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

Warsaw, 3 March 2014

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

1.1. MACROECONOMIC SITUATION

In the first half of 2013 the Polish economy was in a strong phase of slowdown. The Dynamics of Gross Domestic Product remained below the level of 1% y/y (0.5% y/y in Q1 2013 and 0.8% in Q2 2013), with negative growth in domestic demand (minus 0.9% y/y in Q1 2013 and minus 1.7% in Q2 2013). It was caused by decrease in investments and inventories, and also by stagnation of private consumption. However the contribution of net export was relatively high. This was due to low import (the effect of reducing domestic demand) and relatively high export (the effect of relatively weak zloty). In the second half of 2013 the economic recovery was observed, stimulated by an increase of export orders, also supported by increase in domestic demand. In 3Q 2013 the economic growth increased to 1.9% y/y and in 4Q 2013 – according to estimates of BGŻ S.A. – it increased to 2.8% y/y. In 2013 the Polish economy grew by 1.6% y/y compared to 1.9% y/y in 2012. The factors contributing to increase in domestic demand in the second half of 2013 were in particular gradual improvement in labor market and the relevant valorization of social benefits, as well as loosening of the Polish Financial Supervision Authority regulations regarding granting loans by the banking sector. Improvement related to investments was the lowest. This was a result of still high uncertainty about the economic outlook and low absorption of the EU funds.

Chart 1. Growth of GDP (y/y)

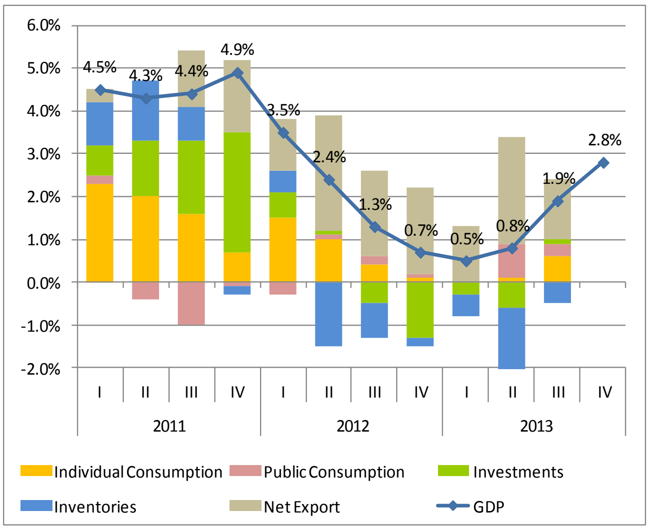
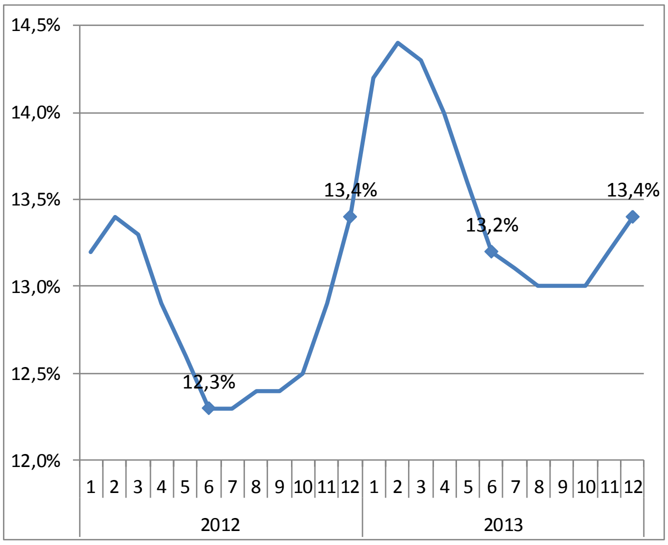


Chart 2. Registered unemployment rate



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

According to estimates, at the end of 2013 the number of employed in the national economy was higher by 0.6% than last year. The employment in the enterprise sector in the first half of 2013 decreased by 0.9% y/y and in the second half of 2013 only by 0.2%. In 4Q 2013 the annualized employment increased for the first time since 2Q 2012. High level of unemployment continued the entire 2013. The inflow into unemployment was slightly higher than last year, but at the same time the number of deletions from unemployed register increased, mainly due to starting work. At the end of December, while a slight increase in the number of registered unemployed was observed, the unemployment rate reached the level from previous year and amounted to 13.4%. Average monthly gross nominal salaries in the enterprise sector in 2013 grew slower than in 2012 (2.9% versus 3.4%), but their dynamics improved in the second half of the year. With a light increase in consumer prices, the purchasing power of wages in 2013 increased by 2.0%, while in the previous year a slight decrease was observed.

Gross agricultural output in 2013, according to preliminary estimates, increased by 1.5% compared to 2012. It was a result of an increase in both crop production (1.0%) and livestock (2.2%). A study conducted at the end of November 2013 indicates reduction in declining pig herd (up to 1.2% per annum). The number of cattle at the end of December 2013 was 1.4% higher than last year.

The economic slowdown and the decline in commodity prices, particularly agricultural and energy resulted in lower increase of prices of goods and services in 2013 as compared to 2012. The average increase amounted to 0.9% y/y in 2013 versus 3.7% in 2012. In addition, there was an average annual decrease in producer prices in industry and construction. Because of low level of actual and expected inflation rate, the Monetary Policy Council (MPC) decreased interest rates by a total of 175 basis points. Following the decrease, the central bank reference rate in July reached the level of 2.5%, which is the lowest in the transformation period (after 1989). The rediscount rate – which is the basis for setting interest rates for agricultural preference loans – was lowered to 2.75%.

In the first five months of 2013, the volatility on the foreign exchange market was moderate. The EUR/PLN exchange rate was in the narrow fluctuation band between 4.05 and 4.20, and USD/PLN exchange rate between 3.03 and 3.28. The stability of zloty was not harmed by the strong inflow of international capital to the domestic treasury bond market. However, in June depreciation of zloty took place and the EUR/USD rate reached more than the level of 4.30. This was the result of the speculations about the reduction of FED quantitative easing, which triggered the outflow of capital from the domestic treasury bond market. The zloty was also influenced by instability of political and budget situation in Poland, and also by speculations of open-end pension funds (OFE) reform. Along with the relaxing of Eurozone situation and Federal Reserve policies, the zloty stabilized in the second half of 2013. At the same time the volatility of the EUR/PLN rate fell to its lowest level in the history. However, zloty significantly appreciated against dollar. This was caused by the depreciation of dollar against euro, connected with improving the Eurozone prospects.

Chart 3. Inflation and interest rates

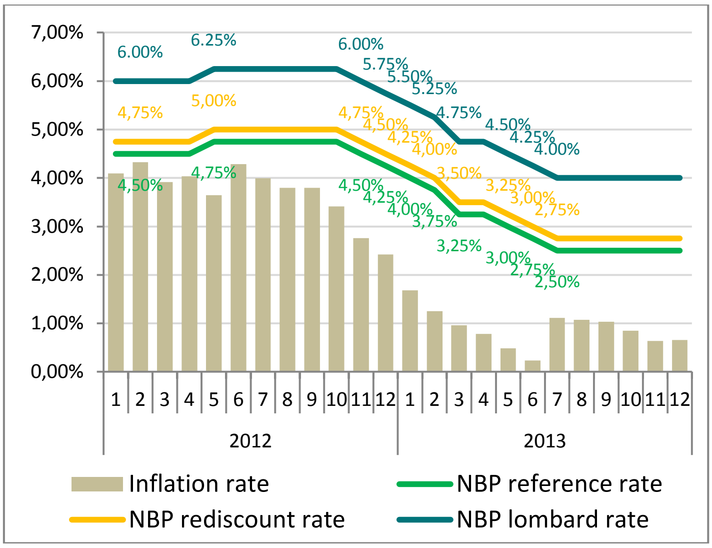
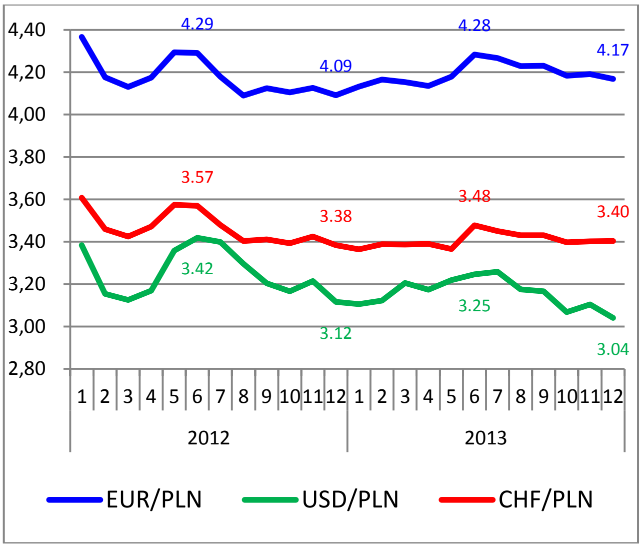


Chart 4. Exchange rate



Source: GUS and NBP

1.2. BANKING SECTOR RESULTS

According to the Polish Financial Supervision Authority data, in 2013 the net financial result of the Polish banking sector decreased by 0.3% y/y and reached the level of PLN 15.43 billion (compared to PLN 15.47 billion in 2012). The annual slight decrease in the net profit of the banking sector was affected by a significant decrease in result on banking activity (by 5.6% y/y). However, the decrease in net profit would be deeper if not for the strong decrease in negative balance of write-downs and other provisions (15.2%), accompanied by a significant improvement in other operating result. The annual change in the net profit of the banking sector was also affected, but relatively less, by reduction of total costs (by 0.6% y/y), with the decrease mainly relating to general and administrative expenses.

The above-mentioned deterioration of the results on banking activity in 2013 was caused by: decline in net interest income (by 3.8% y/y) and decrease in so-called other positions in result on banking activity (by 17.9% y/y). The decrease in net interest income was mainly caused by the cycle of monetary policy easing ended by MPC in July 2013, and also by poor lending activities in the corporate sector and - in the first half of 2013 – in the housing loans for individuals segment. The decrease in other positions in result on banking activity was mainly due to decline in profits earned by the banks on treasury bonds transactions. The negative contribution to the annual change of the results on banking activities was made by decrease in net dividend income (by 17.8% y/y) and deterioration in net fee and commission income (by 2.3% y/y).

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

PLN million	**2013**	**2012**	**Change**	
			PLN thousand	**%**
Net interest income	34 141	35 484	(1 343)	(3.8%)
Net fee and commission income	14 002	14 337	(334)	(2.3%)
Dividend income	759	923	(164)	(17.8%)
Other elements of the net income from banking activity	6 594	8 030	(1 436)	(17.9%)
Result on banking activity (total)	**55 496**	**58 773**	**(3 277)**	**(5.6%)**
Other operating result	922	(275)	1 197	(435.4%)
Employment expenses	(15 341)	(15 368)	26	(0.2%)
Overhead costs	(12 217)	(12 418)	201	(1.6%)
Depreciation and amortization	(2 646)	(2 590)	(55)	2.1%
Expenses (total)	**(30 204)**	**(30 376)**	**171**	**(0.6%)**
Net impairment losses on assets and other provisions	(7 563)	(8 923)	1 360	(15.2%)
Extraordinary operations	402	2	400	17 197%
Profit (loss) before income tax	**19 053**	**19 202**	**(149)**	**(0.8%)**
Income tax expense	(3 627)	(3 735)	108	(2.9%)
Net profit (loss) for the period	**15 426**	**15 467**	**(41)**	**(0.3%)**

Source: PFSA.

The own funds of the domestic banking sector (included in the calculation of the capital adequacy ratio) increased at the end of December 2013 by 8.0% y/y to PLN 139.4 billion compared to the end of 2012. The general capital requirement – with the limited lending activity in some market segments – increased only by 1.1% to PLN 70.8 billion compared to the end of 2012. As a result, the sector's capital adequacy ratio increased by 1.0 pp. reaching 15.8% as compared to the end of 2012.

In 2013 lending activity of the banking sector, measured with the rate of growth in deposit and credit volumes for non-banking clients, remained at a low level. Total loans increased by 3.6% y/y, while in 2012 they increased by 1.7% y/y, but then their nominal growth was limited by the appreciation of zloty against foreign currencies. The growth rate of deposits from non-financial customers remained moderate (up by 5.6% y/y, while in 2012 up by 5.9% y/y).

Debt under loans to private individuals increased at the end of 2013 by 3.8% y/y. In the first half of 2013 the growth of lending activity in this segment was even lower. It was a result of a downward trend in housing loans and continued weak situation of consumer credits. This slowdown was, among other things, caused by termination of government-subsidized program "Rodzina na swoim" and the strict PFSA Recommendations, especially in 1Q 2013, which formally limited availability of housing loans. The other factors restraining customers from incurring new debts were a tough situation on the labor market and an ongoing uncertainty about future financial situation of households.

In the second half of 2013 there was a gradual recovery in lending activity in the private sector, reflected especially in consumer credits. It resulted mainly from significant reductions of interest rates made by the MPC and the liberalization of Recommendation T by the PFSA (especially in terms of debt-to-income ratio and procedures concerning granting low-value cash and installment loans). This contributed to increase of formal and actual availability of housing loans in zloty and consumer credits. On the other hand it also stimulated the demand, especially as the situation on labor market began to stabilize and the service costs of previously taken loans decreased. These changes were accompanied by sustained bank pressure on the sale of cash loans, which reflected in high activity in advertising.

As a result, in September 2013, the annual growth rate of consumer loans for the first time since February 2011 reached the positive value (and remained so until the end of the year). However, this was caused by the one-off factor, i.e. purchase by one of the banks a consumer loans portfolio (PLN 2 billion) from semi-bank institution. On the other hand, the dynamics in this category was reduced by selling part of the “bad” loans portfolio by some banks, which according to PFSA in the first three quarters of 2013 was higher than in 2012 corresponding period.

The currency structure of newly granted housing loans, according to The Polish Bank Association (ZBP), in 2013 was dominated by the housing loans in PLN. The sale of currency housing loans was marginal and the dynamics of private debt concerning them remained negative. The growth rate observed during 2013 was caused by significantly lower appreciation of zloty against CHF in 2013 as compared to 2012. A slight decrease in debt dynamics of housing loans in PLN – with progressive recovery in this market segment – was the result of high base in the previous year.

Table 2. Loan volume of the banking sector

PLN million, as at the end of year	2013	2012	2011	Change	
				2013	2012
Loans for individual clients	**466.8**	**449.5**	**453.2**	**3.8%**	**(0.8%)**
- housing loans	334.2	319.8	317.2	4.5%	0.8%
- PLN loans	168.2	144.3	122.3	16.5%	18.0%
- currency loans	166.0	175.5	194.9	(5.4%)	(10.0%)
- consumer loans	132.6	129.7	135.9	2.3%	(4.6%)
Loans for corporate clients	**466.2**	**451.2**	**432.1**	**3.3%**	**4.4%**
- non-banking financial sector	39.9	32.1	24.8	24.1%	29.5%
- loans for business entities	348.0	339.4	330.5	2.5%	2.7%
corporate customers	259.0	257.0	253.5	0.8%	1.4%
individual entrepreneurs	57.4	53.5	50.7	7.3%	5.6%
individual farmers	26.2	24.1	22.2	8.8%	8.5%
non-profit institutions	5.3	4.8	4.2	9.5%	16.0%
- loans for government sector	78.4	79.6	76.8	(1. 6%)	3.7%
Loans for non-banking clients	**933.0**	**900.6**	**885.3**	**3.6%**	**1.7%**

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

In 2013 the growth of corporate lending activity remained at a low level. It was caused by poor situation of the domestic economy and by uncertainty about its prospects. Negative contribution to the annual change in the volume of corporate loans was made mainly by current loans and housing loans.

The savings of private sector remained the main source of banks’ deposits in 2013. However, their growth rate was noticeably slower than in 2012. The main growth factor, unlike in 2012, was significant increase in volume of current deposits, especially on savings accounts. In the analyzed period, a significant decrease of term deposits was recorded, being a result of lower interest rate on bank deposits, due to the cycle of decreasing of interest rates ended in July 2013 by MPC. These decreases were slowed in 4Q 2013, as a result of growing popularity of deposits with investment fund. Other significant factors that could influence lower dynamics of individuals’ deposits in 2013 were: relatively high unemployment rate and noticeable improvement of situation on Warsaw Stock Exchange. On the other hand, private deposits made by individuals were triggered by jobless fear and low propensity to consume, which resulted in higher propensity to save.

2013 brought stabilization and then gradual improvement on the corporate deposits market and increase of their role as a source of bank funding. The reduction of corporate capital expenditures, increase in revenues from exports and – in the second half of 2013 – increase in sales on domestic market reflected in growing dynamics of retail sales, resulted in rise of corporate deposit activity.

Table 3. Deposit volume of the banking sector

PLN billion, as at the end of 2013	2013	2012	2011	Change	
				2013	2012
Deposits from individual clients	**498.8**	**471.0**	**435.0**	**5.9%**	**8.3%**
- current	242.9	205.6	204.4	18.2%	0.6%
- term	255.9	265.4	230.6	(3. 6%)	15.1%
Deposits from corporate clients	**376.0**	**357.5**	**347.2**	**5.2%**	**3.0%**
- non-banking financial institutions	56.4	56.2	43.1	0.2%	30.4%
- deposits of business entities	263.0	239.6	253.0	9.8%	(5.3%)
corporate customers	208.0	189.8	205.1	9.6%	(7.5%)
individual entrepreneurs	28.3	25.4	24.8	11.3%	2.4%
individual farmers	9.4	7.8	7.9	20.5%	(2.0%)
non-profit institutions	17.4	16.6	15.1	4.6%	9.8%
- deposits from budget sector	56.6	61.7	51.0	(8.2%)	20.8%
Deposits from non-banking clients	**874.8**	**828.5**	**782.2**	**5.6%**	**5.9%**

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

1.3. STOCK EXCHANGE TRENDS AND INVESTMENT TRENDS

A significant difference between stock quotations of the largest companies, and small and medium enterprises (SME) was recorded in 2013 on Warsaw Stock Exchange. On one hand, the WIG20, the index of the largest companies, decreased during the 2013 by 7.0% (partially due to the effect of subtracting dividends, but even without taking into account their payment the WIG20 would ended the year in minus), while on the other hand SME (represented by sWIG80 and mWIG40 indices) increased (mWIG40 by 31.0%, sWIG80 by 37.3%). In the second half of the year all of the indices noted positive result and in this period a greater part of such impressive growth of mWIG40 and sWIG80 took place. The entire market, reflected by WIG index, ended 2013 with a profit of 8.1 %.

General improvement in economic situation in Poland influenced performance on the WSE in whole 2013, which reflected in an increase of expectations of the enterprises' financial results. On the other hand, information about changes in open-end pension funds (OFE) and termination of quantitative easing by FED in the USA had negative impact on the performance on WSE.

