Bank Polski

Financial Results of the PKO Bank Polski SA Group for the year 2013

„PKO Bank Polski. The Best Every Day”

Warsaw, 10th March 2014

Executive summary

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- **Consolidated net income in Q4 2013 rose by 25% q/q to PLN 938 mn, bringing consolidated net income for the year 2013 to PLN 3,230 mn (y/y decline of 13.6%).**
- **Net income on business activity for the year 2013 reached PLN 10.7 bn (y/y decline of 7.9%), including the Q4 2013 increase of 25.8% q/q.**
  - ⇨ Increase in net interest income (+5.4% q/q) achieved primarily through reduction of interest expense resulting from adjustment of the price offer for deposit products and shift in their structure toward current deposits;
  - ⇨ Increase in net fee & commission income (+7.7% q/q) achieved primarily through increased net income from servicing of investment funds and brokerage activities; and increased net income from sale of loan insurance;
  - ⇨ Increase in net other income by PLN 505 mn q/q, primarily the effect of sale of a majority interest in the eService company.
- **Expansion of the operating base**
  - ⇨ Assets increase to PLN 199 bn (+3.1% y/y) as net loans increase to PLN 150 bn (+4.3% y/y), funded through increase in deposits from customers to PLN 152 bn (+3.9% y/y).
- **Cost discipline and improved portfolio quality**
  - ⇨ Reduction of operating costs by 1.3% in annual terms;
  - ⇨ Reduction of the cost of risk by 14 bps y/y, improvement in coverage ratio by 1.2 pps y/y and decline in NPL by 0.7 pps y/y (-0.4 pps q/q).
- **Retention of high operational efficiency**
  - ⇨ Cost / Income ratio (C/I) at 43.2%
  - ⇨ Return on Equity (ROE) at 13.2%
  - ⇨ Return on Assets (ROA) at 1.6%
  - ⇨ Interest margin at 3.7%
- **Strong liquidity and capital position**
  - ⇨ Loans / Stable funding resources at 90%
  - ⇨ Capital Adequacy Ratio at 13.6% (Core Tier 1 at 12.5%)

Selected 2013 Business Initiatives

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Acquisition of Nordea Group assets in accordance with Strategy for 2013-2015

PKO Bank Polski executed an agreement for acquisition of Nordea Bank Polska, Nordea Finance Polska, Nordea Polska TUnŻ, and of a corporate loan portfolio serviced by Nordea, a Nordic-based financial services group. The benefits accruing from the transaction will include, among others: growth of its affluent segment customer base; expansion of the key urban party of its distribution network; and strengthening of its corporate banking operations. The merger has also created growth opportunities for its bancassurance services and mortgage banking.

PKO Bank Polski and EVO Payments International entered into a strategic alliance

The Bank signed an agreement with a leading payment services operator active in US, Canada and Europe under which it sold a share stake in eService and concluded a 20-year strategic alliance in the electronic payments market. The transaction was approved by the European Commission and by the end of 2013 PKO Bank Polski finalised the sale of a 66% equity interest in CEUP eService. The alliance with an international technology partner will accelerate development of the company based on innovative solutions offered to the existing and future clients and customers.

New local mobile payments standard

PKO Bank Polski and five other banks came to an agreement on development of a new mobile payments standard for Poland, which would be based on the innovative IKO mobile payments solution PKO Bank Polski implemented. In December 2013 the aforementioned banks executed a joint investment agreement while in January 2014 they registered with the National Court Register the Polski Standard Płatności Sp. z o.o. company and are currently in the process of organising its operational launch.

PKO Junior or banking for minors of up to 13 years of age

The Bank launched one of the world's first internet banking services addressed to minors, a comprehensive financial education programme in itself. The new personal internet bank account enables children of up to 13 years of age to: collect their allowances and pocket money; initiate money transfers; save for specific purposes; and achieve challenging goals set by parents. Also, with the parents of children between ages of 0 and 12 years in mind the Bank developed the PKO Initial Capital deposit product.

New retail network sales model

Nowy Rytm

The Bank has launched a retail network project aimed at strengthening its market leadership. The project's key pillars include: a new goal setting and rewards system; focus on profit driving activities and initiatives; and new management tools. Under the branch network regeneration scheme, the customers received 105 upgraded branch facilities in 2013 and over 200 such branches over 2012-2013. 2013 also saw reorganisation of the Banks corporate outlet network and implementation of new standards in the work of customer advisers and specialists; all aimed at providing the customers with higher standard customer service efficiency and ensuring greater customer satisfaction at collaboration with the Bank.

Bank`s Quality 2013 and the Most Valuable Brand once more

PKO Bank Polski ranked in the forefront as it took the third position in a league table prepared by TNS Polska and Puls Biznesu. The quality of its customer service standards was rated very highly: with a result of 71.4%, between this year and a year earlier, the Bank leapfrogged four positions.
In 2013 Dom Maklerski PKO Banku Polskiego ranked first in the Forbes league table of brokerage firms; as assessed by institutional investors (up from position no. 5).
The Bank also defended its top positions gained in 2012 and was once again number one among financial companies and number 2 in the general classification of the Ranking of Polish Brands. The banking sector leader's brand was valued at PLN 3.7 bn.

