REPORT ON THE APPROVAL OF THE APPRAISAL REPORT OF THE SUPERVISORY BOARD ON THE FINANCIAL STATEMENTS OF BGŻ BNP PARIBAS S.A. INCLUDING THE BROKERAGE HOUSE, MANAGEMENT BOARD REPORT ON THE BANK'S ACTIVITY, INCLUDING THE BROKERAGE OFFICE, THE CONSOLIDATED FINANCIAL STATEMENTS OF THE CAPITAL GROUP OF BGŻ BNP PARIBAS S.A., AND OF THE MANAGEMENT BOARD REPORT ON THE ACTIVITY OF THE CAPITAL GROUP OF BGŻ BNP PARIBAS S.A FOR THE FISCAL YEAR FROM 1ST JANUARY 2018 TO 31ST DECEMBER 2018, REPORT ON THE NON-FINANCIAL INFORMATION OF BANK BGŻ BNP PARIBAS S.A. AND THE BANK BGŻ BNP PARIBAS S.A. CAPITAL GROUP IN 2018 AND ON THE MOTION OF THE MANAGEMENT BOARD ON THE DISTRIBUTION OF PROFIT FOR THE FISCAL YEAR 2018 TOGETHER WITH THE ASSESSMENT OF ADEQUACY AND EFFECTIVENESS OF THE INTERNAL CONTROL SYSTEM IN THE BANK BGŻ BNP PARIBAS S.A.

BGŻ BNP PARIBAS

Bank
zmieniającego
się świata

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1. FINANCIAL STATEMENTS OF THE BANK BGŻ BNP PARIBAS S.A. FOR 2018

Pursuant to Article 382 § 3 of the Code of Commercial Companies and § 20 paragraph 1 item 2) letter a), of the Articles of Association of the Bank, the Supervisory Board of Bank BGŻ BNP Paribas S.A. conducted an assessment of the financial statements of the Bank for the year ended 31 December 2017, the Management Board Report on the activities of Bank BGŻ BNP Paribas S.A., and the recommendation of the Management Board on the allocation of the profit for the year ended 31 December 2018.
The aforementioned assessment has been made based on:

1. The financial statements of the Bank for the year ended 31 December 2018 covering:

- statement of financial position prepared as at December 31, 2018 showing total assets PLN 106 811 656 thou.,
- profit and Loss account statement for the period from January 1, 2018 to December 31, 2018 showing net profit of PLN 364 739thou.
- statement of total income for the period from January 1, 2018 to December 31, 2018, showing a total income of PLN 363 961 thou.,
- statement of changes in total equity for the period from January 1, 2018 to December 31, 2018 disclosing an increase in equity by PLN 4 010 303 thou.,
- cash-flow statement for the period from January 1, 2018 to December 31, 2018 disclosing a negative net cash in the amount of PLN 67 927 thou.,

and

- notes to financial statements.

2. Management Board Report on the activities of Bank BGŻ BNP Paribas S.A. for 2018.
3. Motion of the Management Board on the profit distribution for the year ended 31 December 2018.
4. Report of independent statutory auditor from audit of the financial statements of Bank BGŻ BNP Paribas S.A.

The Supervisory Board states as follows:

Based on the assessment of the financial statements of Bank BGŻ BNP Paribas S.A. for the year ended 31 December 2018, the Supervisory Board has concluded that these financial statements, in all material aspects, have been prepared:

- in accordance with the International Financial Reporting Standards approved by the European Union;
- based on properly maintained accounting records;
- in accordance with the provisions of the law governing preparation of the financial statements and provisions of the Bank's Articles of Association influencing the form and content of the financial statements;

and give a fair and clear view of all information material for the evaluation of the financial result of business activities for the period from 1 January 2018 to 31 December 2018, as well as the economic and financial position of Bank BGŻ BNP Paribas S.A. as at 31 December 2018.

SELECTED FINANCIAL DATA

PLN '000	12 months ended 31.12.2018	12 months ended 31.12.2017	Change y/y PLN '000	
Profit before income tax	472 678	471 257	1 421	0,3%
Net profit for the period	364 739	298 389	66 350	22,2%
Net profit for the period *excluding one-off events**	10 571 562	6 561 259	4 010 303	61,1%
Total equity	106 811 658	71 804 124	35 007 534	48,8%
Total assets	472 678	471 257	1 421	0,3%

* *One-off events: integration costs (2018 – PLN 265,804 thousand, 2017 –PLN 35, 641 thousand), allowance due to expected credit losses in the 12-month horizon (2018 – PLN 238,897 thousand) and profit from the bargain purchase of the Core Business of RBPL (2018 - PLN 291,706 thousand.*

SEPARATE STATEMENT OF PROFIT AND LOSS

Bank BGŻ BNP Paribas S.A. generated a net profit of PLN 364,739 thousand in 2018, that is PLN 66,350 thousand (22.2%) higher than the amount achieved in 2017.

The net banking income in the analysed period amounted to PLN 3,221,809 thousand and was higher by PLN 536,662 thousand, i.e. 20.0% y/y.

The most important event affecting the level of net profit in 2018 and the comparability of results from 2017 was the finalization (on 31 October 2018) of the acquisition of the Core Business of Raiffeisen Bank Polska S.A. ("RBPL") described in more detail in Chapter 4.2. "Acquisition of the Core Business of Raiffeisen Bank Polska S.A." of the Separate Financial Statement of Bank BGŻ BNP Paribas S.A. for the year ended on 31 December 2018.

As a consequence of the method used to perform and settle the transaction, in the statement of profit or loss of Bank BGŻ BNP Paribas S.A. for 2018, income and expenses of the Core Business of Raiffeisen Bank Polska S.A. generated after 31 October, 2018, i.e. for the last two months of 2018, have been included.

In addition, the following factors related to the aforementioned transaction have affected the comparability of results achieved in 2018 and 2017:

the initial settlement of the merger of entities and calculating the gain on a bargain purchase of the Core Business of RBPL, as a result of which the amount of PLN 291,706 thousand was recognized in the category of other operating income;

an allowance due to expected credit losses in the 12-month horizon for loans and advances to customers and amounts due from banks, without impairment as well as for debt securities recognized in the result of 2018, in the total amount of PLN 238,897 thousand;

integration costs in the amount of PLN 265,804 thousand in the operating expenses and other operating expenses in 2018 (including PLN 9,100 thousand related to the acquisition of SKOK Rafineria) as compared to PLN 35,641 thousand of integration costs in 2017 (concerning earlier merger processes of BGŻ S.A., BNP Paribas Bank Polska S.A. and Sygma Bank Polska S.A.).

Net interest income

Net interest income, constituting the main source of the Bank's income, for 12 months of 2018 amounted to PLN 2,076,518 thousand and was higher by PLN 160,146 i.e. by 8.4% y/y.

In 2018, as compared to 2017, net interest income increased by PLN 268,121 thousand, i.e. by 10.2% y/y with a simultaneous increase in interest expenses by PLN 107,975 thousand, i.e. by 15.0% y/y. A factor positively influencing the level of net interest income in 2018, but at the same time disturbing comparability with 2017, was the fact that the interest income and expenses generated by the acquired Core Business of Raiffeisen Bank Polska S.A. after 31 October 2018, i.e. for the last two months of 2018, were recognized in the profit or loss statement of Bank BGŻ BNP Paribas S.A. for 2018.

Among external factors affecting the level of net interest income, NBP's policy regarding the development of basic interest rates and their stabilization at a record low level (the reference rate as of March 2015 amounts to 1.5%) and market trends in determining interest rates on deposits should be mentioned.

The fact that the Bank's liquidity position was significantly improved as a result of finalizing the acquisition of the Core Business of RBPL (net loans / deposits ratio fell from 97.1% at the end of September 2018 to 79.6% at the end of December 2018) enabled optimization of the pricing policy pursued and, consequently, the improvement of deposit margins both in the case of liabilities to business entities and to retail customers.

The factor negatively affecting the level of the result of net interest income was the fact of lowering the interest rate on funds held as a mandatory reserve at the Central Bank (NBP). It is estimated that for this reason the net interest income in 2018 was lower than the result of 2017 by approx. PLN 15,286 thousand.

At the end of December 2018, the Bank applied fair value hedge accounting. The change in the fair value measurement of hedging transactions is recognized in the result on hedge accounting. Interest on IRS transactions and hedged items is recognized in net interest income. The net interest income on hedging relationships (the sum of interest income and interest expense from derivative instruments under fair value hedge accounting) for 2018 was positive and amounted to PLN 21,641 thousand against PLN 7,601 thousand in 2017.

Net fee and commission income

The net fee and commission income in 2018 amounted to PLN 535,172 thousand, and was higher by PLN 82,217 thousand, i.e. by 18.2% y/y.

A factor positively affecting the level of net fee and commission income in 2018 but at the same time disturbing comparability with 2017 was the fact that the fee and commission expenses generated by the acquired Core Business of Raiffeisen Bank Polska S.A. after 31 October 2018, i.e. for the last two months of 2018, were recognized in the profit or loss statement of Bank BGŻ BNP Paribas S.A. for 2018.

The fee and commission income increased in 2018 as compared to 2017 by PLN 110,621 thousand, i.e. by 19.5% y/y while fee and commission expenses increased by PLN 28,404 thousand i.e. by 24.9%.

The increase in fee and commission income was recorded primarily in terms of income from:

- payment and credit cards - by PLN 28,430 thousand, i.e. by 31.4%,
- asset management and brokerage operations by PLN 21,681 thousand, i.e. by 53.8%,
- lending and leasing activities by PLN 18,178 thousand i.e. by 9.4%,
- execution of transfers and electronic banking services by PLN 10,184 thousand, i.e. by 20.6%,
- guarantee obligations and documentary operations by PLN 9,082 thousand, i.e. by 30.9%.

The increase in fee and commission expense was mainly caused by higher expenses related to:

- intermediation in the sale of the Bank's products and acquiring customers by PLN 16,000 thousand, i.e. by 198.1%,
- handling payment and credit cards by PLN 5,533 thousand, i.e. by 7.3%,
- cash services by PLN 2,805 thousand i.e. by 79.6%,
- other commissions by PLN 2,123 thousand, i.e. by 30.9%.

Dividend income

Dividend income in 2018 was derived from the profits of the companies for 2017, in which the Bank held minority interests, i.e.: Biuro Informacji Kredytowej S.A. (PLN 3,944.0 thousand), Krajowa Izba Rozliczeniowa S.A. (KIR, PLN 783.7 thousand) and VISA (PLN 132.4 thousand), as well as from the profits of subsidiaries: BNP Paribas Group Service Center S.A. (PLN 3,387.9 thousand), TFI BGŻ BNP Paribas S.A. (PLN 2,257.0 thousand).

Dividend income in 2017 came respectively from Krajowa Izba Rozliczeniowa S.A. (KIR, PLN 827.5 thousand), Biuro Informacji Kredytowej S.A. (BIK, PLN 3 881.0 thousand) and VISA organization (PLN 65.9 thousand) and from the profits of subsidiaries: BNP Paribas Group Service Center S.A. (PLN 14,899.6 thousand) and BGŻ BNP Paribas Faktoring Sp. z o.o. (PLN 5 645,6 thousand). In addition, the Bank received an advance dividend from the profit of BNP Paribas Group Service Center S.A. for 2017 in the amount of PLN 12,197.2 thousand.

