



Management Board Report on the Performance of mBank S.A. Group in H1 2018

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1. About mBank Group

1.1. Executive summary

mBank Group is the fourth-largest financial institution in Poland in terms of assets, offering retail, corporate and investment banking as well as other financial services such as leasing, factoring, insurance, financing of commercial real property, brokerage operations, wealth management, corporate finance and capital markets advisory. mBank is the only Polish bank which successfully extended its Polish business model on foreign markets by launching retail operations in the Czech Republic and Slovakia in 2007.

H1 2018 was, with high probability, the best six months for the Polish economy since 2008. During the first six months of 2018 the economy picked up again and grew at a pace exceeding 5.0% year on year. In Q1, the economic growth reached 5.1% year on year and the bank estimates (based on higher frequency data) that in Q2 it might reach 5.3%-5.4% year on year. The available data suggest that private consumption, up by 4.8% in Q1 and by approx. 5.0% in Q2, was still the main driver of economic growth. Investments, likely to have risen by 9% from January to June 2018, were another important contributor to economic growth. They were fuelled predominantly by public sector spending from both government and local government institutions as well as companies in which the state holds majority stakes. Polish export experienced a clear slowdown in the first months of 2018, mainly due to the economic weakening observed in the euro zone since January. H1 2018 was also marked by large fluctuations in inflation: in February and March the inflation rate unexpectedly fell below the target range to 1.3% year on year and then rose to 2.0% year on year in the spring (final June data). Under these circumstances the Monetary Policy Council could comfortably maintain its dovish rhetoric.

Growth in household deposits first reached its lowest compared with the previous year and then rebounded to the highest level since July 2017. Growth in retail deposits was helped by rising nominal wages, no attractive alternatives to savings accounts and the weakening zloty, which increases the present value of foreign currency deposits. The bank reckons that in the next few months the inflow of household deposits will not subside, even amid low interest rates. Growth in corporate deposits was sluggish in the analysed period, most likely due to deteriorating liquidity standing of some companies and worsening financial performance of the corporate sector due to rising labour costs not being fully reflected in the prices of finished goods and services.

Household loans have been on an upward trend for nearly two years. Their growth exceeded 5.0% year on year, excluding one-off seasonal and calendar effects. Lending revival was driven mainly by household loans. Favourable situation on the labour market and high supply of flats will support high demand for housing loans in the coming quarters. Growth in corporate loans was stable in H1 2018 (6.0-7.0% year on year). The role of investment loans has been declining, reflecting private sector's low propensity to invest and its large own contributions to financing investment projects.

In H1 2018, mBank Group reported business growth across all segments. Core income was record high, underpinned by stable growth in volumes, improved structure of assets, rising client base and higher number of transactions per client. In addition, net profit rose, supported by the sale of an organized part of mFinanse.

Key highlights of H1 2018:

- **Increase in the net profit** attributable to owners of mBank by 43.0% to PLN 698.4 million compared with H1 2017.
- **Increase in total income** by 19.7% year on year, driven mainly by a rise in core income (+8.6%) and the proceeds from the sale of an organized part of enterprise of mFinanse in Q1 2018;
- **Rise in operating expenses** (including amortisation) by 4.4% against H1 2017 attributable to higher staff-related expenses, material costs and amortisation, amid higher efficiency measured by the cost to income ratio (normalised cost to income ratio fell to 44.8% in H1 2018 from 46.5% in H1 2017);
- **Increase in net impairment losses and fair value change on loans and advances** by 66.7%, driven by higher provisions in the corporate and retail banking segment.

- Rising volumes:
 - **Increase in net loans and advances** by 6.1% compared with the end of 2017, supported by active sales in the Retail Banking segment as well as in the Corporate and Investment Banking segment. Excluding reverse repo/buy sell back transactions and the FX effect, gross loans rose by 4.1% in H1 2018.
 - **Growth in clients' deposits** (i.e. +6.9% compared with the end of 2017), triggered mainly by higher deposits in current accounts held by individuals.
- Expansion on the retail loans market was reflected in the **record-high sales of non-mortgage loans** reaching PLN 4,331.6 million, which represents an increase by 16.9% compared with H1 2017. Additionally, there was a significant **rise in the sales of mortgage loans**, which stood at PLN 2,147.6 million in H1 2018, up by 19.3% compared with H1 2017.
- As a result of simultaneous growth in loans and deposits, the **loan to deposit ratio reached 91.6%**, down from 92.3% reported at the end of 2017.
- **Accelerating client acquisition:** in 2018, mBank acquired 166 thou. individual and 886 corporate clients.
- **High quality of capital base:** capital ratios surpassing regulatory requirements: CET 1 ratio at 17.1%, Total Capital Ratio at 20.1%.

1.2. mBank's Authorities

In H1 2018 there were no changes in the composition of the Management Board and the Supervisory Board of mBank and as of June 30, 2018, they were composed as follows:

Supervisory Board of mBank

1. Maciej Leśny – Chairman of the Supervisory Board
2. Stephan Engels – Deputy Chairman of the Supervisory Board
3. Tomasz Bieske – Member of the Supervisory Board
4. Andre Carls – Member of the Supervisory Board
5. Marcus Chromik – Member of the Supervisory Board
6. Janusz Fiszer – Member of the Supervisory Board
7. Mirosław Godlewski – Member of the Supervisory Board
8. Jörg Hessenmüller – Member of the Supervisory Board
9. Thorsten Kanzler – Member of the Supervisory Board
10. Michael Mandel – Member of the Supervisory Board
11. Teresa Mokrysz – Member of the Supervisory Board
12. Agnieszka Słomka-Gołębiowska – Member of the Supervisory Board

There newly appointed Supervisory Board has 4 independent members: Tomasz Bieske, Janusz Fiszer, Mirosław Godlewski and Agnieszka Słomka-Gołębiowska.

Management Board of mBank

1. Cezary Stypułkowski – President of the Management Board, Chief Executive Officer
2. Adam Pers – Vice-president of the Management Board, Head of Corporate and Investment Banking
3. Andreas Böger – Vice-president of the Management Board, Chief Financial Officer
4. Lidia Jabłonowska-Luba – Vice-president of the Management Board, Chief Risk Officer
5. Frank Bock – Vice-president of the Management Board, Head of Financial Markets
6. Cezary Kocik – Vice-president of the Management Board, Head of Retail Banking
7. Krzysztof Dąbrowski – Vice-president of the Management Board, Head of Operations and Information Technology.

Further information on competences of particular members of the Management Board can be found at: <https://www.mbank.pl/en/about-us/bank-authorities/>.

1.3. Composition of mBank Group and key areas of activity

In Q1 2018, after the fulfilment of conditions precedent stipulated in the agreement signed in Q4 2017, the sale of an organized part of mFinanse, a subsidiary providing among others insurance intermediary services in the group insurance area, was completed.

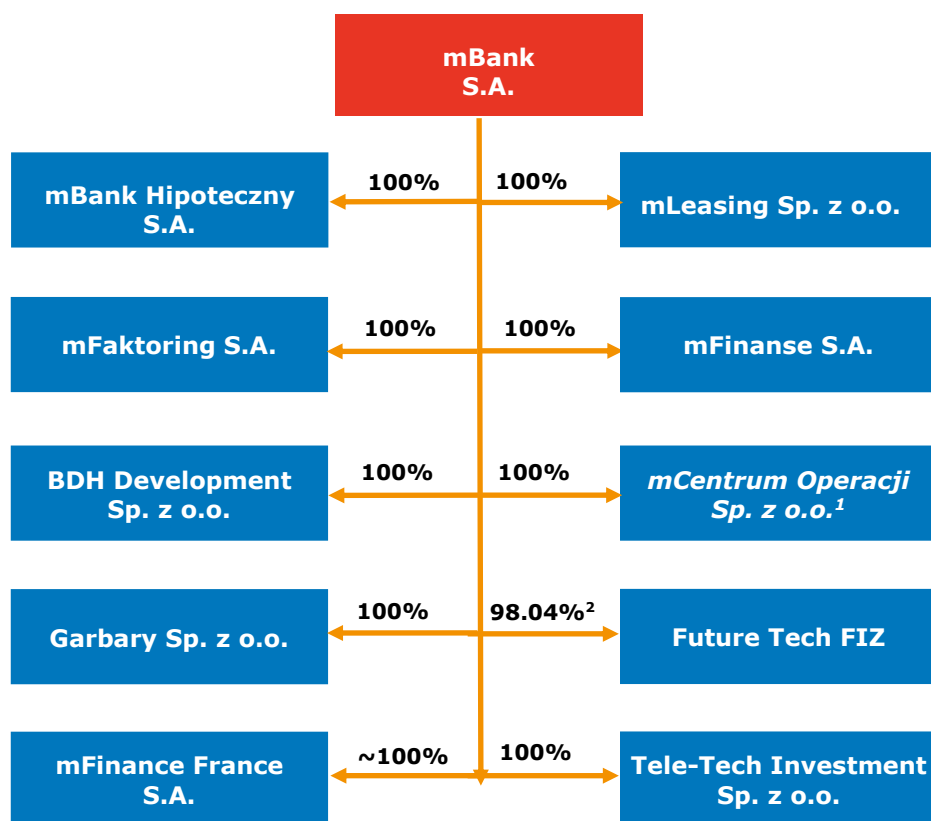
In view of changing business environment, in September 2017 mBank decided to spin off and sell two organized parts of mCentrum Operacji (mCO):

- Automatic Processes Development Line (ZCP 1) - with the largest potential to automate and robotize the implemented processes,
- General Line (ZCP 2) - rendering other services supporting banking processes.

ZCP1 and ZCP 2 were spun off together with their assets, agreements and employees performing tasks from the spun-off areas. On March 1, 2018, the Automatic Processes Development Line was sold to Feronia whose majority shareholder is Future Tech FIZ, a closed-ended investment fund controlled by mBank, for the purpose of robotizing the processes handled by this part of mCO. The General Line was sold to the bank.

The sale agreements were signed on February 28, 2018, and the sale became effective as of March 1, 2018. Consequently, the previous operating activity of mCO is no longer continued.

mBank Group (consolidated subsidiaries) as at June 30, 2018 was composed as presented on the diagram below.



¹ On March 1, 2018, mBank took over most of the tasks performed by mCO, along with the employees assigned to them, as well as assets and contracts.

² Direct share of mBank in the votes at the general meeting of the company.

The table below presents the division of operations of mBank Group into business segments and areas.

Composition of mBank Group

Segment	Retail Banking	Corporates and Financial Markets	
		Corporate and Investment Banking	Financial Markets
Bank	<ul style="list-style-type: none"> Retail clients, private banking clients, and micro-enterprises Affluent clients (Private Banking and Wealth Management) 	<ul style="list-style-type: none"> Service of corporations and non-banking financial institutions (K1) Large companies (K2) Small and medium-sized companies (K3) 	<ul style="list-style-type: none"> Banks Corporate clients in the scope of trading and sales Risk and liquidity management
Consolidated subsidiaries	<ul style="list-style-type: none"> Retail part of mLeasing Sp. z o.o. Retail part of mBank Hipoteczny S.A. mFinanse S.A. 	<ul style="list-style-type: none"> Corporate part of mLeasing Sp. z o.o. Corporate part of mBank Hipoteczny S.A. mFaktoring S.A. Garbary Sp. z o.o. Tele-Tech Investment Sp. z o.o. 	<ul style="list-style-type: none"> mFinance France S.A. mLeasing Sp. z o.o. – in the scope of funding mBank Hipoteczny S.A. – in the scope of funding
	Other subsidiaries	<ul style="list-style-type: none"> mCentrum Operacji Sp. z o.o. (outsourcing services provider) BDH Development Sp. z o.o. (real property manager) Future Tech FIZ (closed-end investment fund) 	

1.4. Subsidiaries of mBank Group



mFinanse is a financial services intermediary operating as an open platform for selling financial products of various institutions including mBank. Its product offer includes loans, accounts, insurance as well as investment and savings products for both individuals and companies. The subsidiary offers the products of 15 financial entities, in more than 172 outlets across Poland.



mLeasing is one of the largest leasing companies in Poland and ranks third on the real property leasing market and on the leasing market at the end of H1 2018.

The subsidiary offers lease financing, loans, and car fleet rental and management services addressed to both corporate and retail clients.

In the corporate segment mLeasing offers various types of leasing products, including lease of private and commercial cars and heavy transport vehicles, car fleet management, lease of machines and equipment, and real property lease.

In the retail segment the subsidiary operates the "Leasing in Retail" programme addressed to micro-enterprises and SMEs, which are offered lease contracts using dedicated lease processes.

Bank Hipoteczny

mBank Hipoteczny (mBH) is a mortgage bank with the longest track record of issuing covered bonds on the Polish capital market.

The main role of mBH is a ability to raise long-term financing in the form of mortgage covered bonds in order to improve the stability and diversification of financing activities of mBank Group.

mBH finances commercial investments on the real property market, including office buildings, commercial centres and facilities, hotels, warehouses, logistics centres, housing estates. Another important area of mBH's operation is lending to the public sector in the area of municipal investments and real properties of local government units.

In addition to its lending activity, mBH offers also market analyses and advisory services addressed to investors and entities active on the commercial real property market.

According to Fitch Ratings, mBH's long-term and short-term ratings are "BBB" and "F2", respectively. The mortgage covered bonds issued by mBH are rated "A". For more information about mBH's ratings, see later in the chapter.

Faktoring

mFaktoring is the sixth largest player on the Polish factoring market among the members of the Polish Factors Association.

The services provided by mFaktoring are complementary to mBank's corporate offer. mFaktoring offers the financing of ongoing business operations, receivables management, credit protection, maintenance of debtors' settlement accounts and enforcement of receivables. In addition, the offer includes domestic and export factoring with recourse and credit protection, as well as import guarantees.

Products offered by mFaktoring are available in all mBank branches providing services to SMEs and corporations in Poland.

1.5. Rating of mBank and mBank Hipoteczny

In 2018, Fitch Ratings, S&P Global Ratings and Moody's Investors Service did not change the ratings and rating outlooks of mBank. There were also no changes in the ratings of mBank Hipoteczny and mortgage covered bond ratings.

On December 8, 2017, Fitch affirmed all ratings and the outlook on the long-term rating of mBank and mBank Hipoteczny, while on May 24, 2018, the rating of bonds under the EMTN Programme was confirmed.

Fitch Ratings	Ratings of mBank	Ratings of mBank Hipoteczny
Long-term IDR	BBB (stable outlook)	BBB (stable outlook)
Short-term IDR	F2	F2
Viability rating	bbb-	
Support rating	2	2
Rating of unsecured debt issued under the Euro Medium Term Note Programme (EMTN)	BBB	
Ratings of mortgage covered bonds issued by mBank Hipoteczny		A (positive outlook)

On June 21, 2018, S&P Global Ratings affirmed mBank's long-term rating at "BBB+" and short-term rating at "A-2". The long-term rating outlook for mBank remained negative and so is Commerzbank's long-term rating outlook. mBank's standalone credit profile was upgraded from „bbb-“ to „bbb“ as a result of the improved capital position and profitability analysis of mBank.

S&P Global Ratings	Ratings of mBank
Long-term Deposit Rating	BBB+ (negative outlook)
Short-Term Rating	A-2
Stand-alone Credit Profile (SACP)	bbb
Rating of unsecured debt issued under the Euro Medium Term Note Programme (EMTN)	BBB+

Moody's ratings for mBank are based solely on publicly available information, and the bank does not take part in the rating process, having the "non-participating issuer" status. The latest change of mBank's rating took place on December 19, 2017, when Moody's upgraded the following ratings: mBank's long-term deposit from Baa2 to Baa1, baseline credit assessment (BCA) from ba2 to ba1, and adjusted BCA from ba1 to baa3. On June 18, 2018, the agency assigned the following counterparty risk assessment (CRA) ratings: long-term at "A3" and short-term at "Prime-2".

Moody's Investors Service	Ratings of mBank
Long-term deposit rating	Baa1 (positive outlook)
Short-Term Rating	Prime-2
Long-Term Counterparty risk assessment (CRA)	A3
Short-Term Counterparty risk assessment (CRA)	Prime-2
Baseline credit assessment (BCA)	ba1
Adjusted BCA	baa3

The table below compares the long-term ratings of Poland, mBank and Commerzbank assigned by the three major agencies, as at the end of H1 2018.

Rating agency	Poland	mBank S.A.	Commerzbank AG
Fitch Ratings	A- (stab.)	BBB (stab.)	BBB+ (stab.)
S&P Global Ratings	BBB+ (pos.)	BBB+(neg.)	A- (neg.)
Moody's Investors Service	A2 (stab.)	Baa1* (pos.)	A2* (pos.)

* Long-term deposit rating.

Rating outlook in brackets: pos. – positive, stab. – stable, neg. – negative

1.6. mBank shareholders and share price on the WSE

Information on mBank shares and shareholders

mBank has been listed on the Warsaw Stock Exchange since 1992. Nominal value per share is PLN 4.00.

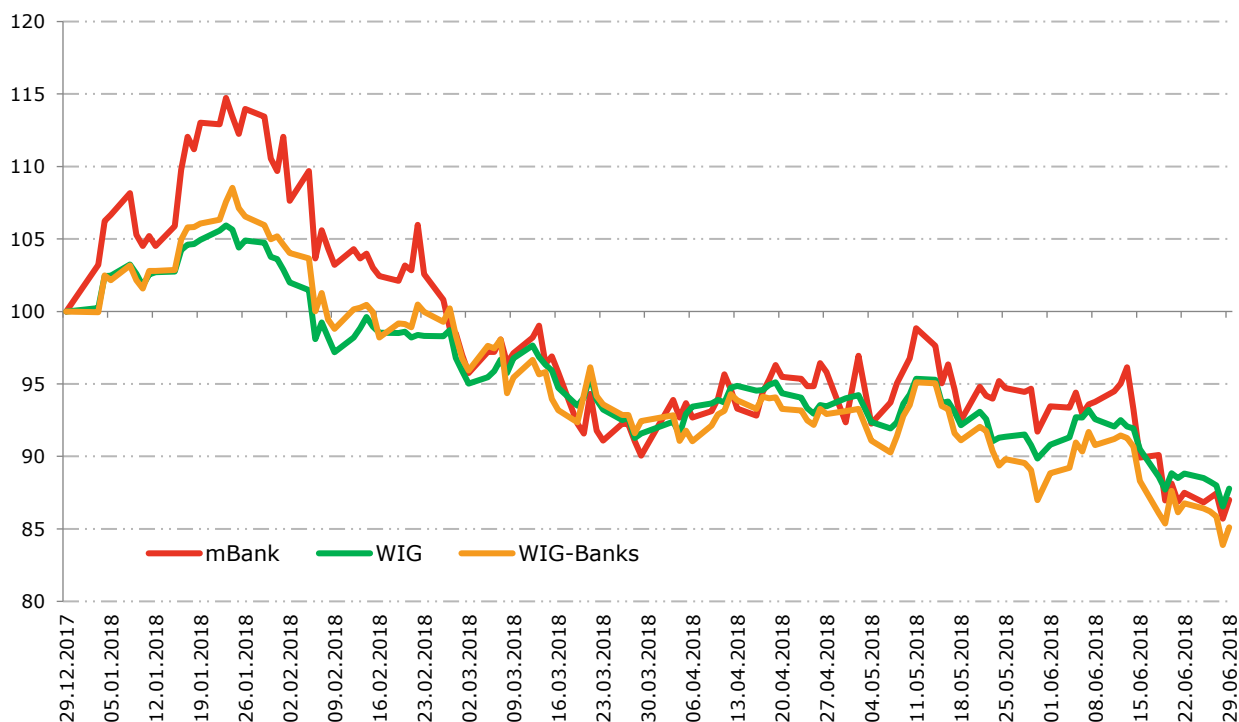
As at June 30, 2018, mBank's registered share capital amounted to PLN 169,248,488. The capital is divided into 42,312,122 ordinary registered shares and bearer shares. Each share represents one vote at the General Meeting. In H1 2018, the number of mBank's shares remained unchanged.

They are part of the following WSE indices: WIG, WIG-Poland, WIG20, WIG30, WIG 20TR, WIG 30TR, WIG-Banki and Respect.

Commerzbank AG is the majority shareholder of mBank, holding 69.37% of the share capital and votes at the General Meeting. Shares accounting for 30.63% of all shares are in free float. These shares are held mainly by financial investors (chiefly Polish pension funds, domestic and foreign investment funds). Nationale-Nederlanden Otwarty Fundusz Emerytalny exceeded the 5% threshold of shares and votes at the General Meeting. At the 31st Annual General Meeting of mBank S.A. on May 9, 2018, Nationale-Nederlanden Otwarty Fundusz Emerytalny registered shares making up 5.0% of the share capital. At the same AGM, AVIVA Otwarty Fundusz Emerytalny AVIVA BZ WBK registered shares accounting for 4.5% of mBank's share capital.

mBank stock performance on the WSE

The situation at the WSE is mainly attributable to foreign investors' attitude towards the emerging markets basket. Strengthening of the US dollar and tightening of the US monetary policy encourages investors to move their assets from riskier markets to US bonds. In H1 2018, despite the favourable economic situation in Poland and outstanding GDP growth when compared to other economies, the WSE was adversely affected by the outflow of foreign funds. This was partly caused by the stronger dollar and growing profitability of American debt, and partly by the eagerness to realize the profits generated in 2017, which was very successful for the WSE. Domestic capital did not stimulate the stock exchange performance, either. Listed companies were under substantial pressure due to redemption of shares in investment fund companies, in shares funds, and very limited demand on the part of open-end pension funds. Trends in global stock markets were not much of help. Since January 2018, many of them have reported drops or consolidation in stock prices.

mBank's share performance v. main WSE indices


In H1 2018, WIG20 and the broad-based index WIG went down by 13.2% and 12.2%, respectively.

The closing price per mBank share during the last session in H1 2018 (June 29) stood at PLN 399.80, representing a decrease by 14.0% compared with the price reported on the last business day of 2017 (December 29), and a decrease by 13.0% compared with the dividend-adjusted price (the dividend was paid on May 24, 2018). In the same period, WIG-Banks index went down by 14.9%. Falling share prices were affected by the receding prospects for growth in interest margins with stable interest rates perspective. For comparison, EURO STOXX Banks Index lost 15.4% in H1 2018.

mBank's capitalisation amounted to PLN 16.9 billion (EUR 3.9 billion) as at June 30, 2018, compared with PLN 19.7 billion (EUR 4.7 billion) at the end of 2017 and PLN 19.5 billion (PLN 4.6 billion) a year before.

P/BV (price/book value) ratio for mBank Group stood at 1.2 at the end of June 2018 compared with 1.4 a year before. P/E ratio (price/earnings per share) reached 12.1 after H1 2018, compared with 20.0 after H1 2017.

The current consensus of expected results of mBank Group is available on mBank's website: <http://www.mbank.pl/relacje-inwestorskie/akcje-mbank/konsensus.html>.

2. Business activity and key achievements

2.1. Key projects of mBank Group in H1 2018

Refreshed online banking

In H1 2018 we started to refresh our online banking for individuals and SMEs (except for mBank CompanyNet addressed to corporate clients). The upgraded online banking should be easy to use and more flexible. We want to make it easier for users to adjust the service to their needs. The previous version was launched five years ago which is a really long period of time in the world of technology.