Selected Business Initiatives in Q4 2013

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PKO Bank Polski investment loans with *de minimis* guarantees

PKO Bank Polski and Bank Gospodarstwa Krajowego signed another cooperation agreement within the framework of a government programme for small and medium enterprises. It enables businesses to apply BGK loan guarantee support toward financing business expansion investment projects. Since March 2013 loan guarantee Programme *de minimis* has suported companies, which had not got sufficient collateral and could not receive a loan. By the 2013-end 17.7 thousand guarantees in the amount of about PLN 2.2 billion was granted via PKO Bank Polski, which was about 30% of all guarantees granted via banks participating in the Programme. Total amount of guaranteed loans, which were sold by PKO Bank Polski excedeed PLN 3.5 billion in 2013

The Inteligo internet banking system experiences important changes

PKO Bank Polski completed the process of migrating Inteligo on to the Alnova IT platform, which the Bank operates on. Having a common IT has opened up possibilities of implementing functionalities Inteligo could not offer before.

IKO a winner of the Effective Mobile Marketing Awards 2013

The IKO application was the winner in the Most Effective Mobile Payment Solution category at the international Effective Mobile Marketing Awards 2013 competition organised by the Mobile Marketing Magazine. The competition organisers praised IKO for its attractive graphics and utility. Over 100,000 users have now activated the app, completing over 250,000 phone-enabled transactions.

Local government friendly PKO Bank Polski

The Bank won a tender for servicing current accounts of the Mazowieckie Region, including its subordinate budgetary units and cultural institutions, for a renewed four-year period. The Bank also services the budgets of the Wielkopolskie, Zachodniopomorskie, Lubelskie and Kujawsko-Pomorskie regions as well as of many municipalities. At the 11th Local Self Government Capital and Finance Forum, held under the auspices of the President of Poland, the Bank was awarded the King Casimir the Great statuette for its attractive offer based on understanding of market realities and its openness to the needs of self-government entities.

Once more the Contact Center leads the Bank Call Centres Ranking

Dedication, credibility and professionalism of its consultants, as well as product knowledge and the capabilities of matching the offer and the customer needs enabled PKO Bank Polski Contact Center to come out the winner of the ARC Rynek i Opinia ranking for the fifth consecutive year. The Bank collected 99.4 out of the 100 points achievable. Interviewers assessed very highly the commitment and professionalism of the Bank's consultants in providing information on mortgage loans, credit cards, loans, bank accounts, etc.

Customer Ombudsman in PKO Bank Polski

Cultivating customer satisfaction and long term customer relationships form part of its priority objectives, which is why PKO Bank Polski appointed the Customer Ombudsman; as one of the few in the Polish banking sector. From 1 January 2014 has been available to the customers, with the primary role of considering applications of customers dissatisfied with the way the Bank had handled their claims and complaints.

Plan for integration of the Nordea assets assumes finalizing the main stage of works in Q2 2015

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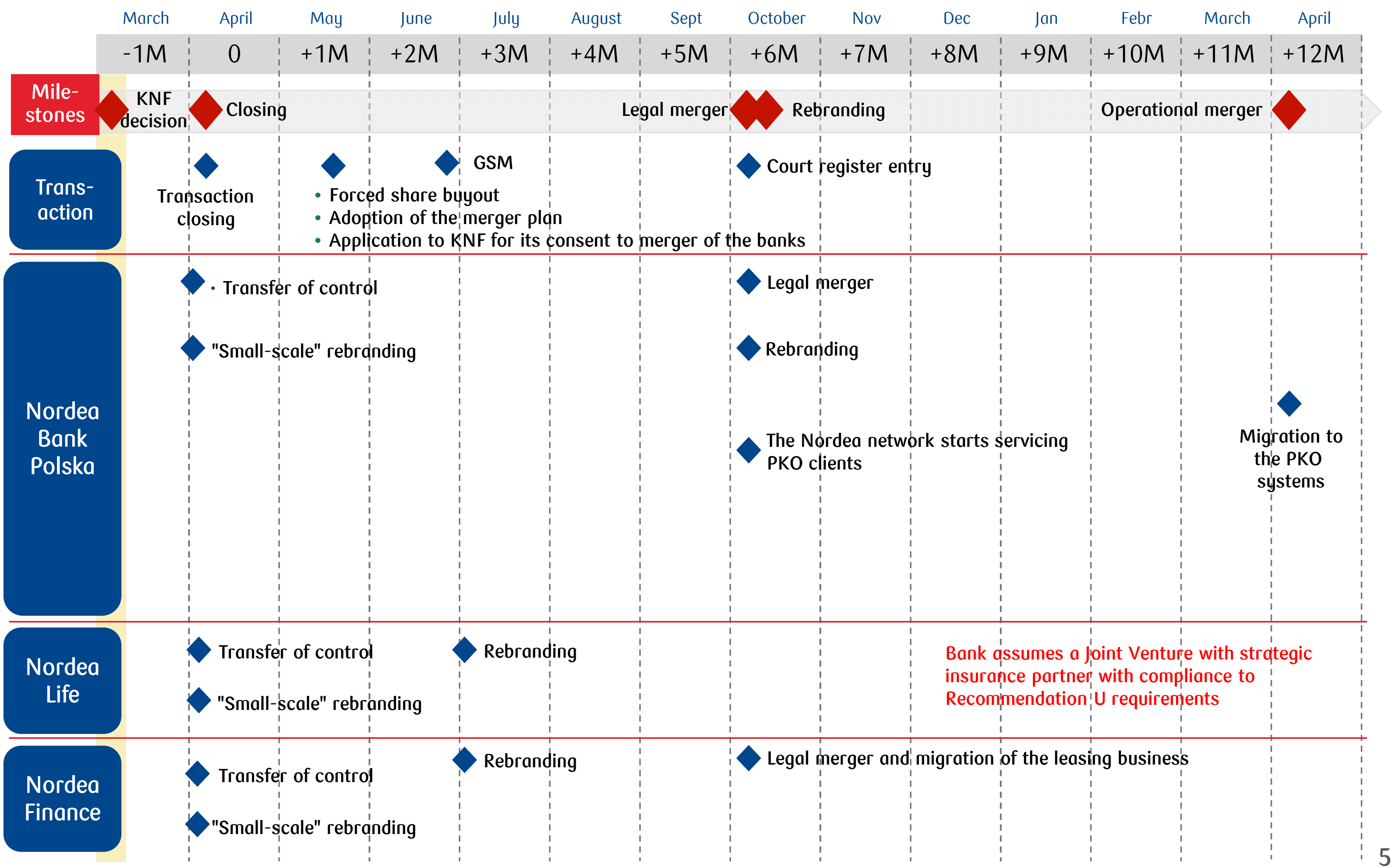

