Management Board Report on the Performance of mBank S.A. Group in H1 2016

Table of contents

1. About mBank Group 3
1.1. Executive summary 3
1.2. mBank's Authorities 4
1.3. Composition of mBank Group and key areas of activity 5
1.4. Subsidiaries of mBank Group 8
1.5. Values of mBank Group 9
1.6. H1 2016 in numbers 10
1.7. Strategy of mBank Group for 2016-2020 11
1.8. Rating of mBank and Group subsidiaries 13
1.9. mBank shareholders and share price on the WSE 15
2. Business activity and key achievements 17
2.1. Key projects of mBank Group in H1 2016 17
2.2. Awards and distinctions 18
2.3. Retail Banking 20
2.4. Corporates and Financial Markets 26
2.5. Subsidiaries of mBank Group 34
2.6. Risk management 38
3. Financial results and macroeconomic environment 59
3.1. Economy and banking sector in H1 2016 59
3.2. Financial results of mBank Group in H1 2016 66
4. Statements of the Management Board 78

1. About mBank Group

1.1. Executive summary

mBank Group is the fourth-largest financial institution in Poland as measured by total assets. It offers 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 market 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.

In H1 2016 the Polish economy slowed down slightly as compared with the end of 2015. The decrease was primarily driven by a strong slowdown in investment, triggered by a considerable decrease in public investment in early 2016, which stems from the fact that the funds from the previous EU financial framework have already been spent and the spending of funds from the new budget is delayed. In these circumstances private consumption has become the main driver of economic growth. As in the past, it is helped by numerous factors, including: a high increase in real wages (the fastest since the outbreak of the financial crisis), first payments under the government's "Family 500+" child benefit programme, an exceptionally good household sentiment, a record-low unemployment rate, and an expansive monetary and fiscal policy.

The recent months have been marked by turbulence and growing volatility on financial markets. The most important event was the British EU referendum, which, to the surprise of a vast majority of observers and analysts, ended with the victory of leave supporters.

The unfavourable market environment taking the form of an economic slowdown, financial market turbulence, continued low interest rates as well as regulatory and tax changes (e.g. introduction of a new tax on assets of financial institutions) made H1 2016 a difficult period for Polish banks. In the discussed period (data until May 2016) the banking sector reported a 17.0% decrease in its cumulative net profit.

Despite the challenging market environment, mBank Group reported business growth across all segments. Driven by growing income, net profit rose compared with H1 2015.

The key events of H1 2016 include:

- Growth in the net profit of mBank Group by 3.6% to PLN 696.3 million compared with H1 2015.
- Adoption of the new 2016-2020 mBank Group's strategy.
- Increase in total income by 10.4% YoY, mainly thanks to higher net interest income and the booking of proceeds from the takeover of Visa Europe Limited by Visa Inc.
- Rise in operating expenses (including amortisation) by 3.8% against H1 2015 attributable to higher amortisation and higher staff-related expenses driven by the rising number of employees.
- Introduction of the so called "bank tax" – taxes on Group balance sheet items amounted to PLN 146.3 million in H1 2016.
- Rising volumes:
  - Increase in gross loans by 3.0% compared with the end of 2015, supported by active sales in the Retail Banking segment as well as in Corporate and Investment Banking segment. Excluding reverse repo/buy sell back transactions and the FX effect, gross loans rose by 2.5% YtD.
  - Considerable growth in clients' deposits (+5.1% compared with the end of 2015), triggered by growing deposits of both client segments, with higher growth recorded in the retail segment.
- The expansion on the market for retail loans was reflected by the record high sales of non-mortgage loans reaching PLN 3,052.9 million, which represents a rise by 24.2% compared with H1 2015.
- As a result of the rapid growth in deposits, the loan to deposit ratio reached a record level of 94.7%.

- Improved quality of assets combined with stable risk costs (47 basis points) compared with H1 2015 (54 basis points).
- High quality of capital base - capital ratios surpassing regulatory requirements: CET 1 ratio at 15.6%, Total Capital Ratio at 18.3%.
- Accelerating client acquisition – in 2016, 199 thousand individual and 658 corporate clients were acquired.

1.2. mBank's Authorities

Supervisory Board of mBank S.A.

In March 2016, Martin Blessing resigned from his position as Member of the Supervisory Board and the Executive Committee of the Supervisory Board as of April 30, 2016.

On March 24, 2016 Michael Mandel was appointed to replace Martin Blessing from May 1, 2016 to the end of the current term of office of the Supervisory Board.

Since 2010 Michael Mandel held the Executive position for Private Clients in Commerzbank AG. In May 2016 Michael Mandel took over the position of Member of the Board of Managing Directors at Commerzbank AG responsible for the private clients segment.

Consequently, the Supervisory Board of mBank S.A. is composed as follows:

1. Maciej Leśny – Chairman of the Supervisory Board
2. Martin Zielke – Deputy Chairman of the Supervisory Board
3. Andre Carls – Member of the Supervisory Board
4. Marcus Chromik – Member of the Supervisory Board
5. Stephan Engels – Member of the Supervisory Board
6. Thorsten Kanzler – Member of the Supervisory Board
7. Michael Mandel – Member of the Supervisory Board (replaced Martin Blessing as of May 1, 2016)
8. Teresa Mokrysz – Member of the Supervisory Board
9. Agnieszka Słomka-Gołębiowska – Member of the Supervisory Board
10. Waldemar Stawski – Member of the Supervisory Board
11. Wiesław Thor – Member of the Supervisory Board
12. Marek Wierzbowski – Member of the Supervisory Board

The five independent members of the Supervisory Board are: Maciej Leśny, Teresa Mokrysz, Agnieszka Słomka-Gołębiowska, Waldemar Stawski and Marek Wierzbowski.

Detailed résumés of all members of mBank authorities are available on www.mBank.pl

The Supervisory Board operates four committees: the Executive Committee, the Risk Committee, the Audit Committee, and the Remuneration Committee. The members of individual committees are presented below (first person listed is the committee chairman).

Executive Committee	Risk Committee	Audit Committee	Remuneration Committee
Maciej Leśny	Marcus Chromik	Stephan Engels	Andre Carls
Martin Zielke	Thorsten Kanzler	Andre Carls	Maciej Leśny
Andre Carls	Maciej Leśny	Maciej Leśny	Marek Wierzbowski
Teresa Mokrysz	Agnieszka Słomka-Gołębiowska	Waldemar Stawski	Martin Zielke

Management Board of mBank S.A.

On April 12, 2016 Jörg Hessenmüller informed the Bank about his resignation from the position of Member of the Management Board, Vice-President of the Management Board of mBank S.A, Chief Financial Officer, as of June 30, 2016. In July 2016 Jörg Hessenmüller assumed the position of Head of Group Strategy and Development in Commerzbank Group.

Jörg Hessenmüller was replaced by Christoph Heins appointed on June 10, 2016 by the Supervisory Board to act as Vice-President of the Management Board, Chief Financial Officer, from July 1, 2016 to the end of the current term of office of the Management Board. Recently Christoph Heins was the Head of Divisional Controlling in Commerzbank Group. Before, he occupied various positions in Commerzbank Group, both in Germany and abroad. In 2008-2012 he worked as CFO of Commerzbank's New York branch.

As at June 30, 2016, i.e. in the period covered by this Report, the Management Board of mBank was composed as follows:

1. Cezary Stypułkowski – President of the Management Board, Chief Executive Officer
2. Przemysław Gdański – Vice-President of the Management Board, Head of Corporate and Investment Banking
3. Jörg Hessenmüller – Vice-President of the Management Board, Chief Financial Officer (by June 30, 2016)
4. Lidia Jabłonowska-Luba – Vice-President of the Management Board, Chief Risk Officer
5. Hans-Dieter Kemler – Vice-President of the Management Board, Head of Financial Markets
6. Cezary Kocik – Vice-President of the Management Board, Head of Retail Banking
7. Jarosław Mastalerz – Vice-President of the Management Board, Head of Operations and Information Technology.

On July 1, 2016 the position of Vice-President of the Management Board, Chief Financial Officer, was assumed by Christoph Heins.

Detailed résumés of all members of mBank authorities are available on www.mBank.pl

1.3. Composition of mBank Group and key areas of activity

In May 2016 the integration of the brokerage operations of mBank S.A., Dom Maklerski mBanku S.A. (mDM) and mWealth Management S.A. (mWm) into an expanded brokerage bureau of mBank was completed. For the purpose of the integration process, the subsidiaries mDM and mWM were divided.

The division of mDM was effected under Article 529 para.1 item 1 of the Code of Commercial Partnerships and Companies and included a transfer of the organised part of mDM's enterprise connected with the provision of brokerage services to mBank and a transfer of the organised part of mDM's enterprise connected with servicing and rendering of human resources and payroll services to mCentrum Operacji Sp. z o.o. The division of mWM was effected under Article 529 para.1 item 1 of the Code of Commercial

Partnerships and Companies and included a transfer of the organised part of mWM's enterprise connected with the provision of brokerage services and the remaining operations not constituting the operations of the Real Estate Market and Alternative Investments Bureau to mBank and a transfer of the organised part of mWM's enterprise connected with advisory and agency services in the scope of purchasing and investing in real estate and other alternative investments for the benefit of natural persons and real estate market analyses to BRE Property Partner Sp. z o.o. (non-consolidated subsidiary). On May 20, 2016 mDM and mWM were struck off the National Court Register.

The aim of the integration of all brokerage entities of mBank Group is to optimise the portfolio of brokerage services offered to all client groups, both individuals and institutions. Moreover, the integration will allow the Bank to better use its resources and potential, thus giving the brokerage services of mBank Group a greater competitive advantage.

Consequently, mBank Group (consolidated subsidiaries) as at June 30, 2016 was composed as presented on the diagram below.

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	■ Retail clients, private banking clients, and micro-enterprises ■ Affluent clients (Private Banking and Wealth Management)	■ Service of corporations and non-banking financial institutions (K1) ■ Large companies (K2) ■ Small and medium-sized companies (K3)	■ Banks ■ Corporate clients in the scope of trading and sales ■ Risk and liquidity management
Consolidated subsidiaries	■ Retail part mLeasing Sp. z o.o. ■ Retail part of mBank Hipoteczny S.A. ■ Aspiro S.A.	■ 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.	■ 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	■ mLocum S.A. (real property developer) ■ mCentrum Operacji Sp. z o.o. (outsourcing services provider) ■ BDH Development Sp. z o.o. (real property manager)	

1.4. Subsidiaries of mBank Group

mBank Hipoteczny S.A.

mBank Hipoteczny (mBH) is the largest mortgage bank in Poland by both the scale of financing of the real property market and covered bond issuance.

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 the retail segment mBH, in cooperation with mBank, extends mortgage loans to individuals. 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.

Moreover, the subsidiary is the largest issuer of covered bonds, which are its core source of funding. The covered bonds issued by mBH rank among the safest investment instruments on the Polish capital market. The value of outstanding covered bonds issued by mBH reached nearly PLN 4.6 billion, representing a market share of ca. 66%.

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 chapter 1.8 Ratings of mBank and mBank Hipoteczny.

Aspiro S.A.

Aspiro 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 25 financial entities, in more than 100 outlets across Poland with the participation of 600 customer advisors.

mLeasing S.A.

mLeasing is one of the largest leasing companies in Poland and ranks second on the real property leasing market and second on the leasing market.

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.

According to the data of the Polish Leasing Association, as at June 30, 2016 the Group's share in the Polish market stood at 7.4%, making it the second largest market player in terms of sales of new lease contracts, with the total value of the lease portfolio approaching PLN 7,227 million.

mFaktoring S.A.

mFaktoring is the eight 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.

In H1 2016 the Group's share in the Polish market stood at 7.4%, with a total value of factoring contracts amounting to PLN 5,451 million.

mCentrum Operacji S.A.

mCentrum Operacji (mCO) provides back-office support to the members of mBank Group.

In particular, the subsidiary handles the instructions and applications of retail and corporate clients of mBank Group. In addition, mCO supports the Group in terms of professional data archiving solutions, both electronic and paper-based.

The company's services enable monitoring of data security and confidentiality, quick access to information, as well as support in planning, controlling and reducing costs.

mLocum S.A.

mLocum S.A. is an experienced and active real property developer that has been present on the real property market since 2000. It is one of the first real property developers in Poland having a presence on many local markets, including Kraków, Łódź, Wrocław, Warsaw, Poznań and Sopot.

The subsidiary organises and manages housing development projects. Other activities of the subsidiary include management of real properties, including condominiums.

So far, mLocum has built more than 4.1 thousand apartments in 33 projects. The subsidiary was a co-founder of the Polish Association of Developers (PZFD) gathering the largest real property developers supporting the development of the Polish housing market.

1.5. Values of mBank Group

mBank, the first fully Internet-based Bank in Poland, for years has been a synonym of innovative solutions in the banking sector. Today it sets standards in the development of mobile and online banking sector. mBank's mission focuses on clients, aspiring to be the Bank which accurately identifies and foresees the needs of its customers being able to meet them precisely.

As a result of unification of the brand policy, which started in 2013, currently all clients are serviced under one brand. At the same time, mBank's team internally developed the model of values and behaviour characterising employees of mBank and targeting the Group's actions at accomplishment of the mission to create a better Bank for its clients.

Specialised banking services dedicated to various groups of clients are constantly improved and adjusted to changing behavioural patterns of clients. Organising around common values shared by employees helps to effectively face market challenges and provide clients with satisfactory experience from cooperation with the Bank.

mBank are mainly people who cooperate with the aim to understand and precisely meet the needs of clients and share the responsibility for their satisfaction. Common values form the basis for the development of organisation and trust in customer relations. A clearly specified model of values (the chart below) is an expression of the internal consistency of the organisation, focused on offering the highest standards of service, as well as setting the direction for actions in increasingly challenging market environment.

1.6. H1 2016 in numbers

Solid profitability amid challenging market environment	■ PLN 907.8 million in profit before tax compared with PLN 857.2 million in H1 2015 (+5.9%) ■ PLN 696.3 million in net profit attributable to the owners of mBank, which represents a rise by 3.6% compared with H1 2015
Income supported by the gain on the takeover of Visa Europe Limited by Visa Inc.	■ PLN 2,211.9 million in total income, which represents an increase by 10.4% YoY ■ Settlement of the takeover of Visa Europe Limited by Visa Inc. generating additional income before tax in the amount of PLN 251.7 million
Strong cost efficiency maintained	■ Operating costs (including amortisation) at PLN 971.5 million (+3.8% YoY), driven by a rising scale of operations and higher amortisation ■ Cost to income ratio at 43.9% (compared with 46.7% a year before)
Risk cost reflecting high quality of assets	■ Loan loss provisions at PLN 186.3 million compared with PLN 207.6 million in H1 2015 ■ Risk cost at 0.47% compared with 0.54% a year before

Growth in client base	■ Number of individual clients: 5,146 thousand (+199 thousand clients year to date) ■ Corporate client base: 20,220 (+658 clients year to date)
Increase in the value of net loans and advances	■ Net loans and advances reached PLN 80,774.8 million, which represents an increase by 3.0% year to date
Dynamic development of deposit base	■ Amounts due to clients stood at PLN 85,302.3 million, up by 5.1% from the beginning of 2016
Solid return on equity	■ Gross ROE: 14.9% (15.7% at the end of H1 2015) ■ Net ROE: 11.5% (12.3% at the end of H1 2015) ■ ROE went down compared with H1 2015 as a result of an increase in average equity
Safe level of capital ratios and liquidity	■ Total Capital Ratio at 18.3% ■ Common Equity Tier 1 ratio at 15.6% ■ Loan to deposit ratio at 94.7%

1.7. Strategy of mBank Group for 2016-2020

2016-2020 strategy - „mobile Bank"

mBank Group's strategy until 2020, titled **mobile Bank**, was accepted by mBank's Supervisory Board on June 10, 2016. The strategy sets the framework for most important strategic activity directions of the Group. It rests on three pillars creating a canvas for implementing specific business actions to be undertaken by mBank over the next years. There are: client centricity, leveraging on mobility and continued improvement of efficiency. The „mobile Bank" strategy also defines the foundations for the strategy implementation, including engagement of mBank employees, principles of the organization development as well as a framework for the bank's technological agility.

Mission: *„To help. Not to annoy. To delight... Anywhere."*

mBank's mission reflects the emergence of the client and mobility eras, which are the two most critical factors about to shape the business models at financial institutions.

„To help. Not to annoy. To delight..."

The time of focusing solely on creating and improving products has come to an end. Clients are at the centre of attention and banking, following the steps of other sectors, has also entered the era of the customer. Agile market disruptors (today e.g. Uber, Airbnb) are obsessively focused on meeting the needs and solving of the most significant issues of the consumers, who increasingly expect to be treated in the same way by mBank.

„Anywhere"

The smartphone, currently perceived as a first truly personal computer, is gradually becoming the management centre of clients' lives. Lean market players are revolutionizing the status quo on different markets (e.g. transport, travel, entertainment) and offer the applications with providing truly mobile end-to-end customer experience and ultimate convenience (e.g. Uber, Airbnb, Spotify, Netflix). mBank aims to take a similar approach ensuring its core products and services can be seamlessly reached via all distribution channels at clients' convenience.

„mobile Bank" strategy pillars:

1. **Empathy for the client** – all mBank's actions will be driven by clients and their individual needs, preferences and behaviours. mBank's ultimate goal is to make sure that clients want to choose it permanently and are keen to recommend it, having been highly satisfied with its services. The goals of the Empathy pillar defined in the new mission are the following:
   - **To help.** To offer what clients really need and when they need it. To construct the offer in such way that it fulfils actual needs of the clients. To simplify so that understanding of the offer and making the right decisions takes minimal amount of time.
   - **Not to annoy** the clients, facilitating the cooperation with the bank and to minimize the hassle and effort for the customers. To deal efficiently with customers' difficulties during the first contact between a client and the bank, regardless of the contact channel.
   - **To delight** the clients by making them feel special and appreciated thus creating the most valuable brand ambassadors at mBank. Satisfied employees are also the natural ambassadors of mBank's services, therefore mBank will strongly promote among them the use of its offer, mobile solutions in particular.
2. **Mobility** – it is mBank's ambition to be the synonym of mobile banking, focusing on the following priorities: convenience, usability and simplicity from customer's point of view. Consequently the development of new application functionalities will be concentrated on three main areas:
   - *Mobile Hub*: gate in a multichannel strategy in contacting the client - Regardless of the starting of a transaction – each distribution channel will be a click away on the client's tablet or smartphone. At the same time mBank expects, that most contacts in the 2020 perspective will commence on a smartphone which will be a "gate" for the client to seamlessly switch between channels;
   - *Reinforcing the role of mobile banking as a contact channel:* minimizing the functionality gap between mobile and internet - mBank will ensure bigger independence of the mobile channel and will limit its functionality gap compared to other distribution channels;
   - *Customer engagement* through use of innovative, unique functionalities engaging the client - mBank will create and reinforce the habit of using its mobile application, which will consequently generate additional opportunities to approach customers with an adequate product offering.
3. **Efficiency** - focus on efficiency supports mBank's profitability in times when returns from core banking products in Poland are under significant pressure. Business development in terms of asset classes, maturities, sources of financing and concentration of the business activity (groups of products and client segments, presence on foreign markets) will be carried out in full compliance with the rules for optimal cost efficiency and process digitalization, efficient capital allocation and stable funding.

Strategy enablers

Implementation of specific, strategic initiatives will require strong engagement of employees of the entire Group, as well as targeted, agile IT strategy. As such, the foundations for the strategy implementation are:

- **Engaged people**: mBank will create conditions for full engagement of employees in building a friendly working environment allowing them to achieve their ambitions. The priority of HR strategy is attracting and retaining the best and motivated specialists and managers in the sector.
- **Technological advantage** - mBank will skilfully build world class IT organization and its agile, client-driven IT will become a source of the bank's competitive advantage.

mBank Group financial targets

In a rapidly evolving business, regulatory and technological environment, a reliable formulation of financial targets in a 5 year horizon becomes a significant challenge. mBank, leveraging on its key strengths has in the past been able to outperform most of its competitors in terms of financial results. It remains mBank's strategic goal to be positioned among the leading banks in Poland in terms of key financial measures.

Determining financial targets for the years 2016-2020 has been based on mBank's ambitious assumptions regarding mainly cost effectiveness as well as returns on equity and assets. Moreover, mBank's intention is to pay dividend of at least 50% of profits, subject to regulatory (Polish Financial Authority's) consent, as well as to further strengthen its funding base.