We have been improving the design and rolling out new features gradually to give our clients time to get used to them. All changes in the design and features have been developed in consultation with our clients.

We started the process by changing the colours used in the online banking. The new pages are white with grey tints and red action buttons. The colours are now more subdued.

Our clients supported us in redesigning the service. We spent more than a year collecting their opinions and asking them about which online banking features were important to them, how they rated the existing service and how they would like to use it in the future. We also added a "Rate us" button in the online banking enabling clients to leave comments in sections which were important to them. The team tasked with upgrading the service analysed 100 thou. ratings and comments spending more than 11 thou. hours on the project.

New mobile app features

In H1 2018, we changed and added new features to our mobile application launched in February 2014 and redesigned in 2017 when it was made easier to navigate and upgraded. The biggest difference can be noticed in how users **manage their cards and limits**. We have introduced a number of changes, including:

- **Simpler card transaction limits** - we did away with monthly limits and introduced simpler daily limits (now there are three amount limits in PLN: a limit on purchases in shops, a limit on online purchases and a limit on cash withdrawals at ATMs). For more security the client can disable the type of transactions which they think they will not use.
- Option to set a **higher one-off limit** for a transaction of a specific type valid until the end of the day. If a client plans a big purchase, e.g. at a furniture shop, they may raise the limit for one day. The bank will automatically restore the lower limit at the end of the day.
- **Temporary card block** - the card holder can place a temporary block on a card and remove it if they find the card. This option is available in the mobile app and online banking.
- **Option to block foreign transactions** - we have offered card holders an easy method for blocking card transactions abroad and thus reducing the risk of unauthorised card transactions. The block does not apply to online transactions in foreign Internet services and on foreign websites.
- **Option to block contactless transactions** - intended to help our clients manage the NFC function of their cards.
- **Notifications about rejected card transactions** - if their card is declined, the client will receive a notification in the mobile app telling them why the transaction could not be effected and what to do to change it.

All the new features are available in the online banking and the mobile app.

We have also launched **Apple Pay** providing our clients with a simpler, safer and more private payment solution.

One in three users of mBank's mobile application pay with a mobile phone. Holders of MasterCard and Visa cards have been able to use Apple Pay since June 19, 2018. The new service marks a revolution in mobile payments offering a simple, fast, safe and private way to make payments.

Apple Pay offers a high level of privacy and security. Debit/credit card numbers are not saved in the device or on Apple's servers. Apple Pay uses a unique Device Account Number which is saved in an encrypted form using the device's secure element. Every transaction is authorised with the use of a unique one-time passcode that is generated dynamically.

Apple Pay is very easy to configure. Users enjoy all benefits of conventional credit and debit card payments. Apple Pay payments in brick-and-mortar shops are available to users of the iPhone SE, iPhone 6 and later as well as Apple Watch.

Paying with Apple Pay for online purchases on websites and in applications supporting the service is just as easy. Such transactions are authorised using TouchID or by double-clicking the side button and glancing at the iPhone X to authenticate Face ID.

In addition to the new payment solution, we have offered our clients the possibility of **opening bank accounts and managing standing orders on a smartphone**. The former is available to users of iOS (Apple) devices. They account for 25% of all users of mBank's mobile app.

The possibility of opening a bank account online on an iOS device without the need to visit a branch or order a courier has been available since June. The service for Android users will be launched soon.

We have also made it possible to manage standing orders using the mobile app. By using the payment options section clients can set new as well as change and modify existing standing orders.

mBank's mobile app has 1.2 million users. Our app ranked third in Europe in *The Forrester Banking Wave™: European Mobile Apps, Q2 2018* report published by Forrester, a global advisory firm. It was appreciated for its unique features and user-friendliness.

mAccelerator – mBank's fund for investments in Fintech start-ups

mAccelerator is an mBank's EUR 50m VC fund launched in June 2017. The fund engages in seed as well as later-stage investments in startups with solutions applicable to the banking and financial sectors, currently focusing on cybersecurity, biometry, robotic process automation, artificial intelligence and digital marketing with focus on chatbots and messengers.

mBank's support is highly appreciated also as a corporate partner for the investments. mBank sets direction of the mobile and on-line banking development in Poland and abroad (which is proven by international acclaim and rewards) and offers a range of collaborative options for our portfolio startups.

Currently, our portfolio contains 3 companies: Centrum Bezpieczeństwa Cyfrowego (cybersecurity solution company) and Digital Teammates (pure-play Robotic Process Automation company) - acquired in 2017 and AI-powered communication platform for messaging apps - Bot4Business (B4B) – added to the portfolio in H1 2018.

B4B develops a platform that allows onboarding of and communication with clients on messaging apps (eg. Messenger, Viber). The platform is equipped with artificial intelligence-powered engine that recommends consultants possible replies to clients. B4B already provides services to one client from cybersecurity sector and is on the track to secure another commercial contract.

EMTN Programme

The Euro Medium Term Notes Programme (EMTN), which makes it possible to issue debt securities with different interest structures in many tranches and currencies up to EUR 2 billion, started in April 2012. The bonds are issued by mFinance France, a company operating under French law based in Paris, and backed by mBank. In the period from 2012 to 2017 mFinance France carried out 6 issues of euro bonds denominated in CHF, EUR and CZK.

On April 11, 2018, mBank's Management Board passed a resolution authorising the execution of a new debt securities issue programme (Euro Medium Term Note Programme) by mBank directly. The programme will be carried out in many tranches and currencies. The securities will have different interest and maturity structure. The maximum principal amount was set at EUR 3 billion ("New EMTN Programme"). The New EMTN Programme is an update of the existing debt securities issue programme implemented by mFinance France.

The debt securities issued as part of the New EMTN Programme may be admitted to trading on the Luxembourg stock exchange and in other European countries. They may also be traded simultaneously on several stock exchanges.

On June 7, 2018, mBank issued four-year bonds with a face value of CHF 180 million and interest of 0.565%. The issued bond tranche was rated BBB+ and BBB by S&P Global Ratings (S&P) and Fitch Ratings (Fitch) respectively. The ratings correspond to the ratings of the EMTN Programme and the long-term ratings of mBank assigned by S&P and Fitch.

The table below presents a summary of outstanding tranches issued by mFinance France and mBank:

Issuer	Date of issue	Nominal value	Maturity date	Coupon
mFinance France	05.09.2013	CHF 200 M	08.10.2018	2.500%
mFinance France	06.12.2013	CZK 500 M	06.12.2018	2.320%
mFinance France	24.03.2014	EUR 500 M	01.04.2019	2.375%
mFinance France	20.11.2014	EUR 500 M	26.11.2021	2.000%
mFinance France	26.09.2016	EUR 500 M	26.09.2020	1.398%
mFinance France	28.03.2017	CHF 200 M	28.03.2023	1.005%
mBank	07.06.2018	CHF 180 M	07.06.2022	0.565%

Process optimisation in Private Banking branches

In order to address the needs of the employees of our private banking branches saying that they were overloaded with operational work, we set ourselves a goal to simplify and standardize customer service processes to give our employees a better sense of comfort and release time that could be used for sales activities.

We started the project with identifying what processes were carried out in branches and estimating the amount of work they required using three groups of positions. Next, we collected all the necessary information and selected the key areas for project work. Optimisation initiatives were implemented in two stages, during which a number of activities were conducted. We organized workshops, devised cooperation rules as well as designed new processes and IT solutions.

We tackled the most time-consuming and complicated process - we have implemented a correspondence circulation system (SOK) and launched a new standardized process for exchanging and archiving documents.

We made an inventory of private banking documents which the employees used to fill in manually. We have also launched a PB documents generator using which the employees can now print the 12 most frequently used aftersales documents.

We have provided the private banking area with a new knowledge base. It was very well received by network employees who expected quality information addressing different aspects of their work in a user-friendly and comprehensive way and in an easy-to-navigate and intuitive form.

2.2. Awards and distinctions

In H1 2018 mBank Group received numerous awards and distinctions, with the most important being:

mBank's mobile application, product offer and customer service quality:

Star of Innovation (Gwiazda Innowacyjności)

Once again we have been awarded in the Stars of Banking competition organized by *Dziennik Gazeta Prawna* daily and PwC. The bank ranked second in the Star of Innovation category (among others in recognition of its application, mobile authorisation and multi-currency card). In the main category honouring growth rate, stability, efficiency, innovation and customer relations mBank came fourth.

Award from moжебankowanie.pl

In Q1 mBank won an award for user-friendly business account opening process in a ranking compiled by moжебankowanie.pl.

Trustworthy Brand (Marka Godna Zaufania)

For the second time mBank won the Trustworthy Brand statuette in the third edition of a poll organized by *My Company Polska* monthly.

We won in two categories: "Bank offering company accounts" and "Bank offering corporate loans". The online poll was conducted in the Polish SME sector by Kantar Millward Brown and covered more than 184 product brands. mBank made it to the elite group of 21 brands given the trustworthy brand title.

Other awards

Three distinctions for mBank in the Golden Banker contest (Złoty Bankier)

In the Golden Banker competition organized by Bankier.pl and *Puls Biznesu* we triumphed in two categories: Socially Responsible Bank (for the book "Mathematics is everywhere. Family adventures with mathematics" published by mFoundation) and Social Media (the best social media appearance). In January mBank made its debut in joining the 26th Grand Finale of the Great Orchestra of Christmas Charity (WOŚP) and was the first in Poland to livestream the event with a "donate" option.

We were also recognised and awarded once again for applying the best security practices. The award was granted not only for the security tools and procedures used at the bank, but also for our additional educational efforts in the area of safe electronic banking. For three years we have been running the Be Cautious Online campaign (Uważni w sieci) raising people's awareness of the threats lurking online and promoting positive behaviours keeping them safe.

The best financing bank award of the Polish Private Equity and Venture Capital Association (Polskie Stowarzyszenie Inwestorów Kapitałowych, PSIK)

In the first edition of the contest mBank received a top honour for being the best financing bank. The contest was organized by the Polish Private Equity and Venture Capital Association, which has been the voice of the PE/VC sector supporting its development since 2002. PSIK embraces private equity and venture capital funds operating in Poland as well as law firms, banks and consultancies active in the PE/VC sector.

The purpose of the contest is to honour the business and social activities of private equity/venture capital funds and promote the achievements of consultancies and banks.

mBank in the Listed Company of the Year ranking (Giełdowa Spółka Roku)

mBank ranked third in the main ranking of the 19th edition of the Listed Company of the Year competition organized by *Puls Biznesu*, while our Investor Relations team came in second.

The contest has not only the longest history but it is also the most prestigious industry ranking. It tells listed companies how they are perceived by the most important market actors (including analysts, brokers and investment advisors).

mBank awarded the Transparent WIG 20 Company of 2017 title

mBank was among the most transparent WIG 20 companies in 2017 in the ranking compiled by *Parkiet* and the Accounting and Tax Institute.

The ranking was compiled based on a survey assessing contestants in areas such as: financial statements and reporting, investor relations and corporate governance.

mBank's press team named the best on the market

In the latest edition of a survey by ARC Rynek i Opinia mBank's press office took the first place. mBank was named the best for its modern (digital) approach, good customer service, professionalism, being recommendable to individual clients, reliable information policy and ability to tackle crisis situations.

The main purpose of the survey of journalists' opinions about banks and their PR activities (conducted every two years by ARC RiO) is to find out the media's opinion and expectations about cooperation with banks' press teams. mBank has been triumphant in similar rankings for several years.

In addition, mBank's management has also been recognised: Mr Cezary Stypułkowski, mBank's CEO, took the third place in the Banker of the Year ranking (Bankowiec Roku) by Forbes.

More information on awards and distinctions is available on the bank's website in the Press Center section: www.media.mbank.pl/.

2.3. Retail Banking

mBank's Retail Banking segment serves 5,508 thou. individuals and microenterprises in Poland, the Czech Republic and Slovakia online, directly through the call centre, via mobile banking and other state-of-the-art technological solutions, as well as in a network of 174 branches*. The Bank offers a broad range of products and services including current and savings accounts, accounts for microenterprises, credit products, deposit products, payment cards, investment products, insurance products, brokerage services, and leasing for microenterprises.



Key financial data (as at the end of H1 2018):

Share in pre-tax profit	Profit before tax	Income
73.2% ↑	PLN 690.7 M ↑	PLN 1,655.4 M ↑

Key highlights

- Core income rose by 9.7% year on year.
- Sales of non-mortgage loans grew by 16.9% year on year to PLN 4.3 billion.
- Sales of mortgage loans increased by 19.3% year on year to PLN 2.1 billion.
- Number of clients grew by 166.1 thou. in 2018.
- Increase in the percentage of sign-in to the mobile application to 59% at the end of H1 2018, compared with 55% at the end of 2017.
- Volume of retail deposits grew by 11.3% year on year, mainly in current accounts (+15.9% year on year).
- Value of transactions made by mBank's payment cards increased by 20.1% year on year with the number of transactions up by 23.1% year on year.

* Including 140 in Poland and 34 in the Czech Republic and Slovakia; excluding mFinanse (41) and mKiosks (131).

Financial results

In H1 2018, the Retail Banking segment generated a profit before tax of PLN 690.7 million, which represents an increase by PLN 238.9 million, i.e. 52.9% compared with H1 2017.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Net interest income	971.1	1 101.4	130.3	13.4%
Net fee and commission income	298.9	291.4	-7.6	-2.5%
Dividend income	0.0	0.0	-	-
Net trading income	54.5	61.3	6.9	12.6%
Net other operating income	-16.5	201.3	217.8	+/-
Total income	1,308.0	1,655.4	347.3	26.6%
Net impairment losses and fair value change on loans and advances	-158.4	-214.0	-55.6	35.1%
Overhead costs and amortization	-599.6	-650.3	-50.7	8.5%
Taxes on bank balance sheet items	-98.3	-100.4	-2.1	2.1%
Profit before tax of Retail Banking	451.7	690.7	238.9	52.9%

The profit before tax of the Retail Banking segment in H1 2018 was driven by the following factors:

- **Increase in total income** by PLN 347.3 million, i.e. 26.6% to PLN 1,655.4 million. Core income increased by 9.7%: net interest income grew by PLN 130.3 million (thanks to a shift towards high-margin products in the credit portfolio structure), while net fee and commission income declined by PLN 7.6 million or 2.5% (higher commissions for loans and for handling payment cards have been balanced out in part by lower commissions for agency service regarding the sale of insurance products offered by external financial entities due to the sale of an organized part of mFinanse acting as an agent in the scope of group insurance). In H1 2018, the financial performance of Retail Banking was greatly impacted by net other operating income (other operating income net of other operating costs), which rose after posting the proceeds from selling an organized part of enterprise of mFinanse in Q1 2018.
- **Increase in operating expenses (including amortisation)** by PLN 50.7 million, i.e. 8.5% year on year, driven mainly by remuneration costs and higher amortisation (+28.1% year on year).
- **Increase in net impairment losses and fair value change on loans and advances** by PLN 55.6 million, i.e. 35.1% year on year, propped up by higher credit volumes and a rising share of unsecured loans in the retail credit portfolio.
- **Tax on the Group's balance sheet items** at PLN 100.4 million.

Business data (mBank only)

thou.	30.06.2017	31.12.2017	30.06.2018	YtD change	YoY change
Number of retail clients, including:	5,233.6	5,342.3	5,508.4	3.1%	5.3%
Poland	4,338.4	4,437.0	4,592.2	3.5%	5.9%
Foreign branches	895.2	905.3	916.2	1.2%	2.3%
The Czech Republic	629.2	633.6	638.3	0.7%	1.5%
Slovakia	266.1	271.8	277.9	2.3%	4.5%
PLN M	,	,	,		
Loans to retail clients, including:	48,731.1	48,122.1	50,513.5	5.0%	3.7%
Poland	44,455.8	43,703.1	45,901.9	5.0%	3.3%
mortgage loans	32,825.7	31,294.8	32,518.2	3.9%	-0.9%
non-mortgage loans	11,630.1	12,408.3	13,383.7	7.9%	15.1%
Foreign branches	4,275.3	4,419.0	4,611.6	4.4%	7.9%
The Czech Republic	3,391.2	3,585.3	3,713.1	3.6%	9.5%
Slovakia	884.1	833.7	898.5	7.8%	1.6%
Deposits of retail clients, including:	54,024.6	55,749.8	59,970.7	7.6%	11.0%
Poland	45,523.2	46,876.5	50,140.0	7.0%	10.1%
Foreign branches	8,501.4	8,873.3	9,830.6	10.8%	15.6%
The Czech Republic	6,046.5	6,346.0	6,999.6	10.3%	15.8%
Slovakia	2,454.9	2,527.3	2,831.0	12.0%	15.3%
Investment funds (Poland)	15,758.2	17,855.0	17,681.5	-0.1%	12.2%
thou.					
Credit cards, including	352.8	362.8	375.0	3.4%	6.3%
Poland	318.9	325.9	335.4	2.9%	5.2%
Foreign branches	33.9	36.8	39.6	7.5%	16.8%
Debit cards, including:	3,566.4	3,713.0	3,774.3	1.7%	5.8%
Poland	3,000.4	3,138.1	3,194.9	1.8%	6.5%
Foreign branches	566.0	575.0	579.4	0.8%	2.4%

¹ The number of retail clients was corrected as a result of obligatory closure of inactive accounts and exclusion of the attorneys-in-fact of micro-enterprises not using the Bank's products as individual clients (respective corrections were also made for previous periods).

² Starting from 2018, the approach to presenting the investment funds held by mBank clients has changed as a result of incorporating mDom Maklerski and mWealth Management into the Bank's structure in 2016.

Retail Banking in Poland

Being a leader of online and mobile banking, mBank focuses on technological innovations which make its processes even more efficient. Having in mind the comfort of using the transaction service, in H1 2018 we embarked on a process to refresh our online banking service for both individuals and small and medium-sized enterprises, and to add new features to our mobile application (for more information about the application, read chapter 2.1 Key projects and innovations in mBank Group in H1 2018).

One of the greatest novelties is Apple Pay. We were one of the first banks to offer our clients payments via Apple devices (iPhone, iPad, iWatch).

Another new feature in our mobile application is *3-D Secure NAM*, which allows clients to authorise 3-D Secure transactions in the mobile application. The clients who use this feature and pay by debit and credit cards online are safer, as thanks to 3-D Secure they receive the authorisation message directly to their mobile application. In addition, there is no need to copy the code sent by a text message to the browser.

Starting from June, clients can open an account during a video chat with our consultant: quickly, without leaving home and with the help from our expert. It can be done anytime, using nothing more than a mobile phone. The new process enables clients to open an account and sign an agreement in the "mobile only" mode, using only their mobile phones. It is especially important for clients living in small towns or having mobility issues for whom a courier had been the only alternative until now. Moreover, clients can now authorise mTransfers by BLIK codes without logging into mBank's application.

Apart from new payment cards which will be discussed later on in this section, we also launched a new payment method in the form of a wristband that can be worn by clients at all times. Every client gets two wristbands (one in black and the other one in red) and a micro-card (a debit card linked to the client's personal account).

In June 2018 mBank concluded a settlement with Orange Polska on terminating the Cooperation Agreement concerning the Orange Finanse Project, the termination will take effect on December 31, 2018.

Retail banking offer for individuals

Loans

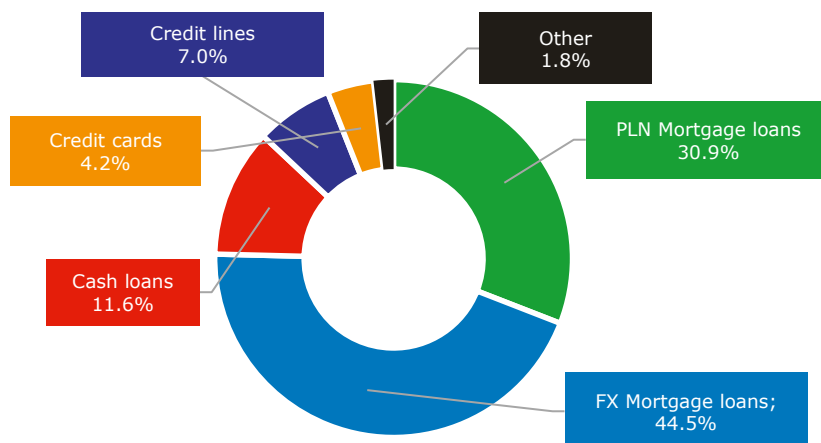
In H1 2018, new sales of non-secured loans to individuals in Poland reached PLN 2,832.7 million, up by 19.7% year on year. In the discussed period, we continued to focus on perfecting our digital sales processes and effectively using channel synergies to build customer relations. At the beginning of the year, we launched new features of our mobile application, such as application/agreement approval (instead of signing a paper-based document), while in Q2 we offered new insurance linked to non-secured loans.

Non-mortgage loans granted to individuals in Poland amounted to PLN 9,599.0 million at the end of H1 2018, compared with PLN 8,274.5 million at the end of June 2017 (+16.0% year on year).

Sales of mortgage loans to individuals went up by 20.4% year on year and stood at PLN 1,623.6 million. At the end of H1 2018, the value of mortgage loans granted to individuals in Poland reached PLN 39,829.1 million compared with PLN 38,779.5 million at the end of June 2017 (+2.7% year on year).

The graph below presents the structure of the Retail Banking loan portfolio in Poland (including mBank Hipoteczny) at the end of H1 2018:

Product structure of Retail Loan Portfolio in Poland



The NPL ratio for mortgage loan portfolio for individuals in Poland has been on a downward trend and stood at 2.9% at the end of June 2018 (against 3.6% in 2017).

Deposits and investment funds

The amount invested in funds available in mBank's Investment Funds Supermarket rose by PLN 233.7 million (5.3%) in H1 2018 despite unfavourable capital market conditions. The increase was driven by clients' growing demand for less volatile investment solutions.

The moderate growth in investment fund assets was accompanied by a strong increase in deposits and core deposits in savings accounts. We continued our efforts to maintain the existing deposit base and attract new deposits.

At the end of H1 2018, retail deposits in Poland amounted to PLN 50,140.0 million compared with PLN 45,523.2 million at the end of June 2017 (up by 10.1% year on year).

Brokerage operations and asset management

The Brokerage Bureau of mBank (BM) provides a comprehensive offer of brokerage services to the largest Polish institutional investors (pension funds, investment funds and asset management companies), foreign funds, and individuals, i.e. retail and affluent clients. The Brokerage Bureau enables clients to trade on regulated markets in Poland and abroad as well as on the OTC (FOREX/CFD) market. As part of wealth management services, clients are offered investment advisory and asset portfolio management services. The Bureau is an active player in the capital market - it prepares and conducts public and private offerings (IPO/SPO/ABB).

In H1 2018, investors' activity on the Warsaw Stock Exchange (WSE) dropped significantly compared with H1 2017, i.e. by 25.1% year on year, which particularly affected the segment of domestic investors. The Bureau's turnover in the WSE's stock market stood at PLN 10.6 billion, i.e. -34.9% year on year, thanks to which mBank ranks tenth in terms of overall turnover (with a share of 4.9%) and fifth as regards turnover on clients' account (with a 6.9% share). On the other hand, investments in foreign markets have enjoyed growing interest among BM clients. At the end of H1 2018, BM clients held 303.9 thou. brokerage accounts.