Net trading income and net investment income

The net trading income in 2018 amounted to PLN 330,619 thousand, and was higher by PLN 79,164 thousand, i.e. by 31.5% y/y. The level and volatility of this result are mainly determined by the valuation of derivative instruments and the result on the exchange position. A factor positively influencing the result on trading activities in 2018 was the fact that the Bank recognized the results of the RBPL Core Business for the last two months of 2018.

The net investment income for 2018 amounted to PLN 47,405 thousand, and was higher by PLN 19,007 thousand, i.e. by 66.9% as compared to the result achieved in 2017.

In 2018, the most important item were the profits from the sale of debt instruments in the amount of PLN 41,244 thousand (including PLN 30,228 thousand in the fourth quarter). The change in the valuation of the portfolio of loans and advances to customers measured at fair value through profit and loss statement as a result of the adjustment to IFRS 9 was positive and amounted to PLN 5,984 thousand.

The result of 2017 consists of profits from the sale of a portfolio of securities available for sale in the amount of PLN 25,543 thousand, and profit from the sale of shares in the amount of PLN 2,855 thousand, including: PLN 2,757 thousand which concerns the sale of shares in BGŻ BNP Paribas Faktoring Sp. z o.o., completed in the fourth quarter of 2017.

Other operating income

Other operating income in 2018 amounted to PLN 393,193 thousand and was higher by PLN 259,819 thousand, i.e. by 194.8% as compared to the previous year.

The increase was primarily due to recognition of PLN 291,706 thousand gain on a bargain purchase, which is the excess of the fair value of the acquired assets and liabilities at the acquisition date over the purchase price of the Core Business of RBPL, under other operating income.

In addition, the level of other operating income in 2018 was positively affected by the increase in income from recovered indemnities by PLN 10,672 thousand, i.e. by 423.5%.

The amount of other operating income in 2018 was adversely affected by:

- a decrease in other operating income by PLN 19,326 thousand, i.e. by 36.2% (the level of this category in 2017 was affected by higher income from re-invoicing and the release of provisions for legal risks, in addition, this item includes the annual adjustment of VAT tax for 2016 - in 2017 in the amount of PLN 7.9 million as compared to the annual adjustment of the calculated tax for 2017 in the amount of PLN 2.9 million - recognized in 2018),
- a drop in profit on the sale or liquidation of fixed assets and intangible assets by PLN 11,452 thousand, i.e. by 45.7%,
- lower income from the release of provisions for litigation and claims by PLN 8,491 thousand, i.e. by 80.0%.

Other operating expenses

Other operating expenses in 2018 amounted to PLN 161,606 thousand and were higher by PLN 22,718 thousand (i.e. by 16.4%) as compared to 2017. The following factors had impact on the current level of operating expenses:

- integration expenses in the amount of PLN 29.6 million (PLN 22.1 million - provision for branch restructuring, PLN 7.5 million - impairment allowance on property, plant and equipment). In 2017, the impact of this category was positive and amounted to 126 thousand;
- reduction of losses on the sale or liquidation of fixed assets and intangible assets by PLN 10,719 thousand, i.e. by 40.1%,
- no impairment allowance on other receivables, which in 2017 amounted to PLN 10,244 thousand (the largest impact on this item was the creation, in the first quarter of 2017, of provisions for unsettled balances of card transactions resulting from the migration of IT systems after the end of the operational merger),
- costs related to compensations, penalties and fines incurred in 2018 in the amount of PLN 2,574 thousand,
- higher costs of debt collection by PLN 2,446 thousand, i.e. by 7.3%.usand.

Net impairment losses on financial assets and provisions for contingent liabilities

The result of impairment losses on financial assets and provisions for contingent liabilities in 2018 amounted to PLN 537,275 thousand and its negative impact on the Bank's results was higher by PLN 194,856 thousand, i.e. by 56.9% y/y.

As a result of the acquisition of the Core Business of Raiffeisen Bank Polska S.A. in 2018, an allowance for expected credit losses in the 12-month horizon for loans and advances to customers and amounts due from banks, without impairment as well as for debt securities, in the total amount of PLN 238,897 thousand was recognized, which was the reason for the deterioration of the balance of allowances as compared to 2017.

In 2018, the Bank concluded agreements regarding the sale of a retail and SME loan portfolios. The amount of receivables sold under agreements covered in a significant part by impairment losses, or derecognized, amounted to PLN 1,072,097 thousand (principal, interest and other side charges). The contractual price for the sale of these portfolios has been set at 126,152 thousand PLN. The net impact on the Bank's result from the sale of portfolios amounted to PLN 30,436 thousand and is presented in the creation and release of impairment allowances on loans and advances.

In 2017, the Bank concluded 9 agreements regarding the sale of the loan portfolio. The amount of receivables (covered by a significant portion of impairment losses, orderecognized) sold under the agreements amounted to PLN 651,152 thousand (principal, interest and other side charges). The contractual price for the sale of these portfolios has been set at PLN 138,119 thousand. The net effect on the Bank's result from the sale of portfolios amounted to PLN 34,881 thousand and was presented in the net impairment losses on financial assets and provisions for contingent liabilities.

The cost of credit risk calculated as the ratio of gross impairment losses to loans and advances to customers measured at amortized cost (calculated on the basis of balances at the end of quarters) amounted to 0.95% in 2018 and deteriorated by 34 p.p. in comparison to 2017 (0.61%). Excluding an additional allowance due to expected credit losses in the 12-month horizon for loans and advances to customers and amounts due from banks, without impairment as well as for debt securities (incurred in connection with the finalization of the acquisition of the Core Business Raiffeisen Bank Polska S.A.), the cost of credit risk would amount to 0.53% and would be 8 bps lower than in 2017.

Considering the key operating segments:

Retail and Business Banking segment recorded an improvement in the balance of allowances by PLN 49,894 thousand y/y,

SME Banking segment - improvement by PLN 29,207 thousand y/y,

Corporate Banking segment (including CIB) - deterioration by 34,397 thousand y/y.

General administrative expenses, personnel expenses, amortization and depreciation

General administrative expenses (including depreciation and amortization) of Bank BGŻ BNP Paribas for 2018 amounted to PLN 1,988,734 thousand and were higher by PLN 333,129 thousand i.e. 20.0% as compared to 2017.

The increase in the expenses was mainly due to the merger of the Bank with the Core Business of Raiffeisen Bank Polska S.A. (RBPL) on 31 October 2018 and the integration costs incurred thereby in 2018.

The total amount of integration costs in 2018 amounted to PLN 265.8 million (including PLN 9.1 million related to the SKOK Rafineria acquisition) against PLN 35.6 million in 2017, out of which:

- PLN 236.2 million has been included in general administrative expenses,
- PLN 29.6 million - in other operating expenses (PLN 22.1 million - branch restructuring provision, PLN 7.5 million - impairment allowance for property, plant and equipment),

The integration costs booked in the overall administrative costs mainly include:

- creation of a provision for employment restructuring - PLN 128.5 million (RBPL) and PLN 2.0 million (SKOK),
- creation of a provision for retention programs - PLN 10.9 million (RBPL),
- costs of legal and consulting services - 49.7 million PLN (RBPL PLN 48.3 million, SKOK PLN 1.4 million),
- costs of accruing accelerated depreciation of systems in connection with the merger processes of banks - PLN 18.5 million.

The largest increase in expenses by type y/y (by PLN 218.6 million) took place in the item "personnel expenses", including:

PLN 156.2 million of the expenses resulting from the RBPL acquisition (PLN 128.5 million - costs of the provision related to employment restructuring, PLN 10.9 million - provision for local retention programs),

PLN 70.8 million resulting from the increase in employment at the Bank due to the acquisition of RBPL employees.

In addition, the level of expenses in 2018 was influenced by higher:

- advisory and consulting expenses related to the preparation for the merger of the Bank with the Core Business of RBPL and the acquisition of SKOK "Rafineria" (included in the non-personnel expenses) - PLN 49.7 million,
- IT and telecommunications expenses related to the increase in the Bank's operations after the merger with RBPL, the integration costs in this item in 2018 amounted to PLN 6.5 million,
- marketing expenses, which resulted from the expenses incurred in connection with the integration, more advertising campaigns (cash loan campaigns, personal account campaigns, campaigns for small businesses) and image-related activities (Szlachetna Paczka (Noble Gift), sponsoring of tennis events),
- contributions to BFG - total contributions recognized in the expenses of 2018 amounted to PLN 117.3 million and were PLN 21.8 million higher than in the previous year, including:
  - the annual contribution to the banks' resolution fund for 2018 (recognized in the first half of the year) was PLN 52.8 million and was PLN 2.2 million higher than in the corresponding period of the previous year,
  - the contribution to the bank guarantee fund due for 12 months of 2018 amounted to PLN 64.5 million and was higher by PLN 19.6 million, which was influenced, inter alia, by merger of the Bank with the Core Business of Raiffeisen Bank Polska S.A. (estimated expenses on this account amount to PLN 6.6 million).

At the same time, a decrease in expenses was recorded in rent expenses by PLN 6.1 million resulting from the optimization of office space (headquarters of the Bank's Head Office at Suwak Street in Warsaw) and sales network (market stands, business centres) as well as the restructuring of the Bank's branch network.

In 2018, the expenses of transformation projects carried out at the Bank amounted to PLN 25.0 million and were higher by PLN 9.6 million as compared to the expenses incurred in 2017.

Depreciation and amortization expenses in 2018 amounted to PLN 188.8 million and were higher by PLN 15.3 million as compared to the previous year, which results mainly from the expenses of accrued accelerated depreciation and amortization (PLN 18.5 million), with simultaneous decrease of depreciation and amortization expenses due to liquidation of assets after the merger of Bank BGŻ with BNP Paribas Bank Polska SA and Sygma Bank Polska SA

STATEMENT OF OTHER COMPREHENSIVE INCOME

The Bank's comprehensive income in 2018 amounted to PLN 363,961 thousand and was by PLN 76,897 thousand lower than in 2017.

The main reason for the observed decline was the lack of a positive change in the valuation of financial assets in 2018 comparable to that observed in 2017 (a positive impact on the comprehensive income of 2017 in the amount of PLN 174,084 thousand, as compared to PLN 831 thousand in 2018), partially offset by the increase in net profit generated in the periods compared.

STATEMENT OF FINANCIAL POSITION

Assets

The total assets of the Bank as at the end of December 2018 amounted to PLN 106,811,658 thousand and was higher by PLN 35,007,534 thousand, i.e. by 48.8%, as compared to the end of December 2017. The change in the scale of the Bank's activity resulted from the finalization of the acquisition of Core Business of RBPL on 31 October 2018, described in detail in Chapter 4.2. "Acquisition of the Core Business of Raiffeisen Bank Polska S.A." of the Separate Financial Statement of Bank BGŻ BNP Paribas S.A. for the year ended on 31 December 2018.

The most important changes in the structure of the Bank's assets that took place as a result of the transaction are: a decrease in the share of loans and advances to customers (the total of portfolios measured at amortized cost and fair value) with simultaneous increase in the share of securities and financial instruments (in 2017, financial assets available for sale).

