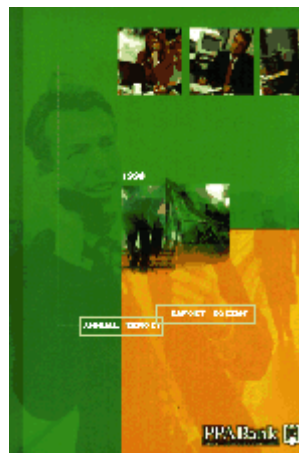


Annual Report 1998

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Letter from the Chairman

The year 1998 was another advantageous year for the First Polish-American Bank SA. The Bank earned net profit of PLN 18,6 million, which compared to 1997 constitutes an increase by 36%. Net interest income has been 23% higher than in the previous year, and there has also been a significant rise in the volume of loans and deposits, respectively, by 146% and 77%.

A steady growth tendency which has been manifest since the establishment of PPABank proves that our excellent performance indicators do not result from any ad hoc measures, but from our commitment to create conditions that favor long-term growth. Our efforts concentrate above all on the improvement of efficiency in all our units and on the maintenance of the highest professional standards of service. Such a policy will allow PPABank to steadily enhance its competitiveness, while keeping down its costs. The strategic decisions that underlie the Bank's development plans translate into a steadfast pursuit of our goals.

Whatever we do, we never lose sight of key strategic issues: Where are we heading? How can we capitalize on our strengths and minimize our weaknesses? How efficient are our operational procedures and our human resources? The PPABank strategy primarily focuses on the small and medium-size enterprise sector in Poland. However, in order to meet the exacting demands of the managers of our client firms and the expectations of independent professionals, in May 1998 PPABank also introduced a package of products tailored for individual customers who maintain their personal accounts with the Bank.



We are well aware that our customers expect the highest level of service. The popular stereotype equates quality with friendly customer service combined with high prices. It is often assumed that it is impossible to obtain a quality product at a reasonable price. The example of PPABank shows this stereotype to be mistaken. We may not be the least expensive bank but it is our firm policy to provide high value at a realistic price. Quality as we understand it means that customers should be furnished with what they need, at the right time and place, and in a problem-free way. Our efforts have been recognized by the "Businessman Magazine" monthly, which ranked us fourth in their "Bank for the Businessman" list in 1998. The verdict of the panel emphasized the adequacy of our offer to the expectations of our target customers.

In order to run a bank, its Directors and Board of Executives need to take into account at all times three main aspects of their institution's operation: financial, functional and personal. In the financial dimension, the bank needs sufficient resources to fulfill its statutory functions and meet the customers' demand in this respect. The PPABank total capital and own funds increased from PLN 91.8 million at the end of 1997 to PLN 131.6 million on December 31, 1998, which was possible thanks to expanding our activities, particularly in the loan market. The functional dimension is concerned with a precise allotment of responsibilities among particular units of the Bank. Efforts are being made to simplify and rationalize the organizational procedures. Finally, the personal dimension of bank management is seen by us as a key to economic success. PPABank attaches great importance to the recruitment of highly qualified and dedicated personnel, and to the constant development of their skills, both through everyday practice, and in the course of various training programs and seminars.

We are convinced that the coordination of these three dimensions will have a synergistic effect that will prove beneficial to the joint interests of the Bank and its customers, as we continue to expand and grow to better serve our clients.

Bank's Authorities

Following the registration of share capital increase and the acquisition of 9.72% of shares by Generale Bank, the Resolution of the Extraordinary Shareholders' Meeting dated December 10, 1997 became effective and Mr. Luc Delvaux joined the Board of Executives on June 4, 1998.

The Board of Directors appointed Mr. Jean-Luc Deguel to the Board of Executives, effective on June 1, 1998.

As of December 31, 1998 the Board of Directors consisted of 8 members and the Board of Executives - of 5.

At the end of 1998 the Bank's authorities comprised:

The Board of Directors

- Joseph S. Conti - Chairman
- Arkadiusz Krezel - Vice-Chairman
- Antoni Potocki - Vice-Chairman
- Luc Delvaux
- Zbigniew Dresler
- Stephen Seamans
- Dariusz Pronczuk
- Juliusz Sikora

The Board of Executives

- Marek Kulczycki - President
- Benjamin H. Turnbull* - First Vice-President
- Thomas C. Cianfrani - Vice-President
- Jean-Luc Deguel - Vice-President
- Leszek Niemycki - Vice-President

Until May 31, 1998 a Vice-President post was also held by Mr Jerzy Markiewicz.

*Mr Benjamin H. Turnbull held the post of First Vice-President until February 28, 1999.

**Marek
Kulczycki**



President

**Leszek
Niemycki**
Vice-
President



**Benjamin
H. Turnbull**
First Vice-
President



**Jean-Luc
Deguel**
Vice-
President



**Thomas C.
Cianfrani**
Vice-
President



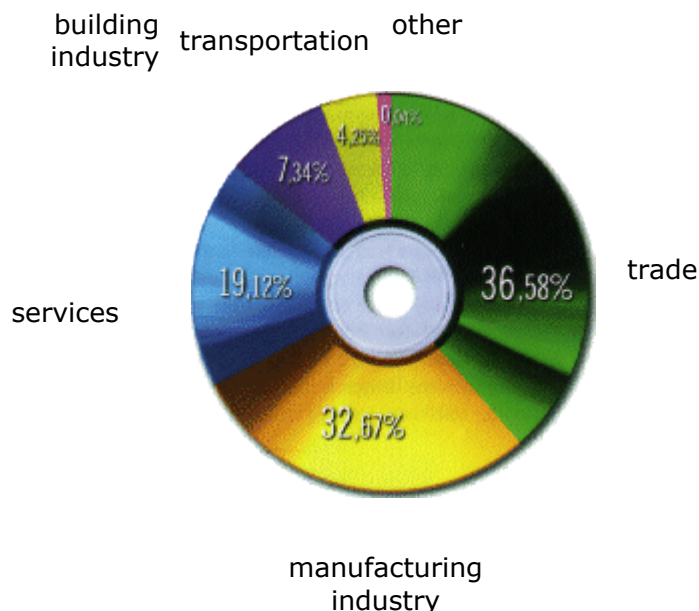
Area of Specialization

PPABank focuses on the sector of small and medium size private enterprises (SME's). This is the fastest growing economic sector and there has been a constant increasing demand for our products and services on the part of SME's. Loans for companies have traditionally met with great customers' interest. PPABank does not offer preferences for any particular branch of the economy, but analyses indicate that the greatest loan concentration occurs in the spheres of trade (37% of the total portfolio), manufacturing (33%) and services (19%). Our loan operations are conducted through the network of representative offices, which monitor the financial standing of the borrowers. The Bank aims to offer comprehensive services for enterprises, which reflects the expectations of demanding customers. We are also aware of the increasing level of expectations concerning the standards of service and our commitment to excellence is part of the PPABank overall strategy. The Bank emphasizes both the need of innovative and user-friendly quality products, and the importance of good customer service (including procedures, personnel competence and communications).

In line with the PPABank mission, the Small and Medium Size Customers Market Group was established in 1998 within the Business Development Department. The principal tasks of this Group include collaboration with other organizational units of the Bank in the development of new products for corporate customers, and establishing procedures that will result in a further improvement in the quality of customer service. Importantly, the Group is also involved in the formulation of marketing plans for the institutional client sector, based on the analysis of their needs and an evaluation of the products offered by other banks on the Polish market.

In response to the current needs, the PPABank Board of Executives established in March 1998 the Customer Product Support Department. The main responsibilities of this new Department include cooperation with the European Desk- formed in 1998 to introduce the Bank to the customers of Generale Bank, and facilitating contacts of customers with the back office of the Bank. The plan for 1999 provides for expanding the Customer Product Support Department into a unit responsible for contacts with all PPABank customers. It is hoped that these measures will contribute to the constant improvement of the quality of services offered by PPABank.

Concentration of loans by sector as of December 31, 1998



Modern Technology

PPABank relies on professionally developed, highly specialized software in most aspects of its operating activities: from daily operations at the branch offices to the workings of the Head Office to the management of large and ever changing databases. Special systems are used for electronic money transfer settlements - domestic (ELIXIR, Cash Management) and foreign (SWIFT, Cash Management).

Comprehensive computerization of PPABank began in 1994 with the implementation of EQUATION - an on-line banking system with a single general ledger processing. It allows transactions performed at any operating unit of the Bank to be applied in real time to the customer's account and general ledger. Thus all settlements between PPABank customers, front and back office and branches take place in real time.

The Bank's corporate on-line network relies on the POLPAK-T system, which integrates a number of local networks from all parts of Poland. The Bank also maintains an emergency telecommunications system based on ISDN backup links. The POLPAK-T network is a modern type of service offered by Telekomunikacja Polska S.A., which combines fast data transmission with the high levels of stability and reliability required by the growing volume of transactions and the Bank's territorial expansion. Owing to the constant development and modernization of its telecommunications and computer system, PPABank remains one of the more state-of-the-art financial institutions in Poland. In order to ensure maximum security of operations, the Bank has established a backup data-processing center which allows all the branches to keep working even in the unlikely event of a total breakdown of the central processing site.

In 1995, PPABank was among the first users of the electronic interbank settlement system ELIXIR, which makes it possible to send and receive domestic transfers in the on-line mode. The Bank recommends the use of the ELIXIR system for incoming and outgoing payments in all those cases when the funds need not be accompanied by paper documents. Foreign transfers are handled in an equally efficient and reliable way, thanks to the participation of PPABank in the international electronic settlement system SWIFT since 1995.

One of the most advanced electronic services offered by PPABank is Cash Management, an electronic banking service, which allows customers to effect banking operations directly from their office premises. Using a computer and modem, they can receive statements and transmit domestic or foreign payment orders. The system also provides customers with constantly updated information about operations in their accounts and about exchange rates. Cash Management, intended mostly for corporate customers, has been part of the Bank's offer since November 1995. It is an off-line system, which means that it is only necessary to log into the Bank's server for the actual transmission of data. Neither the preparation of payment orders, nor browsing through statements received from the Bank requires an active connection. The Cash Management system is now used by several hundred of PPABank customers. The product is well received by the Bank's customers and the number of new potential users interested in this service is rapidly growing.

The PPABank computer network is considered to be one of the best integrated in Poland. This fact has won recognition among experts in the field. In particular, the Bank was short-listed for the title of "Information Technology Leader '97", awarded by the "Computerworld" weekly, in the category of financial and banking institutions.

PPABank was likewise one of the first banking institutions on the Polish market to take notice of the potential offered by the Internet. Since March 1996 the Bank has maintained its Web page, presenting information about its history, products, branches, technological solutions used, as well as financial reports. The PPABank site can be visited at <http://www.ppabank.com.pl/>.

In order to meet the expectations of its customers, the Bank intends to expand the scope of Internet-based services in the summer of 1999, so as to provide customers with a safe and convenient way to access their accounts and implement financial transactions.

One of the strategic information-technology projects pursued by PPABank is Program 2000, launched towards the end of 1997 in order to address the Year 2000 problem in the computer systems.