On the market of Polish treasury bonds, 2013 was concluded with the termination of the rally on market that dominated the entire 2012. At the turn of April and May, the returns on Polish 10-year bonds were close to the level of the 3%, however, the rest of the year brought a strong rebound and increases in yields to above 4,2%.

Table 4. Value of main Stock Exchange indices

Index	31.12.2013	31.12.2012	31.12.2011	Change in 2013	Change in 2012
WIG	51 284	47 461	37 595	8.1%	26.2%
WIG20	2 401	2 583	2 144	(7. 0%)	20.5%
mWIG40	3 345	2 553	2 174	31.0%	17.4%
sWIG80	14 337	10 444	8 497	37.3%	22.9%

Source: WSE.

In 2013, 23 new companies joined the WSE, including 7 whose quotations were transferred from NewConnect. The number of WSE-listed companies increased from 438 at the end of December 2012 to 450 at the end of December 2013. The regulated NewConnect market had 42 new issuers in 2013 (compared to 89 IPOs in 2012).

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

	31.12.2013	31.12.2012	31.12.2011	Change in 2013	Change in 2012
Number of companies	450	438	426	2.7%	2.8%
The capitalization of domestic companies (PLN million)	593 464	523 390	446 151	13.4%	17.3%
The value of trading in shares (PLN million)	256 147	202 880	268 139	26.3%	(24.3%)
Futures trading volume (in PLN thousands)	11 807	10 592	14 609	11.5%	(27.5%)

Source: WSE.

At the end of 2013, the Catalyst Bond market quoted a total of 442 bond issues with the value of issues exceeding PLN 619 billion.

2. IMPORTANT EVENTS IN BGŻ S.A. IN 2013

24.02.2013	The Management Board was notified that Mr Jacek Bartkiewicz had handed in his resignation from serving as the President of the Management Board of Bank Gospodarki Żywnościowej S.A. effective 31 March 2013.
1.03.2013	The Management Board was notified that Ms Monika Nachyła had handed in her resignation from serving as the Member of the Management Board effective 1 April 2013. At the same time, the Supervisory Board appointed Ms. Monika Nachyła as Vice-President of the Management Board effective 1 April 2013 and entrusted the duties of the President of the Management Board. The resolution comes into force on the date of approval by the Polish Financial Supervisory Authority.
28.05.2013	The conclusion of the subordinated loan agreement in the amount of CHF 90 000 000 between the Bank BGZ and Coöperatieve Centrale Raiffeisen-Boerenleenbank BA
28.06.2013	The Supervisory Board overruled resolution from 1 March 2013 on appointing Ms Monika Nachyła as the President of the Management Board. Ms Monika Nachyła remained the Vice-President of the Management Board.
24.07.2013	The Supervisory Board changed the resolution on appointment to the Board of BGŻ S.A. and repealed entrusting Ms Monika Nachyła, Vice President of the Bank, the duties of the President. Simultaneously, the Supervisory Board has entrusted the duties of the President to Mr. Geert Embrechts, First Vice President of the Management Board, and during his temporary absence to Mr. Witold Okarma, Vice-President of the Management Board.
2.09.2013	The Bank received approval from the Financial Supervisory Commission of 28 August 2013 on inclusion of cash in the amount of CHF 90 000 000 (from the subordinated loan) to the supplementary funds of the Bank BGŻ.
5.09.2013	The Supervisory Board appointed Mr. Józef Wancer to the position of Vice President of BGŻ S.A. and entrusted him with the duties of President of the Board of BGŻ S.A. from 16 September 2013, subject to KNF approval.
31.10.2013	The Management Board of BGŻ and Rabobank Poland have agreed and signed plan of merger of BGŻ Bank and Rabobank Poland.
26.11.2013	The Polish Financial Supervision Authority unanimously approved the appointment of Mr. Józef Wancer to the position of President of the Board of Bank BGŻ.
5.12.2013	Rabobank International Holding B.V. and Coöperatieve Centrale Raffeisen reached an agreement with BNP Paribas Group on the sale of 98.5% of the shares held by the Bank Rabobank in BGŻ. The transaction is subject to the signing of binding agreements and to obtaining the necessary regulatory approvals.
20.12.2013	The Polish Financial Supervision Authority has authorized under Art. 124 para. 1 of the Banking Law, the merger of Bank BGŻ with Rabobank Poland S.A.

3. AUTHORITIES OF THE BANK

3.1. CHANGES IN THE COMPOSITION OF THE SUPERVISORY BOARD

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

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

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

The composition of the Supervisory Board from 28 June to 31 December 2013 was as follows:

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

3.2. CHANGES IN THE COMPOSITION OF THE MANAGEMENT BOARD

The composition of the Bank's Management Board in the period between 1 January and 31 December 2013 was as follows:

- Józef Wancer – President of the Management Board (appointed on 16 September 2013 on position of Vice-President, from 26 November- President of the Management Board),
- Jacek Bartkiewicz – President of the Management Board (resignation on 31 March 2013),
- Monika Nachyła – Vice-President of the Management Board (appointed from 1 April 2013 to 24 July 2013 on position of Vice-President - acting President of the Management Board, from 24 July 2013 on position of Vice President of the Management Board),
- Gerardus Cornelis Embrechts – The first Vice-President of the Management Board (between 24 July 2013 and 16 September 2013 on the position of the acting President of the Management Board),
- Magdalena Legęć – Vice-President of the Management Board,
- Johannes Gerardus Beuming – Vice-President of the Management Board,
- Dariusz Odzioba – Vice-President of the Management Board,
- Witold Okarma – Vice-President of the Management Board,
- Wojciech Sass – Vice-President of the Management Board,
- Andrzej Sieradz – Vice-President of the Management Board.

4. EXTERNAL RATING OF THE BANK

4.1. RATINGS

The Bank was rated by the Moody's Investors Service rating agency. On 19 December 2013, Moody's Investors Service ("Moody's", "the Agency") decreased rating for the long-term and short-term deposits of the Bank respectively to Baa3 from Baa2 and to Prime-3 from Prime-2. The outlook for the ratings remains stable.

In support of its assessment, Moody's notes that the reduction of long-term and short-term rating of the Bank's deposits is the result announced on 5 December 2013 of the agreement between Rabobank Group and BNP Paribas in regard of the sale of shares of BGŻ.

Simultaneously the Bank's Financial Strength Rating („BFSR") remained at the level „D" with a stable outlook.

4.2. AWARDS AND DISTINCTIONS

In 2013, the Bank received the following awards and honors:

- In October, the Bank BGŻ was classified in 4th place the TOP brand 2013 ranking prepared by the magazine "Press" and the company Press- Service Monitoring Media. The ranking presents the strongest sector brands in regard of media presence.
- In September, the Bank was on 6th place in the "Newsweek Friendly Bank", in the category "Bank for Kowalski". The Bank moved up in the ranking for the second year in a row - this time by three places and joined the Quality Leaders in Poland. Ranking assesses the quality of activities for customer acquisition and retention, quality of service and features of bank branches .
- In May, the Bank for the third time in a row won in the 9th edition of the Laur Klienta i Konsumenta in category: loans to Small and Medium Enterprises. BGZ got 279 out of 1 003 votes (28%) collected in this category. Respondents were asked to indicate a brand, which they consider to be the best and would recommend it to others.
- In April, the Bank was in the first place in the "Most socially responsible companies" ranking in "banking, finance and insurance". Overall, the Bank was on 11th place, moving up from 24th in 2013. It was already 7th edition of the ranking carried out by "Dziennik Gazeta Prawna" under the auspices of the Responsible Business Forum.
- In January, the Bank was in the 5th place in the "Best Banks in Poland" prepared by research firm Expandi on behalf of the Wirtualna Polska. The report was based on the opinions of the Internet users in the last 12 months on the products and services offered by the biggest banks in Poland.
- In January account "Konto z Premią" of the Bank BGŻ won the third time in the ranking of all types of personal accounts prepared by the portal Money.pl.
- In January, in XIV edition of the "Entrepreneur-Friendly Bank" Bank BGŻ received Honorable Distinction along with Promotional Emblem with six Golden Stars. The title was given for active work for small and medium businesses, the widespread availability of the offer and the high quality of customer service from the SME segment.

5. SHAREHOLDERS' STRUCTURE OF THE BANK

In 2013 there were no any significant changes in the Bank's shareholding.

Table 6. Shareholders' structure of the Bank

Shareholder	31.12.2013		31.12.2012	
	Number of shares	Share (%)	Number of shares	Share (%)
Rabobank International Holding B.V.	45 942 004	89.84	45 941 751	89.84
Coöperatieve Centrale Raiffeisen-Boerenleenbank B.A.	4 303 695	8.42	4 303 695	8.42
Other shareholders	891 065	1.74	891 318	1.74
TOTAL	**51 136 764**	**100.00**	**51 136 764**	**100.00**

6. FINANCIAL POSITION OF THE BANK

6.1. STATEMENT OF PROFIT OR LOSS

In 2013, the Bank has generated net profit of PLN 162 403 thousand i.e. more by PLN 28 060 thousand than in 2012 (20.9%). The main causes for the increase were: limitation of general administrative costs, decrease of net impairment losses on financial assets, higher other operating income and lower other operating expenses

Table 7. Statement of profit or loss

PLN thousand	31.12.2013	31.12.2012	Change	
			PLN thousand	%
Net interest income	1 017 491	1 019 805	(2 314)	(0.2%)
Net fee and commission income	276 492	297 739	(21 247)	(7.1%)
Dividend income	2 848	3 416	(568)	(16.6%)
Net trading income	80 424	98 567	(18 143)	(18.4%)
Result on investing activities	31 902	43 329	(11 427)	(26.4%)
Result on hedge accounting	(1 077)	1 233	(2 310)	(187.3%)
Other operating income	49 613	37 017	12 596	34.0%
Net impairment losses on financial assets and contingent liabilities	(252 246)	(269 662)	17 416	(6.5%)
General administrative expenses	(880 647)	(927 981)	47 334	(5.1%)
Depreciation and amortization	(99 217)	(94 518)	(4 699)	5.0%
Other operating expenses	(21 146)	(30 478)	9 332	(30.6%)
Operating result	**204 437**	**178 467**	**25 970**	**14.6%**
Profit (loss) before income tax	**204 437**	**178 467**	**25 970**	**14.6%**
Income tax expense	(42 034)	(44 124)	2 090	(4.7%)
Net profit (loss) for the period	**162 403**	**134 343**	**28 060**	**20.9%**

Net interest income

In 2013, net interest income decreased by PLN 2 314 thousand, i.e. 0.2%. The relative stability of the annual net interest income was achieved by reducing interest expense by PLN 239 532 thousand, i.e. 21.1% y/y, almost fully compensating decrease in interest income, which amounted to PLN 241 846 thousand, i.e. 11.2% y/y. The dynamics of income and expenses in 2013 was influenced by external factors, and the rate of growth of loans and deposits.

Among the external factors, the most important were the NBP interest rate cuts. In the period from November 2012 to July 2013 there were eight reductions, a total of 2.25 percentage point.

Another important external factor was the entry into force on 24 October 2012, the regulation on payment services in the part concerning information obligations imposed on the service provider in relation to the customer. This regulation imposed a duty to inform customers about changes in the framework agreements - including those related to changes in interest rates - two months in advance. This extended the time for banks to adjust interest rates, particularly savings accounts to the NBP interest rate cuts.

The above-mentioned factors - especially in the first half of 2013 - had put pressure on interest margins realized on deposit products. Positive for net interest income impact of deposit's price adjustments to the low level of interest rates has highlighted fully in the second half of 2013,

The size of the loan portfolio remained stable during 2013, what was the result of the prevailing economic conditions and the credit policy of the Bank.

Table 8. Net interest income

PLN thousand	**31.12.2013**	**31.12.2012**	**Change**	
			PLN thousand	**%**
Loans and advances to banks	32 290	42 890	(10 600)	(24.7%)
Loans and advances to customers in current accounts	275 191	326 276	(51 085)	(15.7%)
Loans and advances to customers	1 236 580	1 482 437	(245 857)	(16.6%)
Hedging instruments	24 424	(1 154)	25 578	(2 216.5%)
Debt securities	344 585	304 467	40 118	13.2%
Interest income	**1 913 070**	**2 154 916**	**(241 846)**	**(11.2%)**
Amounts due to banks	(78 055)	(74 819)	(3 236)	4.3%
Debt securities issued	(79 598)	(107 548)	27 950	(26.0%)
Amounts due to customers	(737 926)	(952 744)	214 818	(22.5%)
Interest expense	**(895 579)**	**(1 135 111)**	**239 532**	**(21.1%)**
Net interest income	**1 017 491**	**1 019 805**	**(2 314)**	**(0.2%)**

Analyzing the components of interest income, its highest position, i.e. interest income on loans and advances decreased by PLN 245 857 thousand (16.6% y/y), what was the result of decrease of interest rates, combined with the fact that the vast majority of the portfolio has variable interest rate. In case of part of preferential loans portfolio the impact of the NBP interest rates fall on decrease in interest income was additionally increased by the multiplier effect (the interest rate is determined as the product of NBP rediscount rate and a multiplier of 1.5 or 1.6). This effect was limited by the use from the second quarter of 2012, hedge accounting, which covered about PLN 3 billion of preferential loans.

At the same time there was an increase in income from debt securities by PLN 40 118 thousand, i.e. 13.2%, where increased, compared to 2012, Bank's liquidity surplus was located - especially in the first half of 2013.

The decrease in interest expenses was mainly affected by the expense on amounts due to customers, which decreased by PLN 214 818 thousand, i.e. 22.5% y/y, mainly due to reductions in interest rates on deposit products in the wake of the reductions in NBP interest rates. However, the reduction in interest expenses was hindered by the above-mentioned statutory two-month delay in the implementation of price changes for certain products.

Net fee and commission income

Net fee and commission income in 2013 was lower by PLN 21 247 thousand, i.e. 7.1% y/y, compared with 2012, due to decrease in income from fees and commissions by PLN 12 402 thousand, i.e. 3.6% y/y and an increase in commission expenses by PLN 8 845 thousand, i.e. 18.3%.

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

- loans and advances – as a result of slowdown of loans on current account and loan commitment growths. In case of loan commitments, an additional factor, which limited income in the statement of profit or loss, was commencement of settling them over time (further description of those changes can be found in Financial Statements of Bank Gospodarki Żywnościowej S.A. as at 31 December 2013 in the note "Changes in accounting policies and changes in presentation of financial data").
- clearing operations - as a result of a slower rate of turnover of transaction in the economy,
- sale of insurance products - as a result of the introduction of settlement in time of net commissions for the sale of insurance products related to the creation of financial assets or liabilities (mainly regarding cash loans insurance). Starting from the 1 January 2013, these fees have become an integral part of the effective interest rate method and are recognized in the statement of profit or loss as interest income.

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

Despite reduced interchange rates, fee and commission income on payment cards increased by PLN 8 135 thousand, i.e. 11.0%, mainly due to higher income from cards organizations for increased number of underlying transactions.

Better stock exchange and the investment fund market situation, as well as the renegotiation of distribution agreements with selected TFI enabled the Bank to increase income from commissions from brokerage operations PLN 3 734 thousand, i.e. 33.7%.

Table 9. Net fee and commission income

PLN thousand	31.12.2013	31.12.2012	Change	
			PLN thousand	%
Fee and commission income				
– loans and advances	95 877	109 934	(14 057)	(12.8%)
– settlements	17 563	20 106	(2 543)	(12.6%)
– account maintenance	91 803	92 550	(747)	(0.8%)
– guarantee commitments	10 557	11 462	(905)	(7.9%)
– brokerage operations	14 810	11 076	3 734	33.7%
– payment cards	82 107	73 972	8 135	11.0%
– insurance activity	15 101	18 437	(3 336)	(18.1%)
– other	5 894	8 577	(2 683)	(31.3%)
Fee and commission income	**333 712**	**346 114**	**(12 402)**	**(3.6%)**
Fee and commission expense				
– loans and advances	(735)	(788)	53	(6.7%)
– payment cards	(33 300)	(24 303)	(8 997)	37.0%
– insurance activity	(13 598)	(13 798)	200	(1.4%)
– other	(9 587)	(9 486)	(101)	1.1%
Fee and commission expense	**(57 220)**	**(48 375)**	**(8 845)**	**18.3%**
Net fee and commission income	**276 492**	**297 739**	**(21 247)**	**(7.1%)**

The increase in costs from fees and commissions was mainly caused by the higher cost of payment cards (by PLN 8 997 thousand, i.e. 37.0% y/y), paid to operators of card due to a larger number of transactions executed by the Bank's customers.

Dividend income

Dividend income in 2013 decreased by PLN 568 thousand, i.e. 16.6%. This was affected by dividends from the Bank's minority interests in the National Bank Clearing House S.A. (KIR), Credit Information Bureau S.A. (BIK) and the Warsaw Stock Exchange (WSE) derived from the profits of these companies for 2012, approved by the General Assemblies. For all of these companies dividend was lower than in previous year.

Net trading income and results from investment activities

Net trading income in 2013 was by PLN 18 143, i.e. 18.4% y/y, lower than in 2012. The level and volatility of this result is shaped mainly by the valuation of the Bank's position in the instruments of interest rate swaps (IRS) as a hedge against interest rate risk, and trading activity on debt securities whose profitability is dependent on the accuracy of predicted changes in the market.

Result on investment activity fell by PLN 11 427 thousand, i.e. 26.4%, compared with 2012, mainly due to impairment loss provision established on shares of associated entity BGŻ Leasing sp. z o.o. in the amount of PLN 7 321 thousand – due to net loss incurred by this entity in 2013. The main component of the result of investment activity remained realized gains on portfolio of securities available for sale. Decisions to sell these securities prior to the maturity date shall be made, taking into account the needs arising from interest rate risk management and the use of favorable market conditions which in 2013 were shaped by the decline in the profitability of debt securities in the wake of decrease in NBP interest rates.

Other operating income

Other operating income in 2013 increased by PLN 12 596 thousand, i.e. 34% compared with the previous year, mainly due to the increase in other operating income from recovery of overdue, amortized and uncollectable debts, and repayment of debts excluded from statement of financial position, which recognized significant income from the repayment of debts writ en off from the balance sheet of a corporate client from agro food sector.

In addition, in the fourth quarter of 2013, the Bank made a partial (PLN 7 788 thousand) release of provisions for fine imposed in 2006 on the Bank by the President of the Office of Competition and Consumer Protection on charges of payment cards – because of the court's decision of reducing the penalty.