Integration synergies and costs in the years 2013-2017

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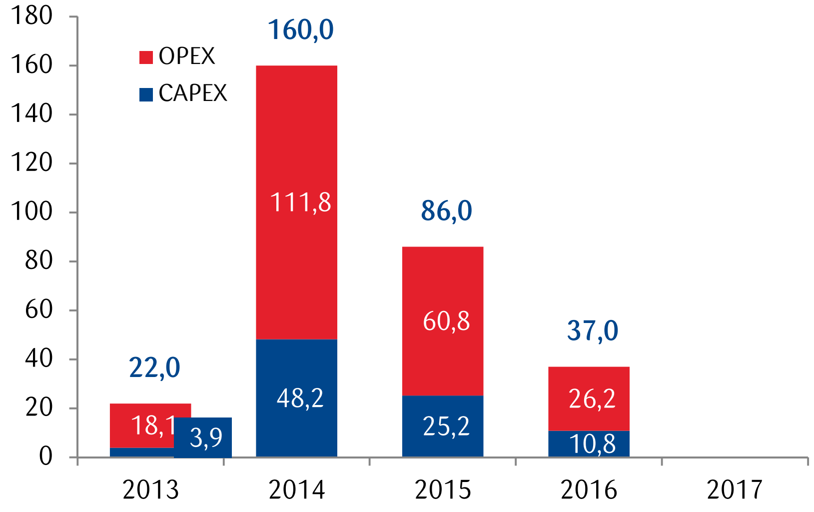
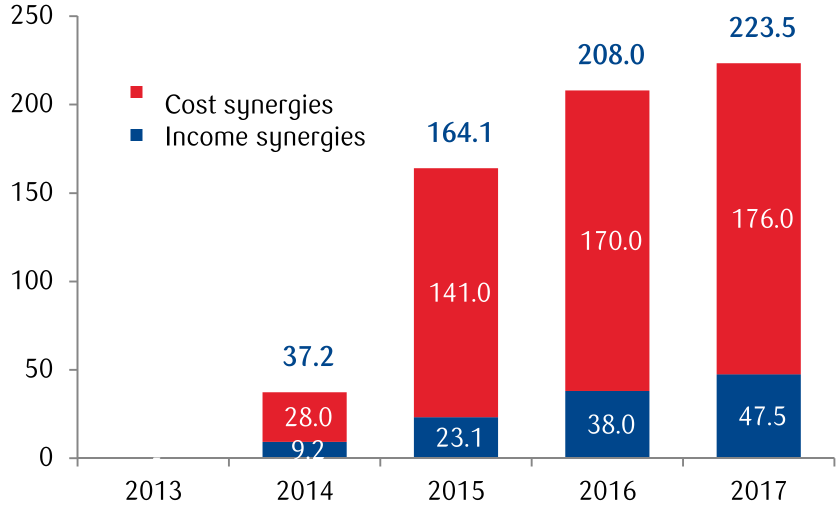
Costs of integration (PLN mn)



Income and costs synergies (PLN mn)



- PKO Bank Polski has assumed the total integration expenditures over four years to close at PLN 305 mn;
- Opex will represent over 75% or PLN 237.8 mn of those expenditures;
- Capex will thus stand at close to 25% of the integration expenditures;
- The key integration budget items will include: IT system migration (over 55%), personnel costs (21%), marketing and communications (7%), real estate (5%) and other (12.5%);
- The assumed integration expenditures are equivalent to average in comparable transactions in both Poland and the international markets, even though the cost structure is somewhat different on account of the cost of unbundling of the IT area.

- After a detailed verification exercise, the Bank now expects the cost saving synergies to be higher than originally assumed;
- The Bank expects to realise the IT area related synergies rather rapidly: at termination of cooperation with the supplier of the IT services carved out of Nordea Bank Polska;
- Total acquisition synergies are estimated at PLN 223.5 mn (gross); as of 2017, i.e. counting from completion of the integration process;
- Key synergies will be delivered through: integration of the functions such as IT, support and cross-selling; acquisition of new clients and customers; and bancassurance in the retail banking business;
- The transaction will have a positive impact on the PKO BP Group's net financial result as early as in 2014;
- At completion of the integration process in 2017, estimated EPS attrition will reach nearly 9%, with ROI of around 13%.

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Financial Summary *

		2013	2012	Change y/y	Q4'13	Q3'13	Change q/q
P&L items (PLN mn)	Net interest income	6 722	8 089	-16.9%	1 715	1 627	+5.4%
	Net F&C income	3 006	2 917	+3.1%	815	757	+7.7%
	Result on business activity	10 707	11 622	-7.9%	3 176	2 525	+25.8%
	Administrative expenses	-4 623	-4 683	-1.3%	-1 281	-1 116	+14.9%
	Net impairment allowance	-2 038	-2 325	-12.4%	-683	-488	+40.1%
	Net profit	3 230	3 739	-13.6%	938	752	+24.7%
Balance sheet (PLN bn)	Assets	199.2	193.2	+3.1%	199.2	201.3	-1.0%
	Net loans	149.6	143.5	+4.3%	149.6	149.6	+0.0%
	Deposits	151.9	146.2	+3.9%	151.9	150.9	+0.7%
	Stable financial resources	166.7	160.6	+3.8%	166.7	165.7	+0.6%
	Total equity	25.2	24.4	+2.9%	25.2	24.2	+4.0%

*) Due to a change in the accounting principles applicable to recognition of insurance products related revenues and expenses, relevant data in respect of the previous periods have been restated to ensure comparability.