The structure of assets is dominated by loans and advances to customers whose share accounted for 66.7% of total assets at the end of 2018 as compared to 72.7% at the end of 2017. In terms of value, the volume of net loans and advances increased by PLN 19,091,964 thousand i.e. by 36.6%.

The second largest asset were securities and financial instruments, which accounted for 26.2% of the total assets at the end of 2018 (at the end of 2017, financial assets available for sale: 19.4%). In 2018, their value increased by PLN 14,096,501 thousand, i.e. 101.3%, mainly as a result of an increase in the portfolio of bonds issued by central level government institutions.

At the same time, the above changes saw a decrease from 3.5% to 0.7% in the share of net amounts due from banks, which dropped by PLN 1,724,386 thousand, i.e. by 68.6%, mainly in the position of current accounts and interbank deposits.

Loan portfolio

Structure and quality of the loan portfolio

At the end of December 2018, gross loans and advances to customers (the total of portfolios measured at amortized cost and at fair value) amounted to PLN 74,426,387 thousand and increased by 19,459,284 thousand, i.e. by 35.4% compared to the end of 2017.

As part of the portfolio valued at amortized cost, the share of loans and advances granted to business entities excluding farmers (PLN 33,521,398 thousand at the end of 2018) increased by 10.6 p.p. and was 46.6%. Loans to individual customers (PLN 27,000,114 thousand) account for 37.6%, with more than half of this portfolio being mortgage loans (PLN 16,054,468 thousand), which account for 22.3% of the entire portfolio measured at amortized cost (decrease by 2.5 p.p. compared to the end of 2017). In the third place are the loans to farmers (PLN 8,681,538 thousand), despite their decline in the entire portfolio by 7.9 p.p., to 12.1% at the end of 2018.

The share of impaired exposures in gross loans and advances to customers and measured at amortized cost improved to 5.8% at the end of 2018 as compared to 7.5% at the end of 2017.

In December 2017, the Bank performed a securitization transaction on the portfolio of cash and car loans. The transaction is a traditional securitization involving the transfer of ownership of the securitized receivables to SPV (BGŻ Poland ABS1 DAC based in Ireland). The revolving period is 24 months.

SPV issued bonds with a total value of PLN 2,180,850 thousand on the basis of securitized assets, and received a loan of PLN 119,621 thousand, which were secured by a registered pledge on the rights to cash flows from securitized assets.

As a result of securitization, the Bank obtained financing in exchange for the transfer of rights to future cash flows resulting from the securitized loan portfolio with a value of PLN 2,300,471 thousand as of 22 November 2017 (the so called cut-off). The maximum deadline for full redemption of bonds and repayment of the loan is 27 April 2032.

The main benefit of the transaction is a positive impact on capital adequacy ratios as well as improved liquidity and diversification of funding sources.

In the light of the records of IAS 39 and IFRS 9, the contractual terms of a securitization do not fulfil the conditions to derecognize securitized assets. In connection with the above, the Bank recognizes securitized assets under the item Loans and advances granted to customers as at 31.12.2018 at net value of PLN 2,150,316 thousand. At the same time, the Bank recognizes a liability due to cash flows from securitisations in the item "Amounts due to customers" in the amount equal to PLN 2,178,530 thousand on 31.12.2018. As att 31.12.2018, the Bank was also in a possession of receivables due to settlements with a securitization company in the amount of PLN 119,721 thousand. These receivables are presented under Other assets.

Liabilities and equity

As of the end of December 2018, the total value of the Bank's liabilities amounted to PLN 96,240,096 thousand, and was by PLN 30,977,231 thousand or 47.5% higher than at the end of 2017. The increase in the scale of the Bank's operations was the result of finalizing on 31 October 2018 the purchase of Core Business of RBPL, described in detail in Chapter 4.2. "Acquisition of the

Core Business of Raiffeisen Bank Polska S.A." Separate Financial Statements of Bank BGŻ BNP Paribas S.A. for the year ended on 31 In the analysed period, the share of liabilities in total liabilities and equity of the Bank remained at a similar level and amounted to 90.1% at the end of December 2018.

In the analysed period, the share of liabilities in total liabilities and equity of the Bank remained at a similar level and amounted to 90.1% at the end of December 2018.

The most significant change in the structure of the Bank's liabilities at the end of 2018 as a result of the acquisition of the Core Business of RBPL was an increase in the share of amounts due to customers (by 3.1 p.p.) with a simultaneous decrease in the share of liabilities to banks. In terms of value, the volume of amounts due to customers at the end of December 2018 increased by PLN 30,849,490 thousand, i.e. by 52.6% as compared to the end of 2017 and amounted to PLN 89,506,557 thousand.

The total value of liabilities to banks as of the end of December 2018 amounted to PLN 1,589,935 thousand and was by PLN 1,336,461 thousand lower than at the end of 2017 (i.e. by 45.7%), with a decrease in loans and advances received from banks and an increase in the share of current accounts and term deposits.

The reduction in debt securities issued is related to the redemption in the first quarter of 2018 of deposit certificates issued on the basis of contracts signed in March 2008 with a total nominal value of PLN 285,000 thousand. In addition, this item in 2017 includes bonds for the total amount of PLN 2,180,850 thousand with a maximum initial maturity date of 21 April 2032, issued in December 2017 by the SPV, as a result of the transaction of securitization of the portfolio of consumer loans carried out by the Bank. The repayment of bonds is secured by receivables from loans and advances subjected to securitization.

Amounts due to customers

At the end of December 2018, amounts due to customers amounted to PLN 89,506,557 thousand, recording growth in almost all product groups and business segments as compared to the end of 2017, which is mainly due to the increase in the scale of the Bank's operations after finalizing the acquisition of Core Business of RBPL.

The largest volume increase (by PLN 17,043,210 thousand) is related to individual customers' deposits, which accounted for 49.9% of all amounts due to customers at the end of December 2018 (increase in the share by 2.8 pp as compared to the end of 2017).

The volume of business entities amounted to PLN 37,283,001 thousand and increased by PLN 12,620,180 thousand, i.e. by 51.2% (of which PLN 11,583,293 thousand were related to current accounts). At the same time, their share in the total amounts due to customers decreased to 41.7% as compared to 42.0% at the end of December 2017.

Non-banking financial entities and institutions of the public sector increased in total by PLN 1,185,100 thousand (increase by 18.6% y/y).

<u>The share of current accounts</u> in the structure of amounts due to customers in total amounted to 62.2% at the end of 2018, noting an increase by 10.5 p.p. as compared to 2017. The funds deposited on current accounts amounted to PLN 55,635,473 thousand and increased by PLN 25,284,432 thousand, i.e. by 83.3%. This was the result of an increase in the volume in the segment of individual customers (by PLN 12,809,999 thousand, +86.5% y/y), as well as funds deposited in current accounts by business entities (by PLN 11,583,293 thousand, +80,4% y/y).

<u>The share of term deposits</u> in the structure of amounts due to customers in the analysed period amounted to 33.8% and decreased by 7.2 p.p. as compared to the end of 2017. Value of term deposits increased by PLN 6,183,702 thousand, i.e. by 25.7% as compared to December 2017 and reached the level of PLN 30,239,128 thousand. The increase mainly concerned the segment of individual customers (increase in volume by PLN 4,088,106 thousand).

<u>The share of loans and advances received and other liabilities</u> in the structure of amounts due to customers totalled 1.5% and decreased by 1.8 p.p. as compared to December 2017.

Equity

As of the end of December 2018, the Bank's equity amounted to PLN 10,571,562 thousand and was PLN 4,010,303 thousand, i.e. by 61.1% higher than at the end of 2017. This increase was the result of:

- increase in share and reserve capital as a result of the J and K series shares issue (the issue value was PLN 799,995 thousand,
- of which PLN 13,300 thousand of share capital, supplementary capital PLN 786,695 thousand, costs of issue reducing the
- reserve capital of -PLN 2,867 thousand);
- increase in share and reserve capital as a result of the issue of L series shares (the issue value amounted to PLN 3,250,000
- thousand, of which share capital was PLN 49,881 thousand, reserve capital PLN 3,200,119 thousand);
- allocating the entire Bank's net profit for 2017 in the amount of PLN 298,389 thousand to the reserve capital in accordance with the Resolution of the Ordinary General Shareholders' Meeting of Bank BGŻ BNP Paribas S.A. of 18 May 2018.

EQUITY AND CAPITAL RATIOS

The total capital ratio of the Bank as at 31 December 2018 amounted to 15.02% and increased as compared to December 2017 by 1.10 p.p. The stand-alone Common Equity Tier 1 capital ratio (CET I) and the stand-alone Tier 1 capital ratio at the end of 2018 were the same and amounted to 12.72% (increase as compared to the end of 2017 by 1.77 p.p.).

Total own funds as at 31 December 2018 increased by PLN 4,541,048 thousand as compared to 31 December 2017, which resulted mainly from the inclusion in own funds of the following items:

- the Bank's net profit for the first half of 2018, in the amount of PLN 194,073 thousand (consent of the Polish Financial Supervision Authority of 27 September 2018),
- the Bank's net profit for the third quarter of 2018, in the amount of PLN 134,237 thousand PLN (consent of the Financial Supervision Authority of 13 December 2018),
- PLN 799,995 thousand connection with the classification of J and K series shares issued by Bank BGŻ BNP Paribas S.A. as instruments in Common Equity Tier 1 (approval of the Polish Financial Supervision Authority of 10 July 2018),
- PLN 3,250,000 thousand in connection with the classification of L series shares issued by Bank BGŻ BNP Paribas S.A. (merger of Bank BGŻ BNP Paribas S.A. with Core Business of Raiffeisen Bank Polska S.A. on 31 October 2018) as instruments in Common Equity Tier 1 (approval of the Polish Financial Supervision Authority of 21 November 2018).

In accordance with the Resolution of the Ordinary General Shareholders' Meeting of Bank BGŻ BNP Paribas S.A. of 18 May 2018, the Bank's entire profit for 2017 in the amount of PLN 298,389 thousand PLN was allocated to reserve capital.

The total risk exposure amount as of 31 December 2018 amounted to PLN 81,493,415 thousand and increased by PLN 26,185,434 thousand as compared to 31 December 2017, which resulted primarily from the merger of Bank BGŻ BNP Paribas S.A. with the Core Business of Raiffeisen Bank Polska S.A. on 31 October 2018.

In accordance with the Act of 5 August 2015 on macroprudential supervision of the financial system and crisis management in the financial sector and the Regulation of the Minister of Finance from 1 January 2018, the capital requirements applicable to banks in Poland increased through:

- introducing a systemic risk buffer of 3%;
- increase in the capital conservation buffer level from 1.25% to 1.875%.

On 8 August 2018, the Bank received a letter from the Polish Financial Supervision Authority (PFSA) informing about the PFSA's review of the adequacy of the buffer rate of other systemically important institution. As a result of the review, the PFSA concluded that there were no reasons to repeal or amend the PFSA's Decision of 4 October 2016, as set out in the PFSA Decision of 19 December 2017 on the Bank (on a consolidated and separate basis) of the buffer of other systemically important institutions equivalent to 0.25% of the total risk exposure amount.

