 766 475**	**5 210 732**
Net impairment losses on financial assets and off-balance sheet commitments	15	**(155 277)**	**(406 170)**	**(138 579)**	**(368 553)**
Net result on financial activity		**1 763 871**	**5 268 052**	**1 627 896**	**4 842 179**
Administrative expenses	16	**(922 069)**	**(2 978 962)**	**(884 976)**	**(2 786 968)**
Personnel expenses		(490 526)	(1 545 699)	(493 184)	(1 445 502)
Other administrative expenses		(431 543)	(1 433 263)	(391 792)	(1 341 466)
Depreciation and amortization	17	**(92 672)**	**(270 345)**	**(84 070)**	**(253 637)**
Net result on other provisions		**(297)**	**(14 364)**	**(7 968)**	**(21 970)**
Net other operating income and expenses	18	**13 574**	**39 294**	**39 630**	**87 522**
Operating costs		**(1 001 464)**	**(3 224 377)**	**(937 384)**	**(2 975 053)**
Gains (losses) on subsidiaries and associates	19	**-**	**-**	**11 105**	**31 659**
Gains (losses) on disposal of property, plant and equipment and intangible assets	20	**30 843**	**26 903**	**375**	**441**
Profit before income tax		**793 250**	**2 070 578**	**701 992**	**1 899 226**
Income tax expense	21	**(186 941)**	**(531 967)**	**(165 406)**	**(477 649)**
Net profit		**606 309**	**1 538 611**	**536 586**	**1 421 577**
1. Attributable to equity holders of the Bank		605 793	1 537 933	536 220	1 420 998
2. Attributable to non-controlling interests		516	678	366	579
Earnings per share (in PLN per share)					
basic for the period	22	2.31	5.86	2.04	5.41
diluted for the period	22	2.31	5.86	2.04	5.41

Notes to the financial statements presented on pages 19 - 126 constitute an integral part of the consolidated financial statements.

Consolidated statement of comprehensive income

(in PLN thousand)

	NOTE	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FROM 01.01.2017 TO 30.09.2017
Net profit		**606 309**	**1 538 611**	**536 586**	**1 421 577**
1. Attributable to equity holders of the Bank		605 793	1 537 933	536 220	1 420 998
2. Attributable to non-controlling interests		516	678	366	579
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		(43 432)	14 827	X	X
Change in fair value of available-for-sale financial assets		X	X	2 986	269 951
Change in fair value of cash flow hedges	30	(28 960)	(49 814)	25 287	(6 811)
Tax on items that are or may be reclassified subsequently to profit or loss	21	13 754	6 647	(5 373)	(49 997)
Items that will never be reclassified to profit or loss:					
Investment in equity instruments designated at fair value through other comprehensive income		1 463	(17 908)	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	(279)	3 402	-	-
Other comprehensive income (net of tax)		**(57 454)**	**(42 846)**	**22 900**	**213 143**
Total comprehensive income		**548 855**	**1 495 765**	**559 486**	**1 634 720**
1. Attributable to equity holders of the Bank		548 339	1 495 087	559 120	1 634 141
2. Attributable to non-controlling interests		516	678	366	579

Notes to the financial statements presented on pages 19 - 126 constitute an integral part of the consolidated financial statements.

Consolidated statement of financial position

(in PLN thousand)

	NOTE	30.09.2018	31.12.2017
ASSETS			
Cash and due from Central Bank	24	5 720 292	5 236 318
Loans and advances to banks	25	4 762 209	2 627 327
Financial assets held for trading	26	540 831	1 730 416
Derivative financial instruments (held for trading)	27	1 063 094	1 349 047
Loans and advances to customers	28	121 392 985	127 949 307
1. Measured at amortised cost		119 903 648	X
2. Measured at fair value through profit or loss		318 464	X
3. Measured at fair value through other comprehensive income		1 170 873	X
Receivables from finance leases	29	4 864 586	4 351 352
Hedging instruments	30	221 139	259 396
Investments (placement) securities	31	39 177 343	36 905 822
1. Measured at fair value through profit or loss		72 737	X
2. Designated at fair value through profit or loss		-	-
3. Measured at fair value through other comprehensive income (debt securities)		28 203 973	X
4. Designated at fair value through other comprehensive income (equity instruments)		259 730	X
5. Measured at amortised cost		10 640 903	X
6. Available for sale		-	33 424 031
7. Held to maturity		-	3 481 791
Assets held for sale	32	40 096	65 565
Investments in associates		-	-
Intangible assets	33	1 474 237	1 525 645
Property, plant and equipment	34	1 351 935	1 425 469
Investment properties		11 242	22 167
Income tax assets		1 231 385	960 754
1. Current tax assets		1 166	9 959
2. Deferred tax assets		1 230 219	950 795
Other assets		1 447 091	1 056 985
TOTAL ASSETS		**183 298 465**	**185 465 570**
EQUITY AND LIABILITIES			
Liabilities			
Amounts due to Central Bank	24	5 045	6 079
Amounts due to other banks	36	4 689 311	4 981 291
Financial liabilities held for trading	26	370 412	469 448
Derivative financial instruments (held for trading)	27	1 781 000	2 030 103
Amounts due to customers	37	143 767 613	146 186 268
Hedging instruments	30	884 037	862 331
Debt securities issued	38	4 742 615	2 771 399
Subordinated liabilities	39	1 267 400	1 257 188
Income tax liabilities		267 723	237 885
1. Current tax liabilities		234 548	200 201
2. Deferred tax liabilities		33 175	37 684
Provisions	40	589 770	602 622
Other liabilities		2 933 229	2 793 142
TOTAL LIABILITIES		**161 298 155**	**162 197 756**
Equity			
Share capital		262 470	262 470
Other capital and reserves		20 798 038	20 561 177
Retained earnings and net profit for the period		928 276	2 444 167
Total equity attributable to equity holders of the Bank		**21 988 784**	**23 267 814**
Non-controlling interests		11 526	-
TOTAL EQUITY		**22 000 310**	**23 267 814**
TOTAL LIABILITIES AND EQUITY		**183 298 465**	**185 465 570**

Notes to the financial statements presented on pages 19 - 126 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 September 2018

	EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK										
	SHARE CAPITAL	OTHER CAPITAL AND RESERVES						RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY ATTRIBUTABLE TO EQUITY HOLDERS OF THE BANK	NON - CONTROLLING INTERESTS	TOTAL EQUITY
		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	**-**	**(42 006)**	**-**	**-**	**840**	**(42 846)**	**-**	**1 537 933**	**1 495 927**	**678**	**1 496 605**
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)	-	12 009	-	-	-	12 009	-	-	12 009	-	12 009
Revaluation or sale of investments in equity instruments designated at fair value through other comprehensive income (net of tax)	-	(13 666)	-	-	840	(14 506)	-	-	(13 666)	-	(13 666)
Revaluation of hedging financial instruments (net of tax)	-	(40 349)	-	-	-	(40 349)	-	-	(40 349)	-	(40 349)
Net profit for the period	-	-	-	-	-	-	-	1 537 933	1 537 933	678	1 538 611
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 30.09.2018	**262 470**	**20 798 038**	**9 137 221**	**1 982 459**	**9 136 862**	**135 036**	**406 460**	**928 276**	**21 988 784**	**11 526**	**22 000 310**

Notes to the financial statements presented on pages 19 - 126 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										
		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 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 19 - 126 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 September 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	**-**	**213 143**	**-**	**-**	**-**	**213 143**	**-**	**1 420 998**	**1 634 141**	**579**	**1 634 720**
Remeasurements of the defined benefit liabilities (net of tax)	-	-	-	-	-	-	-	-	-	-	-
Revaluation of available-for-sale investments (net of tax)	-	218 660	-	-	-	218 660	-	-	218 660	-	218 660
Revaluation of hedging financial instruments (net of tax)	-	(5 517)	-	-	-	(5 517)	-	-	(5 517)	-	(5 517)
Net profit for the period	-	-	-	-	-	-	-	1 420 998	1 420 998	579	1 421 577
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)	-	-	-
Equity as at 30.09.2017	**262 470**	**20 600 414**	**9 137 221**	**1 982 459**	**9 092 735**	**(10 251)**	**398 250**	**1 390 036**	**22 252 920**	**15 503**	**22 268 423**

Notes to the financial statements presented on pages 19 – 126 constitute an integral part of the consolidated financial statements.

Consolidated cash flow statement

(in PLN thousand)

	NOTE	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Cash flow from operating activities – indirect method					
Net profit for the period		**605 793**	**1 537 933**	**536 220**	**1 420 998**
Adjustments for:		**(2 469 659)**	**(9 722 364)**	**(1 165 120)**	**(9 235 874)**
Depreciation and amortization	17	92 672	270 345	84 070	253 637
Share of profit (loss) of associates	19	-	-	(11 105)	(31 659)
(Gains) losses on investing activities		(44 985)	(82 506)	(20 010)	(25 789)
Net interest income	9	(1 257 989)	(3 699 216)	(1 152 121)	(3 403 330)
Dividend income	11	(245)	(20 025)	(223)	(19 641)
Interest received		1 685 271	4 780 782	1 438 563	4 244 292
Interest paid		(285 358)	(811 729)	(254 113)	(806 714)
Income tax		186 941	531 967	165 406	477 649
Income tax paid		(160 455)	(623 129)	(101 018)	(251 285)
Change in loans and advances to banks		292 148	293 116	50 431	164 434
Change in financial assets held for trading		784 559	1 182 914	1 109 718	(367 643)
Change in derivative financial instruments (assets)		172 989	285 953	(78 478)	475 385
Change in loans and advances to customers		(3 639 364)	(7 372 825)	(3 457 151)	(6 403 953)
Change in receivables from finance leases		(193 125)	(516 731)	(157 083)	(278 764)
Change in investment (placement) securities		(11 887)	(493 463)	(241 766)	(327 617)
Change in other assets		(664 276)	(418 610)	(200 208)	(222 576)
Change in amounts due to banks		(632 392)	(238 773)	(70 041)	(328 789)
Change in financial liabilities held for trading		(55 491)	(99 036)	339 750	(43 607)
Change in derivative financial instruments (liabilities)		330 332	(249 103)	(118 163)	(576 374)
Change in amounts due to customers		833 818	(2 427 277)	1 587 059	(1 593 471)
Change in debt securities issued		(23 069)	(19 043)	44 845	51 931
Change in subordinated liabilities		10 387	10 212	-	-
Change in provisions		(69 915)	(73 712)	21 849	36 083
Change in other liabilities		179 775	67 525	(145 331)	(258 073)
Net cash flows from operating activities		**(1 863 866)**	**(8 184 431)**	**(628 900)**	**(7 814 876)**
Cash flow from investing activities					
Investing activity inflows		**31 571 506**	**106 829 392**	**11 220 010**	**31 305 872**
Sale of investment securities		31 275 226	106 069 521	10 954 673	30 663 945
Sale of intangible assets and property, plant and equipment		2 818	17 403	508	815
Dividend received		19 085	20 025	18 468	19 641
Transfer of management funds		-	22 680	-	-
Other investing inflows		274 377	699 763	246 361	621 471
Investing activity outflows		**(29 092 331)**	**(95 568 560)**	**(10 271 583)**	**(21 881 438)**
Acquisition of investment securities		(29 035 215)	(95 423 319)	(10 146 450)	(21 643 952)
Acquisition of intangible assets and property, plant and equipment		(57 116)	(145 241)	(125 133)	(237 486)
Net cash flows from investing activities		**2 479 175**	**11 260 832**	**948 427**	**9 424 434**

Notes to the financial statements presented on pages 19 - 126 constitute an integral part of the consolidated financial statements.

Consolidated cash flow statement (cont.)

(in PLN thousand)

	NOTE	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Cash flows from financing activities	42				
Financing activity inflows		**2 827 560**	**5 922 819**	**1 075 000**	**1 075 000**
Due to loans and advances received from banks		565 838	1 826 914	-	-
Issue of debt securities		2 261 722	4 095 905	1 075 000	1 075 000
Financing activity outflows		**(4 162 366)**	**(6 082 778)**	**(2 334 847)**	**(2 616 269)**
Repayment of loans and advances received from banks		(712 179)	(1 891 377)	(55 722)	(123 685)
Redemption of debt securities		(1 376 674)	(2 117 888)	(885)	(214 344)
Dividends and other payments to shareholders		(2 073 513)	(2 073 513)	(2 278 240)	(2 278 240)
Net cash flows from financing activities		**(1 334 806)**	**(159 959)**	**(1 259 847)**	**(1 541 269)**
Total net cash flows		**(719 497)**	**2 916 442**	**(940 320)**	**68 289**
including effect of exchange rate fluctuations on cash and cash equivalents held		(41 820)	57 508	28 329	(94 664)
Net change in cash and cash equivalents		**(719 497)**	**2 916 442**	**(940 320)**	**68 289**
Cash and cash equivalents at the beginning of the period	42	**10 980 979**	**7 345 040**	**9 674 699**	**8 666 090**
Cash and cash equivalents at the end of the period	42	**10 261 482**	**10 261 482**	**8 734 379**	**8 734 379**

Notes to the financial statements presented on pages 19 - 126 constitute an integral part of the consolidated financial statements.

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

Unconsolidated income statement of Bank Pekao S.A.