The table below presents mBank Group's financial aspirations:

No	Financial measure	Target point
1	Cost efficiency, **Cost-to-Income (C/I)**	**Top 3 in Poland**, **each year** i.e. to be one of three most effective listed banks in Poland
2	Return on capital, **RoE net**	**Top 3 in Poland**, **each year** i.e. to be among the three most profitable listed banks in Poland from the RoE standpoint adjusted for dividend distribution
3	Assets profitability, **RoA net**	**Top 3 in Poland**, **in 2020** i.e. to be one of three listed banks in Poland with highest return on assets
4	Capital position, capital adequacy in terms of core capital **CET1** *(Common Equity Tier1)*	Maintain the ability of dividend pay-out in terms of CET1 ratio, annually - maintain the ratio **min 1.5 pp. above capital requirement for mBank**
5	Financial stability, **Loans/Deposits ratio (L/D)**	Maintain the L/D ratio at most **not significantly higher than 100%, each year**

1.8. Rating of mBank and Group subsidiaries

Rating assigned by Fitch Ratings

On March 7, 2016 Fitch Ratings agency upgraded mBank's long-term foreign currency rating from "BBB-" to "BBB" and short-term foreign currency IDR from "F3" to "F2". The outlook for the long-term rating is stable. The improvement in mBank's rating was connected with upgrading of the long-term rating for Commerzbank from "BBB" to "BBB+". According to Fitch, Commerzbank is highly likely to support mBank if a need arises.

mBank's viability rating assessing mBank's financial credibility based on factors such as business profile, management and strategy, risk profile, financial results and external environment remained unchanged at "bbb-".

Fitch Ratings – ratings of mBank	
Long–term IDR	BBB (stable outlook)
Short-term IDR	F2
Viability rating	bbb-
Support rating	2
Rating of unsecured debt issued under the Euro Medium Term Note Programme (EMTN)	BBB

The rating action on May 7, 2016 covered also mBank Hipoteczny. mBank Hipoteczny's long-term rating was upgraded from "BBB-" to "BBB", while the short-term rating was changed from "F3" to "F2". The

ratings of public and mortgage bonds issued by mBank Hipoteczny were upgraded from "BBB" to "BBB+". On July 1, 2016 Fitch upgraded mortgage bonds issued by mBank Hipoteczny to "A" with a positive outlook.

The rating of mBank Hipoteczny corresponds to the rating of mBank, which proves the importance of this subsidiary to mBank.

Fitch Ratings – ratings of mBank Hipoteczny	
Long–term IDR	BBB (stable outlook)
Short-term IDR	F2
Support rating	2
Ratings of mortgage covered bonds issued by mBank Hipoteczny	A (starting from July 1, 2016)

Rating assigned by Standard & Poor's

On February 3, 2016 S&P Global Ratings (S&P) affirmed the Bank's long-term counterparty credit rating at "BBB" and short-term counterparty credit rating to "A2" and changed its rating outlook from stable to negative due to an analogous change in the outlook for the banking sector. In the opinion of S&P, the ability of the banking sector to absorb losses and to cope with shocks may decrease in the the following two years. According to S&P, the operating conditions for Polish banks remain difficult as the introduction of a new banking tax, increased regulatory costs and costs related to potential foreign-currency loan conversions will put further pressure on the sector's profitability in the low interest rates environment. The agency decided that under these circumstances mBank's ability to generate income may not compensate for the potential decrease in the assessment of Commerbank's support for mBank in case when Commerbank's rating is downgraded.

On March 11, 2016 S&P changed the rating outlook for mBank from negative to stable, following a similar change in Commerzbank AG's rating outlook.

Standard & Poor's – ratings of mBank	
Long-term deposits rating	BBB (stable 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

Rating assigned by the Moody's based on publicly available information

Moody's ratings for mBank are based solely on publicly available information, and mBank does not take part in the rating process, having the "non-participating issuer" status. In H1 2016, both the ratings and outlook remained unchanged.

Moody's – ratings of mBank based on publicly available information	
Long-term deposits rating	Baa2 (stable outlook)*
Short-term rating	Prime-2
Unsecured debt rating	Baa3
Counterparty risk assessment	Baa1 (cr)/ P-2 (cr)

** "Non-participating issuer", rating based solely on publicly available information.*

Ratings of Poland, mBank and Commerzbank – comparison

The table below compares the long-term ratings of Poland, mBank and Commerzbank as of June 30, 2016.

Rating agency	Poland	mBank S.A.	Commerzbank AG
Fitch Ratings	A- (stab.)	BBB (stab.)	BBB+ (stab.)
Standard & Poor's	BBB+ (neg.)	BBB (stab.)	BBB+ (stab.)
Moody's	A2 (neg.)	Baa2 (stab.)	A2 (stab.)

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

1.9. mBank shareholders and share price on the WSE

mBank shares as of June 30, 2016

Key characteristics of mBank shares as at June 30, 2016:

- Nominal value per share: PLN 4.00
- Registered share capital: PLN 168,956 thousand, paid up in full
- mBank shares have been listed on the Warsaw Stock Exchange (WSE) since 1992.
- mBank shares are part of the following WSE indices: WIG, WIG-Poland, WIG20, WIG30 and WIG-Banks; moreover, the shares are also included in derivative indices based on WIG20.

In H1 2016, the number of mBank shares remained unchanged.

Commerzbank AG is the majority shareholder of mBank, holding 69.49% of share capital and votes at the AGM. Moreover, at the end of June 2016, Nationale-Nederlanden Otwarty Fundusz Emerytalny exceeded the 5% threshold of shares and votes at the Annual General Meeting.

On March 24, 2016 the Annual General Meeting of mBank S.A. adopted a resolution under which PLN 30,000,000.00 out of the net profit posted by the Bank in 2015 in the amount of PLN 1,271,449,406.95 was allotted to general risk fund, while the remaining PLN 1,241,449,406.95 remained undistributed.

mBank share price performance

In H1 2016, the performance of mBank shares on the WSE was affected by international economic situation and investors' uncertainty about the effects of some of the economic policies pursued by the Polish government. On the one hand, investors' decisions were affected by global factors, among others, the increasing USD/PLN exchange rate, cheap raw materials, uncertainty as to the development of economic situation in emerging markets, in particular in China, as well as investors' fears about the EU referendum in the UK held in June and the consequences of the so called "Brexit". On the other hand, the share prices of listed companies were adversely affected by the banking tax introduced in February reducing banks' profits, the extraction tax not abolished, as well as the plans concerning providing support for highly indebted mines by the energy sector. Investor sentiment was also adversely affected by rating actions - downgrade of Poland's rating by S&P and change of the rating outlook by Moody's, as well as the paralysis of the Polish Constitutional Court. Political tensions and concerns about the long-term effects of economic policy caused a certain outflow of foreign capital from the WSE.

The performance of banks' shares was strongly impacted by the risk related to the potential conversion of the FX mortgage loans into the zloty. The proposed bill on restructuring of FX mortgage loans provided for imposing significant costs on banks. Since banks account for c. 25% of WIG-20 capitalization, a slide in their share prices had a major impact on the blue chip index.

The closing price of mBank share during the last session in H1 2016 (June 30) stood at PLN 308.95, which represents a drop by 1.6% compared with the price reported on the last business day of 2015 (December 30). During the same period, WIG-Banks index decreased by 6.6%. For comparison, EURO STOXX Banks

Index declined by 3.9%, largely as a result of an unexpected outcome of a referendum on Brexit on June 24, 2016.

WIG-20 dropped by 5.8% in H1 2016, while the broad market index WIG decreased by 3.7%.

The risk of introducing new solutions concerning FX mortgage loans unfavourable to the banking sector affects the share price (target price) and analysts' recommendations for mBank shares. At the end of June "sell" (53%) and "hold" (31%) recommendations were prevailing, while "buy" recommendations accounted for 16% of all recommendations.

The P/BV (price/book value) ratio for mBank Group stood at 1.0 at the end of June compared with 1.5 a year before. The P/E ratio (price/earnings per share) reached 9.4 after H1 2016, compared with 13.0 after H1 2015.

mBank's capitalisation amounted to PLN 13.0 billion (EUR 2.9 billion) as at June 30, 2016, compared to PLN 17.4 billion (EUR 4.2 billion) a year ago and PLN 13.3 billion (EUR 3.1 billion) at the end of 2015.

The current consensus of expected results of mBank Group is available on mBank's website: https://www.mbank.pl/en/investor-relations/shares/consensus.html

mBank's share performance vs. main WSE indices

2. Business activity and key achievements

2.1. Key projects of mBank Group in H1 2016

Strategic partnership with Orange

The joint-venture of mBank and Orange, Poland's leading telecommunications group, Orange Finanse was launched on October 2, 2014.

Thanks to its innovative offer, after only a year and a half following its launch, Orange Finanse became mBank's important client acquisition contributor. Consequently, by mid-2016 nearly 320 thousand accounts were opened with Orange Finanse, including over 60 thousand in H1 2016 alone.

A number of interesting changes were introduced in the mobile application and Internet banking in early 2016. A dedicated version of Orange Finanse for Windows Phone was released. iOS users can now log into the application with a fingerprint. By clicking a dedicated button in the mobile application, the users of all platforms can now quickly get in touch with the Bank's contact centre, a one-of-a-kind solution on the market. A new, more comprehensive credit offer was introduced in June 2016.

Changes in the Group's funding structure

Issue of covered bonds

mBank in cooperation with mBank Hipoteczny pursues a strategy designed to issue covered bonds secured with liabilities backed by mortgage loans, allowing for the narrowing of the maturity gap between assets and liabilities and cutting the cost of new funding.

In H1 2016 mBank Hipoteczny issued covered bonds worth in total PLN 450 million and EUR 50 million, with maturities ranging from 4 to 5.2 years. The issues in PLN placed in April and May 2016 were the first issues of covered bonds bearing interest at a fixed rate in Poland.

The following table presents the issues in H1 2016:

Currency	Amount	Date of issue	Maturity date	Tenor (years)	Margin
PLN	300,000,000	March 9, 2016	March 5, 2021	5.0	WIBOR 3m+120 bps
EUR	50,000,000	March 23, 2016	June 21, 2021	5.2	EURIBOR 3m+87 bps
PLN	50,000,000	April 28, 2016	April 28, 2020	4.0	Fixed (2.91%)
PLN	100,000,000	May 11, 2016	April 28, 2020	4.0	Fixed (2.91%)

EMTN Programme

In Q1 2016 mBank updated the Prospectus for EUR 3 billion Euro Medium Term Notes Programme (EMTN). On March 23, 2016 the updated Prospectus was approved by Commission de Surveillance du Secteur Financier (CSSF) in Luxembourg. The programme aims at issuing debt securities by mFinance France, a subsidiary of mBank Group, in many tranches and currencies, with a diversified interest structure. The potential issues in H2 2016 will depend on market conditions.

The following table presents a summary of outstanding tranches:

Currency	Amount	Date of issue	Maturity date	Tenor (years)	Coupon
CHF	200,000,000	October 8, 2013	October 8, 2018	5.0	2.500%
CZK	500,000,000 [1)]	December 6, 2013	December 6, 2018	5.0	2.320%
EUR	500,000,000	April 1, 2014	April 1, 2019	5.0	2.375%
EUR	500,000,000	November 26,2014	November 26, 2021	7.0	2.000%

[1)] *private placement*

Funding from European Investment Bank (EIB)

In June 2016, mBank obtained additional funding from the European Investment Bank - a loan of EUR 100 million with a maturity of 8 years. The total debt of mBank towards EIB in euros on June 30 2016 stood at EUR 946 million. Credit lines from EIB are intended to finance projects implemented by micro, small and medium-sized enterprises with less than 250 employees and to finance projects implemented by companies employing at least 250 FTE, but not exceeding 3 000 employees (i.e. mid-caps).

Bilateral agreement with Industrial and Commercial Bank of China

On May 20, 2016 mBank signed an agreement with Industrial and Commercial Bank of China (Europe) under which ICBC granted mBank a 3-year loan in the amount of EUR 130 million. It is the first loan that has been granted by ICBC to a Polish bank.

2.2. Awards and distinctions

Since the beginning of 2016, mBank Group received a number of awards and distinctions, in particular:

EUROMONEY PRIVATE BANKING SURVEY 2016	For the eight time Private Banking of mBank has been ranked the best in Poland by Euromoney, a British financial magazine. mBank was also appreciated in six competition sub-categories, among others, for the best specialist services for the most affluent clients, asset management or intergenerational wealth transfer.
★★★★★ w ratingu Forbes Private Banking 2016	For the fifth time in a row Private Banking of mBank has received the highest, Five-Star distinction awarded every year by Forbes magazine. The authors of the ranking appreciated the bank for setting the standards of private banking in Poland, a broad and customized offer and development of mobile banking.
Mobile Trends Awards	The mobile application of mBank won two statuettes in the Mobile Trends Awards competition: First place in Mobile Banking category (jury's verdict) and first place in the Mobile Trends Awards special prize category (votes cast by Internet users). Mobile mTransfer won two awards and was ranked: first in supporting popularization of mobile techniques and technologies category (jury's verdict) and second in the Mobile Trends Awards special prize category (votes cast by Internet users).
BEST TRADE FINANCE BANK AWARD • 2016 GLOBAL FINANCE	mBank was named the Best Trade Finance Bank in Poland by Global Finance. The award is granted in the following categories: Country Winners, Regional Winners and Global Winners. The following areas were assessed: trade finance volumes, comprehensiveness and innovativeness of the product offer, transaction competence and experience, as well as the scale of pursued business activity.
	In the Golden Banker ranking, mBank ranked second in the "Golden Bank" main category for the highest quality of service and won in the "Advertising Spot" and "Socially Responsible Bank" categories. Moreover, mBank received the "Best Practices in System Security" special prize.

	mBank won Service Quality Star in 2016 in the "Banks" category for the most recommended personal account in 2016. The awards for the quality of service are granted based on the assessments and opinions of consumers published on www.jakoscobslugi.pl and via the smartphone Premia360 application. Brands with the highest Customer Satisfaction Index (CSI) that stand out against their competitors and when compared with the Polish Customer Satisfaction Index (PCSI) were awarded.
	mBank in the Czech Republic received three awards, one golden and two silver, in the "Zlatá koruna" competition and voting. mKonto Business won in the entrepreneurs category (first prize), mKonto in the audience category (second prize) and transaction service in the online application category (second prize). The Zlatá koruna competition is held under the patronage of the Minister of Finance of the Czech Republic and every year awards the best financial products on the Czech market.
	In May 2016, the active participants of the capital market were granted the awards of the WSE, BondSpot and KDPW for 2015. Dom Maklerski mBanku won awards for the highest total value of IPOs on the WSE organised in 2015, the highest value of trading in non-treasury bonds on all markets listed on Catalyst and the highest share of the market maker in trading in shares on the main floor. Furthermore, mBank was awarded by the WSE Catalyst in the "highest value of non-treasury debt instruments listed on Catalyst in 2015" category and received KDPW's award for the largest volume and highest value of OTC transactions cleared at KDPW in 2015 and the highest share of the market maker in trading in shares on the main floor.
	mBank was the winner of the award "Private Equity Diamonds" in the category "Bank of the Year." Diamonds have been granted by the Executive Club, comprising representatives of top management, representing the most important Polish and international companies and by the Polish Private Equity Association comprising private equity /venture capital investors.
	mBank triumphed in the innovation category in the Banking Stars competition organised by Dziennik Gazeta Prawna daily and PwC as an independent expert. In addition, mBank ranked second in this contest for the overall operation.

2.3. Retail Banking

Retail Banking in Poland

Retail Banking segment financial results

The Retail Banking segment generated a profit before tax of PLN 592.7 million , which represents a decrease of 28.8 million, i.e. 4.6% year on year.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Net interest income	765.2	838.5	73.3	9.6%
Net fee and commission income	232.9	238.8	5.9	2.5%
Dividend income	0.0	0.0	-	-
Net trading income	47.7	50.5	2.8	5.9%
Gains less losses from investment securities, investments in subsidiaries and associates	194.3	230.5	36.2	18.6%
Net other operating income	15.4	2.9	-12.5	-81.2%
Total income	**1,255.5**	**1,361.2**	**105.7**	**8.4%**
Net impairment losses on loans and advances	-116.4	-140.3	-23.9	20.5%
Overhead costs and amortization	-515.9	-548.8	-32.9	6.4%
Taxes on Group balance sheet items	-1.8	-79.4	-77.6	4311.1%
Profit before tax of Retail Banking	**621.5**	**592.7**	**-28.8**	**-4.6%**

The profit before tax of the Retail Banking segment in H1 2016 was driven by the following factors:

- **Increase of total income** by PLN 105.7 million, i.e. 8.4% year on year to PLN 1,361.2 million. Core income increased: net interest income was higher by PLN 73.3 million (as an effect of growing volumes and repricing of loans and deposits) while net fee and commission income went up by PLN 5.9 million (mainly due to higher credit-related fees and commissions from insurance activity). Moreover, total income was supported by higher gains less losses from investment securities, investments in subsidiaries and associates by PLN 36.2 million due to the booking of the gains on the takeover of Visa Europe Limited by Visa Inc. (in H1 2015 the gains on the sale of the company BRE Ubezpieczenia TUiR and the execution of sales-related agreements with AXA Group companies were booked).
- **Increase of operating expenses (including amortisation)** by PLN 32.9 million, i.e. 6.4% year on year, mainly due to higher amortization, i.e. due to an earlier write-off of unused IT system functionalities.
- **Increase of net impairment losses on loans and advances** by PLN 23.9 million, i.e. 20.5% compared to H1 2015 following the growth of the loan volume, higher FX rates as well as growing share of of unsecured loans in the retail loans portfolio.
- **Taxes on Group balance sheet items** in the amount of PLN 79.4 million.

Activity of Retail Banking (mBank only) segment

thou.	30.06.2015	31.12.2015	30.06.2016	YtD change	YoY change
Number of retail clients, including:	**4,742.9**	**4,947.3**	**5,146.3**	**4.0%**	**8.5%**
Poland	3,968.1	4,127.7	4,280.4	3.7%	7.9%
Foreign branches	774.8	819.7	865.9	5.6%	11.8%
The Czech Republic	541.9	573.1	607.4	6.0%	12.1%
Slovakia	232.9	246.5	258.4	4.8%	10.9%
PLN M					
Loans to retail clients, including:	**45,187.2**	**46,168.7**	**48,220.8**	**4.4%**	**6.7%**
Poland	**41,890.6**	**42,344.7**	**43,962.3**	**3.8%**	**4.9%**
mortgage loans	33,328.0	33,473.4	34,156.7	2.0%	2.5%
non-mortgage loans	8,562.6	8,871.3	9,805.6	10.5%	14.5%
Foreign branches	**3,296.6**	**3,824.0**	**4,258.5**	**11.4%**	**29.2%**
The Czech Republic	2,549.9	2,899.6	3,261.5	12.5%	27.9%
Slovakia	746.8	924.4	997.0	7.8%	33.5%
Deposits of retail clients, including:	**40,901.6**	**45,645.4**	**49,546.0**	**8.5%**	**21.1%**
Poland	**34,933.7**	**39,273.6**	**42,222.1**	**7.5%**	**20.9%**
Foreign branches	**5,967.9**	**6,371.8**	**7,323.9**	**14.9%**	**22.7%**
The Czech Republic	4,140.8	4,488.0	5,246.0	16.9%	26.7%
Slovakia	1,827.1	1,883.7	2,077.9	10.3%	13.7%
Investment funds (Poland)	**6,098.1**	**5,736.2**	**5,510.1**	**-3.9%**	**-9.6%**
thou.					
Credit cards, including	**331.7**	**332.4**	**335.7**	**1.0%**	**1.2%**
Poland	303.1	303.6	304.4	0.3%	0.4%
Foreign branches	28.6	28.8	31.3	8.5%	9.4%
Debit cards, including:	**3,166.6**	**3,242.7**	**3,283.9**	**1.3%**	**3.7%**
Poland	2,617.0	2,701.0	2,739.5	1.4%	4.7%
Foreign branches	549.6	541.8	544.4	0.5%	-1.0%

	30.06.2015	31.12.2015	30.06.2016
Distribution network			
Light branches within "One Network" Project	4	9	12
Advisory Centres	2	4	4
mBank (former Multibank)	128	123	121
mKiosks (incl. Partner Kiosks)	76	83	84
Aspiro Financial Centres	23	23	22
Czech Republic & Slovakia	35	36	36

In H1 2016 the number of mBank retail banking clients in Poland rose by 152.8 thousand, mainly thanks to active acquisition, focused marketing efforts, product mix development and effective cross-selling.

Product mix, acquisition and marketing

At the beginning of 2016 the offer of individual accounts was significantly simplified. Changes consisted of the withdrawal of the following products from mBank's offer: eKonto, eKonto mobilne, eKonto mobilne plus and mKonto Multi. Instead of the aforementioned accounts an eKonto account was introduced in two versions: eKonto with a standard tariff and eKonto with a plus tariff. Both accounts include a mechanism releasing the client from a debit card fee, in a situation when the client makes at least five cash-less transactions a month using the card.

In addition, mBank was the first bank on the market to develop a comprehensive credit guide "Credit ABC", covering all aspects of incurring a loan, from the first formalities to loan repayment. Moreover, it focused on providing expert support in the case when a credit application is rejected. All these changes make the entire borrowing process simpler for mBank clients, which was emphasized in the marketing campaign launched in May.