The Year 2000 issues received the attention of executive management of our Bank and all the necessary steps have been taken to ensure that we will have a solution in place. The required corrective measures are well advanced in respect of suppliers of computer hardware and software and our own developments. PPABank intends to have its technology systems and processes in place by March 31, 1999. The remainder of 1999 is reserved for national banking tests as well as final internal tests with clients, domestic and international service or information providers.

In accordance with the recommendation of the National Bank of Poland, National Banking Supervision Board, PPABank will reach full year-2000 conformity by June 30, 1999.

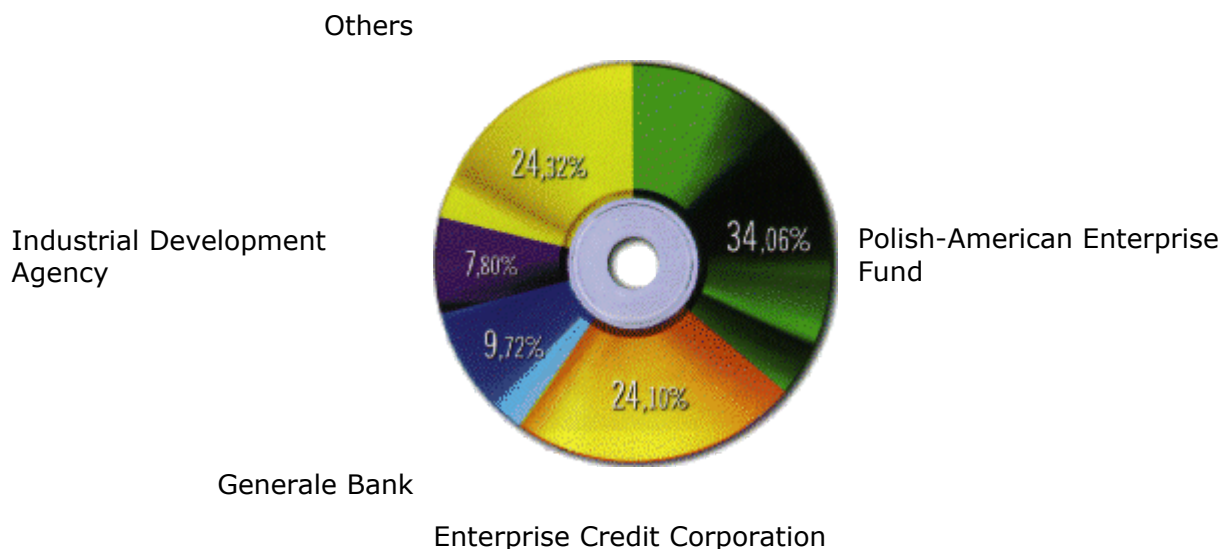
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Shareholders

PPABank is a mixed-capital company with the majority of shares held by renowned financial institutions, such as the Polish-American Enterprise Fund, the Enterprise Credit Corporation, Generale Bank and the Industrial Development Agency. PPABank stock was first quoted on the Warsaw Stock Exchange in November 1994. Following the registration of the fifth issue of shares (series F and G) on June 4, 1998, the Bank's share capital increased by PLN 2,730,000 to PLN 15,230,000 divided into 7,615,000 shares.

Ownership structure

(as of March 31, 1999)



The Polish-American Enterprise Fund (PAEF) was established by the U.S. Congress in 1989. Its objective is to support the market-oriented transformation of the Polish economy. The fund received an initial capital of USD 240 million.

The PAEF organized and financed a major loan program addressed to small and medium-size private enterprises. The Enterprise Credit Corporation, established by PAEF in 1990, initiated the Small Business Loan Program and since 1995 the program has been administered by PPABank. From its inception loans have been granted to more than 7 thousand firms in an aggregate amount of USD 272 million. The loan program is now being continued by PPABank (of which PAEF is a strategic investor), utilizing both PAEF funds and own funds of the Bank.

In order to meet the needs of small firms, whose access to bank credit is restricted in view of their low capital and turnover, the PAEF established Fundusz Mikro in 1994. Fundusz Mikro has already granted nearly 20 thousand loans in an aggregate amount of USD 30 million. In 1997, Fundusz Mikro implemented a special loan program for firms which had sustained losses as a result of the disastrous flood. Thus almost 2 thousand firms were granted loans on preferential terms. Loan operations conducted by Fundusz Mikro are an important supplement to the loan program implemented jointly by the Enterprise Credit Corporation and PPABank.

Recognizing the need for growth in the housing construction sector in Poland, PAEF joined forces with its Polish partners to establish the Polish-American Mortgage Bank - the first Polish bank to specialize in mortgage loans. The Bank has already granted loans to several thousand families from Poland's newly emerging middle class to finance the improvement of their housing standards. In 1998, the PAEF sold its shares in this Bank to the General Electric Capital Corporation. Together with developers, the PAEF established the Housing Development Corporation, and - acting jointly with the Canadian investor Cadim - a Polish Real-Estate Fund. Both of these institutions have already financed the construction of more than a dozen housing developments in Warsaw, Zakopane, Białystok and other places. The Polish-American Enterprise Fund was also one of the founders of the Agro-Industrial Bank, now renamed Rabobank Polska).

The Fund has started more than 50 joint ventures with Polish partners. Its current and former partners include such major enterprises as: ComputerLand (computer systems), W. Kruk (jewelry), Lukas (consumer finance plans), Bauma (construction materials) and others. The PAEF has participated in large-scale investment projects in Poland in cooperation with corporations of a worldwide scope. These included the construction of a printing house in Kraków (together with RR Donnelley) or the privatization of the Glassworks in Jarosław (together with Owens Illinois).

The Fund has been an active participant in the privatization of 15 major state-owned enterprises, including: Energoaparatura Katowice, Hydrotrest Kraków, Stomil Sanok, Polfa Kutno, Zakłady Metali Lekkich (ZML) Kęty, Polar Wrocław and Elektrobudowa Katowice. In all the above-mentioned cases the management of the privatized companies was left in the hands of Polish managers.

The operation of the Fund has stimulated the development of the capital market in Poland. The Fund has been involved in the introduction of the stock of several companies into public trading. The companies in question included, among others: PPABank (1994), Polfa Kutno (1995), ComputerLand (1995), Zakłady Metali Lekkich Kęty (1996), Elektrobudowa (1996), Stomil Sanok (1997), Energoaparatura (1997) and Polar Wrocław (1997).

Currently, the PAEF owns stock in companies which altogether employ over 20 thousand people and their annual revenues exceed USD 1.2 billion.

The Fund promotes economic education. Subsidies for the training of business school students are awarded through the Educational Enterprise Foundation, established jointly with the Polish Government in 1991. More than 15 thousand students have received scholarships so far, and the Foundation has subsidized the publication of 82 books in the field of economy.

Thanks to the activities of the Polish-American Enterprise Fund, whose initial capital was USD 240 million, an additional USD 264 million has been invested in Poland by private investors. It was upon the Fund's initiative that the Polish Private Equity Funds I and II were established in 1992 and the Polish Enterprise Fund in 1997. The capital for those new funds was provided by the European Bank for Reconstruction and Development, as well as by renowned private institutional financial investors from the U.S., Canada and Europe, including pension funds of large American corporations. The investments of the funds are managed by Enterprise Investors.

Generale Bank, a member of the Fortis Group is a bank whose tradition goes back to 1822, when William I of Orange set up the General Company of the Netherlands for National Industry (Algemeene Nederlandsche Maatschappij ter begunstiging van de volksvljijt). This company gave rise to the world's first investment bank, Société Générale - later to become Generale Bank - which was closely involved in Belgium's industrial development and, at a later stage, in its international expansion.

Generale Bank is also a bank of the future that has managed to keep pace with change and adapt to deregulation. Economic development, the increasingly global nature of markets and technological progress have radically changed the face of finance and economics. Yet Generale Bank has been able to maintain its position and continues to adapt to constant change.

Since June 1998, Generale Bank and Fortis Group, an international group operating in the fields of insurance, banking and investments, have joined forces. The new group has a combined market capitalization of some EUR 30 billion, making it the leading financial

institution in Belgium, the second largest in the Benelux region, and the tenth-largest in Europe. Total assets are EUR 335 billion and own funds stand at EUR 13.75 billion. The group has 62 thousand employees world wide.

The integration of the banking business within the Fortis Group commenced in the beginning of 1999 and is expected to take four or five years. It will be centered around Generale Bank and organized according to lines of business. The combined banking group will be a major player in the financial services industry offering flexible and tailor-made solutions to its customers. The group also wants to be recognized as a solid financial institution.

The new entity is first and foremost active in the Benelux, its home market in the heart of Europe. In this region it offers an extensive range of financial products and services for all the customer segments through various distribution channels. Elsewhere in Europe, the group aims to be a leading provider of financial services, including investment banking. In the rest of the world, the Fortis Group will be present in those countries where its customers need it, especially as a financial services provider in the triangle Taiwan, Hong Kong and mainland China, and as a niche player in other parts of the world. Finally, the banking group is a world wide provider of private banking, asset management and financial markets as well as a niche player in certain specialist services to corporate and institutional clients, banks and intermediaries in the financial market.

On February 23, 1999, Generale Bank, the Polish-American Enterprise Fund and the Enterprise Credit Corporation signed an agreement under which Generale Bank undertakes to acquire all the shares in PPABank held by PAEF and ECC (amounting to 58.8% of the total stock). When this transaction is completed, Generale Bank will hold 68.5% of PPABank stock. It is subject to the approval of the National Bank of Poland, the Polish Securities and Exchange Commission and the Anti-Monopoly Office.

Industrial Development Agency was founded on January 25, 1991 as a company wholly owned by the State Treasury. The objective of the Agency is to actively participate in the transformation of economic entities under the conditions of market economy. With respect to various industrial entities, the Agency plays the role of a restructuring agent, creditor, strategic investor, institutional leader, and organizer and manager of special economic zones.

The principal tasks pursued by the Agency include:

- financial restructuring of enterprises
- technical assistance in restructuring
- granting of loans
- acting as a capital investor
- management of special economic zones
- management of property renounced in the course of restructuring.

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Highlights of 1998

- **2 January** - introduction of currency forward contracts, an operating product, which protects customers who make settlements in foreign currencies against the future exchange risk.
- **26 January** - introduction of PPABoom - a 3-month PLN-deposit, available for individual and corporate customers who wish to invest a minimum of PLN 10 000
- **20 April** - introduction of fixed-rate term deposits
- **12 May** - introduction of the PPABank Silver and Gold Packages for individual customers
- **15 May** - introduction of VISA Classic and VISA Gold charge cards
- **5 June** - opening of the Branch Office in Gdynia
- **22 June** - introduction of the "Bankophone" automated telephone service
- **13 October** - announcement by PPABank that Generale Bank, Brussels, which controls 9.72% of votes at the General Shareholders' Meeting, has commenced talks with other principal PPABank shareholders concerning the increase of its capital involvement in PPABank through the acquisition of shares

- **28 October** - conclusion of an agreement with Bank Pekao SA providing for a loan of DEM 12 million to be granted to PPABank for one year in order to expand currency-loan operations under the Small Business Loan Program
- **October** - publication of the "Bank for the Businessman" list of Businessman Magazine, in which PPABank ranks fourth
- **3 November** - opening of the Branch Office in Lodz
- **3 November** - acquisition of a substantial package of PPABank shares by the Polish-American Enterprise Fund, together with its wholly-owned subsidiary, the Enterprise Credit Corporation; the increased holdings of PPABank stock by these two entities gives them 58.16% of voting rights at the General Shareholders' Meeting (of which PAEF controls 34.06% and ECC 24.10%)
- **9 November** - extension of the scope of the "Bankophone" automated telephone service which allows users to make payment orders and start term deposits
- **10 December** - approval of the draft financial plan for 1999 by the PPABank Board of Directors. The projected net profit in 1999 is PLN 28.7 million, 59% up in comparison with the plan for 1998.
- **21 December** - opening of the Branch Office in Wroclaw
- **23 December** - Signing of an amendment to the agreement of 24 September 1998 concluded with Generale Bank SA and Generale Bank Nederland NV. Under the new terms of the agreement, the limit of the credit line granted to PPABank by Generale Bank for a period of seven years is raised from DEM 15 million to 40 million. The purpose of the line is the financing of investment and working-capital loans granted by PPABank to customers recommended by GB or GB Bank Nederland NV, who do business in Poland.