	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Interest income	**1 496 223**	**4 411 880**	**1 382 708**	**4 085 383**
Financial assets measured at amortized cost	1 282 419	3 760 710	X	X
Financial assets measured at fair value through other comprehensive income	166 457	533 314	X	X
Financial assets measured at fair value through other profit or loss	47 347	117 856	X	X
Interest expense	**(269 499)**	**(805 023)**	**(256 177)**	**(761 265)**
Net interest income	**1 226 724**	**3 606 857**	**1 126 531**	**3 324 118**
Fee and commission income	611 712	1 771 804	600 535	1 776 899
Fee and commission expense	(93 827)	(262 234)	(87 251)	(235 973)
Net fee and commission income	**517 885**	**1 509 570**	**513 284**	**1 540 926**
Dividend income	**168**	**255 204**	**136**	**187 940**
Result on financial assets and liabilities measured at fair value through profit or loss	**25 890**	**58 205**	**7 252**	**10 929**
Result on fair value hedge accounting	**1 159**	**3 158**	**919**	**3 966**
Result on derecognition of financial assets and liabilities not measured at fair value through profit or loss	**14 015**	**64 621**	**X**	**X**
Gains (losses) on disposal of financial assets and liabilities	**X**	**X**	**21 882**	**27 824**
Operating income	**1 785 841**	**5 497 615**	**1 670 004**	**5 095 703**
Net impairment losses on financial assets and off-balance sheet commitments	**(148 340)**	**(377 933)**	**(137 889)**	**(363 974)**
Net result on financial activity	**1 637 501**	**5 119 682**	**1 532 115**	**4 731 729**
Administrative expenses	**(849 022)**	**(2 762 916)**	**(833 003)**	**(2 626 802)**
personnel expenses	(425 856)	(1 356 300)	(441 932)	(1 291 921)
other administrative expenses	(423 166)	(1 406 616)	(391 071)	(1 334 881)
Depreciation and amortization	**(84 141)**	**(246 053)**	**(79 733)**	**(240 840)**
Net result on other provisions	**(303)**	**(14 700)**	**(8 102)**	**(19 759)**
Net other operating income and expenses	**10 061**	**32 207**	**37 964**	**83 558**
Operating costs	**(923 405)**	**(2 991 462)**	**(882 874)**	**(2 803 843)**
Gains (losses) on subsidiaries and associates	**-**	**(11 069)**	**-**	**-**
Gains (losses) on disposal of property, plant and equipment, and intangible assets	**30 631**	**36 070**	**197**	**299**
Profit before income tax	**744 727**	**2 153 221**	**649 438**	**1 928 185**
Income tax expense	**(177 773)**	**(502 394)**	**(157 139)**	**(455 683)**
Net profit	**566 954**	**1 650 827**	**492 299**	**1 472 502**
Earnings per share (in PLN per share)				
basic for the period	2.16	6.29	1.88	5.61
diluted for the period	2.16	6.29	1.88	5.61

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

Unconsolidated statement of comprehensive income of Bank Pekao S.A.

	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Net profit	**566 954**	**1 650 827**	**492 299**	**1 472 502**
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	(42 553)	11 118	X	X
Change in fair value of available-for-sale financial assets	X	X	2 896	269 393
Change in fair value of cash flow hedges	(28 960)	(49 814)	25 287	(6 811)
Tax on items that are or may be reclassified subsequently to profit or loss	13 587	7 352	(5 356)	(49 891)
Items that will never be reclassified to profit or loss:				
Investment in equity instruments designated at fair value through other comprehensive income	1 281	(17 944)	X	X
Remeasurements of the defined benefit liabilities	-	-	-	-
Tax on items that will never be reclassified to profit or loss	(244)	3 409	-	-
Other comprehensive income (net of tax)	**(56 889)**	**(45 879)**	**22 827**	**212 691**
Total comprehensive income	**510 065**	**1 604 948**	**515 126**	**1 685 193**

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

Unconsolidated statement of financial position of Bank Pekao S.A.

	30.09.2018	31.12.2017
ASSETS		
Cash and due from Central Bank	5 621 956	5 186 259
Loans and advances to banks	4 949 579	2 692 930
Financial assets held for trading	615 497	1 734 768
Derivative financial instruments (held for trading)	1 066 776	1 351 344
Loans and advances to customers	120 228 440	128 873 178
1. Measured at amortised cost	118 554 369	X
2. Measured at fair value through profit or loss	318 464	X
3. Measured at fair value through other comprehensive income	1 355 607	X
Hedging instruments	221 139	259 396
Investment (placement) securities	38 946 573	36 625 996
1. Measured at fair value through profit or loss	72 737	X
2. Designated at fair value through profit or loss	-	-
3. Measured at fair value through other comprehensive income (debt securities)	28 098 452	X
4. Designated at fair value through other comprehensive income (equity instruments)	245 035	X
5. Measured at amortised cost	10 530 349	X
6. Available for sale	-	33 259 172
7. Held to maturity	-	3 366 824
Assets held for sale	40 096	51 450
Investments in subsidiaries	1 682 756	1 693 825
Investments in associates	-	-
Intangible assets	579 101	629 321
Property, plant and equipment	1 323 970	1 401 291
Investment properties	11 242	12 462
Income tax assets	964 252	717 726
1. Current tax assets	-	9 497
2. Deferred tax assets	964 252	708 229
Other assets	1 243 171	847 062
TOTAL ASSETS	**177 494 548**	**182 077 008**
EQUITY AND LIABILITIES		
Liabilities		
Amounts due to Central Bank	5 045	6 079
Amounts due to other banks	2 997 262	3 438 801
Financial liabilities held for trading	370 412	469 448
Derivative financial instruments (held for trading)	1 790 639	2 036 928
Amounts due to customers	144 284 515	146 898 298
Hedging instruments	884 037	862 331
Debt securities issued	1 150 466	1 470 000
Subordinated liabilities	1 267 400	1 257 188
Income tax liabilities	227 443	188 505
1. Current tax liabilities	227 443	188 505
2. Deferred tax liabilities	-	-
Provisions	591 170	593 635
Other liabilities	2 831 895	2 597 261
TOTAL LIABILITIES	**156 400 284**	**159 818 474**
Equity		
Share capital	262 470	262 470
Other capital and reserves	20 117 715	19 907 935
Retained earnings and net profit for the period	714 079	2 088 129
TOTAL EQUITY	**21 094 264**	**22 258 534**
TOTAL LIABILITIES AND EQUITY	**177 494 548**	**182 077 008**

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

Unconsolidated statement of changes in equity of Bank Pekao S.A.

For the period from 1 January 2018 to 30 September 2018

	SHARE CAPITAL	OTHER CAPITAL AND RESERVES						RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY
		TOTAL OTHER CAPITAL AND RESERVES	SHARE PREMIUM	GENERAL BANKING RISK FUND	OTHER RESERVE CAPITAL	REVALUATION RESERVES	OTHER		
Equity as at 1.01.2018	**262 470**	**19 907 935**	**9 137 221**	**1 982 459**	**8 612 550**	**(57 422)**	**233 127**	**2 088 129**	**22 258 534**
Initial application of IFRS 9	-	240 203	-	-	-	240 203	-	(936 748)	(696 545)
Equity as at 1.01.2018 - restated	**262 470**	**20 148 138**	**9 137 221**	**1 982 459**	**8 612 550**	**182 781**	**233 127**	**1 151 381**	**21 561 989**
Management options	-	**-**	-	-	-	-	-	-	-
Options exercised (share issue)	-	-	-	-	-	-	-	-	-
Revaluation of management options	-	-	-	-	-	-	-	-	-
Comprehensive income	**-**	**(45 039)**	**-**	**-**	**840**	**(45 879)**	**-**	**1 650 827**	**1 605 788**
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)	-	9 005	-	-	-	9 005	-	-	9 005
Revaluation or sale of investments in equity instruments designated at t fair value through other comprehensive income (net of tax)	-	(13 695)	-	-	840	(14 535)	-	-	(13 695)
Revaluation of hedging financial instruments (net of tax)	-	(40 349)	-	-	-	(40 349)	-	-	(40 349)
Net profit for the period	-	-	-	-	-	-	-	1 650 827	1 650 827
Appropriation of retained earnings	-	**14 616**	**-**	**-**	**14 616**	**-**	**-**	**(2 088 129)**	**(2 073 513)**
Dividend paid	-	-	-	-	-	-	-	(2 073 513)	(2 073 513)
Profit appropriation	-	14 616	-	-	14 616	-	-	(14 616)	-
Equity as at 30.09.2018	**262 470**	**20 117 715**	**9 137 221**	**1 982 459**	**8 628 006**	**136 902**	**233 127**	**714 079**	**21 094 264**

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

For the period from 1 January 2017 to 31 December 2017

	SHARE CAPITAL	OTHER CAPITAL AND RESERVES						RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY
		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**	**19 741 712**	**9 137 221**	**1 982 324**	**8 612 550**	**(223 510)**	**233 127**	**2 278 375**	**22 282 557**
Management options	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Options exercised (share issue)	-	-	-	-	-	-	-	-	-
Revaluation of management options	-	-	-	-	-	-	-	-	-
Comprehensive income	**-**	**166 088**	**-**	**-**	**-**	**166 088**	**-**	**2 088 129**	**2 254 217**
Remeasurements of the defined benefit liabilities (net of tax)	-	6 957	-	-	-	6 957	-	-	6 957
Revaluation of available-for-sale investments (net of tax)	-	185 977	-	-	-	185 977	-	-	185 977
Revaluation of hedging financial instruments (net of tax)	-	(26 846)	-	-	-	(26 846)	-	-	(26 846)
Net profit for the period	-	-	-	-	-	-	-	2 088 129	2 088 129
Appropriation of retained earnings	**-**	**135**	**-**	**135**	**-**	**-**	**-**	**(2 278 375)**	**(2 278 240)**
Dividend paid	-	-	-	-	-	-	-	(2 278 240)	(2 278 240)
Profit appropriation	-	135	-	135	-	-	-	(135)	-
Equity as at 31.12.2017	**262 470**	**19 907 935**	**9 137 221**	**1 982 459**	**8 612 550**	**(57 422)**	**233 127**	**2 088 129**	**22 258 534**

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

For the period from 1 January 2017 to 30 September 2017

	SHARE CAPITAL	OTHER CAPITAL AND RESERVES						RETAINED EARNINGS AND NET PROFIT FOR THE PERIOD	TOTAL EQUITY
		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**	**19 741 712**	**9 137 221**	**1 982 324**	**8 612 550**	**(223 510)**	**233 127**	**2 278 375**	**22 282 557**
Management options	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**	**-**
Options exercised (share issue)	-	-	-	-	-	-	-	-	-
Revaluation of management options	-	-	-	-	-	-	-	-	-
Comprehensive income	**-**	**212 691**	**-**	**-**	**-**	**212 691**	**-**	**1 472 502**	**1 685 193**
Remeasurements of the defined benefit liabilities (net of tax)	-	-	-	-	-	-	-	-	-
Revaluation of available-for-sale investments (net of tax)	-	218 208	-	-	-	218 208	-	-	218 208
Revaluation of hedging financial instruments (net of tax)	-	(5 517)	-	-	-	(5 517)	-	-	(5 517)
Net profit for the period	-	-	-	-	-	-	-	1 472 502	1 472 502
Appropriation of retained earnings	**-**	**135**	**-**	**135**	**-**	**-**	**-**	**(2 278 375)**	**(2 278 240)**
Dividend paid	-	-	-	-	-	-	-	(2 278 240)	(2 278 240)
Profit appropriation	-	135	-	135	-	-	-	(135)	-
Equity as at 30.09.2017	**262 470**	**19 954 538**	**9 137 221**	**1 982 459**	**8 612 550**	**(10 819)**	**233 127**	**1 472 502**	**21 689 510**

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

Unconsolidated cash flow statement of Bank Pekao S.A.

	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Cash flow from operating activities – indirect method				
Net profit for the period	**566 954**	**1 650 827**	**492 299**	**1 472 502**
Adjustments for:	**(1 391 240)**	**(7 610 131)**	**(1 178 157)**	**(9 521 347)**
Depreciation and amortization	84 141	246 053	79 733	240 840
(Gains) losses on investing activities	(44 529)	(100 413)	(19 831)	(25 830)
Net interest income	(1 226 724)	(3 606 857)	(1 126 531)	(3 324 118)
Dividend income	(168)	(255 204)	(136)	(187 940)
Interest received	1 636 202	4 754 704	1 407 232	4 148 030
Interest paid	(267 337)	(783 294)	(247 206)	(788 396)
Income tax	177 773	502 394	157 139	455 683
Income tax paid	(140 156)	(561 671)	(80 291)	(218 622)
Change in loans and advances to banks	157 488	225 747	23 638	166 147
Change in financial assets held for trading	776 408	1 112 600	1 120 074	(371 159)
Change in derivative financial instruments (assets)	174 121	284 568	(72 160)	497 994
Change in loans and advances to customers	(2 669 298)	(5 385 959)	(3 612 913)	(7 004 061)
Change in investment (placement) securities	(10 351)	(491 769)	(240 740)	(324 399)
Change in other assets	(650 821)	(421 083)	(172 374)	(193 989)
Change in amounts due to banks	(645 553)	(255 273)	(34 687)	(159 856)
Change in financial liabilities held for trading	(55 491)	(99 036)	339 750	(43 607)
Change in derivative financial instruments (liabilities)	335 308	(246 289)	(118 159)	(567 764)
Change in amounts due to customers	830 826	(2 622 525)	1 567 046	(1 591 703)
Change in debt securities issued	(11 521)	(12 526)	243	826
Change in subordinated liabilities	10 387	10 212	-	-
Change in provisions	(64 447)	(62 820)	28 142	39 104
Change in other liabilities	212 502	158 310	(176 126)	(268 527)
Net cash flows from operating activities	**(824 286)**	**(5 959 304)**	**(685 858)**	**(8 048 845)**
Cash flow from investing activities				
Investing activity inflows	**31 524 526**	**106 955 778**	**11 217 229**	**31 440 753**
Sale of investment securities	31 250 539	105 994 733	10 954 357	30 635 447
Sale of intangible assets and property, plant and equipment	1 612	8 866	115	133
Dividend received	168	255 204	18 381	187 940
Other investing inflows	272 207	696 975	244 376	617 233
Investing activity outflows	**(29 064 976)**	**(95 489 798)**	**(10 266 952)**	**(21 837 716)**
Acquisition of investment securities	(29 015 236)	(95 373 380)	(10 146 588)	(21 612 136)
Acquisition of intangible assets and property, plant and equipment	(49 740)	(116 418)	(120 364)	(225 580)
Net cash flows from investing activities	**2 459 550**	**11 465 980**	**950 277**	**9 603 037**

Unconsolidated Financial Statements of Bank Pekao S.A.

