mBank Hipoteczny S.A.
Directors' Report
for the first half of 2015

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1. Operations of mBank Hipoteczny S.A. in the first half of 2015

In June 2015, mBank Hipoteczny S.A. (hereinafter the "Bank") updated its business strategy for subsequent years (2016–2019). The main directions of development and strategic objectives remained consistent with those specified in the previous version of the strategy.

The Bank continued the actions aimed at increasing the efficiency and dynamics of the Bank's development, by making the best use of its resources and market potential as well as defining its role and responsibilities in the mBank Group, in which the Bank intends to strengthen its position as a strategic entity and issuing bank. The Bank's objective remains the secure growth through specialisation which, given the nature of the Bank and the narrow scope of its activity, is the source of its competitive advantage and high market position. On the other hand, such nature of the Bank determines the limitation of its income sources and, as a consequence, a relatively low rate of return while the Bank's revenues are strongly related to the current market interest rates.

There are two business lines in the Bank:

- retail line, focused on granting mortgage loans to individual customers,
- commercial line, focused on financing of commercial real estate and residential real estate by development companies.

Since the end of 2012, the Bank has not been providing financing to local government units or other entities with a surety of local government units, which results from the risk profile of that segment and inadequate loan margins. This approach was maintained in the strategy revision for the years 2015–2019. However, the Bank has a legacy portfolio of loan transactions for this segment which is the basis for the issue of public sector covered bonds.

In the retail line, the Bank implemented a business model based on close cooperation with the parent universal bank through the use of specialist expertise and market experience of a mortgage bank.

In the first half of 2015, the Bank focused its operations on the development of lending activities in the area of retail mortgage loans, closely cooperating with mBank as regards the product offer and sales network. The Bank continued to build its portfolio in this area on the basis of both the acquisition of new customers, as well as by systematically taking over the existing retail loan portfolio from mBank. This refers only to loans which may constitute a basis for issuing covered bonds.

In the commercial line, the implementation of tasks was undertaken in a strongly competitive commercial project financing market, which is currently dominated by universal banks. The following trends are still observable in this market:

- stricter criteria for project assessment and, as a consequence, a more selective choice of financed undertakings; similar approach of most banks to such key parameters of investment projects as borrower's share, extent of leased area and pre-sale;
- limited exposure to single entities and projects and, as a consequence, a greater tendency to share the risk by participating in bank consortia;
- the financing period shortened to 5–7 years with balloon payments applied;
- reduction of loan margins to a level below 2.0%.

As regards the financing of residential construction the following could be observed:

- the withdrawal of several banks from this segment,
- stricter criteria for project selection;
- stabilisation of margins at the level of 2.8%–3.0%.

1.1 Key projects in 2015

"Covered Bonds" Project

The priority project for 2015 is still the remodelling of the mBank Group's balance sheet on the basis of a long-term source of refinancing composed of covered bonds issued by mBank Hipoteczny. Works regarding the project began in August 2012, and their aim was to create a comprehensive model of cooperation between the mortgage bank and the universal bank in terms of sales, service and management of the portfolio of retail loans secured by mortgage, and subsequently the issuance of covered bonds on this basis. The division of tasks between mBank and mBank Hipoteczny, in line with the competencies and specialisations of the two banks, helps to effectively build and refinance the retail portfolio on the basis of shared lending policy and operational synergy. Over the course of the project implementation, the two banks have been cooperating on an inter-bank outsourcing basis, based on an agency model, which in the second half of 2014 was supplemented with a pooling model, consisting in the take-over of the existing retail loan portfolio of mBank for the purpose of refinancing.

The implementation of the model is aimed at:

- improving the stability of financing of banks within the mBank Group through the application of long-term and innovative solutions regarding the mortgage portfolio in the mBank Group, taking into account liquidity needs resulting from external factors (new regulations – Basel III) and internal ones (including changes in the financing of subsidiary banks in the Commerzbank group),
- diversification of the financing sources — increasing independence from Commerzbank with regard to the financing of the existing portfolio of retail mortgage loans,
- improving long-term liquidity in the mBank Group – adaptation to the requirements of Basel III by increased long-term financing.

The project is a pioneering solution in the Polish banking sector, and its successful implementation will determine the directions of the market's further development as well as searching for long-term sources of refinancing by banks.

Implementation of the IRB approach

The Bank is working on the implementation of the internal ratings-based (IRB) approach, as a matter of high priority and long-term nature. Seven internal models in the commercial area were conditionally approved by the Polish Financial Supervision Authority (PFSA) on 27 August 2012. Three further rating models for the refinancing and financing of hotels and utility premises obtained the approval of the Federal Financial Supervisory Authority (BaFin) and the PFSA on 10 April 2014. A positive conditional decision on expanding the application scope of the IRB approach for the aforementioned models enabled immediate application of the IRB approach (slotting approach) to calculate capital requirements with respect to credit risk on a consolidated (the Commerzbank Group), sub-consolidated (the mBank Group) and individual (mBank Hipoteczny S.A.) basis.

The works are also aimed at covering the retail portfolio with this method, on the basis of adaptation of models used in mBank S.A. In March 2014, in response to the letter of the PFSA, the Bank provided the PFSA with a plan of the gradual implementation of the IRB approach, supplemented with the class of retail exposures secured on residential properties. It is expected that retail exposures secured on residential properties may be covered by the IRB approach at the turn of 2016 and 2017.