Table 10. Other operating income

PLN thousand	31.12.2013	31.12.2012	Change	
			PLN thousand	%
Sales of goods and services	9 076	9 804	(728)	(7.4%)
Release of provisions for litigation and claims as well as other liabilities	9 251	5 965	3 286	55.1%
Recovery of debt collection costs	2 114	2 487	(373)	(15.0%)
Recovery of overdue, amortized and uncollectable debts, and repayment of debts excluded from statement of financial position	17 531	6 778	10 753	158.6%
Other operating income	11 641	11 983	(342)	(2.9%)
Total other operating income	**49 613**	**37 017**	**12 596**	**34.0%**

Net impairment losses on financial assets and contingent liabilities

The result of impairment losses on financial assets and provisions for contingent liabilities for 2013 was improved by PLN 17 416 thousand, i.e. 6.5% compared to 2012. This was mainly affected by lower write-offs on loans to large corporates. Their decline has been shaped mainly by write-offs on exposures to individual companies in the construction sector engaged in construction of highways, which in 2012 was influenced by the bankruptcy of one of these companies, and in 2013, by troubles of another. On the other hand, net write-offs on loans to small and medium-sized enterprises, which are affected by the economic downturn, have increased.

In the retail segment, write-downs on mortgages and loans have decreased. On the other hand cash loans has slightly increased, what was mainly result of the increase in this portfolio.

Changes in methodology and calculation of parameters of write-downs in 2012.

In December 2012, there was a change in the methodology of calculating impairment losses through collective method, as described in the consolidated annual financial statements. The change led to reversal of impairment in the amount of PLN 33 million at its implementation date and further reduction of net impairment losses in the beginning of 2013.

In November 2013, the Bank made methodology review and in consequence another modification of the model parameters of calculating write-offs took place. The purpose was to reduce the historical observation period for the calculation of the parameter PD (probability of default) for corporate customers subject to the provisions of the Accounting Act, for the period of 5.5 years to 2 years, to modify the parameters of the CCF (Credit Conversion Factor) for off-balance sheet exposures and to extend the LIP (loss Identification Period) from 6 months to 9 months for selected portfolios defined under the impairment of financial assets. The combined effect of these changes was additional PLN 22.6 million write-offs.

General administrative expenses, staff costs and depreciation/amortization

General administrative expenses and depreciation/amortization in 2013 decreased by PLN 47 334 thousand, i.e. 5.1%, compared to 2012, which was primarily due to decrease in employee, marketing, external services, other non-personnel and IT costs.

Table 11. General administrative expenses, staff costs and depreciation/amortization

PLN thousand	31.12.2013	31.13.2012	Change	
			PLN thousand	%
Personnel expenses, in this:	(475 129)	(501 418)	26 289	(5,2%)
Wages and salaries	(379 323)	(398 227)	18 904	(4.7%)
Payroll taxes	(56 482)	(57 997)	1 515	(2.6%)
Employee benefits	(5 446)	(8 659)	3 213	(37.1%)
Provision for restructuring	(7 746)	(16 901)	9 155	(54.2%)
Provision for future liabilities for unused vacation and retirement benefits	(8 271)	(1 557)	(6 714)	431.2%
Contributions to the Social Fund	(6 072)	(6 232)	160	(2.6%)
Other	(11 789)	(11 845)	56	(0.5%)
Marketing	(61 225)	(70 162)	8 937	(12.7%)
IT	(76 067)	(79 941)	3 874	(4.8%)
Rental Expenses	(94 056)	(92 677)	(1 379)	1.5%
Other non-personnel expenses	(47 770)	(52 768)	4 998	(9.5%)
External services	(92 864)	(101 032)	8 168	(8.1%)
Bank Guarantee Fund fee	(29 432)	(24 550)	(4 882)	19.9%
Polish Financial Supervision Authority fee	(4 104)	(5 433)	1 329	(24.5%)
Total general administrative expenses	**(880 647)**	**(927 981)**	**47 334**	**(5.1%)**
Property, Plant and Equipment	(51 715)	(51 299)	(416)	0.8%
Intangible assets	(47 502)	(43 219)	(4 283)	9.9%
Depreciation and amortization	**(99 217)**	**(94 518)**	**(4 699)**	**5.0%**
Total (1)	**(979 864)**	**(1 022 499)**	**42 635**	**(4.2%)**

(1) for measurement of ratio expense/ income

The decrease in personnel expenses by PLN 26 289 thousand, i.e., 5.2%, was mainly due to:

- decrease in wages and salaries by PLN 18 904 thousand as a result of: (i) employment restructuring carried out from October 2012, (ii) lower than in 2012, the payment of bonuses and rewards in accordance with the principles of the incentive system in force in the Bank, (iii) higher income from the reversal of provisions for bonuses for previous years

- lower by PLN 9 155 thousand, write-offs for employment restructuring, most of which were incurred in 2012

The decrease in marketing expenses by PLN 8 937 thousand, i.e. 12.7%, was due to limits on expenses on marketing of deposit products in situations of low demand for additional financing due to slower growth in lending.

Restructuring costs also included non-personnel costs, where optimization was made of the use of chosen resources and the renegotiation of a number of agreements with external suppliers, which contributed to savings in the cost of external services (decrease of PLN 8 168 thousand y/y) and information costs (a decrease of PLN 3 874 thousand).

Other material costs decreased by PLN 4 998 thousand, i.e. 9.5%, by reducing the cost of processing and transport of cash, mass printing and queries to databases of credit information.

The increase in fees for the Bank Guarantee Fund of PLN 4 882 thousand comprised:

- increase in capital requirements for individual types of risks, which are the basis for calculating the annual fees (the premium for the next year determined as a percentage of capital requirements at the end of the previous year):
- New prudential charge was introduced from November 2013 – in 2013 the Bank in total made an allowance for the payment of PLN 2 437 thousand

Depreciation for 2013 increased by PLN 4 699 thousand, i.e. 5.0%, compared with 2012. The increase in amortization of intangible assets was the result of investment in information systems, including the system of customer relationship management (CRM). The increase in depreciation of property, plant and equipment resulted from the opening of the last wave of (11) new branches in the second half of 2012 and the first quarter of 2013,

Other operating expenses

Other operating expenses for 2013 were lower by PLN 9 332 thousand, i.e. 30.6% compared to 2012, what was related to the fact that in 2012, in other operating expenses due to write-downs of other receivables the Bank demonstrated PLN 5 909 thousand provisions for operating losses in two branches. In addition, during this period, the Bank incurred significantly lower costs than a year earlier due to creation of provisions for litigation.

Table 12. Other operating expenses

PLN thousand	**31.12.2013**	**31.12.2012**	**Change**	
			PLN thousand	**%**
Sale or liquidation of property, plant and equipment, intangible assets	(2 083)	(1 444)	(639)	44.3%
Impairment charges on other receivables	(2 551)	(7 007)	4 456	(63.6%)
Provisions for litigation and claims, and other liabilities	(2 658)	(8 438)	5 780	(68.5%)
Debt collection	(7 556)	(7 693)	137	(1.8%)
Donations made	(3 200)	(3 185)	(15)	0.5%
Other	(3 098)	(2 711)	(387)	14.3%
Total other operating expenses	**(21 146)**	**(30 478)**	**9 332**	**(30.6%)**

6.2. STATEMENT OF COMPREHENSIVE INCOME

Total comprehensive income of the Bank in 2013 was by PLN 300 534 thousand lower than a year earlier. This was mainly due to negative effects of revaluation of financial assets available for sale (i.e. portfolio of long-term Treasury bonds), while in 2012 demonstrated positive effects on the valuation of these securities. Negative valuation in 2013 was the result of changes in market expectations regarding the development of the long-term interest rates (increase in rates for longer maturities).

In 2013, there have also been demonstrated positive effects of valuation of derivatives instruments hedging future cash flows that occurred in connection with the start of application of hedge accounting from the second quarter of 2012. In particular, the Bank entered into IRS float-to-fix transaction for the period until April 2014, in order to hedge interest rate risk regarding future interest cash-flows from preferential loans granted with interest rates based on NBP's rediscount rate (with multiplier of 1.5 and 1.6).

Table 13. Comprehensive income statement

PLN thousand	**2013**	**2012**	**Change**	
			PLN thousand	**%**
Net profit (loss) for the period	**162 403**	**134 343**	**28 060**	**20.9%**
Other comprehensive income				
Items that will be subsequently reclassified to profit or loss under certain conditions				
Net change in valuation of financial assets available for sale	(139 491)	230 867	(370 358)	(160.4%)
Net change in valuation of cash flow hedges	(13 457)	21 857	(35 314)	(161.6%)
Income tax expense on other comprehensive income	29 060	(48 018)	77 078	(160.5%)
Other comprehensive income (net of tax)	**(123 888)**	**204 706**	**(328 594)**	**(160.5%)**
Total comprehensive income for the period	**38 515**	**339 049**	**(300 534)**	**(88.6%)**

6.3. STATEMENT OF FINANCIAL POSITION

Assets

As at the end of 2013 total assets value of the Bank was PLN 35 763 492 thousand and was by PLN 1 467 201 thousand i.e. 3.9% lower than in 2012.

Table 14. Assets

PLN thousand	**31.12.2013**	**31.12.2012**	**Change**	
			PLN thousand	**%**
Cash and balances with the Central Bank	1 617 713	2 106 657	(488 944)	(23.2%)
Loans and advances to banks	269 757	104 035	165 722	159.3%
Reverse repo transactions	309 255	104 369	204 886	196.3%
Debt securities held for trading	1 018 701	219 051	799 650	365.1%
Derivative financial instruments	363 260	380 473	(17 213)	(4.5%)
Hedging instruments	57 387	69 179	(11 792)	(17.0%)
Loans and advances to customers	26 330 360	26 357 522	(27 162)	(0.1%)
Available for sale financial assets	4 826 073	6 867 557	(2 041 484)	(29.7%)
Investments in associates	51 645	58 720	(7 075)	(12.0%)
Intangible assets	158 589	152 674	5 915	3.9%
Property, plant and equipment	449 139	469 098	(19 959)	(4.3%)
Deferred tax assets	142 792	130 818	11 974	9.2%
Current tax assets	12 519	10 318	2 201	21.3%
Other assets	156 302	200 222	(43 920)	(21.9%)
OTHER ASSETS	**35 763 492**	**37 230 693**	**(1 467 201)**	**(3.9%)**

The main factor of the decrease in assets in 2013 was reduction of excess liquidity stored in debt securities recognized as financial assets available for sale. These assets have been reduced by PLN 2 041 484 thousand, by what part of the released funds was moved into debt securities recorded as held for trading (an increase of PLN 799 650 thousand y/y).

Optimization of the liquidity structure of assets in 2013 was linked to the reduction of funding in the form of commitments to customers, banks and due to issued debt securities and have a positive impact on net interest income of the Bank. Surplus liquidity buffer was maintained at the break of 2012/2013, and in the first half of 2013, in anticipation of accelerating credit growth, which, however, did not materialize. Overall in 2013, loans and advances to customers decreased by PLN 27 162 thousand, i.e. 0.1%. This was due to low demand for loans for enterprises, caused by more conservative planning for investment spending in the situation of economic downturn and also by prudent Bank's policy for crediting sectors with higher risk.

The second significant factor of assets' decline was balance of cash on hand and with Central Bank (a decrease of PLN 488 944 thousand y/y). In the reporting period, the cash balance decreased by PLN 152 228 thousand, i.e. 17.6%, as a result of activities to optimize the maintenance of the Bank's cash in this form. The balance account in the Central Bank decreased by PLN 336 716 thousand. PLN, i.e. 27.1%, whereas they are naturally under huge volatility because they are created by the current needs of the Bank to settle the obligatory reserve requirements.

Liabilities and equity

By the end of 2013, the total value of the Bank's liabilities amounted to PLN 32 258 430 thousand and was lower by PLN 1 505 716 thousand, i.e. 4.5% than at the end of 2012. The main factor of the decrease was liabilities to other banks, customers and due to the issuance of debt securities.

Table 15. Total Liabilities and Equity

PLN thousand	**31.12.2013**	**31.12.2012**	**Change**	
			PLN thousand	**%**
Amounts due to other banks	3 271 414	4 094 436	(823 022)	(20.1%)
Repo transactions	-	32 341	(32 341)	(100.0%)
Financial liabilities held for trading	271 288	72 005	199 283	276.8%
Derivative financial instruments	336 950	326 215	10 735	3.3%
Hedging instruments	-	-	-	-
Amounts due to customers	26 492 774	26 942 029	(449 255)	(1.7%)
Debt securities issued	1 191 157	1 852 776	(661 619)	(35.7%)
Subordinated liabilities	304 817	-	304 817	-
Other liabilities	326 015	379 168	(53 153)	(14.0%)
Deferred tax liabilities	-	-	-	-
Provisions	64 015	65 176	(1 161)	(1.8%)
TOTAL LIABILITIES	**32 258 430**	**33 764 146**	**(1 505 716)**	**(4.5%)**
Share capital	51 137	51 137	-	-
Other supplementary capital	3 085 059	2 950 716	134 343	4.6%
Other reserve capital	206 463	330 351	(123 888)	(37.5%)
Retained earnings	162 403	134 343	28 060	20.9%
- net profit for the period	162 403	134 343	28 060	20.9%
TOTAL EQUITY	**3 505 062**	**3 466 547**	**38 515**	**1.1%**
TOTAL LIABILITIES AND EQUITY	**35 763 492**	**37 230 693**	**(1 467 201)**	**(3.9%)**

The decrease in liabilities due to banks by PLN 823 022 thousand, i.e. 20.1%, was mainly due to the early repayment of part of the loan in CHF from Rabobank (repaid CHF 90 million), while lending this amount to the Bank by Rabobank in the form of a subordinated loan. Its value at 31.12.2013 amounted to PLN 304 817 thousand. In the remainder part, the decrease in liabilities due to banks was caused by the repayment of tranches of the loan in CHF according to the schedule and funding limitations in the form of deposits accepted from the interbank market.

The amounts due to customers decreased by PLN 449 255 thousand, i.e. 1.7% mainly as result of lower funding obtained from non-banking financial institutions in form of high balance deposits.

Liabilities from debt securities issuance has been reduced by PLN 661 619 thousand, i.e. 35.7%, as a result of non-renewal of expiring portion of securities in a situation of reduced Bank's demand for funding.

By the end of 2013, the Bank's equity amounted to PLN 3 505 062 thousand and was by PLN 38 515 thousand lower than at the end of 2012. The change in equity during this period was the result of:

- decrease in other reserves of PLN 123 888 thousand, i.e. 37.5%, due to lower valuation of financial assets (mainly debt securities classified as available for sale);
- retention of the financial results from 2012 in the amount of PLN 134 284 thousand (charged to other supplementary capital);
- higher result for the current period (by PLN 28 060 thousand y/y).

6.4. LOAN PORTFOLIO QUALITY

As at 31.12.2013 the share of receivables that lost their value, in the portfolio of loans and advances granted to customers was 8.1% in comparison to 7.2% to the end of 2012.

Table 16. Credit portfolio quality ratios

PLN thousand	**31.12.2013**	**31.12.2012**	**Change**	
			PLN thousand	**%**
Loans and advances to customers (gross)	27 549 925	27 427 458	122 467	0.4%
Impairment allowances (negative value)	(1 219 565)	(1 069 936)	(149 629)	14.0%
Loans and advances to customers (net)	**26 330 360**	**26 357 522**	**(27 162)**	**(0.1%)**
Losses incurred but not reported (IBNR)				
Gross exposure	25 313 766	25 457 786	(144 020)	(0.6%)
Impairment allowances on receivables assessed collectively with no impairment identified	(100 217)	(77 081)	(23 136)	30.0%
Net exposure	**25 213 549**	**25 380 705**	**(167 156)**	**(0.7%)**
Impaired exposures				
Gross exposure	2 236 159	1 969 672	266 487	13.5%
Impairment allowances on receivables assessed collectively and individually	(1 119 348)	(992 855)	(126 493)	12.7%
Net exposure	**1 116 811**	**976 817**	**139 994**	**14.3%**
Ratios:				
Share of impaired exposures in loan portfolio, gross	**8.1%**	**7.2%**		**0.9%**
Impairment coverage	**(50.1%)**	**(50.4%)**		**0.4%**

Growth rate for the total portfolio was a consequence of the increase of receivable share that have lost value in the mortgage loan portfolio, respectively to 5.2% from 4.9%, and in the portfolio of loans to corporate customers excluding farmers, respectively, to 12.6% from 9.4%. In the latter case, this partially resulted from the increase in value of impaired loans due to the economic downturn, and in part from a decrease in the total value of these loans.

However, the quality of cash loans to retail customers has improved (decrease of respectively from 17.8% to 13.0%), what was caused by the dynamic growth of this portfolio and a number of sale transactions of overdue receivables.

The participation rate of impaired loans in the agriculture portfolio was low and during 2013 it further improved (from 3.6% to 3.5%). The agricultural sector showed good resistance to the economic downturn.

6.5. OWN FUNDS AND CAPITAL ADEQUACY RATIO

The capital adequacy ratio increased from 11.75% at the end of 2012 to 13.22% at the end of 2013.

Table 17. Own funds and Capital Adequacy Ratio

PLN thousand	31.12.2013	31.12.2012	Change	
			PLN thousand	%
Principal funds	**3 336 209**	**3 157 310**	**178 899**	**5.7%**
– share capital	51 137	51 137	-	-
– other supplementary capital	3 085 059	2 950 716	134 343	4.6%
– other reserves capital	25 000	25 000	-	-
– general risk fund	90 000	90 000	-	-
– net profit under authorization in the amount verified by the external auditors	85 013	40 457	44 556	110.1%
Deductions from the principal funds	**(196 550)**	**(174 408)**	**(22 142)**	**12.7%**
– intangible assets	(158 589)	(152 674)	(5 915)	3.9%
– unrealized losses on equity instruments classified as available for sale	-	(26)	26	(100.0%)
– unrealized losses on debt securities classified as available for sale	(20 435)	(121)	(20 314)	16 788.4%
–equity investments in financial institutions	(17 526)	(21 587)	4 061	(18.8%)
Principal funds after deductions	**3 139 659**	**2 982 902**	**156 757**	**5.3%**
Supplementary funds	**404 305**	**195 324**	**208 981**	**107.0%**
– unrealized gains on debt securities classified as available for sale	98 858	194 897	(96 039)	(49.3%)
– unrealized gains on equity instruments classified as available for sale	1 103	427	676	158.3%
– subordinated liabilities	304 344	-	304 344	-
Deductions from the supplementary funds	**(17 526)**	**(21 587)**	**4 061**	**(18.8%)**
– equity investments in financial institutions	(17 526)	(21 587)	4 061	(18.8%)
Short term funds	**14 774**	**14 674**	**100**	**0.7%**
Total Own funds	**3 541 212**	**3 171 313**	**369 899**	**11.7%**
Capital requirements				
– credit risk, counterparty risk, settlement-delivery risk	1 948 729	1 993 346	(44 617)	(2,2%)
– operating risk	187 322	161 386	25 936	16,1%
– general interest rate risk	7 604	4 896	2 708	55,3%
Total capital requirements	**2 143 655**	**2 159 628**	**(15 973)**	**(0,7%)**
Capital adequacy ratio (%)	**13.22%**	**11.75%**		**1.47%**

Own funds increased by PLN 369 899 thousand, which was the result of the following factors:

- inclusion to supplementary funds of subordinated liability in the amount of CHF 90 000 thousand. CHF (304 344 thousand. PLN as at 31/12/2013) to a strategic shareholder, with the consent of the Financial Supervision Authority issued in August 2013;
- retention of net profit for 2012 in the amount of PLN 134 343 thousand, which increased the capital reserve;
- higher by PLN 44 556 thousand profit in the course of approval, which is the net profit for the first half of the year after a review of interim financial statements by an auditor;

- increase in unrealized losses/decrease in unrealized profits on debt securities classified as available for sale and recognized respectively in basic /supplementary funds of the Bank – in total by PLN 115 651 thousand. The mechanism of this decrease has been described in the paragraph devoted to the total income of the Bank.