(in PLN thousand)

	III QUARTER 2018 PERIOD FROM 01.07.2018 TO 30.09.2018	3 QUARTERS 2018 PERIOD FROM 01.01.2018 TO 30.09.2018	III QUARTER 2017 PERIOD FROM 01.07.2017 TO 30.09.2017	3 QUARTERS 2017 PERIOD FRO7M 01.01.2017 TO 30.09.2017
Cash flows from financing activities				
Financing activity inflows	**585 972**	**1 126 875**	**1 025 000**	**1 025 000**
Issue of debt securities	585 972	1 126 875	1 025 000	1 025 000
Financing activity outflows	**(3 004 387)**	**(3 711 208)**	**(2 334 847)**	**(2 616 269)**
Repayment of loans and advances received from banks	(88 282)	(197 488)	(55 722)	(123 685)
Redemption of debt securities	(842 592)	(1 440 207)	(885)	(214 344)
Dividends and other payments to shareholders	(2 073 513)	(2 073 513)	(2 278 240)	(2 278 240)
Net cash flows from financing activities	**(2 418 415)**	**(2 584 333)**	**(1 309 847)**	**(1 591 269)**
Total net cash flows	**(783 151)**	**2 922 343**	**(1 045 428)**	**(37 077)**
including effect of exchange rate fluctuations on cash and cash equivalents held	(54 623)	71 323	31 922	(94 876)
Net change in cash and cash equivalents	**(783 151)**	**2 922 343**	**(1 045 428)**	**(37 077)**
Cash and cash equivalents at the beginning of the period	**10 999 201**	**7 293 707**	**9 758 362**	**8 750 011**
Cash and cash equivalents at the end of the period	**10 216 050**	**10 216 050**	**8 712 934**	**8 712 934**

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 September 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 third quarter 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	
			30.09.2018	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.. including:	Warsaw	Asset management	100.00	100.00
Pekao TFI S.A.	*Warsaw*	*Asset management*	*100.00*	*100.00*

As at 30 September 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	
			30.09.2018	31.12.2017
CPF Management	Tortola, British Virgin Islands	Financial brokerage – not operating	40.00	40.00

As at 30 September 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.

	3 QUARTERS 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)**

Notes to financial statements (cont.)

(in PLN thousand)

3. Business combinations

In the third quarter 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 September 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 6 November 2018.

Notes to financial statements (cont.)

(in PLN thousand)

5. Significant accounting policies

5.1 Basis of preparation of Consolidated Financial Statements

General information

Condensed Consolidated Interim Financial Statements of Bank Pekao S.A. Group for the period of 9 months ended on 30 September 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 September 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.

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.

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.

Notes to the financial statements (cont.)

(in PLN thousand)

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.

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.

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.

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.

Notes to the financial statements (cont.)

(in PLN thousand)

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.

Notes to the financial statements (cont.)

(in PLN thousand)

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 (SPPI criteria are met).

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.

Notes to the financial statements (cont.)

(in PLN thousand)

- 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.

Notes to the financial statements (cont.)

(in PLN thousand)

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.

Notes to the financial statements (cont.)

(in PLN thousand)

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.

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,
   - bonds convertible to shares - includes the fair value of financial instruments issued as part of transactions settled in equity instruments,
   - 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.

Notes to financial statements (cont.)

(in PLN thousand)

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**
	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**

Notes to financial statements (cont.)

(in PLN thousand)

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 September 2018, the fair value of securities reclassified from measured at fair value through equity to those measured at amortized cost amounted to PLN 2 220 281 thousand. If these securities had not been reclassified, the Group would have recognized in other comprehensive income a net profit of PLN 23 562 thousand in the third quarter 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 9 months 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.

Notes to financial statements (cont.)

(in PLN thousand)

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,
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.

(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 September 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 September 2018

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

RATING CLASS	RANGE OF PD	30.09.2018						
		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%	8 658 272	1 867 857	-	3 414	-	10 529 543	20.4%
2	0.06% <= PD < 0.19%	3 882 404	1 421 131	-	2 699	-	5 306 234	10.6%
3	0.19% <= PD < 0.35%	18 674 902	5 394 613	-	5 214	-	24 074 729	45.1%
4	0.35% <= PD < 0.73%	6 801 791	3 083 676	-	4 605	-	9 890 072	18.2%
5	0.73% <= PD < 3.50%	652 593	1 124 978	-	13 534	-	1 791 105	3.1%
6	3.50% <= PD < 14.00%	137 862	471 695	-	31 593	-	641 150	1.2%
7	14.00% <= PD < 100.00%	17 319	615 909	-	93 534	-	726 762	1.4%
Total		**38 825 143**	**13 979 859**	**-**	**154 593**	**-**	**52 959 595**	**100.0%**

Notes to financial statements (cont.)

(in PLN thousand)

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

RATING CLASS	RANGE OF PD	30.09.2018						
		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%	694 289	123 394	-	258	-	817 941	7.5%
2	0.09% <= PD < 0.18%	1 484 697	172 002	-	555	-	1 657 254	15.0%
3	0.18% <= PD < 0.39%	2 583 720	197 177	-	1 829	-	2 782 726	25.0%
4	0.39% <= PD < 0.90%	2 509 935	133 680	-	3 309	-	2 646 924	23.2%
5	0.90% <= PD < 2.60%	1 644 383	148 299	-	5 337	-	1 798 019	15.5%
6	2.60% <= PD < 9.00%	838 175	143 983	-	8 185	-	990 343	8.5%
7	9.00% <= PD < 30.00%	245 811	132 371	-	13 597	-	391 779	3.4%
8	30.00% <= PD < 100.00%	64 634	129 462	-	30 412	-	224 508	1.9%
Total		**10 065 644**	**1 180 368**	**-**	**63 482**	**-**	**11 309 494**	**100.0%**

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

RATING CLASS	RANGE OF PD	30.09.2018						
		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%	315 577	74 201	-	-	-	389 778	1.7%
2	0.15% <= PD < 0.27%	1 865 126	65 017	-	-	-	1 930 143	9.2%
3	0.27% <= PD < 0.45%	2 887 502	204 872	-	-	-	3 092 374	13.4%
4	0.45% <= PD < 0.75%	4 980 241	204 562	-	-	-	5 184 803	21.1%
5	0.75% <= PD < 1.27%	3 439 468	1 039 147	-	-	-	4 478 615	23.1%
6	1.27% <= PD < 2.25%	3 665 867	442 348	-	-	-	4 108 215	14.7%
7	2.25% <= PD < 4.00%	866 990	402 224	-	4 122	-	1 273 336	5.3%
8	4.00% <= PD < 8.50%	1 057 534	859 591	-	2 381	-	1 919 506	9.7%
9	8.50% <= PD < 100.00%	72 058	181 964	186	24 595	-	278 803	1.8%
Total		**19 150 363**	**3 473 926**	**186**	**31 098**	**-**	**22 655 573**	**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	30.09.2018 CARRYING AMOUNT STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED) INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT	PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	%PORTFOLIO
High	1 425 389	51 131	-	-	-	1 476 520	20.9%
Good	4 228 570	-	-	-	-	4 228 570	67.5%
Satisfactory	464 263	90 670	-	-	-	554 933	11.6%
Low	-	-	-	-	-	-	0.0%
Total	**6 118 222**	**141 801**	**-**	**-**	**-**	**6 260 023**	**100.0%**

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

	30.09.2018
Covered by internal rating model:	86 924 662
Mortgage loans	52 959 595
Consumer loans	11 309 494
Corporate loans	22 655 573
Specialized lending exposures	6 260 023
Other, not covered by internal rating model	27 889 836
Total loans and advances to customers subject to impairment (*)	**121 074 521**

(*) Loans and advances measured at amortized cost and measured at fair value through other comprehensive income.

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

RATING	CARRYING AMOUNT STAGE 1 (12M ECL)	STAGE 2 (LIFETIME ECL - NOT CREDIT-IMPAIRED)	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED) INDIVIDUAL ASSESSMENT	GROUP ASSESSMENT	PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL	%PORTFOLIO
DEBT SECURITIES MEASURED AT AMORTISED COST							
A+ do A-	4 269 391	-	-	-	-	4 269 391	39.9%
BBB+ do BBB-	380 976	-	-	-	-	380 976	3.6%
No rating	6 023 403	-	31 124	-	-	6 054 527	56.5%
Gross carrying amount	**10 673 770**	**-**	**31 124**	**-**	**-**	**10 704 894**	**100.0%**
Impairment allowance	(32 867)	-	(31 124)	-	-	(63 991)	-
Carrying amount	**10 640 903**	**-**	**-**	**-**	**-**	**10 640 903**	**-**
DEBT SECURITIES MEASURED AT FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME							
AAA	907 691	-	-	-	-	907 691	3.2%
A+ to A-	19 623 489	-	-	-	-	19 623 489	69.6%
BBB+ to BBB-	695 917	-	-	-	-	695 917	2.5%
No rating	6 976 876	-	-	-	-	6 976 876	24.7%
Carrying amount	**28 203 973**	**-**	**-**	**-**	**-**	**28 203 973**	**100.0%**
Impairment allowance (*)	(26 416)	**-**	**-**	**-**	**-**	(26 416)	**-**
DEBT SECURITIES HELD FOR TRADING							
A+ to A-						491 629	92.5%
BBB+ to BBB-						2 539	0.5%
No rating						36 992	7.0%
Carrying amount						**531 160**	**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 September 2018

	DERIVATIVES HELD FOR TRANDING			HEDGING DERIVATIVES			TOTAL	%PORTFOLIO
	BANKS	OTHER FINANCIAL INSTITUTIONS	NON-FINANCIAL ENTITIES	BANKS	OTHER FINANCIAL INSTITUTIONS	NON-FINANCIAL ENTITIES		
AAA	166 768	112 810	-	38 890	119 980	-	438 448	34.1%
AA+ do AA-	34 558	-	-	-	-	-	34 558	2.7%
A+ do A-	184 957	185	-	31 057	-	-	216 199	16.8%
BBB+ do BBB-	171 870	8	15 518	14 688	-	-	202 084	15.7%
BB+ do BB-	319	-	-	-	-	-	319	-
B+ do B-	1 301	-	-	-	-	-	1 301	0.1%
No rating	114 451	101 574	158 775	16 524	-	-	391 324	30.6%
Total	**674 224**	**214 577**	**174 293**	**101 159**	**119 980**	**-**	**1 284 233**	**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%**

(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 Group adopts 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.

(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 Group will identify a significant increase in credit risk from the initial recognition are classified in Stage 2. The Group 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, in 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 (e.g. 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.

Notes to the financial statements (cont.)

(in PLN thousand)

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.

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 AND WITH CENTRAL BANK MEASURED AT AMORTISED COST (**)						
GROSS CARRYING AMOUNT						
GROSS CARRYING AMOUNT AS AT 1.01.2018	**5 175 069**	**1 071**	**21 014**	**113**	**-**	**5 197 267**
Transfer to Stage 1	168	(166)	-	(2)	-	-
Transfer to Stage 2	(140)	169	-	(29)	-	-
Transfer to Stage 3	(14)	(50)	-	64	-	-
New/Purchased/Granted financial assets	4 546 664	-	-	-	-	4 546 664
Financial assets derecognised, other than write-offs	(1 712 600)	(344)	-	(36)	-	(1 712 980)
Financial assets written off (*)	-	-	(4 909)	-	-	(4 909)
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	100 734	(12)	(6 880)	(9)	-	93 833
GROSS CARRYING AMOUNT AS AT 30.09.2018	**8 109 881**	**668**	**9 225**	**101**	**-**	**8 119 875**
IMPAIRMENT ALLOWANCE						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**425**	**-**	**21 127**	**-**	**-**	**21 552**
Transfer to Stage 1	-	-	-	-	-	-
Transfer to Stage 2	-	-	-	-	-	-
Transfer to Stage 3	-	-	-	-	-	-
New/Purchased/Granted financial assets	609	-	-	-	-	609
Financial assets derecognised, other than write-offs	(200)	(116)	-	-	-	(316)
Financial assets written off (*)	-	-	(4 909)	-	-	(4 909)
Changes in level of credit risk (excluding the transfers between the Stages)	(351)	2	(12)	-	-	(361)
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	745	114	(6 968)	-	-	(6 109)
IMPAIRMENT ALLOWANCE AS AT 30.09.2018	**1 228**	**-**	**9 238**	**-**	**-**	**10 466**

(*) Including the value of contractual interest subject to partial write-off in the amount of PLN 4 909 thousand.