Moreover, in June 2016 mBank launched the third edition of the promotion encouraging clients to actively use mBank's mobile application (Mobile Clients Have It Better - 3rd edition).

Finally, the Bank made it possible for its retail clients to apply for child benefits under the Family 500+ Programme via mBank's online banking system. So far, 96 thousand applications have been filed and PLN 186 million in child benefits have been paid, which ranks mBank second on the market.

Offer for small and medium-sized enterprises

In the area of small and medium-sized enterprises (SME), one of the main achievements in H1 2016 was the launch of mAccounting service. Thanks to the exchange of basic data between banking and accounting systems, SMEs receive benefits which so far have only been available to corporate clients, including automatic monitoring of payments, quick invoicing, simplified invoice payment, analysis of business partners, electronic settlement of tax returns and up-to-date tax data.

With the aim to acquire new clients, mBank incorporated a new promotion "Good start with mBank" into the offer of company accounts. When opening a company account, the client may also order a stamp, a card holder and business cards for his/her new business. This offer has so far been available in mBank's outlets only, but starting from August 2016 it will also be available in direct channels - on the online platform and in the call centre.

Moreover, in an attempt to broaden its offer for small and medium-sized enterprises, the Bank and Akademickie Inkubatory Przedsiębiorczości (Academic Business Incubators, owner of Business Link, an office network) launched a new promotion "mBusiness account plus office". All clients who decide to open company accounts will be offered a free access to Business Link infrastructure for a period of 6 months. Business Link operates 11 business development hubs available round the clock, which makes it the largest

network of this type in Poland. The offices are located in 10 largest Polish cities. As part of the Partner's ecosystem, the clients will have an unlimited access to the office space in the largest Polish cities and will have the chance to meet with mentors/experienced entrepreneurs who can show them possible development opportunities and help them establish valuable business relations with other businessmen, while innovative companies may seek help in finding investors.

H1 2016 was yet another period in which mBank confirmed its leading role in the e-Commerce and m-Commerce transaction area. The Mobile mTransfer solution, making the mTransfer service available in the mobile channel, was once again appreciated by the market in the "Debut of the Year" category at Ekomersy 2015 gala. In addition, Mobile mTransfer was recognised in the Mobile Trend Awards 2016 competition and won 1st award for "Company supporting the popularisation of mobile techniques and technologies" and a Special Award - 2nd place in a vote by Internet users. For more information about awards for mBank Group in H1 2016, see section "Awards and distinctions".

At the beginning of 2016 mBank also expanded the mPlatforma Walutowa service, an FX platform (dedicated to small and medium-sized enterprises) with individual clients segment, offering them mKantor. mKantor offers all the benefits of mPlatforma Walutowa: making transactions in two clicks, very attractive FX rates, possibility to make transactions via a mobile application.

In the area of financing of companies a new product was added to the product offer: an overdraft facility guaranteed by COSME (an EU programme aimed at the strengthening of competitiveness of companies), which combines higher credit amounts with attractive terms of financing. In the case of investment loans with de minimis guarantee and registered pledge, the collateral catalogue was expanded so that mortgage is no longer the main security for the loan.

In March 2016 mBank also obtained the consent of the Minister of Digital Affairs to establishing a centre of confirmation of ePUAP (electronic public administration services platform) trusted profiles, starting the process of integration of the Bank with electronic public administration services. At the same time, the Bank offered account maintenance services to limited partnerships, associations, schools and educational institutions.

Cooperation with AXA Group

In H1 2016 the cooperation with mBank's strategic partner in the insurance sector, AXA Group, was continued. Works are focused on intensifying cross-selling and stand-alone sales among the Bank's clients.

In the insurance area, in H1 2016 the Bank made travel insurance available in the mobile channel and launched civil liability insurance (OC) and comprehensive motor insurance (AC) insurance for small and medium-sized enterprises.

Cooperation with Orange

In H1 2016 mBank continued its cooperation with Orange and worked on developing the product offer as part of the Orange Finanse project. Since the project's launch in October 2014, Orange Finanse has opened more than 320 thousand accounts, including over 60 thousand in H1 2016 alone.

H1 2016 was also a period of changes in the product offer supported by marketing campaigns promoting the Orange Finanse brand among the existing and prospective clients of Orange. The key component of the new offer is the option for active users of the Bank's services to lower their monthly phone bills in a period of up to 24 months. A new, more comprehensive credit offer was introduced in June 2016. The existing clients of Orange Finanse can take out cash loans of up to PLN 150 thousand in all Orange stores.

For more information about the strategic cooperation with Orange, see chapter 2.1. Key projects of mBank Group in H1 2016.

Development of the retail banking offer in Poland

Loans

The graph below presents the structure of the retail banking loan portfolio in Poland (for households) at the end of June 2016:

New sales of non-mortgage loans amounted to PLN 2,799.1 million, up by 22.2% year on year. Sales of mortgage loans in H1 2016 stood PLN 1,019.8 million (including sales of mBank Hipoteczny), which represents a decrease of 26.5% compared to H1 2015. The decrease was driven by the changes in pricing policy of the Group.

H1 2016 was another period when the portfolio of non-mortgage loans granted to households increased dynamically, by PLN 1,243.0 million, i.e., 14.5% compared to the end of June 2015. The portfolio of mortgage loans stood at PLN 34,156.7 million, with an increase by PLN 828.7 year on year.

The NPL ratio of the mortgage loan portfolio remained stable year on year, and stood at 3.8% at the end of June 2016.

Deposits and investment funds

Due to the continuing volatility on the capital markets observed in H1 2016, the tendency among retail clients to replace investment assets with deposit products, such as savings accounts and term deposits, persisted.

In the discussed period clients were particularly interested in safe products with a predetermined and guaranteed rate of return (term deposits with fixed interest rate) and products combining security with high liquidity (savings accounts). In the area of investment products clients were especially interested in solutions offering capital protection (e.g. structured products) or investment funds posing low investment risk (e.g. money market funds or bond funds).

In H1 2016 the Bank's activities in the savings area focused mainly on strengthening of the long-term relations with clients through encouraging them to prolong their maturing term deposits and not to withdraw the funds converted from investment assets. In the area of investment products, in turn, the Bank concentrated primarily on safe solutions (e.g. subscriptions of structured products).

At the end of June 2016, retail deposits amounted to PLN 42,222.1 million compared with PLN 34,933.7 million at the end of June 2015, which represents an increase by PLN 7,288.4 million or 20.9%.

Cards

In H1 2016 the value of payment card transactions made by mBank's retail clients exceeded PLN 12 billion, which represents an increase by 21.5% year on year. The number of transactions made by mBank clients grew by approximately 28.8% compared to the same period a year before. mBank's credit cards are also characterised by a very high average number of transactions per client, which is more than two times higher compared to the market average.

Retail Banking in the Czech Republic and Slovakia

In H1 2016 in the Czech Republic and Slovakia mBank acquired 46.2 thousand clients (out of which 11.9 thousand clients in Slovakia, and 34.3 thousand clients on the Czech market).

The activity of mBank in the Czech Republic and Slovakia in H1 2016 was focused on intensifying its acquisition efforts, as well as continued building the position of a mobile bank of reference.

The branch network modernisation is on track: second "Light branch" financial center in Slovakia, in Żilin, opened in May 2016.

Additionally, the mobile application was upgraded with Click to Call functionality and with a possibility to change limits on credit and debit cards. The application was distinguished in Slovakia by the PC Review with an award for the most client-friendly application.

In H1 2016 mBank in the Czech Republic and Slovakia also extended their offer by adding three new debit cards to the offer: gold debit card, debit phone sticker, and debit card for entrepreneurs.

The activity of mBank in the Czech Republic and Slovakia in H1 2016 was awarded in the Zlata Koruna contest: mBank's account for enterpreneurs was ranked first on the market, while mKonto account and internet banking were ranked second. Additionally, mBank's mortgage loan on refinancing real estate was ranked third in the weekly newspaper Trend.

Loans and deposits

As of June 30, 2016, the loan portfolio of mBank clients in the Czech Republic and Slovakia amounted to PLN 4,258.5 million, with an increase by PLN 961.9 million, i.e. 29.2% compared to the end of June 2015.

The Bank intensified its efforts aimed at increasing the sales of non-mortgage loans. Sales of non-mortgage loans in H1 2016 amounted to PLN 253.8 million, which represents an increase of 50.1% compared to H1 2015. Sales of non-mortgage loans amounted to PLN 188.6 million in the Czech Republic, which represents an increase by 40.0% year on year. At the same time sales of non-mortgage loans in Slovakia totaled PLN 65.3 million, increasing by 89.8% year on year.

Sales of mortgage loans in H1 2016 decreased slightly year on year i.e. by 3.1% compared to H1 2015, and amounted to PLN 462.7 million. Sales of mortgage loans in Czech Republic amounted to PLN 365.9 million, compared to PLN 361.2 million in H1 2015 (up by 1.3%), while in Slovakia stood at PLN 96.7 million (down by 16.8% year on year).

Finally, the Bank's deposit base in the Czech Republic and Slovakia increased by PLN 1,356.0 million or 22.7%. compared to the end of June 2015.

2.4. Corporates and Financial Markets

Corporate and Investment Banking

Corporate and Investment Banking segment financial results

The Corporate and Investment Banking segment generated a profit before tax of PLN 242.5 million, which represents an increase of PLN 5.3 million, i.e. 2.2% year on year.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Net interest income	362.5	363.2	0.7	0.2%
Net fee and commission income	183.9	177.9	-6.0	-3.3%
Dividend income	0.0	0.0	0.0	0.0%
Net trading income	107.7	125.9	18.2	16.9%
Gains less losses from investment securities, investments in subsidiaries and associates	2.1	21.0	18.9	900.0%
Net other operating income	15.3	8.6	-6.7	-43.8%
Total income	**671.5**	**696.6**	**25.1**	**3.7%**
Net impairment losses on loans and advances	-84.8	-47.3	37.5	-44.2%
Overhead costs and amortization	-349.5	-352.8	-3.3	0.9%
Taxes on bank balance sheet items	0.0	-54.0	-54.0	-
Profit before tax of Corporate and Investment Banking	**237.2**	**242.5**	**5.3**	**2.2%**

Profit before tax of the Corporate and Investment Banking segment in H1 2016 was driven by the following factors:

- **Increase of total income** year on year by PLN 25.1 million. The increase was recorded mainly in net trading income (+PLN 18.2 million or +16.9%) due to higher volatility on the financial markets, as well as in gains less losses from investment securities, investments in subsidiaries and associates (+PLN 18.9 million, 900.0%) due to the booking of the gains on the takeover of Visa Europe Limited by Visa Inc.
- **Increase of operating costs (including amortisation)** by PLN 3.3 million, i.e. 0.9% in the period under review.
- **Decrease of net impairment losses on loans and advances** by PLN 37.5 million, i.e. 44.2% year on year, due to lower provisions in K3 client segment as well as in the subsidiaries: mLeasing, mBank Hipoteczny and mFaktoring.
- **Taxes on Group balance sheet items** in the amount of PLN 54.0 million.

Activity of Corporate and Investment Banking (mBank only) segment

	30.06.2015	31.12.2015	30.06.2016	YtD change	YoY change
Number of corporate clients	**18,654**	**19,562**	**20,220**	**3.4%**	**8.4%**
K1	1,867	1,983	2,138	**7.8%**	**14.5%**
K2	5,485	5,748	5,883	**2.3%**	**7.3%**
K3	11,302	11,831	12,199	**3.1%**	**7.9%**
PLN M					
Loans to corporate clients, including	**21,075.6**	**21,071.8**	**21,460.8**	**1.8%**	**1.8%**
K1*	6,329.4	6,162.6	5,603.7	**-9.1%**	**-11.5%**
K2	11,899.7	11,837.6	12,650.5	**6.9%**	**6.3%**
K3	2,823.8	3,049.6	2,946.3	**-3.4%**	**4.3%**
Reverse repo/buy sell back transactions	0.0	0.0	131.6	**-**	**-**
Other	22.6	22.0	128.8	**486.7%**	**468.8%**
Deposits of corporate clients, including	**27,098.0**	**30,202.7**	**29,892.6**	**-1.0%**	**10.3%**
K1	13,488.1	14,019.2	13,328.8	**-4.9%**	**-1.2%**
K2	9,214.6	11,259.6	10,769.0	**-4.4%**	**16.9%**
K3	4,343.1	4,855.9	5,219.3	**7.5%**	**20.2%**
Repo transactions	0.0	0.0	111.4	**-**	**-**
Other	52.2	67.9	464.1	**583.1%**	**788.8%**
Distribution network	**47**	**47**	**45**		
Corporate branches	29	29	29		
Corporate offices	18	18	16		

K1 is the segment of the largest corporations with annual sales over PLN 500 million, the largest public sector entities and non-bank financial institutions (including pension and investment funds and insurance companies); K2 is the segment of corporations with annual sales between PLN 30 and 500 million and medium-sized public sector enterprises; K3 is the segment of SMEs with annual sales of up to PLN 30 million.

H1 2016 was marked by lower economic growth. A main reason of a slowdown were lower investments, resulting mainly from slower implementation of projects from new EU funds for the years 2014-2015.

Banks operated in the environment of record low interest rates, lower interchange fees and higher charges resulting from the new bank tax and contributions to the Bank Guarantee Fund. Among other challenges faced by the banking industry there are the unsolved issue of CHF mortgage loans, more stiff regulatory requirements and capital base optimisation.

In H1 2016 the corporate loans market grew by 3.6% against the end of December 2015 and by 6.7% year on year, whereas the market of corporate deposits shrank by 1.9% against the end of 2015 and rose by 9.3% year on year. mBank reported a similar change in the credit volume, while the year on year increase in deposits was much higher. Corporate loans grew by 3.2% year to date and 5.5% year on year.

Corporate deposits were stable year to date and rose by 12.7% year on year. At the end of H1 2016 mBank shares in the markets of corporate deposits and loans reached 10.0% and 6.3% respectively.

In H1 2016 the Bank intensified its sales efforts, which resulted in record-high acquisition of corporate clients - the corporate client base increased by 658 companies in comparison with the end of 2015.

The acquisition of new clients had a positive impact on the value of funds deposited on the Bank's current accounts, which at the end of June 2016 reached PLN 9,065.0 million, up by 7.1% year to date and by 14.5% year on year. The high volume of current deposits highlights development of transactional banking, which is of vital importance to the Bank due to its revenue potential, low capital requirements, and closer cooperation with clients.

In H1 2016 the Bank continued to pursue the strategy of increasing its share in the sector of small and medium-sized enterprises (SME). The undertaken initiatives aimed at strengthening of the Bank's progress in the position on the SME market, translated into high acquisition of clients in this sector (client base in the K3 segment grew by 368 companies compared with the end of 2015). The implemented solutions designed to facilitate account opening and making financing more accessible and flexible are becoming increasingly popular among clients. The number of clients using the all-in-one offer increased to 2,964 at the end of June 2016 from 1,497 a year before. The Flexible Package includes four modules: the transactional, financial, fx, and group modules. Flexibility of the package implies not only that clients can use modules in order to create diverse variants of the offer; it also embraces price flexibility: preferential terms of money transfers for more active transactional clients, as well as preferential terms for bank accounts based on contracted volumes of activity.

At the end of June 2016, the Bank held an 10.9% share in the corporate bond market, with 5th position on the market.

Products and services

Corporate loans

The value of loans to corporate clients (excluding reverse repo transactions) amounted to PLN 21,329.3 million at the end of H1 2016, which represents an increase by 1.2% compared with the end of December 2015 (PLN 21,071.8 million) and by 1.2% compared with the end of H1 2015 (PLN 19,027.8 million).

Loans to enterprises (NBP category which ensures comparability of results of the banking sector) amounted to PLN 20,069.5 million at the end of H1 2016, up by 3.2% vs. the end of December 2015 (PLN 19,442.2 million) and by 5.5% vs. the end of H1 2015 (PLN 17,235.6 million).

At the same time, the market of loans to enterprises grew by 3.6% and 6.7% respectively. mBank's share in the market of lending to enterprises stood at 6.3% at the end of June 2016, compared with the same value at the end of 2015 and 6.4% at the end of June 2015. The loan-to-deposit ratio for enterprises in the Bank reached 78.3% at the end of H1 2016 and was significantly lower than the market ratio of 124.8%.

The value of loans granted to local governments amounted to PLN 810.6 million at the end of June 2016 compared with PLN 913.6 million at the end of 2015 and PLN 1,092.58 million in H1 2015.

Corporate deposits

Corporate deposits gathered by the Bank (excluding repo transactions) amounted to PLN 29,781.2 million at the end of June 2016, which represents a decrease by 1.4% compared with the end of December 2015 (PLN 30,202.7 million) and an increase by 9.9% compared with the end of H1 2015 (PLN 27,098.0 million).

Current corporate deposits amounted to PLN 9,065.0 million at the end of H1 2016, which represents an increase by 7.1% compared with the end of December 2015 (PLN 8,467.1 million) and by 14.5% compared with the end of H1 2015 (PLN 7,917.1 million).

Deposits of enterprises amounted to PLN 25,638.7 million at the end of H1 2016, stable vs. December 2015 (PLN 25,629.2 million) and up by 12.7% vs. H1 2015 (PLN 22,743.8 million).

The market of deposits of enterprises shrank by 1.9% compared with the end of 2015 and rose by 9.3% against the same period last year. mBank's share in the total deposits of enterprises stood at 10.0% at the end of June 2016, up from 9.8% at the end of December 2015 and 9.7% against June 2015.

Deposits of local governments amounted to PLN 193.2 million as at the end of June 2016 compared with PLN 212.2 million at the end of 2015 and PLN 1,309.3 million at the end of June 2015.

European Union financing

On March 16, 2016 the Bank signed a new agreement with the European Investment Bank (EIB) to open a EUR 100 million credit line dedicated to financing projects and obligations related to the production cycle of mid-caps (entities with a headcount ranging from over 250 to less than 3 thousand employees).

De minimis guarantees

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 with an allocated limit for guarantees at PLN 1,630 million (an amending annex increasing the limit by PLN 330 million was signed on February 16, 2016).

Moreover, on February 22, 2016 mBank signed an agreement with Bank Gospodarstwa Krajowego under which it may offer loans backed by BGK guarantees to innovative clients from the SME sector. The guarantees will be financed from the PLN 250 million pool allocated as part of the Innovative Economy Operational Programme. The BGK guarantee limit for mBank stands at PLN 15 million. The guarantees will enable micro-firms and small and medium-sized enterprises to finance their innovative projects.

At the same time, mBank continued to offer the portfolio guarantee line with a counter-guarantee provided by the European Investment Bank under the COSME programme. The BGK guarantee limit for mBank stands at PLN 120 million. COSME is a European Union programme supporting the competitiveness of enterprises in 2014-2020. The main purpose of the programme with a budget of EUR 2.3 billion is to stimulate lending and capital investments among SMEs.

Corporate debt origination

In H1 2016, mBank organised or co-organised a number of bond issue programs on the domestic market, both for corporate issuers and banks.

The share of mBank in the non-treasury debt market at the end of June 2016 is presented on the chart below.

For years mBank has been the leader of the bank securities market. The largest issues arranged by mBank in H1 2016 included the issue of bonds worth PLN 437 million for the European Investment Bank and PLN 125 million for Eurobank. Other large transactions in which the Bank participated included the issue of covered bonds of mBank Hipoteczny worth EUR 50 million and PLN 450 million.

The Bank ranked fifth on the growing market of corporate bonds, with a market share of 10.9%. A number of new large issues were arranged, including: Kruk S.A. (PLN 150 million), Best S.A. (PLN 90 million), Griffin Real Estate Invest (PLN 53 million), LC Corp SA (PLN 50 million), Magellan SA (PLN 44 million and EUR 7.6 million), EGB Investment (PLN 18 million).

Development of transactional banking

Cash management is an area of Corporate Banking offering state-of-the-art solutions to facilitate planning, monitoring and management of the most 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:

- the number of domestic transfers made by corporate clients in H1 2016 increased by 13.8% year on year;

- the number of outgoing foreign transfers increased by 12.7% in H1 2016 year on year; the number of incoming transfers rose by 20.2%; the number of SEPA transfers (Single Euro Payments Area) grew by 22.4% in the reporting period;
- the number of direct debits rose by 17% in H1 2016 year on year;
- the number of corporate cards issued as at the end of June 2016 increased by 13.1% compared with June 2015;
- as at the end of June 2016 mBank issued a total of 306.7 thousand corporate pre-paid cards, which represents an 80% increase YoY;
- the number of mBank CompanyNet system users rose by 11.1% compared with H1 2015. Currently, there are 91.1 thousand active authorizations allowing the entitled employees of clients to cooperate with mBank.

Development of the Corporate Banking offer

Service of POS terminals

In H1 2016 mBank entered into cooperation with IT Card and Planet Pay in the area of servicing payment cards in terminals. Introduction of the service and the signing of an outsourcing agreement with IT Card, has enriched mBank's transactional banking offer.