Plans for 1999

The long-term development strategy worked out by the PPABank Board of Executives has been approved by the Board of Directors. In particular, the Directors have authorized the opening of branch offices in Gliwice, Szczecin and Bydgoszcz, as well as new branches or sub-branches in Warsaw and Kraków, scheduled for 1999. The plans of the Board of Executives for 1999 also include the opening of an agency in Kielce and representative offices in Bydgoszcz and Bielsko-Biala.

PPABank continually invests in the development of its information-technology infrastructure and the automation of transaction processing. Such a policy minimizes the time needed to establish new branches and make them fully operational.

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Financial Analysis

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- [Profit and Loss Statement](#)
- [Key Financial Indicators](#)

Balance Sheet

PPABank total assets as of December 31, 1998 stood at PLN 1,140,068 thousand, which represents an increase of PLN 499,086 thousand (or 78%) over 1997.

the structure and dynamics of selected balance-sheet items (PLN 000's)

balance-sheet item	1997	proportion in total assets/liabilities	1998	proportion in total assets/liabilities	1997-1998 change
Cash and Central Bank balances	80,033	12.5%	104,001	9.1%	29.9%
Due from financial institutions	91,443	14.3%	86,985	7.6%	(4.9)%
Due from customers and budget sector	311,201	48.6%	766,544	67.2%	146.3%
Due to financial institutions	109,198	17.0%	280,402	24.6%	156.8%
Due to other customers and budget sector	383,788	59.9%	680,356	59.7%	77.2%
Own funds (including net profit)	91,840	14.3%	131,632	11.5%	43.3%
Share capital	12,500	2.0%	15,230	1.3%	21.8%
Total assets	640,982		1,140,068		77.9%

Assets

Asset structure at PPABank underwent some changes in 1998, connected, in particular with credit portfolio growing faster than total assets, and the decreased proportion of securities, cash and current-account balance with the National Bank of Poland (NBP) in total assets.

The principal item in the Bank's assets were loans, which accounted for 67% of total assets at the end of 1998, as compared with 49% at the end of 1997. Net loan portfolio (adjusted for non-performing loans reserve) rose by PLN 455,344 thousand (146%) over the previous year and reached PLN 766,544 thousand. Provisions for non-performing loans were established in the amount of PLN 6,567 thousand. The proportion of non-performing loans in the total portfolio was very low and stood at approximately 2%.

The balance sheet proportion of securities in total assets decreased in 1998. On December 31, 1998, the PPABank security holdings amounted to PLN 108,086 thousand, and their proportion

in total assets was down to 9.5% from 18.9% at the end of 1997. Two main reasons account for this tendency i.e.:

- declining returns on treasury bills and government bonds
- expansion of loan operations.

At the end of 1998, the PPABank security portfolio consisted solely of securities issued by the state, which for all practical purposes can be seen as risk-free. The composition of the portfolio was as follows:

- treasury bills issued by the Ministry of Finance: PLN 85,320 thousand
- State Treasury bonds: PLN 22,766 thousand.

As of the end of 1998, the proportion of cash and central bank balances in total assets had declined, too: from 12.5% in 1997 to 9.1% on December 31, 1998. This was a consequence of two factors:

- beginning from 1998, banks have been allowed to maintain only 10% of NBP mandatory reserves in cash; accordingly, PPABank has adopted measures to reduce its cash holdings
- the remaining part of the mandatory reserve is held in a reserve account with the National Bank of Poland. Since banks are required by law to maintain an appropriate average monthly balance of that account, the actual balance by the end of the reporting period depends upon the Bank's policy and its predictions concerning interest rates.

Amounts due from other financial institutions (placements with other banks) accounted for 7.6% of total assets at the end of 1998, down from 14.3% in the previous year. The structure of this item at the end of 1998 was as follows:

- PLN-denominated deposits: PLN 55,359 thousand,
- foreign currency deposits: PLN 23,488 thousand,
- nostro accounts: PLN 8,138 thousand.

In 1998, the value of fixed assets increased by nearly PLN 7 million. This was connected with the opening of new branches, major investments in the telecommunications and computer network, and measures necessary to ensure Year-2000 conformity of the computer system. The principal components of fixed assets include:

- computer equipment: PLN 6,478 thousand,
- leasehold improvements: PLN 10,220 thousand.

The value of intangible assets at the end of 1998 amounted to PLN 9,434, including:

- software: PLN 6,696 thousand,
- share-issue expenses: PLN 2,738 thousand.

Other assets accounted for 2.5% of the total. This item consists mainly of interbank settlements in the amount of PLN 21,976 thousand.

Liabilities

The principal item on the liabilities side comprises amounts due to customers (current accounts and term deposits). Customer deposits at the end of 1998 reached PLN 680,356 thousand, which represented 60% of total liabilities. Deposits in PLN, in an aggregate amount of PLN 541,507 thousand (91% up from 1997), clearly predominate. Foreign currency deposits reached PLN 138,849 thousand at the end of 1998 and were 38% higher than a year before.

In 1998, the proportion of amounts due to other financial institutions in the overall structure of liabilities increased significantly. On December 31, 1998, this item accounted for 25% of total liabilities, compared with 17% the year before. This increase is due to two main factors:

- a DEM 40-million loan from Generale Bank, Rotterdam,
- an increased balance of placements from other banks.

Special funds and other liabilities accounted for 2% of total liabilities at the end of 1998. The principal item in this group comprises interbank settlements: PLN 19,251 thousand.

The reserves shown in the balance consist of two items:

- reserve for deferred tax: PLN 5,154 thousand
- general risk reserve established in accordance with Art. 130 of the Banking Law Act: PLN 3,581 thousand. This provision covers the risks inherent in banking operations. The regulations that allow the establishment of reserves of this type came into force on January 1, 1998. Accordingly, this is a new item on the PPABank balance sheet.

Own Funds

PPABank primary own funds increased from PLN 91,840 thousand at the end of 1997 to PLN 131,632 thousand as of December 31, 1998.

In 1998, the Bank's share capital grew by PLN 2,730 thousand, following the issue of 1,365 thousand series F and G shares, successfully completed in June 1998.

The Bank's supplementary capital was expanded by PLN 18,550 thousand and reached PLN 66,477 thousand by the end of 1998. This increase was made possible mainly by the sales of series F and G shares at a substantial premium.

In accordance with the provisions of Art. 174 of the Banking Law Act, PPABank transferred funds from the hitherto general risk fund to reserve capital. As a result, the amount of reserve capital increased by PLN 8,240 thousand and reached PLN 17,018 thousand.

The PPABank General Shareholders' Meeting held on June 25, 1998 resolved to allocate the entire net profit for 1997 in the amount of PLN 13,713 thousand to the general risk fund.

In accordance with the provisions of Art. 127 of the Banking Law Act, items that may be classified as the Bank's own funds also include the fixed-asset revaluation fund and subordinated debt. The fixed-asset revaluation fund at the end of 1998 amounted to PLN 551 thousand. Subordinated debt included part of the loan obtained from the Polish-American Enterprise Fund. The inclusion of this item in subordinated debt was authorized by the President of the National Bank of Poland. As of December 31, 1998, subordinated debt stood at PLN 5,618 thousand. Structure of own funds at the end of 1998 is presented in the table below:

the structure of own funds as of the end of 1998 (PLN 000's)

	1997 PLN 000's	1998 PLN 000's
share capital	12,500	15,230
additional capital	47,927	66,477
reserve capital	17,118	17,018
general risk fund	0	13,713
fixed-asset revaluation fund	582	551
subordinated debt	9,363	5,618
total own funds	87,490	118,607

Off-balance Sheet Items

Off-balance sheet items at the end of 1998 totaled PLN 626,865 thousand, which translates into an 88-percent increase over the previous year. These items include:

off-balance sheet items granted:

- guarantees: PLN 193,246 thousand
- credit lines: PLN 171,023 thousand
- opened or confirmed documentary credits: PLN 15,876 thousand

off-balance sheet items received:

- credit lines :PLN 62 702 thousand

- guarantees: PLN 1 322 thousand
- interbank transactions concluded before the end of the year with maturities after December 31, 1998: PLN 174,697 thousand.
- securities operations: PLN 8 000 thousand

The increase in the aggregate guarantee amount is related, for the most part, to guarantees issued in favor of the ECC as collateral for loans granted under the Small Business Loan Program. As regards credit lines, the growth of their total amount is linked to the expansion of loan operations, as indicated in the section on assets.

[financial analysis](#)

Profit and Loss Statement

Profit on Banking Activities

PPABank total revenues in 1998 stood at PLN 174,144 thousand, a 61-percent growth over the previous year. Of these, interest revenues in the amount of PLN 131,361 thousand (53% more than in 1997) remained the principal component. Interest revenues consisted of the following items:

- interest on loans: PLN 94,047 thousand
- interest on interbank placements: PLN 13,987 thousand
- interest on securities: PLN 20,747 thousand
- interest on assets leased to customers: PLN 2,580 thousand.

Considerable dynamics of interest revenues is primarily due to the growth of the loan portfolio. The fact that the rate of interest revenue growth did not match the dynamics of loan operations is a consequence of the declining interest rates on loans in the course of the year. The rates were influenced by the decisions of the Monetary Policy Council, which gradually lowered the key rates. For instance, the Lombard rate of the National Bank of Poland (applied to loans granted to banks by the central bank against security in the form of financial instruments) dropped from 27% at the beginning of 1998 to 20% in December.

PPABank recorded a considerable increase of fee and commission revenues, which reached PLN 27,860 thousand in 1998 and were 68% higher than in the preceding year.

In 1998, net income on foreign currency transactions nearly trebled in comparison with 1997, coming to PLN 14,923 thousand, which accounted for 8.6% of total revenues. Such a good result was achieved owing to:

- an increased number and volume of foreign-trade transactions conducted by PPABank customers
- competent handling of currency-market operations at the time of increased volatility during the Russian crisis
- growth of the foreign-currency loan portfolio.

Costs of Banking Activities

Interest expense during the period in question reached PLN 79,114 thousand and was 82% higher than in 1997. This amount breaks down into the following categories:

- interest on customer deposits: PLN 71,697 thousand
- interest on interbank deposits: PLN 5,000 thousand
- interest on credits and loans: PLN 2,412 thousand.