(**) Receivables from the Central Bank include a current account and deposits

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	2 751 054	(2 743 530)	(620)	(6 904)	-	-
Transfer to Stage 2	(5 658 447)	5 862 082	(6 987)	(196 648)	-	-
Transfer to Stage 3	(578 305)	(523 307)	533 682	567 930	-	-
New/Purchased/Granted financial assets	20 991 861	-	-	-	1 818	20 993 679
Financial assets derecognised, other than write-offs	(11 414 123)	(2 380 768)	(138 529)	(137 892)	(154)	(14 071 466)
Financial assets written off (*)	-	-	(2 706 140)	(1 256 016)	(27)	(3 962 183)
Modifications not resulting in derecognition	-	-	(1 028)	-	1 028	-
Other, in this changes resulting from exchange rates	1 038 725	72 716	632 075	8 590	2 217	1 754 323
GROSS CARRYING AMOUNT AS AT 30.09.2018	**96 865 667**	**21 268 762**	**5 735 500**	**2 306 090**	**87 186**	**126 263 205**
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	82 943	(79 665)	(58)	(3 220)	-	-
Transfer to Stage 2	(21 568)	117 822	(903)	(95 351)	-	-
Transfer to Stage 3	(15 173)	(64 687)	15 990	63 870	-	-
New/Purchased/Granted financial assets	110 082	-	-	-	122	110 204
Financial assets derecognised, other than write-offs	(66 672)	(31 846)	(27 155)	(10)	(2 978)	(128 661)
Financial assets written off (*)	-	-	(2 706 140)	(1 256 016)	(27)	(3 962 183)
Changes in level of credit risk (excluding the transfers between the Stages)	(82 040)	145 954	185 616	174 549	(7 984)	416 095
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	2 788	2 664	637 852	(8 498)	24 522	659 328
IMPAIRMENT ALLOWANCE AS AT 30.09.2018	**363 305**	**738 021**	**3 538 558**	**1 668 861**	**50 812**	**6 359 557**

(*) Including the value of contractual interest subject to partial write-off in the amount of PLN 3 690 102 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	115 788	(114 500)	-	(1 288)	-	-
Transfer to Stage 2	(60 029)	61 582	(842)	(711)	-	-
Transfer to Stage 3	(22 808)	(28 999)	19 743	32 064	-	-
New/Purchased/Granted financial assets	1 551 641	33 545	2 377	2 114	-	1 589 677
Financial assets derecognised, other than write-offs	(1 013 445)	(24 226)	(8 070)	(8 269)	-	(1 054 010)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	10 909	(9 501)	-	(13 547)	-	(12 139)
GROSS CARRYING AMOUNT AS AT 30.09.2018	**4 672 684**	**126 709**	**65 067**	**184 135**	**-**	**5 048 595**
IMPAIRMENT ALLOWANCE						
IMPAIRMENT ALLOWANCE AS AT 1.01.2018	**4 342**	**3 125**	**26 966**	**142 779**	**-**	**177 212**
Transfer to Stage 1	2 493	(1 858)	-	(635)	-	-
Transfer to Stage 2	(157)	267	(60)	(50)	-	-
Transfer to Stage 3	(34)	(420)	335	119	-	-
New/Purchased/Granted financial assets	44	860	3 792	6 144	-	10 840
Financial assets derecognised, other than write-offs	(2 034)	(319)	(768)	(802)	-	(3 923)
Financial assets written off	-	-	-	-	-	-
Changes in level of credit risk (excluding the transfers between the Stages)	-	-	-	-	-	-
Changes in models and risk parameters	5	-	-	3 769	-	3 774
Other, in this changes resulting from exchange rates	(789)	571	(458)	(3 218)	-	(3 894)
IMPAIRMENT ALLOWANCE AS AT 30.09.2018	**3 870**	**2 226**	**29 807**	**148 106**	**-**	**184 009**

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	(432 121)	-	-	-	-	(432 121)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	47 030	-	-	-	-	47 030
CARRYING AMOUNT AS AT 30.09.2018	**1 170 873**	**-**	**-**	**-**	**-**	**1 170 873**
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)	(3 232)	-	-	-	-	(3 232)
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	-	-	-	-	-	-
IMPAIRMENT ALLOWANCE AS AT 30.09.2018	**13 622**	**-**	**-**	**-**	**-**	**13 622**

(*) 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	1 336 829	-	-	-	-	1 336 829
Financial assets derecognised, other than write-offs	(2 278 583)	-	-	-	-	(2 278 583)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	87 720	-	1 093	-	-	88 813
GROSS CARRYING AMOUNT AS AT 30.09.2018	**10 673 770**	**-**	**31 124**	**-**	**-**	**10 704 894**
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	1 948	-	-	-	-	1 948
Financial assets derecognised, other than write-offs	(1 817)	-	-	-	(5 669)	(7 486)
Financial assets written off	-	-	-	-	-	-
Changes in level of credit risk (excluding the transfers between the Stages)	4 951	-	-	-	-	4 951
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	118	-	1 093	-	5 669	6 880
IMPAIRMENT ALLOWANCE AS AT 30.09.2018	**32 867**	**-**	**31 124**	**-**	**-**	**63 991**

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) INDIVIDUAL ASSESSMENT	STAGE 3 (LIFETIME ECL - CREDIT-IMPAIRED) GROUP ASSESSMENT	PURCHASED OR ORIGINATED CREDIT-IMPAIRED (POCI)	TOTAL
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	94 074 437	-	-	-	-	94 074 437
Financial assets derecognised, other than write-offs	(104 433 063)	-	-	-	-	(104 433 063)
Financial assets written off	-	-	-	-	-	-
Modifications not resulting in derecognition	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	530 728	-	-	-	-	530 728
CARRYING AMOUNT AS AT 30.09.2018	**28 203 973**	**-**	**-**	**-**	**-**	**28 203 973**
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	10 477	-	-	-	-	10 477
Financial assets derecognised, other than write-offs	(3 832)	-	-	-	-	(3 832)
Financial assets written off	-	-	-	-	-	-
Changes in level of credit risk (excluding the transfers between the Stages)	(4 566)	-	-	-	-	(4 566)
Changes in models and risk parameters	-	-	-	-	-	-
Other, in this changes resulting from exchange rates	26	-	-	-	-	26
IMPAIRMENT ALLOWANCE AS AT 30.09.2018	**26 416**	**-**	**-**	**-**	**-**	**26 416**

(*) 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.

(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

	30.09.2018						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:	**96 502 362**	**20 530 741**	**2 196 942**	**637 229**	**36 374**	**119 903 648**	**127 949 307**
Forborne exposures gross	480 015	197 307	3 265 947	366 160	23 413	4 332 842	3 987 737
Loss allowance	(6 477)	(20 164)	(1 860 974)	(193 202)	(370)	(2 081 187)	(1 786 125)
Forborne exposures net	473 538	177 143	1 404 973	172 958	23 043	2 251 655	2 201 612
Loans and advances measured at fair value through other comprehensive income, including:	**1 170 873**	**-**	**-**	**-**	**-**	**1 170 873**	**X**
Forborne exposures	-	-	-	-	-	-	X
Loss allowance (*)	-	-	-	-	-	-	X
Loans and advances measured at fair value through profit or loss, including:						**318 464**	**X**
Forborne exposures						1 931	X
Leasing exposure measured at amortised cost, including:	**4 668 814**	**124 483**	**35 260**	**36 029**	**-**	**4 864 586**	**4 351 352**
Forborne exposures gross	3 040	3 146	27 641	5 310	-	39 137	49 104
Loss allowance	(6)	(36)	(6 613)	(3 223)	-	(9 878)	(9 079)
Forborne exposures net	3 034	3 110	21 028	2 087	-	29 259	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.

(in PLN thousand)

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.

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

Structure of CHF loans to individuals

	30.09.2018						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:	**215 091**	**2 922 463**	**71 972**	**135 001**	**734**	**3 345 261**	**3 467 081**
denominated in CHF	215 091	2 906 709	71 972	134 224	734	3 328 730	3 447 189
indexed to CHF	-	15 754	-	777	-	16 531	19 892
Impairment allowances, of which:	**(164)**	**(39 997)**	**(17 350)**	**(65 996)**	**(178)**	**(123 685)**	**(77 018)**
denominated in CHF	(164)	(39 909)	(17 350)	(65 734)	(178)	(123 335)	(76 732)
indexed to CHF	-	(88)	-	(262)	-	(350)	(286)
Carrying amount, of which:	**214 927**	**2 882 467**	**54 622**	**69 005**	**555**	**3 221 576**	**3 390 063**
denominated in CHF	214 927	2 866 801	54 622	68 489	555	3 205 394	3 370 457
indexed to CHF	-	15 666	-	516	-	16 182	19 606

As of 30 September 2018 the average LTV for CHF loans to individuals granted by the Group amounted to 44.9% (46.3% as at 31 December 2017), with an average LTV for the whole portfolio of 62.6% (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.

Notes to financial statements (cont.)

(in PLN thousand)

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.

30.09.2018	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	1 054 826	(763 322)	(169 721)	121 783
Total	**1 054 826**	**(763 322)**	**(169 721)**	**121 783**

30.09.2018	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	2 341 374	(1 419 871)	(817 397)	104 106
Total	**2 341 374**	**(1 419 871)**	**(817 397)**	**104 106**

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**

Notes to financial statements (cont.)

(in PLN thousand)

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.

30.09.2018	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	953 667	Derivative financial instruments (held for trading)	1 063 094	109 427	27
	101 159	Hedging instruments	221 139	119 980	30
Financial liabilities					
Derivatives	1 477 076	Derivative financial instruments (held for trading)	1 781 000	303 924	27
	864 298	Hedging instruments	884 037	19 739	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

(in PLN thousand)

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 September 2018 and in 2017:

	30.09.2018	MINIMUM VALUE	AVERAGE VALUE	MAXIMUM VALUE
foreign currency exchange risk	95	9	169	1 232
interest rate risk	1 477	472	1 061	1 722
Trading portfolio	1 278	526	1 066	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

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 September 2018 and as at 31 December 2017.

SENSITIVITY IN %	30.09.2018	31.12.2017
NII	(8.35)	(8.14)
EVE	0.61	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	30.09.2018	31.12.2017
Currencies total (*)	68	727

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

(in PLN thousand)

Currency position

30.09.2018	BALANCE SHEET OPERATIONS		OFF-BALANCE SHEET OPERATIONS-DERIVATIVES		NET POSITION
	ASSETS	LIABILITIES	LONG POSITION	SHORT POSITION	
EUR	22 592 684	21 525 862	10 002 702	11 049 315	20 209
USD	4 600 420	8 533 400	9 660 664	5 694 638	33 046
CHF	3 581 744	532 146	2 842 942	5 893 970	(1 430)
GBP	242 026	980 576	1 293 990	554 145	1 295
NOK	205 567	39 340	190 443	356 149	521
CZK	62 236	65 730	74 068	70 496	78
SEK	60 880	49 273	86 876	98 923	(440)
Other currencies	115 315	184 601	224 857	153 741	1 830
TOTAL	**31 460 872**	**31 910 928**	**24 376 542**	**23 871 377**	**55 109**

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

30.09.2018	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	35 215 830	8 468 397	23 637 545	56 246 338	59 730 355	183 298 465
Balance sheet liabilities	12 285 154	6 834 089	22 475 290	19 868 557	121 835 375	183 298 465
Off-balance sheet assets/liabilities (net)	(5 450 240)	(488 018)	(1 154 786)	3 384 698	3 040 692	(667 654)
Periodic gap	**17 480 436**	**1 146 290**	**7 469**	**39 762 479**	**(59 064 328)**	**(667 654)**
Cumulated gap	**-**	**18 626 726**	**18 634 195**	**58 396 674**	**(667 654)**	**-**

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

30.09.2018	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 (**)	1 647 411	114 241	420 609	1 738 199	842 611	4 763 071
Amounts due to customers	110 705 793	12 293 966	20 596 975	543 679	28 443	144 168 856
Debt securities issued	193 692	1 532 474	1 416 813	1 500 877	272 850	4 916 706
Subordinated liabilities	20 795	-	20 723	203 715	1 529 812	1 775 045
Financial liabilities held for trading	2 874	-	-	296 626	70 912	370 412
Total	**112 570 565**	**13 940 681**	**22 455 120**	**4 283 096**	**2 744 628**	**155 994 090**
OFF-BALANCE SHEET COMMITMENTS (*)						
Financial liabilities granted	34 580 608	-	-	-	-	34 580 608
Guarantees issued	12 038 797	-	-	-	-	12 038 797
Total	**46 619 405**	**-**	**-**	**-**	**-**	**46 619 405**

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.

(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
30.09.2018	198 311	26 122	251 582	1 017 430	221 065	**1 714 510**
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
30.09.2018						
Inflows	19 838 431	4 487 910	9 583 312	5 190 622	2 205 396	**41 305 671**
Outflows	19 917 531	4 504 831	9 991 379	5 234 796	2 367 397	**42 015 934**
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 September 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

30.09.2018	LEVEL 1	LEVEL 2	LEVEL 3	TOTAL
Assets:	**17 672 762**	**7 545 021**	**6 560 321**	**31 778 104**
Financial assets held for trading	436 102	97 974	6 755	540 831
Derivative financial instruments, including:	1	1 061 612	1 481	1 063 094
- Banks	-	672 743	1 481	674 224
- Customers	1	388 869	-	388 870
Hedging instruments, including:	-	221 139	-	221 139
- Banks	-	101 159	-	101 159
- Customers	-	119 980	-	119 980
Securities measured at fair value through other comprehensive income	17 236 659	6 164 296	5 062 748	28 463 703
Loans and advances to customers measured at fair value through other comprehensive income	-	-	1 170 873	1 170 873
Loans and advances to customers measured at fair value through profit or loss	-	-	318 464	318 464
Liabilities:	**370 412**	**2 665 037**	**-**	**3 035 449**
Financial liabilities held for trading	370 412	-	-	370 412
Derivative financial instruments, including:	-	1 781 000	-	1 781 000
- Banks	-	535 587	-	535 587
- Customers	-	1 245 413	-	1 245 413
Hedging instruments, including:	-	884 037	-	884 037
- Banks	-	864 298	-	864 298
- Customers	-	19 739	-	19 739

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

3 QUARTERS 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:	598 639	263	64 634	5 752	485 494
Reclassification	-	-	-	-	10 160
Transactions made in 2018	-	-	-	209	-
Acquisition	598 355	-	-	-	378 076
Settlement	-	-	-	-	-
Gains on financial instruments	284	263	64 634	5 543	97 258
recognized in the income statement	284	263	24 627	5 543	93 953
recognized in revaluation reserves	-	-	40 007	-	3 305
Decreases, including:	(606 095)	-	(449 725)	(52 425)	(494 801)
Reclassification	(14 211)	-	-	-	(68 220)
Settlement/Redemption	(294)	-	(15 726)	(52 425)	(65 875)
Sale	(591 590)	-	(433 999)	-	(330 332)
Losses on financial instruments	-	-	-	-	(30 374)
recognized in the income statement	-	-	-	-	-
recognized in revaluation reserves	-	-	-	-	(30 374)
Closing balance	**6 755**	**1 481**	**1 170 873**	**318 464**	**5 062 748**
Unrealized income from financial instruments held in portfolio at the end of the period, recognized in:	**8**	**263**	**64 634**	**5 447**	**51 756**
Income statement:	8	263	24 627	5 447	39 197
net interest income	6	-	20 957	1 713	39 197
net impairment losses on financial assets and off-balance sheet commitments	-	-	3 670	-	-
result on financial assets and liabilities held for trading	2	263	-	3 734	-
Other comprehensive income	-	-	40 007	-	12 559

