MANAGEMENT BOARD'S REPORT ON THE ACTIVITIES OF BANK GOSPODARKI ŻYWNOŚCIOWEJ S.A. GROUP FOR THE FIRST HALF OF 2013

Warsaw, 13 August 2013

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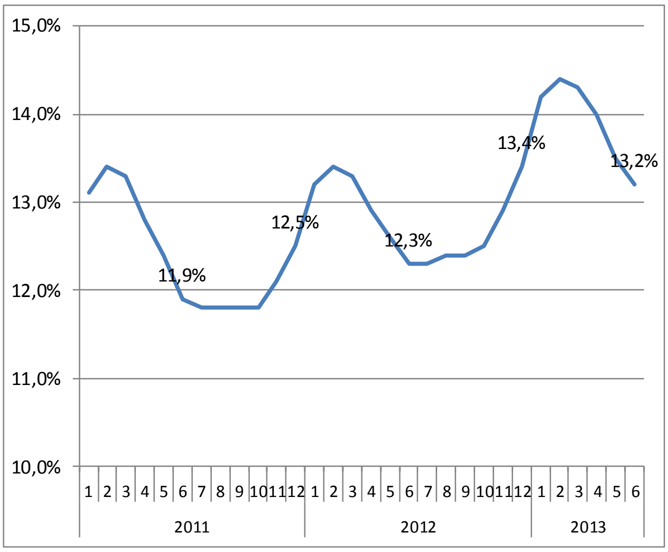
1. EXTERNAL CONDITIONS FOR THE FUNCTIONING OF BGŻ S.A. GROUP

1.1. MACROECONOMIC SITUATION

The dynamics of Gross Domestic Product in Q1 2013 have decreased from 0.7% y/y in Q4 2012 (data after correction) to 0.5% y/y i.e. to the lowest level since Q1 2009. It was caused by a lower contribution of net export to GDP growth (+1.4 p.p. in Q1 2013 compared to +2.4 p.p. in Q4 2012) as a result of ongoing recession in the European Union, and especially of further economic slowdown in Germany. The dynamics of GDP was negatively influenced by investments, however not as significantly as in Q4 2012 (- 0.3 p.p. in Q1 2013 versus -1.2 p.p. in Q4 2012), which was a result of very low investment expenditures in Q1 2012 i.e. a low base. The investments remained at the low level because of very little absorption of the EU funds in Poland, and also because of investment aversion in private sector. According to the Bank's estimates, in the first half of 2013 GDP has grown by 0.7% y/y. It was caused by decrease in investments by 1.6% y/y, which was a result of low level of public investments in infrastructure. The negative dynamics in investments contributed to decrease in domestic demand by 0.7% y/y. GDP growth was supported by private consumption, which increased by 0.2% y/y in the first half of 2013. In regards to individual consumption it was a result of growing real salaries and significant adjustment of social benefits for inflation, and partially of less strict regulations on the consumer credits market.

Chart 1. Growth of GDP (y/y)

Chart 2. Registered unemployment rate



** forecast of BGŻ S.A.*
Source: GUS, own estimation

Continued low economic activity in Europe combined with weakening dynamics in internal demand resulted in drastic fall in industrial production in Q1 2013. The recovery in individual demand in Q2 improved the situation in industrial sector. As a result, the industrial production, which in Q1 dropped by 1.6% y/y, grew by 1.3% y/y in Q2. The first half of 2013 ended with result of -0.1%y/y. The negative dynamics of industrial production and the collapse of construction and assembly production (during the first half of 2013 it decreased by 20.4% when compared to the first half of 2012) resulted in a deterioration of situation on the labour market. As a result, employment dynamics in the enterprise sector fell from -0.1% y/y in the second half of 2012 to -0.9% y/y in the first half of 2013. The unemployment rate (with no seasonal adjustment) in June 2013 equalled to 13.2% compared to 12.3% in the previous year.

As a result of the significant deterioration on the labour market, the dynamics of nominal salaries decreased to 2.1 % y/y in the first half of 2013 (4.6% y/y in the previous year). However, in the first half of 2013 the dynamics of real salaries increased to 1.2% y/y when compared to 0.5% y/y in the previous year. This was a result of decreasing inflation caused by weak demand and falling fuel and energy prices. On average, inflation rate amounted to 0.9% y/y in the first half of 2013.

Because of the low level of actual and expected inflation rate, the Monetary Policy Council *(Rada Polityki Pieniężnej - RPP)* decreased interest rates by a total of 150 basis points. Following the decrease, the central bank reference rate reached the level of 2.75%. The decision was taken by the RPP in the face of the evident economic slowdown indicators. The rediscount rate – which is the basis for setting interest rates for agricultural preference loans – was lowered to 3%. In July 2013 there was another decrease in interest rates by 25 basis points, which has been discounted by financial markets already in June.

In the first five months of 2013, the volatility on the foreign exchange market (especially in terms of zloty) was moderate. The EUR/PLN exchange rate was in the narrow fluctuation band between 4.05 and 4.20, and USD/PLN exchange rate between 3.03 and 3.28. After the period of significant fluctuations in Eurozone (especially in Greece), the actions taken by international institutions resulted in the settling down the situation at the turn of 2012 and 2013. The stability of zloty was not harmed by the strong inflow of international capital to the domestic treasury bonds market. However, in June depreciation of zloty took place and the EUR/USD rate reached more than the level of 4.30. This was the result of the speculations about the reduction of FED quantitative easing, which triggered the outflow of capitals from the domestic treasury bonds market. The zloty was also influenced by instability of political and budget situation in Poland, and also by speculations of open-end pension funds (OFE) reform. Along with the relaxing of Eurozone situation in the first half of 2013, the Swiss Franc gradually depreciated against Euro. However, in comparison to the historic EUR/CHF exchange rate, the scope of this fluctuation was very narrow.

Chart 3. Inflation and interest rates

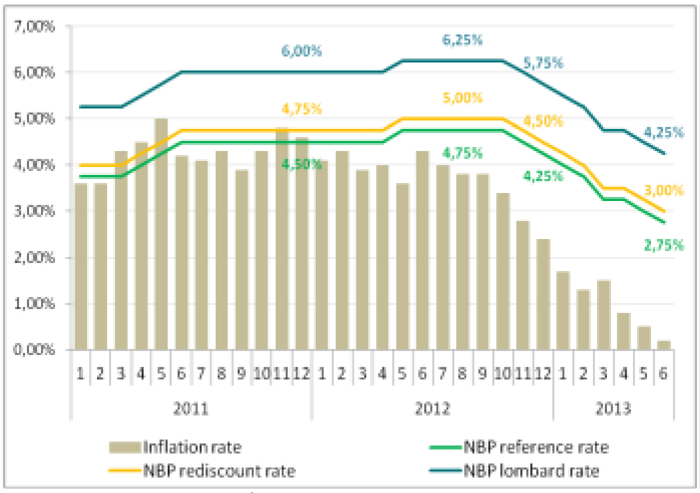
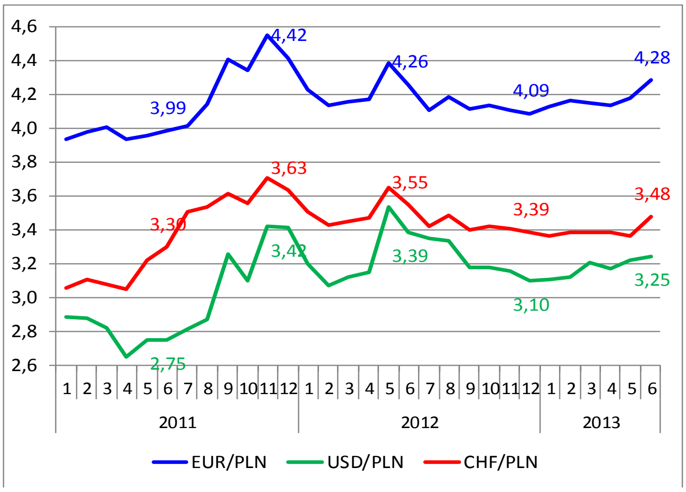


Chart 4. Exchange Rate



Source: GUS and NBP

1.2. BANKING SECTOR RESULTS

According to the Polish Financial Supervision Authority data, in the first half of 2013 the net financial result of the Polish banking sector increased by 1.9% y/y and reached the level of PLN 8.2 billion (compared to PLN 8.0 billion in 2012 corresponding period). The main growth factor of the net financial result was a deep slump of write-offs and provisions balance (by 30.9%), accompanied by increased other operating result (by 110.2% y/y). The annual positive change in the net profit of the banking sector was also slightly affected by reduction of banks' operating costs (by 0.8% y/y), although the decrease in administrative expenses.

The result on banking activities recorded by the banks has significantly deteriorated in the period. It was a result of decrease in net interest income (by 8.9%), caused mainly by the ongoing cycle of monetary policy easing, and also of poor lending activities in the corporate sector and housing loans for individuals segment. In addition to the net interest income drop, net fee and commission income declined by 2.4% y/y. The latter was caused by the reduction of interchange fee, imposed by payment organizations, and probably also by the harsh competition on personal accounts' market and a mentioned poor lending activities in few market segments. The negative contribution to the change of the results on banking activities was made by decrease in net dividend income (by 19.4% y/y) and decrease in so-called other positions in result on banking activity, which stabilized the result of the sector in 2012 (by 3.7% y/y).

Table 1. Selected elements of banking sector's profit and loss statement

PLN million	**I-VI 2013**	**I-VI 2012**	**Change y/y**	
Net interest income	16 297	17 880	(1 583)	(8,9%)
Net fee and commission income	6 997	7 170	(173)	(2,4%)
Dividend income	692	858	(166)	(19,4%)
Other elements of the net income from banking activity	3 800	3 947	(147)	(3,7%)
Result on banking activity (total)	**27 786**	**29 856**	**(2 069)**	**(6,9%)**
Other operating result	864	411	453	110,2%
Costs on bank activities	(13 830)	(13 946)	116	(0,8%)
Depreciation and amortization	(1 297)	(1 287)	(10)	0,8%
Net impairment losses on assets and other provisions	(3 509)	(5 079)	1 569	(30,9%)
Profit (loss) before income tax	**10 033**	**9 954**	**78**	**0,8%**
Income tax expense	(1 847)	(1 919)	72	(3,8%)
Net profit (loss) for the period	**8 183**	**8 028**	**155**	**1,9%**

Source: PFSA.

Capitalised by net profits, the equity of domestic banking sector (taken into account when calculating capital adequacy ratio) increased at the end of June 2013 by 5.3% to PLN 135.9 billion when compared to the end of 2012. However, the general capital requirement – with the limited lending activity in some market segments, and depreciating Polish zloty - increased by 2.1% to PLN 71.5 billion, when compared to the end of 2012. As a result, the sector's capital adequacy ratio increased by 0.5 pp. reaching 15.2%, when compared to the end of 2012.

In the first half of 2013, lending activity of the banking sector, measured with the rate of growth in deposit and credit volumes for non-banking clients, remained at a low level (at the end of June the credits and loans increased by 3.5% y/y). The growth rate of deposits from non-banking clients remained at the moderate level (increase by 7.3% y/y).

Debt under loans to private individuals increased at the end of June 2013 only by 1.7% y/y. It was a result of a downward trend in housing loans and a weak situation on the market of consumer credits (there were the signs of improvement in Q2 2013). This slowdown was, among other things, caused by government-subsidised program "*Rodzina na swoim"* and the strict PFSA Recommendations, especially in the first part of analyzed period, which formally limits availability of housing loans. The other factors restraining customers from incurring new debts were a tough situation on the labour market and an ongoing uncertainty about future financial situation of households. The expectation connected with introduction of a new government-subsidised program "*Mieszkanie dla Młodych"* could also result in delay in credit decision made by customers. It should be noted that in the analysed period – despite the strict banks' lending policy– there was a significant reduction of housing loans costs (and thus improvement of their availability), caused by interest rates decrease made by Monetary Policy Council (RPP). Regarding the currency structure of newly granted housing loans, according to The Polish Bank Association (ZBP), in the first half of 2013 the housing loans in PLN dominated the sale. The sale of currency housing loans was marginal.

Table 2. Loan volume of the banking sector

PLN million, as at the end of year	30.06. 2013	31.12. 2012	30.06. 2012	Change	
Loans for individual clients	**460.5**	**449.5**	**452.9**	**7.6**	**1.7%**
- housing loans	332.2	319.8	320.5	11.7	3.7%
- PLN loans	154.6	144.3	132.3	22.4	16.9%
- currency loans	177.5	175.5	188.2	(10.7)	(5.7%)
- consumer loans	128.3	129.7	132.4	(4.1)	(3.1%)
Loans for corporate clients	**468.2**	**451.2**	**444.0**	**24.2**	**5.5%**
-non-banking financial sector	40.9	32.1	30.0	10.9	36.4%
-loans for business entities	349.2	339.4	340.1	9.1	2.7%
enterprises	263.4	257.0	259.4	4.0	1.6%
individual entrepreneurs	56.0	53.5	53.2	2.9	5.4%
individual farmers	24.9	24.1	23.3	1.6	6.7%
non-profit institutions	4.9	4.8	4.3	0.6	14.0%
- loans for government sector	78.2	79.6	73.9	4.2	5.7%
Loans for non-banking clients	**928.7**	**900.6**	**896.9**	**31.8**	**3.5%**

Source: NBP, data for monetary financial institutions, excluding Central Bank and SKOK, only residents.

In the Q2 2013, there were signs of improvement in the poor situation on the consumer credit market; the decrease dynamics was noticeably slower. This could be a result of a liberalization of T Recommendation announced by PFSA at the end of February 2013, especially while there was still a huge pressure of banks on the sale of cash loans. The decreasing pace of dropping consumer loans volumes, on a yearly basis, could also be a result of, lower than year before, disposal of a part of banks' „bad" loans portfolios.

In the first half of 2013, the growth of corporate lending activity remained at a low level. It was caused by poor situation of the domestic economy and by uncertainty about its prospects. As a result, there was a lower economic activity of firms, limitation of investments expenditures, and also increased use of own funds when investing.

The savings of private sector remained the main source of banks' deposits in the first half of 2013. Their growth rate was close to that from 2012, but caused by significant increase in volume of current deposits, especially on savings accounts. In the analyzed period, a significant decrease of term deposits was recorded, being a result of lower interest rate on bank deposits, due to decrease of interest rates made by Monetary Policy Council (RPP). Other significant factors that could influence the moderate dynamics of individuals' deposits were: high unemployment rate and temporary improvement of situation on WSE. On the other hand, private deposits made by individuals were triggered by job loss fear and a low propensity to consume, which resulted in the higher propensity to save.

The first half of 2013 brought stabilization and then gradual improvement on the corporate deposits market. The reduction of corporate capital expenditures and increase in revenues from exports mainly due to the depreciation of the zloty, resulted in rise of corporate deposit activity. However, an incremental increase in the annual growth rate of corporate deposits in the period was a result of low base effect associated with large capital investment of one of the Polish mining companies, finalized in March 2012.

Table 3. Deposit volume of the banking sector

PLN billion, as at the end of the first half of 2013	30.06. 2013	31.12. 2012	30.06. 2012	Change	
Deposits from individual clients	**489.3**	**471.0**	**452.5**	**36.8**	**8.1%**
- current	239.4	205.6	208.5	30.9	14.8%
- term	249.9	265.4	244.0	5.9	2.4%
Deposits from corporate clients	**367.1**	**357.5**	**345.7**	**21.4**	**6.2%**
-non-banking financial institutions	50.7	56.2	50.4	0.3	0.6%
- deposits of business entities	240.7	239.6	228.5	12.1	5.3%
Enterprises	191.1	189.8	182.9	8.2	4.5%
individual entrepreneurs	23.3	25.4	21.7	1.6	7.4%
individual farmers	8.8	7.8	7.8	1.0	13.4%
Non-profit institutions	17.5	16.6	16.2	1.3	7.9%
- deposits from budget sector	75.8	61.7	66.8	9.0	13.4%
Deposits from non-banking clients	**856.4**	**828.5**	**798.2**	**58.2**	**7.3%**

Source: NBP, data for monetary financial institutions, excluding Central Bank and SKOK, only residents.