Consolidated data

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Key performance indicators*

		2013	2012	Change y/y	Q4'13	Q3'13	Change q/q
Basic financial indicators	ROE net (%)	13.2	16.0	-2.8 pp.	13.2	12.9	+0.3 pp.
	ROA net (%)	1.6	2.0	-0.4 pp.	1.6	1.6	0.0 pp.
	C/I[1] (%)	43.2	40.3	+2.9 pp.	43.2	44.7	-1.5 pp.
	NIM[2] (%)	3.7	4.7	-1.0 pp.	3.7	3.9	-0.2 pp.
Quality of loan pottfolio	NPL ratio[3] (%)	8.2	8.9	-0.7 pp.	8.2	8.6	-0.4 pp.
	Coverage ratio[4] (%)	51.7	50.5	+1.2 pp.	51.7	51.4	+0.3 pp.
	Cost of risk (bp.)	131	145	-14	131	129	2
Capital position	CAR (%)	13.6	12.9	+0.7 pp.	13.6	13.7	-0.1 pp.
	Core Tier 1 (%)	12.5	11.8	+0.7 pp.	12.5	12.6	-0.1 pp.

*) Due to a change in the accounting principles applicable to recognition of insurance products related revenues and expenses, relevant data in respect of the previous periods have been restated to ensure comparability.

(1) Administrative expenses of last 4 quarters / result on business activity for last 4 quarters
(2) Net interest margin = net interest income of last 4 quarters / average interest bearing assets at the beginning and the end of the period of last 4 quarters (formula consistent with that applied in the PKO Bank Polski Group Directors' Report)
(3) Share of loans with recognised impairment in total gross loans
(4) Coverage of loans with recognised impairment with impairment allowances

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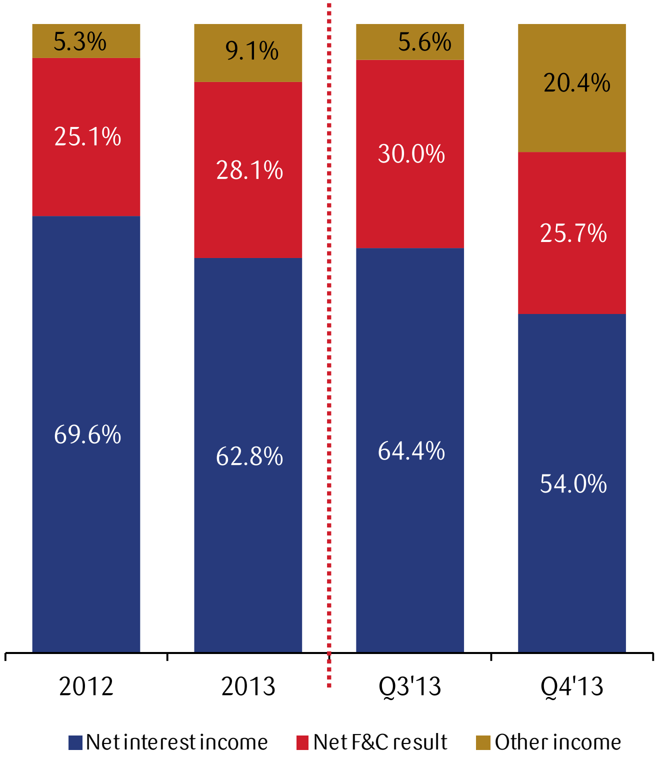
Result on business activity

Split of result on business activity



PLN mn	2012	2013	Change y/y	Q3'13	Q4'13	Change q/q
Net interest income	8 089	6 722	-16.9%	1 627	1 715	+5.4%
Net F&C result	2 917	3 006	+3.1%	757	815	+7.7%
Other income	616	979	+59.0%	141	647	+357.6%
Result on financial operations and didvidens	182	128	-29.9%	35	23	-35.2%
Net FX result	256	242	-5.6%	67	99	+47.5%
Net other income	178	610	+243.2%	39	525	+1247.4%
Result on business activity	**11 622**	**10 707**	**-7.9%**	**2 525**	**3 176**	**+25.8%**

1 In 2013 a change in the accounting principles applicable to recognition of insurance products related revenues and expenses was enacted. As a result:
– the previously presented net interest income of 2012 increased by PLN 207 mn
– the previously presented net F&C income of 2012 decreased by PLN 155 mn
Without the accounting principle adjustment, net interest income would have declined by (-)17.5% y/y while net F&C income would have risen by (+)4.9% y/y

2 For the quarterly data restated for comparability, the following adjustments were made:
– net interest income of Q3'13 increased by PLN 49 mn, and of Q4'13 by PLN 60 mn
– net F&C income of Q3'13 decreased by PLN 52 mn, and of Q4'13 by PLN 60 mn
Without the accounting principle adjustment, net interest income would have risen by (+)5.0% q/q while net F&C income would have risen by (+)7.8% q/q.

3 This net income item increased as it includes income of PLN 315 mn from the sale in Q4'13 of a 66% interest in the eService subsidiary and income of PLN 162 mn on fair value adjustment of the remaining eService share interest.