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 September 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 September 2018 and 31 December 2017 is as follows:

FINANCIAL ASSET/LIABILITY	FAIR VALUE AS AT 30.09.2018	VALUATION TECHNIQUE	UNOBSERVABLE FACTOR	ALTERNATIVE FACTOR RANGE (WEIGHTED AVERAGE)	IMPACT ON FAIR VALUE AS AT 30.09.2018	
					POSITIVE SCENARIO	NEGATIVE SCENARIO
Corporate and municipal debt securities	4 871 638	Discounted cash flow	Credit spread	0.67% - 1.23%	58 774	(58 774)
Derivatives	1 481	Black Scholes Model	Correlation	0-1	662	(329)
Loans and advances measured at fair value through profit or loss	318 464	Discounted cash flow	Credit spread	0.57% – 1.13%	2 411	(2 378)
Loans and advances measured at fair value through other comprehensive income	1 170 873	Discounted cash flow	Credit spread	1.86% – 2.42%	4 317	(4 888)

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 September 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

30.09.2018	CARRYING AMOUNT	FAIR VALUE	OF WHICH:		
			LEVEL 1	LEVEL 2	LEVEL 3
Assets					
Cash and due from Central Bank	5 720 292	5 719 549	2 373 093	3 346 456	-
Loans and advance to banks	4 762 209	4 764 126	-	3 661 325	1 102 801
Loans and advances to customers measured at amortised cost	119 903 648	120 651 222	-	-	120 651 222
Receivables from financial leases	4 864 586	4 952 519	-	-	4 952 519
Debt securities measured at amortised cost	10 640 903	10 666 070	4 080 012	1 292 853	5 293 205
Total Assets	**145 891 638**	**146 753 486**	**6 453 105**	**8 300 634**	**131 999 747**
Liabilities					
Amounts due to Central Bank	5 045	5 049	-	-	5 049
Amounts due to other banks	4 689 311	4 649 054	-	744 175	3 904 879
Amounts due to customers	143 767 613	143 970 647	-	912 953	143 057 694
Debt securities issued	4 742 615	4 752 366	-	4 752 366	-
Subordinated liabilities	1 267 400	1 267 545	-	1 267 545	-
Total Liabilities	**154 471 984**	**154 644 661**	**-**	**7 677 039**	**146 967 622**

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 September 2018

	RETAIL BANKING	PRIVATE BANKING	CORPORATE AND INVESTMENT BANKING	SME BANKING	ASSETS AND LIABILITIES MANAGEMENT AND OTHER	TOTAL
Total net interest income	**2 015 992**	**28 414**	**994 449**	**133 202**	**547 184**	**3 719 241**
Non-interest income	**1 051 925**	**36 457**	**685 076**	**189 099**	**31 718**	**1 994 275**
Operating income	**3 067 917**	**64 871**	**1 679 525**	**322 301**	**578 902**	**5 713 516**
Personnel expenses	(867 671)	(27 894)	(201 437)	(64 846)	(383 851)	(1 545 699)
Other administrative expenses	(823 085)	(23 730)	(281 151)	(158 938)	506 277	(780 627)
Depreciation and amortisation	(107 967)	(1 701)	(18 751)	(15 028)	(126 898)	(270 345)
Operating costs	**(1 798 723)**	**(53 325)**	**(501 339)**	**(238 812)**	**(4 472)**	**(2 596 671)**
Gross operating profit	**1 269 194**	**11 546**	**1 178 186**	**83 489**	**574 430**	**3 116 845**
Net impairment losses on financial assets and off-balance sheet commitments	(226 498)	350	(142 605)	(21 600)	(15 817)	(406 170)
Net operating profit	**1 042 696**	**11 896**	**1 035 581**	**61 889**	**558 613**	**2 710 675**
Net result on other provisions	341	(2 412)	(767)	-	(11 526)	(14 364)
Guarantee funds charges	(126 599)	(437)	(114 460)	(6 369)	13 057	(234 808)
Tax on certain financial institutions	-	-	-	-	(417 828)	(417 828)
Net result on investment activities	198	6	66	-	26 633	26 903
Profit before tax	**916 636**	**9 053**	**920 420**	**55 520**	**168 949**	**2 070 578**
Income tax expense						(531 967)
Net profit for the period						**1 538 611**
Attributable to equity holders of the Bank						**1 537 933**
Attributable to non-controling interests						678
Allocated assets	73 363 425	312 591	100 539 772	3 429 148	(3 204 690)	174 440 246
Unallocated assets						8 858 218
Total assets						**183 298 464**
Allocated liabilities	82 034 559	8 979 930	57 403 761	10 746 855	(3 107 035)	156 058 070
Unallocated liabilities						27 240 394
Total liabilities						**183 298 464**

Notes to financial statements (cont.)

(in PLN thousand)

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

	RETAIL BANKING	PRIVATE BANKING	CORPORATE AND INVESTMENT BANKING	SME BANKING	ASSETS AND LIABILITIES MANAGEMENT AND OTHER	TOTAL
Total net interest income	**1 783 716**	**30 886**	**1 005 789**	**118 183**	**516 056**	**3 454 630**
Non-interest income	**955 174**	**19 423**	**601 721**	**166 758**	**130 319**	**1 873 395**
Operating income	**2 738 890**	**50 309**	**1 607 510**	**284 941**	**646 375**	**5 328 025**
Personnel expenses	(776 264)	(18 385)	(197 778)	(59 073)	(394 002)	(1 445 502)
Other administrative expenses	(789 036)	(19 405)	(254 143)	(160 550)	513 412	(709 722)
Depreciation and amortisation	(105 825)	(1 013)	(16 695)	(14 983)	(115 121)	(253 637)
Operating costs	**(1 671 125)**	**(38 803)**	**(468 616)**	**(234 606)**	**4 289**	**(2 408 861)**
Gross operating profit	**1 067 765**	**11 506**	**1 138 894**	**50 335**	**650 664**	**2 919 164**
Net impairment losses on financial assets and off-balance sheet commitments	(152 239)	(543)	(188 274)	(32 170)	4 772	(368 454)
Net operating profit	**915 526**	**10 963**	**950 620**	**18 165**	**655 436**	**2 550 710**
Net result on other provisions	(2 645)	-	154	-	(19 479)	(21 970)
Guarantee funds charges	(115 528)	(476)	(89 986)	(5 579)	(34 807)	(246 376)
Tax on certain financial institutions	-	-	-	-	(383 480)	(383 480)
Net result on investment activities	(258)	-	302	-	298	342
Profit before tax	**797 095**	**10 487**	**861 090**	**12 586**	**217 968**	**1 899 226**
Income tax expense						(477 649)
Net profit for the period						**1 421 577**
Attributable to equity holders of the Bank						**1 420 998**
Attributable to non-controling interests						579
Allocated assets	66 078 172	256 278	96 354 489	3 168 478	(2 571 343)	163 286 074
Unallocated assets						8 176 783
Total assets						**171 462 857**
Allocated liabilities	74 159 217	8 615 822	57 426 918	9 758 451	(5 592 012)	144 368 396
Unallocated liabilities						27 094 461
Total liabilities						**171 462 857**

Reconciliations of operating income for reportable segments

	3 QUARTERS 2018	3 QUARTERS 2017
Total operating income for reportable segments	**5 713 516**	**5 328 025**
Share in gains (losses) from associates	-	(31 659)
Net other operating income and expenses	(39 294)	(87 522)
Refunding of administrative expenses	-	1 888
Operating income	**5 674 222**	**5 210 732**

Geographical segment

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

(in PLN thousand)

9. Interest income and expense

Interest income

	III QUARTER 2018				III QUARTER 2017
	FINANCIAL ASSETS MEASURED AT AMORTISED COST	FINANCIAL ASSETS DESIGNATED 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	1 236 583	5 669	1 834	1 244 086	1 197 761
Interbank placements	14 888	-	-	14 888	20 969
Reverse repo transactions	7 547	-	-	7 547	6 098
Investment securities	71 552	160 779	-	232 331	158 872
Hedging derivatives	-	-	42 713	42 713	28 628
Financial assets held for trading	-	-	2 502	2 502	1 719
Total	**1 330 570**	**166 448**	**47 049**	**1 544 067**	**1 414 047**

	3 QUARTERS 2018				3 QUARTERS 2017
	FINANCIAL ASSETS MEASURED AT AMORTISED COST	FINANCIAL ASSETS DESIGNATED 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	3 610 138	19 038	5 780	3 634 956	3 481 347
Interbank placements	37 768	-	-	37 768	60 495
Reverse repo transactions	19 623	-	-	19 623	24 813
Investment securities	222 404	512 584	-	734 988	507 501
Hedging derivatives	-	-	103 923	103 923	95 671
Financial assets held for trading	-	-	7 283	7 283	11 753
Total	**3 889 933**	**531 622**	**116 986**	**4 538 541**	**4 181 580**

Interest expense

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Deposits from customers	(236 402)	(702 650)	(233 382)	(685 857)
Interbank deposits	(3 659)	(11 448)	(3 672)	(12 896)
Repo transactions	(9 183)	(27 002)	(10 986)	(44 786)
Loans and advances received	(2 531)	(7 077)	(2 057)	(6 620)
Debt securities	(34 303)	(91 148)	(11 829)	(28 091)
Total	**(286 078)**	**(839 325)**	**(261 926)**	**(778 250)**

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

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Accounts maintenance, payment orders and cash transactions	158 612	464 452	148 764	449 483
Payment cards	152 253	433 252	153 748	436 103
Loans and advances	100 749	282 304	98 757	311 345
Margin on foreign exchange transactions with clients	115 144	339 334	114 439	330 469
Investment products sales intermediation	123 584	381 504	64 997	196 487
Securities operations	15 649	56 351	24 077	69 921
Custody activity	14 797	42 929	19 434	52 727
Pension and investment funds service fees	9 632	25 429	12 700	37 982
Guarantees, letters of credit and similar transactions	17 291	45 346	13 829	40 026
Other	6 971	26 276	8 168	35 448
Total	**714 682**	**2 097 177**	**658 913**	**1 959 991**

Fee and commission expense

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Payment cards	(66 869)	(188 589)	(59 835)	(165 549)
Money orders and transfers	(5 747)	(16 075)	(4 812)	(15 280)
Securities and derivatives operations	(8 548)	(22 284)	(7 341)	(22 021)
Acquisition services	(8 054)	(26 217)	(1 271)	(3 542)
Custody activity	(3 833)	(11 946)	(3 568)	(10 924)
Accounts maintenance	(1 256)	(3 296)	(1 109)	(3 648)
Pension and investment funds management charges	(34)	(1 253)	(79)	(754)
Other	(1 354)	(3 203)	(814)	(2 421)
Total	**(95 695)**	**(272 863)**	**(78 829)**	**(224 139)**

11. Dividend income

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Issuers of securities held for trading	X	X	48	64
Issuers of securities available for sale	X	X	175	19 577
Issuers of securities measured at fair value through profit or loss	220	384	X	X
Issuers of equity instruments designated at fair value through other comprehensive income	25	19 641	X	X
Total	**245**	**20 025**	**223**	**19 641**

Notes to financial statements (cont.)

(in PLN thousand)

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

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Gains (losses) on loans and advances to customers measured mandatorily at fair value through profit or loss	422	(3 793)	X	X
Gains (losses) on securities measured mandatorily at fair value through profit or loss	8 540	17 025	X	X
Foreign currency exchange result	6 942	(8 506)	(9 642)	(32 923)
Gains (losses) on derivatives	7 964	43 576	14 877	37 531
Gains (losses) on securities	2 639	13 869	6 011	15 511
Total	**26 507**	**62 171**	**11 246**	**20 119**

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

Realized gains

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Financial assets measured at amortised cost	362	534	X	X
Financial assets measured at fair value through other comprehensive income	13 921	64 869	X	X
Financial liabilities not measured at fair value through profit and loss	1	1	X	X
Total	**14 284**	**65 404**	**X**	**X**

Realized losses

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Financial liabilities not measured at fair value through profit and loss	(23)	(66)	X	X
Total	**(23)**	**(66)**	**X**	**X**

NET REALIZED PROFIT	**14 261**	**65 338**	**X**	**X**

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

Realized gains

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Loans and other financial receivables	X	X	2 178	2 271
Available for sale financial assets - debt instruments	X	X	19 841	25 594
Held to maturity investments	X	X	-	176
Total	**X**	**X**	**22 019**	**28 041**

Realized losses

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Loans and other financial receivables	X	X	(65)	(65)
Debt securities issued	X	X	(72)	(152)
Total	**X**	**X**	**(137)**	**(217)**

NET REALIZED PROFIT	**X**	**X**	**21 882**	**27 824**

(in PLN thousand)

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

	III QUARTER 2018	3 QUARTERS 2018
Loans and other financial assets measured at amortized cost (*)	(144 798)	(404 487)
Debt securities measured at amortized cost	1 122	586
Loans measured at fair value through other comprehensive income	212	4 538
Debt securities measured at fair value through other comprehensive income	3 255	(2 079)
Off-balance sheet commitments	(15 068)	(4 728)
Total financial assets and off-balance sheet commitments	**(155 277)**	**(406 170)**

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

	III QUARTER 2017	3 QUARTERS 2017
Debt securities measured at fair value through other comprehensive income	(99)	(99)
Loans and advances to banks measured at amortized cost	177	155
Loans and advances to customers measured at amortized cost	(127 974)	(361 733)
Receivables from financial leases	(1 303)	(4 246)
Off-balance sheet commitments	(9 380)	(2 630)
Total financial assets and off-balance sheet commitments	**(138 579)**	**(368 553)**

16. Administrative expenses

Personnel expenses

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Wages and salaries	(412 591)	(1 296 849)	(417 100)	(1 214 392)
Insurance and other charges related to employees	(76 623)	(232 623)	(71 952)	(217 264)
Share-based payments expenses	(1 312)	(16 227)	(4 132)	(13 846)
Total	**(490 526)**	**(1 545 699)**	**(493 184)**	**(1 445 502)**

Other administrative expenses

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
General expenses	(244 594)	(731 465)	(228 207)	(668 480)
Taxes and charges	(9 666)	(30 067)	(9 755)	(31 933)
Bank Guarantee Fund fee	(30 512)	(235 537)	(22 491)	(245 208)
Financial supervision authority fee (KNF)	(5 837)	(18 366)	(544)	(12 365)
Tax on certain financial institutions	(140 934)	(417 828)	(130 795)	(383 480)
Total	**(431 543)**	**(1 433 263)**	**(391 792)**	**(1 341 466)**

Total administrative expenses	**(922 069)**	**(2 978 962)**	**(884 976)**	**(2 786 968)**

(in PLN thousand)

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 91 201 thousand (PLN 66 819 thousand for the three quarters 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 three quarters of 2018.