1.3. STOCK EXCHANGE TRENDS AND INVESTMENT TRENDS

A significant stratification between stock quotations of the largest companies, and small and medium enterprises (SME), was recorded in the first half of 2013. On one hand, the WIG20, the index of the largest companies decreased during the first six months of 2013 by 13% (which means that the gains recorded for entire 2012 were consumed), while on the other hand SME (represented by sWIG80 and mWIG40 indices) resisted to losses and increased (mWIG40 by nearly 9%, sWIG80 by more than 12%). The entire market, reflected by WIG index, ended the first half of the year with a loss of 5.7 %.

The events of the last two weeks of June highly influenced the first half of the year's performance. Firstly, the head of the FED announced the termination of the third round of financial loosening in the US, for which the main world stock exchanges reacted with a panic sale. Next, while the main world markets were making up their losses, in Poland a report was published about the influence of open-end pension funds (OFE) on the economy and initial variants of the pension scheme reform. The market reacted with substantial scepticism, which resulted in lack of significant gains and high volatility of Warsaw Stock Exchange.

On the market of Polish treasury bonds, the first half of 2013 was concluded with the termination of the rally on market that dominated the entire 2012 year. At the turn of the April and the May, the returns on Polish 10-year bonds were close to the level of the 3%, however, the June brought a strong rebound and increases in yields to above 4%.

Table 4. Value of main Stock Exchange indices

Index	30.06.2013	31.12.2012*	30.06.2012	Change Y/Y	Change in the 1st half of 2013
WIG	44 747	47 461	40 811	9.6%	(5.7%)
WIG20	2 245	2 583	2 275	(1.3%)	(13.1%)
mWIG40	2 776	2 553	2 300	20.7%	8.7%
sWIG80	11 716	10 444	9 520	23.1%	12.2%

**the last trading session on WSE in 2012 took place on 28.12.2012*
Source: WSE.

In the first half of 2013, 9 new companies joined the WSE, including 4 whose quotations were transferred from NewConnect. The number of WSE-listed companies increased from 438 at the end of December 2012 to 442 by the end of June 2013. The regulated NewConnect market had 28 new issuers in first half of 2013 (compared to 89 IPOs in 2012).

Table 5. Number of companies, capitalization and turnover on the WSE

	30.06.2013	31.12.2012	30.06.2012	Change Y/Y
Number of companies	442	438	434	1.84%
Capitalization of domestic companies (million PLN)	514 724	523 390	472 690	8.89%
Shares turnover volume (million PLN)	132 156	202 880	102 585	28.83%
Futures turnover volume (thousand units)	6 120	10 592	5 635	8.61%

Source: GPW

At the end of the first half of 2013, the Catalyst bond market quoted a total of 446 bond issues with the value of issues exceeding PLN 615 million.

2. COMPOSITION OF BGŻ S.A. GROUP AND METHODS OF THE REPORT CONSOLIDATION

As at 30 June 2013, Bank Gospodarki Żywnościowej S.A. Group (hereinafter referred to as 'the Group' or 'BGŻ S.A. Group') consist of Bank Gospodarki Żywnościowej S.A., the parent company (hereinafter referred to as 'the Bank' or 'BGŻ S.A.') and:

- Bankowy Fundusz Nieruchomościowy Actus Sp. z o.o. - the subsidiary,
- BGŻ Leasing Sp. z o.o - associated entity.

Table 6. Scope of consolidation

Entity name	Nature of the business	Shareholding of BGŻ S.A. in company's capital	Method of the consolidation/ valuation
Bankowy Fundusz Nieruchomościowy ACTUS Sp. z o.o.	Purchase and sale of real estate	100,0%	Full Method
BGŻ Leasing Sp. z o.o.	Leasing services	49,0%	Equity Method

3. IMPORTANT EVENTS IN BGŻ S.A. IN THE FIRST HALF OF 2013

24.02.2013	The Management Board was notified that Mr Jacek Bartkiewicz had handed in his resignation from serving as the President of the Management Board of Bank Gospodarki Żywnościowej S.A. effective 31 March 2013.
1.03.2013	The Management Board was notified that Ms Monika Nachyła had handed in her resignation from serving as the Member of the Management Board effective 1 April 2013. At the same time, the Supervisory Board appointed Ms. Monika Nachyła as Vice-President of the Management Board effective 1 April 2013 and entrusted the duties of the President of the Management Board. The resolution comes into force on the date of approval by the Polish Financial Supervisory Authority.
28.06.2013	The Supervisory Board overruled resolution from 1 March 2013 on appointing Ms Monika Nachyła as the President of the Management Board. Ms Monika Nachyła remained the Vice-President of the Management Board.

4. AUTHORITIES OF THE PARENT COMPANY

4.1. CHANGES IN THE COMPOSITION OF THE SUPERVISORY BOARD

The composition of the Supervisory Board in the period between 1 January and 28 June 2013 was as follows:

- Jan Alexander Pruijs – President of the Supervisory Board,
- Dariusz Filar – Vice-President of the Supervisory Board,
- Monika Nachyła – Member of the Supervisory Board (resignation on 1 March 2013),
- Evert Derks Drok – Member of the Supervisory Board,
- Jarosław Iwanicki – Member of the Supervisory Board,
- Harry de Roo – Member of the Supervisory Board.

On 28 June 2013, the Ordinary General Meeting of Shareholders, in relation to the expiry of terms of office, chose the Supervisory Board for the new term of office, and then the Supervisory Board at the meeting on the same day passed resolutions on selection of the President and the Vice-President of the Supervisory Board.

The composition of the Supervisory Board since 28 June 2013 is as follows:

- Jan Alexander Pruijs – President of the Supervisory Board
- Dariusz Filar – Vice-President of the Supervisory Board,
- Tanja Cuppen – Member of the Supervisory Board,
- Evert Derks Drok – Member of the Supervisory Board,
- Jarosław Iwanicki – Member of the Supervisory Board,
- Mariusz Warych – Member of the Supervisory Board.

4.2. CHANGES IN THE COMPOSITION OF THE MANAGEMENT BOARD

The composition of the Bank's Management Board in the period between 1 January and 30 June 2013 was the following:

- Jacek Bartkiewicz – President of the Management Board (resignation on 1 March 2013),
- Monika Nachyła – Vice-President of the Management Board acting as President of the Management Board (appointed on 1 April 2013),
- Gerardus Cornelis Embrechts – The first Vice-President of the Management Board,
- Magdalena Legęć – Vice-President of the Management Board,
- Johannes Gerardus Beuming – Vice-President of the Management Board,
- Dariusz Odzioba – Vice-President of the Management Board,
- Witold Okarma – Vice-President of the Management Board,
- Wojciech Sass – Vice-President of the Management Board,
- Andrzej Sieradz – Vice-President of the Management Board.

5. EXTERNAL RATING OF THE BANK

5.1. RATINGS

The Bank was rated by the Moody's Investors Service rating agency. At the end of June 2013, the long-term deposits rating of the Bank was Baa2, with a stable outlook. The Bank's Financial Strength Rating („BFSR") remained at the level „D" with a stable outlook. The rating of the Bank's short-term deposits was confirmed at Prime-2.

6. SHAREHOLDERS' STRUCTURE OF THE BANK

In the period between 1 January and 30 June 2013 there were no significant changes in Bank's shareholding.

Table 7. Shareholders' structure of the Bank

Shareholder	30.06.2013		31.12.2012	
	Number of shares	Share (%)	Number of shares	Share (%)
Rabobank International Holding B.V.	45 94 751	89.84	45 94 751	89.84
Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.	4 303 695	8.42	4 303 695	8.42
Other shareholders	891 318	1.74	891 318	1.74
TOTAL	**51 136 764**	**100.00**	**51 136 764**	**100.00**

7. FINANCIAL POSITION OF THE GROUP

7.1. CONSOLIDATED INCOME STATEMENT

In the first half of 2013, the Bank generated net profit of PLN 82 532 thousand compared with PLN 39 456 thousand in the first half of 2012. The increase of net profit by PLN 43 076 thousand (i.e. 109.2%) was mainly influenced by the decrease of net impairment losses on financial assets and contingent liabilities.

Table 8. Consolidated income statement

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Net interest income	481 572	502 261	(20 689)	(4.1%)
Net fee and commission income	130 100	148 182	(18 082)	(12.2%)
Dividend income	2 837	3 396	(559)	(16.5%)
Net trading income	48 751	39 992	8 759	21.9%
Result on investing activities	20 613	17 545	3 068	17.5%
Result on hedge accounting	(1 099)		(1 099)	-
Other operating income	16 026	17 063	(1 037)	(6.1%)
Net impairment losses on financial assets and contingent liabilities	(91 323)	(156 068)	64 745	(41.5%)
General administrative expenses	(443 892)	(454 672)	10 780	(2.4%)
Depreciation and amortization	(49 257)	(45 425)	(3 832)	8.4%
Other operating expenses	(8 848)	(17 787)	8 939	(50.3%)
Operating result	**105 480**	**54 487**	**50 993**	**93.6%**
Share in profit (loss) of associates	(1 314)	(892)	(422)	47.3%
Profit (loss) before income tax	**104 166**	**53 595**	**50 571**	**94.4%**
Income tax expense	(21 634)	(14 139)	(7 495)	53.0%
Net profit (loss) for the period	**82 532**	**39 456**	**43 076**	**109.2%**

Net interest income

In the first half of 2013, net interest income decreased by PLN 20 689 thousand, i.e. 4.1%, which was due to a decrease of interest income by PLN 9 509 thousand, i.e. 0.9%, while interest expense increased by PLN 11 180 thousand i.e. 2.1%. The dynamics of net interest income was particularly impacted by external factors as well as loans and deposits growth rate.

The most significant external factor was a decrease in NBP interest rates. During the period from May 2012, when the Monetary Policy Council terminated interest rates increase cycle continued since 2011, to June 2013 there have been seven interest rates reductions by 2.00 p.p. in total, including 1.50 p.p. reduction in the first half of 2013. There was another reduction by 0.25 p.p. in July 2013, which was expected by the market and had an effect on market interest rates already in June 2013.

Another significant external factor was coming into force of the Act on Payment Services on 24 October 2012, which partially refers to the disclosure obligation of a service provider with relation to a customer. The Act obliged service providers to inform customers about changes in framework agreements – including interest rates changes – two months in advance. As a result, banks extend the period of interest rates adjustment to NBP interest rates reductions in particular for savings accounts.

In the first half of 2013, the growth dynamics of loan portfolio of the Group continued to slow down to the level of 2.8% y/y as at 30 June 2013, whereas deposits increased by 10.6% y/y, which resulted in higher liquidity surplus of the Group.

The most significant position of interest income is interest income on loans and advances to customers which decreased by PLN 58 724 thousand, i.e. 8.2% y/y due to reduction of interest rates. The major part of loan portfolio is based on a floating interest rate. Considering the part of preferential loans, the decrease in interest income was strengthened by a multiplier effect (an interest rate is defined as NBP rediscount rate multiplied by 1.5 or 1.6). The effect is reduced by the Group through the application of hedge accounting since the second quarter of 2012, which comprised about PLN 3 billion of preferential loans (the total value of preferential loan portfolio was PLN 4.45 billion as at 30 June 2013).

The increase in interest income was also affected by higher income from debt securities by PLN 50 627 thousand, i.e. 35.5%. The increase resulted from the higher investment in debt securities financed from the Bank's higher liquidity surplus in comparison to the first half of 2012.

The increase of interest expense was mainly affected by increase in interest expense on amounts due to customers by PLN 12 398 thousand, i.e. 2.8% y/y. This was mostly determined by the growth of customer deposit base, in particular via internet banking BGŻOptima. The Bank's endeavors to reduce the interest expense increase were impeded by two-month statutory delay in the implementation of certain products price changes, which was described above.

Table 9. Net interest income

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Interest income	**1 024 100**	**1 033 609**	**(9 509)**	**(0.9%)**
Loans and advances to banks	19 054	21 061	(2 007)	(9.5%)
Loans and advances to customers in current accounts	142 429	150 851	(8 422)	(5.6%)
Loans and advances to customers	660 866	719 590	(58 724)	(8.2%)
Hedging instruments	8 622	(395)	9 017	(2 283%)
Debt securities	193 129	142 502	50 627	35.5%
Interest expense	**(542 528)**	**(531 348)**	**(11 180)**	**2.1%**
Amounts due to banks	(41 179)	(38 458)	(2 721)	7.1%
Debt securities issued	(48 578)	(52 517)	3 939	(7.5%)
Amounts due to customers	(452 771)	(440 373)	(12 398)	2.8%
Net interest income	**481 572**	**502 261**	**(20 689)**	**(4.1%)**

Net fee and commission income

Net fee and commission income for the first half of 2013 was lower by PLN 18 082 thousand, i.e. 12.2% in comparison to the first half of 2012. This was mainly due to a slower increase in fee and commission income (by PLN 16 524 thousand, which is 9.5% y/y) and an increase in commission expense (by PLN 1 558 thousand, i.e. 6.0%).

Decrease in net fee and commission income was a result of lower income from:

- loans and advances – as a result of slowdown of overdraft and loan commitment growths. In case of loan commitments, an additional factor, which limited income in the income statement, was commencement of settling them over time (further description of those changes can be found in Semi-annual Consolidated Report of Bank Gospodarki Żywnościowej S.A. Group in the note "Changes in accounting policies and changes in presentation of financial data").
- account maintenance – as a result of increasing payouts to „Konto z Premią" account holders (recognized as decrease in net fee and commission income of the Group)
- insurance activity – as a result of commencement of settling over time net fee and commission income from insurance activity related to creation of financial assets or liabilities (mainly cash loans insurance). Starting with financial statement for the 6-month period ending 30 June 2013, the item of net fee and commission income became integral part of effective interest rate and are recognized in income statement in net interest income.

Changes in accounting policies for net fee and commission income from loan commitments and sale of insurance products were introduced prospectively, i.e. without retroactive adjustment of previous financial statements, because of immaterial amounts.

Despite reduced interchange rates, fee and commission income on payment cards increased by PLN 2 897 thousand, i.e. 8.1%, mainly due to higher income from cards organizations for increased number of underlying transactions.

The increase of fee and commission expense was mainly affected by the increase in commission expense on payment cards (by PLN 3 268 thousand, i.e. 27.7% y/y) for card operators due to a higher number of issued cards and card transactions.

Table 10. Net fee and commission income

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Fee and commission income	**157 609**	**174 133**	**(16 524)**	**(9.5%)**
– loans and advances	46 864	55 064	(8 200)	(14.9%)
– settlements	8 557	10 259	(1 702)	(16.6%)
– account maintenance	42 554	49 527	(6 973)	(14.1%)
– guarantee commitments	5 669	5 677	(8)	(0.1%)
– brokerage operations	5 656	5 598	58	1.0%
– payment cards	38 778	35 881	2 897	8.1%
– insurance activity	5 306	9 656	(4 350)	(45.0%)
– other	4 225	2 471	1 754	71.0%
Fee and commission expense	**(27 509)**	**(25 951)**	**(1 558)**	**6.0%**
– loans and advances	(346)	(2 345)	1 999	(85.2%)
– payment cards	(15 068)	(11 800)	(3 268)	27.7%
– other	(7 100)	(5 722)	(1 378)	24.1%
– insurance activity	(4 995)	(6 084)	1 089	(17.9%)
Net fee and commission income	**130 100**	**148 182**	**(18 082)**	**(12.2%)**

Dividend income

In the first half of 2013, dividend income decreased by PLN 559 thousand, i.e. 16.5%. It was composed of the dividend on shares held by the Bank in the Krajowa Izba Rozliczeniowa - National Clearing House (KIR) and Biuro Informacji Kredytowej Credit Information Bureau S.A. (BIK) derived from the profits of these enterprises for 2012, approved by respective General Shareholders' Meetings. The dividend income from both KIR and BIK has decreased in comparison to the first half of 2012.

The net trading income for the first half of 2013 decreased by PLN 8 759 thousand, i.e. 21.9% y/y in comparison to the first half of 2012. This was mainly due to increase in valuation of IRS instruments held by the Group in order to hedge against interest rate risk. The change in valuation was caused by increase of interest rates at so called long end of interest rate curves near the end of the second quarter of 2013, in relation to expected upcoming termination of interest rates decrease cycle in Poland.

In the first half of 2013, the result on investing activities increased by PLN 3 068 thousand, i.e. by 17.5%, compared to the first half of 2012. The main component of this result was gains made on the portfolio of financial assets available for sale. A decision to sell them before maturity is made with consideration of needs arising from managing interest rate risk and in suitable market conditions, which in the first half of 2013 were shaped by lower profitability of long-term debt securities, following reduction of NBP rates.