The decrease of the capital requirement for credit risk by PLN 44 617 thousand y/y corresponded to the inhibition of lending. The increase in the capital requirement for operational risk corresponded to the increase in the result being a basis for the calculation of this requirement in accordance with BIA method used by the Bank (the requirement is calculated as 15% of the average result for the previous three years).

6.6. FINANCIAL RATIOS

In 2013, the Bank recorded the stabilization of return on equity and return on assets ratios compared to 2012, which was a result from the increase in net profit with simultaneous increase in interim equity and assets' value.

Net interest margin decreased as a result of the reduction of NBP interest rates and delayed possibility of adjustment of prices of some deposit products according to provisions of the Act on Payment Services. The lowest level of margin was recorded in the first and second quarter of 2013, while in the second half of the year there has been a significant improvement under influence of the price adjustment and balance structure optimization.

The ratio of cost effectiveness (Costs/Revenues) slightly improved due to faster decrease in cost than income.

The decrease in credit risk costs ratio corresponded with lower amount of net impairment losses on loans and advances compared to 2012. However, its further improvement was stagnancy of credit portfolio size.

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

Table 18. Financial ratios

	31.12.2013	31.12.2012	Change
Return on Equity(1)	4.7%	4.5%	0.2%
Return on Assets(2)	0.4%	0.4%	0.0%
Net interest margin(3)	2.7%	2.9%	(0.2%)
Costs / Revenues(4)	68.2%	69.5%	(1.3%)
Credit Risk Costs(5)	(1.0%)	(1.1%)	0.1%
Loans / Deposits(6)	104.0%	101.8%	2.2%
Loans / Total sources of funding(7)	89.3%	84.8%	4.5%

(1) Relation of the net profit to average shareholders' capital based on the balances at the end of the quarters (annualized).

(2) Relation of the net profit to average assets based on the balances at the end of the quarters (annualized).

(3) Relation of the net interest income to average assets based on the balances at the end of the quarters (annualized).

(4) Relation of the total of general administrative expenses, and depreciation and amortization to the total result on banking activities and other operating income and costs.

(5) Relation of net impairment losses on loans and advances to the average balance of loans and advances to customers based on the balances at the end of the quarters (annualized).

(6) Relation of gross loans and advances to customers to amounts due to customers based on the balances at the end of the period.

(7) Relation of gross loans and advances to customers to the total amounts due to customers, debt securities issued and loans from other banks. Balances at the end of the period.

7. BANK OPERATIONS IN 2013

7.1. DISTRIBUTION CHANNELS

7.1.1. TRADITIONAL CHANNELS

Branches

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

In 2013, 3 subordinated branches were opened. Based on analysis of financial results and location potential, 6 branches were liquidated, 3 branches were relocated (1 subordinated and 2 operating) and 4 operating branches were transformed into subordinated branches. In addition, 1 external cash desk was liquidated.

As at 31 December 2013, the Bank had 397 branches of retail and business banking, of which 116 were operating branches and 281 subordinated branches (compared to 120 operating branches and 280 subordinated branches as at 31 December 2012). The network of branches was supplemented by 13 external cash desks, which service cash transactions.

Reorganization

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

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

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

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

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

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

ATM network

As at 31 December 2013, the network of ATMs available to the Bank's retail customers for commission-free cash withdrawals comprised, apart from ATMs located at Bank's branches, ATMs of the Euronet network and selected ATMs of Planet cash4you network (automatic teller machines labeled as „Automatic teller machine available to BGŻ customers for commission-free cash withdrawals").

At the end of 2013, retail customers of the Bank could make commission-free cash withdrawals at 4 718 ATMs, of which 419 were located at Bank's branches. Customers holding a Konto Plus personal account could make commission-free cash withdrawals in all ATMs in Poland. Owners of the Plan Aktywny and Konto bardzo osobiste personal accounts could use all automatic teller machines both in Poland and abroad for commission-free cash withdrawals. Institutional Clients holding Plan Agro Lider and Agro Lider Prestiż accounts could use all ATMs in Poland for commission-free cash withdrawals.

On 19 December 2013 the Bank signed an agreement selling ATMs located at Bank's branches to IT card company. After transferring ATMs to the buyer they will have both BGŻ and Planet cash4you logo.

7.1.2. ALTERNATIVE CHANNELS

Internet banking

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

Table 19. Data related to eBGŻ and eBGŻ Firma

		31.12.2013	31.12.2012	Change	
Number of clients with access	eBGŻ	416 514	350 228	66 286	18.9%
	eBGŻ Firma	83 606	70 079	13 527	19.3%
Number of clients actively logging in	eBGŻ	264 534	228 742	35 792	15.6%
	eBGŻ Firma	51 860	43 149	8 711	20.2%
Average number of transactions	eBGŻ	1 172 192	963 788	208 404	21.6%
	eBGŻ Firma	1 038 694	854 009	184 685	21.6%

eBGŻ

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

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

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

In August 2013, a new version of the eBGŻ service was launched for customers from the Personal Banking section. The Bank also launched a new deposit product (Lokata Bardzo Osobista) and contact details of personal customer advisor. Furthermore, presentation of currency exchange rates was added.

The possibility to fully operate Konto z Zyskiem personal account, including lunching the product to the Bank's offer, was introduced in eBGŻ service at the end of August 2013. In addition, the functionality of blocking accounts suspected of involvement in phishing was extended to verify specified string in the title of the transaction.

The functionality dedicated to the management of investment funds was extended to include additional two Investment Fund Managing Companies (TFI): AVIVA Investors and Skarbiec.

The functionality of charging the mobile phones and energy counters was introduced to the users of the eBGŻ service in October 2013.

eBGŻ Firma

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

In the second half of 2013, as part of the implementation of the electronic channels development project, access to the web integration platform was activate for business users. This service functions under the name Platforma Finansowa dla Firm (The Business Financial Platform) and is available at the Internet address https://www.pf.bgz.pl. It is a full-featured trading system, which enable users to manage the funds in their accounts at BGŻ. The supreme value of the new solution is to facilitate access to the Bank's products and services, as well as to support users in everyday business decisions. Via The Business Financial Platform users accessed on a single-sign-on basis (one login, one password, one token) the following internet banking systems: eBGŻ Firma, eBGŻ Treasury, eBGŻ Faktor, eBGŻ SWD, eBGŻ (for those business users who use the retail offer of BGŻ). The users of The Business Financial Platform accessed also economy service (eBGŻ Analizy), which provides up to date economic information from Poland and the world. Selected elements of the service are available exclusively for Bank's customers.

Phone-banking

In 2013, a further increase by 86 866 i.e. 17% in the number of Tele-banking retail and institutional users was recorded in comparison to the end of 2012.

Table 20. Data related to Tele-banking

		31.12.2013	31.12.2012	Change	
Number of customers with access to TeleBGŻ	Retail customers	452 702	388 910	63 792	16,4%
	Institutional customers	132 589	109 515	23 074	21,1%
An average number of incoming and outcoming calls per month		179 170	171 355	7 815	4.6%

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

Furthermore, consultants of the Communication Centre offered the assistance for eBGŻ users in the scope of: sales of cash credits, investment funds and replacing authorization tools to SMS codes.

For clients using the TeleBGŻ service the range of services available via phone-channel was expanded with:

- activation of access to eBGŻ and resignation of access to eBGŻ and TeleBGŻ,
- issuance / replacement of a card,
- change of cash and transaction card limits,
- activation of commission-free cash withdrawals in all ATMs,
- issuance of a certificate confirming bank accounts and account balances.

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

Banking cards

As far as issuance and supporting of cards is concerned, the Bank cooperates with MasterCard and Visa. The portfolio of payment cards includes debit cards, credit cards and cards with deferred payment. As at 31 December 2013, the number of debit card issued to clients was 623 thousand and was nearly 8.9 thousand, i.e. 1.4%, lower than in the previous year. In this period, increase concerned only credit cards to retail clients (an increase of 2.1 thousand, i.e. by 3.8%).

Table 21. Number of banking cards issued by BGŻ S.A.

Cards in thousand	31.12.2013	31.12.2012	Change	
Debit cards retail	504.7	512.6	(7.9)	(1.5%)
Credit cards retail	58.1	56.0	2.1	3.8%
Debit cards business	58.8	61.7	(2.9)	(4.7%)
Business cards with deferred payment	1.4	1.6	(0.2)	(12.5%)
Total number of cards issued	**623.0**	**631.9**	**(8.9)**	**(1.4%)**

The Bank’s activities regarding cards in 2013 concentrated on the implementation of new functionalities (including contactless payments) and on promoting of non-cash transactions made with payment cards. Customers using MasterCard credit cards were awarded the bonus constituting the part of the expenditure paid with the card, and customers of the Konto z Premią obtained the bonus constituting the 1% of the remuneration transferred to an account, provided they made non-cash expenses with card in amount determined by the regulations of the promotion. Visa prepared the special promotion for its customers. The holders of Visa cards were encouraged to pay with their cards for an everyday, even little shopping.

The Bank's policy on credit cards has resulted in their award in the ranking prepared by the financial portal Money.pl in March 2013. A card MasterCard Gold earned the 2nd place in the category of gold credit cards and a card MasterCard Standard took 3rd place in the ranking of silver cards.

In 2013, the Bank’s offer was expended by two cards for the affluent clients. The first one, MasterCard PayPass gold debit card, was included in the Bank’s offer on 31 October 2013. The card has additional facilities such as contactless payments, dual currency functionality (it is available to complete transaction from the account in PLN or directly from account in EUR) and free insurance package including Pakiet bezpieczeństwa, Assistance medyczny and Assistance domowy. The other card, MasterCard Gold credit card, was included in the Bank’s offer in December 2013. This card also allows to make contactless payments, which means by waving over the terminal. If the amount of the transactions does not exceed 50 PLN, it could be completed without a PIN or signature. The Bank did not excluded from its offer cards without functionality of contactless payments, so that the clients were free to choose a suitable card.

Cooperation with intermediaries

At the end of December 2013, the Bank actively collaborated with 22 network intermediaries, such as Open Finance, Notus and Expander and also with 55 local agents. The cooperation was based on the active sale of banking products. Direct supervision over all cooperation agreements (both with networkbased and local) was performed by the Bank’s Head Office.

In the first half of 2013, the Bank introduced some changes to its policies of collaboration with financial intermediaries. The Bank terminated the cooperation with intermediaries in the respect of active sale of banking products offered to institutional clients from SME segment. The products dedicated to retail clients and institutional clients from Microenterprises segment, so far provided with the financial intermediation, remained the object of the active sale. The process of annexing of cooperation agreements in order to withdraw the active sale of products dedicated to SME segment is managed by the Bank’s Head Office.

In 2013, there was carried on a policy of central monitoring how the intermediaries fulfill their agreements of collaboration. The evaluation concerned sale effects, as well as a quality of the credit portfolio provided by intermediaries. These actions resulted, among others, in the termination of 124 contracts during this period.

7.2. RETAIL BANKING

7.2.1. PRODUCT OFFER DEVELOPMENT

2013 was a year of major challenges in the area of maintaining the volume of retail deposits and achieving the target level of net interest margin. Five interest rates reductions made by MPC resulted in a decrease of 1.75 pp. These changes were the main reason for the modification of deposit offer of savings accounts and term deposits. In August 2013, the Bank introduced new savings account Konto z Zyskiem with two different interest rates for client's so called old and new funds. This product enables the Bank to effectively attract new deposits. Furthermore, the Bank included permanently in its offer investment deposits with almost every month new subscriptions, which was also a successful move. With relatively low interest rates for traditional deposits, the investment deposits provide higher return and principal guarantee. In the second half of 2013, the Bank's offer expanded by several promotional term deposits addressing both acquisition and retention targets. The Bank introduced also two editions of term deposits with investment fund Program Inwestuj i Zarabiaj – in August and October 2013. New offers (especially 24-month term deposit) as well as the continuation of a 12-month progressive term deposit contributed to the extension of client's saving period.

During the entire 2013, the Bank continued to develop and attract the Personal Banking offer, introduced at the end of 2012, which is the main tool for building a base of active affluent clients, treating BGŻ as their first banking choice. As a part of the service of the Personal Banking, affluent customers gained in 2012 the personal advisor, attractive package of the Konto Bardzo Osobiste account enabling to use all transaction services without extra charges, as well as new form of depositing cash flows - Automatic Saving Account. In 2013, the offer was expanded with Lokata Bardzo Osobista term deposit, allowing to invest in a very flexible way for period from 1 to 730 days, a dedicated internet banking service, special exchange rates and MasterCard PayPass gold debit card with dual currency functionality.

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

In the beginning of 2013 an innovative housing loan with fixed interest rate in the first 5 years of credit period was introduced into offer. This new solution provides customers with guarantee of financial security. Simultaneously, as part of the introduction of the PFSA recommendation, the Bank implemented more restrictive lending rules, in particular regarding assessing the creditworthiness, lowering the maximum LTV indicator and shortening the maximum credit period. Other changes aimed to improve the profitability of the product based on changes in price terms, mainly margins, commissions and insurance fees offered to retail customers.

Additional actions to increase the profitability of mortgage products were monitoring client's compliance with the conditions in terms of reduced margins, which were offered provided that the client purchase additional products.

7.2.2. BGŻOPTIMA

The BGŻOptima serves as a supplement to the Bank's offer with regards to saving and investment products, and is dedicated to clients who wish to use Internet-based services. The BGŻOptima offer comprises deposits, saving accounts and distribution of open-end investment funds participation units. In 2013, the Bank's offer has been consistently expanding in the area of deposit and investment products – the offer was extended to include new Investment Fund Managing Companies (TFI), investment deposits (structured), regular saving and investment plans. As at 31 December 2013, the number of clients serviced by BGŻOptima amounted to 112.1 thousand, which means that from the beginning of 2013, 36.4 thousand new clients were acquired. In 2013, the Bank concentrated on improving the average margin on deposit products portfolio in BGŻOptima.

7.2.3. DEPOSIT ACTIVITIES

As at 31 December 2013, the value of retail deposits held by the Bank amounted to PLN 16 377 174 thousand and was nearly PLN 574 754 thousand (3.6%) higher than one year before. BGŻOptima continued to be the main growth factor of retail deposits and starting from the second half of 2013 the growth in deposit balances was noted also in the network of branches.

Table 22. Volume and structure of retail deposits

PLN thousand	31.12. 2013	31.12. 2012	Change	
			PLN thousand	%
Current and savings accounts	10 100 652	8 439 404	1 661 248	19.7%
Term deposits	6 208 272	7 351 820	(1 143 548)	(15.6%)
Other liabilities	68 250	11 196	57 054	509.6%
Total amounts owed to retail customers	**16 377 174**	**15 802 420**	**574 754**	**3.6%**
including: BGŻOptima	**4 151 111**	**3 375 643**	**775 468**	**23.0%**

In 2013, the BGŻ S.A. branches acquisition targets in the area of retail deposits were focused on obtaining new personal accounts and maintaining deposit volumes despite decreasing interest rates. At the same time, the Bank aimed to defend the level of interest margins on deposits, adjusting them to decreasing NBP's interest rates.

The Bank's activity on retail deposits portfolio addressed both acquisition and retention targets. The offer was extended to include new saving account and several promotional term deposits. The Bank continued to sale investment deposits with almost every month new subscriptions, Lokata Progresywna term deposit and Zysk pod ochroną insurance, which provide principal guarantee, fixed interest rate and benefits in case of unexpected events in client's life.

The number of personal accounts as at the end of 2013 amounted to 646.9 thousand, which translates into a growth of 45.4 thousand y/y (7.6%). Total sales of new personal accounts in 2013 amounted to 133.6 thousand and were by 14.1% higher than in previous year. Konto z Premią, with its 49% share in sales, remained unquestionably the most popular among all types of personal accounts. Positive sales results were also achieved thanks to advertising campaign. Konto z Premią, among others, was awarded the first place in the ranking of best personal accounts prepared by the Money.pl portal in 2013, which confirms high attractiveness of this offer.

A characteristic phenomenon in 2013 was the increase in current accounts (by PLN 372 million, i.e. 18.8% y/y), with a simultaneous decrease of funds deposited in term deposits. It occurs traditionally in an environment of low interest rates, when opportunity cost of funds for the maintenance of an interest-free overdraft decreases (compared to depositing them in low-interest deposit products). In addition, an increase in current account balances was supported by a dynamic sales of new accounts. The increase in balances on savings accounts by PLN 1 289 million y/y was realized through BGŻOptimy, for which in 2013 was the main canvassing product.

Table 23. Number of retail deposits accounts

Number of items (In thousands)	31.12.2013	31.12.2012	Change	
Number of deposits accounts in branches	**1 190.5**	**1 153.4**	**37.1**	**3.2%**
Personal accounts	646.9	601.4	45.4	7.6%
Saving accounts	288.7	257.9	30.9	12.0%
Number of savings accounts in BGŻOptima	**129.1**	**83.9**	**45.2**	**53.9%**

** From 31 December 2013, the change in presentation. Deposit accounts include personal accounts, savings accounts including IRA, time deposit accounts and investment products. The new value of presenting the number of deposit accounts does not include the number of technical deposits to handle term deposits and loan products.*

7.2.4. LENDING ACTIVITIES

In 2013, lending activities of the Bank BGZ in the area of retail loans has been focused on improving the profitability of credit products and the systematic building of the Bank's share in the retail lending market.

At the end of 2013, the volume of the retail gross loan portfolio amounted to PLN 9 569 195 thousand and was by PLN 594 417 thousand, i.e. 6.6% higher than as at the end of December 2012. The main growth factors included: sale of cash loans, housing loans and credit cards.

In 2013 the Bank was continuing dynamic growth of cash loans. The total sale of this product amounted to PLN 827.8 million and was by 60.0% higher than in the last year. It was caused by the marketing campaigns organized by the Bank in TV, on the Internet and radio, as well as the implementation of new product functionality, including allowing the loan agreement electronically via the transaction in eBGŻ. Cash loan of BGZ has gained recognition both customers and banking environment, which the crowning achievement was the ranking of the prestigious portal devoted to banking. At the end of 2013, cash loans amounted to PLN 997 101 thousand and were by 24.0% higher than at the end of 2012, the same it was one of the fastest growing parts of the Bank's loan portfolio.