17. Depreciation and amortization

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Property, plant and equipment	(43 274)	(128 822)	(42 986)	(128 338)
Investment property	(73)	(468)	(232)	(700)
Intangible assets	(49 325)	(141 055)	(40 852)	(124 599)
Total	**(92 672)**	**(270 345)**	**(84 070)**	**(253 637)**

Notes to financial statements (cont.)

(in PLN thousand)

18. Net other operating income and expenses

Other operating income

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Rental income	5 344	16 565	5 189	15 418
Miscellaneous income	1 426	7 009	4 251	9 611
Recovery of debt collection costs	2 792	9 175	3 638	10 349
Revenues from sale of products, goods and services	20 786	73 944	20 131	59 949
Excess payments, repayments	213	1 378	263	1 393
Compensation, recoveries, penalty fees and fines received	5 594	17 916	31 482	70 191
Revenues from leasing activity	2 283	3 139	809	2 883
Refunding of administrative expenses	-	-	637	1 888
Income from written off liabilities	6	35	59	72
Releases of impairment allowances for litigation and other assets	177	649	150	561
Gains on sale of leasing assets for third person and other assets	179	319	278	576
Other	664	2 456	933	3 423
Total	**39 464**	**132 585**	**67 820**	**176 314**

Other operating expenses

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Costs related to leasing activity	(97)	(720)	(426)	(1 566)
Credit insurance expenses	(844)	(3 104)	(1 540)	(6 187)
Sundry expenses	(434)	(3 008)	(3 110)	(7 254)
Reimbursement and deficiencies	(197)	(1 324)	(189)	(2 751)
Costs from sale of products, goods and services	(20 138)	(71 294)	(18 736)	(55 870)
Customers complaints expenses	(190)	(566)	(248)	(811)
Impairment allowance for litigations and other assets	96	(804)	(591)	(1 997)
Costs of litigation and claims	(296)	(1 166)	(140)	(1 675)
Compensation, penalty fees and fines paid	(83)	(600)	(315)	(533)
Losses on disposal of leasing assets for third person and other assets	(139)	(399)	(33)	(593)
Other	(3 568)	(10 306)	(2 862)	(9 555)
Total	**(25 890)**	**(93 291)**	**(28 190)**	**(88 792)**

NET OTHER OPERATING INCOME AND EXPENSES	**13 574**	**39 294**	**39 630**	**87 522**

Notes to financial statements (cont.)

(in PLN thousand)

19. Gains (losses) on subsidiaries and associates

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Share in gains (losses) from associates				
Dom Inwestycyjny Xelion Sp. z o.o.	-	-	643	2 083
Pekao Investment Management S.A.	-	-	10 462	29 576
Total share in gains (losses) from associates	**-**	**-**	**11 105**	**31 659**
Total gains (losses) from subsidiaries and associates	**-**	**-**	**11 105**	**31 659**

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

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Gains (losses) on disposal of property, plant and equipment classified as assets held for sale	30 408	34 228	663	1 383
Gains (losses) on de-recognition of property, plant and equipment and intangible assets other than classified as assets held for sale	435	(7 325)	(288)	(942)
Total gains (losses) on disposal of property, plant and equipment and intangible assets	**30 843**	**26 903**	**375**	**441**

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

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
INCOME STATEMENT				
Current tax	**(265 423)**	**(656 504)**	**(175 478)**	**(449 962)**
Current tax charge in the income statement	(265 415)	(656 918)	(175 434)	(452 978)
Adjustments related to the current tax from previous years	46	647	-	3 298
Other taxes (e.g. withholding tax)	(54)	(233)	(44)	(282)
Deferred tax	**78 482**	**124 537**	**10 072**	**(27 687)**
Occurrence and reversal of temporary differences	78 482	124 537	10 072	(27 687)
Tax charge in the consolidated income statement	**(186 941)**	**(531 967)**	**(165 406)**	**(477 649)**
EQUITY				
Deferred tax	**13 475**	**10 049**	**(5 373)**	**(49 997)**
Income and costs disclosed in other comprehensive income:				
revaluation of financial instruments - cash flows hedges	5 503	9 465	(4 805)	1 294
revaluation of available for sale financial assets – debt securities	X	X	734	(39 796)
fair value revaluation through other comprehensive income	8 251	(2 818)	X	X
fair value revaluation through other comprehensive income – equity securities	(279)	3 402	(1 302)	(11 495)
Tax on items that are or may be reclassified subsequently to profit or loss	**13 475**	**10 049**	**(5 373)**	**(49 997)**
TOTAL CHARGE	**(173 466)**	**(521 918)**	**(170 779)**	**(527 646)**

(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.

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Net profit	605 793	1 537 933	536 220	1 420 998
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)	2.31	5.86	2.04	5.41

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 September 2018 there were no diluting instruments in the form of convertible bonds in the Group.

	III QUARTER 2018	3 QUARTERS 2018	III QUARTER 2017	3 QUARTERS 2017
Net profit	605 793	1 537 933	536 220	1 420 998
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)	2.31	5.86	2.04	5.41

23. Dividends

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.

(in PLN thousand)

24. Cash and balances with Central Bank

CASH AND DUE FROM CENTRAL BANK	30.09.2018	31.12.2017
Cash	2 373 081	2 686 571
Current account at Central Bank	2 506 076	2 264 688
Other	841 371	285 059
Gross carrying amount	**5 720 528**	**5 236 318**
Impairment allowances	(236)	-
Net carrying amount	**5 720 292**	**5 236 318**

AMOUNTS DUE TO CENTRAL BANK	30.09.2018	31.12.2017
Term deposits	5 045	6 079
Amounts due to Central Bank	**5 045**	**6 079**

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

Cash and balances with Central Bank by currency

30.09.2018	ASSETS	LIABILITIES
PLN	4 974 327	5 045
EUR	311 029	-
USD	225 605	-
CHF	50 532	-
Other currencies	158 799	-
Total	**5 720 292**	**5 045**

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**

(in PLN thousand)

25. Loans and advances to banks

Loans and advances to banks by product type

	30.09.2018	31.12.2017
Current accounts	260 447	335 016
Interbank placements	2 886 615	271 823
Loans and advances	21 376	29 528
Cash collaterals	898 714	1 006 332
Reverse repo transactions	513 569	494 706
Cash in transit	191 718	506 559
Total gross amount	**4 772 439**	**2 643 964**
Impairment allowances	(10 230)	(16 637)
Total net amount	**4 762 209**	**2 627 327**

Loans and advances to banks are measured at amortised cost.

Loans and advances to banks by contractual maturity

	30.09.2018	31.12.2017
Loans and advances to banks, including:		
up to 1 month	4 620 192	2 588 346
between 1 and 3 months	116 657	31 579
between 3 months and 1 year	20 190	7
between 1 and 5 years	160	29
over 5 years	51	50
past due	15 189	23 953
Total gross amount	**4 772 439**	**2 643 964**
Impairment allowances	(10 230)	(16 637)
Total net amount	**4 762 209**	**2 627 327**

Loans and advances to banks by currency

	30.09.2018	31.12.2017
PLN	1 290 857	702 126
CHF	152 618	23 342
EUR	3 075 999	1 346 256
USD	76 613	209 142
Other currencies	166 122	346 461
Total	**4 762 209**	**2 627 327**

Notes to financial statements (cont.)

(in PLN thousand)

26. Financial assets and liabilities held for trading

Financial assets and liabilities held for trading by product type

	30.09.2018	31.12.2017
FINANCIAL ASSETS		
Debt securities	531 160	1 725 858
Equity securities	9 671	4 558
Total financial assets	**540 831**	**1 730 416**
FINANCIAL LIABILITIES		
Debt securities	370 412	469 448
Total financial liabilities	**370 412**	**469 448**

Financial assets and liabilities held for trading are measured at fair value through profit or loss.

Debt securities held for trading

	30.09.2018	31.12.2017
FINANCIAL ASSETS		
Debt securities issued by State Treasury	436 137	1 646 758
T- bills	-	-
T- bonds	436 137	1 646 758
Debt securities issued by banks	22 584	50 258
Debt securities issued by business entities	72 439	28 842
Total financial assets	**531 160**	**1 725 858**
FINANCIAL LIABILITIES		
Debt securities issued by State Treasury	370 412	469 448
T- bonds	370 412	469 448
Total financial liabilities	**370 412**	**469 448**

Notes to financial statements (cont.)

(in PLN thousand)

Equity securities held for trading

	30.09.2018	31.12.2017
Shares	4 645	208
Participation units	5 026	4 350
Total	**9 671**	**4 558**

Debt securities held for trading by maturity

	30.09.2018	31.12.2017
FINANCIAL ASSETS		
Debt securities, including:		
up to 1 month	1 230	123 505
between 1 and 3 months	1	-
between 3 months and 1 year	42 889	12 605
between 1 and 5 years	472 084	1 461 523
over 5 years	14 956	128 225
unspecified term	-	-
Total financial assets	**531 160**	**1 725 858**
FINANCIAL LIABILITIES		
Debt securities, including:		
up to 1 month	2 874	-
between 1 and 3 months	-	-
between 3 months and 1 year	-	-
between 1 and 5 years	296 626	309 328
over 5 years	70 912	160 120
Total financial liabilities	**370 412**	**469 448**

Debt securities held for trading by currency

	30.09.2018	31.12.2017
FINANCIAL ASSETS		
PLN	521 558	1 718 202
EUR	4 102	4 542
USD	5 500	3 114
Total financial assets	**531 160**	**1 725 858**
FINANCIAL LIABILITIES		
PLN	370 412	469 448
Total financial liabilities	**370 412**	**469 448**

(in PLN thousand)

27. Derivative financial instruments (held for trading)

Fair value of trading derivatives

30.09.2018	ASSETS	LIABILITIES
Interest rate transactions		
Interest Rate Swaps (IRS)	796 135	1 450 073
Forward Rate Agreements (FRA)	1 104	204
Options	6 419	3 119
Other	440	217
Foreign currency and gold transactions		
Cross-Currency Interest Rate Swaps (CIRS)	32 941	15 642
Currency Forward Agreements	60 968	137 358
Currency Swaps (FX-Swap)	48 908	64 363
Options for currency and gold	46 044	42 916
Transactions based on equity securities and stock indexes		
Options	4 001	3 980
Other	1	-
Transactions based on commodities and precious metals		
Options	37 480	35 086
Other	28 653	28 042
Total	**1 063 094**	**1 781 000**

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.

(in PLN thousand)

28. Loans and advances to customers

Loans and advances to customers by product type

	30.09.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
Mortgage loans	62 860 117	1 170 873	29 269	64 060 259	59 729 689
Current accounts	12 640 975	-	-	12 640 975	11 028 956
Operating loans	12 807 256	-	29 101	12 836 357	12 916 798
Investment loans	18 560 399	-	106 368	18 666 767	18 665 906
Cash loans	13 237 167	-	-	13 237 167	12 190 872
Payment cards receivables	1 133 708	-	-	1 133 708	1 081 499
Factoring	3 664 267	-	-	3 664 267	3 478 545
Other loans and advances	1 317 366	-	153 726	1 471 092	1 386 808
Debt securities	-	-	-	-	12 749 288
Reverse repo transactions	-	-	-	-	-
Cash in transit	41 950	-	-	41 950	79 144
Gross carrying amount	**126 263 205**	**1 170 873**	**318 464**	**127 752 542**	**133 307 505**
Impairment allowances (*)	(6 359 557)	-	-	(6 359 557)	(5 358 198)
Carrying amount	**119 903 648**	**1 170 873**	**318 464**	**121 392 985**	**127 949 307**

(*) The impairment allowance for loans and advances to customers measured at fair value through equity in the amount of PLN 13 622 thousand is included in the ‘Revaluation reserve’ item and does not reduce the carrying amount of the loan.

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.

Notes to financial statements (cont.)

(in PLN thousand)

Loans and advances to customers by customer type

	30.09.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
Corporate	52 391 858	1 170 873	61 316	53 624 047	58 841 495
Individuals	69 676 702	-	153 726	69 830 428	64 377 510
Budget entities	4 194 645	-	103 422	4 298 067	10 088 500
Gross carrying amount	**126 263 205**	**1 170 873**	**318 464**	**127 752 542**	**133 307 505**
Impairment allowances (*)	(6 359 557)	-	-	(6 359 557)	(5 358 198)
Carrying amount	**119 903 648**	**1 170 873**	**318 464**	**121 392 985**	**127 949 307**

(*) The impairment allowance for loans and advances to customers measured at fair value through equity in the amount of PLN 13 622 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

	30.09.2018				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	15 208 894	-	2 415	15 211 309	14 966 833
between 1 and 3 months	4 179 673	-	5 934	4 185 607	4 657 178
between 3 months and 1 year	11 443 160	121 394	52 670	11 617 224	10 286 555
between 1 and 5 years	37 338 796	425 933	191 919	37 956 648	41 942 265
over 5 years	52 540 223	623 546	62 241	53 226 010	55 962 982
past due	5 552 459	-	3 285	5 555 744	5 491 692
Gross carrying amount	**126 263 205**	**1 170 873**	**318 464**	**127 752 542**	**133 307 505**
Impairment allowances (*)	(6 359 557)	-	-	(6 359 557)	(5 358 198)
Carrying amount	**119 903 648**	**1 170 873**	**318 464**	**121 392 985**	**127 949 307**

(*) The impairment allowance for loans and advances to customers measured at fair value through equity in the amount of PLN 13 622 thousand is included in the 'Revaluation reserve' item and does not reduce the carrying amount of the loan.