Other operating income

In the first half of 2013, other operating income decreased by PLN 1 037 thousand, i.e. 6.1% compared to the first half of 2012, primarily due to decrease in other component of other operating income by PLN 1 874 thousand. This was affected by one-off occurred in the first half of 2012 – release of impairment allowances of non-current assets in the amount of PLN 2 516 thousand due to revaluation of real estate overtaken by the Bank for loan collateral.

Table 11. Other operating income

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Sale or liquidation of property, plant and equipment, intangible assets and assets held for sale	1 541	481	1 060	220.4%
Sales of goods and services	4 208	4 685	(477)	(10.2%)
Release of provisions for litigation and claims. and other liabilities	918	461	457	99.1%
Recovery of debt collection costs	999	1 202	(203)	(16.9%)
Other	8 360	10 234	(1 874)	(18.3%)
Total other operating income	**16 026**	**17 063**	**(1 037)**	**(6.1%)**

Net impairment losses on financial assets and contingent liabilities

In the first half of 2013, net impairment losses on financial assets and contingent liabilities improved by PLN 64 745 thousand, i.e. 41.5%. This was mainly due to lower allowances on loans and advances to LE segment (in the first half of 2012, the Group made significant allowances for one client from the construction industry), and retail loans (both mortgage and cash loans). However, impairment losses on loans and advances to SME and Micro segments (excluding farmers) have increased.

In December 2012, there was a change in the methodology of calculating impairment losses through collective method, as described in the consolidated annual financial statements. The change led to reversal of impairment in the amount of PLN 33 million at its implementation date and further reduction of net impairment losses in the first quarter of 2013. Additional factor positively impacting net impairment losses of loans was repayment of multiple-year overdue mortgage loans in the first quarter of 2013, which translated into improvement of parameters of the impairment calculation in relation to mortgage loans.

General administrative expenses and depreciation/amortization

General administrative expenses and depreciation/amortization in the first half of 2013 decreased by PLN 6 948 thousand, i.e. 1.4%, compared to the first half of 2012, which was primarily due to decreased marketing costs and other non-personnel expenses. In comparison to previous years, increase of the rest of expenses was significantly limited due to:

- Termination of branch development program at the end of first quarter of 2013. As at 30 June 2013, there were 402 branches, compared to 396 as at 30 June 2012. In the first quarter of 2013, 3 new branches were opened.
- Implementation of a number of saving initiatives under restructuring program which began in October 2012. As a result, as at 30 June 2013, the Group headcount totalled to 5 520 in comparison to 5 710 employees as at 30 June 2012 (decrease by 3.4% y/y). Restructuring program also included non-personnel expenses. Many deals with external services were renegotiated and resources were optimized.

Marketing costs decrease by PLN 12 568 thousand, i.e. 31.9% was due to limiting of expenses on marketing of deposits, in situation of lower demand on additional financing due to slower growth of lending activities.

Other non-personnel expenses decrease by PLN 5 179 thousand, i.e. 19.0% was achieved due to limiting of expenses on litigation and claims, cash transporting, bulk printing and loan database queries.

In the second quarter of 2013, the Group created an additional provision of PLN 2 370 thousand for severance payments related to further restructuring of employment in the first half of the year, which was recognized in social benefits and other fringe benefits. Another factor increasing personnel expenses in the first half of 2013, compared to the first half of 2012, was higher cost of provisions for unused holidays and retirement benefits (recognized in general administrative expenses since financial statements for the 6-month period ending 30 June 2013).

The increase in fees on the Bankowy Fundusz Gwarancyjny Bank Guarantee Fund (BFG) and the Polish Financial Supervision Authority, respectively by PLN 1 223 thousand and by PLN 517 thousand y/y was a consequence of the growth in balance sheet assets, being the basis for calculating fee to the PFSA, and the growth of the Bank's total capital requirements, which are the basis for calculating the annual fee for the BFG.

Table 12. General administrative expenses

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Personnel expenses, in this:	(245 855)	(241 591)	(4 264)	1.8%
- wages and salaries	(191 945)	(194 885)	2 940	(1.5%)
-social benefits and other fringe benefits	(53 910)	(46 706)	(7 204)	15.4%
Marketing	(26 788)	(39 356)	12 568	(31.9%)
IT	(38 480)	(36 950)	(1 530)	4.1%
Rental expenses	(46 076)	(46 662)	586	(1.3%)
Other non-personnel expenses	(22 060)	(27 239)	5 179	(19.0%)
External services	(47 031)	(47 012)	(19)	0.0%
Bank Guarantee Fund fee	(13 498)	(12 275)	(1 223)	10.0%
Polish Financial Supervision Authority fee	(4 104)	(3 587)	(517)	14.4%
Total general administrative expenses	**(443 892)**	**(454 672)**	**10 780**	**(2.4%)**
Depreciation and amortization	(49 257)	(45 425)	(3 832)	8.4%
Total	**(493 149)**	**(500 097)**	**6 948**	**(1.4%)**

Other operating expenses

In the first half of 2013, other operating expenses decreased by PLN 8 939 thousand (i.e. 50.3%) in comparison to the first half of 2012, primarily due to one-off provision for operating losses in one of the Bank's branches in the amount of PLN 4 582 thousand in the first quarter of 2012 (presented in Impairment charges on other receivables). Additionally, in the first half of 2013, the Group born significantly lower expenses on provision for litigation and claims, compared to the first half of 2012.

Table 13. Other operating expenses

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Sale or liquidation of property, plant and equipment, intangible assets	(1 106)	(592)	(514)	86.8%
Impairment charges on other receivables	(600)	(5 331)	4 731	(88.7%)
Provisions for litigation and claims, and other liabilities	(699)	(6 201)	5 502	(88.7%)
Debt collection	(3 630)	(3 327)	(303)	9.1%
Donations made	(1 375)	(1 380)	5	(0.4%)
Other	(1 438)	(956)	(482)	50.4%
Total other operating expenses	**(8 848)**	**(17 787)**	**8 939**	**(50.3%)**

7.2. CONSOLIDATED STATEMENT OF OTHER COMPREHENSIVE INCOME

In the first half of 2013, total comprehensive income of the Bank decreased to minus PLN 12 125 thousand, compared to PLN 88 044 thousand in the first half of 2012. It was mainly due to negative valuation of financial assets available for sale (i.e. portfolio of long-term treasury bonds) while in the first quarter of 2012 there was a positive valuation of those securities. The negative valuation of the available for sale financial assets in the first half of 2013 was a result of the change of market expectations referring to long-term interest rates (an increase of interest rates for long term securities).

In the first half of 2013, the positive change in fair value of cash flow hedges was also noted, being a result of applying hedge accounting effective from the second quarter of 2012. In particular, the Bank hedges the interest rate risk related to volatility of cash flows on preferential loans (interest rates are based on the NBP discount rate with a multiplier of 1.5 or 1.6) with the designated IRS transactions (float-to-fix). The cash flows related to the hedged items will occur during the period until April 2014.

Table 14. Consolidated statement of other comprehensive income

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Net profit (loss) for the period	**82 532**	**39 456**	**43 076**	**109.2%**
Net change in valuation of financial assets available for sale	(118 668)	54 735	(173 403)	(316.8%)
Net change in valuation of cash flow hedges	1 808	5 250	(3 442)	(65.6%)
Income tax expense on other comprehensive income	22 203	(11 397)	33 600	(294.8%)
Other comprehensive income (net of tax)	**(94 657)**	**48 588**	**(143 245)**	**(294.8%)**
Total comprehensive income for the period	**(12 125)**	**88 044**	**(100 169)**	**(113.8%)**

7.3. CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Assets

As at the end of the first half of 2013 the total value of the Bank's assets amounted to PLN 36 701 973 663 thousand and was by PLN 544 761 thousand, i.e. by 1.5 p.p. lower than at the end of 2012.

Then main factors for decrease of assets in the first half of 2013 were cash and balances with the Central Bank. In the analyzed period the balance of cash decreased by PLN 210 658 thousand, i.e. 24.3% as a result of optimizing actions which require the Bank to maintain the cash. The balances with the Central Bank decreased by PLN 548 023 thousand, i.e. 44.1%, whereas they are naturally under huge volatility because they are created by the current needs of the Bank to settle the obligatory reserve requirements.

The significant factors for decrease of assets were also loans and advances to customers, which diminished by PLN 354 864 thousand, i.e. 1.3%, mainly due to seasonal repayment of the part of liabilities by entities purchasing agricultural produce. Moreover on the market there was a decrease in the demand for credits by entrepreneurs, caused by uncertainty about the macroeconomic prospects, and more cautious investment plans, as a result.

Table 15. Assets

PLN thousand	30.06.2013	31.12.2012	Change	
			PLN thousand	%
Cash and balances with the Central Bank	1 347 978	2 106 657	(758 679)	(36.0%)
Loans and advances to banks	238 510	104 035	134 475	129.3%
Reverse repo transactions	249 837	104 369	145 468	139.4%
Debt securities held for trading	1 021 476	219 051	802 425	366.3%
Derivative financial instruments	322 529	380 473	(57 944)	(15.2%)
Hedging instruments	36 668	69 179	(32 511)	(47.0%)
Loans and advances to customers	25 968 836	26 323 700	(354 864)	(1.3%)
Available for sale financial assets	6 535 385	6 867 557	(332 172)	(4.8%)
Investment property	62 301	62 301	-	-
Investments in associates	44 816	46 139	(1 323)	(2.9%)
Intangible assets	148 235	152 674	(4 439)	(2.9%)
Property, plant and equipment	456 384	469 098	(12 714)	(2.7%)
Deferred tax assets	131 660	130 818	842	0,6%
Current tax assets	-	10 318	(10 318)	(100.0%)
Other assets	137 358	200 365	(63 007)	(31.4%)
TOTAL ASSETS	**36 701 973**	**37 246 734**	**(544 761)**	**(1.5%)**

Liabilities and Equity

At the end of the first half of 2013, the total value of the Group's liabilities equalled to PLN 33 241 164 thousand, and was lower by PLN 532 953 thousand, i.e. 1.6% in comparison to the end of 2012. The decrease concerned primarily amounts due to other banks and customers.

The amounts due to other banks decreased by PLN 441 872 thousand i.e.10.8% as a result of limited funding raised as interbank deposits, which was in line with the slowdown in lending activity of the Group. Moreover, the balance of loans received from other banks decreased, due to repayment of tranches in CHF loan to Rabobank – according to the repayment schedule.

The amounts due to customers decreased by PLN 264 086 thousand, i.e. 1.0% mainly as result of lower funding obtained from non-banking financial institutions in comparison to the temporary high balance of these sources, which was recorded at the end of 2012.

As at the end of the first half of 2013, the equity of the Group amounted to PLN 3 460 809 thousand and was lower by PLN 11 808 thousand, i.e. 0.3% than at the end of 2012. This resulted from the decrease of other reserve capital by PLN 94 657 thousand concerning lower revaluation reserve from financial assets available for sale described in the paragraph regarding the other comprehensive income of the Group. That factor outweighed increase of the equity which resulted from the appropriation of retained earnings (including the reclassification of the income for 2012 to the other supplementary capital).

Table 16. Total Liabilities and Equity

PLN thousand	30.06.2013	31.12.2012	Change	
			PLN thousand	%
Amounts due to other banks	3 652 564	4 094 436	(441 872)	(10.8%)
Repo transactions	224 639	32 341	192 298	594.6%
Financial liabilities held for trading	93 374	72 005	21 369	29.7%
Derivative financial instruments	278 696	326 215	(47 519)	(14.6%)
Amounts due to customers	26 677 885	26 941 971	(264 086)	(1.0%)
Debt securities issued	1 880 228	1 852 931	27 297	1.5%
Other liabilities	369 975	379 207	(9 232)	(2.4%)
Deferred tax liabilities	9 510	9 510	-	-
Provisions	54 293	65 501	(11 208)	(17.1%)
TOTAL LIABILITIES	**33 241 164**	**33 774 117**	**(532 953)**	**(1.6%)**
Share capital	51 137	51 137	-	-
Other supplementary capital	3 085 059	2 950 716	134 343	4.6%
Other reserve capital	235 694	330 351	(94 657)	(28.7%)
Retained earnings	88 919	140 413	(51 494)	(36.7%)
- from previous periods	6 387	10 364	(3 977)	(38.4%
- net profit for the period	82 532	130 049	(47 517)	(36,5%)
TOTAL EQUITY	**3 460 809**	**3 472 617**	**(11 808)**	**(0.3%)**
TOTAL LIABILITIES AND EQUITY	**36 701 973**	**37 246 734**	**(544 761)**	**(1.5%)**

7.4. LOAN PORTFOLIO QUALITY

The share of impaired receivables in gross amount of loans and advances to customers deteriorated from 7.1% at the end of 2012 to 7.9% at the end of first half of 2013. It was the result of the mortgage portfolio (the increase from 4.9% to 5.3% mainly due to loans from "the old portfolio" in foreign currencies) and portfolio for institutional clients excluding farmers (the increase respectively from 9.1% to 11.6%, mainly in SME and micro-segments). The increasing ratio of the impaired exposures corresponded with worsening macroeconomic background and the inhibition of portfolio growth observed in the first half of 2013.

However, the quality of other loans for retail clients has improved (decrease of the ratio from 16.0% to 14.9%) and loans for farmers (accordingly from 3.6% to 3.4%). The agricultural sector seems to be immune to economic downturn.

Table 17. Credit portfolio quality ratios

PLN thousand	30.06.2013	31.12.2012	Change	
			PLN thousand	%
Loans and advances to customers (gross)	**27 115 879**	**27 393 636**	**(277 757)**	**(1.0%)**
Impairment allowances (negative value)	(1 147 043)	(1 069 936)	(77 107)	7.2%
Loans and advances to customers (net)	**25 968 836**	**26 323 700**	**(354 864)**	**(1.3%)**
Losses incurred but not reported (IBNR)				
Gross exposure	24 964 957	25 457 786	(492 829)	(1.9%)
Impairment allowances on receivables assessed collectively with no impairment identified	(80 639)	(77 081)	(3 558)	4.6%
Net exposure	**24 884 318**	**25 380 705**	**(496 387)**	**(2.0%)**
Impaired exposures				
Gross exposure	2 150 922	1 935 850	215 072	11.1%
Impairment allowances on receivables assessed collectively and individually	(1 066 404)	(992 855)	(73 549)	7.4%
Net exposure	**1 084 518**	**942 995**	**141 523**	**15.0%**
Ratios:				
Share of impaired exposures in loan portfolio, gross	**7.9%**	**7.1%**		**0.9pp**
Impairment coverage	**49.6%**	**51.3%**		**(1.7pp)**

7.5. OWN FUNDS AND CAPITAL ADEQUACY RATIO

The capital adequacy ratio increased from 11.79% at the end of 2012 to 11.92% at the end of the first half of 2013. The equity increased by PLN 9 492 thousand, i.e. 32.4%, which was affected by the two divergent factors:

- inclusion of the net profit for the second half of 2012 in core capital, following an annual audit of the financial statement,
- decrease in fund from revaluation of tangible fixed assets (a decrease in unrealised income and the unrealised losses on debt instruments classified as available for sale); the mechanism of the decrease was described in the paragraph dedicated to other comprehensive income of the Group.

The decrease of the capital requirements by PLN 17 381 thousand i.e. 0.8% corresponded with the slump of lending activity of the Group, which resulted in the lower capital requirement for credits risk.