In June 2016 mBank together with IT Card and Planet Pay signed an agreement on the provision and service of payment terminals for couriers of DPD Polska Sp. z o.o. It was the first such agreement on the Polish market under which 4.5 thousand terminals will be delivered. This transaction sets a new standard of quality and a new direction of settlements on the e-commerce market in the area of 'cash on delivery' mail.

Silesian City Card (ŚKUP)

The Silesian City Card (ŚKUP) is one of the largest city card projects in Poland. It was implemented by way of a public tender for the provision of a comprehensive system of city cards with payment functionality. The system was ordered by the Communication Municipal Association of the Upper Silesian Industrial District (KZK GOP), while the project is implemented by a consortium of Asseco Poland S.A. (Leader) and mBank S.A. The project is co-financed by the European Regional Development Fund.

Since the launch of the ŚKUP system in October 2016:

- nearly 125 thousand personalised ŚKUP cards and almost 5 thousand bearer ŚKUP cards were issued to the inhabitants of the Silesian agglomeration,
- 105 thousand bearer ŚKUP cards were delivered to 958 points of sale with a view to issuing them to the inhabitants of the agglomeration,
- nearly 4 million various tickets encoded on ŚKUP cards were sold for a total of about PLN 23 million,
- the holders of ŚKUP cards made more than 55 thousand card top-up transactions worth jointly ca. PLN 2.1 million.

Financial Markets segment financial results

The Financial Markets segment generated a profit before tax of PLN 61.1 million compared to PLN 1.8 million in H1 2015.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Net interest income	67.0	156.4	89.4	133.4%
Net fee and commission income	-0.9	-1.7	-0.8	88.9%
Dividend income	0.1	0.0	-0.1	-100.0%
Net trading income	-16.9	-36.5	-19.6	116.0%
Gains less losses from investment securities, investments in subsidiaries and associates	3.8	4.4	0.6	15.8%
Net other operating income	0.1	0.4	0.3	300.0%
Total income	**53.2**	**123.0**	**69.8**	**131.2%**
Net impairment losses on loans and advances	-0.5	0.3	0.8	-/+
Overhead costs and amortization	-51.0	-50.4	0.6	-1.2%
Taxes on bank balance sheet items	0.0	-11.7	-11.7	-
Profit before tax of Financial Markets	**1.8**	**61.1**	**59.3**	**3,294.4%**

The profit before tax of the Financial Markets segment in H1 2016 was driven by the following factors:

- **Increase of total income** by PLN 69.8 million year on year. The increase was attributable to significantly higher net interest income, mainly thanks to higher interest on derivatives. At the same time, net trading income was lower by PLN 19.6 million due to the valuation of CIRS instruments.
- **Stable operating costs (including amortisation)** amounting to PLN 50.4 million.
- **Taxes on Group balance sheet items** in the amount of PLN 11.7 million.

Activity of Financial Markets segment

Enhancement of sales of financial markets products

Since January 2016 the activities of the financial market products sales segment have been focused on increasing the activity of new clients and enlarging the Bank's share in the markets of FX products, commodity derivatives and interest rate risk hedging transactions related to large financing projects, as well as on selling commercial securities.

The key initiatives which impacted the volume of transactions and income generated from the Bank's cooperation with clients included:

- Activities aimed at using market volatility to increase the number of transactions per client. The main emphasis was put on active telephone contact with existing and new clients. The activities resulted in a growing number of active clients and rising turnover and margins.
- Micro-enterprises served by the retail part of mBank saw intensive on-boarding activities addressed to new clients and mobilisation campaigns aimed at existing clients who make transactions on Internet currency exchange platforms.

- The Derivative Instruments Division which sells transactions in commodity derivatives adjusted the scopes of responsibilities of sellers to reach a greater group of clients in an effective way and maximise the margins.
- Intensive selling activities were also taking place in the area of project-related transactions. Conducted in collaboration with mLeasing and mBH, they produced a number of new, smaller transactions.
- Measures designed to increase the sales of and margins on Treasury transactions with K0 (global companies) and K1 clients were continued resulting in a substantial increase in both margins and sales, especially on the market of FX derivatives.

mBank's shares in particular financial instruments markets are presented on the charts below.

Financial Institutions

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

As of June 30, 2016 mBank had nineteen active loans in the amount of PLN 23,264.3 million, of which the utilized value stood at PLN 14,334.2 million.

In H1 2016 a loan in EUR in the amount of PLN 88.2 million was repaid on time. In addition, the Bank took out two new loans in EUR in the total amount of PLN 1,018 million. As a consequence, the debt resulting from the loans went up by PLN 2,290.8 million against the end of H1 2015.

At the end of June 2016, mBank's total exposure resulting from loans granted to other banks amounted to PLN 146.9 million. mBank's portfolio comprised thirty-nine short- and medium-term active loans granted to financial institutions from Poland and abroad.

In H1 2016 mBank actively supported trade transactions concluded by Polish exporters by providing short-term financing to financial institutions, and granted financing as part of syndicated loans. At the same time, the Bank continued providing services to banks from the Commonwealth of Independent States and offering them medium-term loans secured with KUKE insurance policies.

mBank's custody services

mBank's custody clients are mainly investment and pension funds, local and foreign financial institutions, banks offering custodian and investment services, insurance companies, asset management institutions and non-financial institutions.

mBank provides services including settlement of transactions in securities registered in local 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, and processing corporate actions.

H1 2016 was another successful period in terms of custody operations. At the end of H1 2016 the number of serviced investment and pension funds rose by 62.0%, amounting to 346, while the total value of their assets grew by 47.0% compared with the end of H1 2015.

2.5. Subsidiaries of mBank Group

Summary of financial results of mBank Group subsidiaries

mBank Group subsidiaries generated a profit before tax of PLN 172.2 million in H1 2016, compared to PLN 187.8 million in H1 2015.

The profits of the subsidiaries mLeasing, mLocum, mBank Hipoteczny, and mFaktoring among others improved in the period under review.

The table below presents the profit before tax of the subsidiaries in H1 2016 compared to H1 2015.

PLN M	H1 2015	H1 2016	change in %
Aspiro	110.0#	78.3	-28.9%
mLeasing	27.8	41.2	48.5%
mLocum	11.1	15.1	35.7%
mBank Hipoteczny	8.3	13.4	61.2%
mFaktoring	2.8	11.2	298.1%
mCentrum Operacji	1.1	-1.0	+/-
Dom Maklerski mBanku	16.0	2.9*	-82.2%
mWealth Management	13.2	9.0*	-31.8%
Other[1]	-2.4	2.2	-/+
Total profit before income tax	**187.8**	**172.2**	-8.3%

1 incl. mFinance France, BDH Development, Garbary and Tele-Tech Investments

 # Including one-off gain on the sale of shares of BRE Ubezpieczenia TUiR in Q1/15

** Companies were integrated into the organizational structure of mBank as of May 20, 2016*

Business activity of mBank Group subsidiaries

An open platform for financial services sale on the intermediaries market
The offer comprises loans, deposits, insurance products, investments and savings for both individual customers and companies
Nearly 600 experienced client advisors

In H1 2016 Aspiro offered products of 25 financial service providers including mBank. The offer comprised 38 products, including mortgage loans, cash loans, insurance products, investment products, leasing and factoring.

Aspiro's sales of mortgage loans decreased by nearly 33.0% in H1 2016 compared to the same period last year. A decrease was strongly correlated with the shift in pricing policy of mBank, one of key business partners of Aspiro.

Despite a decrease in mortgage loans sales volume in mBank, Aspiro consistently develops sales volumes based on the offers of mBank Hipoteczny and other partners.

In H1 2015 Aspiro generated a profit before tax amounting to PLN 78.3 million compared with PLN 110.0 million (including a one-off gain on the sale of BRE Ubezpieczenia TuiR in the amount of PLN 72.5 million concluded in Q1 2015) in H1 2015. To a large extent the result was influenced by a contribution of insurance business area, in which Aspiro acts as an insurance agent.

Financing offer in the form of leasing or rent, and car fleet management
2nd position on the real estate leasing market
2th position on the overall leasing market in Poland

The value of contracts executed in H1 2016 by the subsidiary stood at PLN 2.1 billion compared with PLN 1.9 billion in H1 2015 (+10.0% year on year with the market growing by 18%). The value of lease contracts for movables went up by 23.0% (PLN 2.0 billion in H1 2016 against PLN 1.6 billion in H1 2015).

In H1 2016, in pursuit of the One Bank Strategy and development of a comprehensive offer for clients, the subsidiary continued the "Leasing in Retail" project addressed to micro-enterprises and SMEs, which can enter into contracts to lease vehicles of up to 3.5 tonnes.

In H1 2016 mLeasing posted a profit before tax of PLN 41.2 million, which is higher by 48.5% compared to PLN 27.8 million a year before, due to the decrease of interest expenses.

mBank Hipoteczny

Poland's largest mortgage bank

Focusing on financing commercial and public sector projects and investments of individual clients, market analyses and advisory services for investors and operators of commercial real estate industry

The largest issuer of covered bonds with a 66% market share. Outstanding securities worth PLN 4.6 billion

The gross loan portfolio of mBank Hipoteczny (mBH) reached PLN 8.5 billion in H1 2016 (+34% year on year), driven mainly by a systematic rise in the retail portfolio. In H1 2016 sales in this segment exceeded PLN 605 million. Moreover, in pursuit of its strategy mBank Hipoteczny acquired retail loans (in three tranches) with a total nominal value of over PLN 371,6 million from mBank. In addition, thanks to the effective sales of commercial loans the total value of new contracts in H1 2016 reached over PLN 1.2 billion, which represents a surge by 116% compared with H1 2015.

Despite the additional charge imposed on the bank in the form of a banking tax (PLN 6.4 million), in H1 2016 the subsidiary reported a 61.2% increase in profit before tax compared with H1 2015. As at June 30, 2016 profit before tax amounted to PLN 13.4 million (PLN 8.3 million a year before).

Similarly to the same period of 2015, the bank's profit was driven by the continued growth in the credit portfolio, in particular in the retail banking line. In the period covered by this report, the net interest income of mBank Hipoteczny grew by more than 17%. Moreover, net trading income also rose considerably, helped by improved matching of instruments in the hedge accounting area and a significant positive result on unrealised foreign exchange differences. In addition, compared with the previous year, loan loss provisions in H1 2016 dropped by PLN 3.3 million owing to a change in impairment parameters.

In H1 2016 mBank Hipoteczny was once again very active on the debt issuance market, which was reflected in four issues of mortgage bonds worth a total of PLN 671.3 million. Mortgage bonds were taken up by domestic (PLN 450 million) and foreign (PLN 50 million) institutional investors. Two of the issued mortgage bonds were priced with fixed coupon, for the first time in the history of mortgage banking in Poland. Thereby, the Bank persistently pursues its goal to issue covered bonds worth PLN 1.75 billion in 2016 backed by the growing pool of retail mortgage loans (a share of almost 40% in the collateral register). For more information about mBank Hipoteczny issuance of covered bonds see chapter 1.2. Key projects of mBank Group in H1 2016.

mLocum

A leading real estate developer titled "Developer of the year"

Development projects in Kraków, Łódź, Wrocław, Warszawa, Poznań and Sopot

Member of Polish Developers Association

In H1 2016, the company sold 189 apartments compared to 141 apartments a year earlier, which directly impacted financial results of the company. Currently mLocum leads projects in Kraków, Łódź, Wrocław, Warsaw, Poznań and Sopot.

In H1 2016, mLocum reported a profit before tax of PLN 15.1 million, compared to PLN 11.1 million a year earlier, which represents an increase by 35.7%.

Dom Maklerski

Comprehensive brokerage and capital market services for individuals and institutions as well as issues

The largest number of brokerage accounts on the Polish market, handling nearly 300 thou. customers

At the end of H1 2016, the number of clients of Dom Maklerski mBanku (mDM) stood at 295.0 thousand and increased by 1.0 thousand compared to H1 2015.

In H1 2016, mDM conducted the IPO of Polski Bank Komórek Macierzystych worth PLN 54.6 million. Additionally, Dom Maklerski mBanku took part in two significant transactions conducted on WSE during H1 2016 – public bond issues of BEST SA worth PLN 40.0 million and PLN 50 million.

On May 20, 2016, the process of integration of Dom Maklerski mBanku (and mWealth Management) within the Group structure has been finalized. Brokerage services that so far have been rendered through Dom Maklerski mBanku and mBank are carried out via single entity, i.e. mBank. The new model of rendering brokerage services enables mBank Group to better use its resources and potential, giving it an even greater competitive advantage in the brokerage services market.

Wealth Management

Private Banking & Wealth Management services

Comprehensive asset management by the company's experts and specialists from cooperating companies

In H1 2016, the company continued the development of its comprehensive wealth management services, including investment advisory and asset management. The assets managed by the company were stable compared to December 2015, and stood at PLN 5.3 billion as of May 20, 2016.

mWealth Management, as well as Dom Maklerski mBanku was subject to the integration of brokerage services within mBank Group. Starting from May 20, 2016, mWealth Management services are offered together with Dom Maklerski mBanku services through mBank brokerage bureau.

Faktoring

Domestic and export factoring with recourse, non-recourse factoring, import guarantees

8th position on the factoring market in Poland, with 7.4% market share

mFaktoring generated turnover of PLN 5.5 billion in H1 2016 (+9.0% year on year), which placed the company on the 8th position on the factoring market.

In H1 2016, the profit before income tax reported by mFactoring reached PLN 11.2 million compared to PLN 2.8 million a year earlier (+298.1%). A sharp increase was caused mainly by a lower amount of loan loss provisions booked in H1 2016.

Centrum Operacji

Back-office processes for mBank Group
Settlements servicing and database administration
Documentation storage in electronic and paper form, confidential data protection

In H1 2016, mCentrum Operacji (mCO) continued cooperation with current clients, in the field of services granted to mBank, Orange Finanse and mBank Hipoteczny.

In H1 2016, the company generated loss of PLN 1.0 million compared with PLN 1.1 million profit generated a year earlier.

A negative result for the first half of 2016 was caused mainly by provisions created on real estate properties owned by the company.

2.6. Risk management

Risk management foundations and key changes of H1 2016

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

Lines of defence

Risk management roles and responsibilities in mBank Group are organised around three lines of defence model:

- The first line of defence is **Business** (business lines) responsible for risk and capital management. Its task is to take risk and capital aspects into consideration when making business decisions, within the risk appetite set for the Group.
- The second line of defence, mainly **Risk** (risk management area), **IT, Security and Compliance function**, supports Business by creating strategies of managing particular risk types and relevant policies determining guidelines for Business with regard to decisions on taking risk by Business. The main purpose of the second line of defence is supporting Business in implementing strategies and policies as well as supervising the control functions in the Group and risk exposure.
- The third line of defence is **Internal Audit**, ensuring independent assessment of 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 Risk Catalogue of mBank Group).
- **Risk vs 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.

Risk management area is the key partner to the Business and the Management Board in creating lasting value for the Bank through ensuring a long-term balance between the expected rate of return for investors and the safety of the Group. These strategic objectives require an integrated approach to risk, capital, financing and profitability management.

Business and Risk Forum of mBank Group

In the risk management process, the Bank attaches high importance to the communication between the risk management area and the business lines. The Business and Risk Forum of mBank Group is a formal decision and communication platform for the risk management area and business lines of the Group.

The Forum is constituted by the following bodies:

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

The Committees are composed of the representatives of business lines and respective risk management departments.

Each Committee is responsible for the all types of risk generated by business activity of the given business line and performs the following tasks:

- **Discussing and taking decisions/issuing recommendations** concerning:
  - introduction of new products/instruments to the Bank's offer,
  - rules for managing the risk of products/instruments offered or planned to be offered by business lines, particular customer segments specific for given business line, and individual portfolios,
  - risk appetite of the business lines, e.g. approval of risk limits imposed on the given business line,
  - approval of the risk policies applicable to particular client segments,
  - client segments desired from the point of view of the expected risk portfolio structure,
  - priorities and directions of changes in the organisation of risk assessment processes and tools.
- **Exchange of information** about current and planned actions and projects, including sales plans and their implementation, sales campaigns.
- **Monitoring of the following aspects on the basis of submitted reports and information:**
  - quality and effectiveness of the risk-bearing portfolios held by business lines,
  - operational risk and other non-financial risk types,
  - quality of data used in risk management processes,
  - early symptoms of risk,
  - agreeing on preventive or remedial measures.

Key changes in the risk management area in H1 2016:

- Following the end-2015 update of the Risk Management Strategy of the mBank Group and Operational Risk Management Strategy of mBank Group, in H1 2016 the other strategies for managing particular risks were updated:
  - Retail Credit Risk Management Strategy of mBank Group,
  - Corporate Credit Risk Management Strategy of mBank Group,
  - Market Risk Management Strategy of mBank Group,
  - Liquidity Risk Management Strategy of mBank Group,
  - Reputational Risk Management Strategy of mBank Group.

  All above strategies, including the new challenges facing the risk management area in 2016, were approved by the Management Board and the Supervisory Board of the Bank.

- "The credit policy of financing of developers by mBank Group" was introduced. It is another common policy at the level of mBank Group after the policy regarding the financing of commercial real estate. In the form of a dialogue with the Business, the policy determined the framework for risk appetite and acquisition development of mBank Group on this market, developed the definition of residential development project, indicated risks and their mitigation measures; mBank Group portfolio of developers is limited by a dedicated limit.
- In H1 2016 implementation of the Internal Control System Self-assessment was completed in mBank Group subsidiaries. In the Bank, the Self-assessment was implemented in 2015. Thus, the process covers the whole activity of the Group. Self-assessment process is carried out on an annual basis. It aims at a comprehensive assessment of operational risk through: identification of material operational risks, inventory of control mechanisms dedicated to mitigate those risks, assessment of adequacy and effectiveness of control mechanisms, and assessment of the risk level and the development and implementation of the necessary plans of remedial measures.
- Adaptation works to the requirements of Recommendation W concerning model risk management in banks (published in July 2015 by the Polish Financial Supervision Authority) were completed. The works aimed at:
  - development of principles of models' classification and model risk measurement and monitoring in line with regulatory requirements,
  - implementation of the required reporting system concerning model risk at different levels of the organization,
  - supplementing the existing models' management process, particularly in the field of documentation, with elements indicated in the Recommendation.

  The abovementioned works resulted, among others, in the update of Model Management Policy, which was supplemented with provisions addressing requirements of the Recommendation W. The updated Policy was approved by the Management Board and the Supervisory Board of the Bank.

  In addition, Model Risk Committee responsible for supervising model risk management process, was appointed. The Committee performs information, discussion, decision and legislative functions. In particular, the Committee:
  - approves the new and redesigned models, as well as amendments thereto, deciding also about the resignation from the application of the model,
  - takes decisions on the scope of application of the group and external models, including central models, in banking processes,
  - recommends the tolerance level for model risk and submits its findings to the decision of the Management Board and the Supervisory Board,
  - takes the final decision regarding approval of the significance assigned to a given model,
  - approves preventive and remedial measures indicated within the results of monitoring,
  - accepts the schedule for validation of models and the results of each model validation.

  The functioning of the Committee ensures an adequate level of independence between the various participants in the model risk management process and enables to avoid conflicts of interest between them. The Committee also provides the validation unit with the ability to issue binding recommendations with an adequate priority.
- Programme of continuous increase of work efficiency in the Risk Area based on the Lean Management rules, which started in 2015, was continued in H1 2016. Special emphasis is put on introducing the culture of responsibility and mechanisms for continuous process improvement. The purpose of the programme is to allow the growing number of tasks accompanying business growth and increasing number of regulatory requirements to be absorbed by more effective use of existing resources. The programme is one of the activities supporting the implementation of the new strategy of mBank Group.

- Adaptation works to the requirements of the updated Recommendation C concerning concentration risk management, published by the Polish Financial Supervision Authority in May 2016 (which replaced the Recommendation C on exposure concentration risk management issued by the banking supervision in 2002) have been commenced. The PFSA expects that the revised Recommendation C will be implemented by banks not later than on January 1, 2017. The works will be continued by the Bank in the second half of 2016.
- The Bank carried out IFRS 9 implementation project including, among others, analytical work in assessing the impact of IFRS 9 on the methodology for calculation of provisions in the Group; implementation of the necessary changes was also started. IFRS 9 changes the requirements for classification and evaluation of financial assets and implements the impairment model based on the expected losses calculated for certain instruments over the lifetime of the asset. IFRS 9 will take effect starting from January 2018.

In connection with the approval by the Management Board and the Supervisory Board of the Bank of the mBank Group 2016-2020 Strategy "mobile Bank", risk management area will be actively involved in the implementation of initiatives and actions undertaken under the three pillars of the new strategy: empathy to customers, icon of mobility and efficiency.

Main risks of mBank Group's business

The Management Board of mBank takes measures necessary to ensure that mBank manages all significant risks arising from the implementation of the adopted business strategy.

