

Powszechna Kasa Oszczędności Bank Polski SA

**Independent Registered Auditor's Report
on the financial statements
as at and for year ended 31 December 2008**

**Independent Registered Auditor's Report on the financial statements
as at and for year ended 31 December 2008
To the General Shareholders' Meeting and the Supervisory Board of
Powszechna Kasa Oszczędności Bank Polski SA**

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Powszechna Kasa Oszczędności Bank Polski SA **Independent Registered Auditor's Report on the financial statements** **as at and for year ended 31 December 2008**

I. General information about the Bank

- (a) The Bank was established in 1919 as Pocztaowa Kasa Oszczędnościowa (Postal Savings Bank).

In 1950, the Bank started operating as Powszechna Kasa Oszczędności Bank Państwowy (state-owned bank). On 18 January 2000, on the basis of a Decree of the Council of Ministers, Powszechna Kasa Oszczędności Bank Państwowy was transformed into a joint-stock company wholly owned by the State Treasury, under the name of Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna. On 12 April 2000, the Bank was entered in the Business Register maintained by the District Court for the City of Warsaw, Business Court, 16th Registration Division. Currently, the Bank is registered under the number KRS0000026438, and the District Court for the City of Warsaw, 13th Business Division of the National Court Register is the competent registration court.

The Bank was assigned a tax identification number (NIP) 525-000-77-38 for the purpose of making tax settlements. The Bank was assigned a REGON number 016298263 for statistical purposes.

- (b) As at 31 December 2008, the Bank's registered share capital amounted to PLN 1,000,000 thousand and comprised 1,000,000,000 shares with PLN 1 par value each, including:
- 510,000,000 series A registered shares;
 - 105,000,000 series B registered shares;
 - 385,000,000 series C bearer shares;
- (c) Based on art. 111 of the Act on trading in financial instruments dated 29 July 2005, the Bank conducts brokerage activities through a separate organizational unit (a branch office) of Powszechna Kasa Oszczędności Bank Polski Spółka Akcyjna Oddział – Dom Maklerski PKO Banku Polskiego w Warszawie, with its registered office in Warsaw (hereinafter referred to as “the Brokerage House of PKO BP SA”).

The Brokerage House of PKO BP SA has existed since 1991. Based on Resolution No. 17/91 of the Polish Securities Exchange Commission dated 26 August 1991, the Brokerage House of PKO BP SA obtained a license for public trading in securities. By Resolution No. 24/91 of Giełda Papierów Wartościowych w Warszawie SA (the Warsaw Stock Exchange) dated 26 September 1991, the Brokerage House of PKO BP SA was entered in the register of direct participants of the National Depository for Securities.

- (d) In the audited year, the Bank performed activities typical for a universal bank. At the same time, the Bank carried out brokerage activities through the Brokerage House of PKO BP SA.

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I. General information about the Bank (cont.)

(e) In the financial year, the Management Board of the Bank comprised:

Jerzy Pruski	President of the Management Board	from 20 May 2008
Bartosz Drabikowski	Vice-president of the Management Board	from 20 May 2008
Krzysztof Dresler	Vice-president of the Management Board	from 1 July 2008
Tomasz Mironczuk	Vice-president of the Management Board	from 20 May 2008
Mariusz Klimczak	Vice-president of the Management Board	to 30 September 2008
Jarosław Myjak	Vice-president of the Management Board	from 15 December 2008
Wojciech Papierak	Vice-president of the Management Board	from 1 July 2008
Mariusz Zarzycki	Vice-president of the Management Board	from 1 September 2008
Rafał Juszcak	President of the Management Board	to 20 May 2008
Berenika Duda-Uhryn	Vice-president of the Management Board	to 20 May 2008
Robert Działak	Vice-president of the Management Board	to 20 May 2008
Wojciech Kwiatkowski	Vice-president of the Management Board	to 20 May 2008
Aldona Michalak	Vice-president of the Management Board	to 20 May 2008
Adam Skowroński	Vice-president of the Management Board	to 20 May 2008
Stefan Świątkowski	Vice-president of the Management Board	to 20 May 2008

(f) As of the balance date there were the following related parties to the Bank:

Powszechne Towarzystwo Emerytalne BANKOWY SA	- subsidiary
Centrum Finansowe Puławska Sp. z o.o.	- subsidiary
PKO Inwestycje Sp. z o.o.	- subsidiary
Inteligo Financial Services SA	- subsidiary
Centrum Elektronicznych Usług Płatniczych eService SA	- subsidiary
Bankowy Fundusz Leasingowy SA	- subsidiary
Bankowe Towarzystwo Kapitałowe SA	- subsidiary
PKO Towarzystwo Funduszy Inwestycyjnych SA	- subsidiary
KREDOBANK SA	- subsidiary
PKO Finance AB	- subsidiary
Centrum Haffnera Sp. z o.o.	- jointly controlled entity
Centrum Obsługi Biznesu Sp. z o.o.	- jointly controlled entity
Bank Poczty SA	- associate
Kolej Gondolowa Jaworzyna Krynicka SA	- associate
Ekogips SA (in liquidation)	- associate
Poznański Fundusz Poręczeń Kredytowych Sp. z o.o.	- associate
Agencja Inwestycyjna CORP S.A.	- associate

and companies being members of the capital groups of PKO Inwestycje Sp. z o.o., Bankowy Fundusz Leasingowy SA and Powszechne Towarzystwo Emerytalne BANKOWY SA.

(g) The Bank is an issuer of securities admitted to trading on the Warsaw Stock Exchange. Taking advantage of an option permitted by the Act, since 2005 the Company has been preparing its financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union.

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I. General information about the Bank (cont.)

- (h) As the Parent of the Group, the Bank has also prepared consolidated financial statements according to IFRS as adopted by the European Union as at 31.12.2008. To better understand the Bank's financial position and its results of operations as the parent company, the financial statements should be read in conjunction with the consolidated financial statement.
- (i)

Powszechna Kasa Oszczędności Bank Polski SA **Independent Registered Auditor's Report on the financial statements** **as at and for year ended 31 December 2008**

II. Information about the audit

- (a) PricewaterhouseCoopers Sp. z o.o. was appointed registered auditor to the Bank by Resolution No. 3 of the Supervisory Board dated 17 April 2008, on the basis of paragraph 15, clause 1, item 3, of the Bank's Memorandum of Association.
- (b) PricewaterhouseCoopers Sp. z o.o. and the registered auditor conducting the audit are independent of the audited entity as defined by the Article 66, clause 2 of the Accounting Act.
- (c) The audit was conducted in accordance with an agreement dated 12 May 2008, in the following periods:
 - Interim audit from 13 October to 12 December 2008;
 - Final audit from 12 January to 8 April 2009.

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III. The Bank's results and financial position

The financial statements do not take account of inflation. The consumer price index (on a December to December basis) amounted to 3.3% in the audited year (4.0% in 2007).

The observations below are based on knowledge obtained during the audit of the financial statements.

- As at the balance date, total assets amounted to PLN 131,244,827 thousand and increased by PLN 25,904,573 thousand (25%) compared with 31 December 2007. The increase was financed mainly by the increase in amounts due to customers of PLN 16,641,467 thousand (20%), an increase in liabilities arising on the valuation of derivative instruments (of PLN 4,870,072 thousand, i.e. 380%), an increase in amounts due from banks (of PLN 2,074,997 thousand, i.e. 57%) and the increase in equity of PLN 1,799,831 thousand (15%).
- The balance of amounts due to customers as at the balance date amounted to PLN 101,856,930 thousand and accounted for 78% of total assets (a decrease of 3 p.p. compared with 31 December 2007). The change in the balance of amounts due to customers was mainly due to a significant increase in amounts due to retail customers (of PLN 10,124,892 thousand, i.e. 16% compared with 31 December 2007) and to corporate customers (of PLN 3,925,167 thousand, i.e. 26% compared with 31 December 2007) – see Note 14.
- Liabilities arising on the valuation of derivatives amounted to PLN 6,150,337 thousand as at the end of 2008. The increase in the balance as at the balance date was mainly due to an increased volume of transactions concluded and the developments in the forex market in the second half of 2008 (Note 13).
- The balance of amounts due to banks amounted to PLN 5,699,452 thousand as at the balance date and comprised mainly loans and advances received, denominated in USD, of PLN 2,656,004 thousand, and deposits from other banks of PLN 2,835,727 thousand. The change of PLN 2,074,997 thousand (57%) compared with 31 December 2007 was mainly due to an increase in the balance of deposits accepted (of PLN 1,399,050 thousand, i.e. 97%) and an increase in the valuation of loans received, reflecting the weakening of the Polish currency against US dollar (of PLN 606,728 thousand, i.e. 30%).
- As at 31 December 2008, the equity amounted to PLN 13,529,372 thousand (PLN 11,729,541 thousand as at 31 December 2007). The increase in equity of PLN 1,799,831 thousand (15%) was due to transferring a part of the net profit for 2007 (of PLN 1,624,991 thousand) to supplementary capital (Note 18).
- The value of regulatory capital amounted to PLN 12,389,193 thousand as at 31 December 2008 (PLN 9,543,342 thousand as at 31 December 2007) and exceeded the total capital requirement by PLN 3,567,353 thousand (PLN 8,821.840 at the end of 2008). The solvency ratio calculated as at the balance date based on the banking and trading portfolios amounted to 11.24% and decreased by 0.63 p.p. compared with the end of the prior year.