Due to the difficult economic situation in 2013, there was a noticeable decrease in the propensity of individuals to long-term indebtedness, which affected sales of PLN mortgage loans. In 2013 it amounted to PLN 1 009.1 million and was lower by 27.6% than in 2012. However, sales were sufficient to achieve double-digit growth of the portfolio - by 14.1% y/y.

The value of credit card portfolio at the end of 2013 amounted to PLN 82 273 thousand and was by 16.4% higher than a year earlier. During the same period, the number of issued credit cards has increased to 58.1 thousand units, i.e. by 3.8% y / y, which was due to, among others, introduction to active sales in the first quarter of 2013 of a new standard Visa card.

Table 24. Volume and structure of retail loans

PLN thousand	**31.12. 2013**	**31.12. 2012**	**Change**	
			PLN thousand	**%**
Current account loans	103 674	107 615	(3 941)	(3.7%)
Housing loans	8 038 380	7 600 490	437 890	5.8%
– in PLN	5 035 855	4 412 921	622 934	14.1%
– in foreign currencies	3 002 525	3 187 570	(185 045)	(5.8%)
Cash loans	997 101	803 967	193 134	24.0%
Credit card limits	82 273	70 659	11 614	16.4%
Other loans to retail clients	347 767	392 047	(44 279)	(11.3%)
Total loans to retail clients	**9 569 195**	**8 974 778**	**594 417**	**6.6%**

Table 25. Number of retail credit accounts

Number of items (in thousands)	**31.12.2013**	**31.12.2012**	**Change**	
Mortgage, housing and consolidation loans	54.2	53.3	0.9	1.7%
Cash loans	104.1	92.4	11.7	12.7%

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

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

Brokerage fee income in 2013 amounted to PLN 4 874 thousand, compared to PLN 5 392 thousand in 2012. The decrease in brokerage fee income and number of brokerage accounts, as is detailed below, was caused mainly by the reorganization of brokerage service, including, among others, termination of rendering brokerage services by 20 out of 30 branches, economic slowdown, as well as clients' structure. The Brokerage House renders services mainly to domestic investors, including, in particular, individual investors, whose share in the trading volume has continued to decrease in recent years.

At the same time dynamically increased commissions from the sale of units in investment funds run in COPI and the Bank's branches. In 2013 it amounted to PLN 9 936 thousand and was 74.8% higher than a year earlier. By the end of 2013, the net asset value of investment funds sold through BGZ amounted to PLN 1 013 million and was 65.7% higher than a year earlier.

Table 26. Fee and commission income of the Brokerage House of Bank BGZ

Thousand PLN	31.12.2013	31.12.2012	Change	
			Thousand PLN	%
Brokerage fees and commissions	4 874	5 392	(518)	(9.6%)
Commissions from the sale of units in investment funds	9 936	5 684	4 252	74.8%
Fee and commission income from brokerage operations	**14 810**	**11 076**	**3 734**	**33.7%**

At the end of 2013, the Brokerage House maintained 31 198 brokerage accounts (of which 5 818 internet accounts maintained in the bmBGŻ.net transaction system), which, compared to 32 033 accounts at the end of 2012, equaled to 2.6% decrease.

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

		2013		2012	
		Market share	Volume	Market share	Volume
Stock	PLN million	0.19%	966.51	0.23%	962.19
Bonds	PLN million	1.36%	45.07	0.48%	9.97
Futures	Number of contracts	0.59%	139 579	0.47%	98 770
Investment certificates	PLN million	2.06%	2.20	3.37%	3.86
Options	Number of contracts	0.32%	5 161	0.22%	3 082

7.4. INSTITUTIONAL BANKING

7.4.1. CLIENT SEGMENTATION

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

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

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

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

- **Large Enterprises (LE)** – the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act, with annual sales revenues for the previous financial year of PLN 60 million or more, or with credit exposure to the Bank of PLN 25 million or more,
- **Small and Medium-Sized Enterprises (SME)** – the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act (this condition doesn't have to be met in case of farmers), with annual sales revenues for the previous financial year ranging from PLN 10 million to

PLN 60 million, or with credit exposure to the Bank ranging from PLN 2 million to PLN 25 million (in case of farmers ranging from PLN 1 million to PLN 25 million),

- **Microenterprises (Micro)** – the entrepreneurs who do not conduct the full financial reporting according to Polish Accounting Act and the entrepreneurs who conduct the full financial reporting according to Polish Accounting Act with annual sales revenues for the previous financial year of less than PLN 10 million or with credit exposure to the Bank of less than PLN 2 million

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

7.4.2. PRODUCT OFFER DEVELOPMENT

Product packages and transaction products

Micro segment

In April 2013 the Bank withdrew Biznes Lider Plus package from the offer. On 1 August 2013 the Bank did full modification of package offer. At the same time the Bank prepared a modified package offer, which was introduced on 1 August 2013:

- conditional commission for the conduct of the package from the average balance in the account in the packages: *Biznes Lider* and *e-Plan Firma*
- canvassing package *Biznes Lider* and *Agro Lider* was modified
- Package for active clients of *Biznes Lider Aktywny* was modified

At the same time *Biznes Lider Prestiż* and *Agro Lider Prestiż* were withdrawn from the offer packages. In *Agro Lider* package there has been introduced possibility to receive through *eBGŻ Firma* press *Agro Tydzień*, which is published by the Bank BGŻ. In the package *Biznes Lider Aktywny* packs of 75 external transfers made by *eBGŻ Firma* against a flat fee were withdrawn.

SME and LE segments

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

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

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

On 1 June 2013 the Bank introduced the process of client migration to new comprehensive agreements mentioned below. Completion of the exchange agreements is planned for the first half of 2014. In this period it is assumed that 90% of corporate customers' contracts will migrate (excluding customers from a group of local government units whose contracts cannot be exchanged). The strategic objective of these activities is to increase fee income and interest income on the maintenance of the current level.

Credits

Segment Micro

From 10 January 2013, the changes have been made to credit offer and credit process for clients, including micro on simplified accounting (excluding clients involved in agricultural production) through its simplification and standardize.

Current credit offer to Micro customers on a simplified accounting, with the exception of clients involved in agricultural production are:

- *Ekspres Linia* - working capital overdraft on a general basis (protected) and on a simplified (without protection),
- investment credit, including the financing of investments in renewable energy sources (RES) and from the European Investment Bank,
- secured loan, including the possibility of establishing security by other security than solely or partially involving a mortgage, and unsecured loan

Offer to Micro customers on full accounting did not change significantly.

Signing with Bank Gospodarstwa Krajowego *de minimis* warranty line of the portfolio (with annex), enabled the use of the BGK's guarantee for securing revolving investment loans provided to institutional clients, except for clients involved in agricultural production.

LE and SME segments

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

Agribusiness financing

Warranty line "de minimis"

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

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

13 November 2013, the Bank signed an annex to the agreement of *de minimis* warranty line of the portfolio with BGK. Amendment allows BGK for the settlement of warranties "de minimis" also for investment loans. The products to which the *de minimis* warranty will also apply are commercial investment loans, investment loans from the EIB line, investment loans for the financing of renewable energy - Green Energy Loan. The maximum warranty period for an investment loan is 99 months. Guarantees for investment loans are granted within the limits provided by the BGK PLD agreement dated 6 June 2013.

Agro Progress

In September 2013 new product was introduced - investment loan Agro Progress, which is intended to finance the farms. The loan is an alternative to preferential loans, giving the possibility of a much wider and more flexible range of funding at a comparable cost. It is designed for persons engaged in agricultural activities, who want to enlarge and modernize their farm, especially by the purchase of land.

The loan may be granted up to 30 years, and the Bank BGZ on request issues a promise of credit, valid for 12 months. Thanks to this a borrower can fulfill all of their investment plans during the year. Possibility of choice of fixed interest rate makes payments equal, and the change in interest rates does not affect the household budget. In the case of a temporary deterioration of the situation on the farm, it is possible to suspend the repayment of capital by using the so-called "Vacation credit."

Unlike preferential loans, loan Agro Progress gives the freedom to establish the scope and scale of planned investment and a flexible repayment schedule, tailored to the specifics of the business. In individual cases it is possible to determine the annual repayments of capital. The Bank does not require a high own contribution, and the procedure for granting the loan is friendly and has been kept to a minimum. The customer does not need to present a business plan - assessment of creditworthiness can be carried out on the basis of the currently pursued production.

New credit "klęskowy" with ARiMR subsidies

In September 2013 the Bank introduced an additional offer of revolving loan "*klęskowy*" with interest subsidized by the ARiMR in the form of de minimis aid. This loan is intended to resume production on farms, where losses due to natural disasters were equal to or less than 30% of annual agricultural production. So far affected farmers could benefit from the loan "klęskowy" if losses on the farm as a result of the disaster exceeded 30% of annual production.

Other new products

Since March 2013, customers can benefit from a new product, which is the Investment Loan granted by the European Investment Bank. The main benefit to the borrower, who decide on funding as part of the EIB line is to reduce the margin by min. 30 base points in relation to the rate for comparable loans granted by the Bank BGZ without the support of the EIB. The loan may be classified to the line provided an application for a reservation of sources and receipt of acceptance by the Asset and Liability Management Office (AP Office).

Since June 2013, the Bank also introduced a lease for the implementation of projects within the Sustainable Energy Financing in Poland (PolSEFF). The rules for obtaining financing are the same as for the investment loan.

7.4.3. LENDING ACTIVITIES

In 2013 the Bank recorded a slowdown in lending to institutional clients. As at 31 December 2013 value of gross loan portfolio amounted to PLN 17 980 730 thousand and decreased by PLN 471 950 thousand, i.e. 2.6% compared to 31 December 2012.

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

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

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

Table 28. Loans and advances to institutional customers

PLN thousand	**31.12.2013**	**31.12.2012**	**Change**	
			PLN thousand	**%**
Overdraft facilities, including	**4 168 862**	**4 184 718**	**(15 856)**	**(0.4%)**
– corporate customers	1 907 354	2 251 740	(344 386)	(15.3%)
– individual entrepreneurs	313 552	345 581	(32 029)	(9.3%)
– farmers	1 926 116	1 556 847	369 269	23.7%
Loans and advances to customers:	**13 811 868**	**14 267 962**	**(456 094)**	**(3.2%)**
– corporate customers, including:	6 928 236	8 068 821	(1 140 585)	(14.1%)
- investment loans	4 238 097	4 850 132	(612 035)	(12.6%)
- operating loans	1 752 067	2 088 980	(336 913)	(16.1%)
– individual entrepreneurs	1 259 146	1 242 443	16 703	1.3%
– farmers	5 217 481	4 579 424	638 057	13.9%
– public sector institutions	251 572	313 976	(62 404)	(19.9%)
– other entities	155 433	63 298	92 135	145.6%
Total	**17 980 730**	**18 452 680**	**(471 950)**	**(2.6%)**
of which:				
Preferential loans	4 601 931	4 208 569	*393 362*	*9.3%*

7.4.4. DEPOSIT ACTIVITIES

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

Table 29. Amounts owed to institutional customers

PLN thousand	31.12.2013	31.12.2012	Change	
			PLN thousand	%
Other financial institutions:	**1 046 953**	**2 537 917**	**(1 490 964)**	**(58.7%)**
Current accounts	9 894	9 268	626	6.8%
Term deposits	1 037 048	2 528 638	(1 491 590)	(59.0%)
Other liabilities	11	11	-	-
Corporate customers:	**8 466 581**	**7 924 618**	**541 963**	**6.8%**
Current accounts	4 891 096	3 974 989	916 107	23.0%
Term deposits	3 510 860	3 871 567	(360 707)	(9.3%)
Other liabilities	64 625	78 062	(13 437)	(17.2%)
Corporate customers, of which farmers:	**1 200 404**	**1 009 139**	**191 265**	**19.0%**
Current accounts	1 040 784	856 815	183 969	21.5%
Term deposits	152 923	143 693	9 230	6.4%
Other liabilities	6 697	8 631	(1 934)	(22.4%)
Public sector customers:	**602 066**	**677 074**	**(75 008)**	**(11.1%)**
Current accounts	458 346	484 830	(26 484)	(5.5%)
Term deposits	143 593	192 118	(48 525)	(25,3%)
Other liabilities	127	126	1	0,8%
Total	**10 115 600**	**11 139 609**	**(1 024 009)**	**(9,2%)**

Deposits of enterprises and farmers showed an upward trend. Especially dynamically grew obligations on current accounts (including the savings accounts for farmers and micro-enterprises). The Bank decreased the scale of funding from non-bank financial institutions, particularly in comparison with temporarily high state of these measures, which occurred at the end of 2012,

7.4.5. TRADING BUSINESS FINANCING

Factoring

As part of providing factoring services, in 2013 the Bank acquired 145 739 invoices with a total value of PLN 2 976 388 compared to 121 758 invoices acquired in 2012 with a value of PLN 3 064 791.

In order to simplify product structure and improve quality of document templates used in customer service, changes were made in the Bank's factoring offer in June 2013. Niche products that were withdrawn from the Bank's offer include reverse factoring, financing of debt factoring (repurchase of individual receivables), recourse factoring. Uniform boundary conditions were introduced for all factoring transactions, such as concentration, level of advances, maximum financing term, grace period, number of counterparties etc.   regards to document templates, entries giving uncommitted character to factoring relation were introduced.

In December 2013, there were introduced for factoring, in relation to the rating and sector of client, the same general principles of credit, which are applicable to other loan products of the Bank.

In order to seal the process of operational service of factoring agreements and optimize the entire process of factoring in the Bank, there was implemented a new application to monitoring the timeliness and quality of contractors' factoring payments.

Bank guarantees and letters of credit

Bank realized the recommendation of the Financial Supervision Authority and showed conditional liabilities in respect of undrawn contracts of lines on letters of credit and guarantees - at the end of 2013, the total amount of these liabilities amounted to PLN 332 million.

As at the end of 2013, the total amount of the guarantee obligations granted to customers amounted to PLN 447.3 million in comparison to PLN 615.6 million at the end of 2012. There were 1 522 guarantees granted in the portfolio.

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

In 2013 the Bank issued 261 import letters of credit with a total value of PLN 83.3 million (compared to 277 import letters of credit with a total value of PLN 81.9 million in 2012) and processed 89 export letters of credit with a total value of PLN 58.7 million (compared to 142 export letters of credit with a total value of PLN 71.8 million in 2012).

7.5. ACTIVITIES IN DEBT SECURITIES MARKET

In 2013, the Bank served four issues of debt instruments, including two programs of issue of municipal bonds. In 2013, the Bank organized the issue of corporate bonds for the new entity, and acted with this issue as an issuing agent, paying agent, calculation agent, dealer and custodian.

7.6. ACTIVITIES IN MONEY AND FOREIGN EXCHANGE MARKETS

In 2013, the activities of the Bank in money market and foreign exchange market were significantly influenced by the following factors:

- start of reduction of the quantitative easing (i.e. QE3) by the Federal Reserve in December 2013, a first step in tightening monetary policy in the United States,
- maintaining a low rate of economic growth in the Eurozone combined with a further decline in inflation,
- stop of the negative trend in economic growth in Poland in the second quarter of 2013, followed by the acceleration of economic growth,
- decline in CPI inflation in Poland below the MPC inflation target of 2.5%, followed by its stabilization at a low level in the second half of 2013,
- faster and deeper than originally expected continuation of the cycle of interest rate cuts in Poland to 2.5% linked to the announcement of the MPC of keeping interest rates unchanged until at least the end of the first half of 2014,
- stabilization of PLN against foreign currencies, leading to a decline in the volatility of the EUR/PLN in the fourth quarter of 2013 to historical lows,
- achieving record-low yields of domestic bonds in the second quarter, after which the increase in yields to expected changes in monetary policy by the Federal Reserve and the improving economic situation in Poland,
- persistently high liquidity of the banking sector conducive to reducing and then stabilizing at a low level, the cost of obtaining funds from customers of the Bank.

In 2013, the Bank introduced in the area of Financial Markets changes resulting from the Regulation of the European Parliament and of the Council (EU) No 648/2012 of 4 July 2012 on derivatives traded OTC, by central counterparties and trade repositories (EMIR) in reducing the risk of bilateral transactions, such as the introduction of procedures derivatives portfolio reconciliation and transactions' compression, dispute resolution and processes of timely confirmation of derivative transactions. In 2014, the Bank will continue to work on the implementation of the Ordinance, mainly in the field of transaction reporting to a trade repository and central clearing of OTC transactions.

Activities on own account

FX market

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

Interest rate market

The Bank's trading activities on interest rate market concentrated on PLN yield curve, mainly on the Polish T-bonds. The Bank increased its activity on market of interest rate instruments denominated in foreign currencies mainly EUR, what was the result of higher interest of Bank's clients for instruments hedging interest rate risk in foreign currencies compared to previous year. In 2013, the Bank substantially increased its market share in the segment of Buy-Sell-Back and Sell-Buy-Back transactions hedged with treasury securities. Similar to previous years, the Bank did not conduct trading activities in the market of non-treasury debt securities.

Short-term liquidity management

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

Assets and liabilities management

Asset and liability management is shaping the Bank's balance sheet in a way that minimizes the negative impact of variability of external factors - such as interest rates, exchange rates and the cost of financing - on the Bank's financial stability. At the same time it shall enable - within the assigned risk limits - generating additional income from the Bank's risk position adjustment to long-term market trends.

