

# **Assessment of the Supervisory Board of mBank S.A. on the situation of the company on a consolidated basis, including the adequacy and effectiveness of the company's systems of internal control, risk management, compliance with standards or applicable practices and internal audit**

## **1. Activities of the mBank Group in 2023**

The Supervisory Board analysed mBank Group's financial results and key indicators, taking into consideration external and internal conditions.

The year 2023 brought a distinct slowdown in economic growth. According to preliminary estimates of the Central Statistical Office, GDP dynamics in 2023 decreased to 0.2% from 5.3% in 2022. The inflation rate peaked at the beginning of 2023, and from February it gradually slowed down due to diminishing cost pressures caused by the global supply shock. The average annual inflation in 2023 reached 11.4%. High interest rates contributed to a decline in lending and a significant increase in deposits, mainly as a result of the inflow of household deposits, supported by good situation in the labour market. In September and October 2023, the Monetary Policy Council reduced the NBP reference rate by a total of 1 percentage point.

In 2023, the Supervisory Board of mBank analysed, on a cyclical basis, reports provided by the Management Board and organisational units of mBank, including information prepared at the request of the Supervisory Board on matters deemed significant from the point of view of the assessment of the bank's situation.

In 2023, total income posted by mBank Group reached its all-time high of PLN 10.8 billion.

The main driver of mBank Group's income growth in 2023 was net interest income, which increased by 21.7% year-on-year excluding the impact of loan holidays. The Supervisory Board is pleased to note that the achievement of this net interest income was possible thanks to effective deposit and loan margin management amid high interest rates environment. As a result, net interest margin went up from 3.7% in 2022 to 4.2% in 2023.

Net fee and commission income dropped by 9.6% in 2023 compared with 2022, mainly due to higher commission costs and waiving some of the account maintenance fees charged to corporate clients.

mBank Group remained highly cost effective. The C/I ratio for 2023 stood at 28.5%.

The cost of risk reached 93 bps in 2023 compared with 69 bps in 2022, mostly due to the economic downturn in Poland, higher loan servicing costs and one-off factors. Non-performing loans (NPL) accounted for 4.2% as at December 31, 2023, a result only slightly higher than last year's.

Similarly as in the last two years, the costs of legal risk posed by the portfolio of FX mortgage loans were a major drag on the bank's financial performance. In 2023, court rulings were generally favourable to clients suing banks, which was coupled

with a high influx of new lawsuits. The costs of legal risk connected with FX loans recognised in the group's 2023 profit and loss account amounted to PLN 4.9 billion. These costs were mostly generated by the update of assumptions for the population of clients who sued the bank, the anticipated distribution of court rulings, costs of the settlement programme and changes in other model parameters, in particular as a result of the CJEU ruling in case C-520/21 concerning remuneration for the use of capital when a loan was declared invalid. The Supervisory Board regularly monitored progress in the implementation of the borrower settlement programme which served as an alternative to lengthy and costly lawsuits. As at December 31, 2023, mBank signed more than 13,300 settlements with clients.

In the opinion of the Supervisory Board, the legal risk provision coverage of the CHF credit portfolio, which stood at 99.5% as at the end of 2023, and the bank's capital allocated to the FX mortgage business show that the bank is well prepared for the materialisation of legal risk resulting from FX loans.

mBank Group closed 2023 with a pre-tax profit of PLN 970.6 million. The net profit attributable to the owners of mBank reached PLN 24.1 million vs a net loss of PLN -702.7 million posted in 2022.

The actual achievements of mBank Group in 2023 are reflected in the financial performance of its core business, i.e. excluding the FX mortgage business. In 2023, the Group's core business generated a net profit of PLN 5,041.9 million, twice as much as in 2022. Return on equity (ROE) stood at 40.0%. This demonstrates the effective use of the unique features of the bank's business model and indicates good prospects of continuing organic growth and creating shareholder value.

mBank Group's capital ratios as at December 31, 2023 were higher than a year before. Tier Capital 1 ratio stood at 14.7% and the Total Capital Ratio (TCR) at 17.0%. At the same time, the buffer above the minimum KNF requirements for the Tier 1 capital ratio and TCR, went up from 3.4–3.5 pp at the end of 2022 to 5.6–5.9 pp. The capital ratios improved following a securitisation transaction on the portfolio of retail non-mortgage loans in the amount of approx. PLN 10 billion whereby a significant part of credit risk from the securitised portfolio was transferred to investors.