Table 18. Own funds and Capital Adequacy Ratio

PLN thousand	30.06.2013	31.12.2012	Change	
			PLN thousand	%
Principal funds	**3 257 583**	**3 166 673**	**90 910**	**2.9%**
– share capital	51 137	51 137	-	-
– other supplementary capital	3 085 060	2 950 716	134 344	4.6%
– other reserves capital	25 000	25 000	-	-
– prior period undistributed profit	6 386	10 364	(3 978)	(38.4%)
– general banking risk reserve	90 000	90 000	-	-
– net profit under authorization in the amount verified by the external auditors	-	39 456	(39 456)	(100%)
Deductions from the principal funds	**(193 220)**	**(176 290)**	**(16 930)**	**9.6%**
– intangible assets	(148 235)	(152 674)	4 439	(2.9%)
– unrealized losses on equity instruments classified as available for sale	-	(26)	26	(100%)
– unrealized losses on debt securities classified as available for sale	(22 577)	(121)	(22 456)	(18 558.6%)
–equity investments in financial institutions	(22 408)	(23 469)	1 061	(4.5%)
Principal funds after deductions	**3 064 363**	**2 990 383**	**73 980**	**2.5%**
Supplementary funds	**118 333**	**195 324**	**76 991**	**(39.4%)**
– unrealized gains on debt securities classified as available for sale	117 764	194 897	(77 133)	(39.6%)
– unrealized gains on equity instruments classified as available for sale	569	427	142	33.2%
Deductions from the supplementary funds	**(22 408)**	**(23 469)**	**1 061**	**(4.5%)**
– equity investments in financial institutions	(22 408)	(23 469)	1 061	(4.5%)
Short term funds	**26 117**	**14 674**	**11 443**	**78%**
Total Own funds	**3 186 404**	**3 176 912**	**9 492**	**0.3%**
Capital requirements				
– credit risk, counterparty risk, settlement-delivery risk	1 935 656	1 987 331	(51 675)	(2.6%)
- operating risk	187 120	163 165	23 955	14.7%
- general interest rate risk	15 236	4 896	10 340	211.2%
Total capital requirements	**2 138 011**	**2 155 392**	**(17 381)**	**(0.8%)**
Capital adequacy ratio (%)	**11.92%**	**11.79%**		**0.1%**

Financial ratios

In the first half of 2013, the Group recorded the improvement of return on equity and return on assets ratios compared to the first half of 2012, which resulted from the increase in net profit, because of lower net impairment losses on loans and advances.

Net interest margin decreased as a result of the reduction of interest rates and delayed possibility of adjustment of prices of some deposit products according to provisions of the Act on Payment Services.

The ratio of cost effectiveness (Costs/Revenues) slightly deteriorated due to decrease in revenues, especially from interest, and fee and commissions.

The decrease in credit risk costs ratio corresponded with lower amount of net impairment losses on loans and advances compared to the first half of 2012, when the Group made significant impairment allowance for a loan granted to an entity operating in the construction sector.

The financial ratios as loans/deposits and loans/total sources of funding decreased compared to the end of the first half of 2012, which reflects the decline of excess liquidity on the balance sheet of the Group as a result of adjustment of funding sources to lending activity.

Table 19. Financial ratios

	1st half of 2013	1st half of 2012	Change
Return on Equity (1)	4,8%	2,9%	1,9%
Return on Assets (2)	0,4%	0,2%	0,2%
Net interest margin (3)	2,5%	2,9%	(0,4%)
Costs / Revenues(4)	71,5%	70,4%	1,1%
Credit Risk Costs(5)	(0,7%)	(1,3%)	0,6%
Loans / Deposits(6)	101,6%	108,9%	(7,3%)
Loans / Total sources of funding(7)	84,7%	88,2%	(3,5%)

(1) Relation of the net profit to average shareholders' capital based on the balances at the end of the quarters (annualized).
(2) Relation of the net profit to average assets based on the balances at the end of the quarters (annualized).
(3) Relation of the net interest income to average assets based on the balances at the end of the quarters (annualized).
(4) Relation of the total of general administrative expenses, and depreciation and amortization to the total result on banking activities and other operating income and costs.
(5) Relation of net impairment losses on loans and advances to the average balance of loans and advances to customers based on the balances at the end of the quarters (annualized).
(6) Relation of gross loans and advances to customers to amounts due to customers based on the balances at the end of the period.
(7) Relation of gross loans and advances to customers to the total amounts due to customers, debt securities issued and loans from other banks. Balances at the end of the period.

8. BANK OPERATIONS IN 2012

8.1. DISTRIBUTION CHANNELS

8.1.1. TRADITIONAL CHANNELS

Branches

In the first quarter of 2013, the Bank finished to expand its network of branches. The branch expansion policy started in 2008 in connection with the implementation of a strategy to develop local market growth. In the final stage of the project (2012-2013) new branches were opened in towns, where BGŻ S.A. outlets already existed: Białystok, Bydgoszcz, Toruń and Lublin. The objective of this strategy was to increase the Bank's share in terms of number of branches on a given micro market.

In the first half of 2013, 3 subordinated branches were opened. Based on analysis of financial results and location potential, 1 subordinated branch was liquidated, 1 subordinated branch was relocated and 1 operating branch was transformed into a subordinated branch. In addition, 1 external cash desk was liquidated.

As at 30 June 2013, the Bank had 402 branches of retail and business banking, of which 119 were operating branches and 283 subordinated branches (compared to 120 operating branches and 280 subordinated branches as at 31 December 2012). The network of branches was supplemented by 13 external cash desks, which service cash transactions.

Reorganization

Since 1 January 2013, the Bank launched 10 Centres of Investment Products Service (COPI), which provide the full service of investment products offered by The Brokerage Office of BGŻ (brokerage accounts, stock market orders, intermediation of derivative securities transactions, private placements and public offerings, open-end investment funds).

Since 1 April 2013, a significant change in the organizational structure of the Bank has been made comprising implementation of a clear division of responsibilities between the areas of retail and business, and corporate banking. As a result the Bank's structure was divided into 9 Business and Retail Banking Regions comprising operating and subordinated branches, and 6 Corporate Banking Regions including 44 Business Centres of Small and Medium Enterprises, 6 Business Centres of Large Enterprises (LE) and 1 International Desk Warsaw Business Centre.

Business Centre of Large Enterprises - performs tasks from the scope of the sale of products and banking facilities offered to Customers from the LE section, including: the process of acquiring Clients, defining their needs and preparing the offer, establishing conditions for cooperation with the Client for particular bank products and signing relevant agreements. The Business Centre is responsible for the realization of the planned financial result and increase in the number of Customers from the LE section.

Business Centre of Small and Medium Enterprises - performs tasks from the scope of the sale of products and banking facilities offered to customers of the Small and Medium Enterprises section, including: the process of acquiring Clients, defining their needs and preparing the offer, establishing conditions for cooperation with the Client for particular bank products and signing relevant agreements. The Business Centre is responsible for the realization of the planned financial result and increase in the number of customers in the SME section.

International Desk Warsaw Business Centre - performs tasks from the scope of the sale of products and banking services offered to Dutch corporate customers (irrespective of the section, to which the customer is categorized), including: the process of acquiring Clients, defining their needs and preparing the offer, establishing conditions for cooperation with the customer for individual bank products and signing relevant agreements.

The operational service of Clients from Large Companies as well as Small and Medium Enterprises segments is still carried out through the Bank's branch network.

ATM network

As at June 30, 2013, the network of ATMs available to the Bank's retail customers for commission-free cash withdrawals, comprised, apart from Bank's own network, ATMs of the Euronet and PlanetCash4You networks (automatic teller machines labelled as „Automatic teller machine available to BGŻ customers for commission-free cash withdrawals").

At the end of June 2013, retail customers of the Bank could make commission-free cash withdrawals at 4 387 ATMs, of which 425 were operated by BGŻ S.A. Customers holding a *Konto Plus* personal account could make commission-free cash withdrawals in all ATMs in Poland. Owners of the *Plan Aktywny* and *Konto bardzo osobiste* personal accounts could use all automatic teller machines both in Poland and abroad for commission-free cash withdrawals. Institutional Clients holding *Plan Agro Lider* and *Agro Lider Prestiż* accounts could use all ATMs in Poland for commission-free cash withdrawals.

8.1.2. ALTERNATIVE CHANNELS

Internet banking

In first half of 2013, the Bank recorded a dynamic growth in the number of customers using internet service eBGŻ (retail clients) and eBGŻ Firma (institutional clients). The number of operations executed using the internet channel increased systematically.

Table 20. Data related to eBGŻ

		30.06.2013	31.12.2012	30.06.2012	Change y/y	
Number of customers accessing	eBGŻ	385 099	350 228	315 951	69 148	21.89%
	eBGŻ Firma	78 967	70 079	61 638	17 329	28.11%
Number of active customers logging	eBGŻ	251 688	228 742	202 892	48 796	24.05%
	eBGŻ Firma	47 977	43 149	38 310	9 667	25.23%
The average monthly number of transactions	eBGŻ	1 106 593	963 788	866 857	239 736	27.66%
	eBGŻ Firma	974 017	854 009	775 195	198 822	25.65%

In January 2013, the process of enhancing authentication method in the Internet banking services to retail customers has been automated. Additionally, the Bank has waived the requirement to change the password every 180 days, giving to customer the freedom to manage the frequency of changing internet banking passwords.

In order to streamline the process of logging into the eBGŻ service, this process was shortened by reducing the number of steps/screens while logging into the service.

At the end of February 2013, in relation to the decision of the Bank to withdraw lists of one-time passwords with effect from 1 April this year, the functionality of the eBGŻ service was adapted for the migration process of customers with the lists of one-time passwords to SMS codes.

In the first quarter of 2013, in eBGŻ Firma system, the preview of details of account blockades was made available, including the ones on account of closed payments, foreign orders and card operations.

Phone-banking

In the first half of 2013, a further increase by 95 735 i.e. 21%, in the number of Tele-banking retail and institutional users was recorded in comparison to the end of first half of 2012.

Table 21. Data related to Tele-banking

		30.06.2013	31.12.2012	31.12.2011	Change y/y	
Number of customers with the Access to TeleBGŻ	Retail customers	423 103	388 910	326 843	62 067	19%
	Institutional customers	122 360	109 515	82 149	27 366	33%
An average number of incoming and outcoming calls per month		186 868	171 355	170 901	15 967	9%

At the beginning of 2013, the Communication Centre of BGŻ Bank was expanded with the retention area and the after-sales customer service. Additionally, in the course of developing sales via direct channels, the remote sale of cash credits by the courier was launched.

Based on cyclically collected opinions of customers on the subject of the service in the area of the phone-banking, the Bank carried out actions improving the level of customer service quality for retail and institutional clients via the phone-channel.

Furthermore consultants of the Communication Centre took an active part in the handling of after-sales processes of customers of the Bank, as well as offered the assistance for eBGŻ users in the scope of: sale of investment funds and replacing authorization tools to SMS codes.

Banking cards

The portfolio of payment cards includes debit cards, credit cards and cards with deferred payment. The Bank issues debit, credit and deferred payment cards in MasterCard and Visa -systems. As at 30 June 2013, the number of debit card issued to clients was 622 900 and was nearly 11 000, i.e. 1.8%, higher than in the previous year. This increase was mainly due to issuance of credit cards to retail clients (an increase of 4 300, i.e. by 8%) and debit cards to business clients (an increase of 3 600, i.e. by 6%).

Table 22. Number of banking cards issued by BGŻ S.A.

Thousands units	30.06.2013	31.12.2012	30.06.2012	Change y/y	
Retail customers debit cards	499.9	512.6	496.9	3	0.6%
Retail customers credit cards	58.4	56.0	54.1	4.3	8.0%
Business debit card	63.1	61.7	59.5	3.6	6.1%
Business cards with deferred payments	1.5	1.6	1.6	(0.1)	(6.3%)
Total number of banking cards issued	622.9	631.9	612.1	10.8	1.8%

The Bank consistently promoted non-cash transactions made with payment cards. Customers using MasterCard credit cards are awarded the bonus constituting the part of the expenditure paid with the card, and Customers of the *Konto z Premią* obtain the bonus constituting the 1% of the remuneration transferred to an account, provided they make non-cash expenses with card in amount determined by the regulations of the promotion. In turn, the holders of Visa cards were encouraged by the Bank to pay with their cards for an everyday, even little shopping. Visa prepared the special promotion for its customers. The Bank's policy on credit cards has resulted in their award in the ranking prepared by the financial portal Money.pl in March 2013. A card MasterCard Gold earned the 2nd place in the category of gold credit cards, and a card MasterCard Standard took 3rd place in the ranking of silver cards.

In May the Bank extended the offer of debit cards for retail clients by the product for customers from the Personal Banking section.

Cooperation with intermediaries

At the end of the first half of 2013, the Bank actively collaborated with 24 network intermediaries, such as Open Finance, Notus and Expander and also with 83 local agents. The cooperation was based on the active sale of banking products. Direct supervision over all cooperation agreements (both with network-based and local) was performed by the Bank's Head Office.

In this period the Bank introduced some changes to its policies of collaboration with financial intermediaries. The Bank terminated the cooperation with intermediaries in the respect of active sale of banking products offered to institutional clients from SME segment. The products dedicated to retail clients and institutional clients form Microenterprises segment, so far provided with the financial intermediation, remained the object of the active sale. The process of annexing of cooperation agreements in order to withdraw the active sale of products dedicated to SME segment is managed by the Bank's Head Office.

In this period, there was carried on a policy of central monitoring how the intermediaries fulfil their agreements of collaboration. The evaluation concerned sale effects, as well as a quality of the credit portfolio provided by intermediaries. These actions resulted, among others, in the termination of 84 contracts during first half of 2013.

8.2. RETAIL BANKING

8.2.1. PRODUCT OFFER DEVELOPMENT

In the first half of 2013 *Konto z Premia* account was modified. At the end of May, the Bank introduced new regulations for bonuses, maintaining the privileges only for the clients, who transfer to the account their salary, the disability pension or the retirement pension, and who plan to maintain relationship with the bank in the future – using also other products, such as term deposits, saving accounts or loans.

In terms of deposit offer the changes concerned primarily interest rates, because of the need to adapt to falling interest rates set by the Monetary Policy Council. The Bank's offer extended by four special promotional term deposits addressing both acquisition and retention targets, a new edition of the progressive term deposit and insurance *Zysk pod ochroną*, which in addition to the principal guarantee and fixed interest rate, provide benefits in case of unexpected events in the customer life. New offers, like 12 month progressive term deposit, also aim at customer saving period extension.

In the situation of declining interest rates paid on traditional deposits, the offer has been expended by a number of investment deposits. They offer a principal guarantee and additionally, in contrary to traditional deposits, provide a satisfactory return on investment. Five different subscriptions of this product have been offered since the beginning of the year.

Introduced at the end of 2012, the Personal Banking offer contributed in the first half of 2013 to the building of a base of active affluent clients, treating BGŻ as their first banking choice. At the end of June the Bank was operating more than 9 000 accounts for the affluent clients. As a part of the service of the Personal Banking, customers benefit from the personal advisor, attractive package of the *Konto Bardzo Osobiste* account enabling to use all transaction services without extra charges, as well as new form of depositing cash flows - Automatic Saving Account.

In the area of credit products, a strategy of delivering profitable and safe credits dedicated both to customers of the Bank and to new clients was being carried. The Bank pays the highest attention to measures, which improve the credit processes and optimize the credit risk.

8.2.2. BGŻOPTIMA

The BGŻOptima serves as a supplement to the Bank's offer with regards to saving and investment products, and is dedicated to clients who wish to use Internet-based services. The BGŻOptima offer comprises deposits, saving accounts and distribution of open-end investment funds participation units. In the first half of 2013, the Bank's offer has been consistently expanding in the area of deposit and investment products. In March 2013, the offer of BGŻOptima was extended to include a new Investment Fund Managing Company (TFI) and 5 subfunds. As at 30 June 2013, the number of clients serviced by BGŻOptima amounted to 103 700, which means that from the beginning of 2013, 27 200 new clients were acquired.

8.2.3. DEPOSIT ACTIVITIES

As at 30 June 2013, the value of retail deposits held by the Bank amounted to PLN 16 349 654 thousand and was nearly PLN 1 852 322 thousand (12.8%) higher than one year before and PLN 547 234 thousand (3.5%) higher than as at 31 December 2012. BGŻOptima continued to be the main growth factor of retail deposits.

Table 23. Volume and structure of retail deposits

PLN thousand	30.06.2013	31.12.2012	30.06.2012	Change in the 1st half of 2013		Change y/y	
Current and savings accounts	10 869 480	8 439 404	7 780 093	2 430 076	28.8%	3 089 387	39.7%
Term deposits	5 469 447	7 351 820	6 708 824	(1 882 373)	(25.6%)	(1 239 377)	(18.5%)
Other liabilities	10 727	11 196	8 415	(469)	(4.2%)	2 312	27.5%
Amounts owed to retail customers, total	**16 349 654**	**15 802 420**	**14 497 332**	**547 234**	**3.5%**	**1 852 322**	**12.8%**
including: BGŻOptima	**3 914 748**	**3 375 643**	**2 425 448**	**539 105**	**16.0%**	**1 489 300**	**61.4%**

The BGŻ S.A. branches acquisition targets in the area of retail deposits are focused on obtaining new personal accounts and maintaining deposit volumes despite decreasing interest rates. Since the end of June 2012, there was 3.5% growth in deposits, an increase by PLN 547 234 thousand. The increase in the volume of retail deposits was achieved mainly through personal accounts and saving accounts. The Automatic Saving Account offered to Personal Banking clients significantly contributed to the development of the volume of affluent clients' deposits. The balance of this product at the end of June reached PLN 465 million.