The increase of interest on customer deposits resulted from the following factors:

- a 77-percent increase of the balance due to customers
- a shrinking interest margin
- changed regulations concerning the mandatory reserves transferred to the National Bank of Poland.

Commission and fee expense increased only slightly in 1998 and accounted for a mere 1,7% of total expenditure.

Other Revenues and Expenditures

The remaining operating revenues include:

- operating leasing: PLN 2,795 thousand
- cash collection services: PLN 1,068 thousand
- others: PLN 1,631 thousand.

The remaining operating expenses include:

- cost of sales and liquidation of fixed assets: PLN 1,484 thousand
- others: PLN 1,645 thousand.

The Bank's operating expenses in 1998 reached PLN 52,889 thousand and rose by 43% in comparison with 1997. The increased costs were brought about by the following factors:

- expansion of the branch network and resulting increased payroll and rent expenses
- growing number of customers and operations, leading to higher administrative costs.

It is worth noting that the growth dynamics of operating costs (43%) was considerably lower than the rate of growth of net income on banking activities (47%).

The depreciation of fixed and intangible assets in 1998 amounted to PLN 9,672 thousand and was 19% higher than in the previous year.

In 1998, the establishment of provisions generated a cost of PLN 8,600 thousand, while revenues from released provisions stood at PLN 2,763 thousand, leaving a negative balance of provisions in the amount of PLN 5,837 thousand. The item of decisive importance in this area was the establishment general risk reserve, which at the end of the year reached the level of PLN 3,581 thousand. The Bank authorities decided to create this reserve in order to provide for the safety of the Bank's activities in the future. The balance of the establishment and release of loan-loss provisions was PLN (2 300) thousand.

Profit

In 1998, PPABank generated a pre-tax profit of PLN 27,383 thousand. The Bank's tax liability amounted to PLN 8,741 thousand, which translates into an effective tax rate of 32% - 7 percentage points less than in 1997.

The Bank's tax burden in 1998 was determined by:

- tax paid: PLN 8,076 thousand
- release of the deferred tax reserve: PLN 665 thousand

The lower effective tax rate was mainly the consequence of:

- a lower tax base thanks to an "investment bonus" (tax relief connected with previous year's investments)
- the lowering of the nominal corporate income tax rate from 38% in 1997 to 36% in 1998.

At PLN 18,642 thousand, PPABank's net profit in 1998 (after tax) was 36% higher than in 1997.

growth dynamics of selected items of profit and loss statement (PLN 000's)

	1997	1998	1997-1998 dynamics
net interest income	42,519	52,247	23%
net fee and commission income	15,263	26,456	73%
net income on foreign currency transactions	5,249	14,923	184%
net income on banking activities	63,362	93,416	47%
net operating income	22,553	27,383	21%
gross profit	22,553	27,383	21%

income tax	(8,839)	(8,741)	(1)%
net profit	13,713	18,642	36%

[financial analysis](#)

Financial Indicators

Capital Adequacy Ratio

This indicator represents the ratio of the Bank's own funds to risk-adjusted assets and off-balance sheet items. The weights to be used for the adjustment process are set by the Banking Supervision Board. PPABank own capitals increased by 36% in the course of the year, while assets and off-balance sheet items soared by 91%. The extremely rapid growth of total assets which was not fully matched by the increase of capitals resulted in a lower capital adequacy ratio.

capital adequacy ratio and its determinants

	31.12.1997	31.12.1998
Risk-adjusted assets	348,440	787,146
Risk-adjusted off-balance sheet items	145,657	363,177
Own funds	87,490	118,607
Capital adequacy ratio	17.7	10.3

Despite the recent drop, the capital adequacy ratio, which was so far among the highest in the banking sector in Poland, still exceeds the minimum level stipulated by the Banking Law Act (8%) and by international norms.

Performance Indicators

These indicators are a testimony to a very good performance of PPABank among other Polish banks. Most of the financial ratios represent an improvement over the excellent results attained in 1997.

1. Net profit to average weighted own funds (less subordinated debt) (ROE)
2. Net profit to average weighted total assets (ROA)
3. Operating costs including depreciation to net operating income
4. Net interest income to average weighted total assets
5. Net profit to the number of shares issued
6. Book value at year's end to the number of shares issued

performance indicators

	31.12.1996	31.12.1997	31.12.1998
Return on equity (ROE)	23.6	20.7	18.9
Return on assets (ROA)	2.7	2.7	2.2
Cost/income ratio	200.3	200.1	228.5
Net interest margin	8.2	8.2	6.1
Profit per share	1.5	1.8	2.4
Book value per share	11.8	14.7	17.3

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Money Market

In 1998, the responsibilities of the Treasury Department included the maintenance of liquidity, the management of the Bank's foreign exchange position, and ensuring a balanced structure of the Bank's foreign-currency assets and liabilities. Moreover, the Treasury Department manages the investment portfolio of PPABank and coordinates the policy in the field of cash operations in foreign currencies and in Polish zlotys.

In spite of the unfavorable developments on the world financial markets, especially in the aftermath of the Russian crisis, PPABank has maintained its high standing. Adherence to an investment policy recommended by the Assets and Liabilities Committee (ALCO), which restricts the portfolio to the most stable securities, issued by the government or the Central Bank, makes the Bank's investments in securities largely immune to the fluctuations of the economy.

Income on foreign currency transactions is an important component of the Bank's profits. Customers are offered a full range of currency operations, including currency forward contracts. PPABank follows a policy of frequent exchange-rate adjustments and preferential rates applied to transactions of higher amounts.

The expanding network of PPABank operating units involves an increased responsibility of the Treasury Department for the coordination of cash transactions. Active management of cash resources allows PPABank branches to maintain liquidity at all times and provides for an optimum allocation of assets.

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Organizational Structure

According to the Statute, the Bank's authorities consist of:

- General Shareholders' Meeting
- Board of Directors
- Board of Executives

The Board of Directors approves the Regulations of the Credit Committee which is to decide on credits, loans, guarantees or other agreements regarding financing.

In 1998, the Problem Asset Committee was created to relieve the Credit Committee of its duties in issues not related to loan production. The PAC decides on asset valuation, assignment of problem assets to specific risk categories, creation of reserves and development of relevant procedures. The PAC operates pursuant to Regulations approved by the Board of Directors.

Additionally, the Bank President appoints the Assets and Liabilities Committee (ALCO), an advisory body which is to effectively administer the Bank's assets and liabilities in order to ensure a long-term increase coupled with the realization of current financial plans.

The Bank's operating structure comprises the Head Office and four Regions (Eastern, Western, Malopolska and Slask). Each of the Regions includes branch offices, their sub-branches and agencies, and representative offices. Each region is headed by a Region Manager.

The Bank's Head Office is located in Kraków. On December 31, 1998, the Bank operated the following units:

- 11 full-service Branches (Branches I and III in Kraków, Katowice, Gdynia, Czestochowa, Warsaw, Lodz, Zakopane, Poznan, Wroclaw and Lublin) and one Investment and Leasing Branch in Warsaw,
- 13 Representative Offices (Czestochowa, Gdynia, Gliwice, Katowice, Kraków - two, Lublin, Lodz, Poznan, Szczecin, Warsaw, Wroclaw, and Zakopane),
- Agency of the Branch III in Kraków,
- Two sub-branches of PPABank's Warsaw Branch (at ul. Cypryjska and Marynarska).

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Auditor's Opinion

Auditor's opinion on the financial statements for the General Shareholders' Meeting of First Polish-American Bank S.A.

We have audited the financial statements of First Polish -American Bank S.A. ("PPABank", "the Bank") including:

1. the balance sheet as of December 31, 1998 with assets and liabilities amounting to PLN 1,140,067.6 thousand PLN 1,140,067,607.31);
2. off-balance sheet items as of December 31, 1998 amounting to PLN 626,865.2 thousand of contingencies (PLN 626,865,208.43);
3. the profit and loss account for the period January 1, 1998 to December 31, 1998, with net profit amounting to PLN 18,642.4 thousand (PLN 18,642,414.77);
4. the cash flow statement for the period January 1, 1998 to December 31, 1998, with a net cash inflow amounting to PLN 11,184.8 thousand (PLN 11,184,831.37);
5. notes to the financial statements.

The Management Board is responsible for the fairness and correctness of the information disclosed in the financial statements. Our responsibility is to issue a report on these financial statements based on our audit.

We have carried out the audit in accordance with:

1. section 7 of the Accounting Act dated September 29, 1994 (Official Journal no.121, item 591 with further amendments);
2. auditing standards issued by the National Council of the Chartered Accountants.

In our opinion, the attached financial statements have been prepared, in all material aspects, in accordance with the accounting policies stated in the Accounting Act mentioned above and the Resolution no. 1/98 of the Banking Supervision Commission dated June 3, 1998 on the special rules for bank accounting and the notes to the financial statements (NBP Official Journal no. 14, item 27), the Regulation of the Council of Ministers dated December 22, 1998 regarding type, form and dates of passing current and periodical information by issuers of securities admitted to public trading (Official Journal no. 163, item 1160 and are based on properly held accounting books.

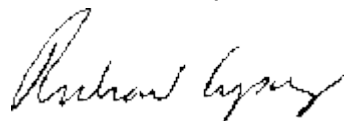
The financial statements fulfill the requirements of the current regulations and the Bank's articles of association with respect to their form and contents and give a true and fair view of all material information relevant to the assessment of profitability and results of operations for the year ending December 31, 1998 and the financial position as of December 31, 1998.

The information included in the management report on the Bank's activities is compliant with the information included in the audited financial statements.

Chartered Accountant
No. 4979/2575
Hanna Fludra



KPMG Polska Audyt Sp. z o.o.
Partner
Richard Cysarz



Warsaw, March 24, 1999

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Auditor's Report

Auditor's report on the audit of the financial statements for the year ending December 31, 1998

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General Information

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1. Introduction

1.1. This report on the audit of the financial statements for the year ending December 31, 1998 was prepared for First Polish-American Bank S.A. ("PPABank", "the Bank") and relates to the financial statements including the following:

- a. the balance sheet as of December 31, 1998 with assets and liabilities amounting to PLN 1,140,067.6 thousand (PLN 1,140,067,607.31);
- b. off-balance sheet items amounting to PLN 626,865.2 thousand of contingencies (PLN 626,865,208.43);
- c. the profit and loss statement for the period from January 1, 1998 to December 31, 1998, with net profit amounting to PLN 18,642.4 thousand (PLN 18,642,414.77);
- d. the cash flow statement for the year ending December 31, 1998 with a net cash inflow amounting to PLN 11,184.8 thousand (PLN 11,184,831.37);
- e. notes to the financial statements.

1.2. The audit was carried out at the Bank's premises during the period January 25 - February 17, 1999, in accordance with "The agreement for audit of the annual and semi-annual financial statements" concluded on December 22, 1998 between:

- First Polish-American Bank S.A. located in Kraków, Kordylewskiego 11; and
- KPMG Polska Audyt Sp. z o.o., located in Warsaw, Al. Jerozolimskie 65/79, enrolled on the list of bodies entitled to audit the financial statements under the registered number 458.

1.3. All of the information and documents required for the audit of the financial statements and preparation of the report were provided.