Implementation of Recommendation D

Implementation of the Recommendation D of the Polish Financial Supervision Authority is one of the key tasks and projects implemented by the Bank. It comprises 42 initiatives, of which 39 had been completed as at the end of December 2014, which made it possible to implement 98 out of 109 specific recommendations identified in the gap analysis process. Other specific recommendations, which had not been implemented until the end of 2014, were presented to the Management Board together with the schedule for 2015. As at 10 February 2015, only one initiative relating to the management of data (Data

Governance) at the Bank is left, and it is being implemented in accordance with the policy adopted in the group of mBank and the agreed schedule, with the completion date set for September 2015. Data Governance is aimed at ensuring that IT systems developed and used at the Bank collect and process data in a secure manner and enable access for appropriate persons and units. Moreover, this process is intended to increase users' awareness of the need to take care of the quality of data by making them responsible for verifying its correctness. Through the implemented data quality management standards, the Bank will be able to maintain high credibility in its business environment (investors, rating agencies). Mention should also be made of meeting the supervisory requirements qualifying IRS systems and process for use in the calculation of the Bank's capital requirement, as well as of benefits resulting from the reduction of the model risk which directly contributes to the mitigation of the threats resulting from the Bank's operational risk.

1.2 Financial credibility

The financial credibility of mBank Hipoteczny is assessed by an international rating agency — Fitch Ratings Ltd. As at 30 June 2015, the following ratings were applicable:

BBB-/F3 — international long-term and short-term rating

2 — support rating

BBB — for public sector covered bonds

BBB — for mortgage covered bonds

On 19 May 2015, as a result of downgrading the IDR rating for Commerzbank AG from "A+" to "BBB" and for mBank S.A. from "A" to "BBB-", Fitch Ratings Ltd, a rating agency, downgraded the international long-term IDR (Issuer Default Rating) rating for mBank Hipoteczny S.A. from "A" (negative outlook) to "BBB-" (positive outlook). As a result of the above rating action, the international short-term IDR rating of the Bank was also downgraded from "F1" to "F3" and the support rating was downgraded from "1" to "2".

Moreover, on 20 and 21 May 2015, Fitch Ratings Ltd downgraded the rating for public sector and mortgage covered bonds issued by the Bank from "A" (negative outlook) to "BBB" (positive outlook).

The change in the ratings for covered bonds of the Bank resulted from downgrading the international long-term IDR rating for mBank Hipoteczny S.A. from "A" to "BBB-".

The above rating action did not result from a change in the Bank's financial standing or in the quality of assets constituting collateral for the covered bonds issued.

Fitch Ratings Ltd. assigns ratings on the following scales (on a decreasing basis):

- international long-term ratings: AAA, AA, A, BBB, BB, B, CCC, CC, C, RD, D
- international short-term ratings: F1, F2, F3, B, C, RD, D
- support ratings: 1, 2, 3, 4, 5

Besides its financial results, ratings assigned to the Bank are influenced by the assessment of mBank and Commerzbank AG, including the support granted by these institutions.

1.3 Financial results

The Bank's financial statements for the first half of 2015 are prepared in accordance with the International Financial Reporting Standards (IFRS) as approved by the European Union. Data presented in the Director's Report are presented according to the management approach and do not always have to be consistent with data contained in the financial statements.

Due to the Bank's specialised profile, its assets comprise mainly loans and advances secured with mortgages, and its liabilities comprise mainly liabilities in respect of covered bonds issuance, which is the main source for the refinancing of lending activity.

Table 1. Dynamics of selected elements of the statement of financial position (in PLN '000)

Key balance sheet items	30.06.2015	31.12.2014	Dynamics
ASSETS	7,231,359	6,176,326	17.08%
including			
Loans and advances to customers	6,229,866	5,325,741	16.98%
LIABILITIES AND EQUITY	7,231,359	6,176,326	17.08%
including			
Debt securities in issue	3,792,086	3,171,588	19.56%
Amounts due to customers	223,337	250,012	-10.67%
Share capital	374,938	374,938	0.00%

At the end of the second quarter of 2015, the Bank introduced a change in the methodology of estimating the "portfolio reserve" (IBNR) for a portfolio of loans from the commercial business line. The primary goal was to better adapt the methodology to requirements of the Polish Financial Supervision Authority who recommended applying the Point-In-Time approach for estimating the probability of default (PD). In particular, the loss identification period (LIP) was extended from six to eight months. As a consequence of these changes, the level of provisions increased as at the end of the 6-month period. As a result, in the first half of 2015, the Bank achieved gross profit amounting to PLN 8,305 thousand. Due to the specialised business profile in which the main source of the Bank's result is the net interest income, the financial performance in the first half of the year was strongly affected by low interest rates. Despite the above, the Bank's result from core activities increased as compared with the first half of 2014 (net interest income was higher by PLN 9,493 thousand or 22.76%, net fee and commission income increased by PLN 852 thousand or 27.35%).

As at the end of the first half of 2014, the valuation of derivative hedging transactions was positive (PLN 7,797 thousand), significantly contributing to the gross profit, while as at the end of the first half of 2015 it was negative (PLN -1,881 thousand).