Net interest income (1)

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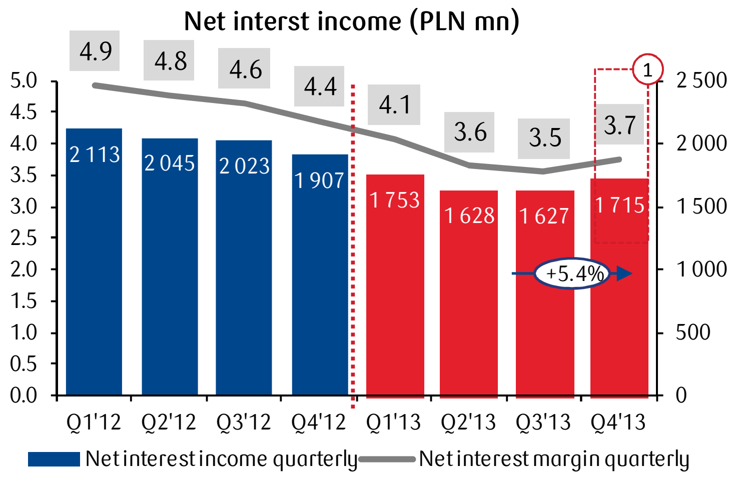

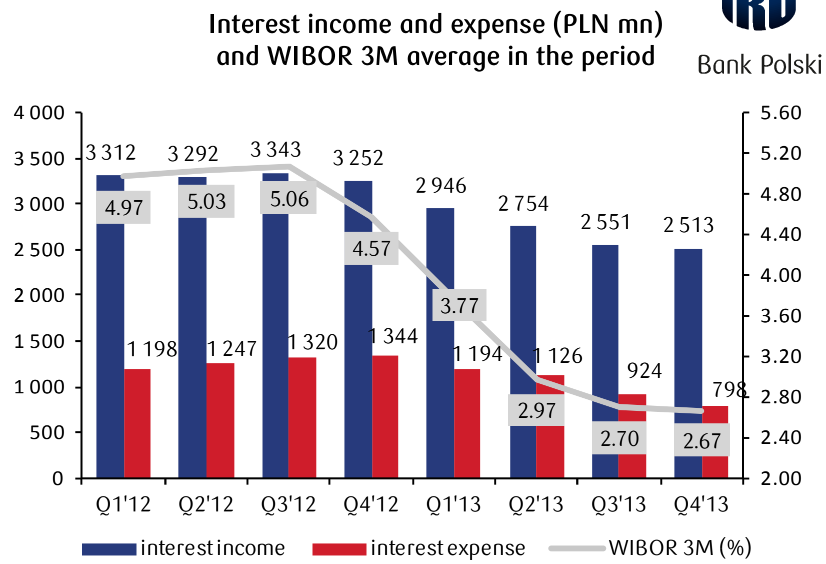

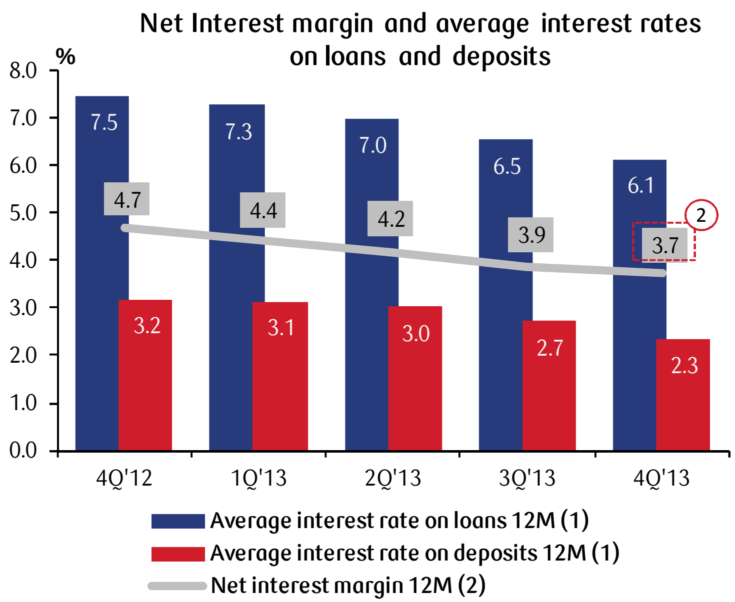

1 Stabilisation of NII and NIM in Q4'13 under conditions of maintenance of low market interest rates; mainly due to lower average interest rates on deposits; adjustment of the price offer for deposit products; and change of the structure in favour of current deposits.

2 Drop in interest margin by 1.0 pp. y/y to 3.7% as a result of a decrease in annualised net interest income (due to a drop in market interest rates causing directly a decrease in interest-bearing assets mostly based on market rates faster paced than the decline in interest rates of the deposit offer); accompanied by an increase in the volume of average interest-bearing assets (mainly the portfolio of loans and advances to customers).
Change of accounting rules increased NIM by ca. 0.1 pp.