Financing Bank activities

In 2013, there are two sub-periods, featuring a different approach to the issue of financing the Bank's operations. In the first half of 2013 there was substantial surplus of funding sources over loans (approximately PLN 4.8 billion), which was to finance the planned growth of the loan portfolio in the coming quarters. In the second half of 2013 , as a result of the economic downturn and the conservative policies of risk (in particular in relation to the segment of non-Agro), this increase did not materialize, so after the financing side the Bank focused on optimizing the size of liabilities and reducing their cost: reduced the interest rates on deposits and accounts in the wake of cuts in interest rates by the MPC, has abandoned further issuance of certificates of deposit (CDs) and did not draw any new long-term credit lines, so that the total volume of these two positions declined in 2013 by PLN 1.1 billion. The Bank reduced the financing obtained from financial institutions – by PLN 1.3 billion - mainly in the form of negotiated deposits from large companies and financial institutions, while maintaining the virtually unchanged level of the most stable deposits from retail customers and small and medium-sized enterprises (including + PLN 0.2 billion) :

Table 30. Financing lending activities by type of source

PLN million	31.12. 2013	30.09. 2013	30.06. 2013	31.03. 2013	31.12. 2012	Change in 2013	Change %
Retail	15 704	15 993	16 239	15 976	15 640	64	0.4%
Micro and SME	7 085	7 131	7 507	7 472	6 931	154	2.2%
DP customers	2 060	1 922	1 755	1 785	1 887	173	9.2%
Financial customers	978	529	992	1 246	2 309	(1 331)	(57.6%)
CD, credit lines	4 373	4 733	5 391	5 674	5 430	(1 057)	(19.5%)
Financing, total	**30 200**	**30 309**	**31 884**	**32 153**	**32 198**	**(1 997)**	**(6.2%)**
Loans	**(27 548)**	**(27 507)**	**(27 087)**	**(27 282)**	**(27 415)**	**(133)**	**0.5%**
Financing surplus	**2 652**	**2 802**	**4 797**	**4 870**	**4 782**	**(2 130)**	**(44.5%)**

Source: Office of Assets and Liabilities Management Board

Aggressive interest rate cuts by the MPC, and followed them by the Bank, resulted in a partial migration of funds deposited by customers from fixed-term deposits for current and savings accounts, where low interest rates is compensated by the greater freedom of access to resources. On the other hand, the Bank increased funding obtained for periods of 12 months or longer, with an attractive offer of long-term retail deposits and investment deposits:

Table 31. Financing lending activities by time of (residual) maturity

PLN million	31.12. 2013	30.09. 2013	30.06. 2013	31.03. 2013	31.12. 2012	Change in 2013	Change %
On demand	15 223	15 966	16 133	14 809	13 236	(1 987)	(13.1%)
1D - 3M	6 105	6 146	7 668	8 595	9 791	3 686	60.4%
3M-12M	2 142	1 766	1 912	2 698	3 173	1 031	48.1%
12M+	6 730	6 430	6 171	6 052	6 000	(730)	(10.8%)
Financing, total	**30 200**	**30 309**	**31 884**	**32 153**	**32 198**	**1 998**	**6.6%**

Source: Office of Assets and Liabilities Management Board

Approx. 17% of the Bank’s assets are loans in foreign currencies, mainly in CHF, EUR and USD. In order to make the liquidity situation and result independent of currency exchange rates, the Bank seeks to balance the assets and liabilities in the same currency: in 2013 loans in EUR and USD were financed by funds collected from customers on current accounts and term deposits, and (in the case of EUR) of the EBRD credit line. The remaining in-use portfolio of mortgage loans in CHF is funded by the CHF line with Rabobank. The remaining open currency position is managed on an ongoing basis using short-term FX swap:

Table 32. Financing of assets in foreign currency

PLN million	31.12. 2013	30.09. 2013	30.06. 2013	31.03. 2013	31.12. 2012	Change in 2013	Change %
				EUR			
EUR Loans	(1 261)	(1 390)	(1 351)	(1 397)	(1 366)	104	(8.0%)
EUR Financing	1 312	1 363	1 149	1 235	1 390	(78)	(6.0%)
EUR Surplus (+) / Gap (-)	**51**	**(27)**	**(202)**	**(162)**	**25**	**26**	**106.0%**
				USD			
USD Loans	(122)	(125)	(119)	(110)	(107)	(15)	14.0%
USD Financing	416	412	393	393	404	12	3.0%
USD Surplus (+) / Gap (-)	**294**	**287**	**274**	**282**	**297**	**(3)**	**(1.0%)**
				CHF			
CHF Loans	(3 224)	(3 354)	(3 471)	(3 456)	(3 463)	239	(7.0%)
CHF Financing	2 751	2 879	2 989	2 997	3 028	(277)	(9.0%)
CHF Surplus (+) / Gap (-)	**(473)**	**(476)**	**(482)**	**(459)**	**(435)**	**(38)**	**9.0%**

Source: Office of Assets and Liabilities Management Board

Interest rate risk, investment portfolio and hedging transactions

Structural Bank's exposure to interest rate risk – i.e. the sensitivity of net interest income, on the scope and direction of interest rates change - was adapted to the changing market situation, ranging from mid-February 2013, the position was gradually reversed from a "long" (favorable for reductions in interest rates) in the "short", supported by the transfer of short term deposits to less sensitive bills on request and shortening OIS transactions by which the AP manages the mismatch in the reprising of assets and liabilities.

As a result, the sensitivity of net interest income of the Bank on increase in interest rates by 200 bps linearly during the year (the Interest at Risk, IAR) was reversed from PLN -3.7 million at the end of December 2012, to PLN 15.8 million at the end of March 2013 and PLN 37.1 million at the end of December 2013. Similarly, the sensitivity of the fair value of equity (the so-called Equity at Risk, EaR) - illustrating the sensitivity of net interest income of the whole balance sheet, and thus also in the horizon longer than one year, was limited in the first and second quarter of 2013 and was rebuilt slowly in the second half of the year

Table 33. Interest rate risk profile (average per month)

Measure of risk	31.12. 2013	30.09. 2013	30.06. 2013	31.03. 2013	31.12. 2012
200 bps upwards (IaR, PLN thousand)	37 083	38 550	30 278	15 824	(3 776)
200 bps downwards (IaR, PLN thousand)	(39 085)	(40 672)	(31 095)	(17 541)	8 968
Sensitivity of fair value of equity (EaR, in years)	0.91	1.05	0.45	0.86	1.04

Source: Office of Assets and Liabilities Management Board

From the perspective of the end of the year, reversing the position was held for 2-3 months too early, which was caused by the expectation that interest rates will be reduced to 3.5% (instead of 2.5%), and therefore the Bank expected completion of the interest rate cuts cycle in March or April.

A large role in shaping the exposure to interest rate risk - EaR - and stabilization of the Bank’s result plays investment portfolio of debt securities. Its value in the 12 months of 2013 increased from PLN 2.5 billion to PLN 3.2 billion, wherein in this period the AP Office sold PLN 0.8 billion of securities maturing in 2015, realizing an additional revenue of PLN 39 million, and bought PLN 1.6 billion of medium-and long-term securities, keeping the interest income from the portfolio of approximately PLN 12-13 million per month, a total of PLN 153 million in 2013

By the end of 2013 the fair value of the portfolio, taking into account accrued interest is PLN 3.44 billion, including PLN +97 million is recognized in the revaluation reserve - this represents the discounted value of the difference between the interest income generated in the future by the portfolio, and the revenue with the same portfolio acquired on the valuation day at market prices.

Funds' transfer price

Low interest rates in Poland as well as all over the world, stable situation on the financial market in respect of country risk and awaiting increase in economic activity in Europe and the USA, favored cuts in financing costs. In 2013, the AP Office performed systematic reviews of internal liquidity margin, reducing it in accordance with market trends - cost ratio fell by 10-20 bps for medium-term deposits and 20-30 bps for long-term loans. As a result, the basic function of the TCF system - risk transfer - has been maintained at the same time stimulating the pricing policy of the Bank: compression of margins on loans was offset by lower margins on deposits renewed.

Sale of treasury products to clients

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

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

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

In the second half of 2013, customers could use functionality in the system eBGŻ Treasury for placing conditional orders, i.e. the "offer to sale" and "offer to purchase" (functionality "Book of orders").

7.7. COLLABORATION WITH FINANCIAL INSTITUTIONS

As at the end of 2013, the Bank maintained correspondent contacts with approximately 870 banks keeping 25 Nostro accounts in 16 main currencies in foreign banks.

As at 31 December 2013, the Bank maintained 28 Loro accounts in 6 currencies for 19 foreign banks, 1 domestic bank and 1 foreign non-banking financial institution. The Loro accounts maintained in books of the BGŻ S.A. represent an external source of securing working capital funds at no cost, which serve to satisfy the operating needs of the Bank. Using these accounts, the Bank executes primarily client transfers and bank-to-bank transfers.

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

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

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

7.8. FINANCING FOREIGN TRADE

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

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

In 2013, the upward trend was maintained in respect of transfers of foreign trade. The share of SEPA Credit Transfer in the total import and export transfers in 2013 increased compared to 2012 and amounted to 69.6% and 67.6%.

Table 34. Statistics of operations handled by BGŻ S.A.

Transaction type	Quantity/value	2013	2012	Change
Transactions using the nostro accounts (commercial banks and NBP)	Number of transactions	782 447	700 253	11.73%
	Value in PLN billion	3 193 006	2 947	8.3%
Transactions using the loro accounts	Number of transactions	101 860	119 303	(14.2%)
	Value in PLN billion	750	783	(4.2%)
Export transfers	Number of transactions	488 319	433 383	12.7%
	Value in PLN billion	21 140	22 887	(8.2%)
including: SEPA Credit Transfer	Number of transactions	330 314	257 397	28.3%
	Value in PLN billion	8 628	6 800	26.9%
Import transfers	Number of transactions	201 401	175 227	14.9%
	Value in PLN billion	12 265	13 427	(9.5%)
including: SEPA Credit Transfer	Number of transactions	140 181	90 789	54.4%
	Value in PLN billion	5 896	4 616	27.7%
Own letters of credit and own documentary collection (newly opened)	Number of transactions	298	328	(9.1%)
	Value in PLN billion	120	81	48.1%
Guarantees and own promissory notes granted	Number of transactions	1174	1533	(23.4%)
	Value in PLN billion	283	390	(27.4%)
Third party letters of credit and third party guarantees	Number of transactions	507	514	(1.4%)
	Value in PLN billion	183	154	18.8%

7.9. BANK ORGANIZATION AND HUMAN RESOURCES

7.9.1. ORGANIZATIONAL STRUCTURE

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

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

- Retail and Business Banking area responsible for sale and development of products targeted at individual customers and microenterprise segment

- Corporate Banking area responsible for sale and development of products targeted at micro, medium and large companies as well as large agro companies.

<u>In the area of Retail and Business Banking</u>, customer service to retail clients and micro enterprises is provided by operational and subordinated branches supported by regional branches and departments of the Head Office focused on the area of Retail and Business Banking.

In order to make support of Head Office in the area of sale and client service more effective and efficient, the Bank put pressure on product offer standardization, automation and simplification of credit process, including shortening decision-making procedures and maintenance of stable, long-term relations strengthen by dedicated approach to Agro clients. Completed developments confirm the importance of what the Bank pays to ensure service quality for external and internal customers in line with their expectations and the efficient management of the process for handling complaints, complaints and customer inquiries.

Under the Corporate Banking, in order to better establish and develop cooperation with corporate clients in the regions, there was created a network of business centers (respectively, small, medium and large enterprises). Their activities are coordinated and supported both at the regional level by the regional directors for corporate banking, as well as from the cells of the Head Office concentrated on the Area of Financial Markets and Corporate Banking.

In the Head Office there were introduced organizational changes supporting management of wide range of products and banking services with application of Internet banking, telephone and mobile channels. tailored to the individual needs of clients as well as strengthening professional business consulting services, supported by product specialists and specialists in Agro. Important action to improve the quality of service for corporate clients was the creation of a central unit - Customer Service, responsible for customer support, Customer Advisors and Product Managers in all stages following the sale of the product/service, ranging from the implementation of the client's daily operational services and information.

An important role in the organizational structure of the Head Office is performed by new cells of Head of Strategy and Development Area, established in July 2013. Its creation proves rank and importance the Bank attaches to the long-term mission of building relationships with customers by offering high quality service and a full range of transparent banking products with particular inclusion of good communication and innovative solutions to support customer relationships with agri-food sector.

Changes in the business areas in 2013 favorably affecting the course of the sales process and customer service from all segments were coordinated with the organizational activities on side of cells grouped in other areas, particularly in the Analysis and Decision Credit Area and Systemic Risk Area. Operation Risk Management was strengthened by centralizing control functions and operational risk management in the regions. Additionally, changes in the process of credit risk assessment, better adapted to the new division of customer segments and in terms of credit administration.

7.9.2. HUMAN RESOURCES

Employment levels

At the end of 2013, the Bank had 5 586 employees (5 526.88 FTE’s), i.e. by 1.1% less than in the previous year. Average employment in 2013 for the Bank amounted to 5 537.94 FTEs compared with 5 683.64 FTEs in 2012 (a decrease of 2.6% y/y - favorably affecting the dynamics of costs).

The Office employment fell by 4.5% y/y. The fall in employment in the Bank was the result of implemented in 2012, the Bank's cost optimization program, in this through optimization of employment, mainly at the Head Office of the Bank.

Table 35. Bank's employment in employees and FTEs

	31.12.2013	31.12.2012	Change	
Network*	4 061	4 085	(24)	(0.6%)
Headquarters*	1 382*	1 438	(56)	(3.9%)
Brokerage Office	58	32	26	81.3%
BGŻOptima	52	49	3	6.1%
Holiday resorts	30	30	-	-
Trade unions	3	3	-	-
Total (employees)	**5 586**	**5 637**	**(51)**	**(0.9%)**
Network*	4 030.19	4 056.45	(26.26)	(0.6%)
Headquarters*	1 362.63	1 426.87	(64.24)	(4.5%)
Brokerage Office	58.00	32.00	26.00	81.3%
BGŻOptima	43.56	39.88	3.68	9.2%
Holiday resorts	29.50	29.50	-	-
Trade unions	3.00	3.00	-	-
Total (employees)	**5 526.88**	**5 587.70**	**(60.82)**	**(1.1%)**

***** *due to changes in organizational structures and the inclusion in the Headquarters of staff networks, the data is not fully comparable between the end of 2013 and 2012,*

Salaries

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

Table 36. Payroll costs

PLN thousand	**2013**	**2012**	**Change**	
			PLN thousand	**%**
Payroll costs including:	**379 323**	**398 227**	**(18 904)**	**(4.7%)**
- base remuneration	338 572	336 242	2 330	0.7%
- other components of salaries and wages *	10 075	6 111	3 964	64.9%
- awards and bonuses	41 359	60 695	(19 336)	(31.9%)
- non-employment contracts	3 395	3 655	(260)	(7.1%)
- provisions for future liabilities**	(14 079)	(8 476)	(5 603)	66.1%
Social security and other employee costs	**95 806**	**103 191**	**(7 385)**	**(7.2%)**
- salary overheads	56 482	57 997	(1 515)	(2.6%)
- employee benefits	5 446	8 659	(3 213)	(37.1%)
- employment restructuring write-off	7 746	16 901	(9 155)	(54.2%)
- Contributions to the Social Fund	6 072	6 232	(160)	(2.6%)
-other	11 789	11 845	(56)	(0.5%)
- provisions for future liabilities**	8 271	1 557	6 714	431.1%
Total payroll	**475 129**	**501 418**	**(26 289)**	**(5.2%)**
Awards and bonuses as % of base remuneration	***12.2%***	***18.1%***		**(5.8%)**

** Contingent liabilities payments due to changes in the Management Board of the Bank*
*** Concerning provisions for liabilities for unused vacation, retirement, disability and death benefits - for the current year and previous years, and provisions for bonuses and awards from previous years.*

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

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

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

The level of the cost of salaries in the Bank in 2013 was primarily influenced by the optimization process of employment, including the reduction of employment in the context of collective redundancies and staff movements. Additionally, the level of costs was influenced by increases in base remuneration running from 1 June 2012 and from 1 July 2013 for the best employees.

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

Incentive schemes

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

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

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

Training and career development

In 2013, a training program was focused on cooperation with business, supporting the realization of the Banks' strategic goals through the development of employee skills and competences. The program covered training organized both in traditional and e-learning form. The number of employees who participated in the Bank's training program was 53 910, including 41 408 participants in e-learning training.

The main areas of trainings were as follows:

- Continuation of awareness raising activities in terms of risk culture in the Bank, especially in the areas of credit and operational risk as well as compliance.
- To promote and exchange knowledge and experiences from the sale of products to customers from Agro segment of the banking business advisors.
- Training for sales employees aimed at improving product knowledge.
- Training in the Personal Banking area preparing advisors to perform their duties and preparing subordinate branch representatives to VIP customers service.
- Continuation of „Po pierwsze klient" project co-financed by the European Social Fund; training intended to implement customer service standards.
- Building advanced sales competencies as a part of implementation of new customer service model – 1-year complex development program High Achiever for Large Companies relationship managers.

Completed development programs:

- Potential Development Program "The Prestige" - continued and completion of the second edition of the program, which aims to identify and develop employees with the highest potential in the fields of management and expertise. The qualification process for third edition has been conducted.
- Sales Talent Development program - which is dedicated to the best advisors, implemented in three development paths consistent with the needs of employees: managerial, sales and expert as well as competence of an individual.
- Leadership Development Program - for top executives from regions of Retail Banking and Business as well as Corporate Banking. The aim of the program was to diagnose leadership skills and their development within the leadership workshops.

Internships programs

The Bank offers internship programs to students and graduates. In 2013, 220 interns had the opportunity to work at the Bank. The Bank established cooperation with Warsaw University of Life Sciences and signed an agreement based on which the Bank admitted students recommended by the University to take part in internship program. A special program of summer internship was developed for this group, under which the Bank organized internship workshops where the participants could improve their skills.

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

The construction of the image of the institution as a desirable employer (employer branding)

In 2013, the Bank carried out activities related to the construction of the image of the employer and the cooperation with external labor market. The main goal was to create consistent and distinctive features of the Bank's image - based on the keynote: "I like when the results count, important is how I achieve them."

In 2013 the project of employer image strategy has been build, under which internal and external brand research was conducted and the most important features distinguishing the Bank from other employers have been chosen.

In 2013 the Bank was again on the list of best employers highlighted in the "Universe TOP 100 Ideal Employer for Students".

Social Welfare and medical care

The social fund is intended for the implementation of benefit payments (awarded on the basis of social criteria) for employees (approximately 5 500 persons) and pensioners of the Bank (approximately 4 500 people). In 2013, 5 600 social benefits have been awarded. The largest contributors were: subsidies for vacation holiday of employees and their children (4 645 benefits), financial aid (705 services) and housing loans (250 loans)

Also funds from ZFŚS are intended for financing: sports and recreation events, tourist trips, sport tickets – Multisport, purchase of tickets/vouchers to theaters/cinemas, events for children of employees. The Bank's employees have the option of profiting from private medical care. Around 75% of employees are covered by such medical care.

7.10. INFORMATICS

In 2013, the IT Department spent PLN 69.84 million on its investment projects. During this period, 15 projects were completed. 20 projects were in progress.

The most significant IT initiatives undertaken are as follows:

- Implementation of the integration between the CRM system and loan application service system for retail clients, which expands the range of loan applications data and customer data.
- Implementation of privilege account management system as well as rules and mechanisms of integrity of data stored in databases and during their exchange for selected payment systems.
- Adjustment of banking systems to clearing services under SORBNET2 due to withdrawal of SORBNET by NBP.
- Implementation of Derivatives module in a computer system of the Bank's Head Office, which ended a multi project implementation of this system.
- Adjustment of the Brokerage Office system to the new Stock Exchange system and to communication with KDPW.
- The implementation of the integration platform Single Sign-On, through which customers will be granted access to transactional services of the Bank.
- Implementation of new functionality to support treasury products servicing in the electronic channel.
- Implementation of new card system module in order to integrate PIN generation and prepare data to be saved on magnetic stripe.
- Implementation of application automatically generating exchange rate tables.
- Migration of SWIFT environment application to virtual platform.
- Implementation of new workflow for retail banking.
- Implementation of new legal documents management system.
- Automation of processes in the area of administration of loans.
- Improving safety and functionality of the service of closed payments.
- The introduction of mobile top-ups and electricity meters by electronic banking.
- Migration of basic transactional system to a new hardware platform and the new version of the database.
- Improvement of safety, capacity and efficiency of the Bank's IT infrastructure (including the implementation of a system to protect against DDOS attacks, the diversification of network devices, servers and exchange matrix).
- Partial implementation of a system of Identity and Access Management class.
- Migration of publishing settlement functionality for bank cards.
- Migration of bank card authorization system to an external supplier.
- The introduction of the sale of consumer loans through the Internet channel.