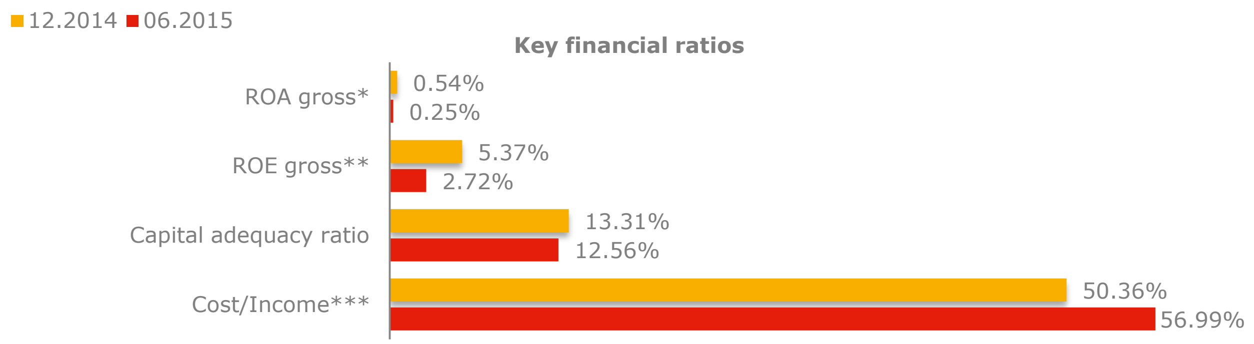
Table 2. Dynamics of selected elements of the income statement (in PLN '000)

Income statement	Period from 01.01.2015 to 30.06.2015	Period from 01.01.2014 to 30.06.2014	Dynamics
Net interest income	51,204	41,711	22.76%
Net fee and commission income	3,965	3,113	27.35%
Net trading income	-1,881	7,797	-124.12%
Net impairment write-downs on loans and advances	-13,608	-9,099	49.56%
Overhead costs	-26,766	-21,699	23.35%
Amortisation and depreciation	-2,276	-2,330	-2.33%
Profit before income tax	8,305	18,589	-55.32%
Net profit	4,956	13,816	-64.13%
Weighted average number of ordinary shares/diluted weighted average number of ordinary shares	2,850,000	2,750,000	3.64%
Earnings per ordinary share/Diluted earnings per ordinary share (in PLN)	1.74	5.02	-65.39%

Table 3. Business effectiveness ratios

BUSINESS EFFECTIVENESS RATIOS	30.06.2015	31.12.2014
Gross ROA*	0.25%	0.54%
Gross ROE**	2.72%	5.37%
Cost/income***	56.99%	50.36%
Capital adequacy ratio	12.56%	13.31%
RATINGS of Fitch Ratings Ltd		
international long-term rating	BBB-	A
international short-term rating	F3	F1
support rating	2	1
public sector covered bonds	BBB	A
mortgage covered bonds	BBB	A
OTHER		
Average employment	213 persons	187 persons
Branches	Head Office + 6 branch offices	Head Office + 6 branch offices

Chart 1. Key financial ratios

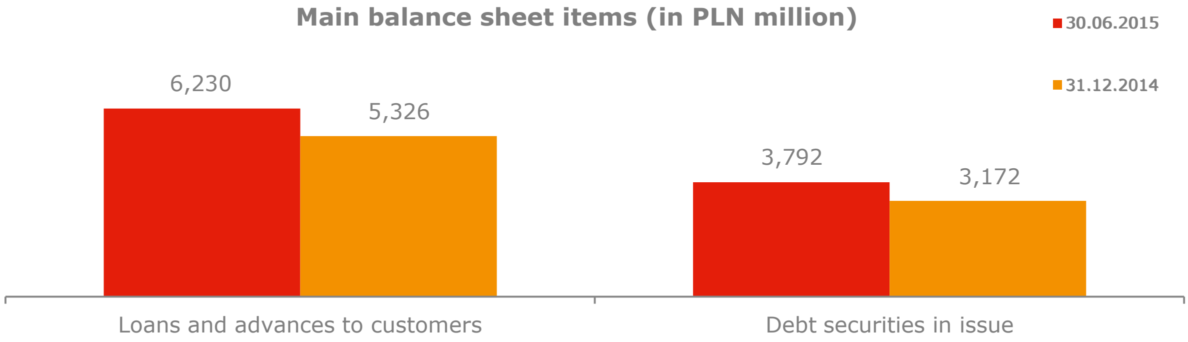


* gross result / average assets

** gross result / (average share capital + financial result from the previous years)

*** (overheads + amortisation and depreciation) / the result on banking operations (defined as the operating result less the general administrative costs, amortisation and depreciation, and the value of net impairment write-downs on loans and advances)

Chart 2. Main balance sheet items (in PLN million)



On the basis of the revised credit policy, optimised lending process and streamlined internal procedures, as well as taking into account the conditions and risks of the market environment, the Bank developed its activity both in the area of loans to business entities and retail customers.

In the first half of 2015, the value of loans granted reached PLN 1,134.5 million and was 75% higher than the value of agreements signed in the first half of 2014. PLN 541.8 million of sales referred to lending activity in the retail area, which was resumed in 2013. Moreover, the loan portfolio increased as a result of pooling transactions in the retail area whose nominal value, on the date of transfer, amounted to PLN 315.6 million. The net value of the entire loan portfolio, taking into account pooling transactions and off-balance sheet exposure, increased at the end of June 2015 by 12.7% in comparison with the end of 2014, reaching the level of PLN 7.2 billion.