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III. The Bank's results and financial position (cont.)

- A higher level of financing was reflected mainly in an increase, as at the balance date, in the balance of loans and advances to customers (of PLN 24,279,826 thousand, i.e. 33%), in investment securities (of PLN 2,914,958 thousand, i.e. 50%) and in receivables arising on the valuation of derivatives (of PLN 2,042,795, i.e. 131%).
- As at the balance date, loans and advances to customers amounted to PLN 98,102,019 thousand and accounted for 75% of total assets (an increase of 5 p.p. compared with the end of 2007). The gross value of the loan portfolio amounted to PLN 100,702,559 thousand as at the balance date and increased by PLN 24,573,638 thousand (32%) compared with 31 December 2007. The major portion of the increase (33%) related to mortgage loans for retail customers (Note 6).
- The quality of the loan portfolio, measured with reference to the share of impaired loans in total gross loans, improved slightly compared with the end of 2007. As at 31 December 2008, the share of impaired loans in total loans was 3.1% (3.0% as at 31 December 2007). At the same time, the coverage of impaired loans with impairment allowances was 61.0% as at 31 December 2008 and decreased by 18.0 p.p. compared with the end of the prior year. It was possible to maintain the quality of the loan portfolio at an unchanged level because of a significant increase in the value of the loan portfolio (a gross increase of 32%) resulting from intensified sales activities.
- The increase in the balance of available-for-sale investment securities to PLN 8,756,511 thousand as at the balance date resulted mainly from an increase in the Bank's exposure to bonds issued by the State Treasury (an increase of PLN 2,193,163 thousand, i.e. 201% compared with 31 December 2007).
- The balance of financial assets designated at fair value through profit or loss as at the balance date amounted to PLN 4,546,497 thousand. The decrease in the balance resulted mainly due to a decrease in the Bank's exposure to Treasury bonds (of 4,908,050 thousand, i.e. 68% compared with 31 December 2007) and bonds issued by other banks (of PLN 591,142 thousand, i.e. 77%).
- The decrease in amounts due from banks of PLN 1,408,826 thousand to PLN 3,906,973 thousand as at the balance date was mainly due to a significant decrease in deposits with other banks (of PLN 2,615,342 thousand, i.e. 55%), partly compensated by a higher balance of amounts due in respect of repo transactions (a more than fourfold increase, of PLN 588,803 thousand) and an increase in the balance of loans granted to other banks (mainly new loans granted to KREDOBANK SA totalling PLN 545,818 thousand). A decrease in amounts due from banks was accompanied with placements of surplus cash with the Central Bank (an increase in the balance of PLN 1,164,164 thousand to PLN 5,758,248).

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III. The Bank's results and financial position (cont.)

- Bank's 1-month and 3-month liquidity ratios calculated on the basis of data about assets receivable and liabilities payable adjusted to real terms amounted to 1.49 and 1.29 respectively (in 2007 2.83 for both terms). The decrease in the ratios values in 2008 resulted from a significant increase in liabilities classified as with maturity up to one month, mainly amounts due to customers and liabilities due to valuation of derivative instruments.
- The operating profit for 2008 amounted to PLN 3,697,850 thousand and was PLN 370,705 thousand, i.e. 11%, higher than in 2007. The operating profit had the following major components: net interest income of PLN 5,968,083 thousand, net fee and commission income of PLN 2,132,815 thousand and net foreign exchange gains of PLN 734,567 thousand. At the same time, items decreasing the operating profit included administrative expenses of PLN 3,969,247 thousand and the net impairment allowance charge of PLN 1,148,930 thousand in 2008.
- Regardless of the fact that in 2008, the interest margin (calculated as the ratio of net interest income to interest income) decreased by 3 p.p. compared with 2007, net interest income in the audited year was 1,464,976 thousand (33%) higher than in the prior year. This was mainly due to an increase in interest income relating to increased lending in 2008. In addition, the rate of interest income on interest-bearing assets increased by 0.4 p.p. and amounted to 8.0% in 2008. The cost of borrowing decreased (from 2.0% in 2007 to 2.7% in 2008) (Note 19).
- Fee and commission income amounted to PLN 2,813,078 thousand in 2008 and increased by PLN 164,986 thousand (6%) compared with 2007, mainly due to an increase in fees and commissions relating to payment cards (of PLN 146,851 thousand, i.e. 21%). Given that fee and commission costs in 2008 increased by PLN 25,943 thousand (or 4%) compared with 2007 (to a level of PLN 680,263 thousand), this resulted in an increase in net fee and commission income for 2008 of PLN 139,043 thousand (7%) compared with 2007, which amounted to PLN 2,678,343 thousand.
- In 2008, net foreign exchange gains increased significantly, by PLN 211,874 thousand (41%) to PLN 734,567 thousand. Foreign exchange differences on revaluation of assets and liabilities in foreign currencies increased more than eleven fold in the audited years and amounted to PLN 2,942,413 thousand (PLN 267,248 thousand in 2007). The increase was partly offset by net losses on the valuation of derivatives, mainly cross-currency interest rate swaps (CIRS), used primarily for managing interest rate and currency risks, amounting to PLN 2,207,846 thousand (in 2007: net gains on the valuation of PLN 255,445 thousand) (Note 23).

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III. The Bank's results and financial position (cont.)

- Net impairment allowance charge also increased by PLN 1,103,982 thousand (a more than 25-fold increase). In 2008, it amounted to PLN 1,148,930 thousand. An impairment allowance of PLN 356,101 thousand recognized in respect of investment in a subsidiary, KREDOBANK SA, in 2008 was the most important factor contributing to the level of net impairment allowance charge. The change in the balance of net impairment allowance charge in 2008 was also due to an increase in the impairment allowance for corporate loans - by PLN 387,823 thousand (i.e. 528%), and consumer loans - by PLN 171,671 (i.e. 74%) (Note 26).
- The larger scale of the Bank's activities in 2008 resulted in an increase in administrative expenses of PLN 283,824 thousand (8%) to the level of PLN 3,969,247 thousand. The increase was mainly due to an increase in overheads of PLN 131,230 thousand (12%) to PLN 1,270,174 thousand and in costs of employee benefits of PLN 114,427 thousand (5%) to PLN 2,269,539 thousand. The overall effectiveness calculated as the ratio of costs to income (C/I) improved in 2008. The C/I ratio in 2008 was 45% and it was 7 p.p. lower than in 2007 (Note 27).
- Gross profitability (measured as the ratio of profit before tax to total income) amounted to 29.6% in the audited year and decreased by 5 p.p. compared with the prior year.
- The income tax expense for 2008 amounted to PLN 816,590 thousand. The effective tax rate for 2008 was 22% and was 4 p.p. higher than in 2007. As a result, in 2008 the Bank recorded a net profit of PLN 2,881,260 thousand, which was PLN 161,269 thousand (6%) higher comparing with 2007. In 2008, net profitability amounted to 23.1% (28.3% in 2007).
- The return on assets (calculated as the ratio of the net profit to average total assets) was 2.4% in 2008 and decreased by 0.3 p.p. compared with 2007. The return on equity in 2008 was also 2.2 p.p. lower, and amounted to 22.8% in the audited year.

The financial statements of the Bank have been prepared in accordance with the going concern principle.

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IV. Discussion of financial statement components

BALANCE SHEET as at 31 December 2008

	Notes	31.12.2008	31.12.2007	Change	31.12.2008	31.12.2007	Change	Structure (%)	Structure (%)
ASSETS		PLN thousand	PLN thousand	PLN thousand	PLN thousand	PLN thousand	(%)		
Cash and balances with the Central Bank	1.	5,758,248	4,594,084	1,164,164			25	4	4
Amounts due from banks	2.	3,906,973	5,315,799	(1,408,826)			(27)	3	5
Trading assets	3.	1,496,147	1,202,919	293,228			24	1	1
Derivative financial instruments	4.	3,599,545	1,556,750	2,042,795			131	3	2
Financial assets designated at fair value through profit or loss	5.	4,546,497	8,101,534	(3,555,037)			(44)	3	8
Loans and advances to customers	6.	98,102,019	73,822,193	24,279,826			33	75	70
Investment securities available for sale	7.	8,756,511	5,841,553	2,914,958			50	7	6
Investments in subsidiaries, jointly controlled entities and associates	8.	823,518	1,054,395	(230,877)			(22)	1	1
Intangible assets	9.	1,155,042	927,610	227,432			25	1	1
Tangible fixed assets	10.	2,462,967	2,270,480	192,487			8	2	2
Current income tax receivables		-	187,707	(187,707)			(100)	-	-
Deferred income tax asset	28.	166,803	35,531	131,272			369	-	-
Other assets	11.	470,557	429,699	40,858			10	-	-
Total assets		131,244,827	105,340,254	25,904,573			25	100	100

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IV. Discussion of financial statement components

BALANCE SHEET as at 31 December 2008 (cont.)