The Bank recorded a dynamic increase in the funds accumulated on personal accounts. As at 30 June 2013 its balance amounted to PLN 2 234 million compared to PLN 1 901 million as at 30 June 2012 (increase of PLN 332 million, i.e. 17.5% y/y) which is a result of, among others, the regular activation campaign on personal accounts portfolio and the main active sale offer *Konto z Premią*. *Konto z Premią* owners are awarded financial bonuses for remuneration transfer and non-cash payments with credit cards.

The number of personal accounts as at the end of June 2013 amounted to 626 000 thousand, which translates into a growth of 26.1 thousand (4.4%) and compared to respective period of the previous year it increased by 36.8 thousand (6.5%). *Konto z Premią,* with its 70% share in sales, remained unquestionably the most popular among all types of personal accounts. Positive sales results were also achieved thanks to advertising campaign. *Konto z Premią,* among others, was awarded the first place in the ranking of best personal accounts prepared by the Money.pl portal in 2013, which confirms high attractiveness of this offer.

Table 24. Number of retail deposits accounts

Number of items (In thousands)	**30.06.2013**	**31.12.2012**	**30.06.2012**	**Change in the 1st half of 2013**		**Change y/y**	
Number of deposits accounts in branches	**1 393.9**	**1 533.4**	**1 486.1**	**(139.5)**	**(9.1%)**	**93.3**	**6.5%**
A 'vista accounts, including:	1 166.7	1 250.5	1 216.7	(83.8)	(6.7%)	98.4	8.5%
Personal accounts	626.0	601.3	578.2	24.7	4.1%	36.8	6.5%
Saving accounts	262.8	251.7	233.5	11.1	4.4%	40.0	18.9%
Term deposits accounts	227.2	282.9	269.3	(55.7)	(19.7%)	(5.1)	(1.8%)
Number of savings accounts in BGŻOptima	**115.1**	**83.9**	**59.6**	**31.2**	**37.2%**	**45.4**	**117.9%**

8.2.4. LENDING ACTIVITIES

In the first half of 2013, lending activities were aimed at increasing profitability of credit products as well as systematic building of the Bank's market share in the retail loan market.

At the end of June 2013, the volume of the retail gross loan portfolio amounted to PLN 9 336 819 thousand and was PLN 362 041 thousand, i.e. 4% higher than as at the end of December 2012, and PLN 567 162 thousand higher than as at the end of June 2012. The main growth factors included: sale of cash loans, housing loans and credit cards.

In the beginning of 2013 an innovative housing loan with fixed interest rate in the first 5 years of credit period was introduced into offer. This new solution provides customers with guarantee of financial security. Simultaneously, as part of the introduction of the PFSA recommendation, the Bank implemented more restrictive lending rules, in particular regarding assessing the credit rating, lowering the maximum LTV indicator and shortening the maximum credit period. In conjunction with reduced propensity of individuals to long term debt, due to difficult economic situation, the sale of PLN housing loans in the first half of 2013 was lower than in the respective period of the previous year and amounted to PLN 459.9 million (decrease of 287.8 million, i.e. 38.5%).

Table 25. Volume and structure of retail loans

PLN thousand	30.06.2013	31.12.2012	30.06.2012	Change in the 1st half of 2013		Change y/y	
Current account loans	96 231	107 615	117 790	(11 384)	(10.6%)	(21 559)	(18.3%)
Housing loans	7 892 242	7 600 490	7 392 994	291 752	3.8%	499 248	6.8%
– in PLN	4 680 710	4 412 921	3 952 628	267 789	6.1%	728 082	18.4%
– in foreign currencies	3 211 533	3 187 570	3 440 366	23 963	0.8%	(228 833)	(6.7%)
Cash loans	896 939	803 967	781 264	92 972	11.6%	115 674	14.8%
Credit card limits	79 772	70 659	61 844	9 112	12.9%	17 928	29.0%
Other loans to retail clients	371 636	392 047	415 765	(20 411)	(5.2%)	(44 129)	(10.6%)
Total loans to retail clients	**9 336 819**	**8 974 778**	**8 769 657**	**362 041**	**4.0%**	**567 162**	**6.5%**

Despite weaker market outlook and severe competitive pressure, the Bank recorded in the first half of 2013, cash loan sales growth to the level of PLN 363.4 million, i.e. PLN 108.3 million (42.5%) more than in the first half of 2012. Positive sales numbers resulted from the presence of the product in advertising campaigns in television, radio and on the Internet. Cash loans offered by the Bank have gained recognition, both from customers and banking environment, and earned an award from prestigious banking portal.

The Bank also implemented a sequence of functional changes in the cash loans offer, widening the accessibility of the product for customers, including an offer of 72-month loan insurance and increase of insurance coverage amount up to PLN 100 thousand for affluent customers covered with Personal Banking services.

At the end of June the volume of cash loans reached PLN 896 939 thousand, and was 11.6% higher than as at the end of 2012. Therefore it was one of the fastest increasing sections of the Group's loan portfolio.

Table 26. Number of retail credit accounts

Number of items (in thousands)	30.06. 2013	31.12.2012	30.06.2012	Change in the 1st half of 2013		Change y/y	
Mortgage, housing and consolidation loans	55.6	53.3	51.1	2.3	4.3%	5.0	10.4%
Cash loans	98.7	92.4	86.4	6.3	6.8%	9.7	11.7%

The highest annual percentage increase of volume at the end of June 2013 was recorded for credit cards. The value of the portfolio amounted to PLN 79 772 thousand and was higher by PLN 17 928 thousand, i.e. 29% compared to the previous year. In the same period, the number of issued credit cards increased by 4.3 thousand, i.e. 8% to the level of 58.4 thousand. The active sale of new Visa Standard card, launched in Q1 2013, contributed to this sharp increase.

8.3. BROKERAGE SERVICES AND DISTRIBUTION OF PARTICIPATION UNITS IN INVESTMENT FUND MANAGING COMPANIES (TFI)

The Brokerage House of the Bank („BM BGŻ" or the "Brokerage House") focuses on retail client services. The offer of rendered services supplements the Bank's offer in the area of investment products. The Brokerage House also provides services to selected institutional clients such as open-end pension funds (OFE), investment fund managing companies (TFI) and other entities managing entrusted assets.

Brokerage fee income in the first half of 2013 amounted to PLN 1 928.3 thousand, compared to PLN 2 712.4 thousand in the first half of 2012. The decrease in brokerage fee income and number of brokerage accounts, as is detailed below, was caused mainly by the reorganization of brokerage service, including, among others, termination of rendering brokerage services by 20 out of 30 branches, economic slowdown, as well as clients' structure. The Brokerage House renders services mainly to domestic investors, including, in particular, individual investors, whose share in the trading volume has continued to decrease in recent years.

At the end of the first half of 2013, the Brokerage House maintained 30 999 brokerage accounts (of which 5 257 internet accounts maintained in the bmBGŻ.net transaction system), which, compared to 32 033 accounts at the end of 2012, equalled to 3.2% decrease.

Table 27. Share of the BGŻ Brokerage Office in trading on the WSE

		30.06.2012		30.06.2013	
		Market share	Volume	Market share	Volume
Stock	PLN million	0.16%	368.89	0.26%	514.34
Bonds	PLN million	0.24%	5.02	0.04%	0.44
Futures	Number of contracts	0.62%	73 941	0.46%	50 492
Investment certificates	PLN million	3.00%	1.36	4.26%	2.65
Options	Number of contracts	0.26%	2 031	0.25%	1 422

At the end of June 2013, the Brokerage House distributed participation units in 66 funds managed by 6 investment fund managing companies (Union Investment TFI, Aviva Investors Poland TFI, Skarbiec TFI, Opera TFI, BPH TFI, Quercus TFI). The product offer of the Brokerage House comprises a variety of participation units in investment fund managing companies, encompassing so-called safe funds (bond and money market funds), balanced and stable growth funds as well as funds of aggressive investing policy (equity funds).

In the first half of 2013, revenues from the sale of participation units amounted to PLN 3 724.4 thousand compared to PLN 2 885.6 thousand in the first half of 2012.

Following an increase in the value of acquired participation units, an increase was recorded in the value of assets acquired by BGŻ S.A. As at 30 June 2013, the value of those assets amounted to PLN 750.9 million compared to PLN 611.2 million at the end of 2012.

Brokerage House acts as an intermediary on the OTC market organised by BondSpot S.A. The Brokerage house has been an active participant in the alternative NewConnect trading system since 2007.

In the first half of 2013, Brokerage House participated in 5 public offerings in the primary market. In case of 3 IPO's, the Brokerage House acted as an offering agent and hence participated at each stage of both the preparation and execution of the offer and as the offering organiser.

8.4. INSTITUTIONAL BANKING

8.4.1. CLIENT SEGMENTATION

Until 31 March 2013 **Institutional Clients of the Bank were allocated to the following segments:**

- Large Enterprises (LE) – the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act, with annual sales revenues of more than PLN 60 million,
- Small and Medium-Sized Enterprises (SME) – the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act, with annual sales revenues of less than PLN 60 million,
- Microenterprises (Micro) – the entrepreneurs who do not conduct the full financial reporting according to Polish Accounting Act.

As part of those segments, additional sub-segments were identified for agro and non-agro clients, farmers, the public sector, non-profit organisations, key clients and financial institutions.

On 1 April 2013 new rules of Client segmentation were introduced. The criteria of Institutional Client classification for LE, SME and Micro segments have changed. According to the new Client segmentation, Institutional Clients of the Bank are allocated to the following segments:

- Large Enterprises (LE) – the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act, with annual sales revenues for the previous financial year of PLN 60 million or more, or with credit exposure to the Bank of PLN 25 million or more,
- Small and Medium-Sized Enterprises (SME) – the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act, with annual sales revenues for the previous financial year ranging from the PLN 10 million to PLN 60 million, or with credit exposure to the Bank ranging from the PLN 2 million to PLN 25 million,
- Microenterprises (Micro) – the entrepreneurs who do not conduct the full financial reporting according to Polish Accounting Act and the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act with annual sales revenues for the previous financial year of less than PLN 10 million or with credit exposure to the Bank of less than PLN 2 million

As part of those segments, additional sub-segments were identified for agro and non-agro clients, farmers, the public sector, non-profit organisations, key clients and financial institutions.

8.4.2. PRODUCT OFFER DEVELOPMENT

Product packages and transaction products

Micro segment

In April 2013 the Bank withdrew *Biznes Lider Plus* package from the offer. At the same time the Bank prepared a modified package offer, which was introduced on 1 August 2013.

The following product packages were modified and included in the offer:

- *Biznes Lider* package – the package dedicated to Micro Non-Agro and Micro Agro clients, with basic product needs,
- *Biznes Lider Aktywny* package – the package dedicated to Micro segment clients with needs of advanced product and attractive offer,
- *Agro Lider* package – the package dedicated to natural persons from Micro Farmer sub-segment, with basic product needs,
- *Społeczny Lider* package – the package dedicated to Non-Profit sub-segment clients with needs of basic product with very competitive pricing offer,

On 1 August the Bank withdrew *Biznes Lider Prestiż* and *Agro Lider Prestiż* packages from the offer.

The product package offer was constructed in a way to ensure that within one agreement a client could acquire many products at one price and, at the same time, had a possibility to acquire other products and services offered by the Bank at preferential prices and with no additional formalities. The main products included in the packages are: current accounts in PLN, phone banking, eBGŻ, deposits and term deposits. In the *Biznes Lider Aktywny* package, apart from the basic products from packages for Micro segment clients, there are included depending on the type of the package: Euro currency accounts, debit cards, individually negotiated deposits and foreign currency transactions. Additionally, the possibility of using a lump sum fee for making internet transfers to other banks was opened. During the period from 1 January 2013 to 8 June 2013 the Bank acquired 12 798 new Micro segment clients. Compared to the corresponding period of 2012, in 2013 the Bank attracted 984 more new clients.

SME and LE segments

On 15 April 2013 the Bank launched the new process of opening a bank account along with the comprehensive agreement on Cash Management products for Corporate Clients (SME and LE). The purpose of the implementation of the new process is to reduce the time to prepare the agreement and simplify the agreement documents. The comprehensive agreement provides the Client within one framework agreement, access to basic Cash Management products, such as settlement accounts, deposits, access to electronic banking, the ability to conduct foreign exchange transactions, access to payer identification services (IDEN), and the ability to use debit cards. Additional products are launched after the Customer files the relevant application, without the need to sign an annex.

At the same time, along with the comprehensive agreement, the Schedule of Fees and Charges for Corporate Clients was introduced. The schedule apart from simplified content includes only an offer for Corporate segment. The new Schedule introduces 3 new tariff plans:

- Standard – the plan dedicated to SME and LE segments, it enables the individual pricing decisions
- *e-Biznes Lider Prestiż* – plan dedicated to SME segment as Internet package i.e. cheap operations conducted via electronic channel, and more expensive operations conducted in branches
- *Agro Lider Prestiż* – the plan dedicated to Farmers, offering among others the cheap operations in branches

On 1 June 2013 the Bank introduced the process of client migration to comprehensive agreements mentioned below**.** The strategic objective of these activities is to increase fee income and maintain the interest income at the same level.

Credits

Micro segment

In April 2013, due to changes in the offer of Packages for Micro segment customers and withdrawal of *Biznes Lider Plus* package from the Bank's offer, credit product in the form of current account overdraft facility was withdrawn.

LE and SME segments

In the first half of 2013, neither new credit products for LE and SME segment customers were introduced, nor changes were made in the principles of credit products already offered by the Bank.

Agribusiness financing

In March 2013, new product was introduced for the clients, i.e. Investment Loan granted from EIB funds. In the case of this loan, the main advantage for the borrower is a margin at least 0.30 percentage point lower compared to loans granted by the Bank without EIB support. The loan can be qualified to the EIB line under condition that an application to put the funds aside is filled and it is accepted by the Asset-Liability Committee.

Since 6 June 2013 there was introduced a leasing for projects in the area of Polish Sustainable Energy Financing Facility (PoLSEFF). The rules of obtaining the funds are the same as the ones referring to investment loan.

The Agreement of the *de minimis* warranty line of the portfolio was signed with Bank Gospodarstwa Krajowego on 6 June 2013. The *de minimis* guarantee offers the collateral of repayment of a loan dedicated to current business financing, and is offered on preferential terms. Clients of the Bank will be allowed to apply for a *de minimis* warranty while they will apply for an overdraft facility, credit facilities and revolving loan. The warranty could also include renewed credit agreements concerning credit facilities. In case of growing value of non-revolving credit, the warranty could include the value, which increases that credit. Creditworthy clients from SME sector could be granted the *de minimis* warranty.

The de minimis warranty of BGK does apply to entities in the field of primary production, processing and placing on the market agricultural products, fishery, aquaculture and coal sector. The main benefits for the customer are: the minimum of formalities while obtaining BGK warranty; the opportunity to be granted with the higher loan value than in the standard offer; the lack of fees for the first year of BGK warranty; the opportunity to be granted the loan even if there are no material collaterals or existing ones are not sufficient.

8.4.3. LENDING ACTIVITIES

Micro segment

In the first half of 2013 the Group recorded a slowdown in lending to institutional clients. As at 30 June 2013 value of gross loan portfolio amounted to PLN 17 779 060 thousand and decreased by PLN 639 798 thousand compared to 31 December 2012. In comparison with the end of the first half of 2012, the Group recorded a slight increase in lending amounting to PLN 267 248 thousand, i.e. 1.5%.

The following factors influenced the decrease of volume of loans in the first half of 2013:

- market situation – reduced propensity of enterprises to run into debt due to economic slowdown, both in case of financing investment activities and working capital,
- Bank's industry policy – identifying high-risk industries and determining tightening of credit conditions for entities operating in these sectors.
- handling of the Bank's loan portfolio quality taking into consideration economic slowdown, in effect of which acquisition of new credit exposures became limited, while in case of clients who are in poor financial standing or in high-risk sectors (especially in case of Large Enterprises sector) the "exit" strategy was executed.