Loans and advances to customers by currency

	30.09.2018				31.12.2017
	AMORTISED COST	FAIR VALUE THROUGH OTHER COMPREHENSIVE INCOME	FAIR VALUE THROUGH PROFIT OR LOSS	TOTAL	TOTAL
PLN	101 337 488	49 051	318 464	101 705 003	107 990 654
CHF	3 376 043	-	-	3 376 043	3 561 945
EUR	12 916 949	1 121 822	-	14 038 771	13 688 524
USD	1 918 985	-	-	1 918 985	2 477 434
Other currencies	354 183	-	-	354 183	230 750
Carrying amount	**119 903 648**	**1 170 873**	**318 464**	**121 392 985**	**127 949 307**

(in PLN thousand)

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:

30.09.2018	GROSS LEASING INVESTMENT	PRESENT VALUE OF MINIMUM LEASE PAYMENTS
Up to 1 year	1 971 863	1 823 429
Between 1 and 5 years	3 078 820	2 900 993
Over 5 years	344 518	324 173
Total	**5 395 201**	**5 048 595**
Unearned finance income	(346 606)	
Net leasing investment	**5 048 595**	
Unguaranteed residual values accruing to the benefit of the lessor	-	
Present value of minimum lease payments	5 048 595	
Impairment allowances	(184 009)	
Carrying amount	**4 864 586**	

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)	
Carrying amount	**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.

Receivables from financial leases by currency

	30.09.2018	31.12.2017
PLN	3 134 165	2 747 448
CHF	239	467
EUR	1 715 464	1 588 474
USD	14 718	14 963
Total	**4 864 586**	**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 September 2018 the Group applies fair value hedge accounting and cash flow hedge accounting:

- fair value hedge accounting
  - Interest rate swaps (IRS) designated to hedge debt securities denominated in PLN, EUR and USD (**FVH IRS bonds**);
- cash flow hedge accounting
  - Interest rate swaps (IRS) designated to hedge floating rate loans and securities denominated in PLN (**CFH IRS loans/bonds**);
  - Interest rate swaps (IRS) designated to hedge deposits denominated in PLN and EUR, which economically reflect long-term variable-rate liability (**CFH IRS deposits**);
  - cross-currency interest rate swaps (CIRS basis swap) designated to hedge floating rate loans denominated in CHF and liabilities denominated in PLN, which economically reflect long-term variable-rate liability (**CFH CIRS deposits/loans**);
  - FX-Swaps designated to hedge floating rate loans denominated in EUR (**CFH FX-Swap loans**).

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). In the past, hedged risk component accounted for a significant portion of changes in fair value of the hedged item.

Risk management strategy regarding fair value hedge relationships, hedge accounting system and main sources of hedge ineffectiveness were described in the financial statement as of 30 June 2018 and have not changed substantially since then.

The Group's approach to market risk management, including interest rate risk, and details regarding exposure of the Group to interest rate risk is presented in the Note 7.2.

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 September 2018 and 31 December 2017.

Notes to financial statements (cont.)

(in PLN thousand)

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

30.09.2018	FVH IRS BONDS – IRS HEDGING DEBT SECURITIES MEASURED AT: AMORTISED COST	FVH IRS BONDS – IRS HEDGING DEBT SECURITIES MEASURED AT: FAIR VALUE THROUGH OTHER CMPREHENSIVE INCOME	TOTAL
HEDGING INSTRUMENTS			
Nominal value	200 000	3 275 926	3 475 926
Carrying amount – assets	-	41 116	41 116
Carrying amount – liabilities	2 956	131 320	134 276
Amount of hedge ineffectiveness recognized in the income statement item: 'Result on fair value hedge accounting'	490	2 668	3 158
HEDGED ITEM			
Carrying amount – assets	203 495	3 482 279	3 685 774
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	1 801	150 693	152 494
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	-	-	-

31.12.2017	FVH IRS BONDS – IRS HEDGING DEBT SECURITIES MEASURED AT: AMORTISED COST	FVH IRS BONDS – IRS HEDGING DEBT SECURITIES MEASURED AT: FAIR VALUE THROUGH OTHER CMPREHENSIVE INCOME	TOTAL
HEDGING INSTRUMENTS			
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
Amount of hedge ineffectiveness recognized in the income statement item: 'Result on fair value hedge accounting'	20	4 596	4 616
HEDGED ITEM			
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
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)

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 and securities 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.

The Group's risk management strategy regarding cash flow hedge relationships, hedge accounting system and main sources of hedge ineffectiveness were described in the financial statement as of 30 June 2018 and have not changed substantially since then.

Impact of cash flow hedge on balance sheet and financial result

30.09.2018	RISK	INTEREST RATE		INTEREST RATE/CURRENCY	
	RELATIONSHIP	CFH IRS LOANS/BONDS	CFH IRS DEPOSITS	RELATIONSHIP	CFH IRS LOANS/BONDS
HEDGING INSTRUMENTS					
Nominal value		7 600 000	729 466	12 192 848	5 532 176
Carrying amount – assets		129 428	768	-	49 827
Carrying amount – liabilities		14 951	1 864	732 946	-
Amount of hedge ineffectiveness recognized in the income statement item 'Result on financial assets and liabilities measured at fair value through profit or loss'		(75)	(13)	8	4
HEDGED ITEMS					
Revaluation reserve due to cash flow hedge accounting for relationships for which hedge accounting will be continued after the end of the reporting period		45 894	753	(89 212)	(668)
Revaluation reserve due to cash flow hedge accounting for relationships for which hedge accounting is no longer applied		-	-	-	-

31.12.2017	RISK	INTEREST RATE		INTEREST RATE/CURRENCY	
	RELATIONSHIP	CFH IRS LOANS/BONDS	CFH IRS DEPOSITS	RELATIONSHIP	CFH IRS LOANS/BONDS
HEDGING INSTRUMENTS					
Nominal value		3 600 000	575 702	12 908 890	2 009 225
Carrying amount – assets		199 832	839	-	42 229
Carrying amount – liabilities		-	1 700	674 529	-
Amount of hedge ineffectiveness recognized in the income statement item 'Result on financial assets and liabilities measured at fair value through profit or loss'		-	-	-	-
HEDGED ITEMS					
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)
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

	3 QUARTERS 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	(55 996)	(58 480)
Part of the loss transferred to the income statement due to the lack of expectation of materialization of the hedged item	-	(56)
INTEREST RATE RISK/CURRENCY RISK		
Gains or losses resulting from hedging, recognized in other comprehensive income during the reporting period	6 182	25 393
Part of the loss transferred to the income statement due to the lack of expectation of materialization of the hedged item	-	-
Closing balance	**(43 233)**	**6 581**

31. Investment (placement) securities

	30.09.2018	31.12.2017
Debt securities measured at amortised cost	10 640 903	X
Debt securities measured at fair value through other comprehensive income	28 203 973	X
Equity instruments designated at fair value through other comprehensive income	259 730	X
Equity instruments mandatorily measured at fair value through profit or loss	72 737	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	**39 177 343**	**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.

Debt securities measured at amortised cost

	30.09.2018	31.12.2017
Securities issued by State Treasury	4 143 813	X
T-bills	-	X
T-bonds	4 143 813	X
Securities issued by Central Banks	-	X
Securities issued by business entities	3 873 076	X
Securities issued by local governments	2 624 014	X
Total	**10 640 903**	**X**
including impairment of assets	(63 991)	X

(in PLN thousand)

Debt securities measured at fair value through other comprehensive income

	30.09.2018	31.12.2017
Securities issued by State Treasury	20 511 180	X
T-bills	-	X
T-bonds	20 511 180	X
Securities issued by Central Banks	-	X
Securities issued by banks	2 499 749	X
Securities issued by business entities	1 814 122	X
Securities issued by local governments	3 378 922	X
Total	**28 203 973**	**X**
including impairment of assets (*)	(26 416)	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)

	30.09.2018	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)

	30.09.2018	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	-

Equity instruments designated at fair value through other comprehensive income

	30.09.2018	31.12.2017
Shares.	245 658	X
Participation units	14 072	X
Total	**259 730**	**X**

Equity instruments mandatorily measured at fair value through profit or loss

	30.09.2018	31.12.2017
Shares	72 737	X
Total	**72 737**	**X**

Equity securities available for sale (AFS)

	30.09.2018	31.12.2017
Shares	X	147 404
Investment certificates	X	37
Total	**X**	**147 441**
including impairment of assets	X	(1 119)

Notes to financial statements (cont.)

(in PLN thousand)

Investment debt securities according to contractual maturity

	30.09.2018	31.12.2017
Debt securities, including:		
up to 1 month	2 025 414	11 112 757
between 1 and 3 months	180 565	121 753
between 3 months and 1 year	3 908 382	6 054 947
between 1 and 5 years	18 537 456	11 762 697
over 5 years	14 193 059	7 706 227
Total	**38 844 876**	**36 758 381**

Investment debt securities by currency

	30.09.2018	31.12.2017
PLN	33 578 303	32 997 942
EUR	3 132 294	2 091 122
USD	2 134 279	1 669 317
Total	**38 844 876**	**36 758 381**

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 September 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:

	30.09.2018	31.12.2017
ASSETS HELD FOR SALE		
Property, plant and equipment	17 580	42 197
Other assets	22 516	23 368
Total assets	**40 096**	**65 565**

The effect of disposal of other assets is as follows:

	3 QUARTERS 2018	3 QUARTERS 2017
Sales revenues	45 695	911
Net carrying amount of disposed assets (including sale costs)	(11 467)	(191)
Profit/loss on sale before income tax	**34 228**	**720**

(in PLN thousand)

33. Intangible assets

	30.09.2018	31.12.2017
Intangible assets, including:	726 589	777 997
research and development expenditures	4	1 073
licenses and patents	475 728	490 762
other	172 007	180 407
assets under construction	78 850	105 755
Goodwill	747 648	747 648
Total	**1 474 237**	**1 525 645**

In the period from 1 January to 30 September 2018 the Group acquired intangible assets in the amount of PLN 82 591 thousand (in 2017 – PLN 230 327 thousand).

In the period from 1 January to 30 September 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 September 2018 the contractual commitments for the acquisition of intangible assets amounted to PLN 53 214 thousand, whereas as at 31 December 2017 - PLN 33 334 thousand.

34. Property, plant and equipment

	30.09.2018	31.12.2017
Non-current assets, including:	1 274 258	1 327 191
land and buildings	935 155	972 863
machinery and equipment	226 006	262 673
transport vehicles	48 431	53 983
other	64 666	37 672
Non-current assets under construction and prepayments	77 677	98 278
Total	**1 351 935**	**1 425 469**

In the period from 1 January to 30 September 2018 the Group acquired property, plant and equipment in the amount of PLN 62 651 thousand (in 2017 - PLN 140 311 thousand), while the value of property, plant and equipment sold amounted to PLN 14 525 thousand (in 2017 - PLN 605 thousand).

In the period from 1 January to 30 September 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 September 2018 the contractual commitments for the acquisition of property, plant and equipment amounted to PLN 9 889 thousand, whereas as at 31 December 2017 - PLN 20 801 thousand.

(in PLN thousand)

35. Assets pledged as security for liabilities

As at 30 September 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	1 034 442	939 275	1 034 858
Coverage of Fund for protection of guaranteed assets to the benefit of the Bank Guarantee Fund	bonds	776 511	730 200	-
Coverage of payment commitments to the guarantee fund for the Bank Guarantee Fund	bonds	61 662	61 000	54 218
Coverage of payment commitments to the resolution fund for the Bank Guarantee Fund	bonds	109 161	108 000	96 470
Lombard and technical loan	bonds	4 450 618	4 372 760	-
Other loans	bonds	258 956	245 600	207 821
Issue of mortgage bonds	receivables backed by mortgage, bonds	1 499 659	1 498 800	1 825 254
Coverage of the Guarantee Fund for the Settlement of Stock Exchange Transactions to Central Securities Depository (KDPW)	bonds, cash deposits	46 765	46 722	-
Derivatives	bonds	662 496	649 998	663 698

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

Notes to financial statements (cont.)

(in PLN thousand)

36. Amounts due to other banks

Amounts due to other banks by product type

	30.09.2018	31.12.2017
Current accounts	652 808	995 307
Interbank deposits and other liabilities	680 603	653 917
Loans and advances received	3 052 949	3 006 353
Repo transactions	264 861	301 439
Cash in transit	38 090	24 275
Total	**4 689 311**	**4 981 291**

Amounts due to other banks are measured at amortised cost.

Amounts due to other banks by currency

	30.09.2018	31.12.2017
PLN	1 403 138	1 635 684
CHF	223 487	591 405
EUR	2 982 801	2 654 770
USD	60 989	89 288
Other currencies	18 896	10 144
Total	**4 689 311**	**4 981 291**

37. Amounts due to customers

Amounts due to customers by entity and product type

	30.09.2018	31.12.2017
Amounts due to corporate, including:	51 360 591	57 397 810
current accounts	35 028 667	38 152 471
term deposits and other liabilities	16 331 924	19 245 339
Amounts due to budget entities, including:	10 715 339	12 192 129
current accounts	8 098 075	9 392 061
term deposits and other liabilities	2 617 264	2 800 068
Amounts due to individuals, including:	80 473 836	75 576 754
current accounts	47 500 562	43 101 222
term deposits and other liabilities	32 973 274	32 475 532
Repo transactions	912 953	788 436
Cash in transit	304 894	231 139
Total	**143 767 613**	**146 186 268**

Amounts due to customers are measured at amortised cost.

Amounts due to customers by currency

	30.09.2018	31.12.2017
PLN	116 092 261	119 945 891
CHF	306 894	336 479
EUR	17 698 583	16 487 441
USD	8 376 147	7 925 639
Other currencies	1 293 728	1 490 818
Total	**143 767 613**	**146 186 268**

Notes to financial statements (cont.)