1.4 Lending activity

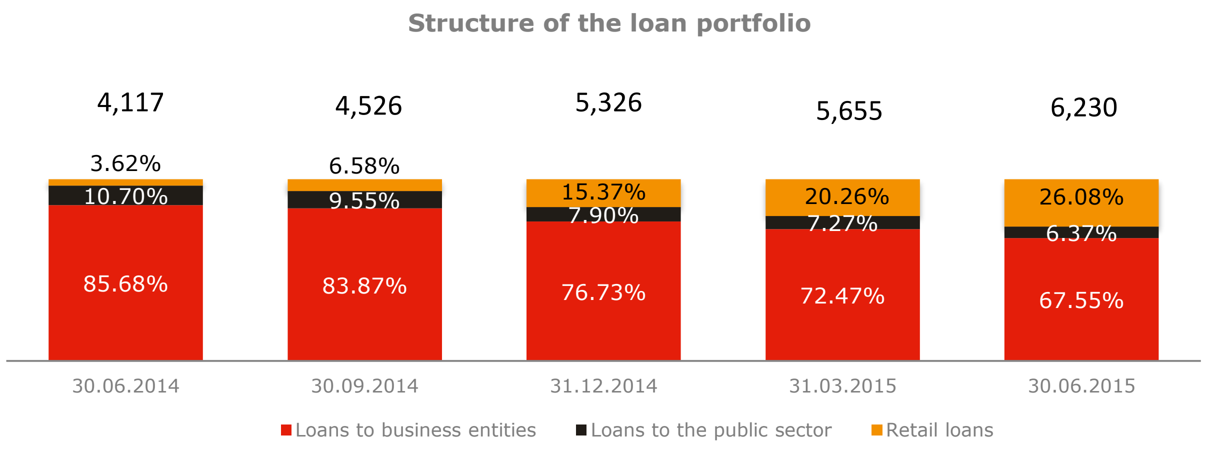
In the first half of 2015, commercial sales amounted to PLN 592.7 million, which means an increase by 12% as compared with the first half of 2014. In the commercial area, the first half of the year, and in particular the first quarter, is a period in which lower sales dynamics are recorded historically. The proper trend in terms of increase (planned annual commercial sales growth dynamics amounts to 12.4%) was confirmed in the second quarter in which the sales amounted to PLN 460.9 million, which is a record performance of the second quarter in the Bank's history.

The share of financing of commercial income-producing real estates increased slightly and accounted for 57% of sales as at the end of June 2015. 43% was attributable to the financing of residential property.

Projects at different stages of processing, acquired both from own acquisition, as well as those that can be undertaken in a consortium with mBank, should ensure the realisation of the sales plan for the entire year. The Bank is also working on transferring projects from mBank to mBank Hipoteczny as part of the commercial pooling, which provides significant support for the realisation of the annual target.

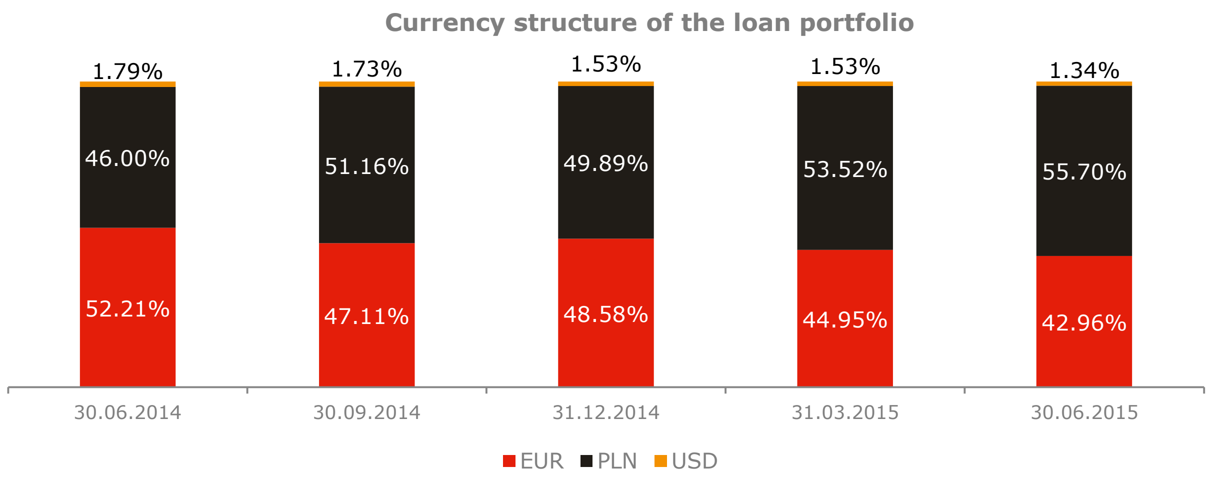
Since September 2013, as part of the project involving the reconstruction of the mBank Group's balance sheet, the Bank's offer has also included retail loans. In 2014, the sale of retail loans in the agency model, through the mBank's sales network, was supplemented with a "pooling" model, under which the Bank acquires mortgage loans granted by mBank which may constitute a basis for the issuance of covered bonds. In the first half of 2015, three pooling transactions were conducted in the retail area, covering loans with the total nominal value of PLN 315.6 million as at the transfer date.

Chart 3. Structure of the loan portfolio in the period 30.06.2014–30.06.2015 (in PLN million)



In the first half of 2015, the currency structure of the loan portfolio was subject to changes resulting from a systematic growth of the portfolio of retail loans granted only in PLN. In comparison with the end of 2014, the share of loans in PLN increased by 5.8 percentage points and, as at the end of June 2015, accounted for more than half of the loan portfolio. The share of loans in EUR decreased to 42.96%.