The issue of green non-preferred senior bonds under the EMTN Programme, with a nominal value of EUR 750 million, enabled the bank to meet the MREL by a significant margin.

mBank Group's liquidity position is comfortable, as demonstrated by high LCR and NSFR and a net loans-to-deposits ratio of 61.2% as at December 31, 2023.

In 2023, mBank Group continued to pursue its strategy for 2021–2025 "From the Icon of Mobility to the Icon of Possibilities". Considering the major change in the external environment and the developments on the financial market observed since the adoption of the Strategy in October 2021 that affected the Group's operation, the bank conducted a fundamental review of the growth directions and strategic goals set in the Strategy. The Supervisory Board acknowledged the mBank Group Strategy implementation status report and approved modifications to financial goals as well as to selected business goals and measures, while keeping the main growth directions for the Group unchanged.

The ESG strategy is an integral part of the mBank Group Strategy. The Supervisory Board believes that the revised aspirations and main directions set in the ESG strategy prove how determined the Group is to integrate social, ethical and environmental aspects in every area of its operation.

In 2023, the Group continued to digitalise, optimise and modernise processes, expanded the range of services available in remote channels, among others by launching new features in the mobile app for retail clients and in the mBank Company Mobile app for corporate clients, and by further developing the personal finance management tools. The bank increased the share of non-mortgage loans sold and banking processes initiated in digital channels and continued to develop e-commerce solutions. All this contributed to an uptick in the number of mBank clients, both retail and corporate, in particular mobile app users. At the same time, 2023 has seen a rise in client satisfaction and loyalty measured by the Net Promoter Score (NPS).

The Supervisory Board is pleased with the bank's progress towards sustainability. In 2023, mBank promoted and expanded the offer of products that support customers in sustainable transformation. The bank supported clients, among others by increasing the share of mortgage loans for the purchase or construction of energy-efficient real estate in total mortgage sales, offering ecological loans for small and medium-sized enterprises co-financed by Bank Gospodarstwa Krajowego, and boosting the bank's share in RES projects financing.

In 2023, mBank continued efforts to reduce and report the carbon footprint. The ultimate goal is to reach net-zero emissions from own operations (scope 1 and 2) by 2040 and to transform credit exposures (scope 3) so that they become net zero by 2050. The bank is one of the financial institutions that joined the Science Based Targets initiative (SBTi), a global initiative that helps companies set ambitious science-based decarbonisation targets. In 2022, the bank also joined the Partnership for Carbon Accounting Financials (PCAF) in order to assess the carbon footprint of its credit portfolio in line with top standards.

The bank is well perceived on the market, mostly thanks to high quality and broad range of services, innovative nature of products and services, advanced digitalisation, qualified personnel and ESG efforts. The new positioning of mBank's brand, as expressed in the tagline "mBank. Technology at your service", highlights that all products and services of the bank are designed with clients' comfort in mind and that the bank is always there to support them.

The Supervisory Board appreciates the bank's involvement in cultural, educational and social campaigns, including its cooperation with the Great Orchestra of Christmas Charity (WOŚP), promotion of mathematical education among kids and youth and the educational campaign promoting online security.

In conclusion, in the opinion of the Supervisory Board, the general economic and financial situation of mBank is stable. The bank meets all the requirements for safe operations, capital adequacy and liquidity, and guarantees that the clients' money is safe. The Supervisory Board positively assesses the results generated by the bank and mBank Group in 2023.

## **2. Assessment of the adequacy and effectiveness of the company's system of internal control, risk management, compliance with standards or applicable practices and internal audit**

The Bank's risk management system and internal control system are organised on three independent levels – lines of defence.