On 15 October 2018, the Bank received a recommendation from the Polish Financial Supervision Authority to maintain own funds of the Bank to cover an additional capital requirement of 0.36 p.p. in order to hedge the risk resulting from FX mortgage loans for households, which should consist at least in 75% of Tier 1 capital (corresponding to 0.27 p.p.) and at least in 56% of Common Equity Tier 1 capital (which corresponds to 0.20 p.p.). On 30 November 2018, these levels were confirmed by the PFSA as being applicable also at the consolidated level.

As a result of the above changes, the minimum levels of capital adequacy ratios resulting from legal regulations and administrative decisions issued by the Polish Financial Supervision Authority ("PFSA") as of 31 December 2018, are as follows:

- Common Equity Tier 1 ratio (CET I) = 9.83%;
- Tier I capital ratio = 11.40%;
- Total capital ratio = 13.49%.

On 12 December 2017, the European Parliament and the EU Council adopted Regulation No. 2017/2395 amending the Regulation (EU) No 575/2013 regarding transitional arrangements to mitigate the impact of the introduction of IFRS 9 on equity and on the treatment of large exposures to entities in the sector publicly denominated in the national currency of any Member State. This Regulation entered into force on the day following its publication in the Official Journal of the European Union and has been applicable since 1 January 2018. The European Parliament and the Council (EU) decided that the application of IFRS 9 could lead to a sudden increase in allowances for expected credit losses, and hence, the fall in Tier 1 capital.

The Group, after analysing the requirements of Regulation No. 2017/2395, decided to apply the transitional provisions provided for in this Regulation, which means that the full impact of the implementation of IFRS 9 will not be taken into account for the assessment of capital adequacy of the Bank. As a result of adjusting the calculation of regulatory capital requirements, it was estimated that taking into account the full impact of the implementation of IFRS 9 on the total capital ratio of the Bank would reduce its value by 69 basis points.

FINANCIAL RATIOS

The Bank's return on equity (ROE) calculated in a normalized approach (excluding the impact of integration costs, additional allowance for expected credit losses for non-impaired loans and receivables and gain on a bargain purchase of the Core Business of RBPL) amounted to 6.6% in 2018 and it was 1.4 p.p. higher than in 2017. Return on assets (ROA) calculated in the same way amounted to 0.6% and increased as compared to 2017 by 0.1 p.p. The ratios calculated on the basis of reported amounts amounted to 4.9% (ROE, up by 0.2 p.p. y/y) and 0.5% (ROA, up by 0.1 p.p. y/y).

The Cost / Income ratio (excluding the integration costs and gain on a bargain purchase of the Core Business of RBPL) was at the level of 59.6%, lower by 1.1 p.p. as compared to 2017. The ratio calculated on the basis of the reported amounts amounted to 62.0%, i.e. unchanged as compared to 2017.

Presentation of ratios calculated on the basis of the profit and loss account category excluding the costs of additional allowances due to expected credit losses in 12 month horizon, gain on a bargain purchase of RBPL Core Business and integration costs (understood as additional costs related to the merger processes) is aimed at providing additional information allowing the assessment of the current potential of the combined banks.

The net interest margin calculated in relation to average assets was 2.7% and did not change as compared to the level calculated for 2017.

The cost of credit risk decreased as compared to the level recorded in 2017 by 0.08 p.p. and amounted to 0.53%. Taking into account the additional allowances for expected credit losses in 12-month horizon, the cost of credit risk amounted to 0.95% in 2018.

The ratio of net loans and advances to deposits improved as compared to the end of 2017 due to the favourable liquidity-wise structure of the acquired assets and liabilities of the Core Business of RBPL.

Financial ratios

	31.12.2018	31.12.2017	31.12.2016	change 2018/2017
Return on equity(1)	6.6%*	5.2%*	3.0%*	1.4 p.p.
Return on assets(2)	0.6%*	0.5%*	0.3%*	0.1 p.p.
Net interest margin(3)	2.7%	2.7%	2.6%	0.0 p.p.
Cost/Income(4)	59.6%*	60.7%*	65.0%*	(1.1 p.p.)
Cost of credit risk(5)	(0.53%)*	(0.61%)	(0.75%)	0.08 p.p.
Net loans and advances/Deposits(6)	79.6%	91.3%	99.8%	(11.7 p.p.)
Gross loans and advances/Total source of funding(7)	80.9%	87.1%	90.0%	(6.2 p.p.)

** Normalized values calculated excluding: integration costs (2018 – PLN 265,804 thousand, 2017 – PLN 35,641 thousand, 2016 – PLN 173 453 thousand), allowance due to expected credit losses created in connection with the acquisition of the Core Business of RBPL (2018: PLN 238,897 thousand) and the gain on the bargain purchase of the Core Business of RBPL (2018: PLN 291,706 thousand). The impact of integration costs was estimated using the standard 19% income tax rate. In the case of the "costs" category, the amount visible in the financial statements was reduced by the amount of integration costs recorded as general administrative expenses and depreciation. In the case of the "income" category, the amount of the income statement comprising the result from banking activities was adjusted for the integration costs recorded under other operating costs and the gain on bargain purchase of the Core Business of the RBPL.*

(1) Net profit in relation to average equity, calculated based on quarter-end balances (annualized ratio).

(2) Net profit in relation to average assets, calculated based on quarter-end balances (annualized ratio).

(3) Net interest income in relation to average assets, calculated based on quarter-end balances (annualized ratio). Due to a significant increase in the balance sheet total as of 31 October 2018 and the prospective recognition of the interest result of the acquired Core Business of RBPL for the last two months of 2018 in the Bank's interest result - for the fourth quarter of 2018 the weighted average number of days was assumed.

(4) Total general administrative expenses, amortization and depreciation in relation to total net banking income, calculated as the total of net interest income, net fee and commission income, dividend income, net trading income, net investment income, result on hedge accounting and other operating income and expenses.

(5) Net impairment losses on loans and advances in relation to the average balance of net loans and advances to customers, calculated based on quarter-end balances (annualized ratio).

(6) (Net) loans and advances to customers in relation to customer deposits, balance at the end of the period.

(7) Gross loans and advances to customers in relation to total liabilities to customers, debt securities issued, loans from other banks and subordinated liabilities, balance at the end of the period.

ASSESSMENT MADE BY THE SUPERVISORY BOARD

After becoming acquainted with the Financial statements of Bank BGŻ BNP Paribas S.A. for the year ended on 31 December 2018 prepared by the Management Board, and the Report of the independent statutory auditor for audit of the financial statement of Bank BGŻ BNP Paribas S.A. for the year ended on 31 December 2018, the Supervisory Board decides to give a positive opinion to the Financial statement of the Bank for the year ended on 31 December 2018, and recommend the approval of the financial statements to the Ordinary General Meeting.

2. REPORT OF THE MANAGEMENT BOARD ON ACTIVITY OF BANK BGŻ BNP PARIBAS S.A. FOR 2018

The Supervisory Board declares that the report of the Management Board on activity of Bank BGŻ BNP Paribas S.A. in 2018 is factually correct and consistent with the books and documents, including information contained in the Financial statement of Bank BGŻ BNP Paribas S.A. for the year ended on 31 December 2018. The Supervisory Board recommends the approval of the report of the Management Board on activity of the Bank BGŻ BNP Paribas S.A. in 2018 to the Ordinary General Meeting of Bank BGŻ BNP Paribas S.A.

3. RECOMMENDATION OF THE MANAGEMENT BOARD ON 2018 PROFIT ALLOCATION

Supervisory Board hereby recommends to the Ordinary Shareholders Meeting of the Bank that the whole profit after taxation (net profit) for the fiscal year 2018 in the amount of PLN 364 738 878,03 PLN (three hundred sixty four million seven hundred thirty eight thousand eight hundred seventy eight zlotys and three grosz) shall be transferred to the reserve capital.

4. FINANCIAL STATEMENTS OF THE BANK'S CAPITAL GROUP

Pursuant to § 20 paragraph 1 item 2) letter b) of the Articles of Association, the Supervisory Board of Bank BGŻ BNP Paribas S.A. conducted an assessment of the consolidated financial statements of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended 31 December 2018 and the report on the activity of the Capital Group in 2018.

The aforementioned assessment was conducted on the basis of:

1. Bank BGŻ BNP Paribas S.A. Capital Group consolidated financial statements for the year ended on 31 December 2018 covering:

- consolidated statement of financial situation drawn up as at December 31, 2018 with balance sheet total of PLN 109 022 519 thou.,
- consolidated profit and loss account for the period from January 1, 2017 to December 31, 2017 showing net profit of PLN 360 378,
- consolidated statement of comprehensive income for the period from January 1, 2018 to December 31, 2018 showing a total income of PLN 359 569 thou.,
- consolidated statement of changes in equity for the period from January 1, 2018 to December 31, 2018 showing a increase in equity of PLN 4 000 350 thou.,
- consolidated cash-flow statement for the period from January 1, 2018 to December 31, 2018 disclosing a negative net cash in the amount of PLN 17 752 thou.,

and

- notes to the consolidated financial statements.

2. Report of the Management Board on the activities of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended on 31 December 2018.

3. Report of independent statutory auditor on audit of the consolidated financial statements of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended on 31 December 2018.

The Supervisory Board states as follows:

As a result of the assessment of consolidated financial statements of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended on 31 December 2018, the Supervisory Board states that the statements in all relevant aspects:

- have been drawn up in accordance with the International Financial Reporting Standards approved by the European Union,
- are compliant with legal provisions regulating the preparation of financial statements, which affect the form and contents of the financial statements,

and reliably and clearly present all information relevant for the assessment of the financial result on the business activity for the period from 1 January 2018 to 31 December 2018, as well as the economic and financial position of Bank BGŻ BNP Paribas S.A. Capital Group as at 31 December 2018.

SELECTED FINANCIAL DATA

PLN '000	12 months ended 31.12.2018	12 months ended 31.12.2017	Change YoY	
			PLN 000	%
Profit before income tax	468 896	453 885	15 011	3,3%
Net profit for the period	360 378	279 707	80 671	28,8%
Net profit for the period *excluding one-off events**	484 528	308 576	175 952	57,0%
Total equity	10 559 813	6 559 463	4 000 350	61,0%
Total assets	109 022 519	72 655 491	36 367 028	50,1%

** One-off events: integration costs (2018 – PLN 265,804 thousand, 2017 – PLN 35,641 thousand), allowance due to expected credit losses in the 12-month horizon (2018 – PLN 238,897 thousand) and gain on the bargain purchase of the Core Business of RBPL (2018 - PLN 291,706 thousand).*

Note: As the figures have been rounded up, the totals in the tables and charts of this Report may not add up

CONSOLIDATED STATEMENT OF PROFIT OR LOSS

In 2018 the Bank BGŻ BNP Paribas SA Capital Group generated a net profit of PLN 360,378 thousand, i.e. by PLN 80,671 thousand (28.8%) higher than the one achieved in 2017.

The result on the banking activity of the Group in the analysed period amounted to PLN 3,289,086 thousand, and was higher y/y by PLN 593,106 thousand, i.e. by 22.0%.

The most important event affecting the level of net profit in 2018 and the comparability of results from 2017 was the finalization on 31 October 2018 of the acquisition of the Core Business of Raiffeisen Bank Polska S.A. ("RBPL") described in more detail in Chapter 4.2. "Acquisition of the Core Business of Raiffeisen Bank Polska S.A." of the Consolidated Financial Statements of the Bank BGŻ BNP Paribas S.A. Capital Group for the year ended 31 December 2018.