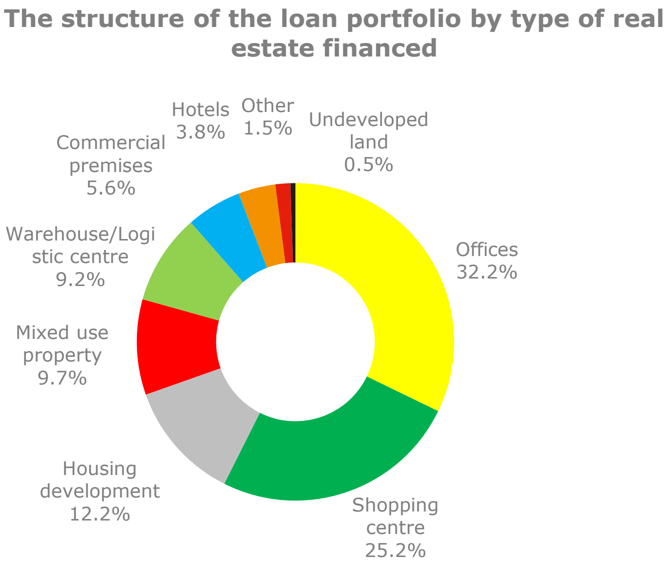
Chart 4. Currency structure of the loan portfolio in the period 30.06.2014–30.06.2015.



Loans to business entities

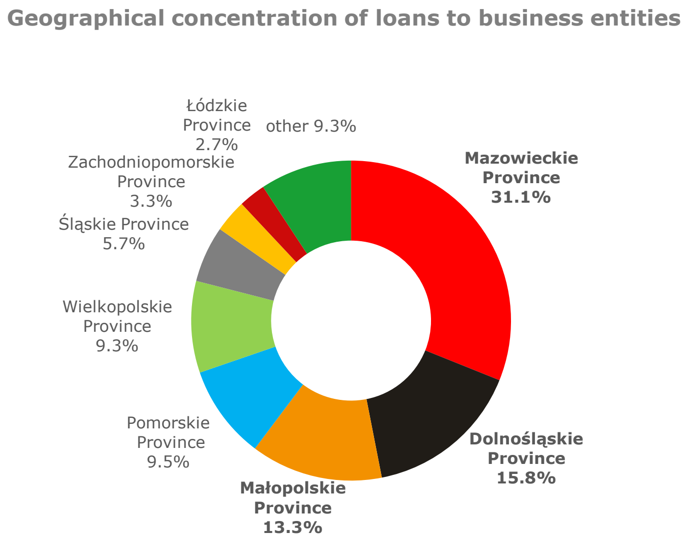
As at 30 June 2015, net balance sheet exposure towards business entities amounted to PLN 4,207.9 million. The main part (79.8%) was attributed to refinancing of finished commercial facilities, exposures in housing projects accounted for 12.4% and loans for the financing of construction of commercial facilities accounted for 7.4%.

Chart 5. Loans to business entities by type of real estate financed as at 30 June 2015.



As at the end of June 2015, within the area of commercial real estate, the Bank particularly financed office buildings and shopping facilities. The Bank focused on the financing of purchases or refinancing of completed facilities with the relevant standard, as well as financing the construction process after which the construction loan is converted into a long-term mortgage loan.

Chart 6. Geographical concentration of loans to business entities as at 30 June 2015



The largest number of financed projects is concentrated within the Mazowieckie province, where the exposure amounts to 31.1% of all credit funds. In the provinces of Dolnośląskie, Małopolskie and Pomorskie, the total balance sheet exposure amounts to 38.6%.

As at 30 June 2015, the portfolio of loans to business entities was dominated by loans in EUR (63.1%) and PLN (35.0%).

Loans to the public sector

Due to the Bank's strategy, there are no new agreements in this portfolio which, together with a substantial volume of early repayments, is reflected in lower (as compared to 30 June 2014) balance sheet exposure in this area (-9.9%).

Retail loans to individual customers

In the first half of 2015, the Bank continued to implement its strategic objectives in the area of mortgage loans for individual customers in cooperation with mBank S.A. The Bank took actions aiming at increasing the share of sales through external channels, outside the mBank group, by improving the quality of the process. The above actions include establishment of a group in the Bank to provide substantive support for brokers and streamlining the application and communication process in the "non-branch circulation area" (sales channels outside the mBank group).

Chart 7. Share of sales channels in the first half of 2015

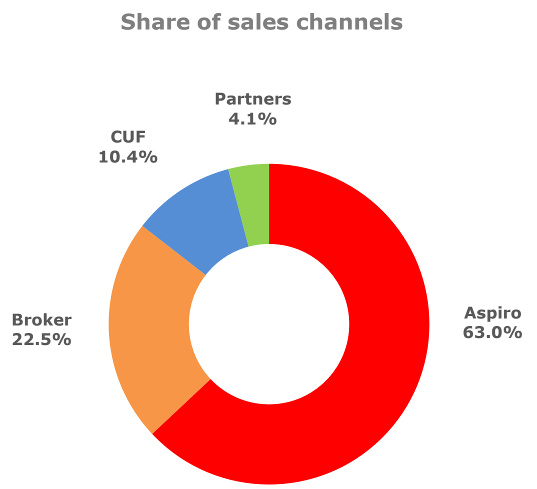
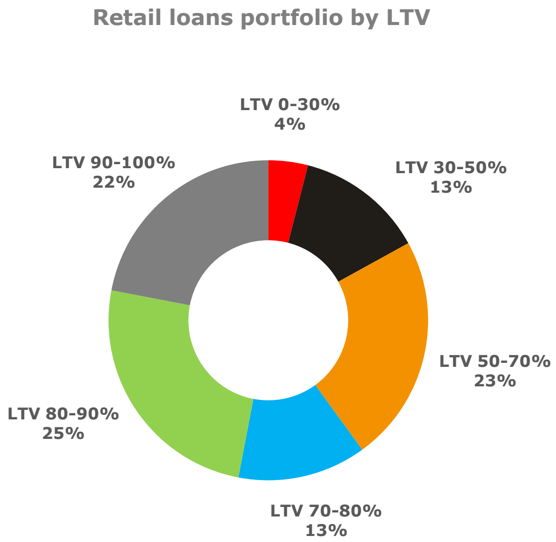


Chart 8. Retail loans portfolio by LTV as at 30 June 2015



The total volume of loan agreements signed in the first half of 2015 amounted to PLN 541.8 million. The average amount of a loan was PLN 280 thousand. At the end of the first half of 2015, the average margin weighted by the portfolio volume amounted to 1.51%. The average commission weighted by the amount of a loan agreement for loans disbursed in the first half 2015 was 0.42%. The largest share in sales is that of loans with LTV of 80–90% and verified customer net income of up to PLN 8 thousand.