Despite worse stock market conditions, the value of assets managed by BM increased by 1.3% to PLN 1.4 billion in H1 2018. mFundusz Lokacyjny Plus, the assets of which grew by PLN 150.8 million, was the most popular fund. Its good investment results were appreciated by the website Analizy.pl, which gave it the highest rating (5) in Q2 2018. In H1 2018, client assets accumulated in the mFundusze Dobrze

Lokujące offered by mBank's Retail Banking increased by 19.7% and totalled PLN 484.3 million at the end of the H1. With respect to the portfolios managed by BM, emphasis was put on geographical diversification, mostly based on exchange-traded fund units (an exchange-traded fund is an investment product constituting a kind of an open-end investment fund designed to follow movements in stock market indices, prices of raw materials or a basket of other assets, e.g. shares or bonds).

H1 2018 was marked by a limited number of capital market transactions. During that time, BM acted as an intermediary in six public calls for shares, buybacks and squeeze outs worth PLN 1,262.9 million in total, e.g. with regard to the shares of Emperia Holding S.A. (PLN 1,191.4 million), AviaAM Leasing S.A. (PLN 43.9 million) and Prochem S.A. (PLN 24.0 million). BM was among the market leaders in that period in terms of the number of announced calls for shares.

Cards

In H1 2018, we launched new special edition Visa debit cards celebrating the FIFA World Cup and a MasterCard debit card designed by Jurek Owsiak's Foundation to celebrate the Pol'and'Rock Festival available for a limited time only.

Affluent clients were offered the new Visa Intensive and MasterCard Intensive payment cards and the new World MasterCard Intensive credit cards.

With new types of blocks, such as the temporary card block, block on contactless payments and block on foreign transactions, the management of payment cards has become easier than ever before. We reduced the number of authorisation limits. For more information about the new features, see section 2.1. Key projects and innovations of mBank Group in H1 2018.

In H1 2018, payment card purchases made by mBank's retail clients in Poland amounted to PLN 17.7 billion, which represents an increase by 20.1% year on year. The number of transactions made by mBank's clients rose by 23.1% year on year. mBank's credit cards are characterized by a high average number of transactions per card. At the end of March 2018, the share of transactions by mBank's cards in the total number of card transactions in Poland stood at 12.5%.

Products and services for affluent clients

We launched the new mKonto Intensive for affluent clients towards the end of June 2018. Clients holding such accounts can make three instant transfers per month free of charge. They also enjoy free cash withdrawals from ATMs all over the world, priority service in the call centre and discounts on third-party liability and comprehensive motor insurance. The account is offered with the new Visa Intensive and MasterCard Intensive payment cards.

Holders of mKonto Intensive accounts can also select the new World MasterCard Intensive credit card. Currency conversion for transactions made abroad and cash withdrawals from ATMs all over the world are always free of charge. Clients can also join the Priceless Specials programme and earn points for everyday payments in Poland and abroad. They can spend the points on airline tickets, accommodation, shopping vouchers for the best shops and many more. The cards are available only to the holders of mKonto Intensive accounts.

The changes in the portfolio of current accounts and cards should enable mBank to even better adjust its offer to the needs of affluent clients.

Offer for small and medium-sized enterprises

H1 2018 was marked by intensive marketing campaigns related to, among other things, the launch of the new service called "Firmootwieracz", which has been used by 4,695 companies.

The service was introduced in Q1 2018 and is an integrated and fully online process enabling clients to set up a business in just 10 minutes. The project is yet another example of cooperation between mBank and public authorities producing client-friendly solutions. It is an expansion of the one stop shop concept transferred to the electronic world. The service is yet another evidence of our friendly approach to business customers. Since the end of February an individual who enters our bank can leave it as a businessman/businesswoman.

The area of financing provided to small and medium-sized enterprises saw a 18.9% year on year increase in the sales of non-mortgage loans in H1 2018. We introduced a new credit application form for SMEs in the mobile application, making it possible to apply for a loan from any place. Clients who send an online credit application wait only three minutes to have the money transferred to their account.

Sales of long-term mortgage loans increased by 10.8% against the same period last year. The growth is an effect of implemented credit process optimisations, especially the mAssistant (mAsystent) - an intuitive credit application form that selects the credit product that best suits the client's needs.

In early March, we added the Currency Counter (Licznik Walutowy) service to our Currency Platform (mPlatforma Walutowa). Clients who use the service can earn points for currency exchange transactions and spend them on free wire transfers in foreign currencies. We are the second financial institution on the market to offer free wire transfers in foreign currencies to clients who actively use the currency exchange service.

Moreover, we started to offer payment terminals within the Cashless Poland programme (Polska Bezgotówkowa). Since April 16, our retail clients have been able to order up to three terminals. They do not pay interchange fees for 12 months and enjoy a free subscription period of up to 24 months.

Since H1 2018, our business clients have been able to order a Visa Photo Business card. The card may feature the logo of a business and thus serve as an advertising tool that one can use to promote their firm while shopping or paying for business dinners. Work on EUR and USD foreign currency cards is underway.

The continuous enhancement of the offer for businesses with new products and improvement of the already existing products were appreciated by both the market and clients. In H1 2018, mBank received its second "Trusted Brand Award" winning in two categories ("Bank offering company accounts" and "Bank offering company loans").

Mobile application

In H1 2018, we changed and added new features to our mobile application launched in February 2014 and redesigned in 2017 when it was made easier to navigate and upgraded (for more information about the application, see section 2.1. Key projects and innovations of mBank Group in H1 2018).

Cooperation with AXA Group

mBank's cooperation with AXA, our strategic partner in insurance, regarding bancassurance started in 2015. We have been cooperating in selling products attached to banking products, e.g. to credit products of different type, and standalone products, such as motor insurance, travel insurance, home insurance and life insurance.

As planned, in Q2 2018, after a review of the existing offer, mBank changed its portfolio of insurance products attached to loans and real property insurance products addressed to individuals, replacing them with new products for individuals to offer clients even better terms and conditions and increase sales in the years to come. The offer has been refreshed further since then.

Retail Banking in the Czech Republic and Slovakia

In H1 2018, the activities of mBank in the Czech Republic and Slovakia continued to be focused on non-mortgage lending enhancement and optimisation of processes related to NML products. The branches completed several projects aimed at sales capacity extension and sales processes fine-tuning. New solutions were introduced, expanding and improving the product offer for the clients.

mBank continued to strengthen its position of a mobile banking leader. Q1 2018 was marked by further development of mobile banking, which started to offer new features such as loan granted based on the pre-approved creditworthiness assessment as well as the option to open current account mKonto via mobile application. Together with the refreshed interface and new features (such as fingerprint and face ID login and Android Pay), the new application fully follows the key pillars of the Group's strategy: mobility, simplicity and empathy. Almost 15 thou. clients started to use Google Pay within 6 months after the launch of the new application in the Czech Republic. In Slovakia Google Pay has been launched in February and mBank is the only bank on this market with this service directly integrated into its own mobile application.

The activities of the branches in the Czech Republic and Slovakia were also focused on active customer acquisition with 21.0 thou. new customers attracted in H1 2018 (including 11.9 thou. in Slovakia and 9.1 thou. in the Czech Republic). At the end of H1 2018, mBank served 916.2 thou. customers in both markets. Following the customer-centricity approach a new flagship "light branch" was opened in Prague in May allowing for closer relationships with the customers.

As a result of the strategic partnership with Broker Consulting, a Czech independent financial services agent, 22 co-branded advisory outlets (OK points) specialising in banking services were newly opened. At the end of June 2018, the number of OK points reached 40. At the same time, 40 depository machines were installed as part of the cooperation. The expansion of OK points and the CDM network will continue during the rest of 2018, owing to their popularity with clients. In the meantime, the partners are in talks about a possible extension of the cooperation to Slovakia.

The activities of mBank in the Czech Republic and Slovakia won several major awards in H1 2018. mBank performed excellently in the Czech Zlatá koruna (Golden Crown) contest. It won a total of 5 awards, including the main awards in the two most important categories - Retail Clients' Choice and Entrepreneurs' Choice. The mortgage loan won gold award and mKonto silver award in the Finparáda - financial product of the year contest. The contest is based on the analysis of annual market data carried out by Scott & Ross. The Czech branch of mBank won another Superbrands award third time in a row, while the Slovak branch won Superbrands award for the second time. The awards confirm mBank's place among the strongest brands in both countries.

Loans and deposits

At the end of H1 2018, the loan portfolio of mBank in the Czech Republic and Slovakia stood at PLN 4,611.6 million, which represents an increase by 7.9% year on year. Mortgage loans portfolio as at the end of June 2018 amounted to PLN 3,705.7 million, meaning +3.6% compared to the end of June 2017.

In the mortgage loans area we focused on sales recovery in Slovakia impacted by the introduction of bank tax in Poland and on the improvement of the level of sales in the Czech Republic. There was a clear year on year change in mortgage sales in Slovakia with new sales in H1 2018 reaching PLN 66.6 million, representing a record-high increase by 219.0% year on year. The branch in the Czech Republic continues positive growth trend (+4.2% year on year). Overall new sales of mortgage loans in H1 2018 stood at PLN 340.2 million, which represents an increase by 20.0% in comparison with H1 2017. The volume of mortgage loans portfolio increased by PLN 129.9 million year on year (i.e. +3.6%).

Thanks to several new activities in the non-mortgage loans area and continuing trend in product and process improvements, the bank managed to significantly strengthen its NML portfolio, which at the end of June 2018 stood at PLN 905.8 million, i.e. +29.5% year on year. New sales of non-mortgage loans decreased slightly by 3.0% compared with H1 2017.

The volume of deposits continued to grow in 2018 to reach PLN 9,830.6 million at the end of June 2018 (up by 10.8% compared to the end of 2017 and by 15.6% compared to the end of June 2017).

In the area of payment cards branches supported cards usage by several campaigns leading to increased number of transactions by 12.5% in the Czech Republic and 17.1% in Slovakia compared to H1 2017.

2.4. Corporates and Financial Markets

The Corporates and Financial Markets segment serves 22,934 corporate clients including large enterprises (K1 - annual sales exceeding PLN 1 billion and non-banking financial institutions), mid-sized enterprises (K2 - annual sales of PLN 50 million – 1 billion) and small enterprises (K3 - annual sales below PLN 50 million), through a network of dedicated 46 branches. mBank Group's offer of products and services for corporate clients focuses on traditional banking products and services (including corporate accounts, domestic and international money transfers, payment cards, cash services, and liquidity management products), corporate finance products, hedging instruments, equity capital market (ECM) services, debt capital market (DCM) instruments, mergers and acquisitions (M&A), leasing and factoring. The segment comprises two areas: Corporate and Investment Banking, and Financial Markets.



Key financial data (at the end of H1 2018):

Share in pre-tax profit	Pre-tax profit	Total income
28.0% ↓	PLN 264.5 M ↓	PLN 931.3 M ↑

Key highlights

- Increase of core income by 7.7% compared to H1 2017.
- Increase in corporate loans by 7.1% compared to H1 2017.
- Increase of corporate deposits by 14.1% compared to H1 2017.
- Acquisition of 1.4 thou. new corporate clients corporate to the end June 2017.
- Increase of mBank's market share on the market of bills and treasury bonds to 17.3% (16.6% in H1 2017) and to 12.3% (from 10.0% in H1 2017) on IRS/FRA market.
- First and largest covered bonds issue of mBank Hipoteczny in the total amount of EUR 300 million on the European market.
- Introduction of a new innovative product – light depositories at the customer's premises – aimed at further digitalisation of the cash service process.
- Introduction of electronic escrow account, enabling opening, running and settlement of transactions on the escrow account without signing the paper account agreement. It is the first mBank's transactional system, serving both retail and corporate clients.

Corporate and Investment Banking

Financial results

In H1 2018, the Corporate and Investment Banking segment generated a profit before tax of PLN 230.2 million. This result marked an increase by PLN 19.1 million or 9.0% year on year.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Net interest income	391.7	440.1	48.4	12.4%
Net fee and commission income	200.1	231.5	31.5	15.7%
Dividend income	0.0	0.0	0.0	-
Net trading income	118.6	125.5	6.9	5.8%
Gains less losses from financial assets and liabilities not measured at fair value through profit or loss and investments in subsidiaries and associates	-7.0	0.2	7.2	+/-
Net other operating income	10.9	24.5	13.6	124.7%
Total income	714.3	821.7	107.4	15.0%
Net impairment losses and fair value change on loans and advances	-47.8	-124.4	-76.6	160.1%
Overhead costs and amortization	-386.7	-391.8	-5.1	1.3%
Taxes on bank balance sheet items	-68.6	-75.3	-6.7	9.8%
Profit before tax of Corporate and Investment Banking	211.2	230.2	19.1	9.0%

The profit before tax of the Corporate and Investment Banking in the period under review was driven by the following factors:

- **Growth in income** by PLN 107.4 million or 15.0% year on year. Core income went up by 13.5% year on year and operating income by PLN 13.6 million or 124.7%. (sale of real property by Garbary sp. z o.o.).
- **Higher operating costs (including amortization)** at PLN 391.8 million in the period under review.
- **Higher net impairment losses and fair value of loans and advances**, up by PLN 76.6 million or 160.1% against H1 2017 due to creation of provisions for several large exposures in Q2 2018. In addition, H1 2017 was marked with particularly low provisions.
- **Tax on the Group's balance sheet items** at PLN 75.3 million.

Business results (mBank only)

	30.06.2017	31.12.2017	30.06.2018	YtD change	YoY change
Number of corporate clients	21,500	22,048	22,934	4.0%	6.7%
K1	2,119	2,093	2,148	2.6%	1.4%
K2	6,835	7,088	7,551	6.5%	10.5%
K3	12,546	12,867	13,235	2.9%	5.5%
PLN M					
Loans to corporate clients, including	22,324.9	23,010.6	23,911.6	3.9%	7.1%
K1	5,115.9	5,316.9	6,150.9	15.7%	20.2%
K2	14,124.1	14,529.7	15,308.4	5.4%	8.4%
K3	2,863.7	2,973.0	2,311.0	-22.3%	-19.3%
Reverse repo/buy sell back transactions	93.8	57.1	29.0	-49.2%	-69.1%
Other	127.4	133.8	112.4	-16.0%	-11.8%
Deposits of corporate clients, including	29,833.5	31,425.5	34,048.5	8.3%	14.1%
K1	11,605.4	11,999.2	15,311.1	27.6%	31.9%
K2	12,038.5	13,483.3	11,758.9	-12.8%	-2.3%
K3	4,768.2	5,079.0	5,329.0	4.9%	11.8%
Repo transactions	1,034.6	439.6	1,137.5	158.7%	9.9%
Other	386.9	424.4	511.9	20.6%	32.3%

H1 2018 was a time of moderate economic growth, which translated into stronger consumption and public investment. Nevertheless, it did not have a major impact on the improvement of business activity and financial results of large companies. Moreover, banks had to operate in an environment of record-low interest rates, reduced interchange fees, increased contributions to the Bank Guarantee Fund (BFG) as well as the banking tax and uncertainty about the size of the potential financial burden arising from CHF loans.

The volume of corporate loans and deposits increased in H1 2018. The corporate loans market grew by 7.0% year on year and the corporate deposits market by 6.5%. In this context, mBank reported higher growth in loan volumes (10.1%) and a slightly lower increase in deposit volumes (5.7%). At the end of H1 2018, mBank's shares in the markets of corporate loans and deposits reached 9.5% and 6.5%, respectively.

In H1 2018, the Bank intensified its efforts to attract new corporate clients, which yet again resulted in high acquisition of new companies – the corporate client base increased by 1,434 companies year on year, reaching the level of 22,934 clients.

The acquisition of new clients boosted the balances deposited in current accounts, which stood at PLN 13,063.2 million at the end of June 2017, representing a decrease by 3.5% year on year. The high volume of current deposits is a springboard for further development of transactional banking, which is of special relevance to the Bank due to the growth potential and forging of closer relations with clients.

In H1 2018, mBank's small and medium-sized enterprises (SMEs - K3) segment acquired 1,600 new clients, which represents an increase by over 40% year on year. More than 65% of new clients opted for

the package offer addressed to this segment. It is worth mentioning that more than twice as many factoring clients were acquired as in H1 2017.

In the period under review, mBank launched two marketing campaigns targeting the SMEs segment. The first one promoted the offer of "Heart-to-heart account" ("Rachunek na dwa serca") aimed at providing extra support to the Great Orchestra of Christmas Charity (WOŚP). The other one, "Frozen VAT" ("Zamrożony VAT"), was addressed to clients seeking additional funding due to introduction of the split payment mechanism in Poland. Clients can use selected financial products offered by mBank under preferential conditions. The offer has attracted great interest.

mBank's corporate banking was praised by the Global Finance international magazine. mBank won the competition and was named the Best Treasury and Cash Management Provider in Poland.

The key objective of Corporate and Investment Banking will be to ensure dynamic development of the Bank in the K3 segment and maintain a strong position in the K2 segment. Moreover, we want to place a great emphasis on further streamlining and simplification of the credit process, documentation, account opening process and introduction of new transactional packages alongside a number of improvements to enhance the client's everyday comfort.

Products and services

Corporate loans

The value of loans granted by mBank to corporate clients (excluding reverse repo transactions) stood at PLN 23,882.6 million at the end of June 2018, representing an increase by 7.4% compared with the end of June 2017 (PLN 22,231.1 million).

PLN M	30.06.2017	31.12.2017	30.06.2018	YoY change
Loans to corporate clients ¹	20,817	22,954	23,883	14.7%
Loans to enterprises ²	19,950	21,969	23,547	18.0%
Loans granted to local governments	708	550	468	-33.9%
Market of loans to enterprises	324,817	344,875	363,519	
mBank's share in the market of lending to enterprises	6.1%	6.4%	6.5%	

¹ Excluding reverse repo transactions.

² NBP category which ensures comparability of results of the banking sector.

Corporate deposits

The value of corporate deposits at mBank (excluding repo transactions) stood at PLN 32,910.9 million at the end of June 2018, up by 14.3% compared with the end of June 2017 (PLN 28,798.9 million).

PLN M	30.06.2017	31.12.2017	30.06.2018	YoY change
Corporate deposits ¹	31,703	30,986	32,911	3.8%
Deposits of enterprises ²	28,450	27,909	26,304	-7.5%
Deposits of local governments	237	506	1,732	7.3x
Market of deposits of enterprises	282,215	231,941	276,006	
mBank's share in the total deposits of enterprises	10.1%	9.6%	6.5%	

¹ Excluding repo transactions.

² NBP category which ensures comparability of results of the banking sector.

De minimis guarantee

The bank continued to participate in the Portfolio Guarantee Line De Minimis (PLD) Agreement as part of the government's "Supporting Entrepreneurship through BGK Sureties and Guarantees" programme. As at June 30, 2018, the amount drawn under the limit reached PLN 2,471.4 million.

On June 25, 2018, mBank signed another Portfolio Guarantee Line De Minimis Agreement (PLD-KFG), being a continuation of the previous agreement (PLD), with an allocated limit for guarantees at PLN 600 million.

COSME

mBank continued to offer the portfolio guarantee line with a counter-guarantee provided by the European Investment Bank under the COSME programme (a European Union programme supporting the competitiveness of enterprises in 2014-2020). The BGK guarantee limit for mBank stands at PLN 550 million. As at June 30, 2018, the amount drawn under the limit reached PLN 294.5 million.

Corporate debt origination

The share of mBank in the non-treasury debt securities market at the end H1 2018 is presented in the table below.

	Short-term debt	Corporate debt	Mid-term bank debt
mBank (PLN M)	1,383	8,725	13,909
Market (PLN M)	14,674	69,792	50,785
Market share	9.4%	12.5%	27.4%
Market position	#4	#3	#1

The largest transactions in H1 2018 included bond issues worth a total of PLN 300 million and PLN 250 million for Bank Gospodarstwa Krajowego.

Other large value transactions arranged by mBank included: PLN 45 million for Santander Bank and bond worth PLN 40 million for mBank Hipoteczny.

In the corporate bonds market, the Bank carried out a series of new issues, i.e.: CCC (PLN 210 million), Echo Investment (PLN 140 million), EFL (PLN 50 million), Polnord (PLN 40 million), BBI Development (PLN 40million).

Transactional banking

Cash management is an area of Corporate Banking offering state-of-the-art solutions to facilitate planning, monitoring and management of highly liquid assets, cash processing, as well as electronic banking. The solutions facilitate daily financial operations, enhance effective cash flow management, and optimise interest costs and income.

mBank's comprehensive cash management offer, supporting long-term relationships with clients, is reflected in the following data:

Number of outgoing foreign transfers	+6.2%
Number of incoming foreign transfers	+18.4%
Number of corporate cards	+12.2%
Number of prepaid corporate cards	+60.3%
Number of mCompanyNet users	+3.0%

Electronic escrow account

It is an electronic platform allowing for opening, holding and settling escrow account transactions without the need to sign paper-based agreements or leave home. Using the platform, clients can easily secure and settle transactions that carry a certain degree of risk. The service process is fully automated, fast and smooth.

Electronic escrow account is the first transactional system offered by mBank that serves both corporate and retail clients. It is integrated with a new transactional system of mBank and mBank CompanyNet where all available functions are fully mobile.

Digitalised cash management process - cash deposit machines on client's premises

In an effort to digitalise its banking service, mBank launched a non-standard solution based on dedicated devices allowing clients to quickly and comfortably deposit cash in their mBank accounts. Installed in a location agreed between a client and the bank, a cash deposit machine allows for making open cash deposits in banknotes and coins in any currency and denomination. The machine performs full automatic verification and identification of deposited funds.

Mobile authorisation

Mobile authorisation is a new, convenient and safe way of logging into mBank CompanyNet or authorising instructions in the system. The operations are executed in a dedicated application installed on smartphones with Android or iOS operating system.

Clients have been offered a convenient and safe solution allowing them to quickly authorise clearly presented operations. There is no need for cyclical replacements of an authorisation device as the application is installed on a client's mobile. Compared to a standard token, the new solution is less expensive and involves no costly logistics.

Administrator's Centre

Working towards digitalisation of processes between the Bank and its clients, we added the Administrator's Centre in mBank CompanyNet. The centre allows clients to manage users, e.g. quickly add a new user or define his/her authorisations in a simplified and convenient manner.

Ultimately, all clients will have users with administrative privileges, which will enable them to not only manage parameters in mBank CompanyNet, but also to apply for banking products without the need to deliver paper-based documentation.

Financial Markets

Financial results

The Financial Markets segment generated a pre-tax profit of PLN 34.3 million in H1 2018, compared with PLN 40.8 million a year earlier (down by 16.0%).