	Notes	31.12.2008 PLN thousand	31.12.2007 PLN thousand	Change PLN thousand	Change (%)	31.12.2008 Structure (%)	31.12.2007 Structure (%)
EQUITY AND LIABILITIES							
Amounts due to the Central Bank		2,816	1,279	1,537	120	-	-
Amounts due to other banks	12.	5,699,452	3,624,455	2,074,997	57	4	3
Derivative financial instruments	13.	6,150,337	1,280,265	4,870,072	380	5	1
Amounts due to customers	14.	101,856,930	85,215,463	16,641,467	20	78	81
Subordinated liabilities	15.	1,618,755	1,614,885	3,870	-	1	2
Other liabilities	16.	1,355,396	1,421,321	(65,925)	(5)	1	1
Current income tax liabilities		470,416	-	470,416	-	-	-
Provisions	17.	561,353	453,045	108,308	24	1	-
Total liabilities		117,715,455	93,610,713	24,104,742	26	90	88
Share capital		1,000,000	1,000,000	-	-	1	1
Other capital		9,648,112	8,009,550	1,638,562	20	7	8
Net profit for the year		2,881,260	2,719,991	161,269	6	2	3
Total equity	18.	13,529,372	11,729,541	1,799,831	15	10	12
Total equity and liabilities		131,244,827	105,340,254	25,904,573	25	100	100

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IV. Discussion of financial statement components (cont.)

INCOME STATEMENT
for the year ended 31 December 2008

	Notes	2008	2007	Change	2008	2007	Change	2008	2007
		PLN thousand	PLN thousand	PLN thousand	Structure (%)	Structure (%)	Structure (%)	Structure (%)	Structure (%)
Interest and similar income		8,646,426	6,245,091	2,401,335	38	69	38	65	65
Interest expense and similar charges		(2,678,343)	(1,741,984)	(936,359)	54	31	54	28	28
Net interest income	19.	5,968,083	4,503,107	1,464,976	33		33		
Fee and commission income		2,813,078	2,648,092	164,986	6	23	6	28	28
Fee and commission expense		(680,263)	(654,320)	(25,943)	4	8	4	10	10
Net fee and commission income	20.	2,132,815	1,993,772	139,043	7		7		
Dividend income	21.	130,896	52,113	78,783	151	1	151	1	1
Net income from financial instruments at fair value through profit or loss	22.	(195,430)	(76,746)	(118,684)	155	2	155	2	1
Gains less losses from investment securities		(951)	6,521	(7,472)	(115)	-	(115)	-	-
Net foreign exchange gains	23.	734,567	522,693	211,874	41	6	41	5	5
Other operating income	24.	160,736	140,607	20,129	14	1	14	1	1
Other operating expenses	25.	(114,689)	(84,551)	(30,138)	36	1	36	1	1
Net impairment allowance charge	26.	(1,148,930)	(44,948)	(1,103,982)	2,456	13	2,456	13	1
Administrative expenses	27.	(3,969,247)	(3,685,423)	(283,824)	8	45	8	45	59
Operating profit / Profit before income tax		3,697,850	3,327,145	370,705	11		11		
Income tax expense	28.	(816,590)	(607,154)	(209,436)	34		34		
Net profit		2,881,260	2,719,991	161,269	6		6		
Total income		12,485,703	9,615,117	2,870,586	30	100	30	100	100
Total expenses		(8,787,853)	(6,287,972)	(2,499,881)	40	100	40	100	100
Profit before income tax		3,697,850	3,327,145	370,705	11		11		

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IV. Discussion of financial statement components (cont.)

Selected ratios summarising the Bank's financial position and results

The following ratios characterize the Bank's activities, results of operations during the audited year and its financial position as at the balance date compared with the prior year (1):

	2008	2007
Profitability ratios:		
Gross profitability (profit before tax / total income)	29.6%	34.6%
Net profitability (net profit/ total income)	23.1%	28.3%
Return on equity (net profit for the year/ average net assets) (2)	22.8%	25.0%
Return on assets (net profit for the year / average total assets) (2)	2.4%	2.7%
Profitability ratio on interest-bearing assets (interest income / average interest-bearing assets) (2)	8.0%	6.6%
Cost / Income ratio (Administrative expenses / the result on banking operation) (3)	45%	52%
Cost of borrowings (interest expenses / average interest bearing liabilities) (2)	2.7%	2.0%
Quality of assets:		
Interest-bearing assets to total assets (4)	91.6%	92.3%
Gross impaired loans to total gross loans	3.1%	3.0%
Impairment allowances on impaired loans and advances to customers to impaired loans and advances to customers	61.0%	79.0%
Liquidity ratio:		
Liquidity I (assets due within 1 month/liabilities due within 1 month) (5)	1.49	2.83
Liquidity II (assets due within 3 months/liabilities due within 3 months) (5)	1.29	2.83
Other ratios:		
Solvency ratio	11.24%	11.87%
Regulatory capital (PLN thousand)	12,389,193	9,543,342
Total capital requirement (PLN thousand)	8,821,840	6,431,473

(1) Individual ratio percentage may differ from those presented in the financial statements due to applying a different method for their calculation.

(2) Average balances of the balance sheet items were calculated on the basis of individual balances as at the beginning and end of the current and previous years

(3) The result on banking operations defined as the operating result less the administrative expenses and net of impairment charge for loans and advances

(4) Interest-bearing assets defined as balances with the central bank (excluding cash), loans and advances to banks and customers, investment and trading securities.

(5) Liquidity ratios are calculated based on undiscounted cash flows, according to their contractual maturities as at the balance date.

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IV. Discussion of financial statement components (cont.)

Balance sheet as at 31 December 2008

1. Cash and balances with Central Bank

As at 31 December 2008, cash and balances with the Central Bank amounted to PLN 5,758,248 thousand (PLN 4,594,084 thousand at the end of 2007). Of this amount, PLN 3,419,832 thousand were balances maintained in its account with the National Bank of Poland (PLN 2,972,067 thousand as at 31 December 2007).

At the balance date, the Bank calculated and maintained the mandatory reserve in accordance with Resolution No. 15/2004 of the Management Board of the National Bank of Poland dated 13 April 2004 on the principles and method of calculating and maintaining mandatory reserves by banks. The declared mandatory reserve to be maintained in December 2008 amounted to PLN 3,519,554 thousand (in December 2007: PLN 2,885,695 thousand).

2. Amounts due from banks

The balances of and movements in, amounts due from banks as at respective balance dates are as follows:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Deposits with other banks	2,108,482	4,723,824	(2,615,342)	(55)
Loans and advances	940,197	513,629	454,635	89
Receivables due from repurchase agreements	603,200	14,397	588,803	4,090
Current accounts	247,292	49,846	197,446	396
Receivables due from unsettled transactions	28,067	-	28,067	-
Cash in transit	7,846	14,379	(6,533)	(45)
Total	3,935,084	5,316,075	(1,380,991)	(26)
Impairment allowances	(28,111)	(276)	(27,835)	10,085
Net total	3,906,973	5,315,799	(1,408,826)	(27)

As at 31 December 2008, 54% of the balance related to deposits with other banks (89% of the balance as at 31 December 2007). Within the balance of amounts due from banks, PLN 698,501 thousand (18%) related to loans granted to KREDOBANK SA (PLN 205,296 thousand, i.e. 4%, at the end of 2007).

Within the balance of deposits with other banks, 82% comprised deposits with banks having a rating above A- (97% as at 31 December 2007).

Receivables due from unsettled transactions of PLN 28,067 thousand relate almost entirely to transactions with derivative instruments declared as default. An impairment allowance covering 100% of these transactions was recognized. Amounts denominated in foreign currencies represented 73% of the balance (55% as at 31 December 2007).

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IV. Discussion of financial statement components (cont.)

3. Trading assets

The balance of trading assets as at 31 December 2008, amounting to PLN 1,496,147 thousand, comprised the following assets:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Treasury bills	772,803	60,172	712,631	1,184
Treasury bonds denominated in PLN	699,119	1,125,562	(426,443)	(38)
Treasury bonds denominated in EUR	19,476	7,395	12,081	163
Other	4,749	9,790	(5,041)	(51)
Total	1,496,147	1,202,919	293,228	24

The increase in the value of financial assets held for trading of PLN 293,228 thousand (24%) as at the balance date was mainly due to the Bank's increasing exposure to Treasury bills combined with a decreasing exposure to bonds. A particularly significant increase in the value of Treasury bills in the portfolio of financial assets held for trading occurred in December 2008 (an increase of PLN 490,349 compared with November). Changes in the structure of the securities portfolio reflect the Bank's intention to invest in securities which are safe, ensure a stable rate of return and are not sensitive to fluctuations in market prices.