As a consequence of the method used to perform and settle the transaction, the income and expenses of the Core Business of Raiffeisen Bank Polska S.A. for the last two months of 2018 are recognized in the profit or loss account of the Bank Capital Group for 2018 (implemented after 31 October 2018).

In addition, the following factors related to the aforementioned transaction have affected the comparability of results achieved in 2018 and 2017:

- the initial settlement of the merger of entities and calculating the gain on the bargain purchase of the Core Business of RBPL, as a result of which the amount of PLN 291,706 thousand was recognized in the category of other operating income.
- an allowance due to expected credit losses in the 12-month horizon for loans and advances to customers and amounts due from banks, without impairment as well as for debt securities, recognized in the result of 2018, in the total amount of PLN 238,897 thousand.
- integration costs in the amount of PLN 265,804 thousand recognized in the general administrative expenses and other operating expenses in 2018 (including PLN 9,100 thousand related to the acquisition of SKOK Rafineria) as compared to PLN 35,641 thousand of integration costs in 2017 (concerning earlier merger processes of BGŻ S.A., BNP Paribas Bank Polska S.A. and Sygma Bank Polska S.A.).

Net interest income

Net interest income, constituting the main source of the Group's income, for the 12 months of 2018 amounted to PLN 2,106,851 thousand, and increased y/y by PLN 180,107 thousand, i.e. by 9.3%.

In 2018, as compared to 2017, interest income increased by PLN 318,611 thousand, i.e. by 12.0% y/y with a simultaneous increase in interest expenses by PLN 138,504 thousand, i.e. by 18.8% y/y.

A factor positively influencing the level of net interest income in 2018, but at the same time disturbing comparability with 2017, was the fact that Bank BGŻ BNP Paribas S.A. Capital Group recognized the interest income and expenses of the acquired Core Business of Raiffeisen Bank Polska S.A. generated after 31 October 2018, i.e. for the last two months of 2018, in the profit or loss account for 2018.

Among external factors affecting the level of net interest income, NBP's policy regarding the development of basic interest rates and their stabilization at record low level (the reference rate as of March 2015 amounts to 1.5%) and market trends in determining interest rates on deposits should be mentioned.

The fact that the Group's liquidity position was significantly improved as a result of finalizing the acquisition of the Core Business of RBPL (net loans / deposits ratio fell from 104.9% at the end of September 2018 to 84.2% at the end of December 2018) enabled optimization of the pricing policy pursued and, consequently, the improvement of deposit margins both in the case of liabilities to business entities and to retail customers.

The factor negatively affecting the level of the result of net interest income was the fact of lowering the interest rate on funds held as a mandatory reserve at the NBP. It is estimated that for this reason the net interest income in 2018 was lower than the result of 2017 by approx. PLN 15,286 thousand.

At the end of December 2018, the Group applied fair value hedge accounting. The change in the fair value measurement of hedging transactions is recognized in the result on hedge accounting. Interest on IRS transactions and hedged items is recognized in net interest income. The net interest income on hedging relationships (the sum of interest income and interest expense from derivative instruments under fair value hedge accounting) for 2018 was positive and amounted to PLN 21,641 thousand against PLN 7,601 thousand in 2017.

Net fee and commission income

The net fee and commission income in 2018 amounted to PLN 567,390 thousand and was higher by PLN 81,411 thousand, i.e. by 16.8% y/y.

A factor positively affecting the level of net fee and commission income in 2018 but at the same time disturbing comparability with 2017 was the fact that Bank BGŻ BNP Paribas S.A. Capital Group in the statement of profit or loss for 2018 has recognized the fee and commission income and expenses of the Core Business of Raiffeisen Bank Polska S.A., realized in the last two months of 2018.

The fee and commission income increased in 2018 as compared to 2017 by PLN 123,233 thousand , i.e. by 20.5% y/y while commission costs increased by PLN 41,822 thousand PLN, i.e. by 36.2%.

The increase in fee and commission income was recorded primarily in terms of revenues from:

- asset management and brokerage operations by PLN 41,919 thousand PLN, i.e. by 85.0%,
- payment and credit cards by PLN 28,430 thousand, i.e. by 31.4%,
- lending and leasing activities by PLN 20,097 thousand, i.e. by 10.4%,
- execution of transfers and electronic banking services by PLN 10,184 thousand, i.e. by 20.6%,
- guarantee obligations and documentary operations by PLN 9,082 thousand, i.e. by 30.9%.

The increase in fee and commission expense was mainly caused by higher expenses related to:

- asset management and brokerage operations of PLN 17,778 thousand, i.e. 762.7%,
- intermediation in the sale of the Bank's products and acquisition of customers by PLN 16,000 thousand , i.e. by 198.1%,
- other commissions by PLN 3,177 thousand, i.e. by 46.1%,
- cash service by PLN 2,818 thousand, i.e. by 79.9%.

Dividend income

Dividend income in 2018 was recognized from the profits of the companies for 2017, in which the Bank held minority interests, i.e.: Biuro Informacji Kredytowej S.A. (BIK, PLN 3,944.0 thousand), Krajowa Izba Rozliczeniowa S.A. (KIR, PLN 773.7 thousand) and VISA (PLN 132.4 thousand).

Dividend income in 2017 came from the profits of companies for 2016, in which the Bank had minority interests, i.e.: Krajowa Izba Rozliczeniowa S.A. (KIR, PLN 827.5 thousand), Biuro Informacji Kredytowej S.A. (BIK, PLN 3,881.0 thousand) and VISA (PLN 65.9 thousand) and a former subsidiary BGŻ BNP Paribas Faktoring Sp. z o.o. (PLN 5,645.6 thousand).

Net trading income and net investment income

The net trading income in 2018 amounted to PLN 330,773 thousand and was higher by PLN 79,365 thousand, i.e. by 31.6% y/y. The level and volatility of this result is mainly determined by the valuation of derivative instruments and the result on the exchange position. A factor positively influencing the result on trading activities in 2018 was the fact that in the Group's result for 2018, the results of the Core Business of RBPL for the last two months of 2018 were recognized.

The net investment income for 2018 amounted to PLN 48,838 thousand and was higher by PLN 20,440 thousand, i.e. by 72.0% as compared to the result achieved in 2017.

In 2018, the most important item was the gain on the sale of debt instruments in the amount of PLN 41,244 thousand (including PLN 30,228 thousand in the fourth quarter). The change in the valuation of the portfolio of loans and advances to customers measured at fair value through profit or loss as a result of the adjustment to IFRS 9 was positive and amounted to PLN 5,984 thousand.

The result of 2017 consists of gain on the sale of a portfolio of securities available for sale in the amount of PLN 25,433 thousand and gain on the sale of shares in the amount of PLN 2,855 thousand, including PLN 2,757 thousand which concerns the sale of shares in BGŻ BNP Paribas Faktoring Sp. z o.o., completed in the fourth quarter of 2017.

Other operating income

Other operating income in 2018 amounted to PLN 387,778 thousand, and was higher by PLN 256,496 thousand, i.e. by 195.4% as compared to the previous year.

The increase was primarily due to recognition under other operating income of PLN 291,706 thousand gain on a bargain purchase, which is the excess of the fair value of the acquired assets and liabilities at the acquisition date over the purchase price of the Core Business of RBPL.

In addition, the level of other operating income in 2018 was positively influenced by:

- increase in income from the sale of goods and services by PLN 10,962 thousand, i.e. by 267.2%,
- increase in income due to recovered indemnities by PLN 10,672 thousand, i.e. by 423.5%.

The amount of other operating income in 2018 was adversely affected by:

- decrease in other operating income by PLN 36,611 thousand, i.e. by 80.6% (the level of this category in 2017 was affected by higher incomes from re-invoicing and the release of provisions for legal risks, in addition, this item includes the annual adjustment of VAT tax charged for 2016 - in 2017 in the amount of PLN 7.9 million as compared to the annual adjustment of the calculated tax for 2017 in the amount of PLN 2.9 million - recognized in 2018),
- decrease in gain on the sale or liquidation of fixed assets and intangible assets by PLN 11,345 thousand, i.e. by 45.2%,

lower income from the release of provisions for litigation and claims by PLN 8,750 thousand, i.e. by 80.1%.

Other operating expenses

Other operating expenses in 2018 amounted to PLN 147,407 thousand, and were higher by PLN 5,912 thousand (i.e. by 4.2%) as compared with 2017. The following factors had impact on the current level of operating expenses:

- integration expenses in the amount of PLN 29.6 million (PLN 22.1 million - provision for branch restructuring, PLN 7.5 million - impairment write-off for property, plant and equipment). In 2017, the impact of this category was positive and amounted to PLN 126 thousand,
- reduction of losses on the sale or liquidation of fixed assets and intangible assets by PLN 10,707 thousand, i.e. by 40.1%,
- no expenses generated due to impairment allowance on other receivables, which in 2017 amounted to PLN 10,244 thousand (the largest impact on this item was the creation, in the first quarter of 2017, of provisions for unsettled balances of card transactions resulting from the migration of IT systems after the end of the operational merger),
- costs related to compensations, penalties and fines incurred in 2018 in the amount of PLN 2,576 thousand,
- higher costs of debt collection by PLN 2,727 thousand, i.e. by 8.1%.

Net impairment losses on financial assets and provisions for contingent liabilities

The result of impairment allowances on financial assets and provisions for contingent liabilities in 2018 amounted to PLN 557,682 thousand, and its negative impact on the Group's results was higher by PLN 202,383 thousand, i.e. by 57.0% y/y.

As a result of the acquisition of the Core Business of Raiffeisen Bank Polska S.A. in 2018, an allowance due to expected credit losses in the 12-month horizon for loans and advances to customers and amounts due from banks, without impairment as well as for debt securities was recognized, in the total amount of PLN 238,897 thousand, which was the reason for the deterioration of the total balance of allowances as compared to 2017.

In 2018, the Bank concluded agreements regarding the sale of portfolios of retail and SME loans. The amount of receivables sold under agreements covered in a significant part by impairment allowances, or derecognized, amounted to PLN 1,072,097 thousand (principal, interest and other side charges). The contractual price for the sale of these portfolios has been set at PLN 126,152 thousand. The net impact on the Bank's result from the sale of portfolios amounted to PLN 30,436 thousand and is presented in the creation and release of impairment allowance on loans and advances.

In 2017, the Bank concluded 9 agreements regarding the sale of the loan portfolio. The amount of receivables (covered by a significant amount of impairment allowances, or derecognized) sold under the agreements amounted to PLN 651,152 thousand (principal, interest and other side charges). The contractual price for the sale of these portfolios has been set at PLN 138,119 thousand. The net effect on the Bank's result from the sale of portfolios amounted to PLN 34,881 thousand and was presented in the result of impairment allowances on financial assets and provisions for contingent liabilities.