1.4. The Board of Executives of PPABank on March 24, 1999 provided us with a statement of assurance on the completeness, truth and fairness of information included in the above mentioned financial statements, as well as assurance that there were no events occurring up to the date of this report, which could significantly influence the amounts presented in the financial statements for the year ending December 31, 1998.

1.5. All figures presented in this report are shown in thousands of Polish zloty (PLN) unless otherwise noted.

[auditor's report](#)

2. Legal Status of the Bank

2.1. Following the decision of the President of National Bank of Poland no 46, dated October 6, 1990, Krakowskie Towarzystwo Bankowe S.A. in Kraków was established. The Notary Act, no A I 15847/90 containing the company agreement and Articles of Association, was signed on November 5, 1990. Krakowskie Towarzystwo Bankowe S.A. became a legal entity on December 19, 1990 by registration in the Local Court for Krakow, under the number H/B 2785.

2.2. The Bank is established for an unlimited period and may carry out banking activities in Poland.

2.3. Following a general meeting of the shareholders on February 16, 1991, some essential changes were made to the legal status of the Krakowskie Towarzystwo Bankowe S.A. The key changes were as follows:

- a. the Polish - American Enterprise Fund was admitted as shareholder;
- b. changes to the Articles of Association, included a change in the name of the Bank to First Polish - American Bank S.A. in Kraków.

All changes were accepted by the President of National Bank of Poland and stated in documents dated May 23, and May 27, 1991 respectively.

2.4. On March 10, 1994 the Securities Commission approved PPABank shares for public trading. The Board of the Warsaw Stock Exchange fixed November 7, 1994 as the first day of quoting the shares at the Stock Exchange.

2.5. The Bank operates in accordance with the Banking Law Regulation, dated August 29, 1997 (Official Journal No 140, entry 939), the President of Republic of Poland Regulation dated June 27, 1934 "Commercial Code" (Official Journal No 57/34, entry 502, as amended), Foreign Exchange Law, dated December 2, 1994 (Official Journal No 136/94, entry 703, with subsequent amendments) and its Articles of Association.

[auditor's report](#)

3. Basic Information on the Bank

3.1. The share capital of the Bank as of December 31, 1998 amounted to PLN 15,230,000 after an increase of PLN 2,730,000 during the year. The ownership structure may be analyzed as follows:

	12/31/1998 %	12/31/1997 %
Polish-American Enterprise Fund	34.1	25.7
Enterprise Credit Corporation (ECC)	24.1	25.1
RBS Trust Bank, London	-	9,7
Industrial Development Agency	7.8	9.5
Generale Bank	9.7	-
Other shareholders	24.3	30.0
	100.0	100.0

3.2. The share capital of the Bank as of December 31, 1998 consists of 7,615,000 shares with a nominal value of PLN 2 each:

	shares	PLN
series A	634,060	1,268,120
series B	1,115,940	2,231,880
series C	2,000,000	4,000,000

series D	1,250,000	2,500,000
series E	1,250,000	2,500,000
series F	625,000	1,250,000
series G	740,000	1,480,000
Total	7,615,000	15,230,000

3.2.1. During the year ending December 31, 1998 the Bank issued 1,365,000. shares through a public offering. On June 4, 1998 the Register Court of Kraków- Śródmieście approved the new share capital, which was fully subscribed. The share issue resulted in the nominal value of share capital increasing by PLN 2,730.0 thousand and the share premium reserve by PLN 18,519.5 thousand.

3.3. The purpose of the Bank is to provide banking and other financial services, both in zlotys and foreign currencies, for domestic and foreign legal entities and individual persons and other organizations including economic organizations with no legal status.

The scope of Bank business shall include the following:

- a. accepting deposits,
- b. maintaining bank accounts,
- c. granting credits and cash loans,
- d. carrying out pecuniary settlements, including use of payment cards,
- e. issuing bank guarantees and sureties,
- f. issuing securities, including convertible bonds, carrying out commissioned tasks, and assuming obligations related to the issuance of securities,
- g. participating in trading in securities,
- h. conducting operations on money and foreign currency markets including forward and derivative instrument transactions,
- i. conducting check and bill-of-exchange operations,
- j. purchasing and selling receivables,
- k. conducting foreign exchange transactions,
- l. safekeeping of valuable objects and securities,
- m. rendering the following financial services:
 - consulting services,
 - custody services,
 - leasing services,
 - brokerage services.

3.3.1. On April 20, 1995 following the decision of the President of the NBP the Bank received a full foreign exchange license.

3.4. During the year the Bank opened branches in Gdynia, Lodz, Czestochowa and Wroclaw. Sub-branch No. 2 of the Warsaw Branch was opened as well as the PPABank S.A. Investment and Leasing Branch in Warsaw. The Bank conducts its operations through its head office in Kraków and a total of twelve branches. The Bank also grants loans from thirteen representative offices located throughout Poland.

3.5. As of December 31, 1998 the Board of Executives of the Bank consisted of:

- Bank President - Marek Kulczycki
- First Vice-President - Benjamin H. Turnbull
- Vice-president - Thomas C. Cianfrani
- Vice-president - Leszek Niemycki
- Vice-president - Jean-Luc Deguel

3.5.1. The composition of the Board of Executives changed during the reporting year. Mr. Jerzy Markiewicz, Vice-President and the Treasury Department Director was a Board of Executives member until May 31, 1998. On June 1, 1998, Mr. Jean Luc Deguel was appointed by the Board of Directors as a Vice-President and Director for International Economic Relations

3.6. On December 31, 1998 the Bank employed a total of 541 full time personnel.

4. Information of the Financial Statement for 1997

4.1. The financial statements for the year ending December 31, 1997 were audited by KPMG Polska Audyt Sp. z o.o. The audit was carried out in accordance with Act on Accounting dated September 29, 1994 (Official Journal no.121, item 591 with subsequent amendments). An unqualified opinion was issued on those financial statements.

4.2. December 31, 1997 closing balances were properly recorded as opening balances as at January 1, 1998.

4.3. The Bank held its Annual General Meeting of Shareholders on June 25, 1998. The protocol from this meeting including approval of the Bank's 1997 financial statements and profit distribution was delivered to Regional Court on July 3, 1998. The Bank's financial statements were submitted for publishing on July 1, 1998 in Monitor Polski B and published in Monitor Polski B no. 408 on October 22, 1998.

4.4. The Board of Executives of the Bank is to propose to the General Meeting of Shareholders the allocation of the whole net profit for 1998, amounting to PLN 18,642.4 thousand to the general risk fund.

Performance Ratios

1.1. Performance and other ratios are as follows:

	12 months ending		
	31.12.98 PLN 000's	31.12.97 PLN 000's	31.12.96 PLN 000's
Total assets	1,140,067.6	640,982.0	419,750.7
Net profit	18,642.4	13,713.3	9,057.2
Capital adequacy ratio	10.3%	17.7%	21.6%
Foreign exchange position			
- global	(2.43)%	(1.8)%	2.8%
- maximum	9.63%	8.1%	6.3%
Income earning assets to total assets	84.9%	83.1%	84.5%
Cost bearing liabilities to total liabilities	84.3%	76.9%	80.5 %
Profit per 1 share (PLN) shares issued with preemptive right to the profits of the year	2.45	1.80	1.45
Profit per 1 share (PLN) weighted average number of shares outstanding during the year	2.68	2.35	2.13
Interest income to income earning assets	13.6%	16.1%	15.3%
Net interest income to income earning assets	5.4%	8.0%	7.7%
Net interest income to interest income	39.8%	49.4%	50.2%
Interest expense to cost bearing liabilities	8.2%	8.8%	8.0%
Income earning assets to cost bearing liabilities	100.7%	108.1%	104.9%

1.2. During the year ending December 31, 1998 the inflation rate, being the annual average index of retail prices of consumer goods and services, amounted to 11.8% and the Polish zloty increased by approximately 0.4% against the US dollar.

1.3. Net profit increased over the corresponding period ending December 31, 1997 by 35.9% mainly due to a 52.7% increase in interest income on loans and securities, and a general increase in commission income, foreign exchange differences income.

1.4. Capital adequacy ratio

The capital adequacy ratio (calculated in accordance with an appendix to the Order of the Banking Supervision Commission No. 3/98 dated June 30, 1998, NBP Official Journal no. 15, item 34 equal the function of net equity reserves to the value of risk weighted assets and off-balance sheet liabilities) amounted to 10.3% at December 31, 1998. This ratio was above the rate recommended by the National Bank of Poland of 8.0%.

1.5. Foreign exchange position

The foreign exchange position of the Bank, both global and maximum (calculated in accordance with the Resolution of the Banking Supervision Commission No 5/98, NBP Official Journal no 15, item 33), remained within the risk limits set by the NBP:

- global position cannot exceed 30% of bank's funds,
- maximum FX position cannot exceed 40% of the bank's own funds.

- global position - (2.43)%
- maximum position - 9.63%

Detailed Information

[auditor's report](#)

1. Accounting Policies

1.1 Accounting books

The Bank's accounting records are computerized using a central data base which results in one general ledger for Head Office and branches. The system operates on-line and accordingly the client accounts balances are updated directly after entering transactions.

The Bank applies a chart of accounts approved by a resolution of the Board of Executives dated August 1, 1994 (with subsequent amendments).

The Books ensure clear and reliable presentation of the assets and of the financial standing of the Bank as well as to enable the preparation of the required financial statements.

Transactions are clearly and fully documented and properly classified in the books. The books are properly kept and maintained. The entries to the books are documented by source documents, which are the basis for the accounting entries.

1.2. Internal control

The internal controls are adequate for the present level of the Bank's activities.

These procedures ensure the limitation of the risk of irregularities by the complete and proper classification and documentation of the Bank's transactions.

1.3. Valuation method

No amendments were made to the accounting policies and methods of valuation in the year ending December 31, 1998.

1.3.1 Fixed assets

Fixed assets are recorded at cost or the revalued amount net of accumulated depreciation. The cost of the fixed assets purchased in foreign currencies is calculated using the official NBP rate of exchange on the day of payment. Depreciation is calculated monthly on a straight line basis in compliance with rates of depreciation and procedures set by the Regulation of the Ministry of Finance dated January 17, 1997 (Official Journal no.6 item 35 with subsequent amendments).

The exceptions are fixed assets under lease agreements and equipment serving cashier's desk and vault which are, in most cases, depreciated on a reducing balance method. Fixed assets with a cost not exceeding PLN 2,500 are fully amortized in the month when they are brought into use.

1.3.2. Intangible assets

Intangible assets are shown at cost net of accumulated depreciation calculated on a straight line basis in compliance with the relevant regulation set out in paragraph 1.3.1. above.

1.3.3. Investment tax relief

Purchased fixed assets eligible for investment tax relief maybe offset against corporate income tax payable under the Law dated February 15, 1992 on corporate income tax (Official Journal No. 106 item 482, with subsequent amendments). The Bank used investment tax relief in the following amounts:

- PLN 439.7 thousand in 1994.
- PLN 3,313.3 thousand in 1997.
- PLN 3,999.9 thousand in 1998.

In 1998, the Bank deducted the amount of PLN 1,656.6 thousand being investment tax premium relating to the investment tax relief claimed in 1997. Taxable income for 1998 was reduced by the relief and premium claimed and a deferred tax liability established for the timing differences between the accelerated tax benefit of the relief and the depreciation schedule of the associated fixed assets. Under this law the Bank may claim a further 50% of relief claimed in 1998 to reduce taxable income in 1999 as a permanent benefit. The above-mentioned Act provides for the possibility that the investment tax relief may be lost in specific cases (among others in the case of overdue tax payments). In case of the withdrawal of investment tax relief, tax liabilities would be recalculated as if the relief had not been taken.