4. Derivative financial instruments

The balance of receivables arising on the valuation of derivative instruments increased more than twofold compared with 2007. As at 31 December 2008, it amounted to PLN 3,599,545 thousand and included the following items:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Interest Rate Swap (IRS)	2,786,213	1,439,884	1,346,329	94
- including CIRS	56,290	410,927	(354,637)	(86)
Currency and equity option	575,003	15,528	559,475	3,603
FX Forward	226,705	101,338	125,367	124
Other	11,624	-	11,624	-
Total	3,599,545	1,556,750	2,042,795	131

The increase in receivables arising on the valuation of interest rate swaps of 94% compared with 31 December 2007 resulted from the Bank intensifying sales of instruments used for hedging against interest rate and currency risks, mainly to the segment of corporate customers.

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IV. Discussion of financial statement components

4. Derivative financial instruments (cont.)

The increase in receivables arising on the valuation of options (mainly currency options) of PLN 559,475 thousand and the twofold increase in receivables arising on the valuation of forward currency transactions resulted from a significant increase in sales of hedging instruments in 2008. The developments in the forex market in the fourth quarter of 2008 resulted in a significant increase in receivables arising on the valuation of these transactions. The valuation of assets arising on derivative transactions as at the balance date includes a fair value adjustment resulting from an analysis of counterparty credit risk, amounting to PLN 115,448 thousand.

5. Financial assets designated at fair value through profit or loss

The balance of financial assets designated at fair value through profit or loss decreased by nearly a half (44%) compared with the end of 2007 and amounted to PLN 4,546,497 thousand as at 31 December 2008. The balance comprises the following assets:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Treasury bills	2,060,454	-	2,060,454	-
Treasury bonds	2,313,167	7,221,217	(4,908,050)	(68)
Foreign bonds	172,876	880,317	(707,441)	(80)
Total	<u>4,546,497</u>	<u>8,101,534</u>	<u>(3,555,037)</u>	<u>(44)</u>

A decrease in the balance of financial assets designated at fair value through profit or loss as at the balance date resulted mainly from the Bank's lower exposure to Treasury bonds, combined with a higher exposure to Treasury bills. During the audited year the Bank gradually reduced its portfolio of Treasury bonds, as part of its liquidity management activities and the financing of lending activities. An increase in the exposure to Treasury bills occurred in the last quarter of the year and reflected the Bank's efforts to invest surplus liquidity in liquid assets which ensure a stable rate of return and are risk-free. At the same time, throughout 2008, the Bank gradually increased its portfolio of foreign bonds issued by banks (a change of PLN 591,142 thousand). This change was due to macroeconomic developments which resulted in an increase in issuer's credit risk and the disappearance of liquidity in the banking debt securities market.

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IV. Discussion of financial statement components (cont.)

6. Loans and advances to customers

a) Structure of the loan portfolio, by type

As at the balance date, the gross loan portfolio comprised:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Financial sector (without banks)	2,592,355	1,508,977	1,083,378	72
Corporate loans	2,592,355	1,508,977	1,083,378	72
Non-Financial sector	94,894,814	70,940,466	23,954,348	34
Consumer loans	20,712,187	18,347,196	2,364,991	13
Mortgage loans	45,524,822	33,099,986	12,424,836	38
Corporate loans	28,657,805	19,493,284	9,164,521	47
Public sector	3,215,390	3,679,478	(464,088)	(13)
Corporate loans	3,215,390	3,679,478	(464,088)	(13)
Loans and advances – gross	100,702,559	76,128,921	24,573,638	32
Impairment allowances	(2,600,540)	(2,306,728)	(293,812)	13
Loans and advances – net	98,102,019	73,822,193	24,279,826	33

As at the balance date, PLN 27,145,521 thousand represented receivables in foreign currencies, gross (PLN 14,736,858 thousand as at 31 December 2007). Of this amount, 82% were amounts in Swiss francs (81% as at 31 December 2007). The Bank's share in the total loan and advances (net) of the banking sector (including cooperative banks) amounted to 16%.

b) Quality of the Bank's loan portfolio

	31.12.2008	31.12.2007	31.12.2008 Structure	31.12.2007 Structure
	PLN thousand	PLN thousand	%	%
Impaired loans	3,161,595	2,317,186	3.1%	3.0%
Non-impaired loans	97,540,964	73,811,735	96.9%	97.0%
Loans and advances - gross	100,702,559	76,128,921	100.0%	100.0%
Impairment allowances for identified loss	(1,928,032)	(1,831,055)	74.1%	79.4%
Allowance for incurred but not reported loss (IBNR)	(672,508)	(475,673)	25.9%	20.6%
Total impairment allowances	(2,600,540)	(2,306,728)	100.0%	100.0%
Loans and advances – net	98,102,019	73,822,193		

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IV. Discussion of financial statement components

6. Loans and advances to customers

b) Quality of the Bank's loan portfolio (cont.)

In 2008 the Bank sold a part of the portfolio of loans and advances to customers (balance and off-balance items) classified as impaired loans. The total gross amount of the sold portfolio amounted to PLN 493,773 thousand.

The quality of the loan portfolio as at the balance date, measured with reference to the proportion of impaired loans, deteriorated compared with the end of 2007 and amounted to 3.1% (3.0% in 2008). At the same time, the coverage of impaired loans with impairment allowances decreased by 18 p.p. to 61.0%. Maintaining the quality of the loan portfolio at an almost unchanged level, despite the fact that additional impairment allowances of PLN 293,812 thousand were recognized, was possible due to the significant growth of the loan portfolio (an increase of PLN 24,573,638 thousand, i.e. 32% compared with 31 December 2007) resulting from intensified sales, particularly in the first three quarters of 2008. Moreover, the share of allowances for incurred but not reported losses (IBNR) in total impairment allowances was higher than in the prior year. It amounted to 25.9% as at the balance date (20.6% as at 31 December 2007).

7. Investment securities available for sale

As at 31 December 2008, the balance of investment securities available for sale amounted to PLN 8,756,511 thousand (PLN 5,841,553 thousand as at the end of the prior year), which represented an increase of PLN 2,914,958 thousand i.e. 50% compared with 31 December 2007.

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Treasury bonds	3,286,726	1,093,563	2,193,163	201
Bonds issued by the central bank, NBP	2,673,729	2,633,505	40,224	2
Municipal bonds	1,418,099	1,176,047	242,052	21
Corporate bonds	1,184,934	852,031	332,903	39
Foreign bonds	122,200	-	122,200	-
Listed equity instruments	65,939	79,350	(13,411)	(17)
Other	4,884	7,057	(2,173)	(31)
Total	8,756,511	5,841,553	2,914,958	50

The change in the balance as at the balance date resulted mainly from the Bank's increased exposure to Treasury bonds (by PLN 2,193,263 thousand). The increase was mainly due to the fact that in the audited year, the Bank purchased Treasury bonds with a fixed interest rate and maturing in 2010 (10-year bonds with a nominal value of PLN 1,580,000 thousand and 5-year bonds with a nominal value of PLN 350,000 thousand). Moreover, in 2008 the Bank purchased Treasury bonds denominated in EUR and USD, with a nominal value of EUR 30,000 thousand and USD 30,000 thousand.

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IV. Discussion of financial statement components

7. Investment securities available for sale (cont.)

The balance of corporate and municipal bonds comprises bonds issued by companies and local authorities. The Bank acted as an underwriter for these bonds. The increase in the balances of both corporate and municipal bonds resulted from the large number of new issues in the first three quarters of 2008.

The balance of foreign bonds includes bonds denominated in EUR, purchased by the Bank in 2008.

8. Investments in subsidiaries, jointly controlled entities and associates

As at 31 December 2008, the balance of investments in subsidiaries, jointly controlled entities and associates amounted to PLN 823,518 thousand and decreased by PLN 230,877 thousand compared with 2007.

In accordance with IAS 27.37a, investments in subsidiaries, jointly controlled entities and associates are valued at cost, less any impairment.

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Subsidiaries	600,805	877,997	(277,192)	(32)
- value at cost	918,835	888,702	30,133	3
- allowance for impairment losses	(318,030)	(10,705)	(307,325)	2.871
Jointly controlled entities	61,869	61,869	-	-
- value at cost	61,869	61,869	-	-
- allowance for impairment losses	-	-	-	-
Associates	160,844	114,529	46,315	40
- value at cost	168,960	168,960	-	-
- allowance for impairment losses	(8,116)	(54,431)	46,315	(85)
Shares in subsidiaries, jointly controlled entities and associates	823,518	1,054,395	(230,877)	(22)

The decrease in the balance of investment in subsidiaries, jointly controlled entities and associates resulted from, *inter alia*, recognizing impairment allowances of PLN 307,364 for shares in KREDOBANK SA. This was partly offset by a release in impairment allowances for shares in Bank Pocztowy SA (PLN 33,500 thousand) and in Kolej Gondolowa Jaworzyna Krynicka SA (PLN 15,531 thousand).