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Net interest income	147.3	125.2	-22.2	-15.1%
Net fee and commission income	-3.6	-4.4	-0.8	21.2%
Dividend income	0.0	0.0	0.0	-
Net trading income	-34.5	-16.2	18.3	-53.0%
Gains less losses from financial assets and liabilities not measured at fair value through profit or loss and investments in subsidiaries and associates	2.8	6.0	3.2	113.2%
Net other operating income	-1.6	-1.0	0.6	-37.4%
Total income	110.5	109.6	-0.9	-0.8%
Net impairment losses and fair value change on loans and advances	2.1	-0.2	-2.2	-/+
Overhead costs and amortization	-57.3	-57.1	0.2	-0.3%
Taxes on bank balance sheet items	-14.5	-18.0	-3.6	24.8%
Profit before tax of Financial Markets	40.8	34.3	-6.5	-16.0%

The pre-tax profit of the Financial Markets segment in H1 2018 was driven by the following factors:

- **Stable income** compared with H1 2017, at the level of PLN 109.6 million, dropping by only 0.8% year on year. Decrease in core income by 16.0% caused by a lower net interest income. At the same time, net trading income increased by PLN 18.3 million or 53.0%, which was attributable to higher income from interest rate derivatives.
- **Negative value in the "Net impairment losses and fair value of loans and advances"** item compared with a positive balance of loan loss provisions in H1 2017 (i.e. PLN 2.1 million compared with -PLN 0.2 million in H1 2018).
- **Stable operating costs (including amortisation)** at PLN 57.1 million.
- **Increase in tax on the Group's balance sheet items** to PLN 18.0 million (by 24.8%).

Activity of Financial Markets

Since January 2018, the activities of the financial market products sales area have been focused on maintaining the current market share in the sales of derivatives upon the implementation of MIFID II.

Additionally, the Financial Markets Sales Department undertook activities aimed at increasing the number of transactions concluded and income generated from the Bank's cooperation with customers, including the following:

- In H1 the Financial Markets Department focused on the integration of the sales teams in order to increase economies of scale and guarantee higher substitutability while at the same time decentralizing product specialists who should now be closer to customers.
- Market fluctuations and conversion of deposit customers to mCompanyNet platform brought about a 7.1% increase in the margin generated by the platform v. the same period last year, whereas the turnover of transactions went up by 0.7% year on year.

- The margins on transactions executed by phone grew by 12.7% year on year, with a 6.2% decrease in the transactions' turnover and a 20.7% increase in their number.
- The Derivative Instruments Division offering commodity derivatives to corporate customers undertook various initiatives to attract customers by promoting acquisition and the bank's participation in meetings important to the commodity sector representatives.

These activities conducted in H1 2018 resulted in an approximately 45% increase of the portfolio of active customers concluding transactions hedging against fluctuations in commodity prices compared with the customer base as at end of 2017.

In the Financial Markets segment, the new Retail Sales Division was established. It is responsible for cooperation with Retail Banking customers - sole traders and Private Banking clients - in the scope of financial markets.

The bank's brokers' team responsible for the Private Banking clients increased the base by 161 active customers. Intensive acquisition measures resulted in an increase in margins (+79.3%) and a higher turnover of transactions (+63.2%) year on year.

mBank's market shares in various financial instrument markets as at May 31, 2018 are presented below:

	Treasury bills & bonds	IRS/FRA
mBank	17.3%	12.3%

Financial Institutions

The Financial Markets area covers relations with financial institutions, focusing mainly on raising capital from other banks and depositing excess funds with them.

As the end of June 2018 mBank had 16 active loans in the amount of PLN 14,035 million, of which the utilized value stood at PLN 7,541 million. In H1 2018, one loan in CHF amounting to PLN 1,320 million and one loan in USD amounting to PLN 187 million were repaid at maturity. Additionally, the bank took out one new loan in USD in the total amount of PLN 187 million. The bank's total debt under loans from other banks was by PLN 3,000 million lower than at the end of H1 2017. At the exchange rates from the end of H1 2017, the decrease would amount to PLN 49 million.

At the end of June 2018, mBank's total exposure resulting from loans granted to other banks amounted to PLN 167.3 million (the total exposure at the end of June 2017 amounted to PLN 128.3 million). mBank's portfolio comprised 13 short- and medium-term active loans granted to financial institutions from Poland and abroad.

The greatest accomplishments of the Financial Institutions Department in H1 2018 include:

- obtaining further, considerable funding in the amount of USD 50 million from Wells Fargo Bank, N.A., and
- further acquisition of several loro accounts as well as maintaining the Bank's position as one of the leading Polish banks in handling settlements in PLN,
- Opening nostro account in Croatian kuna (HRK).

Moreover, in H1 2018 the Financial Institutions Department continued to actively support trade transactions concluded by Polish exporters by offering short-term financing to financial institutions, as well as granted financing as part of syndicated loans. At the same time, the bank was still serving banks from the Commonwealth of Independent States (CIS) and offering them medium-term loans secured with KUKE insurance policies.

mBank's custody services

mBank provides services including settlement of transactions in securities registered in domestic and foreign markets, safe-keeping of clients' assets, maintenance of securities accounts and registers of securities in non-public trading, maintenance of asset registers of pension funds and investment funds, monitoring the valuation of their assets as well as performing operations related to benefits arising from

securities. mBank's custody clients are mainly financial institutions, including in particular investment and pension funds, domestic and foreign financial institutions, banks which offer custodian and investment services, insurance companies, asset management institutions, and non-financial institutions.

As at June 30, 2018, the number of investment funds served by mBank dropped by 17.9% year on year. The decrease resulted from the continuation of changes in the structure of the portfolio of clients served by the Custody Department. In particular, the drop was reported for non-public assets funds.

2.5. Subsidiaries of mBank Group

Summary of financial results of mBank Group subsidiaries

The overall H1 2018 result of mBank Group subsidiaries of PLN 378.5 million was impacted by the completion of the sale of an organized part of enterprise of mFinanse.

The table below presents the profit before tax posted by individual subsidiaries in H1 2018 against H1 2017.

PLN M	H1 2017	H1 2018	Change in %
mFinanse (former Aspiro) ¹	72.1	305.0	322.9%
mBank Hipoteczny	17.0	23.4	37.7%
mLeasing	33.9	19.4	-42.8%
mFaktoring	5.3	11.8	125.2%
mLocum ²	22.1	0.0	-
Other ³	-3.3	18.9	+/-
Total	147.1	378.5	157.2%

¹ Pre-tax profit in H1 2018 including the sale of an organized part of enterprise of mFinanse.

² On June 2, 2017, mBank concluded a preliminary conditional agreement on the sale of mLocum shares to Archicom. The 51% stake in the subsidiary was sold in Q3 2017.

³ Other subsidiaries include mFinanse France, mCentrum Operacji, BDH Development, Garbary, Tele-Tech Investment and Future Tech.

Business activity of selected subsidiaries



In H1 2018, mFinanse posted an increase in mortgage loan sales of 21.5% year on year (PLN 1,074.4 million in H1 2018 v. PLN 884.4 million in the same period last year). The increase in the mortgage loan volume is attributable to the policy of mFinanse's strategic partner - mBank. Reduced prices of mortgage loans offered by mBank resulted in growth in the number of credit applications and, thus, originated loans. Sales of cash loans rose as well in H1 2018. They stood at PLN 323.7 million, up by 53.5% from PLN 210.9 million in H1 2017.

The sales of car loans dedicated to car dealers rose compared with the same period last year (PLN 163.1 million in H1 2018 compared with PLN 141.5 million in H1 2017). The subsidiary's sales results in the area of car leasing improved (PLN 58.9 million in H1 2018 compared with PLN 26.7 million in H1 2017).

In H1 2018, the subsidiary generated a profit before tax in the amount of PLN 305.0 million compared with PLN 72.1 million in H1 2017. The increase is attributable to the sale of an organized part of enterprise of mFinanse.



The total value of contracts executed in H1 2018 amounted to PLN 2,952.5 million compared to PLN 2,354.2 million in H1 2017 (+25.4%).

The value of new movable assets purchased by mLeasing in H1 2018 reached PLN 2,881.5 million, up by 29.3% year on year. In H1 2018, the subsidiary financed real estate worth PLN 71.0 million, down 43.7% compared to H1 2017.

The profit before tax reported by mLeasing in H1 2018 stood at PLN 19.4 million, which represents a 42.8% decrease year on year. The drop was mainly driven by higher cost of risk and financing (which include the bank tax).

Bank Hipoteczny

mBank Hipoteczny (mBH) is a regular issuer of covered bonds with the longest track record in the Polish capital market. As at the end of H1 2018, the total value of outstanding mortgage bonds issued by mBank Hipoteczny amounted to PLN 7,510.8 million.

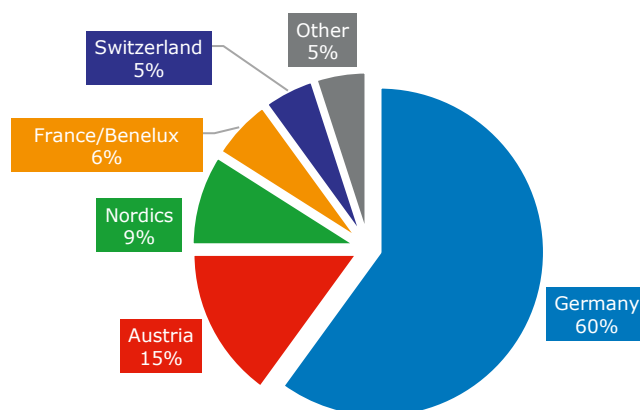
In H1 2018, mBank Hipoteczny issued mortgage bonds worth EUR 300 million and PLN 300 million within its International Mortgage Bond Issue Programme and Domestic Mortgage Bond Issue Programme respectively. The issuing activity of mBH in H1 2018 is summarized in the table below.

Volume	Currency	Issue date	Maturity	Tenor (in years)	Coupon
300 M	EUR	26.04.2018	05.03.2025	7	1.073% (mid-swap rate + 42bps)
300 M	PLN	22.06.2018	10.06.2024	6	WIBOR3M+58bps

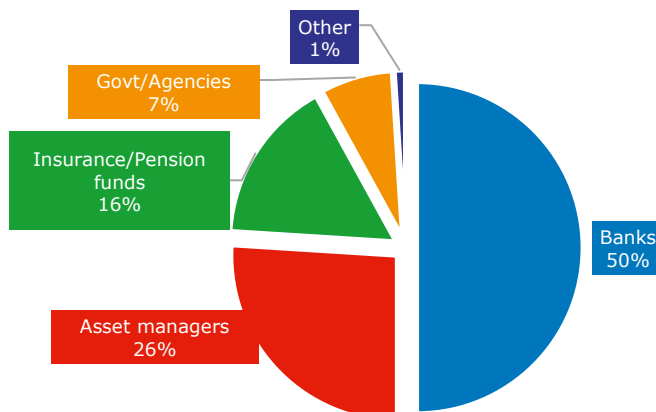
The issue worth EUR 300 million, or ca. PLN 1,250 million equivalent, has been the biggest issue in mBH's history. For mBank Group it has been the debt issue with the longest maturity and most favourable placement conditions in the international market to date. More than 60 investors declared to purchase mBH's covered bonds worth jointly over EUR 800 million (2.7x value of the placed issue).

The transaction structure by geographic distribution and by investors after allocation is presented below:

Distribution by investor location



Distribution by investor type



The covered bonds worth PLN 300 million were issued within the Domestic Covered Bond Issue Programme providing for a new distribution model. mBank was responsible for book building for the part of the offer

addressed to Polish institutional investors, while Erste Group Bank AG generated, captured and recorded the demand from foreign investors.

Twenty-three investors bid for covered bonds worth a total of PLN 577 million (i.e. over 1.9x value of the offer) using their services. The issue was placed with asset management institutions (72%), banks (17%) as well as insurance companies and pension funds (12%). The majority of investors came from Poland (83%), the Czech Republic, Germany and Austria.

In addition, mBH continues to issue unsecured bonds. At the end of H1 2018, 7 series of unsecured bonds worth a total of PLN 490 million were issued. mBH offers zero-coupon and coupon bonds denominated in PLN with maturities ranging from two months to one year.

mBH's gross loan portfolio totalled PLN 11.2 billion in H1 2018 compared with PLN 10.3 billion at the end of H1 2017 (+8.9%). The method for supplying mBH with retail assets changed following the transfer of retail mortgage loan sales to mBank in July 2017. Two pooling transactions took place in H1 2018, as part of which mBH purchased retail receivables in the total amount of PLN 307 million from mBank. Sales of commercial loans stood at PLN 913.9 million in H1 2018.

mBH's profit before tax increased by 37.7% compared with the same period last year (to PLN 23.4 million from PLN 17.0 million in H1 2017) despite the substantial bank tax charge of PLN 13.6 million. The increase in profit in H1 2018 was driven mainly by a reduction in staff-related expenses following the transfer of retail mortgage loan sales and a part of related FTEs to mBank. In addition, mBH posted lower fee and commission expenses (in particular lower agency costs) and a higher net interest income thanks to an increase in the portfolio and interest income resulting from higher commercial loan prepayments.

Faktoring

The amount of invoices purchased by the subsidiary stood at PLN 8.5 billion in H1 2018. This marks a record-high increase (+40.2%) compared with the same period of 2017 and exceeds the average growth rate of the market announced by the Polish Factors Association (29.2%). The significant growth in the amount of purchased invoices secured the subsidiary the sixth place in the Polish factoring market.

The growth coupled with cost discipline allowed the company to achieve a high profit. It earned a profit before tax of PLN 11.8 million in H1 2018, up by 125.2% compared with H1 2017.

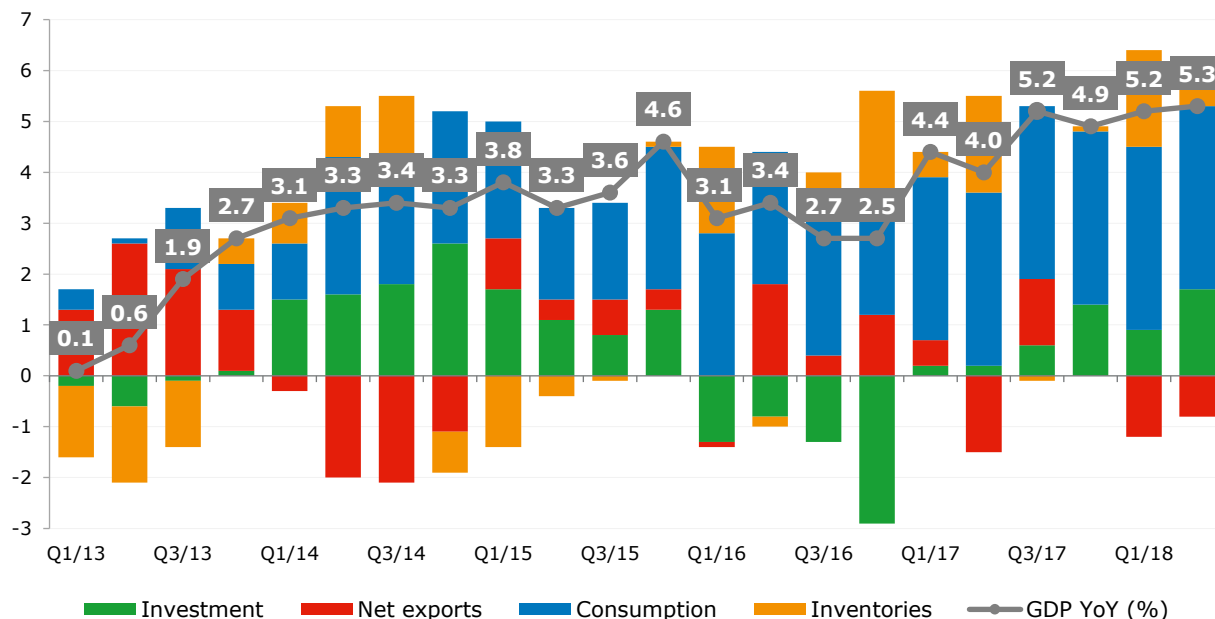
3. Financial results and macroeconomic environment

3.1. Economy and banking sector in H1 2017

Stable economic growth in H1 2018

During the first six months of 2018 the economy picked up again and grew at a pace exceeding 5.0% year on year. In Q1, economic growth reached 5.1% year on year and the Bank estimates (based on higher frequency data) that in Q2 it might reach 5.3%-5.4% year on year, thus making H1 2018 probably the best six months for the Polish economy since 2008.

Contribution to GDP growth



The available data suggest that private consumption, up by 4.8% in Q1 and by approx. 5.0% in Q2, is still the main driver of economic growth. Buoyant private consumption is evidenced by retail sales figures, record-high consumer sentiment in Poland and the continuing solid growth in real income of households. Moreover, robust consumer spending is also helped by favourable conditions on the labour market (with the unemployment rate dropping to a new record low month by month). The Bank reckons that the spending spree is fuelled mainly by higher income base funding consumption with the share of debt remaining stable for years. All this shows that the observed consumption trends are long-lasting and suggests that the end of the consumption cycle is still way ahead. Another important yet underestimated factor triggering higher consumer spending over the last few years is economic immigration to Poland.

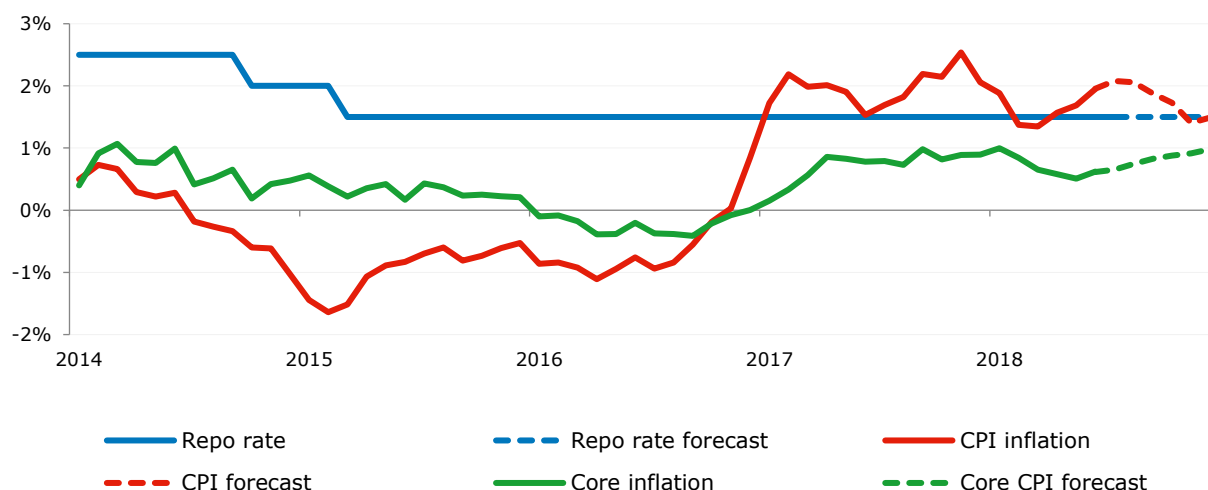
Investments, which were likely to rise by more than 9.0% year on year from January to June, made a solid contribution to economic growth in H1 2018. They were driven predominantly by public sector spending from both government and local government institutions as well as companies in which the state holds majority stakes. Large hikes observed in this category are attributed to the pre-election investment cycle of local governments and accelerated spending financed by EU funds. The available data show that investments of private companies (especially those operating in the sectors characterised by low spending of EU funds) rose only slightly, if at all. Consequently, the investment rate in the Polish economy is still relatively low.

Polish exports experienced a clear slowdown in the first months of 2018, mainly due to the economic weakening observed in the euro zone since January, which was still there as of the date of this report. Taking into account solid growth in imports coupled with high growth in consumption and investments, it is no surprise that net exports made a negative contribution to economic growth in H1 2018, which is expected to continue in the coming quarters.

Inflation stable at around 2%. MPC sees no reason for interest rate changes.

H1 2018 was also marked by large fluctuations in inflation: in February and March the inflation rate unexpectedly fell below the target range to 1.3% year on year and then rose to 2.0% year on year in the spring (final June data). The key factors triggering the inflation rate fluctuations in H1 2018 include: systematically decreasing growth in food prices (effect of high last year's base and the abating of the positive one-time shocks that affected the prices of selected products in H2 2017), increase in oil prices fuelled by the weakening zloty and a slowdown in core inflation. The latter stood at 0.5-0.6% in the last few months, which is the lowest level reported in a year.

CPI Inflation and reference rate



The reasons behind low core inflation are not fully recognised, but consumer services surely play a major role. Despite historic relations between pay rises in the service sector and the prices of services, last year's rise in salaries was not reflected in prices, which makes room for scepticism about the short-term path of core inflation. The Bank reckons that the relations are still in place and the economy follows the path towards further tightening of the labour market, GDP ahead of the potential output, and consequently, higher inflation. H2 2018 will be marked by base effects in fuel and food prices, which will bring CPI growth to 1.5-1.7% at the end of the year, but the following months are expected to see first signs of growing inflationary pressure (observed for core inflation).

Under these circumstances the Monetary Policy Council could comfortably maintain its dovish rhetoric. The period of interest rates stabilization forecast by Adam Glapiński, head of MPC, is expected to last by the end of 2020, thus setting a new record. The Bank does not expect the National Bank of Poland (NBP) to fulfil these promises in full as the combination of ECB's interest rate increases and a clear rise in core inflation will probably force MPC to start tightening its monetary policy towards the end of 2019. The tightening is unlikely to exceed 100 basis points in total.

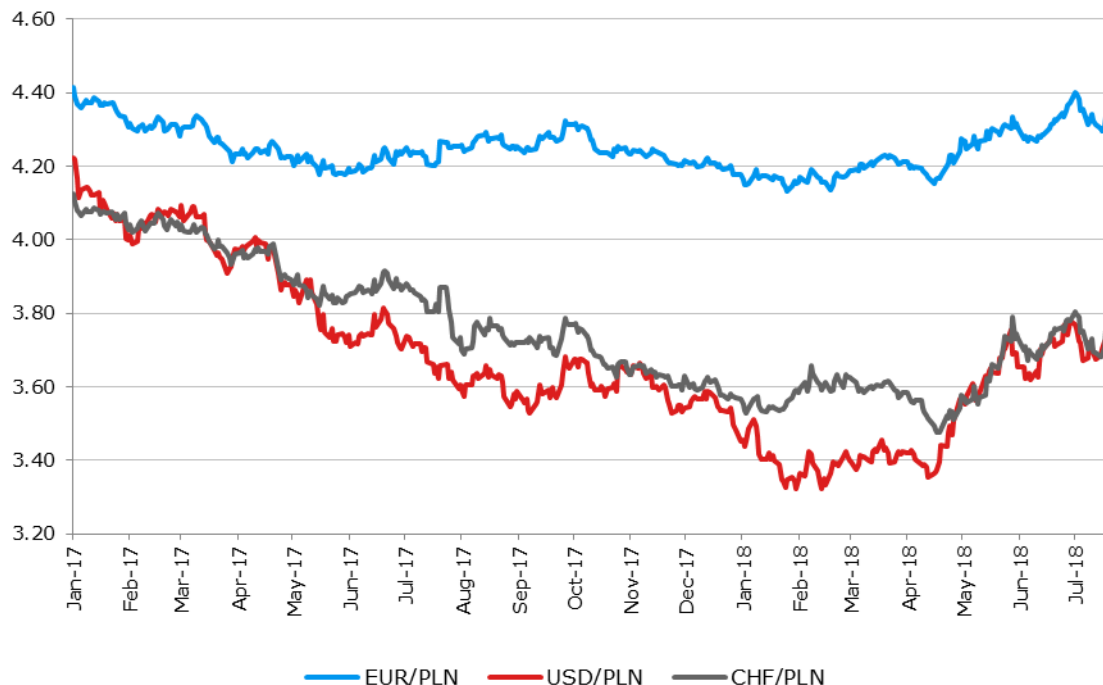
Financial markets: a good six months for bonds, bad for the zloty

In the first months of the year, the main classes of Polish financial assets performed differently. The Polish zloty showed a large decline against the major currencies and share prices on the Warsaw Stock Exchange dropped by nearly 25%, but on the other hand T-bonds were in demand (especially from February to April).