In addition, penalty interest would be calculated on additional tax liabilities for the period from the date of the investment tax relief deduction. Due to an amendment to the corporate income tax Act on November 28, 1998 (Official Journal no. 144, item 931), a taxpayer shall not lose the investment tax relief if he adjusts the tax return and repays the tax liabilities with the interest receivable within 14 days from the date of receiving the Tax Office decision that defines the tax liabilities due.

1.3.4. Loans

Loans granted by the Bank, are disclosed as principal with capitalized interest, accrued interest receivable and interest billed and not paid. To provide against potential losses resulting from loan activities, specific provisions are created in accordance with the Regulation no. 13/94 of the President of NBP on the rules to create specific provisions connected with banks activity dated December 10, 1994 (NBP Official NBP Journal no. 23, item 36) to reduce the nominal value of the loans. Additionally the Bank has established a general risk provision.

1.3.5. Securities

Securities are classified in the investment or trading portfolio. Dependent on the transaction, they are disclosed as follows:

- securities allocated for sale (the trading portfolio) are disclosed at cost with any accrued interest, discount or premium but not higher than the net current sales value. In cases where the value determined by this method is higher than the market value, the difference between the two is charged to the costs of financial operations;
- securities allocated for investment are disclosed at the cost with any accrued interest, discount and premium including a provision for permanent diminution in value if any. In case of a permanent fall in value, the amount is stated net of an appropriate provision.

1.3.6. Interest income and expense

Interest income and expense are disclosed together with any accrued interest on regular loans at the balance sheet date. Accrued interest on irregular loans is not booked to the profit and loss account but is disclosed as interest receivable with a provision held as deferred interest income.

1.3.7 Fees and commission income and expense

All fee and commission income and expense is recognized on a cash basis with the exception of commission income on the management of the ECC loan portfolio which is accounted for on an accrual basis.

1.3.8. Foreign currencies

All balances in foreign currencies were revalued at the average exchange rates announced by the President of NBP as of December 31, 1998. Both realized exchange rate differences and unrealized differences resulting from the revaluation of foreign currency balances are recognized in the profit and loss account.

1.4. Own funds

The Bank's own funds consist of:

- share capital - PLN 15,230.0 thousand
- supplementary capital - PLN 66,476.5 thousand
- reserve capital - PLN 17,018.3 thousand
- general risk fund - PLN 13,713.3 thousand
- fixed assets revaluation funds - PLN 551.4 thousand

According to the paragraph No. 174 of the Banking Law the balance of the General Risk Fund as of December 31, 1997 was liquidated on January 1, 1998. The Fund amounted PLN 8,340 thousand as of December 31, 1997 consisting of PLN 7,840 thousand as deductions from retained earnings and of PLN 500 thousand of charges through the profit and loss account. The total amount transferred to reserve capital amounts to PLN 8,240 thousand. The tax liability arising amounts to PLN 100 thousand and will be paid from January 1998 to December 2000 by equal monthly payments.

In addition the Bank's funds for the purpose of calculation of the NBP capital adequacy ratio includes subordinated debt amounting to PLN 5,618.0 thousand.

1.5. Income tax

The Bank adopts the temporary method of tax effect accounting. Income tax expense is calculated on operating profit adjusted for permanent differences between taxable and accounting income. The tax effect of timing differences, which arise from items being brought to account in different periods for income tax and accounting purposes, is carried forward in the balance sheet as a future income tax benefit or a provision for deferred income tax at the legislated rate of corporate income tax for 1999.

Future income tax benefits are not brought to account unless it is probable that future taxable profit will allow the deferred tax asset to be recovered.

1.6. Foreign currency off balance sheet transactions

1.6.1. Spot foreign exchange transactions

Spot transactions are revalued on a daily basis with the original spot rate compared to the NBP fixing rate. The difference is recognised in profit and loss account result on foreign exchange transactions.

1.6.2. Forward foreign exchange transactions

Forward foreign exchange transactions are valued at their market value. Unrealised gains and losses on forward foreign transactions are recognised in/charged to the profit and loss account.

1.6.3. Foreign exchange swap transactions

The Bank recognises income and expense on foreign currency swap transactions by accruing the difference between the spot leg of the transaction and the forward rate on a straight line basis over the life of the contract. The income and expense on such transactions is recognised in the profit and loss account result on foreign exchange transactions. In addition foreign currency swaps are revalued on a daily basis with the original spot leg of the transaction revalued on the NBP fixing for the day with the resulting gains or losses taken to the profit and loss account result on foreign exchange transactions.

1.7. Post balance sheet events

1.7.1. Based on the Resolution No. 20/99 of February 18, 1999 the Supervisory Board accepted the resignation of Mr. Benjamin H. Turnbull from his position of the First Vice President of PPABank S.A. Board of Executives and decided to recall him from the position of the Vice President of PPABank S.A. Board of Executives effective February 28, 1999.

1.7.2. On February 23, 1999 Generale Bank, the Polish-American Enterprise Fund (PAEF) and Enterprise Credit Corporation (ECC) signed a share purchase agreement in which Generale Bank agrees to purchase PAEF's and ECC's entire stake of 58.8% in PPABank. The transaction will take Generale Bank's stake in PPABank to 68.5%. The price to be paid by Generale Bank for PAEF and ECC shares is expected to be around PLN 40 per share, depending on the book value of the Bank at the closing of the transaction. Following the purchase, Generale Bank will launch a public offer for the remaining shares in PPABank. The transaction is subject to obtaining approval from the National Bank of Poland, the Securities Commission and the Anti-Monopoly Office.

Financial Statements

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Balance Sheet

ASSETS	Notes	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Cash and Central Bank Operations	2.1.	104 001.4	80 032.9
Due from financial sector	2.2.	86 984.5	91 442.5
1. Call		8 177.3	20 961.0
2. Term		78 807.2	70 481.5
Due from customers and budget sector	2.3.	766 544.3	311 200.8
1. Call		122 235.3	62 920.0
2. Term		644 309.0	248 280.8
Securities	2.4.	108 085.8	120 908.7
Other shares		5.5	299.5
Intangible assets	2.5.	9 433.6	6 932.4
Fixed assets	2.6.	31 609.9	24 593.5
Other assets	2.7.	28 618.6	2 715.9
1. Siezed assets		1.3	38.4
2. Other		28 617.3	2 677.5
Interperiod settlements	2.8.	4 784.0	2 855.8
		1 140 067.6	640 982.0
LIABILITIES	Noty	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Due to NBP		-	-
Due to financial sector	2.9.	280 402.4	109 198.0
1. Current		8 014.8	12 837.9

2. Term		272 387.6	96 360.1
Due to customers and budget sector	2.10.	680 355.7	383 788.0
1. Current		151 464.7	112 122.4
2. Term		528 891.0	271 665.6
Special funds and other liabilities	2.11.	25 612.4	37 312.0
Accrued expenses and deferred income	2.12.	7 712.6	4 991.6
Provisions	2.13.	8 734.6	4 489.1
Subordinated debt	2.14.	5 618.0	9 363.3
Share capital	2.15.	15 230.0	12 500.0
Supplementary capital	2.16.	66 476.5	47 927.0
Fixed assets revaluation fund	2.17.	551.4	581.4
Reserve capital	2.18.	30 731.6	17 118.3
Net profit (loss)		18 642.4	13 713.3
		1 140 067.6	640 982.0
Off-balance sheet items granted	2.19.	380 144.7	154 999.1
Off-balance sheet items received	2.19.	64 024.0	83 129.6
Open foreign currency transactions	2.19.	174 696.5	94 997.7
Securities operations	2.19.	8 000.0	122.4

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Profit and Loss Statement (Auditor's report)

	Notes	12 months ending 12/31/1998 PLN 000's	12 months ending 12/31/1998 PLN 000's
Interest income	2.20.	131 361.3	86 008.0
Interest expense	2.21.	(79 114.0)	(43 489.5)
Net interest income		52 247.3	42 518.5
Fee and commission income	2.22.	27 859.8	16 619.5
Fee and commission expense		(1 403.6)	(1 356.2)
Net fee and commission income		26 456.2	15 263.3
Income on financial transactions	2.23.	(210.8)	330.6
Foreign exchange results - net		14 922.9	5 249.4
Profit on banking activities		93 415.6	63 361.8
Other operating income		5 494.4	8 093.2
Other operating expense		(3 128.8)	(3 520.9)
Net operating revenue		95 781.2	67 934.1

General expenses	2.24.	(52 889.4)	(37 017.1)
Depreciation of fixed and intangible assets		(9 671.8)	(8 111.2)
Charges to loan loss provision	2.25.	(8 599.9)	(3 441.8)
Release of provision and other decreases	2.26.	2 762.9	3 188.5
Net release of provision		(5 837.0)	(253.3)
Profit on operating activities		27 383.0	22 552.5
Gross profit (loss)		27 383.0	22 552.5
Income tax	2.27.	(8 740.6)	(8 839.2)
Net profit (loss)		18 642.4	13 713.3

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Cash Flow Statement

		12 months ending 12/31/1998 PLN 000's	12 months ending 12/31/1997 PLN 000's
A.	CASH FLOW FROM OPERATING ACTIVITY		
I.	Net profit (loss)	18 642.4	13 713.3
II.	Adjustments for:	(104 684.0)	76 851.1
1.	Depreciation	9 671.8	8 111.2
2.	Foreign exchange gains (losses)	-	-
3.	Interest and dividend	(20 927.9)	-
4.	Investment activity (gain) loss	758.6	-
5.	Change in provisions	3 581.0	-
6.	Income tax charge	8 740.6	8 839.2
7.	Income tax paid	(12 256.4)	(7 062.1)
8.	Change in securities held	-	-
9.	Change in receivables from financial institutions	(8 325.7)	5 847.8
10.	Change in receivables from customers and budget	(455 343.5)	(132 529.9)
11.	Change in securities bought in repo transactions	-	1 902.1
12.	Change in payables to customers and budget	114 878.1	48 397.2
13.	Change in payables to customers and budget	296 567.7	104 970.3
14.	Change in securities sold in repo transactions	-	-
15.	Change in securities	-	-
16.	Change in other liabilities	(11 799.6)	30 833.2
17.	Change in interperiod settlements	(1 439.5)	(479.8)
18.	Change in deferred income	2 232.3	1 396.2