8. RISK MANAGEMENT

8.1. CREDIT RISK

Credit risk management

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

Credit risk is included in the basic and essential financial activities of the Bank, including both lending activity, as well as the financing of capital market products. As a result, credit risk is identified as having the greatest risk of potential impact on current as well as future profits and equity of the Bank. The significance of credit risk confirms its 70% share in the total amount of economic capital estimated by the Bank to cover the significant risks involved in the activities of the Bank, as well as 90% of the total amount of regulatory capital.

The primary objective of credit risk management is the implementation of the Bank's strategy through harmonious growth of the loan portfolio while maintaining an acceptable level of credit risk appetite.

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

- each credit transaction requires a comprehensive assessment of credit risk, which is reflected by internal rating or scoring,
- thorough and careful financial analysis provides a basis for recognition of customer financial data and information about the value of the collateral as reliable; careful analysis of the Bank always includes the necessary safety margin,
- financial base for the client is - as a rule - its ability to generate cash flows to ensure repayment of financial obligations to the Bank,
- credit risk assessment is additionally verified by independent of the business services, credit risk assessment services,
- price terms of credit transactions must cover the risks of the transaction,
- credit risk is diversified in terms of geographical areas, sectors, products and customers
- credit decisions can be made only by authorized persons,
- the Bank enters into credit transactions only with known customers, and the basis for cooperation with clients are long-term relationships,
- client and concluded with the client transactions are monitored in a manner transparent to the client and strengthening customer relationships.

Collaterals

Established by the Bank means of legal protection of loan transactions are monitored by evaluating the value of any collateral on the basis of documents submitted by borrowers. In addition, during the evaluation of collateral, the Bank uses internal databases that contain historical information about statistics of realization of rights to collateral.

The Bank recognizes that the primary protection of the Bank's interest is good financial standing of a customer, while the acceptance of the material or personal collateral is an additional aspect of mitigating risk in the event of insolvency of the customer.

The key principles of hedging the Bank's credit exposures, including special rules for mortgages, are described in credit handbook of institutional clients and management policy for retail credit exposures of BGŻ S.A., adopted by the Management Board.

As a rule, the Bank requires that the collateral was established prior to release of funds relating to loan transaction, and the form, nature and value of the security was adequate for the identified risk of hedged transaction. When choosing the form and the collateral the Bank takes into account particularly:

- nature, amount and duration of the credit transaction,
- requirements for establishing a specific form of collateral for specific product,
- economic and financial situation of the debtor in respect of a collateral in case of personal security and the value of the collateral for material security,
- liquidity of the collateral, understood as a real opportunity to meet the Bank's claims of security in the shortest possible time, and without a significant decrease in the value of the collateral due to the price fluctuation of the collateral,
- costs incurred by the customer associated with the establishment of collateral,
- availability and the ability to control the collateral and time needed for monitoring by the Bank,
- place in ranking for claiming collateral.

Bank's internal regulations specify the procedures for the establishment, measurement and monitoring of collateral, including requirements for assessment of the financial standing of the personal security issuer, and with respect to the collateral - the principles of valuation of assets that the Bank accepts as a collateral. With respect to the mortgage collateral, the Bank determines the value of the property based on valuations prepared by professional appraisers, and for selected types of real estate Bank accepts internal valuations based on statistical data and transaction prices. In the case of other physical collateral (pledge registration, transfer of ownership) the Bank calculates the value of the collateral, in particular, on the basis of actual transaction prices.

Update of the value of collateral, the evaluation of the technical condition of the collateral and the control of LtV ratio for transactions secured by mortgages, are elements of monitoring customer credit risk, including transactions. Reducing the risk of changes in the collateral value is carried out, inter alia, through including relevant provisions in the loan agreements, including contractual clauses regarding inability to satisfy from fixed asset collateral pledged as security - without consent or notification to the Bank - or a lack of possibility of disposal fixed assets - without consent or notification to the Bank.

Implementing the provisions of the rules and supervisory recommendations, the Bank introduced internal rules complying with the regulations of the Financial Supervision Commission, in particular with Recommendation S concerning the mortgage collateral.

Structure and quality of credit portfolio

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

As at 31 December 2013, the share of receivables that are impaired in the gross portfolio of loans and advances to customers amounted to 8.1% compared with 7.2% for 31 December 2012. Increase in ratio for total portfolio was a result of higher share of receivables that have lost value in the portfolio of mortgage loans, respectively to 5.2% from 4.9%, and the portfolio of loans to corporate customers excluding farmers, respectively to 12.6% from 9.4%. In the latter case, this partially resulted from the increase in value of impaired loans due to the economic downturn, and in part from a decrease in the total value of these loans.

Table 37. Credit portfolio structure

PLN thousand	31.12.2013		31.12.2012	
	PLN thousand	Share in %	PLN thousand	Share in %
Loans and advances, gross	**27 549 925**	**100.0%**	**27 427 458**	**100.0%**
Mortgage loans	8 038 380	29.2%	7 600 490	27.7%
– in PLN	5 035 855	18.3%	4 412 921	16.1%
– in foreign currencies	3 002 525	10.9%	3 187 570	11.6%
Cash loans	997 101	3.6%	803 967	2.9%
Other loans to retail clients	533 714	1.9%	570 321	2.1%
Individual entrepreneurs	1 572 698	5.7%	1 588 024	5.8%
Farmers	7 143 597	25.9%	6 136 271	22.4%
Corporates	8 835 590	32.1%	10 320 561	37.6%
Public sector	252 979	0.9%	252 980	0.9%
Other receivables	175 866	0.6%	154 844	0.6%

The quality of cash loans to retail customers has improved (decrease of ratio respectively from 17.8% to 13.0%), what was driven by the dynamic growth of the portfolio and a number of receivables overdue.

The ratio of share of impaired loans in the portfolio of agriculture was low during 2013, and it further improved (from 3.6% to 3.5%). The agricultural sector showed good resistance to the economic downturn.

Table 38. Quality of the loan portfolio

PLN thousand	31.12.2013			31.12.2012		
	Gross Total	Including: impaired	share %	Gross Total	Including: impaired	share %
Loans and advances, gross	**27 549 925**	**2 236 159**	**8.1%**	**27 427 458**	**1 969 672**	**7.2%**
Mortgage loans	8 038 380	420 367	5.2%	7 600 490	373 815	4.9%
– in PLN	5 035 855	226 555	4.5%	4 412 921	204 505	4.6%
– in foreign currencies	3 002 525	193 812	6.5%	3 187 570	169 310	5.3%
Cash loans	997 101	129 275	13.0%	803 967	143 159	17.8%
Other loans to retail clients	533 714	69 957	13.1%	570 321	76 566	13.4%
Farmers	7 143 597	248 422	3.5%	6 136 271	219 038	3.6%
Corporate clients excluding farmers	10 837 133	1 368 139	12.6%	12 316 409	1 157 095	9.4%

Restructuring and recovery of high risk debt

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

- identification, negotiation and implementation of activities aimed at maximizing repayments by debtors or – where possible – implementation and monitoring of debtor corporate recovery proceedings leading to improvement of debtor financial and economic position, with the overall view to return debtors for servicing by their original sales units,
- active monitoring of execution and bankruptcy proceedings,
- disposal of part of non – performing loans,
- tax optimization of executed strategies,
- identification of early warning signals and taking appropriate actions (where possible, in collaboration with sales units) limiting the risk of potential losses,

- providing a support for business units in handling loans at risk,
- appropriate training for business units personnel and credit area personnel in order to increase efficiency in identifying warning signals, helping with proper granting of loans (particularly in the collateral establishment, which apart from the repayments are the main source of recovery),
- improvement of the Bank's organizational structure, procedures and tools to enhance the efficiency of the tasks carried out.

Debts recovered in 2013 in the amount of PLN 604 million (principal) were the result of the conducted debt enforcement proceedings, bankruptcy proceedings in progress, civil-legal agreements with debtors and composition proceedings in process.

The number of titles of execution issued by the Bank in 2013 amounted to 741 for corporate loans and, 3 969 for retail loans.

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

- institutional in PLN – 57.1%,
- institutional in foreign currencies – 86.4%,,
- retail in PLN – 79.4%,
- retail in foreign currencies – 114.5%.

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

8.2. FINANCIAL RISK

8.2.1. MARKET RISK

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

Market risk in the banking book

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

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

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

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

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

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

In the Money Market portfolio, according to its nature and purpose, equivalent measures to those used for the trading book are applied:

- VaR – Value-at-Risk – showing maximum acceptable level of loss on the given item in normal market conditions in a defined time period that can be exceeded with a defined probability; the Bank applies the parametric model with modified variance – covariance matrix and exponential weighting of historical observations; the accepted confidence level is 99%, and the period of position holding for the banking book is 1 month,
- Scenario analysis and stress tests – supplement VaR to include statistically unpredictable market events: historical economic and political crises, theoretical scenarios,
- BpV (basis point value) – price sensitivity to a parallel shift of the yield curve.

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

Situation in 2013

As at the end of December 2013, the value of the „duration" measure, i.e. the average weighted period to repricing of interest rate for assets remained at the level of 3.8 months (at the end of first half of 2013 - 2.9 months and at the end of 2012 – 2.8 months), whereas for liabilities – equaled to 3.3 months (at the end of first half of 2013 - 3.0 months and at the end of 2012 - 2.6 months). The duration of net capital decreased from 5.2 months at the end of 2012 to 1.4 months at the end of June, so as to increase than to 8.1 months at the end of 2013. The repricing period for almost 90% of assets and liabilities was lower than 6 months (at the end of 2012 - 93%), however almost 53% of assets and liabilities are to be re-valued within one month (at the end of 2012 - 59%)

In the second half of 2013, the interest rate risk (measured IaR) has increased, reaching the average level of PLN 37.4 million in a scenario of 200 bps increase in interest rates and PLN -39.3 million in a scenario of 200 bps decrease in interest rates, in comparison to PLN 12.8 million and PLN -12 million respectively in the first half of 2013. Decrease in interest income in both the first and second half-year would occur in case of decrease of interest rates scenario.

The biggest change of exposure concerned debt securities portfolio (increase in investment portfolio together with increase in equity) and deposit base (not renewed most expensive negotiable deposits, increasing volume of progressive deposits, stable level of BGŻOptima deposits) with gradually improving lending activities. At the same time shortening residual maturity of OIS transactions hedging interest rate risk in ALM portfolio and IRS transactions hedging preferential loans portfolio impacted the structure of repricing gap.

The sensitivity of net interest income (IaR) was as follows as at the end of 2013 (in brackets: values as at the end of the first half-year)

- an immediate increase in interest rates by 50 bps: increase in net interest income during one year by PLN 14.1 million (+ PLN 13.7 million),
- an immediate decrease in interest rates by 50 bps: decrease in net interest income during one year by PLN 15.6 million (- PLN 14.6 million),
- a gradual increase in interest rates by 200 bps during one year: increase in net interest income by PLN 35.8 million (+ PLN 27.6 million),
- a gradual decrease in interest rates by 200 bps during one year: decrease in net interest income by PLN 38.7 million (- PLN 29 million).

The exposure of Money Market portfolio was dominated by positions in 7-day NBP monetary bills (held for a short-term liquidity management purposes) and Interest Rate Swaps transactions (OIS and IRS – exposure adjusting, hedging the price risk) and FX Swap transaction (the financing of the Group in foreign currencies). In the second half of 2013 the average utilization of VaR limits remained at the level of 31% (60% in the first half of 2013). In terms of the currency structure, the exposures in PLN (over 45% of the sensitivity measured in BPV and over 70% in the second half of 2012) as well as EUR and USD had the biggest share.

Market risk in the trading book

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

The key measures for market risk used by the Bank in the trading book are:

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

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

Situation in 2013

Significant positions in the Polish Treasury bonds, particularly long-term, along with the relatively high volatility of major market risk factors have contributed to the high level of use of the VaR limit in the trading portfolio (on average in the second half of the year 66% compared to 75 % in the first half, average in second half of the year was influenced by low value at risk in December: 26%). At the end of 2013 exposure has been significantly reduced as a result of a significant reduction in the portfolio of IR Trading, which took place in December. The market risk of the trading book focused on portfolio interest rate risk (IR Trading) - mainly on interest rate swaps and debt instruments - with the average VaR in the first and second half of the year respectively PLN 1 003 thousand and PLN 886 thousand (with respect to the limit of 77 % and 68 %), while the currency risk (portfolio of FX Trading) remained at a low level, with the average VaR in the first and second half respectively PLN 41 thousand and PLN 52 thousand (with respect to the limit of 16 % and 21 %). In December 2013, the use of VaR limits in the portfolio IR Trading was the lowest. In the second half of 2013, there were no exceeded limits of VaR

In the first half of 2013 the trading portfolio was exposed to a scenario of falling interest rates, while in the second half it was the most exposed to the scenario "LTCM Collapse 1998", the second scenario in this respect was the scenario of parallel displacement curves PLN up, "PLN yield curve parallel shift up". Maximum utilization of the limit stress test was during this period 85%.

Liquidity risk and assessment of finance sources stability

Starting from January until November 2013, the Bank optimized the structure of funding. In this process, the Bank was not rolling most expensive deposits and replacing less stable volumes with volumes of higher stability. As a result, despite a reduction in liquidity buffer supervisory indicators were still at a safe level and stability of funding sources of the Bank rose at the end of 2013 to 89.4 % - mainly due to lower than previously fluctuations in the balances of retail deposits and BGŻOptima (increased stability to the level of 93.5%), extension of certificates of deposit and increase in the stability of the funds deposited by customers from segments of small and medium-sized and micro-enterprises (excluding migration between different products), settlements of large enterprises and public sector, and also due to CHF loan from Rabobank. Possessed financial resources allowed for timely payment of all liabilities of the Bank. The portfolio of the most liquid securities was maintained at a level fully securing potential outflow of the largest depositors. The surplus of liquid assets over the minimum required limit at the end of December 2013 amounted to PLN 796.2 million .

As at the end of 2013 the surplus funding sources outside the interbank market over the balance of loans amounted to PLN 2.96 billion, and surplus of stable deposits over the loan portfolio amounted to PLN 85 million.

8.3. OPERATING RISK

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

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

8.4. LEGAL RISK

The litigation situation in 2013 within insurance and employment claims was stable and did not generate material legal risk for the Bank. There were no court or administrative proceedings held by public administration bodies in relation to liabilities or receivables of the Bank, with the claim amount for at least 10% of the Bank’s equity as at 31 December 2013.

9. INFORMATION ABOUT THE AUDITOR

On 28 January 2013, the Supervisory Board appointed an entity authorized to audit of financial statements - KPMG Audit Sp. z o.o. Sp.k. ("KPMG") with its registered office in Warsaw at Chlodna 51 Street, entered on the list of entities authorized to audit financial statements under the number 3546, which is entrusted with the audit of the annual and semi-annual review of the financial statements of the Bank and the Bank’s Group for the years 2013-2015. The corresponding contract for the provision of audit services was concluded on 10 May 2013.

Selection of KPMG has been made in accordance with applicable regulations and professional standards. The company has also reviewed the interim financial statements of the Capital Group of the Bank in 2013.

Table 39. Auditor's remuneration divided by types of services (in thousand PLN).

PLN Thousand	Year ended 31 December 2013	Year ended 31 December 2012
	KPMG Audyt sp. z o.o. Sp.k.	Ernst & Young Audit Sp. z o.o.*
Mandatory audit /review of financial statements**	576	601
Other attestation services**	232	221
Tax advisory**	117	-
Other services**	214	101
Total	**1 139**	**923**

** previous auditor*
*** including VAT*

10. Salary of the Management Board and the Supervisory Board

Personal data on wages paid in a given year for individual members of the Management Board are as follows:

Table 40. Salaries paid to the members of the Management Board in 2013

Year 2013	Work period		Base Salary	Annual bonus	Other benefits	Total
Name and Surname	since	to				
Bartkiewicz Jacek	01.01.2013	31.03.2013	309	237	3 437	**3 983**
Wancer Józef	16.09.2013	31.12.2013	624	-	13	**637**
Beuming Johannes Gerardus	01.01.2013	31.12.2013	601	56	515	**1 172**
Embrechts Gerardus Cornelis	01.01.2013	31.12.2013	780	69	853	**1 702**
Legęć Magdalena	01.01.2013	31.12.2013	718	70	136	**924**
Nachyła Monika	01.04.2013	31.12.2013	990	-	106	**1 096**
Odzioba Dariusz	01.01.2013	31.12.2013	1 038	163	496	**1 697**
Okarma Witold	01.01.2013	31.12.2013	891	86	87	**1 064**
Sass Wojciech	01.01.2013	31.12.2013	1 315	186	97	**1 598**
Sieradz Andrzej	01.01.2013	31.12.2013	779	76	91	**946**
Total			**8 045**	**943**	**5 831**	**14 819**

Table 41. Salaries paid to the members of the Management Board in 2012

Year 2013	Work period		Base Salary	Annual bonus	Other benefits	Total
Name and Surname	since	to				
Bartkiewicz Jacek	01.01.2012	31.12.2012	1200	791	75	**2066**
Beuming Johannes Gerardus	01.01.2012	31.12.2012	562	125	434	**1121**
Embrechts Gerardus Cornelis	01.01.2012	31.12.2012	691	277	919	**1887**
Nijsen Hieronymus	01.01.2011	01.04.2011	-	121	15	**136**
Legęć Magdalena	01.01.2012	31.12.2012	697	79	154	**930**
Odzioba Dariusz	01.01.2012	31.12.2012	1008	298	470	**1776**
Okarma Witold	01.01.2012	31.12.2012	865	302	61	**1228**
Sass Wojciech	01.01.2012	31.12.2012	1265	538	71	**1874**
Sieradz Andrzej	01.01.2012	31.12.2012	754	346	64	**1164**
Total			**7 042**	**2877**	**2 263**	**12 182**

Provisions for bonuses of the Management Board members amounted to PLN 2 220 thousand in 2013 and PLN 5 521 thousand in 2012.

According to the individual contracts of employment members of the Management Board are entitled to life insurance and medical care package as well as compensatory bonus.