At the beginning of the year, the zloty traded at 4.15 against the euro (3.30 against the dollar), then steadied for a short time to start a systematic decline lasting the major part of H1 2018. Consequently, at the turn of June and July, the exchange rate stood at PLN/EUR 4.40 and PLN/USD 3.80. The Bank thinks that the depreciation of the Polish currency was caused by a combination of several local and global factors. Firstly, the nominal and (in particular) real interest rates in Poland are low at the moment, which changes the spread between Polish interest rates and interest rates of the major world economies to the zloty's disadvantage. Secondly, a rise in risk aversion, worsening of the sentiment towards emerging markets and strengthening of the dollar all served in favour of a sell-off of emerging markets assets in H1 2018,

which also affected the zloty. Finally, due to poor performance of the Warsaw Stock Exchange, even in the periods of rising risk appetite, the zloty did not gain as it had before when GPW had been operating effectively.

Currency exchange rates



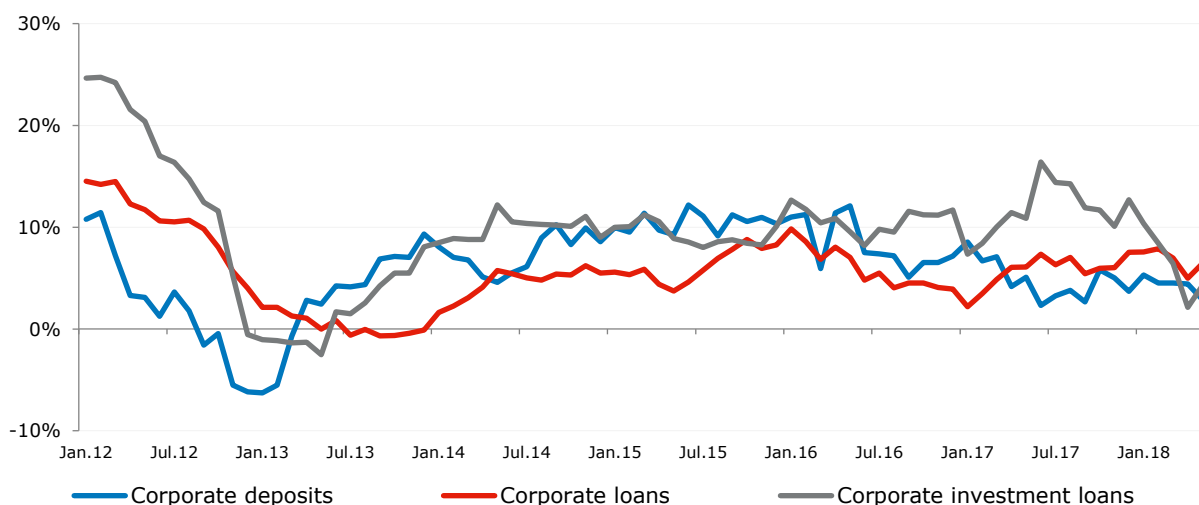
In the case of T-bonds, there were three phases. January saw a sell-off of treasury securities connected with rising global interest rates and optimistic outlook for the world economy. From February to April, the combination of a surprisingly low supply of treasury securities, unexpected decrease in inflation, abrupt deterioration of expectations about global economic growth and fears of a trade war resulted in a major reduction in the price of bonds and a drop in yields by more than 60 basis points (for a 10-year tenor). A period of stabilization (and growing yields) that came afterwards was helped by a stabilization of expectations about the global economy, rising prices of raw materials and higher inflation, partial normalization of the supply of treasury securities and a sell-off of emerging markets assets which affected also Polish bonds.

Money supply and the banking sector as the mirror of the economy

In H1 2018, there were several major trends in banking sector data.

Firstly, growth in household deposits first reached its lowest compared with the previous year and then rebounded towards the end of the analysed period to the highest level since July 2017. Growth in retail deposits was helped by rising nominal wages, no attractive alternatives to savings accounts and the weakening zloty, which increases the present value of foreign currency deposits. The Bank reckons that in the next few months the inflow of household deposits will not subside, even amid low interest rates.

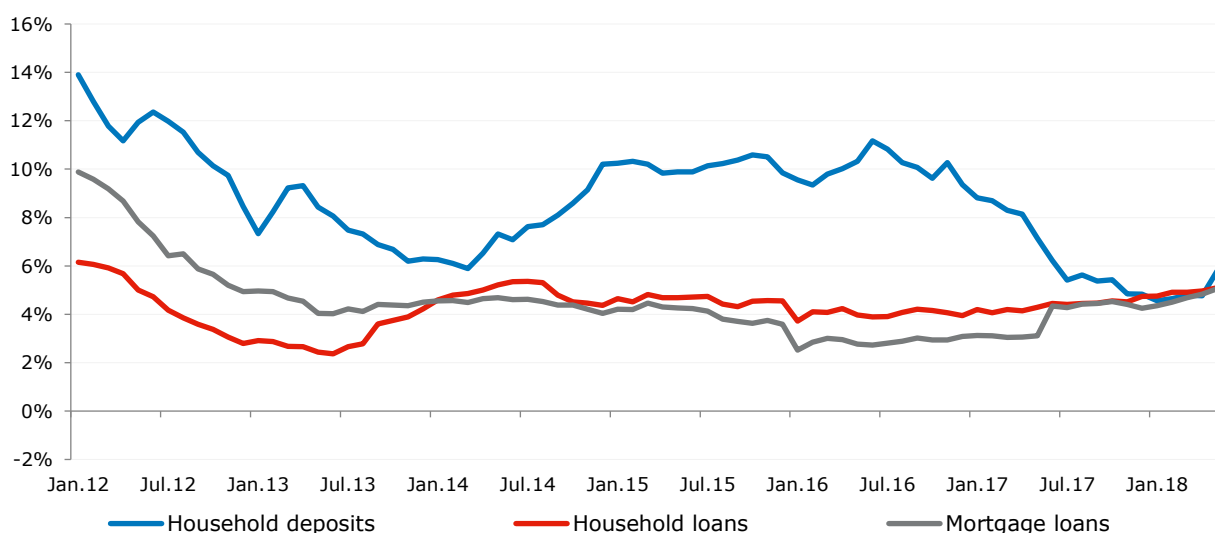
Corporate loans and deposits



Secondly, growth in corporate deposits was sluggish throughout the analysed period, most likely due to deteriorating liquidity standing of some companies and worsening financial performance of the corporate sector due to rising labour costs not being fully reflected in the prices of finished goods and services.

Thirdly, household loans have been on an upward trend for nearly two years. Their growth exceeded 5.0% year on year, excluding one-off seasonal and calendar effects. Lending revival was driven mainly by housing loans, which is evidenced by the available data showing that currently the value of housing PLN loans is at a historic high and only slightly below the value of all loans (in PLN and in foreign currencies) granted in 2007-2008. Favourable situation on the labour market and high supply of flats will support high demand for housing loans in the coming quarters.

Household loans and deposits



Growth in corporate loans was stable in H1 2018 (6.0-7.0% year on year). It was boosted by strong sales of working capital loans and real property loans, while the role of investment loans was in decline, reflecting private sector's low propensity to invest and its large own contributions to financing investment projects.

Outlook for mBank

Net interest income & NIM

(slightly positive)



- Continued gradual increase of margin driven by changing structure of loan portfolio (more higher-yielding products).
- No room for further reduction of funding costs.

Net Fee & Commission income

(neutral)



- Constantly rising client transactionality and strong acquisition in both retail and corporate segment.
- Lower income from insurance products due to the sale of group insurance business.

Total costs

(slightly negative)



- Business-driven costs to be kept well-contained.
- Contribution to the BFG expected to remain stable.
- Rising amortisation due to ongoing investments in IT.

Loan Loss Provisions

(slightly negative)



- Small downside risk due to changing loan book mix.
- Potential increase in provisioning due to IFRS 9.
- Resilient asset quality supported by good macroeconomic situation and low unemployment.

Changes in banking regulationsAct of May 10, 2018 on Personal Data Protection and General Data Protection Regulation (GDPR/RODO)

The EU General Data Protection Regulation (GDPR/RODO) and the related Polish Act of May 10, 2018 on Personal Data Protection entered into force on May 25, 2018. The new regulations have introduced a number of changes in how personal data should be processed by various entities. Their main objective is to increase personal data security. Substantial fines that can be imposed on entities that fail to implement and comply with the new law, direct liability for compliance with the requirements and precise guidelines for internal regulations adopted by banks and other entities resulted in the need for the banks to perform a detailed analysis of compliance of its internal regulations with the new requirements and providing clients with relevant information. The new regulations will increase clients' awareness of how and to what extent their personal data are processed. The data can now be processed only for a specified purpose and in a specified scope in a way that ensures that they are kept safe and confidential.

Act of December 15, 2017 on Amendments to the Goods and Services Tax Act and Certain Other Acts

The Act on Amendments to the Goods and Services Tax Act announced on January 10, 2018 required banks to prepare for handling split payment of transactions performed in the Polish zloty by June 30, 2018. The regulations apply to bank transfers taking place between enterprises based on value-added tax (VAT) invoices. It is up to the payers whether they want to use split payment or a conventional wire transfer. Thus, since July 1, 2018 every enterprise has been obliged to hold a dedicated VAT account in addition to their current account, whereas banks must open such accounts for their clients. The aim of the new law is to close gaps in the tax system, but it may affect firms' liquidity as enterprises are not allowed to freely use the funds accumulated on VAT accounts.

Acts amending the Act on Payment Services and certain other acts

Two acts amending the Act on Payment Services and certain other acts were announced in H1 2018. The Act of March 22, 2018 that will come into force on August 11, 2018, governs wrongly-addressed payments. The new law makes it easier for banks to help clients who transferred a payment to the wrong recipient. Payment service providers have been authorised to inform clients about the personal data of persons who received a wrongly-addressed payment and refused to voluntarily return the money. The change will make it easier for bank clients to tackle such issues in court. The other amendment, dated May 10, 2018, which entered into force on June 20, 2018, adjusted the Polish regulations to Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market (PSD2). The aim of the act is to shorten the execution times of cashless payments and foster the development of cashless settlements and at the same time protect clients against financial fraud in cashless transactions. The act has established a legal framework for the activity of new payment service providers - the Third Party Providers (TTP) - rendering payment initiation and account information services. In addition to that, the act governs the operation of Small Payment Institutions. Such entities have been authorised to provide payment services and are now supervised by the Polish Financial Supervision Authority (KNF). The new regulations are mainly addressed to fintech start-ups. According to the act, the security of transactions remains in the centre of attention of both legislators and the KNF, enhanced further by requirements for strong customer authentication and obligation of payment services providers' to deliver evidence that they implemented the security measures required by the type of their activity.

Act of March 1, 2018 on Amending the Act on Trading in Financial Instruments and Certain Other Acts

On April 21, 2018, the Act on Amending the Act on Trading in Financial Instruments and Certain Other Acts entered into force. It implements the EU regulations governing trading in financial instruments and transactions' transparency (e.g. MIFID2, MIFIR and BMR – benchmarks regulation) to Polish legal framework.

The amendments serve the purpose of increasing investors' confidence, mitigating the risk of distortions on markets in financial instruments and reducing transaction costs. When contacting clients, institutions will be obliged to provide a much broader scope of clear and transparent information in order to ensure fairness of transactions and act in line with the clients' interests and expectations. In particular, the new regulations cover the following: investment services, investment advisory as well as reception, execution and transmission of clients' orders. Moreover, the act introduces new terms such as organized trading

facility, a regulated system applying non-discriminatory rules on access. It also restricts the possibility of receiving or charging fees and other benefits from third parties for investment advisory services.

Pursuant to BMR regulation, in the area of indices used as benchmarks in financial instruments banks are obliged to have contingency plans in place in the event of a disruption to the process of benchmarks' publication (e.g. WIBOR), which upon adding the bank's margin constitutes the actual borrowing rate.

Act of March 1, 2018 on Counteracting Money Laundering and Terrorism Financing

The act serves the purpose of making the Polish system for counteracting money laundering and terrorism financing more effective and bringing it into compliance with Directive of the European Parliament and of the Council amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing, and the revised recommendations of the Financial Action Task Force (FATF). In addition, the act introduces the term "virtual currency" in line with the definition of "virtual currencies" used by FATF. The act was published on April 12, 2018 and enters into force 3 months after the issue date, except for the provisions governing the register of beneficial owners kept by the minister competent for public finances, which enter into force 18 months after the issue date.

Bank Supervisory Review and Evaluation Methodology for 2018 (BION)

On March 28, 2018, the Polish Financial Supervision Authority published the BION Methodology for 2018, supplemented by the requirements set out in MIFID II package and the criteria for detailed assessment of banks' IT risk profile.

3.2. Financial results of mBank Group in H1 2017

All growth rate figures presented in the analysis of financial results have been calculated on the basis of the Consolidated Financial Statements for H1 2018 (in PLN thou.).

Income statement

Profit before tax generated by mBank Group in H1 2018 stood PLN 944.1 million, compared to PLN 712.2 million in H1 2017 (+PLN 231.9 million or 32.6%). Net profit attributable to the owners of mBank amounted to PLN 698.4 million as compared with PLN 488.5 million in the same period last year (+PLN 210.0 million or 43.0%).

The key drivers of mBank Group's profit in H1 2018 included:

- **Increase in total income** by 19.7% year on year, mainly attributable to the increase in core income by 8.6% and profit from the sale of an organized part of mFinanse in Q1 2018;
- **Increase in total overhead costs** (including amortization) by 4.4% v. H1 2017 attributable to higher staff-related expenses, material costs and amortization;
- **Increase in net impairment losses and fair value change on loans and advances** by 66.7% driven by higher provisions in the corporate and retail banking segment;
- **Increase in taxes on the Group's balance sheet items** up to PLN 196.8 million v. PLN 184.3 million in H1 2017 (by 6.7%);
- **Continued organic growth and business expansion** as demonstrated by:
 - The number of retail clients served in Poland, the Czech Republic and Slovakia growing to 5,508 thou. (+166 thou. clients year to date);
 - The number of corporate clients hitting 22,934 (+886 year to date).

In H1 2018, the net value of loans and advances increased by 6.1% (or 4.1% net of reverse repo transactions and FX effects) as compared with December 31, 2017 and by 7.5% v. the end of June 2017 (or 7.3% net of reverse repo transactions and FX effects). Deposits grew by 6.9% v. the end of 2017 (or 6.2% net of repo transactions) and 10.9% v. the end of June 2017 (or 10.9% net of repo transactions). Consequently, the loan to deposit ratio stood at 91.6% compared with 92.3% at the end of 2017 and 94.6% on June 30, 2017.

The changes in the Group's results translated into the following profitability ratios:

- Gross ROE of 13.7% (11.0% at the end of H1 2017).
- Net ROE of 10.1% (7.5% at the end of H1 2017).

The Total Capital Ratio stood at 20.1% compared with 21.0% at the end of 2017 and 21.2% at the end of June 2017. The Common Equity Tier 1 Capital Ratio stood at 17.1% compared with 18.3% at the end of 2017 and 18.5% at the end of June 2017. The drop in capital ratios stems from a substantial increase in the total risk exposure amount in this period.

Contribution of business lines and segments to the financial results

The table below presents the contribution of individual business areas to the Group's profit before tax:

PLN M	H1 2017	H1 2018	Change in %	% share in profit before tax
Retail Banking	451.7	690.7	52.9%	73.2%
Corporate and Investment Banking	211.2	230.2	9.0%	24.4%
Financial Markets	40.8	34.3	-16.0%	3.6%
Other	8.5	-11.1	-230.1%	-1.2%
Profit before tax of mBank Group	712.2	944.1	32.6%	100.0%

Retail Banking was the largest contributor to the profit before tax of the Group (73.2%) in H1 2018 (an increased share compared to the previous periods resulted from the sale of an organized part of enterprise of mFinanse).

The profit earned by the Corporate and Investment Banking and by the Financial Markets accounted for 24.4% and 3.6% of the Group's total profit before tax, respectively.

Income of mBank Group

Total income generated by mBank Group was PLN 2,588.8 million in H1 2018, compared with PLN 2,162.7 million a year before, representing an increase by PLN 426.1 million or 19.7%. Higher income is attributable to the increase in core income by PLN 172.7 million and the profit on the sale of an organized part of enterprise of mFinanse in Q1 2018.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Interest income	1,973.8	2,156.2	183.4	9.3%
Interest expense	-459.0	-485.4	-26.4	5.7%
Net interest income	1,513.8	1,670.8	157.0	10.4%
Fee and commission income	822.4	852.6	30.1	3.7%
Fee and commission expense	-320.3	-334.7	-14.4	4.5%
Net fee and commission income	502.2	517.9	15.7	3.1%
Dividend income	3.1	3.1	0.0	-0.7%
Net trading income	138.0	169.2	31.2	22.6%
Other income	-16.7	6.0	22.7	+/-
Other operating income	149.0	321.8	172.8	115.9%
Other operating expenses	-126.8	-100.0	26.8	-21.1%
Total income	2,162.7	2,588.8	426.1	19.7%

Other income – calculated as the sum of gains less losses from financial assets and liabilities not measured at fair value through profit or loss and investments in subsidiaries and associates and gains less losses from investment securities, investments in subsidiaries and associates.

Net interest income remained mBank Group's largest source of income in H1 2018 (64.5% of total income). It stood at PLN 1,670.8 million compared with PLN 1,513.8 million in H1 2017, up by

PLN 157.0 million or 10.4%. Despite low interest rates, a substantial increase in interest income was posted.

Interest income increased by PLN 183.4 million or 9.3% year on year in H1 2018 and stood at PLN 2,156.2 million. Income on loans and advances to customers, which with a share of 75.0% is the main source of interest income, stood at PLN 1,616.6 million, up by PLN 171.2 million or 11.8% year on year. This was possible thanks to rising credit volumes and shifts in the structure of assets towards high-margin products, especially non-mortgage loans. The discussed period also saw a rise in income from derivative instruments classified into the banking book - up by PLN 14.8 million or 20.3% v. H1 2017. It was attributable to an increase in the volume of these instruments caused by changes in the funding structure of mBank Group.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Loans and advances	1,445.5	1,616.6	171.2	11.8%
Investment securities	341.0	337.5	-3.5	-1.0%
Cash and short term funds	30.0	25.7	-4.4	-14.6%
Debt securities held for trading	42.3	32.4	-9.9	-23.5%
Interest income on derivatives classified into banking book	73.1	87.9	14.8	20.3%
Interest income on derivatives concluded under the fair value hedge	31.5	38.0	6.4	20.4%
Interest income on derivatives concluded under the cash flow hedge	7.1	15.8	8.7	122.9%
Other	2.4	2.4	0.0	0.3%
Total interest income	1,972.8	2,156.2	183.4	9.3%

Interest income from loans and advances includes interest income from loans and advances on the following items: assets held for trading, non-trading financial assets measured mandatorily at fair value through profit or loss and financial assets at amortised cost.

Interest income from investment securities includes interest income on the following items: non-trading financial assets measured mandatorily at fair value through profit or loss, including debt securities, financial assets measured at fair value through other comprehensive income and financial assets measured at amortised cost, including debt securities.

Interest expense increased by PLN 26.4 million or 5.7% year on year in H1 2018. Costs related to settlements with customers rose by PLN 17.6 million or 7.1% due to the higher volume of retail and corporate deposits. Costs of issued debt securities went up by PLN 15.4 million or 11.4% due to a larger volume of these securities (a new EMTN tranche in the amount of CHF 180 million was issued in June 2018 and new issues of covered bonds by mBank Hipoteczny).

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Amounts due to banks	-30.6	-29.0	1.6	-5.2%
Amounts due to customers	-248.5	-266.1	-17.6	7.1%
Debt securities in issue	-134.7	-150.1	-15.4	11.4%
Subordinated liabilities	-35.2	-35.1	0.2	-0.5%
Other	-10.0	-5.1	4.9	-48.7%
Total interest expense	-459.0	-485.4	-26.4	5.7%

Net interest margin rose to 2.57% in H1 2018 from 2.42% a year before.

Net fee and commission income amounted to PLN 517.9 million in H1 2018, up by PLN 15.7 million or 3.1% year on year. The increase in net commission income was driven mainly by higher credit-related commissions and payment card-related fees.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Payment cards-related fees	182.0	206.1	24.1	13.2%
Credit-related fees and commissions	159.8	188.8	28.9	18.1%
Commissions for agency service regarding sale of insurance products of external financial entities	93.9	64.2	-29.7	-31.6%
Fees from brokerage activity and debt securities issue	68.4	54.4	-14.0	-20.4%
Commissions from bank accounts	91.8	103.6	11.8	12.9%
Commissions from money transfers	57.6	64.0	6.4	11.2%
Commissions due to guarantees granted and trade finance commissions	34.1	42.6	8.5	24.8%
Commissions for agency service regarding sale of other products of external financial entities	71.6	57.3	-14.3	-20.0%
Commissions on trust and fiduciary activities	13.1	13.4	0.3	2.0%
Fees from portfolio management services and other management-related fees	7.5	6.6	-0.9	-11.5%
Fees from cash services	26.1	27.7	1.6	6.2%
Other	16.4	23.8	7.4	44.8%
Fee and commission income	822.4	852.6	30.1	3.7%

Commission income increased by PLN 30.1 million or 3.7% year on year. Payment card-related fees, which make the biggest contribution to commission income, increased by PLN 24.1 million or 13.2% year on year in the period under review thanks to an increase in the volume and value of non-cash transactions.

Credit-related fees and commissions increased by PLN 28.9 million or 18.1% year on year as a result of higher sales of retail mortgage, non-mortgage and corporate loans.

Due to the sale of an organized part of enterprise of mFinanse, acting as an agent in the scope of group insurance, in Q1 2018, commissions for agency service regarding the sale of insurance products of external financial entities dropped by PLN 29.7 million or 31.6% year on year.

Lower turnover in the Warsaw Stock Exchange and lower number of transactions executed in H1 2018 by Dom Maklerski mBanku resulted in a decrease in commissions from brokerage activity and debt securities issue by PLN 14.0 million or 20.4% year on year.

The increase in the customer base and expansion of transactional banking had a favourable impact on bank account commissions, which increased by PLN 11.8 million or 12.9%, and money transfer commissions, which grew by PLN 6.4 million or 11.2%.

Fee and commission expenses increased by PLN 14.4 million or 4.5% year on year in H1 2018. The increase was mainly driven by other fees and commissions paid and payment card-related costs.

Dividend income in H1 2018 amounted to PLN 3.1 million and remained unchanged year on year. Similarly to the previous year, the income booked in H1 2018 included dividends received from Biuro Informacji Kredytowej (BIK) and Krajowa Izba Rozliczeniowa (KIR), in which the Bank holds minority interests.

Net trading income amounted to PLN 169.2 million in H1 2018 and was by PLN 31.2 million higher (+22.6%) compared with the previous year. An increase in FX result was reported (+PLN 16.7 million or 12.5%) coupled with a rise in gains or losses on financial assets held for trading (+PLN 13.0 million or 119.5%).