Within the Group's risk inventory process implemented under the principles of ICAAP (Internal Capital Adequacy Assessment Process), the following risks were recognized as material in the operations of the Group as of June 30, 2016:

1. credit risk,
2. operational risk,
3. market risk,
4. business risk (including strategic risk),
5. liquidity risk,
6. reputation risk,
7. model risk,
8. capital risk (including risk of excessive leverage).

The Bank monitors all the aforementioned risks within ICAAP. Due to the specificity and characteristics of the portfolio, the section presents the rules of monitoring credit risk, operational risk, liquidity risk, market risk of the trading book as well as interest rate risk of the banking book 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 and T) 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 Group subsidiaries internal regulations.

The Bank and Group subsidiaries in their credit risk management process use the core risk measures defined under the AIRB approach:

- PD – Probability of Default (%),
- LGD – Loss Given Default (%),
- EAD – Exposure at Default (amount),
- EL – Expected Loss (amount), as well as related measures including:
- RD – Risk Density, which is defined as EL to EAD (%),
- LAD - Loss at Default (amount of 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 risk. Capital required to cover unexpected loss is estimated at a confidence level of 99.91%. For this purpose, the Bank uses the following measure:

- RWA – Risk Weighted Assets used under the AIRB approach to calculate regulatory capital required to cover credit risk (unexpected loss).

In managing mortgage-secured credit exposures for different types of real estate and also for different products, 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.

Thanks to its simplicity, this measure is broadly used in communication with clients and in the construction of price matrices for credit products.

Stress testing is an additional tool of credit risk assessment which supplements CVaR (Credit Value at Risk) measurement of unexpected loss. Stress testing of the economic capital required to cover credit risk is measured quarterly.

Stress tests of credit risk are two-dimensional, analysed separately and jointly:

- The analysis of sensitivity of ECVaR model indications to assumptions concerning credit exposures (e.g., correlation) – i.e., parametric tests.
- The analysis of extreme credit losses on the assumption of an unfavourable macroeconomic situation – i.e., macroeconomic tests in which an econometrical model forecasts values of input parameters for the economic capital model (PD, LGD) based on assumptions of the Chief Economist about macro parameters in the case of the negative economic scenario. The risk parameters developed according

to the above scenario form the basis for calculating economic capital both before and after the assumptions of parametric tests are taken into account.

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

For corporate credit risk, the Group estimates 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.
- 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, including exposures of both mBank and the Group's subsidiaries.

To minimise credit risk, the Group uses a broad range of collateral for credit products, also necessary to actively manage the capital requirement. In their assessment of the quality of risk products, mBank and mLeasing use the MRV ratio (Most Realistic Value), which reflects the worst-case scenario of debt enforcement through forced sale of collateral.

In addition, the decision-making process and the assessment of profitability per client in the CRM system use the RORAC ratio (Return on Risk Adjusted Capital), or return on the capital invested in risk products.

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 represent the quality of cohorts of loans at a different phase of their lifetime taking into account disbursement time (e.g. each quarter), clients' characteristics etc., based on DPD.
- 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

The Strategy of the corporate credit risk management in mBank Group was updated in March 2016. The main goal of mBank Group in corporate credit risk management is to unlock synergies in the Group by integrating the offer of the Bank and Group subsidiaries in sales of risk-bearing products to mBank Group clients, ensuring closer co-operation in credit risk measurement and management, defining a safe level of risk appetite. The Strategy is complemented by sector policies, the limit book, the credit process rules, decision-making powers and detailed banking procedures both in mBank and the Group subsidiaries which generate credit risk and impact the quality of corporate credit risk management. The implementation of uniform risk measures and risk controlling processes at the Group level takes into account the specificities of the Group entities. The Bank makes sure that the process does not affect client relations. Update of the Strategy also implemented the further unification of corporate credit risk management parameters applied in mBank and Commerzbank which is reflected in changes of the Steering Matrix used to on-going management of concentration risk (new definition of the High Attention Part).

In H1 2016 "The credit policy of financing of developers by mBank Group" was drafted and approved. A uniform approach to credit risk assessment of developers was adopted in mBank and mBank Group subsidiaries. A framework was set up to safely build a portfolio of exposures financing the developers by defining the preferred acquisition market and outlining the recommended terms of financing.

To complement the Food & Agribusiness (F&A) clients finance policy approved in May 2015 by KRK, at the beginning of 2016 the process of servicing F&A clients was finally implemented, including individual farmers serviced in the corporate area of mBank.

The diversified approach to corporate clients is tied to the client's risk level as measured by PD and credit risk concentration measured with LAD of a client or a group of related clients, taking into account the exposure of the Group subsidiaries.

The credit decision-making system is consistent with the Corporate Credit Risk Management Strategy and the approved principles of the Credit Risk Policy. The competent decision-making levels are defined in a decision-making matrix. On that basis, depending on the EL-rating and the aggregate exposure for a client or group of related clients, the appropriate decision-making level responsible for the credit decision is assigned.

mBank follows a simplified credit decision-making procedure for a defined group of clients and transactions, in particular transactions under fast credit procedures (FCP), which enhances effectiveness while ensuring compliance with all legal and supervisory requirements and good practice of credit risk management.

The restructuring of the process also includes phased implementation of anti-fraud mechanism. The new strategy has enabled not only the development of a new workflow platform but also in accordance with the spirit of 'Client centric' simplified documentation, required and delivered to client, and its digitisation in credit process. 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 and the resulting formal limits, guidelines and recommendations on the Group's exposure to selected companies, 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.

In order to mitigate the risk of lending and guarantees, the Bank classifies and monitors credit risk products. The Group uses write-offs and provisions under the International Financial Reporting Standards (IFRS). The Bank also 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 corporate banking, the Group avoids concentration in industries and sectors whose credit risk is considered excessively high. The acceptable risk level is defined taking into account market segmentation and sector concentration limits. In compliance with Recommendation S of the Polish Financial Supervision Authority, the Bank has identified a mortgage-secured credit exposure portfolio, not only in retail banking but also in corporate banking. 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. The main principles of mortgage-secured credit exposure risk management in corporate and investment banking, the risk profile, division of responsibilities, rules of determining internal limits, and rules of reporting are set out in the mBank Mortgage-Secured Credit Exposure Risk Management Policy.

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 which are low in capital consumption, in particular products of investment banking (ECM, DCM, M&A), transactional banking and financial markets, as well as arrangement of syndicated finance for selected big ticket clients to ensure satisfactory profitability and mitigate the risk of high concentration of individual clients/groups of related companies.

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 state-of-the-art transactional platform, savings and insurance products address all financial needs of clients within the Group.

Apart from the Polish market, Retail Banking credit products are offered (since 2007) 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 since 2000. The share of the foreign branches' exposure portfolio was ca. 9% of the value of the retail loans portfolio at the end of June 2016. The Bank ensures the coherence of the credit risk management policy on all markets; any differences in specific rules or parameter values 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, 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);
- alignment of decision-making endowment with mass acquisition, including automation of decision-making for selected transactions;
- 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 segmentation serves two main functions:

- ensuring correct alignment of risk rating methods (models, procedures, required documentation) with the client's risk profile, exposure and business requirements,
- defining homogeneous transaction sub-portfolios to enable assessment of their quality in the context of the generated income margin.

The main point of reference in the retail banking credit risk management process is risk appetite defined in correlation with the strategy of the Bank which provides for:

- optimisation of the balance-sheet structure in terms of profitability and financing by reducing the growth rate of credit portfolios with long tenors (and low margins) while supporting growth of short-term loans (with high margins),
- developing long-term financing of the Group's lending with mortgage bonds issued against retail mortgage loans.

Taking into account the above assumptions, the general principle underlying the lending strategy of the Group 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.

These initiatives include lending to clients under a joint project of mBank and one of the biggest telecom operators (Orange Finanse Project). Furthermore, the Bank increasingly provides financing to clients doing shopping online. To reduce operational risks of accepting new clients, the Bank develops its credit policy using, among others, credit testing and is actively developing its fraud prevention system.

mBank decided to stop acquisition of mortgage products for private individuals commencing July 1, 2016. In the mBank Group, the sale of loans for financing residential real estate will be carried out by mBank Hipoteczny. The new acquisition will be restricted to products which may be financed with issue of mortgage bonds - non-purpose mortgage loans and loans to finance cooperative ownership right to premises will be withdrawn from the offer. Only mortgage loans for Private Banking clients will remain in the offer of mBank's retail banking area. The current conservative policy of assessing borrowers' reliability and creditworthiness will be maintained; 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.

In its credit risk management process, the Bank attaches great importance to communication between the risk area and the retail banking area. The Retail Banking Risk Committee is a platform of decision-making and dialogue between the two areas. The Committee covers both credit risk and all secondary risks derived from accepted credit risk (reputation risk, legal risk, operational risk, data quality risk, etc.).

Quality of the loan portfolio

As of 30.06.2016, the share of impaired exposures in the total (gross) amount of loans and advances granted to clients remained at the level noted at the end of 2015, i.e. 5.8%.

Provision for loans and advances to customers increased from PLN 2,975.9 million at the end of 2015 to PLN 3,087.4 million at the end of June 2016. The IBNI (Incurred But Not Identified) loss provision increased from PLN 247.2 million to PLN 253.3 million in that period.

The ratio of provisions to non-performing loans remained unchanged (58.5%).

To assess impairment, the Bank applies credit the risk parameters based on those derived from the A-IRB methodology.

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.

At the end of June 2016, the Group's loans and advances (net) to customers rose by 3.0%, where the increase was in half driven by the rising mortgage and housing exposure. In the corporate portfolio, term loans granted to SME grew, while the exposure to large enterprises decreased.

The table below presents the quality of mBank Group's credit portfolio as at the end of June 2016 compared to the end of 2015 and the end of June 2015.

Quality of mBank Group's Loan Portfolio	30.06.2106 (in PLN thou.)	31.12.2015 (in PLN thou.)	30.06.2015 (in PLN thou.)
Loans and advances to individuals:	**48 272 191**	**46 258 683**	**45 328 730**
- current accounts	6 276 593	5 897 129	5 800 143
- term loans, including:	41 995 598	40 361 554	39 528 587
- housing and mortgage loans	35 220 185	34 184 208	33 521 442
- other	-	-	-
Loans and advances to corporate entities:	**33 936 902**	**33 446 644**	**32 226 547**
- current accounts	4 725 577	3 976 187	4 218 458
- term loans:	**27 424 522**	26 976 422	25 752 358
- large enterprises	5 293 658	5 825 318	5 843 425
- medium & small enterprises	22 130 864	21 151 104	19 908 933
- reverse repo/buy sell back	131 734	1 031 029	842 093
- other	1 655 069	1 463 006	1 413 638
Loans & advances to public sector	**1 357 033**	**1 520 728**	**1 661 475**
Other receivables	**296 038**	**183 355**	**1 043 880**
Total (gross) loans and advances to customers	**83 862 164**	**81 409 410**	**80 260 632**
Provision for loans and advances to customers (negative amount)	(3 087 355)	(2 975 864)	(3 019 034)
Total (net) loans and advances to customers	**80 774 809**	**78 433 546**	**77 241 598**
Short-term (up to 1 year)	26 897 267	26 169 938	23 185 351
Long-term (over 1 year)	53 877 542	52 263 608	54 056 247
Incurred but not identified (IBNI) losses			
Gross balance sheet exposure	79 016 656	76 777 938	75 411 743
IBNI loss provision for portfolio exposures	(253 341)	(247 198)	(261 858)
Net balance sheet exposure	**78 763 315**	**76 530 740**	**75 149 885**
Impaired exposures			
Gross balance sheet exposure	4 845 508	4 631 472	4 848 889
Provisions for impaired exposures	(2 834 014)	(2 728 666)	(2 757 176)
Net balance sheet exposure	**2 011 494**	**1 902 806**	**2 091 713**

Market risk

mBank organises market risk management processes in line with the requirements resulting from law and recommendations issued by regulators, in particular PFSA Recommendations (among others A, 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, prices of securities, 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) which may materialise in the form of losses reflected in mBank's financial performance. Moreover, the Bank 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. In particular, in order to measure the interest rate risk of Retail and

Corporate Banking products without a fixed interest revaluation date or with rates administered by the Bank, the Bank uses replicating portfolio models. Since 2013, the Bank uses the capital modelling concept, which is reflected in market risk measurement at the level of the Bank's internal organisational structures. Market risk measures of the interest positions of the banking book are calculated with the use of net present value (NPV) models. Market risk exposure is quantified by measurement of Value at Risk (VaR), measurement of expected loss under condition that this loss exceeds value at risk (ES – Expected Shortfall) and by use of stress tests.

Stress testing reflects the hypothetical change in the present valuation of mBank's portfolios that would occur as a result of stress-test scenarios, i.e., specific stressed values of risk factors in a one-day time horizon.

Stress testing includes a standard stress test defined for standard risk factors: FX rates, interest rates, stock prices and their volatility, as well as a stress test including change of credit spreads. This addresses among others the requirement for stress tests to cover independent impact of underlying risk (spread between T-bond yields and IRS rates) to which the Bank is exposed by holding a portfolio of T-bonds.

Value at Risk measures the potential loss of market value (of a financial instrument, a portfolio, an institution) such that the probability of generating or exceeding it within a set time horizon is equal to the set tolerance (confidence) level assuming an unchanged portfolio structure within a defined period of time. mBank calculates and limits one-day Value at Risk at a 97.5% confidence level. In addition, VaR is calculated for the following risk factors: interest rates, FX rates and their volatility, stock prices and their volatility, and credit spreads. Additionally, from September 2015 measurement of the value at risk in stressed conditions was introduced as observed measures. It is the potential loss in unfavourable market conditions different from typical market behaviour. Stressed VaR is a version of VaR measure in defined stressed conditions.

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 mBank limited risk appetite for interest rate risk in long term buckets by setting BPV (+1bp) limit for total interest rate mBank Group position for tenors above 20 years and above 30 years, as well as it established allowed risk appetite for credit spread risk by setting CS BPV (+1bp) limits in structure described by rating categories for all treasury, commercial and own receivables debt papers on mBank Group portfolio from 1 January 2016.

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. 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.

The market risk profile is derived from the strategic goals of business units, the policy of 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 of organisation of the market risk management process stipulates separation between the market risk monitoring and control function and the functions related with opening and maintaining open market risk positions.

The market risk monitoring and control functions (assigned to the second line of defence) are performed by the Financial Markets Risk Department (DRR) in the Risk Area of the Bank supervised by the Vicepresident of the Management Board, Chief Risk Officer, whereas operational management of market risk positions (assigned to the first line of defence) takes place in the Financial Markets Department (DFM), and the Treasury Department (DS) supervised by the Vicepresident of the Management Board, Head of

Financial Markets, in the Debt Securities Issue Department (DCM) and Structured and Mezzanine Finance Department supervised by the Vicepresident of the Management Board, Head of Corporate and Investment Banking, as well as in Own Transactions Department in Brokerage Bureau (BM_DTW) supervised by the Vicepresident of the Management Board, Head of Retail Banking.

In H1 2016 mDom Maklerski was merged with mBank. As a result Own Transactions Department in Brokerage Bureau (BM_DTW) was established and replaced Brokerage Bureau. BM_DTW carries out its operations focusing on financial instruments traded on the Warsaw Stock Exchange (WSE). The Debt Securities Issue Department (DCM) is responsible for debt origination and management of positions in non-Treasury securities on the banking book. Investment positions sensitive to market risk factors are managed by the Structured and Mezzanine Finance Department (DFS).

In addition, the Bank applies the rule of organizational separation between managing banking book operations (including portfolios of Treasury Department, Debt Securities Issue Department and Structured and Mezzanine Finance Department) and trading book operations (including portfolios of Financial Markets Department and Own Transactions Department in Brokerage Bureau).

In order to limit the level of exposure to market risk, the Bank's Management Board (for the Bank portfolio) and the Financial Markets Risk Committee operating as part of the Business and Risk Forum (for portfolios of business units) set VaR limits, stress test limits, as well as maturity gap limits which are warning thresholds. These limits are cascaded to lower levels in accordance with the principles of the management of specific types of market risk and the internal procedures of the front-office units, which are dedicated to individual portfolios or risk positions. This is aimed at conscious development of the required market risk structure and acceptable level of exposure to individual type of market risk.

In Q1 2016, the Bank finalised a review of the Market Risk Management Strategy of mBank Group. The modified Strategy was approved by the Bank's Management Board on February 9, 2016, received a positive opinion of the Risk Committee of the Supervisory Board, and was finally approved by the Supervisory Board on March 24, 2016.

Measuring mBank's risk

Value at Risk

In H1 2016, 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 average utilisation of VaR limits for the portfolio of the Financial Markets Department (DFM), whose positions consist of trading book portfolios, amounted to 40% (PLN 2.2 million), for the Own Transactions Department in Brokerage Bureau (BM_DTW) 15% (PLN 0.15 million), and for the Treasury Department (DS), whose positions are classified solely in the banking book, 81% (PLN 34.2 million) for the positions without capital modelling, and 63% (PLN 26.3 million) for the positions with capital modelling. The average utilisation of the VaR limit for the positions of the Debt Securities Issue Department (DCM) was 44% (PLN 0.8 million). In H1 2016, the VaR figures for the Bank's portfolio were driven mainly by portfolios of instruments sensitive to interest rates and to selected credit spread – T-bonds portfolios managed by DS in the banking book and managed by DFM in the trading book including interest rate swap positions. The DFM portfolios of instruments sensitive to changes in exchange rates, such as FX futures and options, and the exposure of the BM_DTW portfolios to equity price risk and the risk of implied variability of options traded on the WSE had a relatively low impact on the Bank's risk profile. In H1 2016 mDom Maklerski was merged with mBank. As a result of the merger of units carrying out its operations focusing on financial instruments traded on the stock exchanges in both entities Own Transactions Department in Brokerage Bureau was established and replaced the previous Brokerage Bureau. Increase of market risk measures caused by the merger was insignificant.

The table below presents VaR statistics of mBank's portfolio in H1 2016:

PLN thousand	H1 2016				2015			
	30.06.16	average	max	min	31.12.2015	average	max	min
VaR IR	12 274	14 097	18 454	11 042	13 688	16 085	23 329	12 739
VaR FX	561	518	794	351	496	685	1 096	453
VaR EQ	188	150	424	62	79	5 170	6 588	67
VaR CS	27 734	27 844	29 622	26 058	26 320	23 916	26 345	20 426
VaR	**33 452**	**35 981**	**40 726**	**29 334**	**29 943**	**27 877**	**34 881**	**21 266**

VaR IR – interest rate risk
VaR FX - FX risk
VaR EQ – stock price risk
VaR CS – credit spread risk

The graph below presents changes in VaR for mBank in 12 months to 30.06.2016 (PLN M):

VaR statistics in stress conditions

Since the beginning of September 2015 new VaR statistics in stress conditions have been introduced (it is a tracked measure). The table below presents VaR statistics in stress conditions for H1 2016 in comparison to statistics of this measure for Q4 2015:

PLN thousand	H1 2016				Q4 2015			
	30.06.2016	average	max	min	31.12.2015	average	max	min
Stressed VaR IR	40 836	42 497	48 483	36 890	37 742	35 742	39 293	31 053
Stressed VaR FX	1 134	1 202	2 655	576	1 338	1 376	2 933	516
Stressed VaR EQ	230	180	519	2	4	8 721	13 074	4
Stressed VaR CS	89 770	85 549	91 729	74 731	73 992	75 255	77 899	73 530
Stressed VaR	**119 956**	**117 252**	**126 171**	**105 462**	**103 060**	**111 038**	**116 945**	**102 035**

Stress testing

The utilisation of stress tests for mBank in H1 2016 is presented in the table below:

PLN M	H1 2016				2015			
	30.06.2016	average	max	min	31.12.2015	average	max	min
Base stress test	51	90	120	51	74	107	134	68
CS stress test	683	687	724	636	640	689	770	611
Total stress test	**734**	**776**	**841**	**703**	**714**	**796**	**900**	**699**

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 2016, the average utilisation of the stress test limits for mBank without capital modelling was 60% (PLN 776.4 million). The average utilisation of the stress test limits was 69% (PLN 659.1 million) for the portfolio held by DS without capital modelling and 69% (PLN 658.9 million) with capital modelling. The average utilisation of the limit was 37% (PLN 93.2 million) for the DFM portfolio, 11% (PLN 0.8 million) for the BM_DTW portfolio, and 55% (PLN 33.6 million) for the DCM portfolio. 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 interest rates.

Interest rate risk of the banking book

In H1 2016, 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 value of the portfolio over the period, was as presented in the table below:

PLN M	H1 2016				2015			
	30.06.16	average	max	min	31.12.15	average	max	min
PLN	109,5	71,5	117,3	34,7	99.4	55.4	122.2	8.4
USD	7,5	6	13	1,2	3.7	2.4	7.5	0.7
EUR	69,2	62,5	128,7	50,2	52.5	37.3	63.1	0.0
CHF	2,3	4,2	12,2	0	2.4	8.1	38.8	0.0
CZK	3,1	3,2	6,3	2,4	2.7	2.3	4.8	1.3

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 H1 2016 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 H1 2016.