Additionally benefits available to members of the Management Board (on the basis of individual contracts of employment) include:

- Housing allowance specified in employment contract,
- Coverage or reimbursement of the expenses incurred due to delegation to work in Poland,
- Once a year private travel expense coverage for the delegated member of the Management Board and members of his or her family living in Poland,
- Coverage of the school expenses for the children of the members of the Management Board,
- One time addition to the salary due to change of work place.

Personal data on wages paid in a given year for individual members of the Supervisory Board are as follows:

Table 42. Salaries paid to the members of the Supervisory Board in 2013

Year 2013	Work period		Base salary
Name and Surname	Since	to	
Drok Evert Derks	01.01.2013	31.12.2013	93
Pruijs Jan Aleksander	01.01.2013	31.12.2013	139
De Roo Johannes Henricus	01.01.2013	28.06.2013	54
Filar Dariusz	01.01.2013	31.12.2013	116
Iwanicki Jarosław	01.01.2013	31.12.2013	93
Nachyła Monika	01.01.2013	01.03.2013	23
Tanja Cuppen	28.06.2013	31.12.2013	39
Warych Mariusz	28.06.2013	31.12.2013	39
Total			**596**

Table 43. Salaries paid to the members of the Supervisory Board in 2012

Year 2012	Work period		Base salary
Name and Surname	Since	to	
Adams Hendrik	01.01.2012	28.08.2012	66
De Roo Johannes Henricus	01.01.2012	31.12.2012	90
Dekker Roelof	01.01.2012	22.06.2012	51
Drok Evert Derks	25.06.2012	31.12.2012	40
Pruijs Jan Aleksander	01.01.2012	31.12.2012	136
Filar Dariusz	01.01.2012	31.12.2012	113
Iwanicki Jarosław	01.01.2012	31.12.2012	90
Maj Waldemar	01.01.2012	22.08.2012	65
Nachyła Monika	01.01.2012	31.12.2012	90
Zdebski Andrzej	01.01.2012	28.08.2012	66
Total			**807**

11. BASIC AVERAGE INTEREST RATES USED DURING THE YEAR

Table 44. Average interest rates in the Bank in 2013, based on compulsory reporting to the NBP Department of Statistics

Products	PLN	EUR	CHF
Deposits	**1.77%**	**0.10%**	
Households and non-profit institutions	**1.92%**	**0.10%**	
current	1.15%		
term	3.53%		
Enterprises	**1.27%**	**0.10%**	
current	0.45%		
term	2.62%		
Loans	**8.14%**	**1.44%**	**1.92%**
Households and non-profit institutions	**8.65%**	**2.28%**	**1.92%**
credit cards	19.64%		
consumer	15.55%		
mortgages	5.59%		
other purposes	5.93%		
Enterprises	**7.26%**	**1.38%**	
in current account	7.83%		
in credit account	6.85%		

12. REPORT APPLICATION OF CORPORATE GOVERNANCE STANDARDS IN 2013 BY BGŻ S.A.

Statement on application of Corporate Governance Standards

In accordance with § 91 section 5 paragraph 4 of the Regulation of the Minister of Finance of 19 February 2009 on current and periodic information published by issuers of securities and conditions for recognizing as equivalent information required by the law of non-member state (Journal of Laws 2009 No. 33, item. 259, with later amendment), the Management Board presents the following information on the application of the principles of corporate governance in 2013.

Corporate governance principles, which were subject to the Bank and places where principles are publicly available

Corporate governance principles, which were subject to the Bank in 2013 is contained in the "Code of Best Practice for WSE Listed Companies" being an annex to Resolution No. 19/1307/2012 of the WSE Supervisory Board dated 21 November 2012. The document is publicly available on the website at http://corp-gov.gpw.pl/publications.asp., which is the official website of the Warsaw Stock Exchange devoted to issues of corporate governance of listed companies.

Information concerning the provisions of the corporate governance principles, which the issuer has departed from and explanation of the reasons of non-compliance

The Bank has adopted the application of the principles of corporate governance resulting from the "Best Practices of WSE Listed Companies ("Best Practices") amended by update of these rules made by the WSE Supervisory Board’s Resolution No. 19/1307/2012 on 21 November 2012 concerning the adoption of changes in the "Best Practices of WSE Listed Companies". Best Practices in the above mentioned form have been adopted for use by the Management Board by Resolution No. 189/BZ/55/2012 adopted on 18 December 2012.The Bank has decided that:

1 / principle laid down in part. II, paragraph 9a of Best Practices on the conduct of the Company's corporate website and posting on it, in addition to the information required by law - records of the proceedings of the general meeting, in the form of audio or video, and

2 / the principle laid down in part. IV, paragraph 10 of Best Practices concerning the provision by the Company to participate in the General Meeting by means of electronic communication

- will not be applied by the Bank

Explanation:

- For point 1 above - currently only 1.74% of the Bank's shares are held by shareholders outside the Rabobank Group. Accordingly, the Bank does not expect registration of the general meeting in the form of audio or video, and publishing the proceedings of the Bank's website. Management believes that the publishing of current reports and information relating to the conduct of the General Meeting on the Bank's website ensures transparency and fully protects the rights of minority shareholders,

- For point 2 above - currently only 1.74% of the Bank’s shares are held by shareholders outside the Rabobank Group. In the opinion of the Management Board solutions in force at the Bank for shareholders’ participation in General Meetings allow adequate implementation of the rights arising from shares held and fully protect the interests of minority shareholders.

The Management Board declares that the Bank and its authorities complied with adopted by the Bank principles of corporate governance set out in the Code of Best Practice in 2012. In the period covered by this report there were no violations of the corporate governance rules adopted by the Bank.

The description of Key Features of the Bank’s internal control and risk management systems related to the preparation of financial statements and consolidated financial statements

The Bank has a system of internal control and internal audit tailored to the organizational structure, which includes the organizational units and the basic organizational units of the Bank and a subsidiary of the Bank.

The purpose of the internal control system of the Bank is to support decision-making processes to ensure:

- the effectiveness and efficiency of the Bank’s operations,
- reliability of financial reporting,
- the Bank's compliance with laws and internal regulations.

The Bank's internal control system includes:

- mechanics of risk control
- reviewing of the Bank’s compliance with internal law and regulations
- internal audit
- functional control

In the Bank there is functioning, organizational unit conducting internal audit, whose task is to examine and assess, in an independent and objective way, adequacy and effectiveness of internal controls and creating opinions of the Bank's management system, including the effectiveness of the risk management of the Bank's operations. Detailed rules for the internal control system are defined by internal regulations of the Bank. Director of Internal Audit Department reports directly to the President of the Management Board.

The Bank has adopted accounting policy, in accordance with the International Financial Reporting Standards. Preparation of financial statements, interim financial reporting as well as providing management information is the responsibility of the Finance and Reporting Division and Controlling Department, supervised by the First Vice-President of the Management Board.

Information on shareholders owning directly or indirectly a significant block of shares together with identification of number of shares owned by those shareholders, percentage of shareholders share in share capital, number and percentage of votes at the Bank's General Meeting resulting from owned shares

The main shareholders of the Bank are the following entities:

- Rabobank International Holding B.V. based in Utrecht, (Croeselaan 18, 3521 CB Utrecht, The Netherlands) [RIH], holding directly 45 941 751 shares of the Bank, which represents 89.84% of the share capital of the Bank. RIH is a holding company of Rabobank Group, which deal primarily with banking operations and the provision of banking services.

- Coöperatieve Centrale Raiffeisen-Boerenleenbank BA, with headquarter in Amsterdam and principal place of business in Utrecht (Croeselaan 18, 3521 CB Utrecht, The Netherlands) which holds directly 4 303 695 shares of the Bank, representing 8.42% of the share capital of the Bank.

Coöperatieve Centrale Raiffeisen-Boerenleenbank BA is the direct parent company of RIH and has a 100% interest in the RIH.

Detailed information on the shareholding structure of the Bank is located in Table 6 Shareholding structure of the BGZ S.A. in the section "Shareholder Structure".

Information on the holders of securities that confer special control rights with description of these rights

The Bank's shares are ordinary bearer shares and registered shares (as at 31 December 2013 - 8 022 915 were registered shares). Ordinary bearer shares do not have any special rights of control. However, registered shares of series B (as at 31 December 2013 - four shares) are preference shares with the right to obtain payment of the full nominal amount per share in the event of liquidation of the Bank after satisfying creditors, firstly before payments attributable to ordinary shares, which due to the implementation of the privilege may not cover the total nominal value of these shares.

Information on any restrictions of voting rights, such as restriction of voting rights of holders of given number or percentage of votes, temporary restrictions of voting or provisions according to which, with cooperation of a company, rights resulting from securities are separated from the fact of holding those securities

The Statute of the Bank does not establish any restrictions on voting rights and it does not contain any provisions under which financial rights attached to securities are separated from the ownership of securities. In accordance with § 10 section 4 of the Bank's Statute, each share gives right to one vote at the General Meeting.

Information on any restrictions of ownership transfer of securities issued by the Bank

The Bank's Statute does not introduce restrictions on the transfer of ownership of securities issued by the Bank.

Description of rules governing appointment and dismissal of members of managerial bodies and their rights, in particular right to decide whether to issue or repurchase shares

According to § 21 section 1 of the Bank's Statute, the Bank's Management Board consists of four to eight members, appointed for a joint term of office of three years.

The Board consists of the President, First Vice President, Vice Presidents and/or members of the Board who are appointed, dismissed and suspended from office by the Supervisory Board. At least two of the members of the Management Board, including the Chairman of the Board, should have knowledge and experience enabling sound and prudent management of the Bank. At least half of the members of the Management Board are people who are familiar with the Polish banking market, i.e. they are permanently domiciled in Poland, have command of Polish language and have relevant professional experience gained on the Polish market (§ 21 of the Bank' Statute).

The Management Board runs the business and represents the Bank. The Bank's Statute does not grant to the Bank's Management Board any special powers to issue or buy back shares. A detailed description of the operation, including rights of the Board, is included in § 22 paragraph 2 of the Statute of the Bank.

Description of rules for issuer's change of Statute

Any amendment to the Bank' Statute requires adoption by way of resolution of the Bank's General Shareholdera Meeting and registering the amendment in the National Court Register. To the extent specified in paragraph 34 section 2 of the Banking Act from 29 August 1997 (consolidated text. Journal of Laws of 2002 No. 72, item 665, as amended) amendment of the Statute requires approval of the Financial Supervisory Commission.

Conclusions of the Management Board on amendments to the Bank' Statute, as well as other cases brought by the Board for consideration by the General Meeting, shall be presented to the Supervisory Board for review.

The issues concerning, among others, amendments to the Statute, in particular with regard to the change of the Bank's firm, its registered office, business profile, referred to in § 5 paragraph 2 of the Bank's Statute, increase or reduction of the share capital of the Bank, the resolutions of the General Meeting shall be passed by a majority of three fourths of the votes. (§ 13 paragraph 2 of the Bank's Statute).

Referring to the provisions of § 20 paragraph 1 point ł of the Bank's Statute, immediately upon completion of the General Meeting enforcing amendments to the Bank's Statute, the Supervisory Board is responsible for determining the consolidated text of the Statute and introducing other amendments to the Statute of the nature specified in the resolution of the General Meeting.

Operations of the General Meeting and its basic rights and the rights of shareholders and the manner of their execution, in particular those arising from the regulations of the General Meeting, to the extent not resulting directly from the law

In accordance with the provisions of § 8 paragraph 6 of the Statute of the Bank, the General Assembly shall be called by the announcement made on the Bank's website and in the manner specified for providing current information, in accordance with the rules, about public offering and conditions governing introduction of financial instruments to organized trading and about public entities for at least 26 days before the General Meeting.

General Meetings are held at the headquarters of the Bank, which is located in Warsaw. The General Meeting shall be convened as ordinary and extraordinary. The General Meeting is convened by the Management Board. The Annual General Meeting is held once a year, not later than 6 months after the end of each fiscal year (§ 8 paragraph 2 of the Statute of the Bank).

The Extraordinary General Meeting shall be called as it is necessary by the Management Board on its own initiative or at the request of the Supervisory Board, or at the request of a shareholder or shareholders representing a total of at least 1/20 of the share capital (§ 8 paragraph 3 of the Statute of the Bank).

A shareholder or shareholders representing at least one twentieth of the share capital of the Bank may request the convening of an Extraordinary General Meeting, as well as the inclusion of certain issues on the agenda of the General Meeting. Shareholders representing at least half of the share capital of the Bank, or at least half of the total votes in the Board may convene an Extraordinary General Meeting. Shareholders appoint the chairman of the meeting (§ 8. 5 of the Statute of the Bank).

In accordance with § 9 of the Statute of the Bank, all matters submitted by the Board to the General Meeting shall be first submitted to the Supervisory Board for consideration.

A shareholder or shareholders representing in aggregate at least one twentieth of the share capital of the Bank may request that certain items on the agenda of the next General Meeting, should be submitted in writing or in electronic form to the Management Board, which in turn will present it with its opinion to the Supervisory Board. The application of the shareholder containing justification or a draft resolution concerning the proposed agenda shall be submitted to the Management Board no later than

21 days before the scheduled date of the General Meeting (§ 9 paragraph 1 second sentence of the Statute of the Bank).

Removal from the agenda or abandonment of review of an issue placed on agenda on shareholders' request requires the resolution of the General Meeting of the Bank and the consent of all shareholders of the Bank, who submitted a proposal to place a particular issue on the agenda of the General Meeting.

General Meeting of the Bank shall be valid regardless of the number of shares represented. In addition to the Commercial Companies Code issues related to the calling and functioning of the General Meeting are set out in the Bank's Statute, Regulations of the General Meeting and the notice convening the General Meeting.

On 21 July 2011, the Extraordinary General Meeting approved the new Regulations of the General Assembly, in accordance to which the General Meeting should be held in accordance with the provisions of the Commercial Code, the Banking Law, the Bank's Statute, the Rules, including the Code of Best Practice. In accordance with § 10 of the Rules of Procedure of the General Meeting, in the General Meeting participate members of Supervisory Board and Management Board in the composition that can give essential answers to the questions asked during the General Meeting. If the financial affairs shall be the subject of the General Meeting, general auditor should be present during the meeting. Regulations of the General Meeting shall include in particular provisions concerning elections, including elections to the Supervisory Board by voting in separate groups.

In accordance with the provisions of the Commercial Companies Code, the Banking Law and the Statute of the Bank the basic (core) competences of the General Meeting include:

- consideration and approval of the Management Board Report on the activities of the Bank and financial statements for the previous financial year,
- consideration and approval of the Management Board Report on the activities of the Group and consolidated financial statements of the Group for the previous financial year,
- adopting a resolution on profit distribution or coverage of loss,
- granting discharge to members of the Supervisory Board and Management Board in respect of their duties.

Apart from the above, the General Meetings may also adopt resolutions in regard of:

- change of the Banks Statute
- appointment and dismissal of the Supervisory Board's members
- increase/decrease of the Bank's share capital
- issuing of convertible bonds and bonds with pre-emptive right to acquire shares of the Bank, as well as warrants
- redemption of shares and determination of the specific conditions of such redemption,
- merger or liquidation of the Bank, the choice of liquidators and the conduct of the liquidation,
- determining the remuneration rules and remuneration for members of the Supervisory Board,
- submitted by the Supervisory Board or the Management Board,
- brought by shareholders in accordance with applicable regulations and Statute of the Bank,
- other restricted under the law and Statute of the Bank.

The personal composition and the changes that occurred during the last financial year, and a description of management, supervisory or administrative bodies of the issuer and its committees

Composition of the Management Board and the Supervisory Board is in Chapter 4 - The authorities of the parent company.

During 2013, the Supervisory Board supervised the activities of the Bank including: monitoring the implementation of the Bank's strategy, approving financial plans, policies and strategies of the Bank's audit plans, changes in the Management Board and plan of merger with Rabobank Poland S.A. The Board was acquainted with information on significant issues in the Bank's operations, including the implementation of the financial plan, the implementation of projects, risk occurring in the Bank, capital adequacy and rules for cooperation with the auditor of the Bank.

The work of the Supervisory Board was supported by two committees appointed from among the members of the Supervisory Board:

- Internal Audit Committee of the Bank,
- Commission for Human Resources and Remuneration Committee.

Internal Audit Committee of the Bank became acquainted with the results of both internal and external monitoring, information on the implementation of audit recommendations and the recommendations of the Financial Supervision Authority, the reports of the risks, compliance activity reports, information on the review of risks present in the Bank, documents concerning risk appetite, reports on the complaints lodged, reports on the activities of the restructuring and debt collection, reports on operational risk, the most significant correspondence with the Financial Supervision Authority.

Members of the Committee in 2013:

Tanja Cuppen – Chairwoman (appointed 5 September 2013)

Harry de Roo – Chairmen (the expiration of the mandate on 28 June 2013)

Dariusz Filar – Member (until 28 June in regard with expiring mandate, appointed for the next term of Office on 5 September 2013)

Monika Nachyła – Member (resigned 1 March 2013)

Evert Derks Drok – Members (until 28 June in regard with expiring mandate, appointed for the next term of Office on 5 September 2013).

The Commission on Human Resources and Remuneration discussed among others the List of leadership positions in BGZ S.A., under Resolution No. 258/2011 of the Financial Supervision Commission of 4 October 2011, proposals of objectives for the Management Board in 2013, Remuneration Policy of the Management Board and the Remuneration Policy of the Bank's employees. Also it became acquainted with information on employment and wages in 2012, and has analyzed the proposals for changes in the structure and amount of remuneration of the members of the Management Board - adapting to the requirements of the regulator and market practice, information on the implementation of EBA guidelines on the assessment of the qualifications of members of the management body, and persons holding key functions and information on the overall savings plan indicating the areas and relationship of employment’s reduction with the changes in the Bank in the areas of risk, back office and new systems.

13. DEVELOPMENT PERSPECTIVES FOR BGZ S.A

In line with its strategy, BGZ is a universal bank specializing in the agri-food sector. From the customer's perspective, BGZ wants to be a bank that builds solid relationships, perceived as a responsible partner and involved in local communities defined as centers with 20-150 thousand residents.

In universal banking the strategy provides for the strengthening of the Bank's position in retail banking by widening the product offer and to attract customers with a segment of the middle class (including through alternative distribution channels) to provide funding for core segments of its operations. The Bank is also focused on further growth in the business of operating small and medium-sized and micro-enterprises in local markets.

In the field of banking for the agri-food sector the Bank strengthens its leadership position based on the range of product offer and service model tailored to the needs of this market.

....	*................................*	*................................*
Józef Wancer	*Gerardus Cornelis Embrechts*	*Witold Okarma*
President	*First Vice-President*	*Vice-President*
....	*................................*	*................................*
Andrzej Sieradz	*Monika Nachyła*	*Johannes Gerardus Beuming*
Vice-President	*Vice-President*	*Vice-President*
....	*................................*	*................................*
Dariusz Odzioba	*Wojciech Sass*	*Magdalena Legęć*
Vice-President	*Vice-President*	*Vice-President*

Warsaw, 3 March 2014