Other income (including gains less losses on investment securities and investments in subsidiaries and associates and gains less losses from financial assets and liabilities not measured at fair value through profit or loss and investments in subsidiaries and associates) stood at PLN 6.0 million against -PLN 16.7 million in H1 2017, when an impairment connected with the sale of mLocum, a revaluation loss on one of the companies from the portfolio of investments held for sale and a revaluation loss on the portfolio of debt securities available for sale were reported.

Net other operating income (other operating income net of other operating expenses) was PLN 221.8 million, compared with PLN 22.3 million in H1 2017 (+PLN 199.5 million). It resulted mainly from the profit from selling an organized part of enterprise of mFinanse in Q1 2018 in the amount of PLN 219.7 million and a part of profit recognized over time in the amount of PLN 19.1 million booked in Q2 2018.

Net impairment losses and fair value change on loans and advances

In H1 2018, net impairment losses and fair value change on loans and advances in mBank Group (being the sum of two items: impairment or reversal of impairment on financial assets not measured at fair value through profit or loss and gains or losses on non-trading financial assets measured mandatorily at fair value through profit or loss) stood at PLN 338.8 million, being higher than net impairment losses on loans and advances in H1 2017 which amounted to PLN 203.3 million (-PLN 135.5 million or -66.7%). In H1 2018, impairment or reversal of impairment on financial assets not measured at fair value through profit or loss amounted to -PLN 278.4 million and gains or losses from non-trading financial assets mandatorily measured at fair value through profit or loss amounted to -PLN 60.4 million. Impairment or reversal of impairment on financial assets not measured at fair value through profit or loss is related to the part of the portfolio of loans and advances that is measured at amortised cost. The item "gains or losses from non-trading financial assets mandatorily measured at fair value through profit or loss" is mainly related to the credit risk of the portfolio of loans and advances measured with the use of that method.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Retail Banking	-158.4	-214.0	-55.6	35.1%
Corporates and Financial Markets	-45.8	-124.6	-78.8	172.2%
Other	0.9	-0.2	-1.1	-/+
Total net impairment losses and fair value change on loans and advances	-203.3	-338.8	-135.5	66.7%

Net impairment losses and fair value change on loans and advances in the Retail Banking grew by PLN 55.6 million in H1 2018 compared to H1 2017. The hike was a result of higher loan volume as well as a shift in the retail loan portfolio structure, in which non-mortgage loans have an ever bigger share.

Net impairment losses and fair value change on loans and advances in the Corporates and Financial Markets Segment increased in H1 2018 by PLN 78.8 million compared to H1 2017 due to provisions created on several larger exposures in Q2 2018. Moreover, in H1 2017 provisions were exceptionally low.

Costs of mBank Group

In the period under review, mBank Group pursued further investments in growth in the strategic areas, which will help to boost income in the coming years. At the same time, high operational efficiency, measured by the cost to income ratio, was maintained.

Total overhead costs of mBank Group (including amortisation) stood at PLN 1,109.6 million in H1 2018, representing an increase by PLN 46.9 million or 4.4% year on year.

PLN M	H1 2017	H1 2018	Change in PLN M	Change in %
Staff-related expenses	-447.2	-466.4	-19.2	4.3%
Material costs, including	-349.5	-365.6	-16.1	4.6%
- administration and real estate services costs	-179.0	-182.2	-3.2	1.8%
- IT costs	-81.3	-85.7	-4.4	5.5%
- marketing costs	-52.8	-60.0	-7.2	13.7%
- consulting costs	-30.6	-31.4	-0.8	2.7%
- other material costs	-5.9	-6.2	-0.4	6.4%
Taxes and fees	-10.7	-11.1	-0.4	3.6%
Contributions and transfer to the Bank Guarantee Fund	-149.1	-138.1	11.0	-7.4%
Contributions to the Social Benefits Fund	-3.7	-4.0	-0.4	10.0%
Amortization	-102.7	-124.5	-21.8	21.2%
Total overhead costs and amortization	-1,062.8	-1,109.6	-46.9	4.4%
Cost/Income ratio	49.1%	42.9%	-	-
Employment (FTE)	6,514	6,358	-156	-2.4%

Staff-related expenses increased by PLN 19.2 million or 4.3% year on year due to higher remuneration costs. The number of FTEs went down by 156 in this period mainly as result of organizational changes within the Group.

Material costs went up by PLN 16.1 million or 4.6% in the period under review. In H1 2018, mBank Group reported higher marketing, IT, administration and real estate services costs.

Amortisation charges went up by PLN 21.8 million or 21.2% year on year due to earlier investment outlays on IT systems.

The contribution to the Bank Guarantee Fund (BFG) in H1 2018 stood at PLN 138.1 million, down by PLN 11.0 million v. H1 2017. Both, H1 2018 and H1 2017 costs comprised the annual contribution to the resolution fund registered in Q1.

As a result of the changes in the income and costs of mBank Group, the cost to income (C/I) ratio of mBank Group amounted to 42.9% compared with 49.1% a year before. The normalised cost to income ratio (adjusted for the one-off income from the sale of an organized part of enterprise of mFinanse and contribution to the resolution fund for H2) decreased in H1 2018 to 44.8% compared to 46.5% in H1 2017 (adjusted for the contribution to the resolution fund for H2).

Changes in the consolidated statement of financial position

Changes in the assets of mBank Group

In H1 2018, the assets of mBank Group rose by PLN 8,593.8 million or 6.5%. As at June 30, 2018, the assets amounted to PLN 140,017.8 million.

PLN M	30.06.2017	31.12.2017	30.06.2018	YtD change	YoY change
Cash and balances with Central Bank	5,855.4	7,384.9	5,514.9	-25.3%	-5.8%
Loans and advances to banks	2,259.1	1,707.7	3,787.0	121.8%	67.6%
Trading securities	3,296.6	1,525.4	3,445.0	125.8%	4.5%
Derivative financial instruments	1,325.1	1,236.3	1,189.9	-3.8%	-10.2%
Net loans and advances to customers	83,377.0	84,475.8	89,601.4	6.1%	7.5%
Investment securities	30,469.6	32,144.7	33,388.4	3.9%	9.6%
Non-current assets held for sale	170.8	42.1	0.0	-	-
Intangible assets	627.9	710.6	703.5	-1.0%	12.0%
Tangible assets	711.9	758.7	715.5	-5.7%	0.5%
Other assets	1,323.9	1,437.7	1,672.2	16.3%	26.3%
Total assets	129,417.5	131,424.0	140,017.8	6.5%	8.2%

Investment securities – calculated as the sum of debt securities at fair value through other comprehensive income, debt securities measured at amortised cost and non-trading equity instruments mandatorily at fair value through profit or loss.

Net loans and advances to banks – calculated as the sum of loans and advances measured at amortised cost and loans and advances mandatorily at fair value through profit or loss.

Loans and advances to customers retained the largest share in the balance sheet of mBank Group at the end of H1 2018. Their net volume increased by PLN 6,224.4 million or 7.5% year on year. As at June 30, 2018, they accounted for 64.0% of the balance sheet total against 64.4% at the end of H1 2017 and 64.3% at the end of 2017.

PLN M	30.06.2017	31.12.2017	30.06.2018	YtD change	YoY change
Loans and advances to individuals	48,757.8	48,142.8	51,133.6	6.2%	4.9%
Loans and advances to corporate entities	36,150.5	37,941.7	40,756.3	7.4%	12.7%
Loans and advances to public sector	1,081.1	995.6	790.3	-20.6%	-26.9%
Other receivables	239.5	307.6	-	-	-
Total (gross) loans and advances to customers	86,228.9	87,387.7	92,680.1	6.1%	7.5%
Provisions for loans and advances to customers	-2,851.8	-2,911.9	-3,078.7	5.7%	8.0%
Total (net) loans and advances to customers	83,377.0	84,475.8	89,601.4	6.1%	7.5%

In H1 2018, gross loans and advances to individuals rose by PLN 2,990.8 million or 6.2%. The value of mortgage and housing loans decreased by PLN 1,363.7 million or 3.9% despite growing sales, which reached PLN 2,147.6 million or +19.3% year on year in H1 2018 (PLN 1,800.0 million in H1 2017). The decrease was driven by systematic repayments of mortgage loans in the Swiss franc – the portfolio went down by 9.2% (in the original currency) in H1 2018. In H1 2018, mBank Group sold PLN 4,331.6 million worth of non-mortgage loans, which represents a 16.9% hike as compared with H1 2017. Net of the FX effect, loans and advances to individuals grew by 3.9% compared with the end of 2017 and by 5.1% year on year.

The volume of gross loans and advances to corporate clients grew by PLN 2,814.6 million or 7.4% in H1 2018. Excluding reverse repo/buy sell back transactions and the FX effect, the value of loans to corporate clients increased by 5.9% against the end of 2017 and 11.9% against H1 2017.

The volume of gross loans and advances to the public sector decreased by PLN 205.3 million or 20.6% in H1 2018.

Investment securities constituted mBank Group's second largest asset category (23.8%). In H1 2018, their value increased by PLN 1,243.7 million or 3.9%. The portfolio of debt securities issued by the central bank increased a dozen or so times, reaching PLN 2,201.3 million against the end of June 2017.

The balance of trading securities went up by PLN 1,919.6 million or 125.8% in H1 2018 as a result of extending the treasury bonds portfolio (+152.2%).

Changes in liabilities and equity of mBank Group

The table below presents changes in the liabilities and equity of mBank Group in H1 2018:

PLN M	30.06.2017	31.12.2017	30.06.2018	YtD change	YoY change
Amounts due to other banks	8,641.3	5,073.4	4,548.8	-10.3%	-47.4%
Derivative financial instruments	1,114.5	1,095.4	1,110.8	1.4%	-0.3%
Amounts due to customers	88,155.9	91,496.0	97,794.4	6.9%	10.9%
Debt securities in issue	13,011.7	14,322.9	16,817.7	17.4%	29.3%
Subordinated liabilities	2,232.8	2,158.1	2,206.7	2.3%	-1.2%
Liabilities held for sale	61.6	0.0	0.0	-	-
Other liabilities	2,519.2	2,986.7	3,018.8	1.1%	19.8%
Total Liabilities	115,737.1	117,132.5	125,497.2	7.1%	8.4%
Total Equity	13,680.4	14,291.6	14,520.6	1.6%	6.1%
Total Liabilities and Equity	129,417.5	131,424.0	140,017.8	6.5%	8.2%

Amounts due to customers are the principal source of funding of mBank Group. Their share in the structure of liabilities and equity of mBank Group reported a significant increase year on year. As at the end of June 2018, they accounted for 69.8% of the Group's total liabilities and equity as compared with 69.6% at the end of 2017 and 68.1% at the end of June 2017.

PLN M	30.06.2017	31.12.2017	30.06.2018	YtD change	YoY change
Individual customers	53,835.2	55,693.6	59,902.8	7.6%	11.3%
Corporate customers	32,737.1	34,589.6	35,591.7	2.9%	8.7%
Public sector customers	1,583.6	1,212.8	2,299.9	89.6%	45.2%
Total amounts due to customers	88,155.9	91,496.0	97,794.4	6.9%	10.9%

Amounts due to customers increased by PLN 6,298.4 million or 6.9% in H1 2018, up to PLN 97,794.4 million. The period under review saw a rise in amounts due to all clients' groups.

Amounts due to corporate clients went up by 2.9%. The increase of funds in term deposits (+26.4%) and repo transactions was partially offset by the outflow of funds in current accounts (-10.0%).

Amounts due to individuals rose by PLN 4,209.2 million or 7.6% in H1 2018. Growth was reported in funds in current accounts (+8.9%) as well as in term deposits (3.1%).

Amounts due to the public sector went up by 89.6% to PLN 2,299.9 million, which was chiefly attributable to an increase in the volume of term deposits.

Amounts due to other banks decreased by PLN 4,092.6 million or 47.4% year on year to PLN 4,548.8 million. Compared with the end of 2017, amounts due to banks declined by PLN 524.6 million or 10.3%, mainly due to the repayment of two loans in CHF and USD. In addition, the Bank took out a new loan in USD amounting to PLN 187 million.

The share of debt securities in issue in the funding structure of mBank Group grew from 10.9% at the end of 2017 to 12.0% at the end of June 2018. Their value grew by PLN 2,494.9 million or 17.4% compared with the end of 2017. The growth is mainly attributable to the issue of covered bonds by mBank Hipoteczny and the issue of a bond tranche worth CHF 180 million within the new EMTN programme.

In H1 2018, subordinated liabilities increased slightly against the end of 2017 (by 2.3%).

In H1 2018, equity grew by PLN 229.1 million or 1.6% as a result of an increase in retained profits, while its share in total liabilities and equity of mBank Group accounted for 10.4% at the end of H1 2018 (10.9% at the end of 2017 and 10.6% the year before).

Financial results of mBank Group in Q2 2017

The profit before tax generated by mBank Group in Q2 2018 stood at PLN 384.5 million against PLN 559.6 million in the previous quarter. Net profit attributable to the owners of mBank reached PLN 287.4 million, down from PLN 411.0 million in Q1 2018.

PLN M	Q1 2018	Q2 2018	Change in PLN M	Change in %
Interest income	1,053.6	1,102.6	48.9	4.6%
Interest expense	-237.2	-248.2	-11.0	4.6%
Net interest income	816.4	854.4	37.9	4.6%
Fee and commission income	429.5	423.1	-6.4	-1.5%
Fee and commission expense	-160.6	-174.1	-13.5	8.4%
Net fee and commission income	268.9	249.0	-19.9	-7.4%
Core income	1,085.3	1,103.3	18.0	1.7%
Dividend income	0.2	2.9	2.8	14.5x
Net trading income	84.5	84.7	0.2	0.2%
Other income	4.3	1.7	-2.6	-60.1%
Other operating income	268.9	52.9	-216.1	-80.3%
Other operating expenses	-62.6	-37.4	25.3	-40.4%
Total income	1,380.6	1,208.2	-172.4	-12.5%
Net impairment losses and fair value change on loans and advances	-121.8	-217.1	-95.3	78.3%
Overhead costs and amortization	-601.0	-508.7	92.3	-15.4%
Taxes on bank balance sheet items	-98.5	-98.3	0.2	-0.2%
Result on entities under the equity method	0.3	0.3	0.0	-
Profit before income tax	559.6	384.5	-175.1	-31.3%
Income tax expense	-148.6	-97.1	51.6	-34.7%
Net profit attributable to:	411.0	287.4	-123.6	-30.1%
- Owners of mBank S.A.	411.0	287.4	-123.6	-30.1%
- Non-controlling interests	0.0	0.0	0.0	-
ROA net	1.3%	0.8%		
ROE gross	16.2%	11.1%		
ROE net	11.9%	8.3%		
Cost/Income ratio	43.5%	42.1%		
Net interest margin	2.6%	2.6%		
Common Equity Tier 1 ratio	17.9%	17.1%		
Total capital ratio	20.9%	20.1%		

Other income – calculated as the sum of gains less losses from financial assets and liabilities not measured at fair value through profit or loss and investments in subsidiaries and associates and gains less losses from investment securities, investments in subsidiaries and associates.

The main drivers of mBank Group's financial results in Q2 2018 included:

- **Increase in net interest income** by PLN 37.9 million or 4.6% driven by an increase in interest income by 4.6% quarter on quarter;
- **Decrease in net fee and commission income** by PLN 19.9 million or 7.4% resulting from the Q1 sale of an organized part of mFinanse, which acts as an agent in the scope of group insurance;
- **Stable net trading income** with a rise in the FX result by 11.5% quarter on quarter;
- **Decrease in operating costs (including amortization)** by PLN 92.3 million or 15.4%, driven by the annual contribution to the resolution fund of the Bank Guarantee Fund made in Q1 2018;
- **Increase in net impairment losses and fair value change on loans and advances** (by PLN 95.3 million) driven by a rise in provisions in the Corporates and Financial Markets segment, which stood at PLN 110.7 million against PLN 13.9 million in the previous quarter. In the analyzed period, impairment losses on loans and advances in the Retail Banking segment amounted to PLN 106.2 million v. PLN 107.9 million in Q1 2018;
- **Stable taxes on Group's balance sheet items** at PLN 98.3 million.

The balance sheet total of mBank Group stood at PLN 140,017.8 million as at June 30, 2018 compared with PLN 133,640.2 million at the end of March 2018.

Net loans and advances to clients increased by PLN 3,938.0 million or 4.6% in Q2 2018. Higher volume of loans was reported in both the retail clients segment (up by PLN 2,308.3 million or 4.7%) and the corporate clients segment (up by PLN 1,996.4 million or 5.2%). Net of FX effects, the value of loans and advances to individuals rose by approx. 2.7%. In Q2 2018, mBank Group sold PLN 1,152.8 million worth of mortgage loans and PLN 2,331.6 million worth of non-mortgage loans.

At the same time, amounts due to clients rose by PLN 3,485.8 million or 3.7%. Growth was reported in amounts due to individuals (up by PLN 2,182.8 million or 3.8%) and to corporate clients (up by PLN 1,567.0 million or 4.6%). In both cases, this was attributable to the inflow of funds to current and savings accounts. Funds in current accounts of individuals rose by PLN 2,244.6 million or 4.9% and of corporate clients by PLN 1,178.0 million or 6.5%.

4. Risk management

4.1. Risk management foundations and key changes in H1 2018

mBank Group manages risk on the basis of regulatory requirements and best market practice by developing risk management strategies, policies and guidelines.

The risk management process is conducted at all levels of the organizational structure, starting at the levels of the Supervisory Board (including the Risk Committee of the Supervisory Board) and the bank's Management Board, through specialised committees and units responsible for risk identification, measurement, monitoring, control and reduction, down to each business unit.

Three lines of defence

Risk management roles and responsibilities in mBank Group are organized around **the three lines of defence scheme**:

- The first line of defence is **Business** (business lines), whose task is to take risk and capital aspects into consideration when making all business decisions, within the risk appetite limits set for the Group.
- The second line of defence, mainly **Risk** (risk management area), **IT, Security and Compliance function**, is responsible for determining framework and guidelines concerning managing individual risks, supporting Business in their implementation as well as supervising the control functions and risk exposure. To ensure that the Business is supported and supervised in an objective manner, the second line functions act independently of the Business.
- The third line of defence is **Internal Audit**, ensuring independent assessment of activities connected with risk management performed by the first and the second line of defence.

Pillars of risk management

The framework for risk management at mBank Group derives from the **concept of three pillars**:

- **Client-centric approach** – striving to understand and balance specific needs of the Risk's diverse stakeholders (Business, the Management Board, the Supervisory Board, shareholders, regulators).
- **One Risk** - integrated approach to risk management and responsibility to the clients for all risks (defined in the Risk Catalogue of mBank Group).
- **Risk v. Rate of Return** perspective – supporting business decision-making process on the basis of long-term relationship between risk and rate of return avoiding tail risks.

Vision and mission of the risk management area

Vision of the risk management area

We take advantage of the opportunities in a dynamically changing environment, using innovative methods of risk management.

Bearing in mind the bank's efficiency and safety, we create value for the customer in a partner dialogue with the business.

The **Mission** of the risk management area is to be actively involved in the initiatives and actions undertaken while realization of the strategy of the mBank Group. This support is organized around five challenges facing the risk management area in the coming years:

- **Empathy** understood as active adaptation of risk management to the changing needs of different groups of customers.
- Promoting the experience of **mobility**.

- **Efficiency** understood as: measuring, improving and automating risk processes in the culture of Lean; shaping - through a partner dialogue - risk appetite ensuring safe and profitable balance sheet of the bank.
- **Engaged employees.** This challenge is realized through building a work environment which fosters innovation, attracts, maintains and develops employees with knowledge of business and risk management, curious to find solutions and openly communicating.
- **Technological advantage**, which means the implementation of risk management based on a common integrated data platform (CDL, Common Data Layer) and the search for technological solutions enabling innovative risk management.

Business and Risk Forum of mBank Group

In the risk management process, the bank attaches high importance to the communication between organizational units in the area of risk management and lines of defence in mBank as well as between the bank and the Group subsidiaries. An important role in this regard is played by the **Business and Risk Forum of mBank Group** which is a formal decision and communication platform dedicated for finding solutions ensuring the optimal relation between profits and risk taking, in accordance with the risk appetite approved by the Management Board. The Forum is constituted by the following Committees assigned to individual business lines:

- Retail Banking Risk Committee (KRD),
- Corporate and Investment Banking Risk Committee (KRK),
- Financial Markets Risk Committee (KRF).

The Committees are composed of the representatives of business lines and respective risk management area departments of mBank and the respective organizational units of the Group subsidiaries. Each Committee is responsible for all risks generated by business activity of the given business line.

Key activities and changes in the risk management area in H1 2018

The risk control and management process in the mBank Group is subject to continuous improvement with emphasis on the improvement of customer-oriented integrated risk management. Selected activities carried out in 2018 are described below:

- Risk appetite was defined for the subsequent planning horizon with special attention paid to 2018. Conclusions from analyses and discussions on potential impact on the Group of several issues identified during the managerial dialogue with particular emphasis on the package of non-financial risks, were taken into account while formulating risk appetite.
- Review and update of the strategies for managing particular risks (credit risk in the corporate and the retail areas, market risk, liquidity risk, operational risk and reputational risk).
- The internal capital adequacy assessment process (ICAAP) and the internal liquidity adequacy assessment process (ILAAP) were reviewed. The results of the reviews were presented to the Management Board and the Supervisory Board of mBank.
- The process related to the application of the strategy for stabilizing net interest income from instruments financed by stable parts of capital and current accounts as well as the method of measuring the interest rate risk of the banking book were changed to facilitate the control of the impact of the adopted strategy on the market risk level. Measurement and analysis take place in two perspectives (including and without taking into account the modeling of stable parts of capital and current accounts, insensitive to changes in interest rates). The change was widely discussed in the organization and was approved by the Management Board.
- Programme of continuous increase of work efficiency based on the Lean Management rules was continued. Further processes in the risk management area are reviewed and streamlined using the lean

philosophy and tools. The purpose of the programme is to allow the growing number of tasks accompanying business growth and increasing number of regulatory requirements without the need to significantly increase resources and to reallocate resources from the streamlined operating areas to the areas where resources need to be increased due to the realized projects or growing scope of tasks.

4.2. Main risks of mBank Group's business

The Management Board of mBank takes measures necessary to ensure that the Group manages all material risks arising from the implementation of the adopted strategy of mBank Group, in particular, through approving strategies and processes for managing material risks in the Group.

In accordance with the Risk Catalogue of mBank Group, the following risks were recognized as material in the Group's operations as of June 30, 2018:

- credit risk,
- operational risk,
- market risk,
- business risk (including strategic risk),
- liquidity risk,
- reputation risk,
- model risk,
- capital risk (including risk of excessive leverage),
- regulatory risk.

mBank monitors all the aforementioned risks. The following section presents the rules of monitoring credit, market, liquidity and operational risk in mBank Group using risk measures applied by mBank and taking into account differences in the profile and scale of business of the Group.

Credit risk

The Bank organises credit risk management processes in line with the principles and requirements set out in the resolutions and recommendations of the Polish Financial Supervision Authority (in particular Recommendation S, T and C) and CRR/CRDIV, which address issues related to credit risk management.