1.5 Refinancing and issuance of covered bonds

In the first half of 2015, mBank Hipoteczny successfully placed on the market five issues of mortgage covered bonds with a total nominal value of approx. PLN 790 million as at 30 June 2015.

The value of two issues denominated in the domestic currency was PLN 450 million. The Bank also issued three series of mortgage covered bonds denominated in EUR for the total amount of EUR 81 million.

The value of all covered bonds issued by the Bank and outstanding as at the end of the first half of 2015 was over PLN 3 billion, representing more than 70% of the covered bonds market in Poland according to the Bank's estimates.

Covered bonds of mBank Hipoteczny are classified as instruments marked by a low level of investment risk due to the legal requirement of multi-stage collateral for their issuance and trading. This is confirmed by the Fitch Ratings Ltd rating agency, which assigned BBB level ratings to mortgage and public sector covered bonds issued by the Bank.

Issues of mortgage covered bonds of mBank Hipoteczny S.A. in public offerings

Organisers of the offering: Offerer: Dom Maklerski mBanku S.A., Biuro Maklerskie mBanku S.A., Leading manager: mBank S.A.

Issue date	Redemption date	Currency	Value	Rating Fitch Ratings Ltd.
28.09.2010	28.09.2015	PLN	100,000,000	BBB
28.04.2011	20.04.2016	PLN	200,000,000	BBB
15.06.2011	16.06.2017	PLN	200,000,000	BBB
07.07.2011	07.07.2015	PLN	100,000,000	BBB
20.04.2012	20.04.2017	PLN	200,000,000	BBB
15.06.2012	15.06.2018	PLN	200,000,000	BBB
30.11.2012	15.11.2016	PLN	100,000,000	BBB
20.06.2013	21.06.2019	PLN	80,000,000	BBB
28.07.2014	28.07.2022	PLN	300,000,000	BBB
04.08.2014	20.02.2023	PLN	200,000,000	BBB
20.02.2015	28.04.2022	PLN	200,000,000	BBB
15.04.2015	16.10.2023	PLN	250,000,000	BBB
TOTAL		**PLN**	**1,780,000,000**	

Issue date	Redemption date	Currency	Value	Rating Fitch Ratings Ltd.
19.10.2012	19.10.2017	EUR	10,000,000	BBB
26.07.2013	28.07.2020	EUR	30,000,000	BBB
22.11.2013	22.10.2018	EUR	50,000,000	BBB
17.02.2014	15.02.2018	EUR	7,500,000	BBB
28.02.2014	28.02.2029	EUR	8,000,000	BBB
17.03.2014	15.03.2029	EUR	15,000,000	BBB
30.05.2014	30.05.2029	EUR	20,000,000	BBB
22.10.2014	22.10.2018	EUR	20,000,000	BBB
28.11.2014	15.10.2019	EUR	50,000,000	BBB

25.02.2015	25.02.2022	EUR	20,000,000	BBB
24.04.2015	24.04.2025	EUR	11,000,000	BBB
24.06.2015	24.06.2020	EUR	50,000,000	BBB
TOTAL		**EUR**	**291,500,000**	

Issues of public sector covered bonds of mBank Hipoteczny S.A. in public offerings

Organisers of the offering: Offerer: Dom Maklerski mBanku S.A., Biuro Maklerskie mBanku S.A., Leading manager: mBank S.A.

Issue date	Redemption date	Currency	Value	Rating Fitch Ratings Ltd.
29.11.2010	30.11.2015	PLN	100,000,000	BBB
27.07.2012	28.07.2015	PLN	100,000,000	BBB
28.09.2012	28.09.2016	PLN	150,000,000	BBB
TOTAL		**PLN**	**350,000,000**	

Basis for issuing covered bonds

In accordance with the Act on covered bonds and mortgage banks, the basis for the issue of mortgage covered bonds are receivables entered into the cover register, secured with mortgages established on the right of perpetual usufruct or the ownership of real estate, entered as the first item in the land and mortgage register.

Public sector covered bonds are backed with receivables in respect of loans granted to local government units and loans secured with guarantees or warranties of local government units.

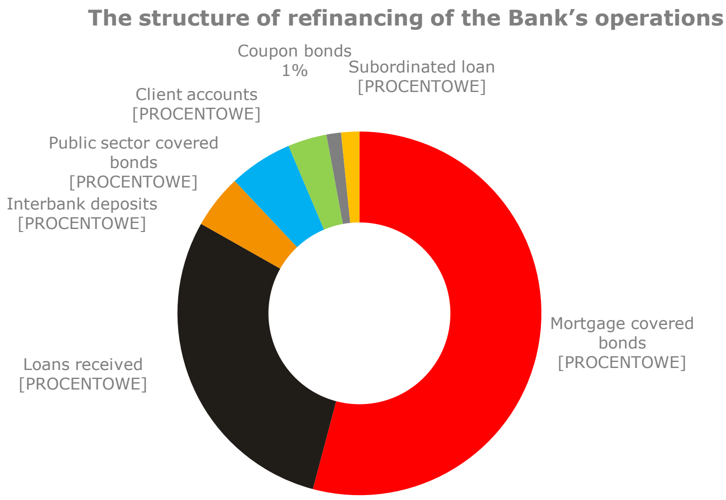
As at 30 June 2015, the collaterals of:

- the public sector covered bonds comprised receivables of PLN 398.3 million relating to 69 loans in total,
- the mortgage covered bonds comprised receivables of PLN 4,583.9 million relating to 4,842 loans in total.

