

21. Hedge accounting

Fair value hedge accounting

The Group applies fair value hedge accounting, under which the only kind of hedged risk is the risk of changes in interest rates.

At the end of each month, the Group evaluates effectiveness of the applied hedging by carrying out analysis of changes in fair value of the hedged and hedging instruments in respect of the hedged risk in order to confirm that hedging relationships are effective in accordance with the accounting policy described in Note 2.14.

Description of the hedging relation

The Group hedges against the risk of change in fair value:

- fixed interest rate Eurobonds issued by mFinance France S.A. (mFF), subsidiary of mBank. The hedged risk results from changes in interest rates.
- mortgage bonds issued by mBank Hipoteczny (mBH), a subsidiary of mBank. The hedged risk results from changes in interest rates.
- loans received by mBank from European Investment Bank. The hedged risk results from changes in interest rates.

Hedged items

The hedged items are:

- three tranches of fixed interest rate Eurobonds issued by mFF with a total nominal value of EUR 1 500 000 thousand,
- two tranches of fixed interest rate Eurobonds issued by mFF with a total nominal value of CHF 400 000 thousand,
- fixed interest rate Eurobonds issued by mFF with a nominal value of CZK 500 000 thousand,
- fixed interest rate mortgage bonds issued by mBH with a nominal value of EUR 124 000 thousand,
- fixed interest rate loans received by mBank from European Investment Bank with a nominal value of respectively EUR 100 000 thousand and CHF 113 000 thousand.

Hedging instruments

IRS is the hedging instrument swapping the fixed interest rate for a variable interest rate.

Presentation of the result from hedged and hedging transactions

Fair value adjustment of the hedged assets and liabilities as well as valuation of the hedging instruments are recognised in the income statement as trading income.

The total results of fair value hedge accounting recognised in the income statement

	Year ended 31 December	
	2017	2016
Interest income on derivatives concluded under the fair value hedge accounting (Note 6)	66 808	59 936
Net profit on hedged items (Note 9)	72 015	(16 903)
Net profit on fair value hedging instruments (Note 9)	(78 131)	20 098
The total results of fair value hedge accounting recognised in the income statement	60 692	63 131

Cash flow hedge accounting

The Group applies cash flow hedge accounting of the part of loans at a variable interest rate indexed to the market rate portfolio, granted by the Bank. An Interest Rate Swap is the hedging instrument changing the variable interest rate to a fixed interest rate. The interest rate risk is the hedged risk within applied by the Group cash flow hedge accounting. The ineffective portion of the gains or losses on the hedging instrument is presented in Note 9 in the position "Other net trading income and result on hedge accounting". Portion of the gains or losses on the hedging instrument

that is an effective hedge, is presented in the statement of comprehensive income as "Cash flow hedges (net)".

The following note presents other comprehensive income due to cash flow hedges as at 31 December 2017 and 31 December 2016.

	Year ended 31 December	
	2017	2016
Other gross comprehensive income from cash flow hedge at the beginning of the period	(1 907)	1 061
- Unrealised gains/losses included in other gross comprehensive income during the reporting period	(4 511)	(2 968)
Accumulated other gross comprehensive income at the end of the reporting period	(6 418)	(1 907)
Deferred income tax on accumulated other comprehensive income at the end of the reporting period	1 220	362
Accumulated net other comprehensive income at the end of the reporting period	(5 198)	(1 545)
Impact on other comprehensive income in the reporting period (gross)	(4 511)	(2 968)
Deferred tax on cash flow hedges	858	564
Impact on other comprehensive income in the reporting period (net)	(3 653)	(2 404)

	Year ended 31 December	
	2017	2016
Gains/losses recognised in comprehensive income (gross) during the reporting period, including:		
- Unrealised gains/losses included in other comprehensive income (gross)	(4 511)	(2 968)
- Amount included as interest income in income statement recognised during the reporting period	15 780	15 874
- Ineffective portion of hedge recognised in other net trading income	(6 539)	(17 624)
Impact on other comprehensive income in the reporting period (gross)	4 730	(4 718)

Total results of cash flow hedge accounting recognised in the income statement

	Year ended 31 December	
	2017	2016
Interest income on derivatives concluded under the cash flow hedge (Note 6)	15 780	15 874
Ineffective portion of cash flow hedge accounting (Note 9)	(6 539)	(17 624)
The total results of cash flow hedge accounting recognised in the income statement	9 241	(1 750)

The period from January 2018 to February 2023 is the period in which the cash flows are expected, and when they are expected to have an impact on the result.

Below is given the timetable prepared as at 31 December 2017, presenting the periods in which the cash flows from loans secured under the cash flow hedge accounting are expected and their impact on the profit and loss account.

Cash flows from loans secured under the cash flow hedge accounting (PLN 000's)		
up to 3 months	period from 3 months to 1 year	period from 1 year to 5 years
25 720	77 036	297 008

Below is given the timetable prepared as at 31 December 2016, presenting the periods in which the cash flows from loans secured under the cash flow hedge accounting were expected and their impact on the profit and loss account.

Cash flows from loans secured under the cash flow hedge accounting (PLN 000's)		
up to 3 months	period from 3 months to 1 year	period from 1 year to 5 years
10 631	16 492	48 498

The fair value equal to book value of derivatives hedging was presented in Note 20 "Derivative financial instruments".