(1) Interest income (expense) for last 4 quarters / average net loans (deposits) at the beginning and the end of the period of last 4 quarters
(2) Net Interest income for last 4 quarters / average interest bearing assets at the beginning and the end of the period of last 4 quarters (formula consistent with that applied in the PKO Bank Polski Group Directors' Report)

% Change q/q

Stable growth of F&C income despite of interchange fee drop and lower market growth

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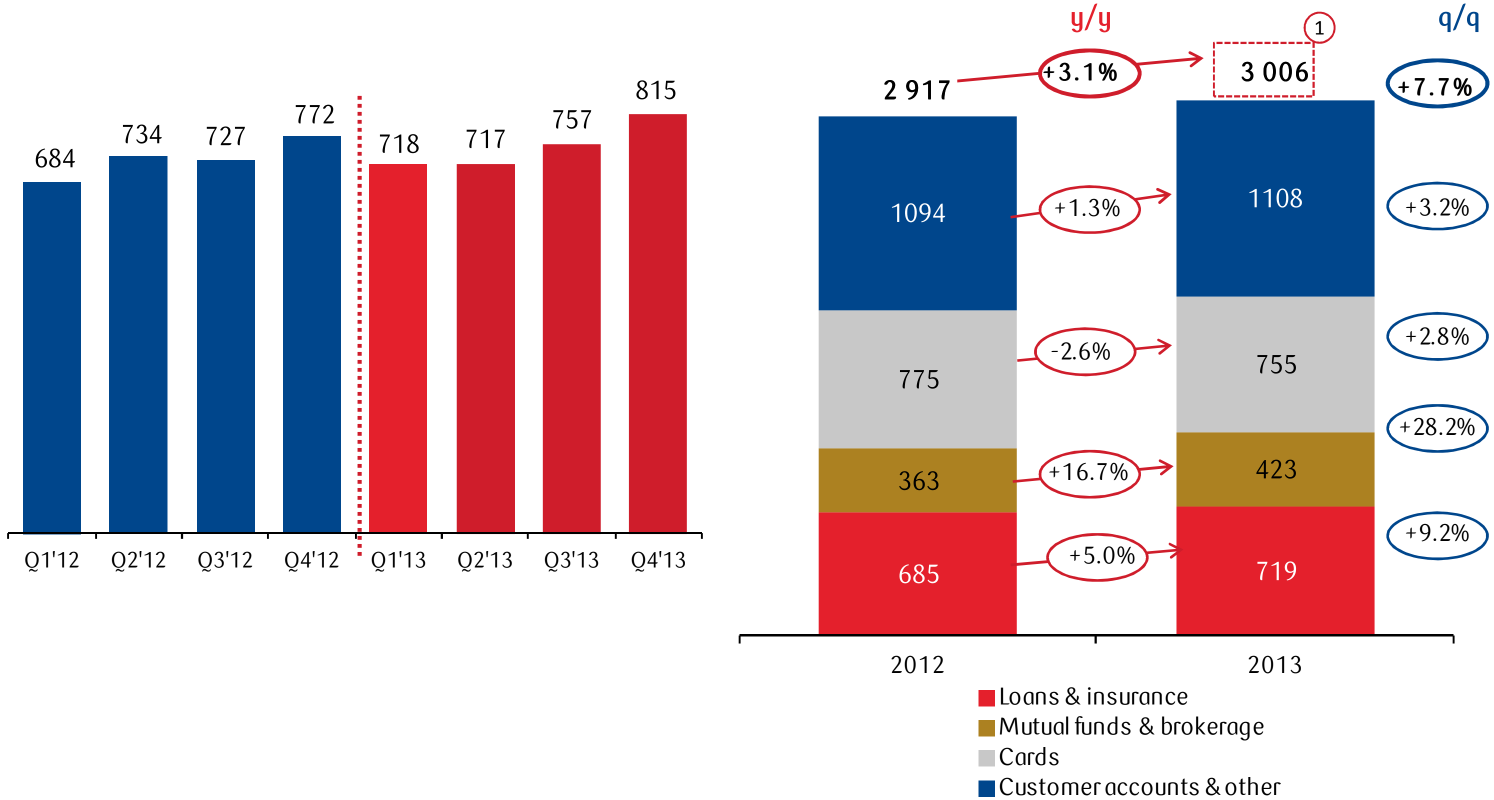
Net fee and commission income (PLN mn)



1 Net fee & commission income was primarily determined by:

- increase in income from servicing of investment and pension funds (including management fees) resulting from: improved profitability of the funds' sales structures; over 40% increase in the value of assets under management; and the takeover in Q2'13 of the assets of OFE Polsat;
- increase in net income from loan insurance; an effect of increase in saturation of loans with insurance policies, additionally supported by an increase in new loan sales;
- increase in income from servicing of bank accounts;
- decline in net income from banking cards primarily the effect of decline in interchange fee (IF) commissions, as the Visa and MasterCard payment organisations reduced the IF rates at the beginning of the year; the lower IF commissions were accompanied by an increase in card transactions;
- decline in commission income from treasury bond issue agent services;
- decline in income from cash transactions; as driven by the development of electronic banking.