PLN thousand	mBank Group	mBank	mBH	mLeasing
VaR IR average	14 557	14 097	184	292
VaR FX average	531	518	33	19
VaR EQ average	170	150	0	0
VaR CS average	27 844	27 844	0	0
VaR average	36 473	35 981	195	294
VaR max	41 221	40 726	302	339
VaR min	29 551	29 334	100	261
VaR 30.06.2016	**34 008**	**33 452**	**198**	**298**

For comparison, at the end of 2015, VaR for mBank Group was PLN 30 158 thousand, including VaR of mBank at PLN 29 943 thousand, mBank Hipoteczny – PLN 99 thousand and mLeasing – PLN 273 thousand.

The graph below presents changes in VaR for mBank Group in H1 2016 (PLN M):

Stress testing

The utilisation of stress tests for mBank Group in H1 2016 is presented in the table below:

PLN M	H1 2016				2015			
	30.06.2016	average	max	min	31.12.2015	average	max	min
Base stress test	56	95	125	56	78	111	139	72
CS stress test	700	701	742	642	647	691	772	613
Total stress test	**756**	**796**	**864**	**714**	**725**	**802**	**905**	**705**

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 2016, the average utilisation of the stress test limits for mBank Group without capital modelling was 59% (PLN 796.1 million) and for mBank Group with capital modelling was 56% (PLN 756.2 million).

Liquidity risk

mBank organises liquidity risk management processes in line with the requirements resulting from law and recommendations issued by regulators in particular PFSA Recommendations (among others P, 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).

For this purpose, 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 Financial Markets Risk Department. The main measures used in liquidity risk management of the Bank include ANL (Available Net Liquidity) measures, the regulatory measures (M1, M2, M3, M4) and LCR, and NSFR for analysis only. ANL measures reflect the projected future cash flow gap of assets, liabilities and off-balance-sheet commitments of the Bank, which represents potential risk of being unable to meet liabilities within a specific time horizon and under a certain scenario. ANL scenarios have been modified in Q4 2015 in order to comply with the update of Recommendation P and were operationally implemented in Q1 2016. These measures include base scenario (ANL Base), and three liquidity stress test scenarios: internal (ANL Stress), systemic (ANL Stress Market) and a combination of both (ANL Stress Combined). Cash flow projections used in these measures are based on crisis scenarios, which include 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 Bank has a process of reporting and monitoring of intraday liquidity position.

In order to support the process of liquidity risk management, Bank has a system of early warnings indicators (EWI). 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.

In October 2015, the Commission Delegated Regulation (EU) No 2015/61 of 10.10.2014 to supplement Regulation (EU) 575/2013 came into force. Starting with the report as of October 31, 2015, mBank reports to the Polish Financial Supervision Authority its calculations of LCR with implemented changes according to the mentioned delegated regulation using special forms designed by the PFSA. Moreover, the Bank reports to the NBP according to existing standards. EBA and NBP announced that receiving reports of LCR according to new technical standard will be ready in October 2016 starting with report as September 30, 2016, which means that two standards will be in force until September 30, 2016. In terms of the NSFR works have been carried out to adapt to the guidelines set out in the document BIS Basel III: the net stable funding.

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 and internal measures.

The first category includes four liquidity measures determined by the Polish Financial Supervision Authority: M1, M2, M3, M4 and LCR measure, which is additionally reported to the National Bank of Poland. NSFR measure (Net Stable Funding Ratio) is monitored.

The liquidity risk internal limit system is based mainly on defining acceptable level of gaps in defined tenors for ANL measures 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.

The Bank has a centralised approach to the Group's funding management in order to increase the efficiency of liquidity resources used. According to its principles, mBank Hipoteczny raises additional funding in the market by issuance of covered bonds and from mBank, while mLeasing and other subsidiaries raise almost all of their funding from mBank. Financing of subsidiaries is done via the Treasury Department.

The centralised approach to the financing of the Group subsidiaries enables to ensure better matching of the tenors of funding and a uniform treatment of particular subsidiaries within the unified system of transactional rates.

In Q1 2016, the Bank finalised a review of the Liquidity Risk Management Strategy of the mBank Group. The modified Strategy was approved by the Bank's Management Board on January 26, 2016, received a positive opinion of the Risk Committee of the Supervisory Board, and was finally approved by the Supervisory Board on March 24, 2016.

The Contingency Plan in case of the threat of losing financial liquidity is in place at the Bank. It sets the strategy and procedures in the event of the threat of a liquidity loss by mBank Group aimed at neutralization of the threat. The regulation defines the division of responsibility for monitoring, identifying threats and actions during the emergency. Contingency Plan is tested at least annually.

Bank limits the volume of foreign currency funding of mBank with FX-swaps and CIRS. The limit is set in order to determine the relevant risk appetite accepted by the Bank in this respect. 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 limit structure reflects the Bank's preference for currency funding with long tenors.

Due to the ongoing works on the act on the conversion of the FX mortgage portfolio, mBank maintains the funding strategy adopted in 2015 of increased share of fx-swaps and CIRS in funding FX loans portfolio. Adopted strategy is associated with increased risk of concentration of short term transactions and their frequent rollovers. For this purpose the monitoring of concentration in fx-swap transactions with maturities below 12 months is in place with MAT (Management Action Trigger) numbers on concentration in particular terms. Moreover the liquidity gap includes an outflow covering additional need for potential collateral resulting from unfavorable market factors influencing the valuation of fx-swap and CIRS transactions.

Measuring mBank's liquidity risk

The liquidity of mBank remained safe in H1 2016, as reflected in the high surplus of liquid assets over short-term liabilities in ANL measures and in regulatory measures. Since May 21, 2016 the data includes Dom Maklerski mBanku, which was merged with mBank S.A. on that day.

The table below presents the ANL gaps for tenors up to 1M and 1Y in H1 2016 as well as the regulatory measures M1, M2, M3, M4 and LCR:

Measure*	H1 2016			
	30.06.2016	mean	maximum	minimum
ANL Base 1M**	16 583	15 263	18 470	12 252
ANL Base 1Y**	15 356	14 835	17 127	12 392
ANL Stress 1M**	14 283	12 996	16 172	10 377
ANL Stress 1Y**	12 808	12 922	14 656	10 458
ANL Stress Market 1M**	13 201	11 549	13 538	9 650
ANL Stress Combined 1M**	12 417	10 788	12 761	8 913
M1	14 544	12 581	16 182	7 681
M2	1,47	1,40	1,54	1,26
M3	4,74	4,57	4,98	4,03
M4	1,36	1,31	1,36	1,28
LCR mBank	149%	138%	149%	126%

** ANL Base, ANL Stress, ANL Stress Market, ANL Stress Combined and M1 are shown in PLN million, M2 is a relative measure presented as a decimal, ANL Stress is limited up to 1Y, ANL Stress Market and ANL Stress Combined are limited up to 1M*

*** Means, maximums and minimums are calculated for period starting from February 1, 2016.*

Measuring the Group's liquidity risk

The Group's liquidity risk measurement includes mBank Hipoteczny, mLeasing, and until 20th May 2016 Dom Maklerski mBanku, which was merged with mBank S.A. on May 21, 2016. mBank monitors liquidity risk of the subsidiaries in the ANL Stress tenors so as to protect liquidity also at the Group level in the event of adverse events (crises).

The Group's liquidity was safe in H1 2016, as reflected in the high surplus of liquid assets over short-term liabilities in the ANL Stress tenors calculated at Group level.

The table below presents the ANL Stress gap for tenors up to 1M and 1Y at mBank Group level:

Measure*	H1 2016			
	30.06.2016	mean	maximum	minimum
ANL Stress 1M**	15 410	14 519	17 441	12 214
ANL Stress 1Y**	13 713	14 458	15 893	12 176

** ANL Stress is shown in PLN million.*

*** Means, maximums and minimums are calculated for period starting from February 1, 2016.*

Operational risk

mBank organises the operational risk management process taking into account the rules and requirements set out in the Resolution No. 76/2010 of the Polish Financial Supervision Authority of March 10, 2010 as well as in the Regulation (EU) No 575/2013 of the European Parliament and of the Council of June 26, 2013. The abovementioned regulations as well as recommendations of the Polish Financial Supervision Authority (including Recommendations M, H and D, in particular) constitute a starting point for developing the framework of the operational risk control and management system in mBank Group.

Tools and measures

The Bank understands operational risk as the possibility of incurring a loss arising from inadequate or defective internal processes, systems, errors or actions taken by the Bank's employee or from external events. In particular, operational risk includes legal risk.

Operational risk accompanies all processes at banks (inadequate or defective internal processes, systems, human errors or external events) 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 (identification, monitoring, measurement, assessment, reporting as well as reduction, avoidance, transfer or acceptance of 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 once a year by the Bank's organizational units. The aim of the process is to increase the awareness of operations risk, create a platform for communication about the necessity of changes and improvements in control processes, and thus a more active approach to operational risk management. The end result of the self-assessment is to identify and assess key risks and control mechanisms as well as to create 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 implementation of the self-assessment process was completed in the Bank in September 2015. The process replaced formerly existing functional control and Business Environment Assessment Surveys. The implementation of the self-assessment process in mBank Group subsidiaries and foreign branches was completed in H1 2016.

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

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.

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 and Capital Management Department and at organizational units, which 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 implementation of qualitative elements and comprehensive collection of operational loss data is required for both the standard and the advanced measurement method (AMA) for the calculation of regulatory capital in accordance with the requirements of the New Capital Accord and in order to fulfil the relevant Pillar II requirements.

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 and Capital 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.

Capital Adequacy

Maintaining an adequate level of capital is one of the main aims of the Bank. The Management Board of mBank ensures consistency of the capital and risk management process by means of a system of strategies, policies, procedures and limits for the management of particular risks which constitute the ICAAP (Internal Capital Adequacy Assessment Process) architecture. Furthermore, in line with the Capital Management Policy applicable at mBank, the Bank maintains an optimum level and structure of own funds, guaranteeing maintenance of the Capital Adequacy Ratio at a level higher than the statutory minimum, at the same time covering all significant risks identified in the Bank's operations. mBank's capital targets are being set based on the regulatory requirements and simulated capital needs to cover unfavourable changes in the external environment and within the Bank.

The Capital Management Policy at mBank is based on two main pillars:

- Maintenance of an optimal level and structure of own funds, with the use of available methods and means (retained net profit, issue of shares, subordinated bonds, etc.).
- Effective use of the existing capital among others by applying a system of capital utilisation measures resulting in reduction of the activity that is not generating the expected return and development of products with lower capital absorption.

Capital Adequacy of mBank Group

The capital ratios of mBank Group in first half of 2016 were driven by the following factors:

- inclusion of net profit of mBank Group for the year 2015 in Common Equity Tier 1 capital, net of expected charges and dividend;
- inclusion of net profit of mBank Group for the 1st quarter of 2016, net of expected charges and dividends, on the basis of the PFSA (Polish Financial Supervisory Authority) permission from June 21, 2016;
- change of the limit for grandfathered subordinated instruments included in own funds;
- inclusion of 60% of unrealised gains measured at fair value in the own funds calculation;

- change of methodology of additional value adjustments calculation, deducted from Common Equity Tier 1;
- change of accounting policy concerning the valuation of subsidiaries, associates and joint ventures in the stand-alone financial statements;
- recalibrations of AIRB models;
- expansion of mBank Group business activity;
- depreciation of the Polish currency against the foreign currencies in the first half of 2016.

Starting from 2016, banks are obliged to maintain additional own funds to cover conservation buffer of 1.25% of total risk exposure amount in the light of the entry into force in 2015 of the Act on Macro-prudential Supervision over the Financial System and Crisis Management in the Financial System transposing CRD IV provisions to Polish prudential regulations.

In December 2015, Financial Stability Committee (macro prudential supervision comitee) decided to set a the countercyclical capital buffer rate at the level of 0%, that shall be applicable till the day preceding the day since an institution will be obliged to apply the rate indicated in the regulation of the Minister of Finance.

Minimum requirements for capital ratios imposed for banks for 2016 by the PFSA stood at 13.25% and 10.25% for total capital ratio and Common Equity Tier 1 ratio respectively, including conservation buffer for 2016.

Additionally, as a result of risk assessment carried out by the PFSA within the supervisory review and evaluation process, in particular with regard to evaluation of risk related to portfolio of foreign exchange retail mortgage loans, mBank on the consolidated level received an individual recommendation to maintain own funds to cover additional capital requirement of 3.72 pp in order to mitigate the risk (2.79 p.p. for Tier 1 capital). On individual basis those recommendations are 4.39 pp. at the level of own funds and 3.29 p.p. at the level of Tier 1 capital.

mBank comfortably meets the KNF's recommendations: its capital ratios on consolidated basis were above the target values, i.e. 16.97% at the level of own funds and 13.04% at the level of Tier 1 capital.

Respectively its capital ratios on individual basis were above the target values, i.e. 17.64% at the level of own funds and 13.54% at the level of Tier 1 capital.

As of June 30, 2016, the non-consolidated total capital ratio of mBank stood at 21.82% and the Common Equity Tier 1 ratio at 18.62%.

As of June 30, 2016, the consolidated total capital ratio of mBank Group stood at 18.33% and the Common Equity Tier 1 ratio at 15.61%.

The leverage ratio calculated in accordance with the CRR Regulation, including provisions regarding transitional period, amounted to 7.59%.

Stress tests

For meeting the regulatory requirement under normal and stress conditions The Group and the Bank carry out reverse stress tests, the goal of which is to identify events potentially leading to unviability of the Group and the Bank. These analysis are used for calculation of capital buffers for key risk concentration.

Additionally, there are conducted integrated stress tests 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, in a one-year horizon). The risk scenario, i.e., the most plausible (in at least a full two-year time horizon) 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 take part in regulatory stress tests conducted by the PFSA in order to determine the impact of assumed macroeconomic stress scenarios on the Group's balance sheet and P&L as well as on external supervisory norms.

3. Financial results and macroeconomic environment

3.1. Economy and banking sector in H1 2016

Polish economy slowed down slightly in H1 2016

In H1 2016 the Polish economy slowed down slightly as compared with the end of 2015. According to mBank's assessment based on GDP estimates for Q1 and higher frequency data from the following months, the Polish GDP grew by 3.2% YoY in H1 against 3.9% in the period from July to December 2015.

Contribution to GDP growth

Lower economic growth in the discussed period is not surprising. The decrease was primarily driven by a strong slowdown in investment, triggered by a considerable decrease in public investment in early 2016, which, in the Bank's opinion, stems from the fact that the funds from the previous EU financial framework have already been spent and the spending of funds from the new budget is delayed. It resembles the trend in investment observed in late 2012 and early 2013. The problem is especially acute in the case of local governments and railway companies with the former posting an almost 30% plunge in investment in Q1 alone (YoY). The data on the inflow of EU funds and tenders organised by local governments demonstrate that investments financed from the new EU budget are starting slowly and that the contribution of public investment to this year's growth will be negative. Coupled with a slight slowdown in private investment (due to rising uncertainty driven by internal and external factors), it becomes clear that investment demand will not be the driving force of the Polish economy in 2016.

In these circumstances, it is private consumption that has become the main driver of economic growth this year. As in the past, private consumption is helped by numerous factors, including: a high increase in real wages (the fastest since the outbreak of the financial crisis), first payments under the government's "Family 500+" child benefit programme, an exceptionally good household sentiment, a record-low unemployment rate, and an expansive monetary and fiscal policy. Hence it is not a surprise that consumption growth is accelerating gradually. In the Bank's opinion, it could even hit 3.5% in Q2. Such conclusions are supported by the data on retail sales and revenues of companies operating in the consumer sector. If nothing changes, consumption is likely to accelerate further in H2 2016 and in 2017.

Two years of deflation. A new, prudent MPC.

The first half of 2016 was again a time of deflation with consumer price index falling by an average of 0.9% YoY - a drop equal to the average figure in 2015. The structure of deflation changed slightly as compared with the previous year. It is no longer attributable to low food prices (the YoY change in this category is close to zero), the decrease in oil prices slowed down as well, but the counter-inflation trends in the remaining part of the consumer basket deepened. In H1 core inflation amounted to -0.2% YoY o(-0.4% in April and May) and was much below the 2015 average of 0.3%. In the Bank's opinion, it is core inflation that best reflects how permanent and deep the deflation in Poland is. In addition to external factors, it is driven by high competition among companies and a dynamic decrease in the expectations of

consumers and entrepreneurs. A slow increase in inflation should be expected in the months to come, but it will be mainly related to base effects, rather than a rising pay and price pressure in the economy.

Despite the deepening and prolonged deflation, the Monetary Policy Council (MPC) maintained a neutral bias on monetary policy - changes in the composition of the Council with Adam Glapiński replacing Marek Belka as the president of the National Bank of Poland did not have an impact on MPC's rhetoric. Repeated announcements of interest rate stabilisation in the following years toned down the expectations of the market with regard to monetary policy - a vast majority of analysts do not expect further softening of monetary policy, while the valuations on interest rate markets merely take certain risk of cuts into account. In the Bank's opinion, it is too early to assume that interest rate cuts are over. In an environment characterised by small growth and low interest rates, deteriorating growth prospects abroad could force the MPC to relax its monetary policy.

Turbulence on the financial markets

The recent months have been marked by turbulence and growing volatility on financial markets. The most important event was the British EU referendum, which, to the surprise of a vast majority of observers and analysts, ended with the victory of leave supporters. This caused a rapid increase in risk aversion and an over 10% decrease in the value of the pound (the Polish zloty was weakening for some time too). In the opinion of the Bank, the decision will have only minor consequences in the short term, but the ultimate benefits and costs are highly uncertain as it remains unknown how long it will take for the UK to leave the EU and what the results of the negotiations will be. The Brexit referendum was only the last of the numerous disturbances driven by the anxiety about global economic growth, weakness of European banks, changing expectations concerning U.S. monetary policy, S&P's decision to cut Poland's rating, and the uncertainty regarding the form and costs of the new law designed to help FX borrowers. As a consequence, H1 may be described as a period of increased volatility of all classes of Polish assets: at the beginning of 2016 and in late March and early April EUR 1 was worth PLN 4.22, but in mid-January and immediately after the British referendum the EUR/PLN exchange rate went up to 4.50; yields on Polish 10-year bonds were fluctuating between 2.80 and 3.30% (following the rating downgrade and again after the British referendum); the WIG20 index was going up and down by approx. 20%.

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

Despite fears, the changes in the regulatory and tax environment of the banking industry (including the imposition of the tax on assets of financial institutions) did not have a major impact on the volume of loans to the private sector: according to the Bank's calculations, the value of loans to businesses at the end of May this year was higher by 7.4% than in the same period last year (at the end of 2015 the increase in this segment amounted to 8.6%); loans to households increased by 4% YoY (as compared with a 4% decrease at the end of 2015).

The analysed period also saw an increase in the deposit base with the value of household and corporate deposits (data as at the end of May) rising by 10.8% and 13.2% YoY, respectively. Solid growth was also reported in the segment of local government institutions, non-monetary financial institutions and NGOs. The first half of the year was thus yet another period of decrease in the relation of loans to deposits in the banking sector.

Changes in recommendations of the Polish Financial Supervision Authority (PFSA) and other regulations concerning banks

Act on Tax on Certain Financial Institutions

On February 1, 2016 the Act on Tax on Certain Financial Institutions introducing the so-called bank tax entered into force. The new levy has been imposed on domestic banks, branches of foreign banks, branches of credit institutions, cooperative savings and credit unions, domestic insurance and reinsurance companies, branches and main branches of foreign insurance and reinsurance companies, and lending institutions. Monthly tax (0.0366% per month or 0.4400% per annum) is calculated at the end of every month on the basis of the value of total assets in excess of PLN 4 billion reduced by the value of own funds and Treasury securities.

Act on Macroprudential Supervision over the Financial System and Crisis Management in the Financial System

The Act entered into force on November 1, 2015, but its provisions on mandatory capital buffers (among them a security buffer of 1.25%) and restrictions on dividend payouts (MDA – Maximum Distributable Amount) took effect on January 1, 2016. Institutions' ability to pay out dividends and variable components of remuneration will be determined by the amount of own funds they hold. The Act introduces additional capital buffers described in CRD IV to Polish legal framework. It implements also provisions concerning corporate governance, disclosure framework and crisis management principles, establishing the BFG as a resolution authority in Poland equipped with the resolution tools (BRRD partial implementation). On June 8, 2016 PFSA published "Shortened description of methods of supervisory assessment during identification of other systemically important institutions" which will be the basis for imposition of O-SII buffer by the PFSA according to the competence introduced by the act.

Act on the Bank Guarantee Fund

On March 23, 2016 the Act of March 11 amending the Act on the Bank Guarantee Fund in the scope of, among others, banks' mandatory contributions to BFG entered into force. The one-off annual contribution payable on an annual basis has been replaced by quarterly payments. The amendment authorises banks to recognise the contributions as costs by spreading them over time on a pro rata basis.