The internal control system supports the management of the Bank by contributing to ensuring the effectiveness and efficiency of the Bank's operations, the reliability of financial reporting, compliance with risk management principles, and the Bank's compliance with laws and internal regulations.

The internal control system includes:

1. The control function which aims to ensure compliance with control mechanisms relating in particular to risk management in the Bank, which includes positions, groups of people or organisational units responsible for the performance of tasks assigned to this function. The function is carried out in a systematic manner by employees at all organisational levels by means of:
  - continuous monitoring, consisting of the examination of selected operations or activities performed at the Bank,
  - periodic verification, consisting of an examination of selected operations or activities already completed in order to check the adequacy and effectiveness of the continuous monitoring.
2. The compliance function which is responsible for identifying, assessing, controlling and monitoring the risk of non-compliance of the Bank's operations with the law, internal regulations and market standards, as well as for presenting reports in this respect. The tasks of the compliance function are performed by the Compliance Department.
3. An independent internal audit function which aims to examine and assess, in an independent and objective manner, the adequacy and effectiveness of the risk management system and the internal control system. The tasks of the independent internal audit function are performed by the Internal Audit Department.

The Audit Committee provides the Supervisory Board with its opinion on the assessment of the internal control system based on information from the Bank's Management Board on the functioning of the internal control system, reports on the effectiveness of the control function, significant and critical irregularities and the status of recovery plans, reports on compliance risk management, the assessment from an internal audit perspective, as well as the results of audits. The Committee takes into account in its opinion information from the parent company, subsidiaries, the auditor, supervisory institutions (e.g., the Polish Financial Supervision Authority), as well as from other third parties. The Committee assesses the performance of the Compliance Department and the Internal Audit Department on the basis of annual activity reports presented directly by the Directors of the Compliance and Internal Audit Departments.

The Internal Audit Department included sustainability issues in its audit testing and assessment of the internal control system.

The Directors of the Compliance Department and the Internal Audit Department took measures on an on-going basis to ensure that adequate human resources and the necessary financial resources were available to systematically improve the qualifications, experience and skills of the staff of those units.

Based on the information received in 2023, the Supervisory Board assesses the adequacy and effectiveness of the internal control system (including the control function, the compliance function, and the internal audit function) in relation to the complexity of the Bank's activities, organisational structure, and risk management system as fair. As part of the assessment of the internal control system, on the basis of an opinion of the Audit Committee, the Supervisory Board identified the strengths of the system and areas for further improvement. The Supervisory Board assessed that the units responsible for the control function, compliance risk management, and internal audit carried out their tasks in accordance with the internal regulations on a continuous basis, and that the Bank's Management Board and Audit Committee, as well as the Supervisory Board, received adequate reports and information on the effects of such activities. The independence of the Compliance Department and the Internal Audit Department was ensured as defined in the Rules of the Compliance Department and the Audit Charter, respectively. In performing their duties, employees of those units performed their activities with independence and objectivity, did not execute processes which were subject to their controls, and did not engage in activities which could give rise to a conflict of interest with their duties.

The mBank Group's risk management system is based on the concept of three lines of defence.

The Bank has in place risk committees for each business line: the Retail Banking Risk Committee, the Corporate and Investment Banking Risk Committee, and the Financial Markets Risk Committee, which define the risk management principles and determine the risk appetite of the business line. Risks are also an important focus of the work of other committees in the Bank chaired by members of the Management Board.

The Bank has in place methodologies and processes where risks are identified and assessed to determine their potential impact on current and future operations. The comprehensive risk management structure is complemented by a consistent system for monitoring and reporting risk levels and breaches of limits set. The reporting system covers the key management levels.

The Supervisory Board receives periodic reports presenting an assessment of the level of risk identified and the effectiveness of the actions taken by the Management Board. In matters of risk, the Supervisory Board acts through the Risk Committee, which exercises on-going oversight of individual risks, in particular credit risk (including concentration risk), market risk, operational risk, liquidity risk, reputation risk, and business risk. The Committee makes recommendations on significant exposures with single business entity risk.

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