The impairment allowance of 100% recognized for shares in KREDOBANK SA resulted from an analysis of their recoverable value, performed in connection with a deterioration in the operating environment of banks in the Ukraine in 2008. In the first half of 2008, the Bank released the entire previously recognized allowance for shares in Bank Pocztowy SA. The allowance was released as a result of an impairment test performed using the discounted cash flow method, which showed that the value of this investment exceeded the carrying value, recorded at cost.

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IV. Discussion of financial statement components (cont.)

9. Intangible assets

As at the balance date, intangible assets increased by PLN 227,432 thousand (25%) and comprised:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Software	1,787,570	1,567,880	219,690	14
Other, including capitalised expenses	216,154	131,387	84,767	65
Gross total	2,003,724	1,699,267	304,457	18
Accumulated amortisation	(833,309)	(756,284)	(77,025)	10
Impairment allowance	(15,373)	(15,373)	-	
Net total	1,155,042	927,610	227,432	25

The Integrated Information System (ZSI) with a net book value PLN 577,925 thousand as at the balance date was the largest component of the balance. Total outlays on ZSI amounted to PLN 160,490 thousand.

In the audited year the impairment allowance was not changed and related to unused functionalities of ZSI.

The wear-and-tear of intangible assets, measured as a ratio of accumulated amortization to gross book value was 42% as at the balance date (45% as at 31 December 2007).

10. Tangible fixed assets

As at the balance date, the net book value of tangible fixed assets amounted to PLN 2,462,967 thousand and increased by PLN 192,487 thousand compared with 31 December 2007.

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Equipment and machinery	2,082,754	2,311,757	(229,003)	(10)
Land and buildings	1,954,645	1,922,591	32,054	2
Assets under construction	530,553	271,305	259,248	96
Investment properties	32,009	39,012	(7,003)	(18)
Means of transport	8,101	12,433	(4,332)	(35)
Other	383,710	367,183	16,527	5
Gross value of fixed assets	4,991,772	4,924,281	67,491	1
Accumulated amortisation	(2,526,889)	(2,651,844)	124,955	(5)
Impairment allowance	(1,916)	(1,957)	41	(2)
Net value of fixed assets	2,462,967	2,270,480	192,487	8

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IV. Discussion of financial statement components

10. Tangible fixed assets (cont.)

The change in the balance resulted mainly from new capital expenditure of PLN 432,349 thousand and a decrease in the gross book value of equipment and machinery of PLN 312,932 thousand.

As at 31 December 2008 the impairment allowance amounted to PLN 1,916 thousand and concerned buildings (PLN1,216 thousand) and assets under construction (PLN 700 thousand).

The wear-and-tear of tangible fixed assets measured as the ratio of accumulated depreciation to gross book value was 51% as at the balance date, and decreased by 3 p.p. compared with the end of 2007.

11. Other assets

As at the balance date, other assets increased by PLN 40,858 thousand (10%) and comprised:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Amounts due from customers	157,892	156,938	954	1
Settlements of payment cards transactions	131,974	154,187	(22,213)	(14)
Financial instruments settlements	55,628	24,388	31,240	128
Unregistered capital increase in KREDOBANK	48,737	-	48,737	-
Prepayments	29,729	21,377	8,352	39
Inventory (related to utilization, auxiliary operations and investments)	15,211	9,910	5,301	53
Receivables from the State budget due to distribution of Treasury stamps	8,883	8,373	510	6
Receivables relating to foreign exchange activity	8,628	15,892	(7,264)	(46)
Receivables from securities trading	7,255	6,614	641	10
Other	135,156	98,980	31,520	32
Gross total	599,093	496,659	97,778	20
Impairment allowance	(128,536)	(66,960)	(56,920)	85
Net total	470,557	429,699	40,858	10

As at the balance date, the amount of PLN 111,289 thousand of trade receivables accounted for settlements with a subsidiary company eService SA.

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IV. Discussion of financial statement components

11. Other assets (cont.)

The balance of financial instruments settlements as at the balance date comprised mainly amortization of a premium paid in respect of options purchased amounting to PLN 42,994 thousand (PLN 15,879 thousand as at 31 December 2007).

The impairment allowance as at 31 December 2008 includes an impairment allowance of PLN 48,737 thousand covering 100% of the value of the increase in capital of KREDOBANK SA, unregistered as at the balance date. As at the balance date, other impairment allowances referred to among others trade receivables in the amount of PLN 20,803 thousand and settlements of payment card transactions in the amount of PLN 7,630 thousand.

12. Amounts due to other banks

As at the balance date, amounts due to other banks increased by PLN 2,074,997 thousand (57%) and comprised:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Other banks' deposits	2,835,727	1,436,677	1,399,050	97
Loans and advances	2,656,004	2,049,276	606,728	30
Other money market deposits	115,171	43,502	71,669	165
Current accounts	92,550	95,000	(2,450)	(3)
Total	<u>5,699,452</u>	<u>3,624,455</u>	<u>2,074,997</u>	<u>57</u>

New loans and advances obtained (of PLN 25,000 thousand) only slightly affected the balance. The increase in the balance of loans and advances was primarily due to the appreciation of the Swiss franc, which is the currency of the majority of foreign currency loans and advances obtained by the Bank (84% as at 31 December 2008 and 67% as at 31 December 2007, respectively).

As at the balance date, 55% of the balance represented liabilities in foreign currencies (84% as at 31 December 2007).

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IV. Discussion of financial statement components (cont.)

13. Derivative financial instruments

As at the balance date, liabilities arising on the valuation of derivatives amounted to PLN 6,150,337 thousand and increased by PLN 4,870,072 thousand (380%) compared with the end of 2007.

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Interest Rate Swap (IRS)	5,070,104	1,159,941	3,910,163	337
- including CIRS	2,391,272	200,717	2,190,555	1.091
Currency and equity options	585,414	16,424	568,990	3.464
FX transactions	494,759	103,507	391,252	378
Other	60	393	(333)	(85)
Total	6,150,337	1,280,265	4,870,072	380

The increase in the balance was mainly due to an increase in liabilities arising on the valuation of currency transactions. The Bank follows the principle of closing the majority of transactions concluded with customers on a "back-to-back" basis, i.e. of entering into transactions which are counter to options and currency forwards offered to customers in the interbank market.

At the same time, the Bank hedged its portfolio of foreign currency loans using cross-currency interest rate swaps (CIRS). The increase in liabilities arising on the valuation of these transaction of 337% compared with 31 December 2007 was due to the higher volume of transactions concluded in response to an increase in the portfolio of foreign currency loans and the weakening of the Polish zloty in the second half of 2008.

14. Amounts due to customers

As at the balance date, amounts due to customers increased by PLN 16,641,467 thousand (20%) compared with the end of 2007.

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Amounts due to retail clients	75,413,447	65,288,555	10,124,892	16
Amounts due to corporate entities	19,164,051	15,238,884	3,925,167	26
Amounts due to state budget entities	7,279,432	4,688,024	2,591,408	55
Total	101,856,930	85,215,463	16,641,467	20

In 2008, the Bank pursued a strategy of expanding its deposit base. This objective was achieved by intensified marketing activities addressed mainly to retail customers and by introducing new deposit products offering high interest rates ("9-12-15" deposits, "Progresja" deposits, new 3-months and 6-month deposits and "MaxLokata" deposit).

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IV. Discussion of financial statement components

14. Amounts due to customers (cont.)

In the audited year, the aforementioned activities resulted in the increase of the Bank's deposit base by 20%, which amounted to PLN 101,856,930 thousand as at 31 December 2008. The Bank's share in the total amount of amounts due to customers of the banking sector (including cooperative banks) amounted to 18%.

As at 31 December 2008 the deposits to loan and advances (gross) ratio was improved and amounted to 101% (111% as at the end of previous year)

As at the balance date, 6% of the balance represented liabilities in foreign currencies (7% as at 31 December 2007). Liabilities with a contractual maturity of less than 1 month accounted for 60% of amounts due to customers (72% as at the end of 2007).

15. Subordinated liabilities

The balance of subordinated liabilities as at 31 December 2008 comprised the valuation of subordinated bonds issued by the Bank in 2007, with a nominal value totalling PLN 1,600,700 thousand and a maturity date of 30 October 2017.

The said bonds were issued based on the Act on bonds dated 29 June 1995 with a view to increasing the Bank's supplementary funds, in accordance with art. 127, para. 3, item 3b of the Banking Law. The value of bonds as at 31 December 2008 increased by PLN 3,870 thousand compared with the end of 2007 as a result of an increase in the value of interest accrued, not due, following an increase in the interest rate on these bonds to 7.88% (6.35% as at 31 December 2007)

In accordance with Decision No. 91 of the Banking Supervision Commission dated 5 December 2007, the Bank included the entire nominal value, as at the balance sheet, of subordinated bonds issued amounting to PLN 1,600,700 to the Bank's supplementary capital under of art. 127, para. 3, item 2b of the Banking Law.

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IV. Discussion of financial statement components (cont.)