19.	Other items	(31 021.5)	6 625.7
III.	Net cash flow from operations	(86 041.6)	90 564.4
B. CASH FLOW FROM INVESTING ACTIVITY			
I.	Receipts from investing activity	156 941.7	203 113.9
1.	Sale of intangible fixed assets	-	0.8
2.	Sale of tangible fixed assets	1 532.3	7 101.6
3.	Sale of shares and participation investments	-	-
4.	Sale of shares and affiliated investments	-	-
5.	Sale of shares and investments in a controlling entity	-	-
6.	Sale of shares and investments in other units, other securities (including marketable securities) or other property rights	120 705.2	196 011.5
7.	Other receipts	34 704.2	-
II.	Expenditures on investment activity	(132 233.3)	(256 645.1)
1.	Acquisition of intangible fixed assets	(4 704.6)	(3 431.3)
2.	Acquisition of tangible fixed assets	(15 290.5)	(16 390.5)
3.	Acquisition of shares and participation investments	-	-
4.	Acquisition of shares and affiliated investments	-	-
5.	Acquisition of shares and investments in a controlling entity	-	-
6.	Acquisition of shares and investments in other units, other securities or other property rights (including marketable securities)	(111 048.9)	(236 823.3)
7.	Acquisition of own shares for sale	-	-
8.	Other items	(1 189.3)	-
III.	Net cash flow from investments	24 708.4	(53 531.2)
C. CASH FLOW FROM FINANCIAL ACTIVITY			
I.	Receipts from financial activity	73 830.5	19 375.0
1.	Raised long term credits from banks	52 581.0	-
2.	Raised long term loans from other financial institutions	-	-
3.	Issue of bonds and other securities for other financial institutions	-	-
4.	Increase in subordinated debt	-	-
5.	Receipts from issue of own shares	21 249.5	19 375.0
6.	Share capital payments	-	-
7.	Other items	-	-
II.	Expenditures on financial activity	(1 312.5)	430.5

1.	Repayment of long term credits from banks	-	-
2.	Repaid long term credits to other financial institutions	-	-
3.	Redemption of bonds and other securities to other financial institutions	-	-
4.	Decrease in subordinated debt	-	-
5.	Own share issue expense	-	-
6.	Own share amortization	-	-
7.	Payment of dividends and other payments to owners	-	-
8.	Payments from profit for the managing and supervising staff	-	-
9.	Expenses on socially useful purposes	645.6	430.5
10.	Liabilities related to financial lease agreements	-	-
11.	Other items	(1 958.1)	-
III.	Net cash flow from financial activity	72 518.0	19 805.5
D.	NET CASH FLOW	11 184.8	56 838.7
E.	CHANGE IN CASH IN BALANCE SHEET	11 184.8	56 838.7
	change in cash related to exchange rate differences	1 009.9	4 197.1
F.	CASH AT PERIOD BEGINNING	100 993.9	44 155.2
G.	CASH AT PERIOD END	112 178.7	100 993.9

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Foot Notes

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2.1. Cash and Central Bank operations

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
NBP current account	103 946.0	75 590.1
Obligatory reserve account	0.0	4 431.7
Other	55.4	11.1
	104 001.4	80 032.9

[assets](#)

2.2. Due from financial sector

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Performing receivables	86 615.1	91 203.6
Accrued interest	369.4	238.9
	86 984.5	91 442.5

2.2.1 Maturity of term placements with financial sector

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Due within 1 month	86 615.1	90 531.2
Due between 1 and 3 months	-	672.4
Due between 3 months and 1 year	-	-
Due between 1 and 5 years	-	-
Due after 5 years	-	-
Non-performing loans	-	-
Accrued interest	369.4	238.9
	86 984.5	91 442.5

[assets](#)

2.3. Due from customers and budget sector

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Performing loans	749 412.0	305 582.4
- accrued interest	7 948.6	4 688.4
Non-performing loans	23 698.8	9 871.3
- substandard	14 092.3	2 283.6
- doubtful	812.5	-
- loss	4 021.3	3 947.8
- accrued interest	4 772.7	3 639.9
Total	773 110.8	315 453.7

2.3.1 Classification of non-performing loans provisions

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
- substandard	2 562.7	658.1
- doubtful	409.5	-
- loss	3 594.3	3 594.8
Total	6 566.5	4 252.9

2.3.2 Maturities of amounts due from customers and budget sector

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Overdrafts	120 228.7	61 429.9
Due within 1 month	26 845.2	28 971.6
Due between 1 and 3 months	37 634.0	19 672.2
Due between 3 months and 1 year	165 841.3	60 577.4

Due between 1 and 5 years	346 253.9	128 465.6
Due after 5 years	44 660.3	1 777.3
Non-performing loans	12 359.6	1 978.5
Interest	12 721.3	8 328.3
Net	766 544.3	311 200.8
Non-performing loans provisions	6 566.5	4 252.9
Total	773 110.8	315 453.7

2.3.3 Change in provisions

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	4 252.9	3 866.1
Increases:	4 754.0	2 856.4
- change of risk category	4 318.8	2 050.5
- others	388.5	761.3
- exchange rate differences	46.7	44.6
Decreases:	(2 440.4)	(2 469.6)
- payments	(1 796.8)	(2 463.3)
- change of risk category	(610.9)	-
- others	(32.7)	(6.3)
Closing balance	6 566.5	4 252.9

2.3.4 Collateral for non-performing loans

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
- substandard loans	1 361.8	-
- doubtful loans	-	-
- loss loans	415.1	353.0
Total	1 776.9	353.0

[assets](#)

2.4. Securities

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Issued by State	108 085.8	118 990.1
- treasury bills	85 320.3	77 378.8
- government bonds	22 765.5	41 611.3
Bills of non-financial institutions	-	1 918.6
Total	108 085.8	120 908.7

2.4.1 Investment portfolio - shares, investments and other securities

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
securities with unlimited rights to sale. listed on the stock exchange	22 765.5	41 611.3
government bonds (book value)	22 765.5	41 611.3
- adjustments	1 276.0	3 193.2
- purchase price	21 489.5	38 418.1
securities with unlimited rights to sale. traded over-the-counter	85 320.3	77 378.8
treasury bills (book value)	85 320.3	77 378.8
- adjustments	7 568.8	7 695.8
- purchase price	77 751.5	69 683.0
unlisted and not traded over-the-counter securities with unlimited rights to sale	-	1 918.6
bills of non-financial institutions (book value)	-	1 918.6
- adjustments	-	36.2
- purchase price	-	1 882.4
Purchase price	99 241.0	109 983.5
Adjustments	8 844.8	10 925.2
Book value	108 085.8	120 908.7

2.4.2. PLN 20 million of securities are pledged as collateral for transactions on Polish interbank market, PLN 15 million of securities are pledged as collateral for a foreign currency loan and an additional PLN 1,200 thousand is pledged towards the Bank Guarantee Fund as at December 31, 1998.

[assets](#)

2.5. Intangible assets

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Series A,B,C,D,E,F,G share issue expense	2 737.6	3 154.4
Computer software and licenses	6 696.0	3 778.0
Total	9 433.6	6 932.4

2.5.1 Changes in intangible assets

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	9 607.6	5 952.9
Additions	4 704.6	3 666.3
- purchase	4 108.8	1 978.3

- costs of raising capital	595.8	1 669.7
- settlements of investments	-	18.3
Disposals	(0.3)	(11.6)
- liquidation	-	(11.6)
- return of amount overpaid	(0.3)	-
Closing balance	14 311.9	9 607.6
Accumulated depreciation as at 01/01	(2 675.2)	(1 089.7)
Depreciation for the year	(2 203.1)	(1 585.5)
- purchase	(1 190.8)	(581.2)
- costs of raising capital	(1 012.3)	(1 015.1)
- liquidation	-	10.8
Accumulated depreciation as at 12/31	(4 878.3)	(2 675.2)
Net book value as at 12/31	9 433.6	6 932.4

[assets](#)

2.6. Fixed assets

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Equipment	11 459.8	10 615.6
Vehicles	4 746.0	6 809.7
Other	11 538.0	7 072.5
Assets under construction	2 676.8	95.7
Advances on investments	1 189.3	-
Total	31 609.9	24 593.5

2.6.1 Changes in fixed assets

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	37 135.2	31 415.7
Additions	20 438.5	11 834.3
- purchases	14 359.0	9 585.5
- settlements of investments	4 624.7	2 248.8
- advances on investments	1 189.3	-
- reclassification	134.0	-
- other	131.5	-
Disposals	(10 411.6)	(6 114.8)
- sale	(4 133.7)	(5 589.0)
- liquidation	(1 387.7)	(181.3)

- settlements of investments	(4 624.7)	(246.2)
- reclassification	(134.0)	-
- other	(131.5)	(98.3)
Closing balance	47 162.1	37 135.2
Accumulated depreciation as at 01/01	(12 541.7)	(9 296.2)
Depreciation for the year	(3 010.5)	(3 245.5)
- purchases	(6 537.1)	(6 301.9)
- assets sold	2 667.9	2 927.8
- liquidation	858.7	128.6
Accumulated depreciation as at 12/31	(15 552.2)	(12 541.7)
Net book value as at 12/31	31 609.9	24 593.5

2.6.2 Fixed assets (ownership structure)

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Own and used by the Bank	25 289.9	15 170.9
Customer leases or other agreement disclosed as the property of the Bank	6 320.0	9 422.6
Total	31 609.9	24 593.5

[assets](#)

2.7. Other assets

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Siezed assets held for sale	1.3	38.4
Other assets	28 617.3	2 677.5
- income tax receivables	4 966.1	425.3
- interbank settlements	21 976.3	779.1
- other	1 674.9	1 473.1
Gross other assets	28 618.6	2 715.9

2.7.1 Assets for sale

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Property	-	33.3
Inventory	1.3	5.1
Total	1.3	38.4

[assets](#)

2.8. Interperiod settlements

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Prepayments	4 329.5	2 755.8
- rent	2 961.5	2 245.3
- other	1 368.0	510.5
Other interperiod settlements	454.5	100.0
Total	4 784.0	2 855.8

[liabilities](#)

2.9. Maturities of term deposits due to financial sector

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Due within 1 month	172 302.9	83 236.5
Due between 1 and 3 months	-	-
Due between 3 months and 1 year	25 098.0	-
Due between 1 and 5 years	82 003.0	25 816.7
Due after 5 years	-	-
Accrued interest	998.5	144.8
Total	280 402.4	109 198.0

[liabilities](#)

2.10. Maturity of amounts due to customers and budget sector

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Due within 1 month	529 414.8	277 881.6
Due between 1 and 3 months	82 603.9	51 029.0
Due between 3 months and 1 year	58 751.6	45 789.3
Due between 1 and 5 years	3 099.8	3 614.1
Due after 5 years	-	50.0
Accrued interest	6 485.6	5 424.0
Total	680 355.7	383 788.0

[liabilities](#)

2.11. Special funds and other liabilities

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Special funds	230.1	153.3
- social fund	153.1	111.5
- other	77.0	41.8

Others	25 382.3	37 158.7
- interbank settlements	19 251.3	32 595.1
- tax settlements	1 634.9	998.8
- other	4 496.1	3 564.8
Total	25 612.4	37 312.0

[liabilities](#)

2.12. Accrued expenses and deferred income

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Interperiod settlements	1 246.8	758.1
- employee bonus	910.0	500.0
- other	336.8	258.1
Deferred income	6 465.8	4 233.5
- income in suspense	5 036.6	3 659.8
- other	1 429.2	573.7
Total	7 712.6	4 991.6

[liabilities](#)

2.13. Provisions

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Deferred tax provision	5 153.6	4 489.1
Other provisions	3 581.0	-
- general risk provision	3 581.0	-
Total	8 734.6	4 489.1

2.13.1 Change in provisions

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	4 489.1	2 623.7
Increases:	10 782.7	4 388.4
- deferred tax provision	6 924.7	4 388.4
- general risk provision	3 858.0	-
Decreases:	(6 537.2)	(2 523.0)
- deferred tax provision	(6 260.2)	(2 523.0)
- general risk provision	(277.0)	-
Closing balance	8 734.6	4 489.1

[liabilities](#)

2.14. Subordinated debt

Item	Amount	Currency	Interest rate	Maturity
PAEF	2,000,000	USD	5.5	I installment - 2,000,000 USD - 9/25/2000
				II installment - 2,000,000 USD - 3/15/2001

On November 8, 1996 the NBP gave approval for the Bank to classify PLN 11,236 thousand PAEF loan as subordinate debt. The debt is in USD and interest is 5.5% per annum. USD 2 million matures in September 2000 and the remaining USD 2 million in March 2001. The amount of the subordinated debt was, according to the recommendation from the General Banking Inspectorate, decreased on March 15, 1998 and on September 25, 1998. As a result, the subordinated debt amounts to PLN 5,618 thousand at December 31, 1998 (PLN 9,363.3 thousand at December 31, 1997). The remaining debt is disclosed as "Due to financial sector".