In addition to loan receivables, a substitute cover in the form of treasury bonds with the nominal value of PLN 20 million (for public sector covered bonds) was entered in the respective register.

The Bank raises funds for lending activities mostly by the issuance of covered bonds, followed by loans received and term deposits — mainly from the inter-bank market.

Chart 8. The structure of refinancing of the Bank's operations as at 30 June 2015



2. Risk management

2.1 Credit risk

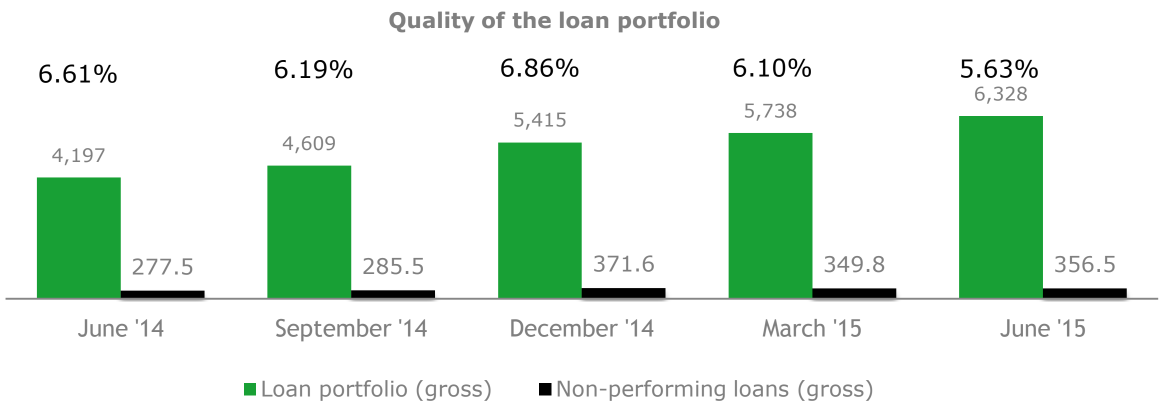
Loan portfolio

The rules of granting loans are specified in the Bank's credit policy and the existing loan portfolio is managed mainly through current monitoring of credit exposures.

Due to actions taken by the Bank in the area of problem loans management and as a result of an increase in the loan portfolio, the share of non-performing loans in the Bank's loan portfolio decreased to the level of 5.63%. Most liabilities are repaid in a timely manner, and borrowers with a higher risk profile have been subjected to intensified monitoring. In the first half of 2015, the net value of the loan portfolio increased by PLN 904.1 million in comparison with the end of 2014, which resulted mainly from the increase in the retail portfolio (agency model loans and retail pooling).

Impairment provisions reaching PLN 95,728.4 thousand together with mortgages established on the financed properties constitute the relevant collateral against potential losses resulting from credit risk.

Chart 9. The share of non-performing loans* in the Bank's loan portfolio (gross values, in PLN million)



*Non-performing loans — loans for which a loss event has been identified — in accordance with IAS 39

The main area of the Bank's activities in the first half of 2015 was the refinancing of commercial real estate including in particular shopping centres and offices. These activities are based on a uniform policy of the entire mBank SA group for financing commercial real estate, containing key elements of approval policy for individual segments of the real estate market. By utilising its experience in financing housing investment, the Bank continued to finance housing development projects, focusing on the selective financing of projects with the most favourable market parameters (the offer's adjustment to the market needs, positive history of the developer's activity, adequate level of own participation, as well as verified pre-sales).

The retail portfolio is characterised by very good quality which, apart from the applied credit policy, is clearly affected by the fact that it is a very young portfolio in which no customers have become unable to repay their loans and, as a consequence, no losses were incurred on that account. Loans to individual customers are monitored on a monthly basis for the timeliness of repayment and regularities as regards the established effective mortgage collateral. In the same period, the implementation of all contractual obligations of the customer is monitored (including insurance of the real property and assignment of rights under insurance policies).

Credit risk management

The Bank’s strategy is to maintain the level of credit risk in line with the level of risk appetite defined by the target level of capital adequacy and exposure limits. At the same time, the objective of credit risk management is to ensure that the loans are of the quality required under the Act on mortgage bonds and mortgage banks in order to ensure the maximum utilization of the loans as a basis for covered bonds issues.

In the corporate area, the Bank plans to work mainly with reliable customers who have considerable experience in the real estate segment (without any delays in meeting their obligations towards the Bank, borrowers who continue to work with the Bank in the next stages of project implementation, companies with a strong market position).

The priority is to increase the share of the loans for the purchase or refinancing of the existing or new commercial real estate or completely renovated real estate, which are comprehensively utilised and remain economically competitive over a longer period of time, in the total loan sales.

On 11 May 2015, the Management Board of the Bank decided to introduce changes to the Lending policy of mBank Hipoteczny S.A., consisting in standardisation of the approach to the CRE (commercial real estate) financing in the mBank Group. As a result of the changes introduced, preferred acquisition markets were determined and cases of increased risk, classified as “exception from the policy”, “outside the policy” or excluded from financing irrespective of the credit decision level, were defined.