16. Other liabilities

Other liabilities as at the balance date amounted to PLN 1,355,396 thousand and decreased by 5% compared with 2007. The balance comprised the following items:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Accounts payables	213,723	198,251	15,472	8
Deferred income	178,246	197,154	(18,908)	(10)
Other liabilities relating to:	963,427	1 025,916	(62,489)	(6)
inter-bank settlements	241,034	164,641	76,393	46
liabilities relating to settlements of security transactions	205,896	322,897	(117,001)	(36)
liabilities arising from social and legal transactions	116,903	131,650	(14,747)	(11)
liabilities arising from foreign currency activities	76,854	64,176	12,678	20
financial instruments settlements	57,764	17,447	40,317	231
liabilities relating to investment and administration activities	51,164	33,525	17,639	53
settlement of acquisition of machines, materials, works and services regarding construction of tangible assets	34,465	58,328	(23,863)	(41)
liabilities due to suppliers	29,308	28,209	1,099	4
liabilities due to UOKiK (the Competition and Consumer Protection Office)	22,310	16,597	5,713	34
liabilities arising from transactions with non-financial institutions	9,947	66,083	(56,136)	(85)
liabilities relating to payment cards	4,815	41,120	(36,305)	(88)
other	112,967	81,243	31,724	39
Total	<u>1,355,396</u>	<u>1,421,321</u>	<u>(65,925)</u>	<u>(5)</u>

The decrease in the balance was mainly due to lower liabilities relating to the settlement of transactions with securities (a decrease of 117,001 thousand, i.e. 36% compared with 31 December 2007) and a lower balance of "other" items, resulting mainly from a significant decrease in liabilities resulting from transactions with non-financial entities (a decrease of PLN 56,136 thousand, i.e. 85%).

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IV. Discussion of financial statement components (cont.)

17. Provisions

The balance of provisions as at 31 December 2008 comprised:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Provisions for anniversary bonuses and retirement benefits	364,945	320,757	44,188	14
Provisions for liabilities and guarantees granted	77,782	27,624	50,158	182
Provision for legal claims	6,841	6,841	-	-
Other provisions	111,785	97,823	13,962	14
Total	561,353	453,045	108,308	24

The increase in provisions as at the end of 2008 resulted mainly from recognition of a provision for unconditional off-balance sheet liabilities in the amount of PLN 77,782 thousand. The level of provisions was also affected by additional actuarial provisions created for future liabilities to employees of PLN 46,609 thousand. The change was due to the lower discounting rate used for calculating the provision, reflecting a decrease in market interest rates. Revaluation of the provision was prepared on the basis of an actuarial valuation performed at the balance date by an independent actuary, described in a report dating February 2009.

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IV. Discussion of financial statement components (cont.)

18. Equity

Movements in equity in the audited year are presented in the table below:

	Share capital	Reserve capital	Revaluation reserve	General banking risk fund	Other reserves	Other Capital	Retained earnings	Net profit	TOTAL EQUITY
	PLN thousand	PLN thousand	PLN thousand	PLN thousand	PLN thousand	PLN thousand	PLN thousand	PLN thousand	PLN thousand
31.12.2007	1,000,000	5,591,995	(42,445)	1,070,000	1,390,000	8,009,550	-	2,719,991	11,729,541
Net change in available for sale investments less deferred tax	-	-	8,571	-	-	8,571	-	-	8,571
Net profit for 2008	-	-	-	-	-	-	-	2,881,260	2,881,260
Transfer of net profit from previous years	-	-	-	-	-	-	2,719,991	(2,719,991)	-
Transfer from net profit to reserves	-	1,624,991	-	-	5,000	1,629,991	(1,629,991)	-	-
Transfer from net profit to dividends	-	-	-	-	-	-	(1,090,000)	-	(1,090,000)
31.12.2008	1,000,000	7,216,986	(33,874)	1,070,000	1,395,000	9,648,112	-	2,881,260	13,529,372

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IV. Discussion of financial statement components

18. Equity (cont.)

On 20 May 2008, the General Shareholders' Meeting of Powszechna Kasa Oszczędności Bank Polski passed a resolution on the distribution of the net profit for 2007 of PLN 2,719,991 thousand: PLN 1,624,991 was transferred to supplementary capital, PLN 5,000 thousand – to other reserves and PLN 1,090,000 thousand was earmarked for the payment of dividend.

As at 31 December 2008, the Bank's registered share capital amounted to PLN 1,000,000 thousand and comprised 1,000,000,000 ordinary shares with PLN 1 par value each, including:

- 510,000,000 series A registered shares;
- 105,000,000 series B registered shares;
- 385,000,000 series C bearer shares;

The Bank's core capital, calculated in accordance with the Banking Law and Resolution No. 2/2007 of the Banking Supervision Commission, amounted to PLN 12,389,193 thousand as at 31 December 2008 (PLN 9,543,342 thousand as at 31 December 2007) and exceeded by PLN 3,559,517 thousand the total capital requirement which amounted to PLN 8,821,840 thousand (PLN 6,431,473 thousand as at 31 December 2007). The solvency ratio was 11.24% (11.87% as at 31 December 2007).

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IV. Discussion of financial statement components (cont.)

Income statement for the year ended 31 December 2008

19. Net interest income

In 2008, net interest income increased by PLN 1,464,976 thousand (33%):

	2008	2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Interest and similar income:	8,646,426	6,245,091	2,401,335	38
Income from loans and advances to customers	7,296,124	4,859,524	2,436,600	50
Income from securities at fair value through profit or loss	433,975	549,200	(115,225)	(21)
Income from placements with other banks	389,275	490,256	(100,981)	(21)
Income from investment securities	355,460	249,718	105,742	42
Income from Bank Gospodarstwa Krajowego due to subsidies for loan interests	92,486	67,482	25,004	37
Income from trading securities	64,046	24,527	39,519	161
Other	15,060	4,384	10,676	244
Interest expense and similar charges:	(2,678,343)	(1,741,984)	(936,359)	54
Interest expense on amounts due to customers	(2,496,984)	(1,572,859)	(924,125)	59
Interest expense on deposits from other banks	(60,771)	(106,663)	45,892	(43)
Interest expense on debt securities in issue	(115,315)	(17,511)	(97,804)	559
Other	(5,273)	(44,951)	39,678	(88)
Net interest income	<u>5,968,083</u>	<u>4,503,107</u>	<u>1,464,976</u>	<u>33</u>

The increase in interest income of PLN 2,401,335 thousand (38%) in 2008 resulted from higher interest income on loans and advances to customers (an increase of PLN 2,436,600 thousand, i.e. 50%). This was due primarily to the growth of the Bank's loan portfolio (Note 6).

The growth rate of interest expense was higher than the growth rate of interest income and amounted to 54%, which resulted in an increase in interest expense of PLN 936,359 thousand in 2008. Of this amount, PLN 924,125 thousand related to interest paid on amounts due to customers.

The interest margin, being the ratio of net interest income to interest income, was 69% in 2008 (72% in 2007). This was due to shrinking market margins on loans and higher cost of borrowings, particularly in the last quarter of 2008.

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IV. Discussion of financial statement components (cont.)

20. Net fee and commission income

	2008	2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Fee and commission income	2,813,078	2,648,092	164,986	6
Income from payment cards	848,610	701,759	146,851	21
Income from maintenance of bank accounts	780,759	748,760	31,999	4
Income from loans and advances	313,309	262,635	50,674	19
Income from loan insurance intermediary and other services	225,063	202,260	22,803	11
Income from cash transactions	188,345	203,871	(15,526)	(8)
Income from portfolio and other management fees	159,570	240,330	(80,760)	(34)
Income from securities transactions	43,873	87,699	(43,826)	(50)
Income from foreign mass transactions	41,181	36,878	4,303	12
Income from sale and distribution of marks	21,738	28,523	(6,785)	(24)
Other	190,630	135,377	55,253	41
Fee and commission expense	(680,263)	(654,320)	(25,943)	4
Expenses on payment cards	(348,243)	(283,868)	(64,375)	23
Expenses on acquisition services	(134,773)	(129,001)	(5,772)	4
Expenses on loan insurance intermediary and other services	(94,140)	(155,707)	61,567	(40)
Expenses on fee and commissions for operating services granted by other banks	(8,112)	(9,264)	1,152	(12)
Expenses on fee and commissions paid to PPUP	(5,240)	(5,735)	495	(9)
Other	(89,755)	(70,745)	(19,010)	27
Net fee and commission income	2,132,815	1,993,772	139,043	7

Compared with 2007, net fee and commission income increased by PLN 139,043 thousand (7%) in the current financial year.

In 2008, fee and commission income increased by PLN 164,986 thousand. The increase in 2008 was mainly due to the fact that income on payment cards was PLN 146,851 thousand (21%) higher than in the prior year. Moreover, income on loans and advances granted increased significantly in the audited year (an increase of PLN 50,674 thousand, i.e. 19%) as a result of the loan portfolio growth. These commissions are deferred and recognized in the income statement on a straight line basis. They relate mainly to guarantees and sureties granted, overdrafts, working capital loans and other credit products which do not have fixed repayment schedules, and as a result, cannot be accounted for using the effective interest rate.