[liabilities](#)

2.15. Share capital

The nominal value of share capital was increased following a public offer of 1,365,000 shares with nominal value of PLN 2 each during the period. Share capital as at December 31, 1998 is PLN 15,230 thousand.

2.15.1.

Shares series	Number of shares	Nominal value of shares (PLN thousands)	Date of registration	Participation in the net profit distribution
A	634,060	1,268,120	12/19/1990	from full payment of shares
B	1,115,940	2,231,880	4/30/1991	from full payment of shares
C	2,000,000	4,000,000	7/17/1994	1/1/1994
D	1,250,000	2,500,000	7/11/1996	1/1/1995
E	1,250,000	2,500,000	4/11/1997	1/1/1996
F	625,000	1,250,000	6/4/1998	1/1/1997
G	740,000	1,480,000	6/4/1998	1/1/1997
	7,615,000	15,230,000		

2.15.2. Change in share capital

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	12 500.0	10 000.0
Increases:	2 730.0	2 500.0
- share issue	2 730.0	2 500.0
Closing balance	15 230.0	12 500.0

[liabilities](#)

2.16. Supplementary capital

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Supplementary capital from share premium	66 115.9	47 596.4

Obligatory capital	360.6	330.6
Total	66 476.5	47 927.0

2.16.1. Change in supplementary capital

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	47 927.0	31 012.5
Increases:	18 552.1	16 914.5
- issue of shares with premium	18 519.5	16 875.0
- liquidation of fixed assets	32.6	39.5
Decreases:	(2.6)	-
- liquidation of fixed assets	(2.6)	-
Closing balance	66 476.5	47 927.0

[liabilities](#)

2.17. Fixed assets revaluation fund

Change in fixed assets revaluation fund

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	581.4	620.9
Increases:	2.6	-
- liquidation of fixed assets	2.6	-
Decreases:	(32.6)	(39.5)
- liquidation of fixed assets	(32.6)	(39.5)
Closing balance	551.4	581.4

[liabilities](#)

2.18. Reserve capital

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Banking general risk	-	8 340.4
General risk fund	13 713.3	-
Others. of which:	17 018.3	8 777.9
- reserve capital	17 018.3	8 777.9
Total	30 731.6	17 118.3

2.18.1. Change in reserve capital

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Opening balance	17 118.3	8 061.1
Increases:	13 713.3	9 057.2

- distribution of profit	13 713.3	9 057.2
Decreases:	(100.0)	-
- income tax related to charge of general risk fund	(100.0)	-
Closing balance	30 731.6	17 118.3

[liabilities](#)

2.19. Off-balance sheet items

	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Contingent liabilities granted to financial institutions and commercial enterprises:		
- guarantees	193 245.5	75 229.9
- letters of credit	15 876.1	12 443.4
- unused credit lines	171 023.1	67 325.8
	380 144.7	154 999.1
Contingent liabilities received from financial institutions:		
- guarantees	1 321.5	825.6
- others	62 702.5	82 304.0
	64 024.0	83 129.6
Open foreign currency transactions	174 696.5	94 997.7
Securities operation	8 000.0	122.4
Total	626 865.2	333 248.8

2.19.1 In guarantees mentioned above amounting to PLN 193,245.5 thousand, the value of PLN 134,392.3 thousand relates to guarantees granted to ECC.

[profit and loss](#)

2.20. Interest income

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Interest from:		
operations with financial institutions	14 214.7	12 789.5
operations with customers and budget sector	96 400.0	54 981.3
securities operations:	20 746.6	18 237.2
- fixed income securities	20 746.6	18 237.2
	131 361.3	86 008.0

[profit and loss](#)

2.21. Interest expense

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Interest from:		
- operations with financial institutions	10 585.1	6 358.6
- operations with customers and budget sector	68 132.4	36 513.5
- others	396.5	617.4
	79 114.0	43 489.5

[profit and loss](#)

2.22. Fee and commission income

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Fees and commissions on:		
- loans granted	9 550.1	4 266.4
- financial institutions transactions	7 627.0	6 737.7
- customer transactions	10 512.7	5 615.4
- transactions with budget sector	170.0	-
	27 859.8	16 619.5

Included in fee and commission income for the twelve months ending December 31, 1998 is PLN 7,541.2 thousand (1997 PLN 6,162.4 thousand) received from a related party, ECC for the management of the ECC loan portfolio.

[profit and loss](#)

2.23. Income on financial transactions

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Income from securities transactions	(296.1)	(186.8)
- revenues on securities transactions	127.8	4.1
- expenses of securities transactions	(423.9)	(190.9)
Income on other financial transactions	85.3	517.4
	(210.8)	330.6

[profit and loss](#)

2.24. General expenses

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Compensation:	26 919.0	18 908.6
- salaries	18 615.9	12 772.8
- surcharges on salaries	7 416.6	5 250.6
- social support of employees	886.5	885.2
Other general expenses:	25 970.4	18 108.5
- advertising and marketing	2 791.2	1 400.7
- rents	6 185.4	3 805.6
- telecommunication	2 741.3	1 772.9
- office supplies	1 985.2	1 229.4
- representation costs	409.9	390.6
- business travel	386.6	615.9
- advisory services	1 320.4	1 376.2
- Bank Guarantee Fund contribution	841.4	771.6
- other	9 309.0	6 745.6
	52 889.4	37 017.1

[profit and loss](#)

2.25. Charge to loan loss provision

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Charges to provisions for:	(8 599.9)	(3 441.8)
- non-performing loans	(4 707.4)	(2 811.8)
- general risk fund	(3 858.0)	-
- other	(34.5)	(630.0)
	(8 599.9)	(3 441.8)

[profit and loss](#)

2.26. Release of provision and other decreases

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Release of provisions for:	2 762.9	3 188.5
- non-performing loans	2 407.7	2 469.6

- other	355.2	718.9
	2 762.9	3 188.5

[profit and loss](#)

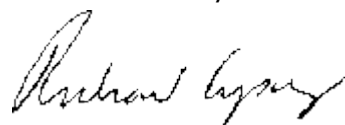
2.27. The reconciliation of gross profit and the basis for the income tax calculation is as follows:

	Year ending	
	12/31/1998 PLN 000's	12/31/1997 PLN 000's
Gross profit in the financial statements	27 383.0	22 552.5
Costs not allowed for tax	12 439.3	10 312.7
- provisions	7 639.7	4 186.6
- accrued interest	1 920.3	2 354.9
- other	2 879.3	3 771.2
Incomes not treated as taxable	(11 091.0)	(10 769.5)
- accrued interest	768.5	(6 483.9)
- provisions	(3 601.5)	(3 047.7)
- foreign exchange rate differences	(7 466.8)	805.4
- other	(791.2)	(2 043.3)
Other changes	(6 297.6)	(3 743.7)
- investment tax relief	(3 999.9)	(3 313.2)
- investment tax premium	(1 656.6)	-
- donations	(641.1)	(430.5)
Income before taxation	22 433.7	18 352.0
Income tax (38%) 1997	-	6 973.8
Income tax (36%) 1998	8 076.1	-
Deferred tax (36%) 1997	-	1 865.4
Deferred tax (34%) 1998	664.5	-
Total	8 740.6	8 839.2

Chartered Accountant
No. 4979/2575
Hanna Fludra



KPMG Polska Audyt Sp. z o.o.
Partner
Richard Cysarz



Warsaw, March 24, 1999

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PPABank Branches

Head Office

Address ul. K. Kordylewskiego 11
31-547 Kraków

Phone (48 12) 618 33 33

Fax (48 12) 618 33 44

E-mail ppabank@ppabank.com.pl

Internet: <http://www.ppabank.com.pl/>

Branch in Czestochowa

Address ul. ks. J. Popieluszki 2
42-200 Czestochowa

Phone (48 34) 365 68 77

Fax (48 34) 365 68 88

Branch in Gdynia

Address Pl. Kaszubski 8
81-350 Gdynia

Phone (48 58) 661 74 72

Fax (48 58) 661 74 76

Branch in Katowice

Address ul. Piotra Skargi 2
40-951 Katowice

Phone (48 32) 203 77 23

Fax (48 32) 206 24 08

1st Branch in Kraków

Address ul. K. Kordylewskiego 11
31-547 Kraków

Phone (48 12) 618 34 55

Fax (48 12) 618 34 66

3rd Branch in Kraków

Address al. Marszałka F. Focha 1
30-111 Kraków

Phone (48 12) 423 14 74

Fax (48 12) 422 68 54

Agency of the 3rd Branch in Kraków

Address ul. Ciepłownicza 1
31-587 Kraków

Phone (48 12) 644 92 27

Fax (48 12) 644 92 27

Branch in Lublin

Address ul. Probostwo 6a
20-089 Lublin

Phone (48 81) 534 68 11

Fax (48 81) 534 64 74

Branch in Lodz

Address ul. S. Zeromskiego 96
90-550 Lodz

Phone (48 42) 637 13 40

Fax (48 42) 637 22 78

Branch in Poznan

Address ul. Wierzbicice 1
61-569 Poznan

Phone (48 61) 833 05 97

Fax (48 61) 833 08 37

Branch in Warsaw

Address ul. Fredry 8
00-097 Warszawa

Phone (48 22) 829 97 00

Fax (48 22) 829 97 95

1st Sub-branch of the Branch in Warsaw

Address ul. Cypryjska 2a
02-761 Warszawa

Tel/Fax (48 22) 642 11 43

2nd Sub-branch of the Branch in Warsaw

Address ul. Marynarska 13
02-674 Warszawa

Phone (48 22) 541 18 88

Fax (48 22) 541 18 89

Branch in Wroclaw

Address ul. Ruska 20/21
50-079 Wroclaw

Phone (48 71) 346 09 24

Fax (48 71) 346 09 23

Branch in Zakopane

Address ul. T. Kosciuszki 11
34-500 Zakopane

Phone (48 18) 201 32 46

Fax (48 18) 201 32 49

Representative Office in Gliwice

Address ul. I. Daszynskiego 5
44-100 Gliwice

Phone (48 32) 231 80 00

Fax (48 32) 231 80 93

Representative Office in Szczecin

Address ul. J. Matejki 22
70-530 Szczecin

Phone (48 91) 489 21 92

Fax (48 91) 489 21 91

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