Compared to clients from non-agro-food sector, the loan portfolio growth dynamics for farmers was relatively high (double digit). It concerned both loans in the current account represented by *Agro Ekspres* loan, and in the loan account, with dominant position of preferential loans. The factor which reduced the dynamics of the second portfolio in the first half of 2013 was low limit level set to banks compared to the same period last year. It resulted in exhaustion of lending activities at the beginning of May 2013 and necessity of suspending lending activities. At the end of June, new lending activities were launched thanks to the effort of banking environment and organizations financing agriculture. Despite the problems with obtaining limit on preferential loans from The Agency for Restructuring and Modernization of Agriculture, the portfolio was still growing both in the first half of 2013 and also compared to the previous year.

Table 28. Loans and advances to institutional customers

PLN thousand	30.06.2013	31.12.2012	20.06.2012	Change in the 1st half of 2013		Change y/y	
Overdraft facilities, including	**4 071 259**	**4 184 718**	**3 998 089**	**(113 459)**	**(2.7%)**	**73 170**	**1.8%**
– businesses	2 031 975	2 251 740	2 225 948	(219 765)	(9.8%)	(193 973)	(8.7%)
– individual entrepreneurs	326 648	345 581	371 387	(18 933)	(5.5%)	(44 739)	(12.0%)
– farmers	1 673 206	1 556 847	1 361 649	116 359	7.5%	311 557	22.9%
Loans and advances to customers:	**13 707 801**	**14 234 140**	**13 513 723**	**(526 339)**	**(3.7%)**	**194 078**	**1.4%**
– businesses, including:	7 238 932	8 034 999	7 547 725	(796 067)	(9.9%)	(308 793)	(4.1%)
- investment loans	4 535 650	4 850 132	4 538 249	(314 482)	(6.5%)	(2 599)	(0.1%)
- operating loans	1 675 785	2 088 980	1 847 477	(413 195)	(19.8%)	(171 692)	(9.3%)
– individual entrepreneurs	1 220 963	1 242 443	1 206 979	(21 480)	(1.7%)	13 984	1.2%
– farmers	4 908 308	4 579 424	4 368 846	328 884	7.2%	539 462	12.3%
– public sector institutions	272 937	313 976	282 399	(41 039)	(13.1%)	(9 462)	(3.4%)
– other entities	66 661	63 298	107 774	3 363	5.3%	(41 113)	(38.1%)
Total	**17 779 060**	**18 418 858**	**17 511 812**	**(639 798)**	**(3.5%)**	**267 248**	**1.5%**
of which:							
Preferential loans	*4 451 979*	*4 208 569*	*4 141 855*	243 410	5.8%	310 124	7.5%

8.4.4. DEPOSIT ACTIVITIES

In the first half of 2013, the Bank pursued a conservative pricing policy in case of deposits for institutional clients that aimed at obtaining better interest margins and securing the required liquidity levels. Another priority of the Bank was to increase current account balances in all segments.

The total volume of corporate, farmer and budget sector deposits tended to grow, both compared to the end of 2012 and to the end of the first half of 2012. The liabilities in current accounts (including also saving accounts for farmers and microenterprises) increased particularly dynamically. However, the Group decreased the scale of funding from non-banking financial entities, especially compared to temporary high balance of these sources, which was recorded at the end of 2012.

Table 29. Amounts owed to institutional customers

PLN thousand	30.06.2013	31.12.2012	30.06.2012	Change in the 1st half of 2013		Change y/y	
Other financial institutions:	**1 064 957**	**2 537 917**	**1 371 133**	**(1 472 960)**	**(58.0%)**	**(306 176)**	**(22.3%)**
Current accounts	12 097	9 268	11 364	2 829	30.5%	733	6.5%
Term deposits	1 052 849	2 528 638	1 359 758	(1 475 789)	(58.4%)	(306 909)	(22.6%)
Other liabilities	11	11	11	-	-	-	-
Corporate customers:	**8 498 249**	**7 924 560**	**7 544 918**	**573 689**	**7.2%**	**953 331**	**12.6%**
Current accounts	4 476 755	3 974 931	2 948 990	501 824	12.6%	1 527 765	51.8%
Term deposits	3 947 843	3 871 567	4 527 811	76 276	2.0%	(579 968)	(12.8%)
Other liabilities	73 651	78 062	68 117	(4 411)	(5.7%)	5 534	8.1%
Corporate customers, of which farmers:	**1 235 686**	**1 009 139**	**991 269**	**226 547**	**22.4%**	**244 417**	**24.7%**
Current accounts	1 070 874	856 815	806 979	214 059	25.0%	263 895	32.7%
Term deposits	157 188	143 693	178 201	13 495	9.4%	(21 013)	(11.8%)
Other liabilities	7 624	8 631	6 089	(1 007)	(11.7%)	1 535	25.2%
Public sector customers:	**765 025**	**677 074**	**710 429**	**87 951**	**13.0%**	**54 596**	**7.7%**
Current accounts	473 172	484 830	385 069	(11 658)	(2.4%)	88 103	22.9%
Term deposits	291 727	192 118	325 222	99 609	51.8%	(33 495)	(10.3%)
Other liabilities	126	126	138	-	-	(12)	(8.7%)
Total	**10 328 231**	**11 139 551**	**9 626 480**	**(811 320)**	**(7.3%)**	**701 751**	**7.3%**

8.4.5. TRADING BUSINESS FINANCING

Factoring

As part of providing factoring services, in the first half of 2013 the Bank acquired 73 756 invoices with a total value of PLN 1 525 406 861 compared to 63 772 invoices acquired in 2012 with a value of PLN 1 499 067 127.

In order to simplify product structure and improve quality of document templates used in customer service, changes were made in the Bank's factoring offer. Niche products that were withdrawn from the Bank's offer include reverse factoring, financing of debt factoring (repurchase of individual receivables), recourse factoring. Uniform boundary conditions were introduced for all factoring transactions, such as concentration, level of advances, maximum financing term, grace period, number of counterparties etc. In regards to document templates, entries giving uncommitted character to factoring relation were introduced.

In order to improve factoring deals and optimize the whole factoring process, the Bank implemented new application to monitor quality of payments from factoring debtors.

Bank guarantees and letters of credit

As at the end of June 2013 the total value of guarantee liabilities granted to clients amounted to PLN 578 453 thousand. The Bank's portfolio included 1 667 granted guarantees which represented an 11% increase compared to the corresponding period of the previous year (1 505 guarantees).

The Bank not only issues letters of credit to Polish and foreign customers but also services and confirms letters of credit issued by other banks as well as discounts receivables from letters of credit.

In the first half of 2013 the Bank issued 122 import letters of credit with a total value of PLN 30.8 million (compared to 128 import letters of credit with a total value of PLN 38.8 million in the first half of 2012) and processed 41 export letters of credit with a total value of PLN 14.5 million (compared to 63 export letters of credit with a total value of PLN 47.1 million in the first half of 2012).

8.4.6. ACTIVITIES IN DEBT SECURITIES MARKET

In the first half of 2013, the Bank serviced 2 local government debt securities issuance programs. During this period of time, the Bank did not act as an organiser of new issues of debt securities.

8.5. ACTIVITIES IN MONEY AND FOREIGN EXCHANGE MARKETS

In the first half of 2013, the activities of the Bank in money and foreign exchange markets were significantly affected by the following factors:

- further slowdown in economic growth in Poland, observable especially in the first quarter of the year, which was accompanied by a decrease in the inflation rate to the level below the Monetary Policy Council (RPP) target;
- continued decrease of interest rates by the RPP in response to slow economic growth and decrease in inflation below target. The main reference rate has been decreased to 2.75%;
- stabilisation and subsequent depreciation of zloty against foreign currencies due to deterioration of economical situation in Poland and concerns about possible change of monetary policy by Federal Reserve;
- reduction in interest rates by the RPP led to a decrease in profitability of Polish debt securities at the beginning of the second quarter of 2013. Subsequently, profitability of Polish debt securities increased in expectance of substantial decline of aggregate demand for bonds, due to expected change in monetary policy by Federal Reserve;
- stable, high liquidity of Polish banking sector conducive to reduction and then stabilisation on the low level of the cost of finance from the Bank's clients.

Activities on own account

FX market

In the first half of 2013, activities of BGŻ S.A. in the inter-bank market focused on zloty and currencies of the G7 countries. The turnover achieved by the Bank in the inter-bank FX market continued to be stable. The highest trading result was recorded for the EUR/PLN currency pair and then for the USD/PLN and GBP/PLN currency pairs. The Bank's activities in the market of foreign currency options remained at a low level, which is mainly the effect of a low interest of the clients.

Interest rate market

While the Bank's trading activities on interest rate market concentrated on zloty yield curve, the Bank increased its activity on market of instruments denominated in foreign currencies (mainly EUR, USD and CHF) compared to previous year. This was due to customers' increased interest in hedging against exchange rate risk and increased trading activity in this area. In the first half of 2013, the Bank substantially increased its market share in the segment of Buy-Sell-Back and Sell-Buy-Back transactions hedged with treasury securities. Similar to previous years, the Bank did not conduct trading activities in the market of non-treasury debt securities. In 2013, the Bank participates in the competition for performing the function of Treasury Securities Dealer.

Short-term liquidity management

The purpose of the Bank's activity on the unsecured inter-bank deposit market was to manage immediate and short-term liquidity. The main instrument for placing short-term liquidity surpluses were NBP money bills and short-term State Treasury bonds. The Bank did not treat neither the interbank market nor resources of non-bank financial institutions as sources of financing for its credit activities. Market risk relating to short-term liquidity management and to instruments offered to clients was actively managed by such transaction as: OISs, FRAs, IRSs and FX Swaps. Bank is an active member of inter-bank market in terms of short term interest rate derivatives. Until the end of April 2013, the Bank was a Money Market Dealer, but ceased to be one since May 2013 because of changes in the Money Market Dealer system imposed by the National Bank of Poland. In the first half of 2013, the Bank did not participate in WIBOR and WIBID reference rate fixing.

Assets and liabilities management

As far as assets and liabilities management is concerned, the Bank conducted financial operations in order to manage structural exposure of the Bank to interest rate, foreign currency and liquidity risk by way of, among other things, setting hedging transactions against the interest rate and foreign currency risk, investing the surplus of available finance sources, gaining long-term finance and issuance of debt securities.

Hedging transactions

Interest rate risk arising from Clients' transactions – loans, deposits, current and savings account – was centrally managed by the Bank, taking into account expected changes of the market conditions in medium and long term. For this purpose, the Bank entered into IRS, OIS, CIRS and FRA transactions to achieve the optimum profile, from the point of view of risk (limits utilisation) and profitability. In 2012, in order to stabilise margin of preferential loans with subsidies from The Agency for Restructuring and Modernisation of Agriculture (ARMA), the Bank entered into a series of 2-year IRS transactions for the total amount of PLN 1.5 billion, to which the Bank for the first time applied the mechanism of hedge accounting which resulted in limiting financial result volatility. Besides that, the Bank entered into a series of hedging transactions in the first half of 2013. As at 30 June 2013, positive valuation of the above hedging in the amount of PLN 23 666 thousand was recognised in equity.

For the purpose of neutralizing influence of interest rate decreases planned and enacted in the first half of 2013, the Bank entered into a series of, among others, OIS transactions. Primary term of those transactions ranged from 1 to 12 months with PLN 4.3 billion being their average nominal value.

Long-term financing

The Bank has been proactive in increasing the share of long-term, stable financing in the balance sheet structure. In June 2013 the Bank pre-paid a part of CHF loan granted by Rabobank and at the same time obtained CHF subordinated loan from Rabobank for 10 years tenor in the amount of CHF 90 million and cost of CHF Libor 6M + 2.01%. The loan will be reflected in balance sheet structure as supplemental funds of the Bank after approval from Polish Financial Supervision Authority.

Issue of debt securities

Certificates of Deposit are used by the Bank since 2008 to diversify sources of financing. After expiration of Certificates of Deposit Issuance Program in March 2013, the Bank decided to extend it. On 28 March 2013 the Bank signed agreements to launch a new Debt Securities Issuance Program, which was expanded with, among others, a possibility of issuing paper bonds and book-entry bonds with maturity of up to 10 years and with a possibility of secondary market quotation. In the new Program previous dealers (PEKAO S.A., BRE Bank, Bank Handlowy) were joined by ING Bank Śląski. Additionally, the amount of the whole program was increased to PLN 3.5 billion. In the first half of 2013, the Bank continued to implement changes in accordance with strategy accepted in 2012, which assumed prolongation of maturity of issued certificates of deposit. As at 30 June 2013, the Bank's position from own issue comprised certificates of deposit with a value of PLN 1.08 billion and residual maturity of less than 1 year and certificates of deposit with a value of nearly PLN 0.8 billion and residual maturity of 1 - 5 years.

Investment portfolio

The investment portfolio of the Bank is composed of liquid treasury bonds and NBP treasury bills. As at 30 June 2013, the nominal value of Bank's investment portfolio was PLN 3.1 billion, of which PLN 120 million were NBP treasury bills. Additionally, in 2013 the Bank began to place its liquidity in investment portfolio in the form of NBP money bills. As at 30 June 2013, liquidity surplus amounted to PLN 1.25 billion. Taking over management of this part of liquidity surplus was a result of its stability and a long-term perspective to keep it. Maturity of bonds in the portfolio ranges from a few months to over 10 years. In the first half of 2013, revenue in the investment portfolio - interest, settlement of premium/discount and sale result amounted to PLN 128.1 million, of which the result on sale of some items before the maturity date was PLN 20.6 million. Disposal of bonds before the maturity date was conducted in the conditions of decreasing profitability, with the bonds reaching its lowest profitability level in May 2013. The bonds disposed by the Bank were mostly two-year bonds. In order to replace those bonds, the Bank purchased mostly NBP money bills and long-term bonds with higher profitability. As at 30 June 2013, fair value of treasury securities portfolio in amount of PLN 124.4 million was allocated to revaluation reserve.

Sale of treasury products to clients

In the first half of 2013, the dynamics of sale of treasury products in all segments of institutional clients portfolio were comparable to the previous year.

The most significant factors influencing growth revenue were currency spot and forward transactions supported by the electronic treasury eBGŻ channel. Hedging solutions in the first half of 2013 were less diversified than in 2012, although more corporate i.e. SME and LE clients hedged against interest rate risk.

The Bank continues the sale of treasury instruments hedging against interest rate risk, which were introduced the previous year, i.e. interest rate options and instruments hedging against the risk of changes in prices of goods, such as commodity options and swaps.

8.6. COLLABORATION WITH FINANCIAL INSTITUTIONS

In the first half of 2013, the Bank maintained correspondent contacts with approximately 870 banks, keeping 25 Nostro accounts in 16 main currencies in foreign banks.

As at 30 June 2013, the Bank maintained 29 Loro accounts in 6 currencies for 20 foreign banks, 1 domestic bank and 1 foreign non-banking financial institution. The Loro accounts are maintained in the BGŻ S.A. books of account and represent an external source of securing working capital funds at no cost, which serve to satisfy the operating needs of the Bank. Using these accounts, the Bank executes primarily client transfers and bank-to-bank transfers.

The Bank also dealt with cooperative banking sector, both in transactional and treasury banking.

In the first half of 2013, BGŻ S.A. collaborated with one foreign non-banking financial institution offering cheap and fast electronic money transfer services, i.e. MoneyGram (USA). The subject of collaboration was both money orders as well as transfers to bank accounts. Transactions were executed in both directions i.e. to and from Poland.

The Bank also continued collaboration with other domestic and foreign financial institutions, mainly with investment funds, insurers, pension funds, brokers and banks. This collaboration enabled the Bank to offer a wide range of treasury and deposit transactions. The Bank has entered into many agreements with new and already collaborating partners from those segments, which enable the Bank to settle transactions for old and new products.

8.7. FINANCING FOREIGN TRADE OPERATIONS

The product offer dedicated to finance foreign trade operations of the Bank comprises of: export and import letters of credit, export and import documentary collection, letter of credit discount, Nostro and Loro guarantees, avals and guarantees, factoring, payment orders and foreign exchange payment orders.

On 10 June 2013, a new system SORBNET2 was implemented based on international standard for SWIFT messages exchange, which replaced SORBNET used since 1996. RTGS-SORBNET2 is the most important Polish payment system, in which financial market operations and high-value customers' orders are settled. It also services settlements of other payment and clearing systems. New technological standards applied in SORBNET2 system are designed to increase reliability and efficiency of the system and, as a result, safety and effectiveness of interbank trading.

In the first half of 2013, the Bank maintained an upward trend in foreign trade transfers. The share of SEPA Credit Transfer in the total number of import and export transfers increased and amounted to 69% and 67%, respectively.

Table 30. Statistics of operations handled by BGŻ S.A.