Tools and measures

Credit risk inherent in financing of mBank Group clients is assessed based on shared statistical models developed for the AIRB (Advanced Internal Rating-Based) approach and uniform tools, and is based on common definitions of terms and parameters used in the credit risk management and rating process. The bank ensures their cohesion at the Group level.

The Group uses different models for particular client segments. The rules governing clear assignment of clients to a system are defined in the bank and the Group subsidiaries internal regulations.

In their credit risk management process, the bank and the Group subsidiaries use the core risk measures defined under the AIRB approach:

- PD – Probability of Default (%),
- LGD (Loss Given Default) – estimated relative loss in case of default (%),
- EAD (Exposure at Default) – estimated exposure at the time of default (amount),
- EL – Expected Loss taking into account the probability of default (amount);

and related measures including:

- RD (Risk Density) – relative expected loss defined as EL to EAD (%),
- LAD (Loss at Default) – estimated loss (amount) in case of default (the product of EAD and LGD).

In the decision-making process, for reporting and communication with business units, PD and EL are expressed in the language of rating classes whose definitions (Masterscale) are uniform across the Commerzbank Group.

In its credit risk management process, the bank also attaches great importance to the assessment of unexpected loss. For this purpose, the bank uses the RWA (Risk Weighted Assets) measure, which is applied, under the AIRB approach, to calculate regulatory capital required to cover credit risk (unexpected loss).

In managing mortgage-secured credit exposures the Group uses the LtV ratio (Loan to Value), i.e. the value of the loan to the market value (or mortgage banking calculated value) of the real estate which secures the loan.

Stress testing is an additional tool of credit risk assessment. Stress testing of the regulatory capital and economic capital required to cover credit risk is carried out quarterly.

In addition to the tools listed above, which are applied both in the corporate and in the retail credit risk measurement, the Group uses tools specific to these areas.

For corporate credit risk the Group defines maximum exposure to a client/group of related clients using the following credit risk mitigating measures:

- MBPZO (Maximum Safe Total Exposure), which defines the maximum level of financial debt of an entity from financial institutions calculated under the bank's methodology, approved by the bank's competent decision-making body. An alternative measure used by the Bank to clients applying for small exposure is Borrowing Capacity (BC).
- LG (General Limit), which defines the level of credit risk financial exposure to a client/group of related clients acceptable to the Group, approved by the bank's competent decision-making body. LG includes a structured limit and products granted outside the structured limit.

In order to minimise credit risk, the Group uses a broad range of collateral for credit products, which also enable active management of the capital requirement. In the assessment of the quality of collaterals for risk products, mBank and mLeasing use the MRV ratio (Most Realistic Value) reflecting the pessimistic variant of debt recovery from the collateral through forced sale.

In addition, the RORAC ratio (Return on Risk Adjusted Capital) is applied in the decision-making process and the assessment of profitability of a client in the CRM system.

Retail credit risk measures are constructed to reflect the characteristics of this customer segment and, in the case of portfolio measures, the high granularity of the loan portfolio:

- DtI (Debt-to-Income) - i.e. monthly credit payments to the net income of a household (used for individual customers).
- DPD (Days-Past-Due) - a family of portfolio risk measures based on the number of days past due date (e.g. share of contracts which are from 31 to 90 days past due date in the total portfolio by number or by value).
- Vintage ratios, which present the quality of cohorts of loans grouped by disbursement time at a different phase of their lifetime.
- RC LLP (Risk Cost LLP) - cost of risk for a loan portfolio (segment), i.e. increment in loan loss provisions to the performing loan portfolio balance.
- Roll-rates, which measure the migration of contracts between days-past-due brackets (1-30, 31-60, 61-90 DPD, etc.).

Strategy

Corporate and Investment Banking

In accordance with the Corporate Credit Risk Management Strategy in mBank Group, the main goal in this area is defining a safe level of risk appetite in sales of risk-bearing products to the Group clients and use synergies by integrating the offer of the bank and Group subsidiaries. The Strategy is realised by credit risk policies, including industry policies, limits reducing the risk and the principles of risk assessment of

business entities applying for financing. The bank manages credit risk both at the single entity level and the consolidated level. The Strategy was updated in February 2018, Credit risk policies are updated at least once a year, taking into consideration particularly risk appetite, present economic trends and prospects for development of sectors, industries and groups of clients being financed by the bank.

In H1 2018, as a part of the strategic project of credit process reconstruction, the bank implemented a new process of assessing credit applications for selected groups of clients, with support of the new tool, achieving the shortening of the time for credit decision and optimizing the involvement of the process participants.

The Group actively manages credit risk aiming to optimise profitability taking into account return on risk. Analyses of the Group's risks are performed on an on-going basis. Risk management is supported by analyses of the Group's credit portfolio structure, limits, guidelines and recommendations on the Group's exposure to selected sectors and geographic markets. In its current credit risk management and determination of concentration risk, the bank performs quarterly portfolio analyses using a Steering Matrix which incorporates PD rating and LAD.

The bank monitors credit portfolio on a quarterly basis including an analysis of the dynamics of change in size and (sector) segmentation of the credit portfolio, client risk (analysis of PD rating), quality of collateral against credit exposures, the scale of change in EL, Risk Density, and default exposures.

In the corporate banking the Group avoids concentration in industries and sectors where credit risk is considered excessively high. The bank uses industry limits to manage the sector concentration risk. In 2017 new methodology of assigning industry limits was introduced and it enhances the existing mechanisms for controlling industry concentration risk by using quantitative factors based on portfolio data while maintaining the importance of expert's opinions as well.

In 2017 the limit for shadow banking exposures was introduced; the limit is in line with EBA guidelines regarding shadow banking entities (the limits for exposure to entities form the parallel banking system).

In compliance with the Recommendation S of the Polish Financial Supervision Authority, the bank has identified a mortgage-secured credit exposure portfolio in retail and corporate banking and applies the Mortgage-Secured Credit Exposure Risk Management Policy. The bank manages the mortgage-secured credit exposure portfolio risk with a focus on defining an optimised portfolio structure in terms of quality (rating), currencies, country regions, tenors, and types of properties.

mBank Group strives to unlock synergies with Commerzbank more broadly in syndicated finance of selected Group clients. For international companies, non-banking financial institutions and biggest corporate clients, mBank Group promotes innovative products with low capital consumption, in particular products of investment banking (ECM, DCM, M&A), transactional banking and financial markets instruments.

mBank promotes financing alternative to banking loans by arranging public and private programmes and club deals for bonds issued by clients with a stable financial position.

Retail Banking

Lending in retail banking is a key segment of the Group's business model, both in terms of the share in total assets and the contribution to its profits.

The bank's retail credit offer covers a broad range of products financing the needs of individual customers (OF) and micro-companies (MF). The offered credit products in combination with the constantly upgraded transactional platform, savings and insurance products address all financial needs of clients within the Group.

Apart from the Polish market, the Retail Banking credit products are offered through the foreign branches (OZ) of the bank in the Czech Republic and Slovakia in an online banking model similar to that operating in Poland. The share of the foreign branches' exposure portfolio was around 10% of the aggregate retail portfolio at the end of 2017 (by value). The bank ensures the coherence of the credit risk management policy on all markets; any differences in specific rules or parameter values in credit policy derive from the specificities of local markets or different goals of business strategies and are at each time subject to approval by the Retail Banking Risk Committee.

As credit exposures are highly granular (more than 2 million active loans), the retail banking credit risk management process is based on a portfolio approach. This is reflected in the statistical profile of risk rating models including the models which fulfil the regulatory requirements of the Advanced Internal Ratings-Based approach (AIRB). The AIRB parameters (PD, LGD and EL) are used widely in order to estimate credit requirements, to determine acceptance criteria and terms of transactions, and to report risks.

Furthermore, the Retail Banking credit risk management has the following characteristics:

- high standardisation and automation of the credit process, including decision-making, both in acquisition, post-sale services, and debt collection;
- little (as compared to Corporate Banking) discretionary competences in the decision-making process (e.g. no discretionary adjustment of clients' ratings);
- extensive risk reporting system based on portfolio analysis of credit exposure quality, including vintage analysis and roll-rates analysis.

Under the portfolio approach, exposures are classified (separately for each market) as ML (mortgage-secured products) or NML (unsecured products or products with non-mortgage collateral). Furthermore, the segmentation includes products for individuals (ML OF, NML OF) and products for business clients (ML MF, NML MF).

The main point of reference in the retail banking credit risk management process is risk appetite defined in correlation with the strategy of the mBank Group. The general principle underlying the lending strategy of the Group in terms of sales of retail loans is to address the offer to clients who have an established relationship with the bank or to address it to new clients for whom the loan is a product initiating a long-term relationship of highly transactional nature. Consequently, the bank continues to focus its NML policies on lending to existing clients with a high creditworthiness while systematically growing the acquisition of external clients. To achieve this growth bank provides financing to clients doing shopping online. To reduce risks of accepting new clients, the bank develops its credit policy using, among others, credit testing and is actively developing its fraud prevention system.

The new acquisition focuses on products which may be financed with issue of mortgage bonds. Those exposures will then be transferred to mBank Hipoteczny in the pooling process to enable the issue of mortgage bonds. The conservative policy of assessing borrowers' reliability and creditworthiness is applied; taking into account, inter alia, current, historically lowest, levels of interest rates, the Group attaches special attention to the application of long-term estimates of interest rate while assessing creditworthiness.

Additionally, in order to mitigate the risk associated with a decrease in the value of mortgage collateral in relation to the value of credit exposure, the Group's credit offer is (and will be) directed mainly to clients who buy properties within large urban areas.

Quality of the mBank Group loan portfolio

As a result of implementation of IFRS 9 on January 1, 2018, new model of impairment of financial assets has been introduced. It is based on the concept of expected credit loss (ECL) which includes information about future events. The change has influence on classification of exposures, modelling of risk parameters and level of credit risk provisions, which incorporate forecasts of economic environment in respect to credit risk measurement.

Part of the portfolio measured in IAS 39 at amortized cost, after the implementation of IFRS 9 is measured at fair value through profit and loss. For this part of the portfolio, specific credit risk adjustment is being reported as credit risk costs.

As of June 30, 2018, the share of impaired exposures in the total (gross) amount of loans and advances granted to clients remained stable at 5.2% in comparison to the end of 2017.

Credit risk costs for loans and advances to customers increased from PLN 2,911.9 million at the end of December 2017 to PLN 3,340.1 million at the end of June 2018. This change takes into account the effect of the transition from IAS 39 to IFRS 9 (including the impact of the valuation of part of the portfolio at fair value through profit and loss, starting from January 1, 2018).

The ratio of credit risk costs to impaired exposures remained at a similar level – 59% at December 2017, 60% at June 2018.

The manner of identifying evidence of default is based on all available credit data of a given client and encompasses all of the client's liabilities towards the bank.

The table below presents the quality of mBank Group loan portfolio as at the end of June 2017, the end of December 2017 and as at the end of June 2018. The summary for June 2018 is presented in accordance with the reporting requirements of International Financial Reporting Standard 9 and it includes loans and advances to customers that are classified as assets measured at amortized cost.

Quality of the mBank Group loan portfolio	30.06.2017 (in thou. PLN)	31.12.2017 (in thou. PLN)
Loans and advances to individuals:	48,757,793	48,142,786
- current accounts	7,039,110	7,324,329
- term loans, including:	41,718,683	40,818,457
- housing and mortgage loans	34,005,417	32,593,180
- other	-	-
Loans and advances to corporate entities:	36,142,978	37,941,722
- current accounts	5,126,975	5,187,588
- term loans:	29,077,561	30,599,981
- large enterprises	4,840,701	5,030,702
- medium & small enterprises	24,236,860	25,569,279
- reverse repo/buy sell back	93,825	57,119
- other	1,844,617	2,097,034
Loans & advances to public sector	1,081,106	995,570
Other receivables	239,484	307,627
Total (gross) loans and advances to customers	86,221,361	87,387,705
Provision for loans and advances to customers (negative amount)	-2,844,336	-2,911,861
Total (net) loans and advances to customers	83,377,025	84,475,844
Short-term (up to 1 year)	27,827,783	29,191,490
Long-term (over 1 year)	55,549,242	55,284,354
Incurred but not identified (IBNI) losses		
Gross balance sheet exposure	81,653,575	82,883,395
IBNI loss provision for portfolio exposures	-232,926	-243,810
Net balance sheet exposure	81,420,649	82,639,585
Impaired exposures		
Gross balance sheet exposure	4,567,786	4,504,310
Provisions for impaired exposures	-2,611,410	-2,668,051
Net balance sheet exposure	1,956,376	1,836,259

Loans and advances to customers 30.06.2018	Gross carrying amount	Gross carrying amount		
		Individual customers	Corporate customers	Public sector customers
Current accounts	11,786,887	6,587,808	5,192,844	6,235
Term loans, including:	65,791,297	42,008,608	23,014,624	768,065
- housing and mortgage loans to individual customers	33,963,379	33,963,379	-	-
Reverse repo/buy-sell-back	29,025	-	29,025	-
Finance leases	9,836,152	-	9,836,152	-
Other loans and advances	2,377,853	199,040	2,178,813	-
Other receivables	138,098	-	138,098	-
Total gross carrying amount	89,959,312	48,795,456	40,389,556	774,300

Loans and advances to customers 30.06.2018	Accumulated impairment	Accumulated impairment		
		Individual customers	Corporate customers	Public sector customers
Current accounts	-1,013,211	-759,159	-254,052	-
Term loans, including:	-1,801,788	-994,568	-806,416	-804
- housing and mortgage loans	-439,463	-439,463	-	-
Reverse repo / buy-sell-back	-	-	-	-
Finance leases	-237,120	-	-237,120	-
Other loans and advances	-26,602	-	-26,602	-
Other receivables	-3	-	-3	-
Total accumulated impairment	-3,078,724	-1,753,727	-1,324,193	-804
Total gross carrying amount	89,959,312	48,795,456	40,389,556	774,300
Total accumulated impairment	-3,078,724	-1,753,727	-1,324,193	-804
Total net carrying amount	86,880,588	47,041,729	39,065,363	773,496

In addition, the accumulated credit risk costs related to the portfolio of loans and advances to customers, which from January 1, 2018 are obligatorily measured at fair value through profit and loss, amounted to PLN 261,4 million as at June 30, 2018.

Market risk

mBank organises market risk management processes in line with the requirements resulting from the law and supervisory recommendations, in particular the PFSA Recommendations (among others A, C, G and I) and EBA guidelines, concerning market risk management.

Tools and measures

In its business, mBank is exposed to market risk, i.e. the risk of unfavourable changes in the present value of financial instruments in the bank's portfolios due to changes in market risk factors: interest rates, FX rates, stock prices and index value, the implied volatility of options, and credit spreads. In terms of the banking book mBank identifies interest rate risk, which is defined as a risk of adverse change in both valuation of banking book positions and net interest income arising from adverse movements in interest rates.

The bank identifies market risk related to positions of the trading book measured at fair value (using the direct measurement method or the model measurement method) attributes market risk to the banking book positions (regardless of the methods for calculating earnings generated from those positions used for the purpose of accounting reporting). Market risk measures of the interest positions of the banking book are calculated with the use of net present value (NPV) models.

In order to reflect the interest rate risk of products without a fixed repricing date and with rates administered by the bank, replicating portfolio models are used. Since the beginning of 2018 the approach to current accounts takes into account the division of the stable part into the parts sensitive and insensitive

to changes in interest rates. The tenor structure adopted for stable parts of the capital and current accounts, insensitive to changes in interest rates, reflects the bank's strategy to stabilize the net interest income. Measurement and analysis of market risk takes place in two perspectives (including and without taking into account the modelling of stable parts of capital and current accounts, insensitive to changes in interest rates), which allows controlling the impact on the market risk level of the applied strategy for stabilizing net interest income

Market risk exposure is quantified by measurement of Value at Risk (VaR), Stressed Value at Risk (Stressed VaR), expected loss under condition that this loss exceeds Value at Risk (ES – Expected Shortfall) and by use of stress tests.

Market risk, in particular interest rate risk of the banking book, is also quantified by measurement of Earnings at Risk (EaR) of the banking book.

The bank uses BPV and CS BPV measures (+1 basis point) to limit the exposure of the mBank Group to interest rate risk in tenors above 20 and 30 years and the credit spread risk, respectively.

Strategy

The implementation of market risk management strategy involves managing the bank's positions in a way enabling to maintain market risk profile within the risk appetite defined by the bank.

The bank is focused on meeting customers' business needs, while reducing trade in derivatives in terms of currency, currency pairs, nominal values and tenors of transactions, as well as applying the principle of lack of commodity open positions. mBank has limited appetite for currency risk, which is expressed through market risk limits. The bank conducts trading activity on well-known markets using financial instruments the bank has adequate expertise in and that have been approved for trading.

Bank stabilizes interest income using long-term fixed-rate assets and derivatives and assuming - for stable parts of equity and current accounts - the maximum modelled maturity profile of 5 years. Managing interest rate risk of the banking book takes into account the economic and accounting perspectives, and the financial instruments used for hedging are adequate to the bank's expertise and have been approved for trading.

The market risk profile is derived from the strategic goals of business units, the policy of the Committee (ALCO) in charge of shaping the structure of the Group's assets and liabilities and the limits on market risk exposure established by the Financial Markets Risk Committee (KRF) at the bank level, and by the Management Board and Supervisory Board at the Group level. The system of limits reflects in a quantitative manner the defined risk appetite.

In accordance with the previously described general principles of risk management, market risk management is organized under so-called three lines of defence. The main principle stipulates separation between the market risk monitoring and control function and the functions related to opening and maintaining open market risk positions.

In addition, the bank applies the rule of organizational separation between managing banking book and trading book operations.

Measuring mBank's market risk

Value at Risk

In H1 2018, the bank's market risk exposure, measured by Value at Risk (VaR, for one day holding period, at 97.5% confidence level), was moderate in relation to the VaR limits.

The VaR figures were driven mainly by portfolios of instruments sensitive to interest rates and to selected credit spread – T-bonds portfolios in the banking and trading book and interest rate swap positions.

The table below presents VaR statistics of mBank's portfolio (excluding the modelling of stable parts of capital and current accounts, insensitive to changes in interest rates) in H1 2018 in comparison to statistics of this measure without capital modelling for 2017:

PLN thou.	H1 2018				2017			
	30.06.18	average	max	min	31.12.17	average	max	min
VaR IR	26,767	25,185	27,962	23,487	9,423	9,970	15,641	5,281
VaR FX	359	416	660	232	545	360	870	138
VaR EQ	18	70	207	18	53	140	1,151	15
VaR CS	13,003	11,534	13,223	10,659	11,441	13,980	23,320	10,431
VaR	29,619	24,270	31,175	20,129	14,038	18,685	34,560	13,429

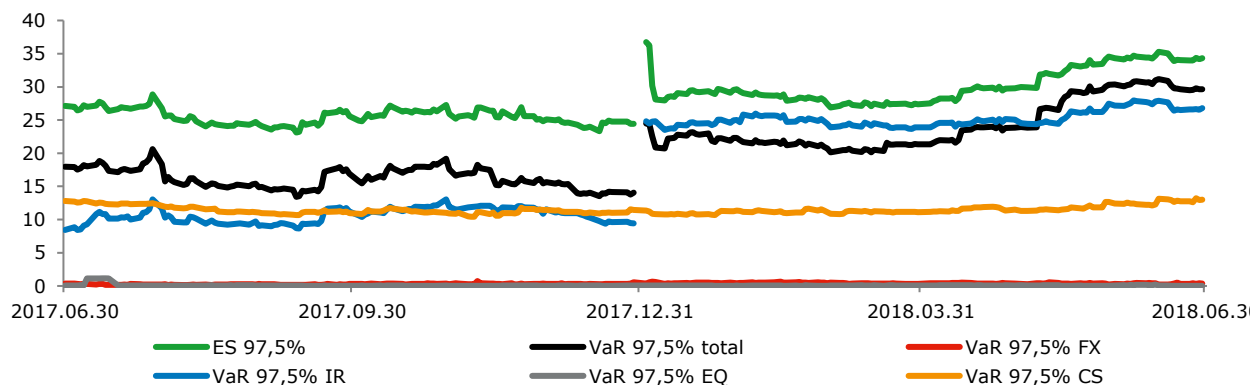
VaR IR – interest rate risk

VaR FX – FX risk

VaR EQ – stock price risk

VaR CS – credit spread risk.

VaR for mBank by risk factors



In H1 2018, VaR increased mainly due to change in approach to stable parts of current accounts insensitive to changes in interest rates and changes of observations in the 12-month window taken to calculation.

Stress testing

The results of stress tests for mBank (excluding the modelling of stable parts of capital and current accounts, insensitive to changes in interest rates) in H1 2018 in comparison to statistics of this measure without capital modelling for 2017 is presented in the table below:

PLN M	H1 2018				2017			
	30.06.18	average	max	min	31.12.17	average	max	min
Base stress test	481	437	485	393	141	85	147	9
CS stress test	760	718	768	694	694	688	767	624
Total stress test	1,241	1,155	1,246	1,104	835	774	882	638

Base stress test – standard stress test

CS stress test – stress test with scenarios including credit spread changes

Total stress test – total stress test (sum of the standard stress test and the stress test with scenarios including credit spread changes).

In H1 2018, the average utilisation of the stress test limit for mBank was:

- 62% (PLN 1 155.1 million) – for portfolio without modelling of stable parts of capital and current accounts, insensitive to changes in interest rates,
- 58% (PLN 843,0 million) - for portfolio with modelling of stable parts of capital and current accounts, insensitive to changes in interest rates

The main part of the presented stress test results is the value of stress tests for change of the credit spread of T-bond portfolios because the stress test scenarios assume on average a 100 bps increase of credit spreads.