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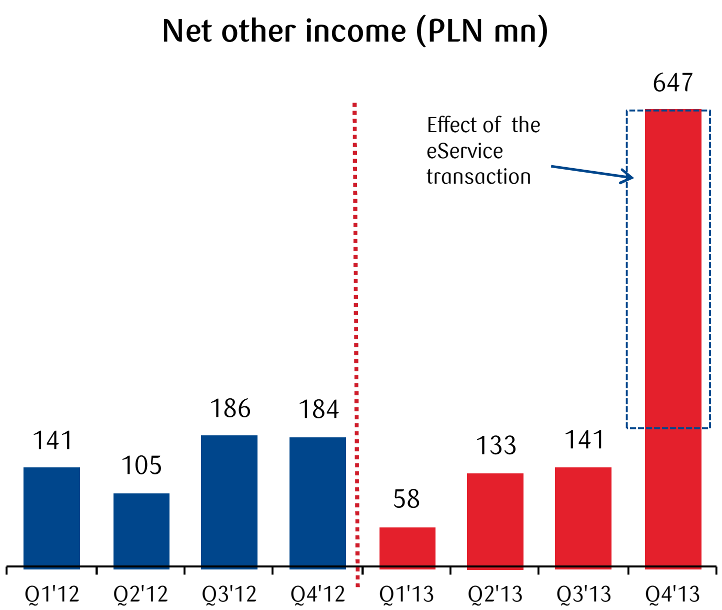
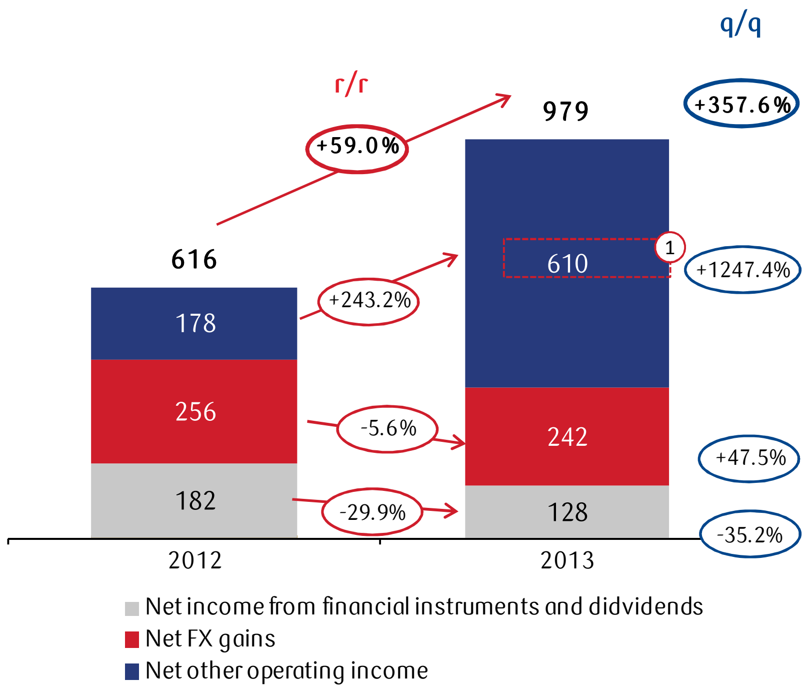
Net other income





1 Growth in net other operating income on annual and quarterly basis resulted from inclusion in this item of income on the sale in Q4'13 of a 66% stake in the eService subsidiary amounting PLN 315 mn and on fair value readjustment of the remaining share interest in the eService amounting PLN 162 mn.

Administrative expenses

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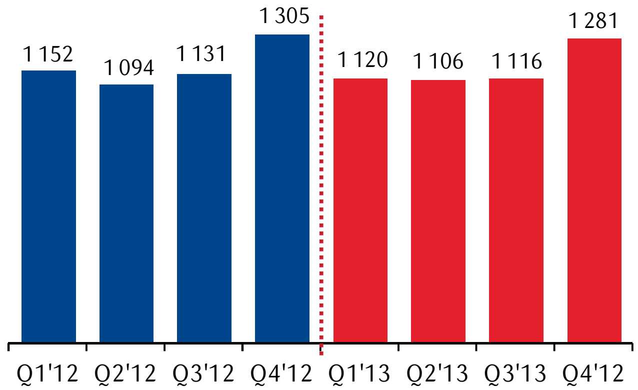
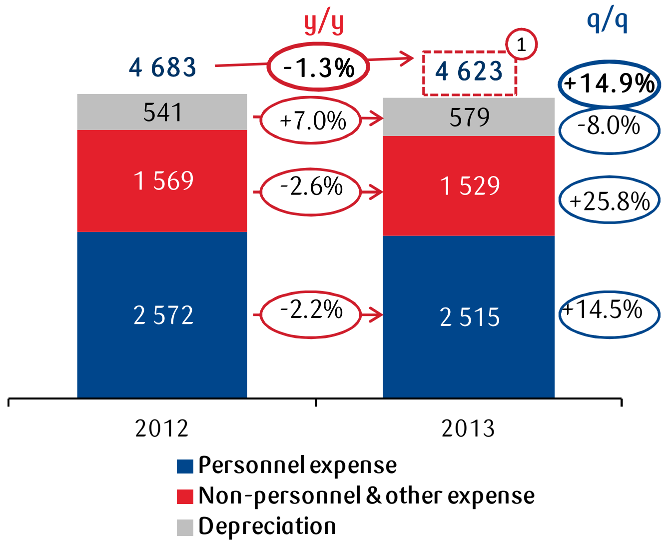
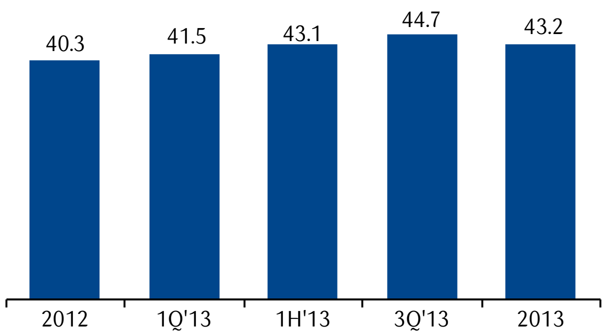
Administrative expenses (PLN mn)





C/I ratio



Employment (FTEs) eop

	2012	2013	Change y/y	
			FTEs	%
Bank	25 399	24 437	-962	-3.8%
Group	28 556	27 387	-1 169	-4.1%

1 Value of general and administrative expenses was primarily determined by:

- decline in employee benefit costs by PLN 57 mn y/y;
- decline in material and other costs by PLN 41 mn y/y, resulting, among others, from decline in costs of property maintenance and rental, in promotional expenses and KNF costs, and at increase in the Bank Guarantee Fund costs; primarily as a result of introduction of the prudential fee;
- increase in depreciation by PLN 38 mn y/y; primarily as a result of increase in amortisation of intangible fixed assets.