Transaction type	Quantity/value	1st half of 2013	1st half of 2012	Change y/y
Transactions using the nostro accounts (commercial banks and NBP)	Number of transactions	371 723	327 545	13.5 %
	Value in PLN billion	1 794	1 468	22.2 %
Transactions using the loro accounts	Number of transactions	51 140	60 606	(15.6%)
	Value in PLN billion	421	364	15.7%
Export transfers	Number of transfers	226 812	205 524	10.4%
	Value in PLN million	10 208	10 138	0.7%
including: SEPA Credit Transfer	Number of transfers	152 042	114 936	32.3%
	Value in PLN million	3 851	2 844	35.4%
Import transfers	Number of transfers	94 255	84 825	11.1%
	Value in PLN million	5 705	6 990	(22.6%)
including: SEPA Credit Transfer	Number of transfers	65 210	37 531	73.8%
	Value in PLN million	2 781	1 917	45.1%
Own letters of credit and own documentary collection (newly opened)	Number	142	146	(2.7%)
	Value in PLN million	48	40	20%
Guarantees and own promissory notes granted	Number	636	814	(21.9%)
	Value in PLN million	156	171	(8.8%)
Third party letters of credit and third party guarantees	Number	281	274	2.5%
	Value in PLN million	92	103	(10.7%)

8.8. BANK ORGANIZATION AND HUMAN RESOURCES

8.8.1. ORGANIZATIONAL STRUCTURE

The most significant changes in the Bank's organisational structure made in the first half of 2013 related to implementation of a new customer service model based on the new approach to sales management, especially in the area of new institutional clients acquisition.

Two main areas of sales were separated, both in the Head Office as well as in the branches:

- Retail and Business Banking area responsible for sale and development of products targeted at individual customers and microenterprise segment
- Corporate Banking area responsible for sale and development of products targeted at micro, medium and large companies and agro companies i.e. operating in the food and agriculture sector.

In the area of Retail and Business Banking, client service is becoming more effective and efficient due to product offer standardization, automation and simplification of credit process, including shortening decision-making procedures and maintenance of stable, long-term relations strengthen by dedicated approach to Agro clients. From the organizational perspective, customer service to retail clients and micro enterprises is provided by operational and subordinated branches supported by regional branches and departments of the Head Office focused on the area of Retail and Business Banking.

In the area of Corporate Banking, the Bank concentrates on professional business consultancy services supported by product specialists and Agro experts, maintenance of local relationships and operational services together with wide range of product solutions tailored to the individual customer needs. For purposes of developing cooperation with corporate clients in regions, network of business centers was created (for small and medium, as well as for large companies). Activity of the business centres is coordinated and supported both on the regional level by regional corporate banking directors, and on the central level by Head Office divisions focused on the area of Financial Markets and Corporate Banking.

Detailed information on the new customer service model is presented in the chapter in which Group's distribution channels are described.

8.8.2. HUMAN RESOURCES

Employment levels

At the end of June 2013, BGŻ S.A. had 5 570 employees, i.e. 3.5% less than in the previous year. In the Head Office, the number of employees decreased by 11.1% y/y. On 30 June 2013 the process of group redundancies has ended. It was the effect of the Bank's program to increase efficiency, mainly in the Headquarters.

Table 31. Bank's employment in employees and FTEs

	30.06.2013	31.12.2012	30.06.2012	Change y/y	
Network	4 103	4 085	4 163	(60)	(1.4%)
Headquarters	1 334	1 438	1 500	(166)	(11.1%)
Brokerage Office	56	32	36	20	55.6%
BGŻOptima	44	49	43	1	2.3%
Holiday resorts	30	30	30	-	0.0%
Trade unions	3	3	3	-	0.0%
Total (employees)	**5 570**	**5 637**	**5 775**	**(205)**	**(3.5%)**
Network	4 074.24	4 056.45	4 130.13	(55.88)	(1.4%)
Headquarters	1 319.85	1 426.87	1 489.94	(170.09)	(11.4%)
Brokerage Office	55.50	32.00	36.00	19.50	54.2%
BGŻOptima	37.44	39.88	22.39	15,06	67.3%
Holiday resorts	29.50	29.50	29.50	-	0.0%
Trade unions	3.00	3.00	3.00	-	0.0%
Total (FTEs)	**5 519.54**	**5 587.70**	**5 710.95**	**(191.41)**	**(3.4%)**

Salaries

The key objective of the Bank's remuneration policy, which serves execution of the Bank's business strategy and creation of its competitive advantage, is to attract, keep and motivate top-notch employees. The Bank's remuneration policy is based on the concept of a comprehensive approach to employee rewarding and accounts for, apart from such major main elements as fixed and variable remuneration, the issues of recognition, career development, work environment and business culture.

The Bank has pursued a reasonable and balanced remuneration policy which reflects its client-oriented approach, accounts for the long-term Bank's interests and supports reasonable and effective risk management.

The Bank participates in salary market research and thus has regularly monitored competitiveness of its remuneration package (of fixed and variable part) against the market.

The Bank's remuneration policy also includes detailed rewarding regulations for these employees at managerial posts who have a considerable impact on the Bank's risk profile (as per the PFSA Resolution No. 258/2011).

Table 32. Payroll costs

PLN thousand	1st half of 2013	1st half of 2012	Change	
			PLN thousand	%
Payroll costs including:	**(191 861)**	**(194 801)**	**2 940**	**(1.5%)**
- base remuneration	(168 133)	(165 198)	(2 935)	1.8%
- other components of salaries and wages *	(6 312)	(1 922)	(4 390)	228.4%
- awards and bonuses	(29 246)	(32 111)	2 865	(8.9%)
- non-employment contracts	(1 455)	(1 649)	193	(11.7%)
- provisions for future liabilities*	13 286	6 079	7 207	118.6%
Social security and other employee costs	**(53 902)**	**(46 686)**	**(7 216)**	**15.5%**
- salary overheads	(40 568)	(39 816)	(752)	1.9%
- employee benefits	(2 331)	(3 251)	919	(28.3%)
- employment restructuring write-off	(2 370)	-	(2 370)	-
- provisions for future liabilities*	(8 633)	(3 620)	(5 013)	138.5%
Total payroll	**245 763**	**(241 497)**	**487 260**	**(201.8%)**
Awards and bonuses as % of base remuneration	***17.4%***	***19.4%***		**(2.0%)**

**Contingent liabilities payments due to changes in the Management Board of the Bank.*

Higher basic salaries in the first half of 2013 resulted from remuneration increase implemented in June 2012 to reward the best employees. Other factors were staff mobility and the process of group redundancies.

Variable remuneration (awards and bonuses) in the Bank is related to the Bank's net profit and achievement of employee individual goals.

Incentive schemes

In the Bank there are incentive schemes that combine three elements: goals relating to priorities set in the Bank's strategy and financial plans, results which are the work output of the Bank's employees, and the amount of bonus.

The incentive schemes, adjusted to the specific character of tasks performed in the area of sales, sales support and risk and risk support, are based primarily on the Management by Objects (MbO) formula, which means that an individual bonus is related to the level and quality of the task performed. The system focuses on defining tasks or goals which set the development direction of the entire organisation and then are divided into the objectives of individual organisational units and individual employees.

There is also a separate bonus system in the Bank for variable remuneration, including bonuses for employees holding managerial positions who have a significant impact on the Bank's risk profile. The adopted solution is also a result of implementation of the PFSA Resolution No. 258/2011 dated 4 October 2011.

Training and career development

In the first half of 2013, a training program was focused on cooperation with business, supporting the realisation of the Banks' strategic goals through the development of employee skills and competences. The program covered training organised both in traditional and e-learning form. The number of employees who participated in the Bank's training program was 15 794.

The main areas of trainings conducted in the first half of 2013 were as follows:

- Continuation of awareness raising activities in terms of risk culture in the Bank, especially in the areas of credit and operational risk, compliance.
- Training for sales employees aimed at improving product knowledge.
- Training in the Personal Banking area preparing advisors to perform their duties and preparing subordinate branch representatives to VIP customers service.

- Continuation of *„Po pierwsze klient"* project co-financed by the European Social Fund; training intended to implement customer service standards.
- Training in the area of credit processes for business banking employees aimed at adjustment of credit competences due to organizational and process changes.
- Building advanced sales competencies as a part of implementation of new customer service model – 1-year complex development programe High Achiever for Large Companies relationship managers.

The Bank continued realization of the II edition of "Prestige" Potential Growth Program, which aims at identification and development of employees with the highest potential in managerial and expert areas of competencies.

Internship programs

The Bank offers internship programs to students and graduates.

In the first half of 2013, 130 interns had the opportunity to work at the Bank. The Bank established cooperation with Warsaw University of Life Sciences and signed an agreement based on which the Bank admitted students recommended by the University to take part in internship program. A special program of summer internship was developed for this group, under which the Bank organised internship workshops where the participants could improve their skills.

In addition, the Bank continued its summer internship program targeted at the group of about 100 students and graduates. This year, in cooperation with BGŻ Foundation and businesses, program for graduates *"Klasa BGŻ"* was established for the first time focusing especially on young talented people from rural areas.

Employer branding

In the first half of 2013, the Bank continued its employer branding activities. In 2013, the Bank was again placed on the list of Best Employees in the Universum ranking of TOP 100 Ideal Employers for Students.

8.9. IT DEPARTMENT

In the first half of 2013, the IT Department spent PLN 24.26 million on its investment projects. During this period, 5 projects were completed, 29 projects were in progress.

The most significant IT initiatives undertaken are as follows:

- Implementation of the integration between the CRM system and loan application service system for retail clients, which expands the range of loan applications data and customer data.
- Implementation of privilege account management system as well as rules and mechanisms of integrity of data stored in databases and during their exchange for selected payment systems.
- Adjustment of banking systems to clearing services under SORBNET2 due to withdrawal of SORBNET by NBP.
- Implementation of new card system module in order to integrate PIN generation and prepare data to be saved on magnetic stripe.
- Implementation of application automatically generating exchange rate tables.
- Migration of SWIFT environment application to virtual platform.
- Implementation of new workflow for retail banking.
- Implementation of new legal documents management system.

9. OPERATIONS OF SUBSIDIARIES AND ASSOCIATE ENTITIES OF BGŻ S.A. GROUP

9.1. BANKOWY FUNDUSZ NIERUCHOŚCIOWY ACTUS SP. Z O.O.

The company was founded in 1999 and its main activities include:

- acquisition and disposal of real estate and limited property rights related to real estate,

- management of own and third-party construction projects,
- real estate trading intermediary services and lease of premises,
- lease of real estate and rental of premises,
- services relating to real estate valuation, management and advisory (real estate management agency activities).

As at 30 June 2013, the company's investment portfolio comprised open land real estate in Wrocław – Marszowice with square footage of 48.4112 ha. In accordance with binding Local Spatial Management Plan, the real estate is destined for residential development.

In the first half of 2013, supervisory activities undertaken towards the Company concentrated on creating conditions for sale of real estate situated in Wrocław – Marszowice.

Table 33. Basic financial data of BFN Actus Sp. z o.o.

PLN thousand	30.06.2013	31.12.2012	30.06.2012
Total assets	62 467.3	62 502.0	63 574.0
Long-term investments	62 301.0	62 301.0	63 401.0
Equity	17 937.5	18 975.4	20 899.4
in this: net result	(1 166.9)	(3 207.0)	(1 109.8)

9.2. BGŻ LEASING SP. Z O.O.

The company was founded in April 2007 as an associate entity of De Lage Landen International B.V. (Rabobank Group). The main activity of the company is to offer lease products, especially lease of machines, vehicles and other fixed assets as well as loans. In the first half of 2013, as many as 824 deals were made totaling PLN 190.70 million, compared to 951 deals totaling PLN 309.16 million in the first half of 2012.

In the first half of 2013, the company recorded net loss, mainly due to impairment charges on receivables from LE clients.

Table 34. Basic financial data of BGŻ Leasing Sp. z o.o.

PLN thousand	30.06.2013	31.12.2012	30.06.2012
Total assets	1 050 826	1 073 868	1 059 157
Net receivables from leases and loans	941 423	954 922	941 848
Equity	91 462	94 144	92 985
in this: net result	(2 682)	(662)	(1 821)

10. RISK MANAGEMENT

10.1. CREDIT RISK

Credit risk management

Credit risk is defined as the risk of default of financial liabilities by debtor, being – in particular – the risk of non - payment of loan as well as the risk of worsening of the financial situation of debtor, which both affect valuation and quality of the Bank's assets.

For the purpose of managing credit risk, the Bank' determines credit risk appetite in the annual cycles as the maximum credit risk exposure that the Bank is prone to accept in connection with its business strategy and the accepted financial plan. Credit risk exposure is determined by a set of risk measures divided into economy sectors, products, business lines and client segments.

In the process of credit risk management, the Bank's activities are based on current analyses of the macroeconomic environment and internal analyses of credit portfolios. The applied approach facilitates taking up swift remedial measures when unfavourable trends appear in the external environment or in the quality or structure of the credit portfolio. Active credit risk management is executed by the Bank, by way of, among others:

- regular adjustment of credit policy, methods and tools for risk assessment and measurement to changing market conditions,
- tight supervision over the portfolio of existing credit exposures.

The main activities in respect to credit risk realized by the Bank in the first half of 2013 are as follows:

- review and update of the risk appetite,
- review and update of the system of key credit risk limits and concentration limits in order to manage portfolio risk and concentration risk more effectively,
- implementation of a new credit worthiness assessment model for institutional clients using simplified reporting,
- development of risk base pricing model for institutional clients using simplified reporting,
- implementation of new more conservative rules of financing retail clients applying for mortgage products (underwriting criteria),
- review of collaterals' rules of loans, collaterals monitoring and the range of gathered information about collaterals in order to, among others, meet the requirements ensuing from Recommendation J and S of Polish Financial Supervision Authority and more effectively managing the residual risk by the Bank.

Structure and quality of credit portfolio

The Bank's credit portfolio is characterized by a high share of loans with relatively safer risk profile i.e. housing loans and loans granted to farmers. The share of cash loans with higher risk of default is relatively low. In the first half of 2013, share of loans granted to large companies has shrunk significantly.

Table 35. Structure of the loan portfolio

PLN thousand	**30.06.2013**		**31.12.2012**		**30.06.2012**	
	PLN thousand	***Share in %***	***PLN thousand***	***Share in %***	***PLN thousand***	***Share in %***
Loans and advances, gross	**27 115 879**	**100.0%**	**27 393 636**	**100.0%**	**26 281 469**	**100.0%**
Mortgage loans	7 892 242	29.1%	7 600 490	28.3%	7 392 994	28.1%
– in PLN	4 680 710	17.3%	4 412 921	13.9%	3 952 628	15.0%
– in foreign currencies	3 211 533	11.8%	3 187 570	14.4%	3 440 366	13.1%
Cash loans	896 939	3.3%	803 967	2.9%	781 264	3.0%
Other loans to retail clients	547 638	2.0%	570 321	2.5%	595 399	2.3%
Individual entrepreneurs	1 547 611	5.7%	1 588 024	5.9%	1 578 366	6.0%
Farmers	6 581 514	24.3%	6 136 271	21.0%	5 730 495	21.8%
Corporates	9 270 907	34.2%	10 286 739	37.7%	9 773 673	37.2%
Public sector	286 585	1.1%	314 877	1.2%	307 252	1.2%
Other receivables	92 443	0.3%	92 947	0.5%	122 026	0.5%

The share of impaired loans in gross amount of loans and advances to customers increased from 7.1% as at the end of 2012 to 7.9% as at 30 June of 2013. The deterioration concerned mortgage loan portfolio (the increase from 4.9% as at the end of 2012 to 5.3% as at 30 June 2013 mainly of loans in foreign currencies belonging to the old portfolio) and mostly loan portfolio of institutional clients, excluding loans granted to farmers (the increase from 9.1% to 11.6% mainly concerning SME clients). The increasing share of impaired loans corresponded to the worsening microeconomic situation and inhibiting of the portfolio growth in the first half of 2013.

On the other side, the quality of both other loans granted to retail clients and loans to farmers has improved (the share ratio of retail loans decreased from 16.0% as at the end of 2012 to 14.9% as the 30 June 2013 while the loans to farmers decreased respectively from 3.6% to 3.4%). The sector of agro clients remains resistant to economic downturn.