A major amendment to the Act on Bank Guarantee Fund, Deposit Guarantee Scheme and Resolution was signed by the President on June 30, 2016. The purpose of the amendment is to transpose into Polish law Directive 2014/59/EU establishing a framework for recovery and resolution and Directive 2014/49/EU on deposit guarantee schemes. In particular, the amended Act authorised BFG to resolve financial institutions and obliged it to draw up individual resolution plans for every entity in cooperation therewith and to impose individual minimum requirements for own funds and eligible liabilities to be written down or converted MREL (the minimum requirement of own funds and eligible liabilities). Moreover, the PFSA was granted early intervention powers. Financial institutions were obliged to draw up their recovery plans individually

(within 3 months following the effective date of the Act) and to adjust their systems for the processing of information on guaranteed deposits (for example accounts maintained for investment firms).

Under the Act, the order of priority of claims under insolvency proceedings as well as the principles of raising funds by BFG have been modified. The funds raised by BFG so far will be allocated to two funds: a guarantee fund (the target level of 2.6% of guaranteed funds is expected to be reached by July 3, 2030) and a resolution fund (the target level is 1.2% of guaranteed funds, set for December 31, 2030). The target levels will be financed from contributions calculated based on banks' liabilities.

Act on Assistance to Home Loan Borrowers in a Difficult Financial Situation

The Act on Assistance to Borrowers in a Difficult Financial Situation entered into force on February 19, 2016. The borrowers meeting specific criteria can apply for interest-free support in repaying their housing loans until December 31, 2018. The monthly payment of up to PLN 1,500, covering principal and interest instalments, will be transferred by BGK directly to the account of the bank that granted the loan over a period of up to 18 months. The repayment of the support should be completed within 8 years and start 2 years after the last support instalment was paid.

The support will be paid from the Borrowers Assistance Fund with an initial value of PLN 600 million, financed by payments made by lenders proportionally to their share in the housing loans for households which are 90 days or more past due. If the value of the Fund falls below PLN 100 million, banks will be obliged to make additional payments in proportion to the amount of support already provided to the clients of a given lender in order to bring the value of the Fund back to the level of at least PLN 300 million.

KNF's Recommendation W on model risk management in banks

In 2015 the Polish Financial Supervision Authority (KNF) issued Recommendation W on model risk management in banks, setting the standards of model risk management process and the rules for building models and assessing the quality of their operation, while ensuring appropriate corporate governance solutions. The purpose of this recommendation is to define supervisory expectations as to effective model risk management process, in particular, to set the level of banks' tolerance to this risk type and to limit the exposure of the banking sector to model risk. Recommendation W has been in force since June 30, 2016. The Bank has already completed the relevant adaptation works which included, among others, an update of the Model Management Policy, which now provides for a classification of models and outlines the process of model risk assessment. The amended Policy was approved by the Management Board and the Supervisory Board of the Bank.

Amendments to KNF's Recommendation K concerning the principles of banks' maintenance of registers of security for covered bonds

KNF's resolution on Recommendation K entered into force on March 1, 2016. The Recommendation provides for qualitative guidelines with regard to registers of security for covered bonds. The aim of the amendments is to adjust the recommendation to the new legal environment created by the amendments to the Act on Covered Bonds and Mortgage Banks which became law on January 1, 2016. The Act should make the purchase of and trading in covered bonds more secure and thus indirectly facilitate the development of the Polish mortgage lending sector.

"Anti-usury Act" - Act on Amending the Act on Financial Market Supervision and Certain Other Acts

On March 11, 2016 the Act of August 5, 2015 providing customers with a higher level of protection against unfair provisions of contracts concluded with lenders entered into force. To accomplish this aim, the Act provides for a maximum amount of non-interest costs, i.e. total costs a customer must pay under a consumer credit agreement aside from interest. The maximum amount of such costs must not exceed the total amount of the loan. In addition, the Act has capped the amounts of fees and interest on overdue debt.

Restructuring Law

On January 1, 2016 the regulations stipulated in the Restructuring Law Act of May 15, 2015 took effect (except for the transitional provisions specified in the Act). The Act should facilitate effective restructuring of debtors and prevent them from being wound down by way of a composition with creditors or with the help of restructuring measures, as far as such are available. The Act provides also for a number of amendments to other regulations, including the Bankruptcy and Restructuring Law, by changing the classification of receivables that may be repaid with assets belonging to the bankruptcy estate.

Act on Capital Market Supervision

The provisions of the Act of June 12, 2015 on Amendments to the Act on Capital Market Supervision and Certain Other Acts entered into force on January 1, 2016, introducing changes to the system of financing the supervision. All entities operating on the capital market have been obliged to pay annual fees for the supervision. This has changed the size of charges that were earlier incurred only by selected market participants.

Recommendation C

On May 24, 2016 KNF amended Recommendation C on concentration risk management, which will enter into force on January 1, 2017. The Recommendation sets out the principles of identification, measurement, monitoring and mitigation of concentration risk. All these processes should be covered by the internal control system, including interdependencies between exposures to one or several risks.

Act on Amendments to the Act on Investment Funds and Certain Other Acts

On June 4, 2016 the Act on Amendments to the Act on Investment Funds of March 31, 2016 entered into force. The main changes affecting banks acting as depositories of investment funds include the assumption of responsibility for correct calculation of the net value of assets of an investment fund and the obligation to ensure that the duties of a fund are performed in compliance with the law and the fund's statute.

Regulation of the Minister of Finance of March 21, 2016 on time limits for making, amounts of and method of calculating the payments covering the costs of operation of the Financial Ombudsman and his Office, as amended by the regulation of the Minister of Finance of April 21, 2016

The regulation issued based on the Act on Handling Complaints by Financial Market Entities and on the Financial Ombudsman of August 5, 2015 set out precise time limits for making, amounts of and method of calculating the payments due from individual institutions to cover the costs of operation of the Financial Ombudsman and his office.

Moreover, legislative works on a number of other regulatory proposals which will materially affect the functioning of banks are underway. The proposals include amendments to the Act on the Bank Guarantee Fund, Deposit Guarantee Scheme and Resolution which aims at transposing Directive EU 2014/59 establishing a framework for recovery and resolution and Directive EU 2014/49 on deposit guarantee schemes, as well as the bill on the manners of restoring the equality of parties to certain credit agreements regarding FX denominated and indexed loans.

Challenges for the banking industry in the coming quarters

In the coming quarters the performance of the banking sector will be determined by a range of various factors.

Stable macroeconomic environment

The relatively high economic growth rate will be helped by growing internal demand, triggered by the positive impact of the Family 500+ programme on consumption. Towards the end of the year there may be a rise in investments (both public and corporate), driven in particular by higher absorption of EU funds. The labour market improvement, lower unemployment rate and higher salaries, coupled with historically low interest rates, as well as good financial standing of companies and low prices of raw materials will positively affect the demand for loans and the quality of credit portfolio. On the other hand, risk factors include fears of a deepening slowdown in emerging economies (especially in China) and anxiety about future economic growth in the euro zone (strengthened by the uncertain influence of "Brexit") and in the

USA. If negative scenarios materialise, the adverse impact on the Polish economy would occur via the trade channel and would result from weakening corporate and consumer confidence.

Risk of Poland's rating cut

According to S&P and Moody's the outlook on Poland's credit rating is negative. A potential rating downgrade would bring about a rise in the banks' funding costs, deterioration of the investment climate, depreciation of the zloty and an increase in the PLN value of the credit portfolio. Furthermore, fiscal policy of the government aimed to secure enough revenues to cover growing expenditures may lead to excessive tax burdens, and consequently, negatively impact the dynamics of economic growth.

Low market interest rates

In the last few months the expectations of interest rate cuts in Poland weakened clearly; however, one cannot rule out further interest rate cuts, if symptoms of an economic slowdown occur. Moreover, a hypothetical reduction in interest rates would adversely affect banks' interest margins and net interest income.

Growing capital requirements for banks

Pursuant to Capital Requirements Directive IV (CRD IV) banks are or may be required to maintain additional capital buffers, i.e. a capital conservation buffer, a countercyclical capital buffer, a buffer relating to global systemically important institutions, a buffer relating to other systemically important institutions and a systemic risk buffer, which together constitute the combined buffer requirement. The capital necessary to cover the requirements on account of individual buffers must qualify as Common Equity Tier 1 and at the same time it cannot be the capital maintained to meet the minimum regulatory requirements arising from Article 92 of Regulation (EU) No. 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms (Capital Requirements Regulation - CRR). So far Poland has introduced the countercyclical capital buffer (initially set at 0%), while the capital conservation buffer has been introduced gradually (1.25% in 2016-2017, 1.875% in 2018 and 2.5% from 2019). Therefore, banks must be aware of the risk of being required to hold additional capital buffers under CRD IV. Moreover, in 2015 the Polish Financial Supervision Authority imposed capital add-ons on banks having considerable portfolios of mortgage-backed FX loans to households to cover the risk posed by these portfolios. High capital requirements coupled with other charges imposed on banks may reduce their ability and willingness to further expand lending activity.

Proposed solutions to the FX mortgage loans problem

On January 15, 2016 the President's Office published its draft bill on restructuring of FX mortgage loans, proposing the conversion of Swiss franc denominated mortgage loans held by individuals into PLN and ways of compensating borrowers for excessive FX spreads. The proposal includes three mechanisms of loan restructuring. The first two solutions are based on conversion of FX mortgage loan at "fair" rate of exchange, which is calculated by comparison of FX rate at origination, corrected by the accumulated difference in servicing costs of FX mortgage loan in comparison to a similar PLN denominated mortgage loan. The third solution is a transfer of the property to the bank, and release of the debtor from the debt, if the conversion would not have taken place. According to the National Bank of Poland the likely cost of the Presidential proposal for the banking sector would reach PLN 44 billion, including PLN 35 billion on application of adjusted FX rates for repayment and PLN 9 billion on refund of spreads. The Polish Financial Supervision Authority among banks estimated (based on a survey) that Polish banks could take PLN 66.9 billion hit on their 2016 results from the presidential bill on FX restructuring under the most probable scenario. It would threaten the stability of some banks and lead to a loss of trust in the banking system. Therefore the Polish President's Office appointed a team of experts to amend the proposal.

On June 6, 2016 the team of experts created by the President's Office proposed their solutions of the FX denominated mortgage loans issue. The scenarios presented by the presidential experts included, in addition to the previous proposal of the President's Office, new versions of the „fair" exchange rate used to the potential conversion of the loans. The President's Office is currently working on the final solution.

If introduced, forced restructuring of FX mortgage loans could lead to a material deterioration of banks' financial results, weakening of the capital base and to other adverse financial consequences for the banking sector.

Banking tax

The banking tax introduced in February 2016 adds to the pressure on banks' results. According to the International Monetary Fund (IMF), a negative impact of tax on bank assets is reflected not only in deteriorated profitability of the banking sector, but it will also reduce lending by 3-4 percentage points in relation to a no-tax scenario.

NBP data on loans to customers for June 2016 confirms a slowdown in lending. In addition, the Polish Financial Supervision Commission concluded that the introduction of banking tax besides the impact on banks' profitability entailed changes in balance-sheet management and management of subsidiaries. Some banks intend to continue reductions of their cost of deposits, focus on high-margin products and optimize branch network.

Currently the Ministry of Finance is analysing the data on banking tax operation, which may lead to some adjustments in the construction of the banking tax.

Risk of additional financial charges

It cannot be ruled out that the obligatory charges paid by banks, in particular on account of bankruptcies of cooperative banks and credit unions, will be raised.

In the past two years the financial situation both in credit unions and in cooperative banks deteriorated. In 2015, credit unions recorded a net loss in the amount exceeding PLN 100 million and their capital adequacy ratio, after the adjustments of the inspection of the Polish Financial Supervision Authority, would have been negative. In 2016, the operations of some SKOKs were suspended and two credit unions were taken over by one of the domestic banks. Also, a number of cooperative banks, having a surplus of deposits over loans of the financial sector, have difficulty in maintaining profitability in the environment of low interest rates. In 2015 the bankruptcy of the largest cooperative bank (SK Bank) forced banks to make additional contributions to the Bank Guarantee Fund (BFG) of more than PLN 2 billion.

3.2. Financial results of mBank Group in H1 2016

All dynamics presented in the analysis of financial results were calculated on the basis of the Consolidated Financial Statement for 1H 2016 (in PLN thousand).

Profit and Loss Account

Profit before tax generated by mBank Group in H1 2016 stood at PLN 907.8 million, up from PLN 857.2 million in H1 2015 (+PLN 50.6 million or 5.9%). Net profit attributable to the owners of mBank amounted to PLN 696.3 million as compared to PLN 672.3 million in the same period last year (+PLN 24.0 million or 3.6%).

The key drivers of mBank's profit in H1 2016 included:

- **Total income growing** by 10.4% against H1 2015, mainly due to higher net interest income and the booking of proceeds from the takeover of Visa Europe Limited by Visa Inc.;
- **Increase in operating expenses** (including amortisation) by 3.8% vs. H1 2015 attributable to higher amortisation and growing staff-related expenses driven by the rising number of employees;
- **Decrease in impairment losses on loans and advances** by 10.3% attributable to high quality of credit portfolio, prudent risk policy pursued in the previous periods and improving economic conditions;
- **Increase of taxes on the Group balance sheet items** to PLN 146.3 million from PLN 1.8 million in H1 2015;
- **Continued organic growth and business expansion** as demonstrated by:
  - Retail client base in Poland, the Czech Republic and Slovakia growing to 5,146 thousand (+199 thousand clients year to date);
  - Increase of the number of corporate clients to 20,220 (+1,566 year on year and +658 year to date).

Gross loans and advances increased by 3.0% in H1 2016 (or 2.5% net of reverse repo transactions and FX effects) as compared to December 31, 2015 and by 4.5% vs. the end of June 2015 (or 3.9% net of reverse repo transactions and FX effects). Deposits grew by 5.1% (or 5.0% net of repo transactions) and 16.8% (or 16.6% net of repo transactions), respectively. Consequently, the loan-to-deposit ratio fell to 94.7% from 96.7% at the end of 2015 and 105.7% as at June 30, 2015.

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

- Gross ROE of 14.9% (15.7% at the end of H1 2015).
- Net ROE of 11.5% (12.3% at the end of H1 2015).

Increased own funds brought an improvement in the capital ratios of mBank Group. Total Capital Ratio as at June 30, 2016 amounted to 18.3% against 17.3% at the end of 2015 and 16.4% at the end of June 2015. Common Equity Tier 1 capital ratio reached 15.6% compared to 14.3% at the end of 2015 and 13.5% as of June 30, 2015.

Contribution of business lines and segments to the financial results

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

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Retail Banking	621.5	592.7	-28.8	-4.6%
Corporate and Investment Banking	237.2	242.5	5.3	2.2%
Financial Markets	1.8	61.1	59.3	3294.4%
Other	-3.3	11.5	14.8	-/+
Profit before tax of mBank Group	**857.2**	**907.8**	**50.6**	**5.9%**

Retail Banking was the major contributor to the profit before tax of the Group (65.3%) in H1 2016. The profit earned by the Corporate and Investment Banking and Financial Markets accounted for 26.7% and 1.3% of the Group's total profit before tax respectively.

Income of mBank Group

Total income generated by mBank Group reached PLN 2,211.9 million in H1 2016, compared to PLN 2,003.0 million a year before, representing an increase of PLN 208.9 million, or 10.4%. The increase in income was driven by a considerably higher net interest income and the booking of the gains on the takeover of Visa Europe Limited by Visa Inc. (whereas in H1 2015 mBank Group posted the gains on the sale of BRE Ubezpieczenia TUiR to AXA Group and the execution of agreements related to this transaction). At the same time, net fee and commission income dropped slightly, mainly due to lower net commission income on brokerage activity.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Interest income	1,781.2	1,892.5	111.3	6.3%
Interest expense	-588.2	-531.7	56.5	-9.6%
Net interest income	**1,193.0**	**1,360.8**	**167.8**	**14.1%**
Fee and commission income	680.0	717.2	37.2	5.5%
Fee and commission expense	-255.8	-295.7	-39.9	15.6%
Net fee and commission income	**424.2**	**421.4**	**-2.8**	**-0.6%**
Dividend income	3.2	2.6	-0.6	-18.9%
Net trading income	137.9	143.6	5.7	4.1%
Gains less losses from investment securities, investments in subsidiaries and associates	196.4	248.2	51.8	26.4%
Other operating income	134.3	149.2	14.9	11.1%
Other operating expenses	-86.0	-113.9	-27.9	32.4%
Total income	**2,003.0**	**2,211.9**	**208.9**	**10.4%**

Net interest income remained mBank Group's largest source of income in H1 2016 (61.5% of total income). It stood at PLN 1,360.8 million, compared with PLN 1,193.0 million in H1 2015, up by PLN 167.8 million or 14.1%. Despite low interest rates, an increase in interest income coupled with lower interest expense was posted.

Interest income increased by PLN 111.3 million or 6.3% year on year in H1 2016 and stood at PLN 1,892.5 million. Income on loans and advances to customers, with a share of 70.5%, remained the main source of interest income, and stood at PLN 1,334.6 million, up by PLN 66.3 million or 5.2% year on year. It was driven by rising credit volumes and shifts in the structure of assets towards higher-margin products, especially non-mortgage loans. The discussed period also saw an increase in income from derivative instruments classified into the banking book - up by PLN 53.9 million or 102.2% against H1 2015. It was attributable to an increase in the volume of these instruments caused by changes in the funding structure of mBank Group. At the same time, interest income from investment securities fell by PLN 28.9 million or 7.6%, which was caused by their lower profitability.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Loans and advances including the unwind of the impairment provision discount	1,268.3	1,334.6	66.3	5.2%
Investment securities	382.8	353.9	-28.9	-7.6%
Cash and short-term placements	26.5	26.4	-0.1	-0.1%
Trading debt securities	20.8	32.9	12.1	57.7%
Interest income on derivatives classified into banking book	52.8	106.7	53.9	102.2%
Interest income on derivatives concluded under the fair value hedge	21.4	28.2	6.8	31.9%
Interest income on derivatives concluded under the cash flow hedge	6.2	7.9	1.7	27.5%
Other	2.3	1.9	-0.4	-20.0%
Total interest income	**1,781.2**	**1,892.5**	**111.3**	**6.3%**

Interest expenses decreased by PLN 56.5 million or 9.6% year on year in H1 2016. A further decrease in interest expenses paid to customers caused by lower average interest on deposits was observed - down by PLN 7.1 million or 2.1%. It was coupled with an increase in the volume of deposits. Interest expenses on issued debt securities declined by PLN 20.4 million or 14.9% due to a smaller volume of such securities (redemption of an EMTN tranche in the amount of EUR 500 million in October 2015). Interest expenses paid to banks decreased by PLN 17.8 million or 32.0%, which was attributable to a lower volume of liabilities to other banks (repayment of loans with Commerzbank in the amount of CHF 850 million). At the same time, interest expenses on subordinated debt decreased by PLN 10.8 million or 24.3% thanks to a fall of market interest rates in Q1 2015.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Paid to banks	-55.6	-37.8	17.8	-32.0%
Paid to customers	-345.1	-338.0	7.1	-2.1%
Issued debt securities	-137.6	-117.2	20.4	-14.9%
Subordinated liabilities	-44.5	-33.7	10.8	-24.3%
Other	-5.2	-4.9	0.3	-5.6%
Total interest expenses	**-588.2**	**-531.7**	**56.5**	**-9.6%**

Net interest margin rose to 2.27% in H1 2016 from 2.08% a year before.

Net commission income amounted to PLN 421.4 million in H1 2016, down by PLN 2.8 million or 0.6% year on year. The decrease in net commission income was mainly attributable to lower commissions from brokerage activity.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Payment cards-related fees	160.1	168.7	8.6	5.4%
Credit-related fees and commissions	131.7	138.4	6.7	5.1%
Commissions from insurance activity	66.2	78.1	11.9	17.9%
Fees from brokerage activity	63.8	58.0	-5.8	-9.0%
Commissions from bank accounts	82.2	84.5	2.3	2.8%
Commissions from money transfers	51.0	53.9	2.9	5.7%
Commissions due to guarantees granted and trade finance commissions	23.7	28.6	4.9	20.7%
Commissions for agency service regarding sale of products of external financial entities	54.0	51.3	-2.7	-5.1%
Commissions on trust and fiduciary activities	11.5	12.6	1.1	9.0%
Fees from portfolio management services and other management-related fees	7.6	5.7	-1.9	-24.6%
Fees from cash management	18.7	23.4	4.7	25.2%
Other	9.5	14.1	4.6	47.7%
Total fee and commission income	**680.0**	**717.2**	**37.2**	**5.5%**

Commission income increased by PLN 37.2 million or 5.5% year on year. Payment card-related fees, which make the biggest contribution to commission income, increased by PLN 8.6 million or 5.4% year on year in the period under review due to an increase in the volume and value of non-cash transactions.