The year 2013 saw introduction of a change in accounting rules relating to presentation of actuarial gains and losses, which led to upward adjustment by PLN 64 mn of the previously presented employee benefit costs for the year 2012 (effect of implementation of a change in MSR 19).

Net impairment allowance

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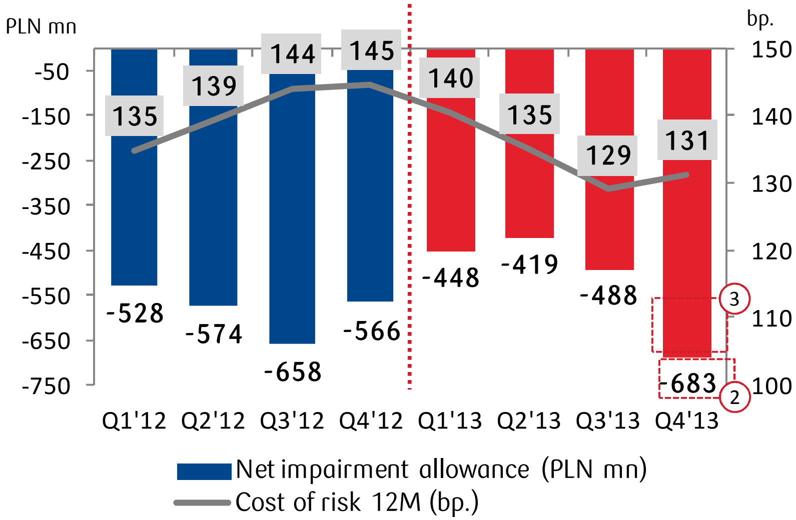
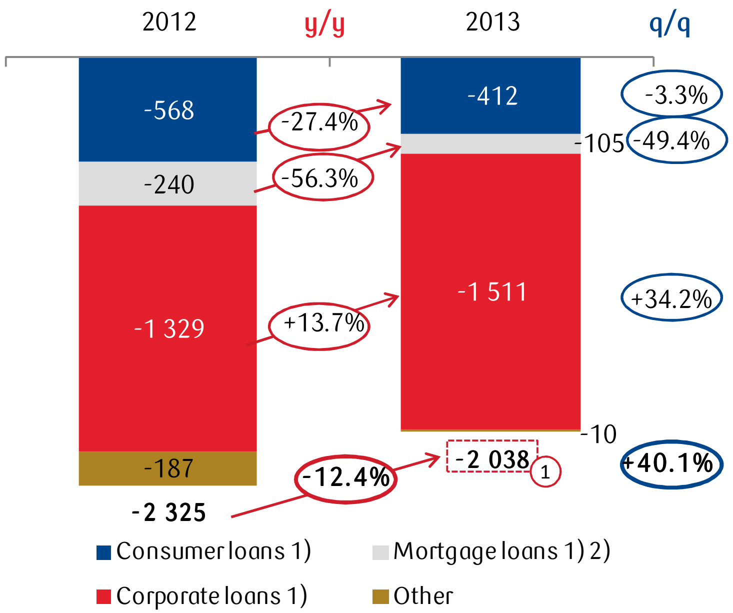
Net impairment allowance and write-offs (PLN mn)





Share of loans with recognized impairment[3)]

	2012	2013	Change y/y
Consumer loans	8.9%	9.7%	+0.8 pp.
Mortgage loans	3.7%	3.6%	-0.1 pp.
PLN	*3.6%*	*3.1%*	-0.5 pp.
FX	*4.0%*	*4.6%*	+0.6 pp.
Corporate loans	14.1%	12.6%	-1.5 pp.
Total	**8.9%**	**8.2%**	**-0.7 pp.**

1. Improvement in net income for the year primarily coming from reduced write-offs on consumer and housing loan portfolios and resulting from improved quality of the new loan originations comparative to the loans of the earlier generations.

2. Increase in net impairment allowances in Q4'13 resulting from increased write-offs on corporate loans.

3. Increase in write-offs in Q4'13 by circa PLN 100 mn in the subsidiaries operating in Ukraine; caused by the economic conditions prevailing in that country and differed tax write-off.

(1) management accounts data (2) Housing loans to individuals
(3) Calculated by dividing the gross carrying amount of impaired loans and advances to customers by the gross carrying amount of loans and advances to customers

Basic operational data

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Item (eop)	2012	1Q'13	1H'13	3Q'13	2013	Change	
						y/y	q/q
Number of current accounts ('000)	6 220	6 245	6 254	6 283	6 318	+1.6%	+0.6%
Number of banking cards ('000)	7 164	7 120	7 225	7 090	7 080	-1.2%	-0.1%
of which: credit cards	*980*	*938*	*919*	*899*	*893*	-8.9%	-0.7%
Number of branches:	1 198	1 199	1 177	1 181	1 186	-1.0%	+0.4%
- retail	1 134	1 135	1 138	1 142	1 147	+1.1%	+0.4%
- corporate	64	64	39	39	39	-39.1%	0.0%
Number of agencies	1 208	1 202	1 149	1 115	1 074	-11.1%	-3.7%
Number of ATMs	2 803	2 911	2 945	2 960	2 992	+6.7%	+1.1%
Number of active IKO applications ('000)	x	11	39	57	101	x	+78.4%
Number of eService terminals	68 877	71 706	79 928	84 020	89 645	+30.2%	+6.7%