The cost of credit risk expressed as the ratio of net impairment allowances on loans and advances to customers, measured at amortized cost (calculated on the basis of balances at the end of the quarters) amounted to 0.96% in 2018 and deteriorated by 35 bps in comparison to 2017 (0.61%). Excluding an additional allowance due to expected credit losses in the 12-month horizon for loans and advances to customers and amounts due from banks, without impairment as well as for debt securities in the total amount of PLN 238,897 thousand recognized in connection with the purchase of the Core Business of RBPL the cost of credit risk in 2018 would amount to 0.55% and would improve by 6 bps.

Considering the key operating segments[1]:

- the Retail and Business Banking segment recorded an improvement in the balance of allowances by PLN 49,894 thousand y/y,
- SME Banking segment - improvement by PLN 29,207 thousand y/y,
- Corporate Banking segment (including CIB) - deterioration by PLN 34,397 thousand y/y.

General administrative expenses, personnel expenses, amortization and depreciation

General administrative expenses (including depreciation and amortization) of the Bank BGŻ BNP Paribas Capital Group for 2018 amounted to PLN 2,049,386 thousand, and were higher by PLN 368,456 thousand, i.e. by 21.9% as compared to 2017.

The increase in the expenses was mainly due to the merger of the Bank with the Core Business of Raiffeisen Bank Polska S.A. (RBPL) on 31 October 2018 and the integration costs incurred thereby in 2018.

- PLN 29.6 million - in other operating expenses (PLN 22.1 million - branch restructuring provision, PLN 7.5 million - impairment write-off for property, plant and equipment),

The integration costs booked in the overall administrative costs mainly include:

- creation of a provision for employment restructuring - PLN 128.5 million (RBPL) and PLN 2.0 million (SKOK),
- creation of a provision for retention programs - PLN 10.9 million (RBPL),
- costs of legal and consulting services – PLN 49.7 million (RBPL PLN 48.3 million, SKOK PLN 1.4 million),
- costs of accruing accelerated depreciation of systems in connection with the merger processes of banks - PLN 18.5 million.

The largest increase in expenses by type y/y (by PLN 225.2 million) occurred in the item "personnel expenses", which is mainly due to the costs of provisions created for employment restructuring and employment growth due to the acquisition of RBPL employees (increase of costs by PLN 70.8 million) and inclusion in the Group's structure of employees of three companies previously owned by the RBPL Capital Group.

In addition, the level of expenses in 2018 was influenced by the increase of the following expenses:

- advisory and consulting expenses related to the preparation for the merger of the Bank with the Core Business of RBPL and the acquisition of SKOK "Rafineria" (included in the item other non-personnel costs) - PLN 49.7 million,
- IT and telecommunications expenses related to the increase in the Bank's operations after the merger with RBPL, the integration costs in this item in 2018 amounted to PLN 6.5 million,

[1] *Information based on the note on operational segments included in the Consolidated financial statements of the Bank BGŻ BNP Paribas S.A. Capital Group for the year ended 31 December 2018*

- marketing expenses, which resulted from the expenses incurred in connection with the integration, more advertising campaigns (cash loan campaigns, personal account campaigns, campaigns for small businesses) and image-related activities (Szlachetna Paczka (Noble Gift), sponsoring of tennis events),
- contributions to BFG – total contributions included in the expenses of 2018 amounted to PLN 117.3 million and were by PLN 21.8 million higher than in the previous year, including:
  - the annual contribution to the banks' resolution fund for 2018 (settled in the first half of the year) was PLN 52.8 million and was PLN 2.2 million higher than in the corresponding period of the previous year,
  - the contribution to the Bank Guarantee Fund due for 12 months of 2018 amounted to PLN 64.5 million and was higher by PLN 19.6 million, which was influenced, inter alia, by merger of the Bank with the Core Business of Raiffeisen Bank Polska S.A. (estimated expenses on this account amounted to PLN 6.6 million).

At the same time, a decrease was recorded in rent expenses of PLN 5.0 million resulting from the optimization of office space (headquarters of the Bank's Head Office at Suwak Street in Warsaw) and sales network (market stands, business centres) as well as the restructuring of the Bank's branch network.

In 2018, the expenses of transformation projects conducted at the Bank amounted to PLN 25.0 million and were higher by PLN 9.6 million as compared to the costs incurred in 2017.

Depreciation and amortization expenses in 2018 amounted to PLN 189.7 million and were higher by PLN 15.7 million as compared to the previous year, which results mainly from the costs of accelerated depreciation and amortization (PLN 18.5 million), with a simultaneous decrease in depreciation and amortization expenses due to liquidation of assets after the merger of Bank BGŻ with BNP Paribas Bank Polska S.A. and Sygma Bank Polska S.A.

STATEMENT OF COMPREHENSIVE INCOME

The comprehensive income of the Capital Group in 2018 amounted to PLN 359,569 thousand, and was by PLN 62,623 thousand lower than in 2017.

The main reason for the observed decline was the lack of a positive change in the valuation of financial assets in 2018 comparable to that observed in 2017 (a positive impact on the total income of 2017 in the amount of PLN 174,113 thousand, as compared to PLN 789 thousand in 2018), partially offset by the increase in net profit generated in the periods compared.

STATEMENT OF FINANCIAL POSITION OF THE CAPITAL GROUP

Assets

The total assets of the Group as at the end of December 2018 amounted to PLN 109,022,519 thousand and were higher by PLN 36,367,028 thousand, i.e. by 50.1%, as compared to the end of December 2017. The change in the scale of the Group's activity resulted from the finalization, on 31 October 2018, of the acquisition of the Core Business of RBPL, described in detail in Chapter 4.2. "Acquisition of the Core Business of Raiffeisen Bank Polska S.A." of the Consolidated Financial Statements of the Bank BGŻ BNP Paribas S.A. Capital Group for the year ended 31 December 2018.

The most important changes in the structure of the Bank's assets that occurred as a result of the transaction are: a decrease in the share of loans and advances to customers (the sum of portfolios measured at amortized cost and fair value) with simultaneous increase in the share of securities and financial instruments (in 2017: financial assets available for sale).

The structure of assets is dominated by loans and advances to customers whose share accounted for 67.3% of all assets at the end of 2018 compared to 72.9% at the end of 2017. In terms of value, the volume of net loans and advances increased by PLN 20,446,382 thousand , i.e. by 38.6%.

The second largest asset were securities and financial instruments, which constituted 25.7% of the balance sheet total at the end of 2018 (at the end of 2017, financial assets available for sale: 19.2%). In 2018, their value increased by PLN 14,096,458 thousand, i.e. 101.2%, mainly as a result of an increase in the portfolio of bonds issued by central government institutions.

At the same time, the above changes were paralleled by a decrease from 3.6% to 0.9% in the share of amounts due from banks, which dropped by PLN 1,642,193 thousand, i.e. by 63.1%, mainly in the item of current accounts and interbank deposits.

Loan portfolio

Quality and structure of loan portfolio

At the end of December 2018, gross loans and advances to customers (the total of portfolios measured at amortized cost and at fair value) amounted to PLN 76,595,082 thousand, and increased by PLN 20,842,734 thousand, i.e. by 37.4% compared to the end of 2017.

As regards the portfolio measured at amortized cost, the share of loans and advances to business entities excluding farmers (PLN 33,932,209 thousand at the end of 2018) increased by 10.3 p.p. and was at the level of 45.8%. Loans for retail customers (PLN 27,001,876 thousand) account for 36.5%, with more than half of this portfolio being mortgage loans (PLN 16,054,468 thousand), which account for 21.7% of the entire portfolio measured at amortized cost (decrease by 2.7 p.p. compared to the end of 2017). Ranked third are loans for farmers (PLN 8,681,538 thousand) despite the decrease in their share in the entire portfolio by 8.0 p.p., to 11.7% at the end of 2018.

The ratio of impaired exposures in total gross loans and advances to customers and measured at amortized cost improved to 5.6% at the end of 2018 as compared to 7.4% at the end of 2017.

In December 2017, the Bank performed a securitization transaction on the portfolio of cash and car loans. The transaction is a traditional securitization involving the transfer of ownership of the securitized receivables to SPV (BGŻ Poland ABS1 DAC based in Ireland). The revolving period is 24 months.

SPV issued bonds with a total value of PLN 2,180,850 thousand on the basis of securitized assets, and received a loan of PLN 119,621 thousand, which were secured by a registered pledge on the rights to cash flows from securitized assets.

As a result of securitization, the Bank obtained financing in exchange for the transfer of rights to future cash flows resulting from the securitized loan portfolio in a value of PLN 2,300,471 thousand as of 22 November 2017 (the cut-off date). The maximum deadline for full redemption of bonds and repayment of the loan is 27 April 2032.

The main benefit of the performed transaction is a positive impact on capital adequacy ratios and improvement of liquidity and diversification of financing sources.

In the light of the provisions of IAS 39 and IFRS 9, the contractual terms of the securitization do not fulfil the conditions for derecognition of securitized assets. In connection with the above, the Bank recognizes securitized assets in "Loans and advances to customers" as at 31 December 2018 at net value of PLN 2,150,316 thousand. At the same time, as at 31 December 2018 the Bank recognizes a liability due to cash flows from securitizations in "Amounts due to customers" in the amount equal to PLN 2,178,530 thousand as at 31 December 2018. As at 31 December 2018, the Bank held receivables due to settlements with a securitization company in the amount of PLN 119,721 thousand. These receivables are presented in "Other assets".

Liabilities and equity

As at the end of December 2018, the total value of the Group's liabilities amounted to PLN 98,462,706 thousand, and was by PLN 32,366,678 thousand , i.e. by 49.0% higher than at the end of 2017. The increase in the scale of the Bank's operations was the result of finalizing, on 31 October 2018, the acquisition of the Core Business of RBPL, described in detail in Chapter 4.2. "Acquisition of the Core Business of Raiffeisen Bank Polska S.A." in the Separate Financial Statements of Bank BGŻ BNP Paribas S.A. for the year ended 31 December 2018.

In the analysed period, the share of liabilities in total liabilities and equity of the Group remained at a similar level and amounted to 90.3% at the end of December 2018.

The most significant change in the structure of the Group's liabilities at the end of 2018 as a result of the acquisition of the Core Business of RBPL was an increase in the share of amounts due to customers (by 3.3 p.p.) to the level of 88.6%. In terms of value, the volume of amounts due to customers at the end of December 2018 increased by PLN 30,862,811 thousand, i.e. by 54.8% compared to the end of 2017 and amounted to PLN 87,191,708 thousand.

The total value of amounts due to banks as of the end of December 2018 amounted to PLN 3,976,469 thousand, and was by PLN 85,234 thousand higher than at the end of 2017 (i.e. by 2.2%), with a decrease in loans and advances received from banks and an increase in the share of current accounts and interbank deposits.

The reduction in debt securities issued is related to the redemption of deposit certificates issued on the basis of contracts signed in March 2008 with a total nominal value of PLN 285,000 thousand, conducted in the first quarter of 2018. In addition, this item includes bonds for the total amount of PLN 2,180,850 thousand, with a maximum initial maturity date of 27 April 2032, issued in December 2017 by SPV, as a result of the transaction of securitization of the portfolio of consumer loans performed by the Bank. The repayment of bonds is secured by receivables from loans and advances subject to securitization.

Amounts due to customers

At the end of December 2018, amounts due to customers amounted to PLN 87,191,708 thousand, recording growth in almost all product groups and business segments as compared to the end of 2017, which is mainly due to the increase in the scale of the Bank's operations after finalizing the acquisition of the Core Business of RBPL.