Credit related fees and commissions increased by 5.1% year on year mainly as a result of higher sales of retail non-mortgage loans.

Commissions for agency service regarding sale of insurance products of external financial entities rose by 17.9% year on year, which confirms the positive results of cooperation with AXA Group, particularly in the areas of leasing and stand-alone products.

The increase in the customer base, the expansion of transactional banking and the increased transactional activity of clients improved commissions on money transfers, which increased by 5.7% and commissions on bank accounts, which grew by 2.8%.

A decrease of 9.0% was reported in commission income from brokerage activity and debt securities issuance. It was attributable to a lower number of IPOs organised by Dom Maklerski mBanku and lower activity of investors on the Warsaw Stock Exchange.

Fee and commission expenses increased by PLN 39.9 million or 15.6% year on year in H1 2016. The increase was mainly driven by payment card-related costs (+PLN 12.6 million) and cash service expenses (+PLN 8.6 million).

Dividend income in H1 2016 amounted to PLN 2.6 million compared to PLN 3.2 million a year before. Similar to H1 2015, the income booked in H1 2016 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 143.6 million in H1 2016 and was higher by PLN 5.7 million (+4.1%) compared to the previous year. The increase was driven by higher net other trading income and result on hedge accounting (+PLN 12.5 million), while foreign exchange result fell by PLN 6.8 million.

Gains less losses on investment securities and investments in subsidiaries and associates stood at PLN 248.2 million in H1 2016 compared to PLN 196.4 million in H1 2015. In H1 2016 mBank Group

booked the result on the takeover of Visa Europe Limited by Visa Inc. in the amount of PLN 251.7 million, including the cash amount received in June 2016, the deferred payment falling due in 2019 and the valuation of preferred shares. Moreover, the Bank booked a charge on one of the companies from the portfolio of investments held for sale in the amount of -PLN 7.7 million. In H1 2015 mBank Group recognised gains on the sale of BRE Ubezpieczenia TUiR and the execution of sales-related agreements with AXA Group subsidiaries worth PLN 194.3 million. More on the takeover of Visa in Consolidated Financial Statement of mBank Group for 1H 2016, Selected explanatory information, point 4.

Net other operating income (other operating income net of other operating expenses) stood at PLN 35.3 million compared to PLN 48.3 million in H1 2015 (PLN -13.0 million or -27.0% year on year). The drop results from the lack of income from insurance activity, arising from attribution of premiums in 2016, as a result of a shift in the structure of income from insurance activities that occurred following the disposal of BRE Ubezpieczenia TUiR in H1 2015. In H1 2015 the figure stood at PLN 23.9 million. At the same time, in H1 2016 net income from the sales of apartments by mLocum rose on a year-on-year basis (+PLN 6.0 million or +28.9%).

Net impairment losses on loans and advances

Net impairment losses on loans and advances in mBank Group amounted to PLN 186.3 million in H1 2016 compared with PLN 207.6 million a year before, which represents a decrease by PLN 21.3 million or 10.3%.

PLN M	H1 2015	H1 2016	Change in PLN m	Change in %
Retail Banking	116.4	140.3	23.9	20.5%
Corporates and Financial Markets	85.2	47.0	-38.2	-44.8%
Other	6.0	-1.0	-7.0	+/-
Total net impairment losses on loans and advances	**207.6**	**186.3**	**-21.3**	**-10.3%**

Net impairment losses on loans and advances in the Retail Banking segment grew by PLN 18.0 million in H1 2016 compared to H1 2015, mainly as a result of a change in the structure of the retail loans portfolio with the rising share of unsecured loans.

Net impairment losses on loans and advances in the Corporates and Financial Markets segment declined by PLN 38.2 million in H1 2016. Lower loan loss provisions were posted mainly in K3 segment and in the following subsidiaries: mBank Hipoteczny, mFaktoring and mLeasing. This highlights a continued improvement in the quality of the corporate loans portfolio, driven by positive changes in the macroeconomic environment supporting the financial standing of corporate clients.

Costs of mBank Group

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

Total overhead costs of mBank Group (including amortisation) stood at PLN 971.5 million in H1 2016, representing an increase by PLN 35.1 million, i.e. 3.8% year on year.

PLN M	H1 2015	H1 2016	Change in PLN M	Change in %
Staff-related expenses	427.2	436.8	9.6	2.2%
Material costs, including:	322.3	319.7	-2.6	-0.8%
- logistic costs	168.3	168.8	0.5	0.3%
- IT costs	60.5	66.1	5.6	9.1%
- marketing costs	60.1	57.4	-2.7	-4.5%
- consulting services costs	27.7	22.9	-4.8	-17.2%
- other material costs	5.6	4.5	-1.1	-20.6%
Taxes and fees	18.9	20.1	1.2	6.7%
Contributions and transfer to the Bank Guarantee Fund	68.2	74.2	6.0	8.7%
Contributions to the Social Benefits Fund	3.5	3.6	0.1	4.1%
Amortisation	96.3	117.1	20.8	21.6%
Total overhead costs and amortisation	**936.4**	**971.5**	**35.1**	**3.8%**
Cost / Income ratio	46.7%	43.9%	-	-
Employment (FTE)	6,446	6,529	83	1.0%

Staff-related expenses increased by PLN 9.6 million, i.e 2.2% year on year. The increase in wages and salaries was driven by rising employment in mBank Group. The number of FTEs grew from 6,446 at the end of June 2015 to 6,529 at the end of June 2016 (+83 FTEs).

Material costs dropped slightly by PLN 2.6 million, i.e. 0.8% in the period under review. In H1 2016 mBank Group reported lower costs of consulting services and marketing.

Amortisation rose by PLN 20.8 million or 21.6% year on year, i.a. due to an earlier write-off of unused IT system functionalities.

A slight increase in contributions to the Bank Guarantee Fund from PLN 68.2 million in H1 2015 to PLN 74.2 million in H1 2016 resulted from an increase in the annual levy from 0.239% to 0.246% of risk-weighted assets.

Changes in the income and costs of mBank Group resulted in a lower cost/income ratio (43.9% in H1 2016 against 46.8% a year before). Excluding the one-off income from the takeover of Visa Europe Limited by Visa Inc., the ratio stood at 49.6%.

Changes in the consolidated financial statement of financial position

Changes in the assets of mBank Group

In H1 2016, the assets of mBank Group rose by PLN 5,210.5 million or 4.2%. As at June 30, 2016, the assets amounted to PLN 128,733.5 million.

The table below presents changes in particular items of mBank Group assets.

PLN M	30.06.2015	31.12.2015	30.06.2016	YtD change	YoY change
Cash and balances with the Central Bank	3,187.5	5,938.1	6,433.2	8.3%	101.8%
Loans and advances to banks	2,072.0	1,897.3	1,680.8	-11.4%	-18.9%
Trading securities	2,597.3	557.5	3,233.2	479.9%	24.5%
Derivative financial instruments	3,345.9	3,349.3	2,411.5	-28.0%	-27.9%
Net loans and advances to customers	77,241.6	78,433.5	80,774.8	3.0%	4.6%
Investment securities	29,515.8	30,736.9	31,644.3	3.0%	7.2%
Intangible assets	469.9	519.0	503.6	-3.0%	7.2%
Tangible assets	691.8	744.5	722.8	-2.9%	4.5%
Other assets	1,482.3	1,346.6	1,329.3	-1.3%	-10.3%
Total assets	**120,604.1**	**123,523.0**	**128,733.5**	**4.2%**	**6.7%**

Loans and advances to customers retained the largest share in the balance sheet of mBank Group at the end of H1 2016. The net volume of loans and advances to customers increased by PLN 2,341.3 million or 3.0% compared with the end of 2015. As at June 30, 2016 they accounted for 62.7% of the balance sheet total compared with 63.5% at the end of 2015.

PLN M	30.06.2015	31.12.2015	30.06.2016	YtD change in PLN M	YtD change in %
Loans and advances to individuals	45,328.7	46,258.7	48,272.2	2,013.5	4.4%
Loans and advances to corporate entities	32,226.5	33,446.6	33,936.9	490.3	1.5%
Loans and advances to public sector	1,661.5	1,520.7	1,357.0	-163.7	-10.8%
Other receivables	1 043.9	183.4	296.1	112.7	61,5%
Total (gross) loans and advances to customers	**80,260.6**	**81,409.4**	**83,862.2**	**2,452.8**	**3.0%**
Provisions for loans and advances to customers (negative amount)	-3,019.0	-2,975.9	-3,087.4	-111.5	3.7%
Total (net) loans and advances to customers	**77,241.6**	**78,433.5**	**80,774.8**	**2,341.3**	**3.0%**

In H1 2016 gross loans and advances to individuals rose by PLN 2,013.5 million or 4.4%. The value of mortgage and housing loans increased by PLN 1,036.0 million or 3.0%. It was mainly due to the new sales which reached PLN 1,482.5 million in H1 2016 against PLN 1,864.6 in H1 2015, depreciation of the zloty against the Swiss franc and systematic repayments of mortgage loans. At the same time, in H1 2016 mBank Group sold PLN 3,052.9 million worth of non-mortgage loans, which represents a 24.2% hike as compared with H1 2015. Net of the FX effect, loans and advances to individuals grew by 2.4% in H1 2016.

The volume of gross loans and advances to corporate clients grew by PLN 490.3 million or 1.5% in H1 2016 against the end of 2015. Excluding reverse repo/buy sell back transactions and the FX effect, the value of loans to corporate clients increased by 2.9% in the last six months.

The volume of gross loans and advances to public sector decreased by PLN 163.7 million or 10.8% in H1 2016.

Investment securities constituted mBank Group's second largest asset category (24.6% of total assets). In H1 2016, their value increased by PLN 907.4 million or 3.0%. The portfolio of treasury bonds and bills increased by 29.5% year to date while the portfolio of debt instruments issued by the central bank decreased by 77.8%.

The balance of trading securities went up by PLN 2,675.7 million in H1 2016 as a result of extending the treasury bonds portfolio.

Changes in the liabilities and equity of mBank Group

The table below presents changes in the liabilities and equity of mBank Group in H1 2016:

PLN M	30.06.2015	31.12.2015	30.06.2016	YtD change	YoY change
Amounts due to other banks	15,675.9	12,019.3	12,058.2	0.3%	-23.1%
Derivative financial instruments	3,302.2	3,173.6	2,157.2	-32.0%	-34.7%
Amounts due to clients	73,058.3	81,140.9	85,302.3	5.1%	16.8%
Debt securities in issue	11,013.9	8,946.2	10,115.5	13.1%	-8.2%
Subordinated liabilities	3,896.6	3,827.3	3,910.5	2.2%	0.4%
Other liabilities	2,109.7	2,140.7	2,392.8	11.8%	13.4%
Total liabilities	**109,056.6**	**111,248.0**	**115,936.5**	**4.2%**	**6.3%**
Total equity	**11,547.5**	**12,275.0**	**12,797.0**	**4.3%**	**10.8%**
Total Liabilities and Equity of mBank Group	**120,604.1**	**123,523.0**	**128,733.5**	**4.2%**	**6.7%**

Amounts due to customers remained the principal source of funding of mBank Group. Their share in the Group's funding structure has been increasing systematically. As at the end of June 2016 they accounted for 66.3% of Group's total liabilities and equity as compared with 65.7% at the end of 2015 and 60.6% at the end of June 2015.

PLN M	30.06.2015	31.12.2015	30.06.2016	YtD change in PLN M	YtD change in %
Individual customers	41,411.3	46,117.1	49,452.5	3,335.4	7.2%
Corporate customers	29,661.2	34,423.9	35,119.1	695.2	2.0%
Public sector customers	1,985.8	599.9	730.6	130.7	21.8%
Total amounts due to customers	**73,058.3**	**81,140.9**	**85,302.3**	**4,161.4**	**5.1%**

Amounts due to customers increased by PLN 4,161.4 million or 5.1% in H1 2016, to PLN 85,302.3 million.

The increase was observed mainly in amounts due to individuals which rose by PLN 3,335.4 million or 7.2% against the end of 2015. The volume of customers' deposits in current accounts increased by 8.0%, while term deposits went up by 5.5%.

Amounts due to corporate clients increased by PLN 695.2 million or 2.0% in H1 2016, driven mainly by increased balances of current accounts (+5.2%), loans and advances received (+15.8%) and repo/buy sell back transactions (+17.7%). Excluding repo transactions, amounts due to corporate clients rose by 1.5% compared with the end of 2015.

Amounts due to other banks grew by PLN 38.9 million or 0.3% to PLN 12,058.2 million compared with the end of last year. A rise was observed in loans and advances received. In H1 2016 mBank took out a loan in the amount of EUR 130 million and repaid one loan amounting to EUR 20 million. On the other hand, the value of deposits placed by other banks with mBank, term deposits and repo transactions declined.

The share of debt securities in issue in the funding structure of mBank Group grew from 7.2% at the end of 2015 to 7.9% at the end of June 2016. Their value increased by PLN 1,169.3 million or 13.1% year to date, which is attributable mainly to the issuance of covered bonds by mBank Hipoteczny worth PLN 450 million and EUR 50 million and depreciation of the zloty against the euro and the Swiss franc.

Subordinated liabilities rose by 2.2% in H1 2016, driven mainly by changes in the Swiss franc/zloty exchange rate, as the subordinated liabilities to Commerzbank are denominated in the Swiss franc.

In H1 2016 equity grew by PLN 522.0 million or 4.3% as a result of an increase in retained profits, while its share in total liabilities and equity of mBank Group accounted for 9.9% at the end of H1 2016, which is the same as the figure reported as at December 31, 2015.

Performance indicators

The table below presents mBank Group's key performance indicators:

	H1 2015	H1 2016
ROA net	1.1%	1.1%
ROE gross	15.7%	14.9%
ROE net	12.3%	11.5%
C/I ratio	46.7%	43.9%
Net Interest Margin	2.1%	2.3%
Common Equity Tier 1 Capital Ratio	13.5%	15.6%
Total Capital Ratio	16.4%	18.3%

ROA net: Net profit attributable to owners of the Bank / Average total assets

ROE gross: Profit before income tax / Average total equity net of the year's result

ROE net: Net profit attributable to owners of the Bank / Average total equity net of the year's result

C/I ratio – Cost to Income; calculated as: (overhead costs + amortisation) / total income (including net other operating income/costs)

Net interest margin: Net interest income / Average interest earning assets

Tier 1 Capital Ratio (CET1 ratio): Tier 1 Capital expressed as a percentage of the Total Risk Exposure Amount (TREA)

Total Capital Ratio (TCR): Own funds expressed as a percentage of the Total Risk Exposure Amount (TREA)

The decrease of gross and net return on equity in H1 2016 compared to H1 2015 despite an increase of the profit before tax and the net profit of the Group was due to an increase of the Group's average equity, which increased by 10.7% year on year. Return on assets remained stable, while average assets increased by 2.3% compared to the end of June 2015. The capital ratios increased mainly as a result of the inclusion of the Group's 2015 net profit and a part of the Group's Q1/2016 net profit into Tier 1 capital.

Financial results of mBank Group in Q2 2016

In Q2 2016, mBank Group generated a profit before income tax of PLN 505.5 million compared to PLN 402.3 million in Q1 2016. Net profit attributable to the owners of mBank reached PLN 388.5 million, up from PLN 307.8 million in Q1 2016.

PLN M	Q2 2015	Q1 2016	Q2 2016	QoQ	YoY
Interest income	868.9	945.5	947.1	0.2%	9.0%
Interest expense	-263.3	-269.1	-262.6	-2.4%	-0.3%
Net interest income	**605.5**	**676.4**	**684.4**	**1.2%**	**13.0%**
Fee and commission income	365.5	351.9	365.3	3.8%	-0.1%
Fee and commission expense	-135.2	-140.2	-155.6	11.0%	15.1%
Net fee and commission income	**230.3**	**211.7**	**209.7**	**-1.0%**	**-9.0%**
Dividend income	3.2	0.0	2.6	-	-18.1%
Net trading income	35.3	84.1	59.5	-29.2%	68.5%
Gains less losses from investment securities, investments in subsidiaries and associates	1.3	3.4	244.8	7042.0%	18138.1%
The share in profits (losses) of investments in joint ventures	0.0	0.0	0.0	+20.0%	220.0%
Other operating income	45.6	94.1	55.1	-41.5%	20.7%
Other operating expenses	-36.5	-60.8	-53.0	-12.8%	45.4%
Total income	**884.8**	**1 008.9**	**1 203.0**	**19.2%**	**36.0%**
Net impairment losses on loans and advances	-107.7	-68.5	-117.7	71.8%	9.4%
Overhead costs and amortization	-484.4	-480.8	-490.7	2.1%	1.3%
Taxes on bank balance sheet items	-0.9	-57.3	-89.0	55.3%	9923.8%
Profit before income tax	**291.9**	**402.3**	**505.5**	**25.7%**	**73.2%**
Income tax expense	-70.2	-92.8	-116.3	25.4%	65.8%
Net profit attributable to:	**221.7**	**309.5**	**389.2**	**25.7%**	**75.5%**
- Owners of mBank S.A.	**221.3**	**307.8**	**388.5**	**26.2%**	**75.5%**
- Non-controlling interests	0.4	1.7	0.7	-59.9%	79.0%
ROA net (YtD)	1.1%	1.0%	1.1%		
ROE gross (YtD)	15.7%	13.2%	14.9%		
ROE net (YtD)	12.3%	10.1%	11.5%		
Cost / Income ratio (YtD)	46.7%	47.7%	43.9%		
Net interest margin (YtD)	2.1%	2.3%	2.3%		
Common Equity Tier 1 ratio	13.5%	16.2%	15.6%		
Total Capital Ratio	16.4%	19.0%	18.3%		

The main drivers of mBank Group's financial results in Q2 2016 included:

- **A one-off income** from the booking of the gains on the takeover of Visa Limited by Visa Inc. in the amount of PLN 251.7 million;
- **Increase in net interest income** by PLN 8.0 million or 1.2% driven mainly by a 2.4% decrease in interest expense;
- **Decrease in net fee and commission income** by PLN 2.0 million or 1.0% resulting predominantly from lower commissions on payment cards;
- **Decrease in net trading income** by PLN 24.6 million or 29.2% vs. the previous quarter, driven mainly by weaker other trading income affected by negative valuation of interest rate derivatives;
- **Increase in overhead costs (including amortisation)** by PLN 9.9 million or 2.1% mainly resulting from a write-off of unused IT system functionalities;
- **Increase in loan loss provisions** (by PLN 49.2 million) driven by a rise in provisions in the Corporates and Financial Markets segment, which stood at PLN 43.6 million vs. PLN 3.7 million in the previous quarter. In the analysed period, net impairment losses on loans and advances in the Retail Banking segment rose to PLN 75.6 million from PLN 64.7 million in Q1;
- **Increase of taxes on the Group balance sheet items** to PLN 89.0 million from PLN 57.3 million in Q1 2016 (by PLN 31.7 million or 55.3%).

The balance sheet total of mBank Group stood at PLN 128,733.5 million as at June 30, 2016 compared with PLN 123,268.4 million at the end of March 2016.

Net loans and advances to clients increased by PLN 2,834.0 million in Q2 2016. Higher volume of loans was reported in both the retail clients segment (+PLN 1,761.2 billion or 3.8%) and the corporate clients segment (+PLN 1,131.5 million or 3.4%; net of the impact of reverse repo / buy sell back transactions, loans and advances to corporate entities rose by ca. 3.1% in the analysed period). Gross loans and advances to individuals net of the impact of FX changes went up by ca. 1.5%. In Q2 2016, mBank Group sold PLN 764.4 million worth of mortgage loans and PLN 1,714.5 million worth of non-mortgage loans.

At the same time, amounts due to customers grew by PLN 4,168.4 million or 5.1% in the analysed period; in the corporate clients segment the rise amounted to 7.7%; however, excluding the impact of repo transactions, amounts due to corporate clients went up by 6.5%. The upward trend in amounts due to individuals continued and the quarterly rise stood at 3.4%.

4. 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 2016 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 2016 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 2016 and IFRS Condensed Stand-alone Financial Statements of mBank S.A. for the first half of 2016 – PricewaterhouseCoopers Spółka z ograniczoną odpowiedzialnością - 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
28.07.2016	Cezary Stypułkowski	President of the Management Board, General Director of the Bank	
28.07.2016	Lidia Jabłonowska-Luba	Deputy President of the Management Board, Chief Risk Officer	
28.07.2016	Przemysław Gdański	Deputy President of the Management Board, Head of Corporate and Investment Banking	
28.07.2016	Christoph Heins	Deputy President of the Management Board, Chief Financial Officer	
28.07.2016	Hans-Dieter Kemler	Deputy President of the Management Board, Head of Financial Markets	
28.07.2016	Cezary Kocik	Deputy President of the Management Board, Head of Retail Banking	
28.07.2016	Jarosław Mastalerz	Deputy President of the Management Board, Head of Operations and Information Technology	