Table 36. Quality of the loan portfolio

PLN thousand	30.06.2013	31.12.2012	30.06.2012*	Change 30.06.2013 vs 31.12.2012		Change 30.06.2013 vs 30.06.2012	
				PLN thousand	*Share in %*	*PLN thousand*	*Share in %*
Retail loans	**9 336 819**	**8 974 778**	**8 769 657**	**362 041**	**4.0%**	**567 162**	**6.5%**
impaired	634 487	593 540	478 976	40 947	6.9%	155 511	32.5%
% share	6.8%	6.6%	5.5%		0.2%		1.3%
Corporate loans	**17 779 060**	**18 418 858**	**17 511 812**	**(639 798)**	**(3.5%)**	**267 248**	**1.5%**
impaired	1 516 435	1 342 310	1 197 354	174 125	13.0%	319 081	26.6%
% share	8.5%	7.3%	6.8%		1.2%		1.7%
of which: farmers	**6 581 514**	**6 136 271**	**5 730 495**	**445 243**	**7.3%**	**851 019**	**14.9%**
impaired	221 357	219 038	183 910	2 319	1.1%	37 447	20.4%
% share	3.4%	3.6%	3.2%		(0.2%)		0.2%
Total	**27 115 879**	**27 393 636**	**26 281 469**	**(277 757)**	**(1.0%)**	**834 410**	**3.2%**
impaired	**2 150 922**	**1 935 850**	**1 676 330**	**215 072**	**11.1%**	**474 592**	**28.3%**
% share	**7.9%**	**7.1%**	**6.4%**		**0.9%**		**1.6%**

*Data prior to the change of impairment model implemented in December 2012

Restructuring and recovery of high risk debt

The policy of restructuring and debt recovery, conducted in the first half of 2013, was a continuation of activities conducted in the area of:

- identification, negotiation and implementation of activities aimed at maximizing repayments by debtors or – where possible – implementation and monitoring of debtor corporate recovery proceedings leading to improvement of debtor financial and economic position, with the overall view to return debtors for servicing by their original sales units,
- active monitoring of execution and bankruptcy proceedings,
- disposal of part of non – performing loans,
- tax optimization of executed strategies,
- identification of early warning signals and taking appropriate actions (where possible, in collaboration with sales units) limiting the risk of potential losses,
- providing a support for business units in handling loans at risk,
- appropriate training for business units personnel and credit area personnel in order to increase efficiency in identifying warning signals, helping with proper granting of loans (particularly in the collateral establishment, which apart from the repayments are the main source of recovery),
- improvement of the Bank's organizational structure, procedures and tools to enhance the efficiency of the tasks carried out.

Debts recovered in the first half of 2013 in the amount of PLN 188 million (principal) were the result of the conducted court executive procedures, bankruptcy proceedings in progress, civil-legal agreements with debtors and composition proceedings in process.

The number of enforceable titles issued by the Bank in the first half of 2013 amounted to 410 for corporate loans and, 2 246 for retail loans.

The value of collaterals in the portfolio, which is recovered or restructured, is as follows (in the context of the LTV ratio for mortgage loans and loans secured by mortgages):

- institutional in PLN – 49.1%,
- institutional in foreign currencies – 84.6%,
- retail in PLN – 80.6%,
- retail in foreign currencies – 119.4%.

The above information reflects a relatively adequate level of collateralization with the concurrent limitation of risk of debt non-recovery. A high LTV ratio for retail loans results mainly from currency appreciation (CHF) in previous years.

10.2. FINANCIAL RISK

10.2.1. MARKET RISK

The Bank's operations are recorded in the trading and banking books. Fluctuations in market interest rates, currency exchange rates, prices of securities or in the implied volatility of option instruments cause changes in present values of these books. The risk of unfavourable fluctuations in value due to the above risk factors is recognised by the Bank as market risk, and due to the different nature of these books, this risk is monitored and managed separately for each book. In addition, the Bank resigned from conducting activities on the stock market by the Brokerage Office.

Market risk in the banking book

The banking book of the Bank consists of two elements – ALM, which aims to manage the interest rate risk and long-term liquidity of the Bank. The second part is Money Market Portfolio, which functions as a short term liquidity management centre.

ALM consists of deposits and loans, strategic positions (long-term investments and debt securities issue), financial market transactions hedging the banking book (derivatives) and non-interest items (i.e. equity, tangible assets, intangible assets, taxes and provisions, result for the period). Management over all these elements is transferred to Bank's Headquarters through Funds' Transfer Pricing (TCF) system.

Money Market encompasses liquid assets and the closed-up differences on client's derivatives transactions (mostly regarding currency forward/futures contracts). This portfolio consists of derivatives instruments, whose goal is to stabilize the cost of financing, to meet the needs of ALM portfolio through market operations, to secure cash flows from client's transactions and to adjust the level of portfolio risk to the acceptable level.

The Bank's policy with respect to the banking book is to earn additional income above the product margin, while avoiding the risk of instability of deposits placed by clients, equity or financial result. The Bank achieves this goal by keeping or adjusting the natural risk exposure resulting from deposit and lending activities within current risk limits or middle- and long-term financial market trends.

The main measures of the market risk applied by the Bank in the ALM portfolio are:

- interest rate revaluation gap,
- the weighted average duration of assets/liabilities and equity known as 'duration',
- sensitivity measures – defining sensitivity of the financial item – valuation, interest income, net economic value of equity – to changes in risk factors,
- IaR (Interest-at-Risk – sensitivity of interest result),
- EaR (Equity-at-Risk – sensitivity of the current value of net capital).

The portfolio of Money Market, according to its nature and purpose, apply measures equivalent to those used for the trading book:

- VaR – Value-at-Risk – showing maximum acceptable level of loss on the given item in normal market conditions in a defined time period that can be exceeded with a defined probability; BGŻ S.A. applies the parametric model with modified variance – covariance matrix and exponential weighting of historical observations; the accepted confidence level is 99%, and the period of position holding for the banking book is 1 month,

- Scenario analysis and stress tests – supplement VaR to include statistically unpredictable market events: historical economic and political crises, theoretical scenarios,
- BpV (basis point value) – price sensitivity to a parallel shift of the yield curve.

The Bank manages the banking book risk by limiting risk measures and monitoring the risk on an ongoing basis.

Situation in the first half of 2013

As at the end of June 2013, the value of the „duration" measure, i.e. the average weighted period to repricing of interest rate for assets remained on the level of 2.9 months (at the end of 2012 - 2.8 months), whereas for liabilities – equalled to 3 months (previously 2.6 months). The duration of net capital in the ALM portfolio decreased from 5.2 months at the end of 2012 to 1.4 months at the end of June. The repricing period for almost 92% of assets and liabilities was lower than 6 months (at the end of 2012 - 93%), however almost 53% of assets and liabilities are to be re-valued within one month (previously - 59%).

In the first half of 2013, the interest rate risk (measured IaR) has increased, reaching the average level of PLN 12.8 million in a scenario of 200 bps increase in interest rates and PLN 12.0 million in a scenario of 200 bps decrease in interest rates, in comparison to PLN 1.3 million and PLN 1.9 million respectively in the first half of 2012 (decrease in net interest income in the first half of 2013 would occur if the interest rates decreased). However, the interest rate risk remained on a low level in relation to 12-month net interest income (PLN 1 024.4 million in 2012). The biggest change of exposure concerned debt securities portfolio and deposit base (not renewed most expensive negotiable deposits, increasing volume of progressive deposits, stable level of BGŻOptima deposits) with worse than planned lending activities. At the same time shortening residual maturity of OIS transactions hedging interest rate risk in ALM portfolio impacted the structure of repricing gap.

The sensitivity of net interest income (IaR) was as follows as at 30 June 2013:

- an immediate increase in interest rates by 50 bps: increase in net interest income during one year by PLN 13.7 million (at the end of 2012: decrease by PLN 1.3 million),
- an immediate decrease in interest rates by 50 bps: decrease in net interest income during one year by PLN 14.6 million (at the end of 2012: increase by PLN 3.5 million),
- a gradual increase in interest rates by 200 bps during one year: increase in net interest income by PLN 27.6 million (at the end of 2012: decrease by PLN 4.0 million),
- a gradual decrease in interest rates by 200 bps during one year: decrease in net interest income by PLN 29.0 million (at the end of 2012: increase by PLN 8.8 million).

The exposure of Money Market portfolio was dominated by positions in 7-day NBP monetary bills (held for a short-term liquidity management purposes) and Interest Rate Swaps transactions (OIS and IRS – exposure adjusting, hedging the price risk) and FX Swap transaction (the financing of the Group in foreign currencies). In the first half of 2013 the average utilization of VaR limits remained on 60% (42% in the second half of 2012). In terms of the currency structure, the exposures in PLN (over 45% of the sensitivity measured in BPV and over 70% in the second half of 2012), USD (23%), EUR, and CHF had the biggest share.

Market risk in the trading book

Trading activities of the Bank are supplementary in nature and are conducted to support sales of financial products to corporate clients, financial non-banking clients (directly) and retail clients. By opening own positions for these purposes, the Bank generates revenues from short-term fluctuations in price parameters (foreign currency exchange rates, interest rates, debt securities prices etc.) whilst keeping the exposure within defined risk limit. The Bank does not have open position in currency and commodity options and for this reason market risk in the options portfolio does not exist.
The key measures for market risk used by the Bank in the trading book are:

- Value-at-Risk (VaR) – showing maximum acceptable level of loss on the given item in normal market conditions in a defined time period that can be exceeded with a defined probability; BGŻ S.A. applies the parametric model with modified variance – covariance matrix and exponential weighting of historical observations; the accepted confidence level is 99%, and the period of position holding for the trading book is 1 day,
- Scenario analyses and Stress Test – supplement VaR to include statistically unpredictable market events: historical economic and political crises, theoretical scenarios, expected shortfall analyses (expected loss of value above confidence level) and max-loss (the highest possible loss based on a known history of fluctuations in market-based factors),
- BpV (basis point value) – price sensitivity to a parallel shift of the yield curve,
- Nominal measures – among others, value of currency position during a day and at day end, securities nominal value,
- Non-monetary limitations – among others, allowed types of instruments, currencies and pairs of currencies, maximum maturity dates, minimal credit rating for acquired debt securities,
- Stop – loss limits (level of the maximum loss acceptable) – for various time periods (day, month, year) at the portfolio and sub-portfolio level.

In order to limit the exposure to market risk, based on the decisions of the Committee for Risk and Balance Sheet Management, limits are established for IaR, VaR and FX VaR, risk appetite, stress tests, BpV sensitivity and other measures. Utilisation of all limits is monitored and controlled on a daily basis.

Situation in first half of 2013

At the end of 2012 the Group performed a review of limits in the trading book. As a result, the delta limit (BPV) for PLN and EUR increased, whereas VaR limits and stress test remained unchanged. The higher limits are effective since the beginning of 2013. Simultaneously the Group introduced the extended list of stress test scenarios (additional standard scenarios of Rabobank Group).

Higher level of utilization of VaR limit in the trading book was mainly affected by higher delta limits and increasing volatilities of main risk factors (PLN swap curves, PLN OIS, PLN GOVT). The profile of interest rate risk changed gradually during the first half of 2013. The position in debt securities issued by governments (mainly low price-risk securities) generally did not exceed PLN 1 billion during the first half of 2013, whereas the positive sensitivity of outbalancing interest rates swaps accounted for the counterweight for the position in bonds. As a consequence, the trading portfolio was generally exposed to interest rates decrease scenario. The currency risk remained at low level, and the activity was focused on EUR and partially on USD. During the first half of 2013 the currency exposure of the Group generally has been reducing at the end of the day, mainly due to clients' activity.

The value at risk, which is the measure of trading portfolio exposure to the price risk, remained on the average level of 75% of the limit in the first half of 2013 (in the previous half of the year - 70%). This was mainly affected by interest rate exposure. VaR for interest rate risk average accounted for 77% of limit (in the previous half of the year – 75%), whereas for currency risk - 16% of the limit (in the previous half of the year – 7%). The VaR limit for interest rate risk was exceeded one time during the first half of 2013 (by 3%).

Liquidity risk and assessment of finance sources stability

During the first half of 2013, the Bank maintained safe level of financial liquidity. The financial resources allowed the Bank to discharge all its liabilities on time. The portfolio of the most liquid securities was kept at the level entirely securing any potential outflow of funds by largest Bank's deposit owners. At the end of June 2013, the excess of liquid assets over the minimum limit amounted to PLN 2.16 billion.

At the end of the first half of 2013, the excess of financing resources originated from non inter-banking market above loans value, amounted to PLN 4.89 billion, whilst the excess of stable deposits over loan portfolio amounted to PLN 1.31 billion.

The Bank benefited from the very positive liquidity situation and therefore began the process of optimization of financial resources. As the result of this process, the Bank stopped raising the most expensive deposits and replaced less stable volumes with more stable ones. Because of that, the stability of financial resources of the Bank increased to the level of 89.3 % in the first half of 2013. The main reasons for that were a lower fluctuation of balances of retail deposits and of BGŻOptima (the stability increased to 93.3%), the growth of stability of resources deposed by SME and Micro segments clients (excluding migration between the products), stable deposits of LE and budget entities, growing balance of certificates of deposit, and due to the CHF loan received from Rabobank.

10.3. OPERATING RISK

In accordance with the regulations in force, the Bank defines operating risk as a risk of loss or unjustified costs resulted from inadequacy or failure of internal processes, people, systems or external factors. The Bank includes also the risk of non-compliance, including legal risk.

The purpose of operating risk management is to limit losses and costs arising from the risk, ensure rendering services of the highest quality as well as the security and compliance of Bank's activities with binding laws and regulations.

10.4. LEGAL RISK

The litigation situation in 2013 within insurance and employment claims was stable and did not generate material legal risk for the Bank. There were no court or administrative proceedings held by public administration bodies in relation to liabilities or receivables of the Bank, with the claim amount for at least 10% of the Bank's equity as at 30 June 2013.

11. DEVELOPMENT PROSPECTS OF THE GROUP

In the first half of 2012, the Bank has reviewed and updated its strategy for years 2010 – 2014 and extended it to 2016. The strategy was approved by the Supervisory Board on 21 June 2012.

According to the strategy, the Bank is focused on the continued development of its activities as a universal bank, specializing in rendering services for the agricultural and food sector. From the perspective of the client, the Bank strives to develop long-term relations and be perceived as a responsible partner engaged in local communities, which are defined as centres with 20 – 150 thousand residents.

Within the scope of universal banking, the strategy assumes further strengthening of the Bank's position in retail banking by expanding the product offer and attracting customers from medium class segment (including alternative distribution channels) in order to provide funds for key segments of its activities. The Bank will continue to develop its branch network, which, however, will be limited in comparison to previous years. The development of the branch network will be carried out in medium-sized cities, where the Bank has been already located and has a strong position.

The Bank plans to concentrate on further growth of the business relating to providing services for small, medium and micro – businesses in local markets.

In the area of banking services for agricultural and food sector, the Bank intends to strengthen its leadership based on the product range and a service model tailored to the needs of that market.

A number of internal project and initiatives including inter alia the development of traditional and virtual distribution channels, optimization of internal processes and support functions for business activity will help to achieve its strategic goals. The high importance is placed on the development of Client Relationship Management systems (CRM), improvement of operating effectiveness and human management potential.

The strategy assumes also necessary recapitalization of the Bank, as a result of which the 12% targeted capital adequacy ratio shall be achieved.

Both the Management Board of Bank and its shareholders are convinced of the long-term potential of the banking sector in Poland and wish to continue their commitment in future development of the Bank.

12. SIGNIFICANT DEVELOPMENTS AFTER THE REPORT DATE

On 24 July 2013, the Supervisory Board has changed the resolution no. 5/2013, overruling the appointment of the Vice-President - Mrs Monika Nachyła to act as the President of the Management Board. Simultaneously, the Supervisory Board has appointed the first Vice-President of the Management Board - Mr. Gerardus Cornelis Embrechts as the Acting President of the Management Board. The Supervisory Board also decided to start the recruitment process for the position of the President of The Management Board.

....
Gerardus Cornelis Embrechts
The first Vice-President of the Management Board acting as President of the Management Board

....
Witold Okarma
Vice-President of the Management Board

....
Andrzej Sieradz
Vice-President of the Management Board

....
Monika Nachyła
Vice-President of the Management Board

....
Johannes Gerardus Beuming
Vice-President of the Management Board

....
Dariusz Odzioba
Vice-President of the Management Board

....
Wojciech Sass
Vice-President of the Management Board

....
Magdalena Legęć
Vice-President of the Management Board

Warsaw, 13 August 2013