In 2008, fee and commission expense increased by PLN 25,943 thousand compared with 2007. The increase was mainly due to commission expense relating to payment cards being PLN 64,375 thousand higher. These expenses relate to commission for payment card organizations (VISA, MasterCard and Polcard).

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IV. Discussion of financial statement components (cont.)

21. Dividend income

In 2008, dividend income amounted to PLN 130,896 thousand and was higher by PLN 78,783 thousand (151%) higher than in 2007. Dividend income comprised mainly dividends paid by PKO Towarzystwo Funduszy Inwestycyjnych SA (PLN 92,250 thousand), VISA (PLN 18,013 thousand) and Centrum Finansowe Puławska Sp. z o.o. (PLN 16,627 thousand).

22. Net income from financial instruments at fair value through profit or loss

Net income from financial instruments at fair value through profit and loss decreased by PLN 118,684 thousand (155%) in 2008 compared with the prior year:

	2008	2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Derivative instruments	(158,013)	260,798	(418,811)	(161)
Debt securities	(31,774)	(337,827)	306,053	(91)
Equity instruments	(5,716)	291	(6,007)	(2,064)
Other	73	(8)	81	(1,013)
Total	(195,430)	(76,746)	(118,684)	155

“Derivative instruments” include the result realized on and the valuation of derivatives, excluding cross-currency interest rate swaps (CIRS) whose valuation and result are included in net foreign exchange gains. The loss incurred in 2008 resulted from net losses on the valuation of derivatives (Notes 4 and 13).

“Debt securities” include the result on sales and the valuation of debt securities classified as instruments at fair value through profit or loss.

23. Net foreign exchange gains

Net foreign exchange gains amounted to PLN 734,567 thousand in 2008 and included gains and losses on revaluation of assets and liabilities in foreign currencies and the valuation at fair value of currency derivatives (FX forwards, FX swaps and CIRSs). Compared with 2007, net foreign exchange gains increased by PLN 211,874 thousand (41%).

The increase in net foreign exchange gains was mainly due to a significant increase in the value of loans denominated in foreign currencies (Note 6) in 2008, resulting from a higher volume of currency loans granted in 2008 and the weakening of the Polish currency in the last quarter of 2008. Foreign exchange differences on revaluation of assets and liabilities in foreign currencies increased more than eleven fold in the audited years and amounted to PLN 2,942,413 thousand (PLN 267,248 thousand in 2007). This increase was partly offset by net losses on the valuation of derivatives, mainly cross-currency interest rate swaps (CIRS), used primarily for managing interest rate and currency risks, amounting to PLN 2,207,846 thousand (in 2007: positive valuation of PLN 255,445 thousand).

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IV. Discussion of financial statement components (cont.)

24. Other operating income

In 2008, other operating income amounted to PLN 160,736 thousand and comprised:

	2008	2007	Change	Change
	<u>PLN thousand</u>	<u>PLN thousand</u>	<u>PLN thousand</u>	<u>(%)</u>
Recovery of expired and written-off receivables	31,150	19,469	11,681	60
Sundry income	22,849	23,842	(993)	(4)
Sales and disposal of tangible fixed assets, intangible assets, and assets held for sale	6,130	17,555	(11,425)	(65)
Sale of shares in subordinates	3,746	-	3,746	-
Other	96,861	79,741	17,120	21
Total	<u>160,736</u>	<u>140,607</u>	<u>20,129</u>	<u>14</u>

As at the balance date "Other" included, among others, refund of costs of debt collection proceedings and costs related to restructuring of doubtful and defaulted receivables (total amount of PLN 44,940 thousand) and income from deposits withdrawn by the customers before due date amounting to PLN 25,755 thousand.

Recovery of expired and written-off receivables concerns those receivables, which in previous periods were removed from the balance sheet evidence and in the reporting period were sold or recovered (for example repay despite of prescription).

25. Other operating expenses

In 2008, other operating expenses amounted to PLN 114,689 thousand and comprised:

	2008	2007	Change	Change
	<u>PLN thousand</u>	<u>PLN thousand</u>	<u>PLN thousand</u>	<u>(%)</u>
Impairment allowances for other assets	(46,368)	(17,322)	29,046	(168)
Costs of sale and disposal of tangible fixed assets, intangible assets and assets held for sale	(13,152)	(14,460)	1,308	(9)
Donations	(4,353)	(7,123)	2,770	(39)
Sundry expenses	(5,399)	(4,224)	(1,175)	28
Costs of tangible fixed assets construction and intangible assets development - not capitalized	(426)	(4,013)	3,587	(89)
Other	(44,991)	(37,409)	(7,582)	(20)
Total	<u>(114,689)</u>	<u>(84,551)</u>	<u>(30,138)</u>	<u>36</u>

The increase in other operating expenses was mainly due to increased costs of additional impairment allowances recognized in respect of other receivables.

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IV. Discussion of financial statement components (cont.)

26. Net impairment allowance charge

The net impairment allowance charge was negative (impairment allowances recognized exceeded those released) and amounted to PLN 1,148,930 thousand in 2008 (an increase in the negative balance of PLN 1,103,982 thousand compared with 2007):

	2008	2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Loans and advances to customers and amounts due from other banks valued at amortised cost	(763,932)	(116,076)	(647,856)	558
Investments in subsidiaries, associates and jointly controlled entities	(261,050)	(10,666)	(250,384)	2,347
Other	(126,308)	13,663	(139,971)	(1,024)
Financial assets available for sale	2,796	2,481	315	13
Tangible fixed assets	(436)	49,342	(49,778)	(101)
Intangible assets	-	16,308	(16,308)	(100)
Net impairment allowances	<u>(1,148,930)</u>	<u>(44,948)</u>	<u>(1,103,982)</u>	2,456

The change in net impairment allowance charge in 2008 was mainly due to an increase in impairment charge for corporate loans (of PLN 387,823 thousand, i.e. 528%) and consumer loans (of PLN 171,671, i.e. 74%). The detailed information on the quality of the loan portfolio is presented in Note 6.

Additionally, in 2008 the Bank recognised impairment allowance for the subsidiary KREDOBANK SA of PLN 356,101 thousand (of which PLN 48,737 thousand is presented in "Other" in the table above and relates to the increase in capital of KREDOBANK SA not registered as at the balance date). The Bank's exposure to Kredobank SA is described in Note 8 and 11. The impact of recognised impairment allowances was offset by release of impairment allowance in respect of subsidiaries: Bank Pocztowy SA (amounting to PLN 33,500 thousand) and Kolej Gondolowa Jaworzyna Krynicka SA (amounting to PLN 13,851 thousand).

The difference between the change in the amount of PLN 293,812 thousand in impairment allowance for loans and advances to customers presented in the balance sheet and the impairment charge recognized in the income statement in the amount of PLN 763.932 thousand, resulted mainly from the sale of a part of the loan portfolio to customers conducted by the Bank in the audited year. Decrease of impairment allowances resulting from the sale had no impact on the income statement in the audited year and amounted to PLN 470.352 thousand.

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IV. Discussion of financial statement components (cont.)

27. Administrative expenses

In 2008, administrative expenses were PLN 283,824 thousand (8%) higher than in 2007:

	2008	2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Staff costs	(2,269,539)	(2,155,112)	(114,427)	5
Overheads	(1,270,174)	(1,138,944)	(131,230)	12
Depreciation and amortisation	(361,382)	(323,755)	(37,627)	12
Taxes and other charges	(51,415)	(53,930)	2,515	(5)
Contribution and payments to Banking Guarantee Fund	(16,737)	(13,682)	(3,055)	22
Total	(3,969,247)	(3,685,423)	(283,824)	8

The increase in staff costs in 2008 was mainly due to an increase in costs of salaries and wages of PLN 104,771 thousand (6%), to PLN 1,896,469 thousand.

Overheads also increased in 2008, mainly due to an increase in promotion and advertising costs of PLN 65,067 thousand (in connection with the promotion of many new products of the Bank) and in costs of fixed assets maintenance and lease of PLN 30,407 thousand.

The Bank's effectiveness ratios in the audited year were as follows:

	2008 PLN thousand	2007 PLN thousand
Administrative expenses	3,969,247	3,685,423
Average annual employment (in persons)	30,113	31,305
Administrative expenses per employee	132	118
Net profit per employee	96	87

The cost to income ratio in the audited year was 45% (52% in 2007). At the same time, the net profit per 1 employee increased significantly (an increase of 17% compared with 2007). Administrative expenses per 1 employee increased mainly due to a reduction of 1,192 employees, i.e. 3.8% (average annual).

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IV. Discussion of financial statement components (cont.)

28. Income tax expense

The total income tax expense for the audited year was as follows:

	2008 PLN thousand	2007 PLN thousand	Change PLN thousand	Change (%)
Current income tax expense	(949,873)	(640,233)	(309,640)	48
Deferred income tax	133,283	33,079	100,204	303
Income tax disclosed in the income statement	(816,590)	(607,154)	(209,436)	34
Tax expense disclosed in the equity	2,011	10,829	(8,818)	(81)
Total	(814,579)	(596,325)	(218,254)	37

The effective tax rate for 2008 was 22% and was 4 p.p. higher than in the prior year.