The largest volume increase (by PLN 17,103,395 thousand) is related to individual customers' deposits, which accounted for 51.3% of all amounts due to customers at the end of December 2018 (share increase by 2.2 p.p. compared to the end of 2017). The volume of business entities amounted to PLN 37,339,344 thousand, and increased by PLN 12,676,523 thousand, i.e. 51.4% (including: PLN 11,583,293 thousand related to current accounts). At the same time, their share in the total amounts due to customers decreased to the level of 42.8%, as compared to 43.8% at the end of December 2017.

Non-banking financial entities and the public sector institutions increased in total by PLN 1,082,893 thousand (increase by 27.0% y/y).

<u>The share of current accounts</u> in the structure of amounts due to customers totalled 63.6% at the end of 2018, recording an increase of 9.8 p.p. in comparison to 2017. The funds deposited on current accounts amounted to PLN 55,490,951 thousand, and increased by PLN 25,156,068 thousand, i.e. 82,9%. This was the result of an increase in the volume in the segment of individual customers (by PLN 12,809,999 thousand, +86.5% y/y), and in the business entities segment (by PLN 11,583,293 thousand, + 80.4% y/y).

<u>The share of term deposits</u> in the structure of amounts due to customers in the analysed period amounted to 34.7% and decreased by 8.0 p.p. compared to the end of 2017. Value of term deposits increased by PLN 6,205,644 thousand, i.e. by 25.8% compared to December 2017 and reached the level of PLN 30,239,128 thousand. The increase mainly concerned the segment of individual customers (increase in volume by PLN 4,088,106 thousand).

<u>The share of loans and advances received</u> <u>and other liabilities</u> in the structure of amounts due to customers dropped by 1.8 p.p.

Equity

As of the end of December 2018, the Group's equity amounted to PLN 10,559,813 thousand, and was by PLN 4,000,350 thousand, i.e. by 61.0% higher than at the end of 2017. This increase was the result of:

- increase in share and reserve capital as a result of the J and K series shares issue (the issue value was PLN 799,995 thousand, including PLN 13,300 thousand of share capital, PLN 786,695 thousand of supplementary capital, PLN - 2,867 thousand of costs of issue reducing the reserve capital);
- increase in share and reserve capital as a result of the issue of L series shares (the issue value amounted to PLN 3,250,000 thousand, including PLN 49,881 thousand of share capital, PLN 3,200,119 thousand of reserve capital);
- allocating to the reserve capital the entire Bank's net profit for 2017 in the amount of PLN 298,389 thousand in accordance with the Resolution of the Ordinary General Shareholders' Meeting of Bank BGŻ BNP Paribas S.A. of 18 May 2018.

EQUITY AND CAPITAL RATIOS

The total capital ratio of the Group as at 31 December 2018 amounted to 14.63% and increased as compared to December 2017 by 0.88 p.p. The consolidated Common Equity Tier 1 ratio (CET I) and consolidated Tier 1 ratio (Tier I) of the Group at the end of 2018 were the same and amounted to 12.38% (increase compared to the end of 2017 by 1.57 p.p.).

Total own funds as at 31 December 2018 increased by PLN 4,510,465 thousand as compared to 31 December 2017, which resulted mainly from the allocation to the own funds of the following items:

- the Bank's net profit for the first half of 2018, in the amount of PLN 194,073 thousand (consent of the Polish Financial Supervision Authority of 27 September 2018),
- the Bank's net profit for the third quarter of 2018, in the amount of PLN 134,237 thousand (consent of the Financial Supervision Authority of 13 December 2018),
- PLN 799,995 thousand in connection with the classification of issued series J and K shares as instruments in Common Equity Tier 1 (approval of the Polish Financial Supervision Authority of 10 July 2018),
- PLN 3,250,000 thousand in connection with the classification of issued series L shares (merger of Bank BGŻ BNP Paribas S.A. with Raiffeisen Bank Polska S.A.'s Core Business on 31 October 2018) as instruments in Common Equity Tier 1 (approval of the Polish Financial Supervision Authority of 21 November 2018).

In accordance with the Resolution of the Ordinary General Shareholders' Meeting of Bank BGŻ BNP Paribas S.A. of 18 May 2018, the Bank's entire profit for 2017, in the amount of PLN 298,389 thousand, was allocated to reserve capital.

As at 31 December 2018, the total risk exposure amounted to PLN 83,451,281 thousand and increased by PLN 27,526,151 thousand as compared to 31 December 2017, which resulted primarily from the merger of Bank BGŻ BNP Paribas S.A. with the Core Business of Raiffeisen Bank Polska S.A. on 31 October 2018.

In accordance with the Act of 5 August 2015 on macroprudential supervision of the financial system and crisis management in the financial sector and the Regulation of the Minister of Finance from 1 January 2018, the capital requirements applicable to banks in Poland increased through:

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In accordance with the Act of 5 August 2015 on macroprudential supervision of the financial system and crisis management in the financial sector and the Regulation of the Minister of Finance from 1 January 2018, the capital requirements applicable to banks in Poland increased through:

- introducing a systemic risk buffer of 3%;
- increase in the capital conservation buffer level from 1.25% to 1.875%.

On 8 August 2018, the Bank received a letter from the Polish Financial Supervision Authority (PFSA) informing about the PFSA's review of the adequacy of the buffer rate of other systemically important institution. As a result of the review, the PFSA concluded that there were no reasons to repeal or amend the PFSA's decision of 4 October 2016, as set out in the PFSA Decision of 19 December 2017 on the Bank (on a consolidated and stand-alone levels) of the buffer of other systemically important institutions equivalent to 0.25% of the total risk exposure amount.

On 15 October 2018, the Bank received a recommendation from the Polish Financial Supervision Authority to maintain equity of the Bank to cover an additional capital requirement of 0.36 p.p. in order to hedge the risk resulting from FX mortgage loans for households, which should consist at least in 75% of Tier 1 capital (corresponding to 0.27 p.p.) and at least in 56% of Common Equity Tier 1 capital (which corresponds to 0,20 p.p.). On 30 November 2018, these levels were confirmed by the PFSA as being applicable also on the consolidated level.

As a result of the above changes, the minimum levels of capital adequacy ratios resulting from legal regulations and administrative decisions issued by the PFSA as at 31 December 2018, are as follows:

- Common Equity Tier 1 ratio (CET I) = 9.83%;
- Tier I capital ratio = 11.40%;
- Total Capital Ratio = 13.49%

On 12 December 2017, the European Parliament and the EU Council adopted Regulation No. 2017/2395 amending the Regulation (EU) No 575/2013 regarding transitional arrangements to mitigate the impact of the introduction of IFRS 9 on equity and on the treatment of large exposures to entities in the sector publicly denominated in the national currency of any Member State. This Regulation entered into force on the day following its publication in the Official Journal of the European Union and has been applicable since 1 January 2018. The European Parliament and the Council (EU) decided that the application of IFRS 9 could lead to a sudden increase in allowances for expected credit losses, and hence, the decrease in Tier 1 capital.

The Group, after analysing the requirements of Regulation No. 2017/2395, decided to apply the transitional provisions provided for in this Regulation, which means that the full impact of the implementation of IFRS 9 will not be taken into account for the assessment of capital adequacy of the Bank. As a result of adjusting the calculation of regulatory capital requirements, it was estimated that taking into account the full impact of the implementation of IFRS 9 on the total capital ratio of the Bank would reduce its value by 70 basis points.

Financial ratios

The Group's return on equity (ROE) calculated in a normalized approach (excluding the impact of integration costs, additional allowances due to expected credit losses in the 12-month horizon for the non-impaired loans and the gain on a bargain purchase of the Core Business of RBPL) amounted to 6.5% in 2018 and it was by 1.7 p.p. higher than in 2017. Return on assets (ROA) calculated in the same way amounted to 0.6% and increased as compared to 2017 by 0.2 p.p. The ratios calculated on the basis of the reported amounts amounted to 4.8% (ROE, up by 0.4 p.p. y/y) and 0.5% (ROA, up by 0.1 p.p. y/y).

The Cost/Income ratio (excluding the integration costs and gain on the bargain purchase of the Core Business of RBPL) is at the level of 59.9%, lower by 1.1 p.p. as compared to 2017. The ratio calculated on the basis of the reported amounts amounted to 62.3%, i.e. the same as in 2017.

Presentation of ratios calculated on the basis of the profit or loss categories excluding the costs of additional allowances due to expected credit losses in 12 month horizon, gain on a bargain purchase of RBPL Core Business and integration costs (understood as additional costs related to the merger processes) is aimed at providing additional information allowing the assessment of the current potential of the combined banks.

The net interest margin calculated in relation to average assets was 2.7% and did not change as compared to the level calculated for 2017.

The cost of credit risk decreased as compared to the level recorded in 2017 by 0.06 p.p. and amounted to 0.55%. Taking into account the costs of additional allowance for expected credit losses, the cost of credit risk amounted to 0.96% in 2018.

The ratio of the net loans and advances to deposits improved as compared to the end of 2017 due to the favourable liquidity-wise structure of the acquired assets and liabilities of the Core Business of RBPL.

	31.12.2018	31.12.2017	31.12.2016	change 2018/2017
Return on equity(1)	6.5%*	4.8%*	3.6%*	+1.7 p.p.
Return on assets(2)	0.6%*	0.4%*	0.3%*	+0.2 p.p.
Net interest margin(3)	2.7%	2.7%	2.7%	0.0 p.p.
Cost/Income(4)	59.9%*	61.0%*	64.6%*	(1.1 p.p.)
Cost of credit risk(5)	(0.55%)*	(0.61%)	(0.74%)	(0.06 p.p.)
Net loans and advances/Deposits(6)	84.2%	96.6%	103.7%	(12.4 p.p.)
Gross loans and advances/Total source of funding(7)	81.3%	87.2%	90.4%	(5.9 p.p.)

** Normalized values calculated excluding: integration costs (2018 – PLN 265,804 thousand, 2017 – PLN 35,641 thousand, 2016 – PLN 181,404 thousand), allowance due to expected credit losses created in connection with the acquisition of the Core Business of RBPL (2018: PLN 238,897 thousand) and the gain on the bargain purchase of the Core Business of RBPL (2018: PLN 291,706 thousand). The impact of integration costs was estimated using the standard 19% income tax rate. In the case of the "costs" category, the amount visible in the financial statements was reduced by the amount of integration costs recorded as general administrative expenses and depreciation. In the case of the "income" category, the amount of the income statement comprising the result from banking activities was adjusted for the integration costs recorded under other operating costs and the gain on bargain purchase of the Core Business of the RBPL.*

(1) Net profit in relation to average equity, calculated based on quarter-end balances (annualized ratio).

(2) Net profit in relation to average assets, calculated based on quarter-end balances (annualized ratio).

(3) Net interest income in relation to average assets, calculated based on quarter-end balances (annualized ratio). Due to a significant increase in the balance sheet total as of 31 October 2018 and the prospective recognition of the interest result of the acquired Core Business of RBPL for the last two months of 2018 in the Bank's interest income - for the fourth quarter of 2018 the weighted average number of days was assumed.