(in PLN thousand)

38. Debt securities issued

Debt securities issued by type

	30.09.2018	31.12.2017
Liabilities from bonds	2 067 155	90 092
Certificates of deposit	1 150 465	1 470 000
Mortgage bonds	1 524 995	1 211 307
Total	**4 742 615**	**2 771 399**

Amounts debt securities issued are measured at amortised cost.

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

Debt securities issued by currency

	30.09.2018	31.12.2017
PLN	4 415 685	2 410 014
EUR	326 930	361 385
USD	-	-
Total	**4 742 615**	**2 771 399**

39. Subordinated liabilities

As at 30 September 2018

TYPE OF TRANSACTION	NOMINAL AMOUNT	CURRENCY	INTEREST RATE	ISSUE DATE	MATURITY DATE	SPECIAL TERMS	BALANCE SHEET VALUE AS AT 30.09.2018
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	1 267 400

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

(in PLN thousand)

40. Provisions

Changes in provisions in the reporting period

3 QUARTERS 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	14 961	20 754	149 098	17 407	202 220
Provision utilization	(3 200)	(36 452)	(24 808)	(15 490)	(79 950)
Provision releases	(598)	-	(144 370)	-	(144 968)
Foreign currency exchange differences	-	-	992	-	992
Other changes	16 597	180	(43 760)	-	(26 983)
Closing balance	**44 892**	**284 730**	**209 898**	**50 250**	**589 770**
Short term	2 835	13 594	27 888	2 156	46 473
Long term	42 057	271 136	182 010	48 094	543 297

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.

Notes to financial statements (cont.)

(in PLN thousand)

41. Contingent commitments

Lawsuits

As at 30 September 2018 the following lawsuits for payment are ongoing with involvement of the Group, that are important in view of the value of the subject of dispute:

1) in the group of liabilities (against the Group):

- brought by a legal person – lawsuit for payment by virtue of inadequate performance of agreement; value of the subject of dispute 17 521 646 EUR (which as at 28 September 2018 at mid NBP rate amounted to 74 841 958.72 PLN); litigation initiation date – 19 July 2018; in the present factual and legal state the Bank assesses the funds outflow risk as possible,
- brought by the receiver for a joint stock company in liquidation bankruptcy – lawsuit for payment of compensation for a damage incurred as a result of the Bank's demanding immediate payment of the amounts due in virtue of payment of the price from the credit liabilities transfer agreement and conducting enforcement collection of the portion of the price remaining for payment; value of the subject of dispute 57 450 130 PLN; litigation initiation date – 30 April 2015; in the present factual and legal state the Bank assesses the funds outflow risk as minor,
- brought by a beneficiary of warranty – lawsuit for payment of a claim by virtue of the warranty issued by the Bank; value of the subject of dispute 55 996 064.23 PLN; litigation initiation date – 20 May 2014. On 10 October 2018 the Plaintiff withdrew the lawsuit.
- brought by a natural person – lawsuit for payment by the Bank of an amount charged by virtue of settlement of forward financial transactions; value of the subject of dispute 38 916 555.18 PLN; litigation initiation date – 2 October 2016; in the present factual and legal state the Bank assesses the funds outflow risk as possible,
- brought by a beneficiary of warranty – lawsuit for payment of a claim by virtue of the warranty issued by the Bank; value of the subject of dispute 32 750 000 PLN; litigation initiation date – 14 January 2014; in the present factual and legal state the Bank assesses the funds outflow risk as minor,
- brought by a beneficiary of warranty – lawsuit for payment of a claim by virtue of the warranty issued by the Bank; value of the subject of dispute 29 204 684 PLN; litigation initiation date – 16 January 2015. On 10 October 2018 the Plaintiff withdrew the lawsuit.

2) in the group of receivables (brought by the Group):

- Bank's lawsuit for payment against limited debtor by virtue of mortgage collateralizing repayment of the granted loan; value of the subject of dispute 132 877 901 PLN; litigation initiation date – 21 January 2016,
- Bank's mutual lawsuit for payment of amounts due by virtue of the transfer of liabilities; value of the subject of dispute 89 977 886 PLN; litigation initiation date – 28 February 2013,
- Bank's intervention lawsuit against the parties of the main lawsuit – the subject of the main intervention is the demand to execute (pay) the liabilities purchased by the Bank from one of the defendants against the other defendant; value of the subject of dispute 67 432 617.21 PLN; litigation initiation date – 23 January 2006.

None of the litigations ongoing in the third quarter of 2018 before a court, authority competent for arbitrary proceedings or a body of public administration posed a threat for financial liquidity of the Group.

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 September 2018 is PLN 44 892 thousand (PLN 17 132 thousand as at 31 December 2017).

Notes to financial statements (cont.)

(in PLN thousand)

Financial commitments granted

Financial commitments granted by entity

	30.09.2018	31.12.2017
Financial commitments granted to:		
financial entities	1 722 596	785 430
non - financial entities	32 013 640	32 495 145
budget entities	844 375	599 409
Total	**34 580 611**	**33 879 984**

Guarantees issued

Guarantees issued by entity

	30.09.2018	31.12.2017
Issued to financial entities:	997 021	1 093 608
guarantees	996 094	1 093 608
confirmed export letters of credit	927	-
Issued to non - financial entities	10 599 787	9 970 336
guarantees	7 161 543	6 726 612
securities' underwriting guarantees	3 351 995	3 070 727
sureties	86 249	172 997
Issued to budget entities:	441 989	434 737
guarantees	26 973	13 186
securities' underwriting guarantees	415 016	421 551
Total	**12 038 797**	**11 498 681**

Off-balance sheet commitments received

Off-balance sheet commitments received by entity

	30.09.2018	31.12.2017
Financial received from:	900 307	384 961
financial entities	890 307	384 961
non - financial entities	10 000	-
budget entities	-	-
Guarantees received from:	17 786 600	13 871 406
financial entities	3 666 417	3 116 556
non - financial entities	13 141 249	9 824 811
budget entities	978 934	930 039
Total	**18 686 907**	**14 256 367**

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

(in PLN thousand)

42. Additional information to the consolidated cash flow statement

Cash and cash equivalents

	30.09.2018	31.12.2017	30.09.2017
Cash and amounts due from Central Bank	5 720 292	5 236 318	6 106 127
Loans and receivables from banks with maturity up to 3 months	4 541 190	2 108 722	2 628 252
Cash and Cash equivalents presented in the cash flow statement	**10 261 482**	**7 345 040**	**8 734 379**

Restricted availability cash and cash equivalents as at 30 September 2018 amounted to PLN 5 063 787 thousand (PLN 4 786 930 thousand as at 31 December 2017, PLN 4 761 958 thousand as at 30 September 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 SEPTEMBER 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	1 978 017	-	-	-	(6 801)	4 742 615
Subordinated liabilities	1 257 188	-	-	-	-	10 212	1 267 400
Loans and advances received	3 006 353	(64 463)	-	111 228	-	(169)	3 052 949
Total	**7 034 940**	**1 913 554**	**-**	**111 228**	**-**	**3 242**	**9 062 964**

	BALANCE AS AT 1 JANUARY 2017	CHANGES FROM FINANCING CASH FLOWS	NON-CASH CHANGES				BALANCE AS AT 30 SEPTEMBER 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	860 656	-	-	-	52 313	2 435 932
Loans and advances received	3 249 417	(123 685)	-	(66 008)	-	(113 981)	2 945 743
Total	**4 772 380**	**736 971**	**-**	**(66 008)**	**-**	**(61 668)**	**5 381 675**

(in PLN thousand)

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 September 2018

NAME OF ENTITY	RECEIVABLES FROM LOANS AND PLACEMENTS	SECURITIES	RECEIVABLES FROM REVALUATION OF DERIVATIVES	OTHER RECEIVA BLES	LIABILITIES FROM LOANS AND DEPOSITS	LIABILITIES FROM REVALUATION OF DERIVATIVES	OTHER LIABILITIES
PZU S.A. – the Bank's parent entity	30	-	-	3 241	7 446	-	117
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	8 028	375	-	3 897	37 647	7 310	1 618
Key management personnel of the Bank Pekao S.A.	475	-	-	-	9 690	-	-
Total	**8 533**	**375**	**-**	**7 138**	**54 783**	**7 310**	**1 735**

Receivables from loans and placements by contractual maturity

30.09.2018	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	30	-	-	-	-	-	30
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	10	7 867	21	97	33	-	8 028
Key management personnel of the Bank Pekao S.A.	-	-	6	14	64	391	475
Total	**40**	**7 867**	**27**	**111**	**97**	**391**	**8 533**

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

Liabilities from loans and deposits by contractual maturity

30.09.2018	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	7 446	-	-	-	-	-	7 446
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	35 147	2 500	-	-	-	-	37 647
Key management personnel of the Bank Pekao S.A.	7 189	101	1 173	1 227	-	-	9 690
Total	**49 782**	**2 601**	**1 173**	**1 227**	**-**	**-**	**54 783**

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

Notes to financial statements (cont.)

(in PLN thousand)

Receivables from loans and placements by currency

30.09.2018	EUR	USD	CHF	PLN	OTHER	TOTAL
PZU S.A. – the Bank's parent entity	-	-	-	30	-	30
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	-	-	8 028	-	8 028
Key management personnel of the Bank Pekao S.A.	-	-	392	83	-	475
Total	**-**	**-**	**392**	**8 141**	**-**	**8 533**

Liabilities from loans and deposits by currency

30.09.2018	EUR	USD	CHF	PLN	OTHER	TOTAL
PZU S.A. – the Bank's parent entity	308	-	-	7 138	-	7 446
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	639	88	536	35 961	423	37 647
Key management personnel of the Bank Pekao S.A.	3 362	447	150	5 724	7	9 690
Total	**4 309**	**535**	**686**	**48 823**	**430**	**54 783**

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 September 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	297	(199)	1 147	-	240	(5 549)
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities	319	(343)	18 702	(114)	1 053	(8 278)
Key management personnel of the Bank Pekao S.A.	1	(46)	1	-	-	-
Total	**617**	**(588)**	**19 850**	**(114)**	**1 293**	**(13 827)**

Income and expenses from transactions with related parties for the period from 1 January to 30 September 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 (*)	32	(58)	2 192	-	11	(111)
Entities of PZU S.A. Group excluding the Bank Pekao S.A. Group entities (*)	173	(134)	3 126	(28)	1 464	(39)
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.	-	(294)	30	-	248	-
Pekao Investment Management S.A.	-	(1 417)	7	-	-	-
Pekao TFI S.A. (PIM S.A. subsidiary)	-	(981)	148 480	-	11	(4)
Total Associates of Bank Pekao S.A. Group	**-**	**(2 692)**	**148 517**	**-**	**259**	**(4)**
Key management personnel of the Bank Pekao S.A.	107	(181)	2	-	-	-
Total	**3 741**	**(4 471)**	**157 549**	**(1 287)**	**17 716**	**(5 704)**

(*) 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 September 2018

NAME OF ENTITY	GRANTED		RECEIVED	
	FINANCIAL	GUARANTEES	FINANCIAL	GUARANTEE
PZU S.A. – the Bank's parent entity	2 821	-	-	-
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	584	6 000	-	6 000
Key management personnel of the Bank Pekao S.A.	573	-	-	-
Total	**3 978**	**6 000**	**-**	**6 000**

Off-balance sheet financial commitments and guarantees by contractual maturity

30.09.2018	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	-	-	-	-	2 821	-	2 821
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	20	-	-	564	-	584
Key management personnel of the Bank Pekao S.A.	-	-	24	69	51	429	573
Total	**-**	**20**	**24**	**69**	**3 436**	**429**	**3 978**
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

30.09.2018	EUR	USD	CHF	PLN	OTHER	TOTAL
FINANCIAL COMMITMENTS GRANTED						
PZU S.A. – the Bank's parent entity	-	-	-	2 821	-	2 821
Entities of PZU S.A. Group excluding of Bank Pekao S.A. Group entities	-	-	-	584	-	584
Key management personnel of the Bank Pekao S.A.	-	-	-	573	-	573
Total	**-**	**-**	**-**	**3 978**	**-**	**3 978**
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	
	3 QUARTERS 2018	3 QUARTERS 2017
Management Board of the Bank		
Short-term employee benefits (*)	9 367	21 219
Post-employment benefits	1 088	-
Long-term benefits (**)	3 230	1 794
Share-based payments (***)	-	9 555
Total	**13 685**	**32 568**
Supervisory Board of the Bank		
Short-term employee benefits (*)	1 034	823
Total	**1 034**	**823**

(*) 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 September 2018 and in the period from 1 January to 30 September 2017.

Remuneration expenses of Supervisory Boards and Management Boards of subsidiaries

	VALUE OF BENEFITS	
	3 QUARTERS 2018	3 QUARTERS 2017
Companies' Management Boards		
Short-term employee benefits	12 709	11 181
Long-term benefits	1 723	-
Post-employment benefits	747	-
Termination benefits	1 634	-
Share-based payments	-	808
Total	**16 813**	**11 989**
Companies' Supervisory Boards		
Short-term employee benefits	429	189
Total	**429**	**189**

44. Subsequent events

Significant subsequent events are presented in the Note 8.8 'Subsequent events' of the Report on the activities of Bank Pekao S.A. Group for the third quarter of 2018.

Signatures of the Management Board Members

Date	Name/Surname	Position/Function	Signature
06.11.2018	Michał Krupiński	President of the Management Board	
06.11.2018	Roksana Ciurysek-Gedir	Vice President of the Management Board	
06.11.2018	Andrzej Kopyrski	Vice President of the Management Board	
06.11.2018	Tomasz Kubiak	Vice President of the Management Board	
06.11.2018	Michał Lehmann	Vice President of the Management Board	
06.11.2018	Marek Lusztyn	Vice President of the Management Board	
06.11.2018	Tomasz Styczyński	Vice President of the Management Board	
06.11.2018	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.