(a) Deferred income tax

Deferred income tax relates to timing differences between the book values of assets and liabilities and their tax bases. The balance of deferred tax comprises deductible and taxable temporary differences:

	Balance Sheet 31.12.2008 PLN thousand	Balance Sheet 31.12.2007 PLN thousand	Income Statement PLN thousand
Deferred tax liability:			
Capitalised interest on mortgage loans	258,759	277,827	(19,068)
Interest accrued on receivables	100,892	99,944	948
Interest on securities	44,113	28,126	15,987
Valuation of securities, of which:	11,486	1,901	x
- transferred to income statement	6,365	705	5,660
- transferred to equity	5,121	1,196	x
Difference between book value and tax value of tangible assets	196,000	133,926	62,074
Other taxable temporary positive differences	3,597	2,804	793
Gross deferred tax liability	614,847	544,528	66,394

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IV. Discussion of financial statement components

28. Income tax expense

(a) Deferred income tax (cont.)

	Balance Sheet 31.12.2008 PLN thousand	Balance Sheet 31.12.2007 PLN thousand	Income Statement PLN thousand
Deferred tax assets:			
Interest accrued on liabilities	223,004	138,252	84,752
Valuation of securities:	27,825	33,217	x
- transferred to income statement	14,759	22,065	(7,306)
- transferred to equity	13,066	11,152	x
Adjustment to valuation at amortised cost	166,449	149,499	16,950
Cost of accruals	159,789	79,193	80,596
Provision for anniversary bonuses and retirement benefits	110,037	88,874	21,163
Valuation of derivative instruments	77,734	62,331	15,403
Other	16,812	28,693	(11,881)
Gross deferred income tax asset	781,650	580,059	199,677
Deferred income tax asset	166,803	35,531	133,283

Due to the fact that as at the end of 2008 deductible temporary differences exceeded taxable ones, the Bank recognised a deferred tax asset of PLN 166,803 thousand (PLN 35,531 thousand as at the end of 2007).

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IV. Discussion of financial statement components

28. Income tax expense (cont.)

(b) Current income tax

In the current financial year, income tax was calculated at 19% of the gross profit determined based on IFRS as adopted by the European Union, adjusted for non-taxable income and non-deductible costs.

	2008	2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Profit before income tax	3,697,850	3,327,145	370,705	11
Corporate income tax calculated using the enacted tax rate 19% (2007: 19%)	(702,592)	(632,158)	(70,434)	11
Permanent differences between accounting gross profit and taxable profit, of which:	(114,506)	24,345	(138,851)	(570)
- Other non-tax-deductible expenses	(19,593)	(19,169)	(424)	2
- Impairment allowance for KREDOBANK SA	(67,659)	-	(67,659)	-
- Reversed provisions and positive revaluation not constituting taxable income	(57,138)	30,413	(87,551)	(268)
- Other non-taxable income	5,294	3,366	1,928	57
- Dividend income	21,140	9,901	11,239	114
- Other	3,450	(166)	3,616	(2,178)
Other differences between gross financial result and taxable income, including donations	508	659	(151)	(23)
Income tax disclosed in the income statement	(816,590)	(607,154)	(209,436)	34

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29. Off-balance sheet items

Off-balance sheet items are presented in the table below:

	31.12.2008	31.12.2007	Change	Change
	PLN thousand	PLN thousand	PLN thousand	(%)
Contingent liabilities:	30,756,418	28,515,534	2,240,884	8
Financing granted	26,196,875	24,298,778	1,898,097	8
Guarantees and warranties granted – nominal value	4,559,543	4,216,756	342,787	8
Contingent assets:	3,829,183	3,985,062	(155,879)	(4)
Guarantees received	3,370,219	3,444,213	(73,994)	(2)
Other	458,964	540,849	(81,885)	(15)

The increase by PLN 2,240,884 thousand (8%) in contingent liabilities resulted from the increase in financing granted of PLN 1,898,097 thousand (8%) and the increase in guarantees and warranties granted of PLN 342,787 thousand (8%).

Contingent assets decreased in 2008 by PLN 155,879 thousand.

Powszechna Kasa Oszczędności Bank Polski SA **Independent Registered Auditor's Report on the financial statements** **as at and for year ended 31 December 2008**

V. The independent registered auditor's statement

- (a) The Management Board of the Bank provided all the information, explanations, and representations required by us in the course of the audit process and provided us with a representation letter confirming the completeness of the information included in the accounting records and the disclosure of all contingent liabilities and post-balance-sheet events which occurred up to the date on which that letter was signed.
- (b) The scope of the audit was not limited.
- (c) The Bank has up-to-date documentation of its accounting policies, approved by the Management Board. The Bank's accounting policies were tailored to its needs and ensured the specification of all the events material to the assessment of its financial position and results, taking into consideration the prudence principle. The principles have been exercised in consistency with the previous year.
- (d) The closing balances as at the end of the prior year were correctly brought forward as the opening balances of the current financial year in all material respects.
- (e) We have assessed the operation of the accounting system and related internal control system. Our assessment covered in particular:
 - the accuracy of the documentation relating to business transactions,
 - the fairness, accuracy and verifiability of the accounting records, including computerized accounting records,
 - the methods used for controlling access to data and computerized data processing systems,
 - the safeguarding of accounting documentation, accounting records and the financial statements.

Based on the above assessment, together with our verification of individual items of the financial statements, we concluded that the accounting system and related internal control system are a basis for expressing a general, comprehensive and unqualified opinion on the truth and fairness of these financial statements. The audit was not intended to provide a comprehensive opinion on the operations of the said systems.

- (f) The additional information present all the significant information required for disclosure by International Financial Reporting Standards as adopted by the European Union.
- (g) Bank's Director's Report includes all information required by the Polish Accounting Act. Information included in the Bank's Director's Report is matching to the information included in the Bank's separate financial statements.
- (h) Counts of assets and equity and liabilities were carried out and reconciled in accordance with the Accounting Act, and their results were included in the accounting records for the audited year.

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V. The independent registered auditor's statements (cont.)

- (i) During the audit, no material violations of the law were identified which had an impact on the financial statements.
- (j) We determined the materiality levels at the planning stage. Materiality levels specify the limits up to which identified irregularities may be left unadjusted without any detriment to the quality of the financial statements and to the correctness of the underlying books of account, since failing to make such adjustments will not be misleading for the readers of the financial statements. Materiality measures both the quantity and quality of audited items and that is why it varies for different balance sheet and income statement items. Due to the complexity and quantity of the materiality levels adopted for audit purposes, they are included in the audit documentation.
- (k) The total regulatory requirement, together with the requirement concerning the risk of excessive capital exposure, amounted to PLN 8,821,840 thousand as at the balance date. The capital adequacy ratio as at 31 December 2008 amounted to 11.24%. As at the balance date, the Bank complied with the prudence principle in all material respects.
- (l) The Bank's financial statements for the year 2007 were audited by other auditor. The registered auditor issued an unqualified opinion.
- (m) The financial statements of the Bank as at and for the year ended 31 December 2007 were approved by resolution no. 4/2008 passed by the General Shareholders' Meeting on 20 May 2008, filed with the National Court Register in Warsaw on 11 June 2008 and published in the *Monitor Polski* B, No. 1033 on 30 July 2008.

VI. Final information and comments

This report has been prepared in relation to our audit of the annual financial statements of Powszechna Kasa Oszczędności Bank Polski SA (hereinafter referred to as the Bank), headquartered in Warsaw, at 15 Puławska Street, which comprise:

- (a) The balance sheet as at 31 December 2008, showing total assets and total equity and liabilities of PLN 131,244,827 thousand;
- (b) the income statement for the financial year from 1 January 2008 to 31 December 2008, showing a net profit of PLN 2,881,260 thousand;
- (c) the statement of changes in equity for the financial year from 1 January 2008 to 31 December 2008, showing an increase in equity of PLN 1,799,831 thousand;
- (d) the cash flow statement for the financial year from 1 January 2008 to 31 December 2008, showing net outflows of PLN 945,615 thousand;
- (e) the additional notes and explanations.

The financial statements were signed by the Bank's Management Board and the person responsible for maintenance of accounting records on 3 April 2009. This report should be read in conjunction with the Independent Registered Auditor's Opinion to the Shareholders and the Supervisory Board of Powszechna Kasa Oszczędności Bank Polski SA, signed on 8 April 2009, concerning the above-mentioned financial statements. The opinion is a general conclusion drawn from the audit and involves assessing the materiality of individual audit findings rather than being a sum of all the evaluations of individual financial statement components. This assessment takes into account the impact of the facts noted on the truth and fairness of the financial statements as a whole.

Person conducting the audit on behalf of PricewaterhouseCoopers Sp. z o.o.:

Antoni F. Reczek
President of the Board
Registered Auditor
No. 90011/503

Registered Audit Company
No. 144

Warsaw, 8 April 2009