(4) Total general administrative expenses, amortization and depreciation in relation to total net banking income, calculated as the total of net interest income, net fee and commission income, dividend income, net trading income, net investment income, result on hedge accounting and other operating income and expenses.

(5) Net impairment allowances on loans and advances in relation to the average balance of net loans and advances to customers, calculated based on quarter-end balances (annualized ratio).

(6) Net loans and advances to customers in relation to customer deposits, balance at the end of the period.

(7) Gross loans and advances to customers in relation to total liabilities to customers, debt securities issued, loans from other banks and subordinated liabilities, balance at the end of the period

ASSESSMENT MADE BY THE SUPERVISORY BOARD

After becoming acquainted with the Consolidated financial statements of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended on 31 December 2018 prepared by the Management Board, and the opinion and Report of the independent statutory auditor on the audit of consolidated financial statements of Bank BGŻ BNP Paribas S.A. Capital Group, the Supervisory Board decides to give a positive opinion to the financial statements of the Group for the year ended on 31 December 2018, and recommend the approval of the financial statements to the Ordinary General Meeting.

5. REPORT OF THE MANAGEMENT BOARD ON ACTIVITY OF BANK BGŻ BNP PARIBAS S.A. CAPITAL GROUP IN 2018

The Supervisory Board declares that the Report of the Management Board on activity of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended 31 December 2018 is factually correct, consistent with the books and documents, including information contained in the Consolidated financial statements of Bank BGŻ BNP Paribas S.A. Capital Group for the year ended on 31 December 2018. The Supervisory Board recommends the approval of the Report on activity of the Bank BGŻ BNP Paribas S.A. Capital Group for the year ended 31 December 2018 to the Ordinary General Meeting of Bank BGŻ BNP Paribas S.A.

6. ASSESSMENT OF REPORT ON THE NON-FINANCIAL INFORMATION OF BANK BGŻ BNP PARIBAS S.A. AND THE BANK BGŻ BNP PARIBAS S.A. CAPITAL GROUP IN 2018

As a result of the assessment of Report on the non-financial information of Bank BGŻ BNP Paribas S.A. and the Bank BGŻ BNP Paribas S.A. Capital Group in 2018 the Supervisory Board states that the report was prepared in compliance to Art. 49b of the Accounting Act dated 29 September 1994 and presents in a reliable and clear manner the non-financial effectiveness indicators connected to the Bank and Bank's Capital Group activities, as well as information on employment and natural environment matters that are relevant to the assessment of economic activity for the period from 1 January 2018 to 31 December 2018. The Supervisory Board recommends the approval of the Report on the non-financial information of Bank BGŻ BNP Paribas S.A. and the Bank BGŻ BNP Paribas S.A. Capital Group in 2018 to the Ordinary General Meeting of Bank BGŻ BNP Paribas S.A.

7. ASSESSMENT OF ADEQUACY AND EFFECTIVENESS OF THE INTERNAL CONTROL SYSTEM AT THE BANK

The organisation of the internal control system complies with the requirements set forth in the Banking Law Act of 29 August 1997, Ordinance of the Minister of Development and Finance of 6 March 2017 on risk management system and internal control system, remuneration policy, as well as detailed manner of internal capital estimation at banks and Recommendation H. The internal control system is the component of the Bank's management system, made of three defence lines that comprises: control mechanisms, independent monitoring of their application and activities of the Compliance Line and Internal Audit Line. The internal control system matches the specific nature of the business pursued and factors in the resources of the Bank. The Bank assesses annually the efficiency of the key control mechanisms, implementation testing as well as the adequacy and effectiveness of the internal control system.

The Management Board of the Bank is responsible for the effectiveness of the following: risk management system, internal control system, internal capital estimation process and performance of reviews, internal capital estimation and maintenance, likewise for supervision over the effectiveness of the respective processes, by making necessary adjustments and improvements in case of any change in the level of the risk involved in the Bank's operations, economic environment factors or any irregularities in functioning of systems or processes. Furthermore, the Management Board defines the principles governing operation of organisational units involved in the Bank's management and assumes responsibility for formulation, implementation and updating written policies, strategies and procedures in this respect.

The Supervisory Board oversees implementation and ensuring the operation of the adequate and effective internal control system at the Bank and assesses, on an annual basis, the adequacy and effectiveness of the internal control system, including the adequacy of the control function, compliance unit and internal audit unit, based on the formulated and approved assessment criteria as well as the opinions issued by the Audit Committee of the Bank. The assessment made by the Audit Committee is based, among others, on results of the audits carried out by the Internal Audit Line, of which the Committee is informed in periodic reports on the activity of the Internal Audit Line. In addition, the Audit Committee familiarizes itself with the progress in implementation of the recommendations issued by the Internal Audit Line, external auditor and supervision authorities.

The Audit Committee was informed of the changes introduced in the Audit Plan and degree of the Plan execution. The Internal Audit Line monitors on an ongoing basis the situation at the Bank and changes occurring in its environment, and if need arises, it makes necessary corrections in the Audit Plan.

The Compliance Line is tasked with compliance monitoring and provides support to the Management Board and Supervisory Board with respect to identification and assessment of the following types of risk:

1) compliance risk,
2) risks pertaining to counteracting money laundering and sanctions.

The compliance monitoring also cover employees' behaviours, systems and processes occurring at the Bank in terms of compliance with the requirements laid down in generally applicable law provisions, regulations implemented at the Bank as well as conduct standards, including market standards.

Identification and assessment of the compliance risk is performed based, among others, on an analysis of changes in the regulatory environment of the Bank, assessment of the compliance risk key factors, results of the compliance risk monitoring, including efficiency of the mechanisms ensuring the control over the risk, likewise opinions to internal regulations, issued by organisational units included in the Compliance Line, and risk assessment carried out as a part of the process of implementation of new banking products and services.

Results of the assessment are submitted to the Management Board of the Bank, and subsequently, to the members of the Supervisory Board through presentation of reports on the Compliance Line activity as a part of the works performed by the Audit Committee.

The Compliance Line supports decision-making processes at the Bank by assisting the Management Board of the Bank and Supervisory Board of the Bank in identifying and assessing the compliance risk, and by playing an advisory role in this respect as the Compliance Line points out potential threats and puts forward proposals of solutions to effectively control and monitor the compliance risk.

The Operational Risk, Credit Control and Fraud Prevention Line, within which the Operational Risk Department operates, is also the component of the internal control system. The Operational Risk Department supervises and coordinates the horizontal testing process at the Bank, carried out on a half-year basis, and process of assessment of the key control mechanisms, results of vertical testing as well as status of implementation of remedy and disciplinary measures, performed annually. Horizontal testing is performed on a permanent basis and reported every six months by managers of each unit of the Bank (network and Head Office units) or persons designated by them.

The Operational Risk Department prepares half-year reports on horizontal testing results, specifying the areas with the largest number of detected irregularities. Measures aimed at elimination of irregularities in future are determined in consultation with competent units. Reports are submitted to the Management Board for its approval.

The Operational Risk Department also oversees the process of vertical testing at the Bank, which constitutes the second level control, under which it coordinates and supports the implementation of the concept of Fundamental Monitoring Points (FMP) at the Bank, and cooperates with units responsible for operational controls performed at the Bank.

The Operational Risk, Credit Control and Fraud Prevention Line supports the Management Board and Supervisory Board in identification and assessment of the following types of risk:

1) operational risk,
2) fraud risk,
3) personal data risk.

SUPERVISORY BOARD ASSESSMENT

The Supervisory Board positively assessed the Bank's standing. At the same time, the Supervisory Board asserts that the system of internal control mechanisms is effective and efficient, except for gaps detected during the control processes. With respect to material deficiencies of the internal control system, the Supervisory Board monitored implementation of actions plans addressing the identified gaps in effectiveness and efficiency. As for the risk management, compliance and internal audit function systems, including control mechanisms covering financial reporting and operational activity, it is the view of the Supervisory Board that the respective systems operate correctly and match the Bank's activity level and complexity, as well as they comply with the adopted principles. In the opinion of the Supervisory Board, the internal control system is consistent with the level and complexity of the Bank's operations.

8. ASSESSMENT OF ADEQUACY AND EFFECTIVENESS OF RISK MANAGEMENT WITH REGARD TO RISKS ESSENTIAL FOR THE BANK

The system of risk management in the Bank is a formal system governed, i.a., by the policy of managing and reporting capital adequacy of the Bank (ICAAP), credit policy, policy of managing retail exposure risk, strategy of risk management, specifying the Bank's appetite for key risks associated with the Bank's activity, approved by the Supervisory Board. The Bank has a list of essential risks, approved by the Management Board, and the system of their measuring, limiting and reporting. The limits and thresholds for the major risks are specified once a year and reflected in the risk appetite statement of Bank BGŻ BNP Paribas. The Bank regularly monitors and reports compliance with the limits, and if a limit is exceeded, the Bank takes actions to restore the situation where the risks are held within the limits specified by the Management and Supervisory Boards of the Bank. Regular monitoring and reporting cover also the size and type of deviations from the principles and policies applicable in the Bank.

The Management Board of the Bank and the relevant Committees approve detailed policies and principles of risk management and perform daily supervision over the risk management system. The Bank operates the **Assets and Liabilities Committee (ALCO)** responsible for supervision and supporting management risks associated with financial liquidity risks and market risks within the Bank's portfolio. The Bank also has the **Risk Management Committee** responsible for various risks associated with Bank's activities including the risks associated falling under ALCO controls. The Bank has the **Internal Control Coordination Committee**, which supports the Bank's Management Board in implementing the Bank's operational risk strategy and in particular, performs control of consistency, completeness and effectiveness of the internal control system, and the processes of operational risk management. The Committee also manages major risks connected to the system of internal control in the Bank and its subsidiary entities.

With the above in mind as 31 December 2018 amongst others the following committees operated in the Bank:

- Risk Management Committee
- RB Risk Committee,
- PF Risk Committee,
- Credit Committee,
- Bad Loan Committee,
- Capital Investments Committee,
- Information Security and Business Continuity Committee,
- Internal Control Coordination Committee,
- Products, Services, Transactions and Activities Approval Committee (NPAO),
- Customer Approval Committee (CAC),
- Disciplinary Committee,
- Investment Project Committee,
- Assets and Liabilities Committee (ALCO),
- Reference Rate Quote Committee,
- Real Estate Committee,
- Brokerage House Investment Committee,
- Financial and Compliance Risk Committee,
- Procurement Committee,
- Bonds Committee,
- Compliance and Risk Evaluation Committee,
- Complaints Committee,
- Data Governance Strategy Committee.

The Bank's Management Board through dedicated committees obtains regular and comprehensive information on the Bank's exposures to credit risks, operational risks, financial liquidity risks as well as market and interest rate risks.

Appropriate committees within their competences define task which must be undertaken in case the Bank engages in excessive risks.

Supervisory Board regularly obtains reports prepared by organizational units of the Head Office covering significant risks in Bank's operations. Additionally the Supervisory Board has established two committees operating Internal Audit Committee and Risk Committee.

The scope of reported information covers the Bank's exposures to various risks including credit (including stress test risk), operational, interest rate and liquidity risks.

SUPERVISORY BOARD ASSESSMENT

In the opinion of the Supervisory Board the key risks management system is managed adequately and is carried out in accordance with policies adopted by the Bank.