Interest rate risk of the banking book

In H1 2018 the interest rate risk of the banking book as measured by EaR, i.e. potential decrease of interest income within 12 months assuming an unfavourable 100 bps change of market interest rates (parallel shift of the curve by 100 basis points) and based on a stable portfolio over the period, was as presented in the table below:

PLN M	H1 2018				2017			
	30.06.18	average	max	min	31.12.17	average	max	min
PLN	163.9	145.9	192.1	98.5	186.0	137.4	254.3	86.8
USD	8.9	13.8	16.3	8.9	14.9	13.6	17.9	8.6
EUR	91.5	102.9	117.0	88.1	84.9	94,1	113.1	67.3
CHF	0.0	0.0	0.0	0.0	0.0	0.1	0.1	0.0
CZK	21.1	17.8	23.9	9.2	12.0	4.8	12.0	2.2

Measuring mBank Group's market risk

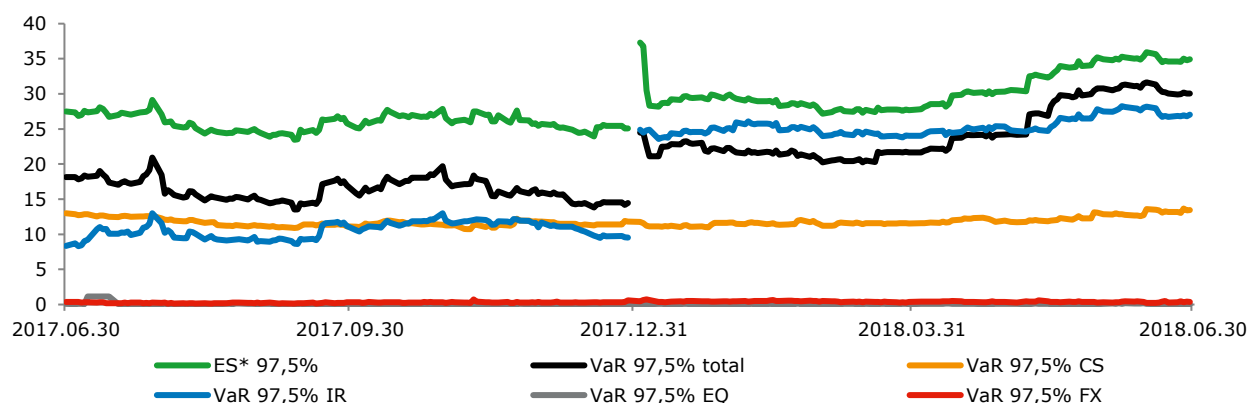
The main sources of market risk of the Group are mBank's positions. The table below shows VaR statistics (VaR at a 97.5% confidence level for a one-day holding period) for mBank Group in 2017 for individual members of the Group in which market risk positions were identified (i.e. portfolios of mBank, mBank Hipoteczny, mLeasing) and their decomposition to the VaR corresponding to the main risk factor types – interest rate risk (VaR IR), foreign exchange risk (VaR FX), stock prices/index value risk (VaR EQ), and credit spread risk (VaR CS).

The table below presents VaR statistics (in approach without modelling of stable parts of capital and current accounts, insensitive to changes in interest rates) in H1 2018:

PLN thou.	mBank Group	mBank	mBH	mLeasing
VaR IR average	25,353	25,185	156	46
VaR FX average	422	416	24	10
VaR EQ average	70	70	0	0
VaR CS average	11,927	11,534	410	0
VaR average	24,509	24,270	417	48
VaR max	31,644	31,175	498	85
VaR min	20,228	20,129	353	25
VaR 31.12.2017	30,070	29,619	474	67

For comparison, at the end of 2017, VaR for mBank Group (without capital) was PLN 14,472 thou., including VaR of mBank at PLN 14,038 thou., mBank Hipoteczny – PLN 408 thou. and mLeasing – PLN 29 thou.

VaR for mBank Group by risk factors



Stress testing

The result of stress tests for mBank Group (without modelling stable parts of capital and current accounts, insensitive to changes in interest rates) in H1 2018 in comparison to statistics of this measure without capital modelling for 2017 is presented in the table below:

PLN M	H1 2018				2017			
	30.06.18	average	max	min	31.12.17	average	max	min
Base stress test	484	443	493	399	146	89	155	11
CS stress test	782	740	791	713	713	703	782	635
Total stress test	1,266	1,183	1,278	1,131	859	792	903	655

Base stress test – standard stress test

CS stress test – stress test with scenarios including credit spread changes

Total stress test – total stress test (sum of the standard stress test and the stress test with scenarios including credit spread changes).

In H1 2018, the average utilisation of the stress test limit for mBank Group was:

- 62% (PLN 1 183.3 million) – for portfolio without modelling stable parts of capital and current accounts, insensitive to changes in interest rates,
- 57% (PLN 855.8 million) – for portfolio with modelling stable parts of capital and current accounts, insensitive to changes in interest rates.

Liquidity risk

mBank organises liquidity risk management processes in line with the requirements resulting from the law and supervisory recommendations in particular the PFSA Recommendations (among others P, C, H and S) as well as EBA guidelines concerning liquidity risk management.

Tools and measures

In its operations, mBank is exposed to liquidity risk, i.e. the risk of being unable to honour its payment obligations, arising from the bank's balance-sheet and off-balance-sheet positions, on terms favourable to the bank and at a reasonable price.

In terms of its sources, liquidity risk may result from internal factors (reputation risk resulting for instance in excessive withdrawal of cash by bank clients, materialisation of credit risk) and external factors (turbulences and crises in the financial markets, country risk, turbulences in the operation of clearing systems).

The bank has defined a set of liquidity risk measures and a system of limits and warning thresholds which protect the bank's liquidity in the event of unfavourable internal or external conditions. Independent measurement, monitoring and controlling of liquidity risk is performed daily by the Integrated Risk Management Department. The main measures used in liquidity risk management of the bank include

measures based on liquidity gap calculation in LAB methodology, the regulatory measures (M3, M4, LCR) and also NSFR (Net Stable Funding Ratio) for analysis only. LAB measures reflect the projected future cash flow gap of assets, liabilities and off-balance-sheet commitments of the bank, which represent potential risk of being unable to meet liabilities within a specific time horizon and under a certain scenario.

The methodology for measuring the liquidity gap (LAB) includes normal conditions scenario (LAB Base Case) and stress scenarios, of which the following are limited:

- LAB Bank Stress (short-term) – short-term scenario (up to 2 weeks) of the idiosyncratic stress,
- LAB Market Stress (long-term) – long-term scenario (up to 2 months) of the market crisis,
- LAB Combined Stress I – combined stress scenario that presents the effects of the simultaneous occurrence of short-term idiosyncratic stress and long-term market related stress,

Cash flow projections used in LAB measures are based on crisis scenarios, which include among others excessive withdrawal of cash by the bank's clients and being unable to liquidate some assets due to an external crisis occurring to various extent dependent on assumed scenario.

Moreover, the bank has a process of reporting and monitoring of intraday liquidity position including crisis scenario for intraday liquidity. The reverse stress scenario is the complement of the liquidity stress testing system.

In order to support the process of liquidity risk management, the bank has a system of early warnings indicators (EWI) and recovery indicators. It is composed of indicators monitoring the level of regulatory and internal limits and additionally, indicators monitoring significant changes of market factors, as well as changes in the bank's balance sheet. Exceedance of thresholds by defined indicators may be a trigger for the launch of the Contingency Plan or the Recovery Plan.

LCR calculation and reporting is carried out in accordance with the Delegated Commission Regulation (EU) 2015/61 of October 10, 2014, which has been in force since October 2015.

With the respect of NSFR, the bank reports to the NBP according to the standards established by EBA in 2014, and reports to the PSFA in the form of a dedicated questionnaire.

Strategy

The liquidity strategy is pursued by active management of the balance sheet structure and future cash flows as well as maintenance of liquidity reserves adequate to liquidity needs depending on the activity of the bank and the current market situation as well as funding needs of the Group subsidiaries.

The bank manages liquidity risk at two levels: strategic (within committees of the bank) and operational (Treasury Department).

Liquidity risk limiting covers supervisory (M3, M4, LCR) and internal measures.

The liquidity risk internal limit system is based mainly on defining acceptable level of gaps in stress conditions in specific time horizons and for different liquidity risk profiles (for all currencies in aggregate converted to PLN) and for specific foreign currencies. Internal limits also apply to M1 and M2, which are no longer regulatory measures.

The bank has a centralised approach to the Group's funding management in order to increase the efficiency of liquidity resources used. Financing of subsidiaries is done from mBank via the Treasury Department. Additionally mBank Hipoteczny raises funding in the market by issuance of covered bonds and short-term debt securities and mLeasing raises funding by issuance of short-term debt securities.

The bank has the Contingency Plan in case of a threat of losing financial liquidity, which sets the strategy and procedures to be implemented in the event of a situation connected with the risk of losing liquidity by the mBank Group and aimed at neutralising this threat. The document defines the division of responsibility for monitoring and identifying threats, and actions during the emergency situation. The Contingency Plan is tested at least annually.

The bank has developed the Recovery Plan of mBank Group covering situations, where a broader range of actions, than those defined in the Contingency Plan, is required.

Bank limits the volume and term concentration of foreign currency funding of mBank with FX swaps and CIRS. In addition, the limit is decomposed into individual limits for CIRS and FX swaps as well as limits for funding in EUR and CHF. The structure of these limits reflects the bank's preferences for funding structure in those currencies.

In the bank the review of internal liquidity adequacy assessment process (ILAAP) is conducted. The process covers the bank and the mBank Group. The results of the review are presented to the Management Board and the Supervisory Board.

Measuring mBank's liquidity risk

The liquidity of mBank remained at a safe level in H1 2018, as reflected in the high surplus of liquid assets over short-term liabilities in LAB measures and in the levels of regulatory measures.

The table below presents the LAB gaps for tenors up to 1M and 1Y and the regulatory measures M3, M4, LCR in H1 2018:

Measure*	2018			
	30.06.2018	average	maximum	minimum
LAB Base Case 1M	17,269	15,593	19,353	12,420
LAB Base Case 1Y	11,348	9,054	12,525	4,634
LAB Bank Stress 1M	11,087	9,971	13,506	6,650
LAB Market Stress 1M	13,949	13,780	17,092	10,051
LAB Combined Stress 1M	9,474	9,456	12,957	5,410
M3	4,82	4,56	4,83	4,09
M4	1,40	1,39	1,41	1,35
LCR	144%	161%	184%	137%

* LAB measures are shown in PLN million; M3, M4 and LCR are relative measures presented as a decimal.

Measuring the Group's liquidity risk

The Group's liquidity risk measurement includes in addition mBank Hipoteczny and mLeasing. mBank monitors liquidity risk of the subsidiaries to protect liquidity also at the Group level in the event of adverse events (crises).

The Group's liquidity was at a safe level in H1 2018, as reflected in the high surplus of liquid assets over short-term liabilities in the LAB measures and the LCR calculated at the Group level.

The table below presents the LAB gaps for tenors up to 1M and 1Y and the LCR at the mBank Group level:

Measure*	2018			
	30.06.2018	average	maximum	minimum
LAB Base Case 1M	19,687	17,623	21,060	14,952
LAB Base Case 1Y	17,057	13,513	17,177	9,961
LAB Bank Stress 1M	13,505	11,993	15,213	9,123
LAB Market Stress 1M	16,367	15,803	18,890	12,349
LAB Combined Stress 1M	11,892	11,479	14,725	7,883
LCR Group	166%	194%	227%	165%

*LAB measures are shown in PLN million, LCR is relative measure presented as a decimal.

Operational risk

mBank organises the operational risk management process taking into account the rules and requirements set out in external regulations, in particular in the Recommendations M, H and D of the Polish Financial Supervision Authority, CRR Regulation and Regulation of the Minister of Development and Finance (on the risk management system and internal control system, remuneration policy and detailed method of estimating internal capital in banks), which constitute a starting point for the framework of the operational

risk control and management system in mBank Group. In addition through operational risk tools, the bank analyses the potential risks that may occur in various banking areas and defines corrective action plans that are intended to protect the bank from unexpected events.

Tools and measures

Operational risk accompanies all processes at banks and its consequences can be often very harmful. It is characterized by an asymmetric distribution of losses; overwhelmingly, these are small value losses. Large losses are rare but the size of such a loss may exceed the sum of all the remaining operational losses in a given reporting period.

In order to effectively manage operational risk, the bank applies quantitative and qualitative methods and tools. The tools applied by the bank intend to cause-oriented operational risk management.

The basic qualitative tool is the internal control system self-assessment carried out by the bank's organizational units and the Group subsidiaries. The aim of the process is to ensure communication about the necessity of changes and improvements in control processes, and thus a more active approach to operational risk management and to increase the awareness of operations risk in mBank Group. In Self-Assessment process the significant processes were indicated and their connection to general and specific objectives. The end result of the self-assessment is the assessment of risks and control mechanisms as well as the creation of recovery plans aimed at changing the structure or the optimization of the control mechanisms in order to improve the adequacy and effectiveness of internal control system.

The bank prepares also scenario analyses describing risks associated with rare operational risk events with potentially very serious consequences.

In accordance with the requirements of Recommendation M, the bank has a process for identifying threats associated with operational risk in all relevant areas of the bank's operations and for creating new and modifying existing products, processes and systems, as well as for changes in the organizational structure.

Quantitative tools of the operational risk methodology include mainly collection of data on operational events and effects. With the use of the database available at the mBank Group, data on operational risk losses are recorded with an emphasis on the cause. Recorded data are analysed by the Integrated Risk Management Department and at organizational units. This approach allows organizational units to carry out ongoing monitoring of their current risk profile. mBank has an access to external operational loss databases and applies them to analyse operational risk and potential threats, that institutions operating in the financial sector are exposed to.

The key risk indicators (KRI) are another tool. Ongoing monitoring of risk factors recognized as key at the given moment will allow for prediction of an increased level of operational risk and adequate response by the organizational units in order to avoid the occurrence of operational events and losses.

Strategy

The operational risk control and management system, forms an organisational basis in order to enable effective control and management of operational risk at every level of mBank's organisational hierarchy. The structure of operational risk control and management covers in particular the role of the Management Board of the bank, the Business and Risk Forum, the Chief Risk Officer, the Integrated Risk Management Department, and the tasks assigned to persons managing operational risk in particular organisational units and business areas of the bank. The operational risk control and management process at mBank is developed and co-ordinated by the central operational risk control function while operational risk management takes place in every organisational unit of the bank and in every subsidiary of mBank Group. It consists in identifying and monitoring operational risk and taking actions aimed to avoid, mitigate or transfer operational risk.

The entire operational risk control process is supervised by the Supervisory Board of the bank through its Risk Committee.

4.3. Capital adequacy

One of the bank's main tasks is to ensure an adequate level of capital. As part of the capital management policy, the bank creates a framework and guidelines for the most effective planning and use of the capital base, which:

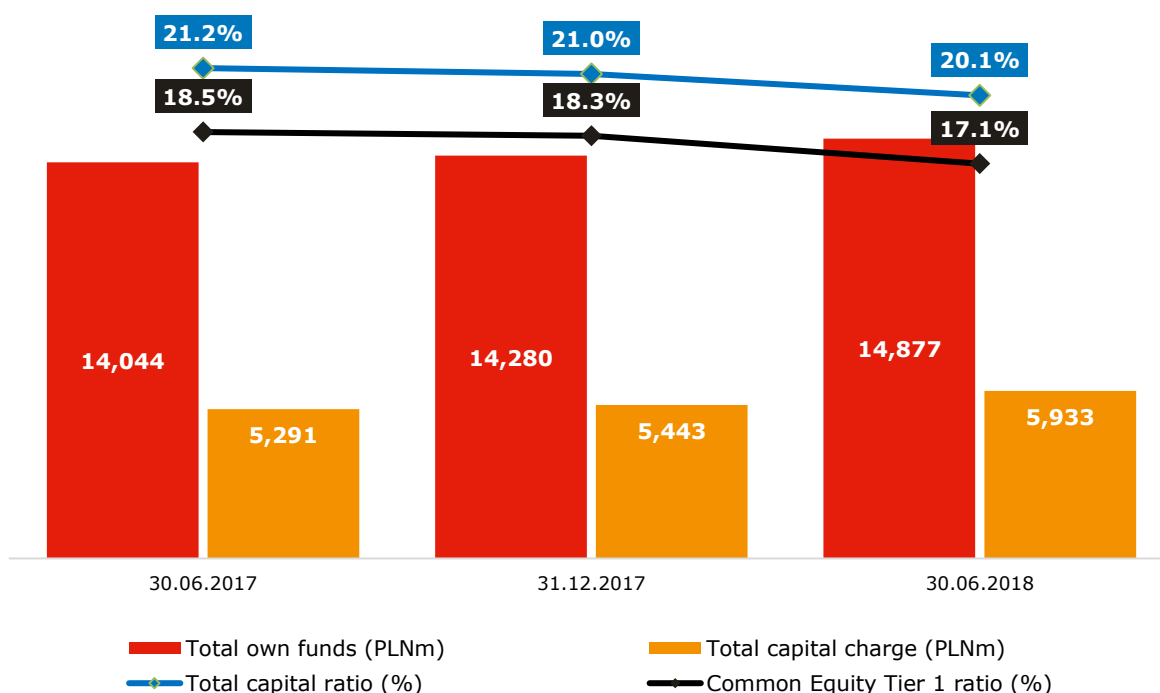
- are compliant with external and internal regulations in force,
- guarantee a continuity of financial targets achievement, which render an appropriate rate of return for shareholders,
- ensure the maintenance of a strong capital basis being a fundamental support for business development.

The capital management policy in mBank is based on:

- maintenance of an optimal level and structure of own funds with the application of available methods and means, like among others retention of net profit, subordinated loan or issue of shares,
- effective use of existing capital, among others through application of a set of measures of effective use of the capital, limitation of activities that do not provide an expected rate of return and development of products with lower capital absorption.

The strategic goals of mBank and mBank Group are aimed at maintaining the total capital ratio as well as the Common Equity Tier 1 capital ratio above the levels required by the supervision authority. This allows to maintain business development while meeting the supervisory requirements in the long perspective.

Capital adequacy of mBank Group



The capital ratios of mBank Group in H1 of 2018 were driven by the following factors:

- inclusion, in Common Equity Tier 1 capital, of the additional remaining part of the verified net profit of the mBank Group for Q1, Q2 and Q3 2017, not included in Common Equity Tier 1 capital net of expected charges and dividends, on the basis of the PFSA decisions of March 29, 2018 (no DBK-DBK2.700.5.2018, nr DBK-DBK2.700.7.2018, nr DBK-DBK2.700.9.2018);

- inclusion in Common Equity Tier 1 capital of the remaining part (not included earlier) of the net profit of mBank Group for the year 2017 as approved by the General Meeting of Shareholders, net of paid dividend;
- change of the limit for unrealized gains measured at the fair value included in the own funds calculation from 80% in 2017 to 100% in 2018;
- discontinued application of the transitional provisions for own funds in terms of grandfathering with regard to subordinated instruments included in the own funds;
- expansion of the mBank Group business activity;
- depreciation of the Polish zloty against the foreign currencies;
- implementation of the International Financial Reporting Standard 9, which had no significant impact on Group's capital ratios.

The level of the required capital ratios at the end of June 2018 was among others affected by the following administrative decisions and applicable regulations:

- according to the PFSA decision, in 2016 mBank had been identified as other systemically important institution (O-SII) subject to a capital buffer; according to the PFSA decision of December 19, 2017, the capital buffer amounted to 0,75% of the total risk exposure amount, calculated in accordance with the provisions of the CRR Regulation, to be maintained on individual and consolidated levels. The required capital buffer was applicable as of June 30, 2018;
- according to the PFSA decision of November 20, 2017, and the subsequent communication of December 15, 2017 mBank should maintain additional own funds on individual basis with regard to the risks related to the portfolio of FX retail mortgage loans of 4.10% at the level of total capital ratio and 3.07% at the level of Tier 1 capital (on consolidated basis: 3.53% and 2.65% accordingly);
- starting from January 1st, 2018 the Regulation of the Minister of Development and Finance with regard to systemic risk buffer entered into force. The Regulation introduced systemic risk buffer of 3% of the total risk exposure amount applied to all exposures located in Poland. Due to the fact that not all exposures are located in Poland, due to mBank two foreign branches in Czech Republic and in Slovakia, the systemic risk buffer rate applicable to mBank Group amounted to 2,8% in June 2018.

Consequently the level of the required capital ratios encompasses:

- the basic requirement resulting from CRR provisions to maintain the total capital ratio of 8% and the Tier 1 ratio of 6%;
- the additional capital charge in Pillar II with regard to FX mortgage loan portfolio – 3.53% at the level of total capital ratio and 2.65% at the level of Tier 1 capital on consolidated basis (and on individual basis 4.10% and 3.07% accordingly);
- the combined buffer requirement of additional 5.45%, which consists of the capital conservation buffer (1.88%), the other systemically important institution's buffer (0.75%), systemic risk buffer (2.8%) and countercyclical capital buffer (0.02%).

Capital ratios on consolidated and individual basis were above the values required throughout H1 2018.

With a considerable surplus of own funds mBank Group comfortably meets the additional own funds requirement and the combined buffer requirement.

Capital ratio	mBank Group		mBank	
	Required level	30.06.2018	Required level	30.06.2018
Total capital ratio (TCR)	17.0%	20.1%	17.5%	23.7%
Tier 1 ratio	14.1%	17.1%	14.5%	20.2%

The consolidated leverage ratio as of June 30, 2018, calculated in accordance with the provisions of the CRR Regulation and Commission Delegated Regulation (EU) 2015/62 of October 10, 2014, amending Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to the leverage ratio, including provisions regarding transitional period, amounted to 8.52%. The stand-alone leverage ratio amounted to 8.64%.

Stress tests

Stress tests are an essential tool used for managing the bank and the Group and for capital and liquidity planning. In order to ensure compliance with regulatory requirements under normal and stress conditions the Group and the bank carry out sensitivity analyses and scenario analyses for key concentration risks. The Management Board decides on the choice of a risk scenario used for management purposes to ensure adequate capital and liquidity resistance of the mBank Group in crisis situations.

Additionally integrated stress tests are conducted based on scenario of unfavourable economic conditions that may adversely affect the bank's financial position in at least a full two-year time horizon (for liquidity risk: a one-year time horizon). The risk scenario, i.e. the most plausible scenario of negative deviations from the base scenario, expressed in terms of macroeconomic and financial ratios, is common for all risk types, applied at Group level and aligned with the corresponding scenario accepted by the consolidating entity.

The Group and the bank carries out so called reverse stress tests the goal of which is to identify events potentially leading to unviability of the Group and the bank. Reverse stress tests are used for the verification of capital and liquidity contingency plans of the Group and for making strategic decisions concerning accepted risk profile of the Group.

5. Statements of the Management Board

True and fair picture in the presented reports

The Management Board of mBank S.A. declares that according to their best knowledge:

- IFRS Condensed Consolidated Financial Statements for the first half of 2018 and the comparative figures were prepared in compliance with the binding accounting principles and present a true, fair and clear picture of the financial position and the condition of the assets of mBank S.A. Group as well as its financial performance;
- Management Board Report on the Performance of mBank S.A. Group in the first half of 2018 presents a true picture of the developments, achievements, and situation of the mBank S.A. Group, including a description of the main risks and threats.

Appointment of the auditor

The Auditor authorised to audit financial statements and performing the review of the IFRS Condensed Consolidated Financial Statements of mBank S.A. Group for the first half of 2018 and IFRS Condensed Stand-alone Financial Statements of mBank S.A. for the first half of 2018 – Ernst & Young Audyt Polska spółka z ograniczoną odpowiedzialnością spółka komandytowa - was appointed in compliance with legal regulations. The audit company and its auditors fulfilled the conditions necessary for issue of a review report of these financial statements, in compliance with respective provisions of Polish law and professional standards.

Signatures of the Management Board of mBank S.A.

Date	First and last name	Position	Signature
31.07.2018	Cezary Stypułkowski	President of the Management Board, General Director of the Bank	
31.07.2018	Frank Bock	Deputy President of the Management Board, Head of Financial Markets	
31.07.2018	Andreas Böger	Deputy President of the Management Board, Chief Financial Officer	
31.07.2018	Krzysztof Dąbrowski	Deputy President of the Management Board, Head of Operations and Information Technology	
31.07.2018	Lidia Jabłonowska-Luba	Deputy President of the Management Board, Chief Risk Officer	
31.07.2018	Cezary Kocik	Deputy President of the Management Board, Head of Retail Banking	
31.07.2018	Adam Pers	Deputy President of the Management Board, Head of Corporate and Investment Banking	