In the retail loans area, the Bank’s objective is to acquire affluent clients of the previously indicated target group who have a verified record of transactions within the banking system. The Bank seeks to maximise the share of loans secured on typical residential real estate located in highly liquid markets.

The Bank seeks to maintain a low portfolio loss ratio through the use of a conservative approach to the assessment of customer creditworthiness. In this area, the Bank intends to operate in accordance with the best market practices and draw on the experience of its parent company, providing the basis for credit policy and decision-making process according to the principles successfully applied by mBank S.A.

The Bank seeks to eliminate the foreign exchange risk — in the case of new transactions, the Bank aims to grant loans only in the currency of the customer’s income.

The Bank updated the impairment measurement methodology, in particular with respect to estimating the IBNR provision. The LIP (Loss Identification Period) parameter used for corporate exposures was extended from six to eight months. As expected by the Polish Financial Supervision Authority, the Point-in-Time nature of the PD (Probability of Default) parameter determination model was also increased. The above changes resulted in the increase in the INBR provision at the end of June 2015.

2.2 Market risk

The risk of incurring a loss due to unfavourable changes in the market parameters from the perspective of the term structure of the Bank’s portfolio is maintained at the lowest possible level, owing to the nature of the Bank’s operations and its efficient system of risk mitigation and risk management on the operating level.

In order to mitigate the market risk, the Bank adjusts the currency and term structure of the financing sources to the structure of loans, uses linear, plain vanilla derivatives, and concludes spot or forward currency transactions and FX SWAP transactions.

The amount of market risk to which the Bank is exposed daily is determined using the Value at Risk (VaR) method at the 97.5% confidence level. As at the end of June 2015, VaR amounted to PLN 74.8 thousand. The currency risk amounted to PLN 54.7 thousand and the interest rate risk amounted to PLN 20.1 thousand.

The interest rate risk is a risk arising from exposure of the financial result and capital of the Bank to the unfavourable effect of changes in the interest rates. The Bank manages the interest rate gap by matching the repricing dates of assets and liabilities. Sensitivity of the Bank’s portfolio to extreme interest rate fluctuations is determined on the basis of results of stress tests and scenario analyses. The interest rate risk is measured, among other things, by the Earnings at Risk (EaR) ratio, which at the end of June 2015 reached a safe level of 5.18%. The Bank's portfolio components which are exposed to interest rate risk are hedged with linear interest rate derivatives.

The currency risk is mitigated by the immediate hedging of the foreign exchange position. The currency risk scale and structure are measured on the basis of the Bank's current foreign exchange position. The foreign exchange position taking the expected repayments and disbursements of loans into account is also subject to the monitoring process. The currency risk is controlled using the foreign exchange position limits for each of the currencies together with the stop loss limit (limit of the acceptable maximum loss) for open intra-day positions as at the end of a given business day, separately for each currency.

2.3 Liquidity risk

Liquidity risk management is carried out at the level of current, short-term, medium-term and long-term liquidity, the absence of which indicates the Bank's inability to finance its assets and settle its liabilities in a timely manner as part of the Bank's ordinary business activities.

Due to the fact that the maturities of long-term securities and assets are not matched, the Bank secures its liquidity by maintaining reserves of liquid assets.

As at the end of June 2015, liquidity reserves represented ca. 10.3% of the balance sheet total. The Bank is not exposed to the risk of short-term refinancing to maturity or to the risk of withdrawal of deposits by the largest deposit holders due to a small share of deposits from the non-financial sector in the balance sheet total (2.96%).

In the first half of 2015, the financing of the Bank's lending activities was performed mainly through the issuing of short- and medium-term covered bonds in PLN and EUR. The Bank's long-term liquidity is stable. Deposits obtained from mBank S.A. constitute a significant share in the financing of long-term credit receivables.

With the need to preserve liquidity ratios at the appropriate level, the need to offset the mismatch between the assets structure and the liabilities that finance them and the need to increase the stability of financing sources, mBank Hipoteczny will continue its activities aimed at replacing short-term financing with financing in the form of covered bonds issues with maturities of 5 years and more.

The share of stable financing sources and liquidity reserves adequate to the scale of the Bank's operations enables the Bank to meet the M4 long-term liquidity standard set by the Polish Financial Supervision Authority. M4 ratio as at the end of June 2015 was 1.073. M1 and M2 short-term liquidity standards remained at a safe level of PLN 613,750 thousand and 2.164, respectively. The M3 standard was to 39.744.

In the first half of 2015, the limit of liabilities set under Article 15.2 of the Act on covered bonds and mortgage banks was utilised in 72.8% (on average) and it was not exceeded throughout the half-year.

As at the end of June 2015, the average maturity of covered bonds issued amounted to 5.3 years for mortgage covered bonds and to 0.6 years for public sector covered bonds, whereas the average maturity of long-term deposits and loans received from other banks amounted to 3.3 years. The margin on mortgage covered bonds issued in 2015 was 0.82% (on average), with an average maturity of 7.3 years. No public sector covered bonds were issued in 2015.

2.4 Operational risk

In the recent period, the main source of operational risk were changes in the profile of operating activities (extending the business profile of the Bank with retail mortgage loans) and the significant scale of activities entrusted to third parties. The Bank adapted its internal procedures and operating practices in order to ensure proper control of risk categories related to these factors. For proper management of the outsourcing risk, a structure covering business units and the compliance unit has been implemented. The basic tool used to monitor outsourcing risk are risk assessments concerning the outsourced processes and risk assessment concerning entities carrying out activities at the request of the Bank.

These assessments are carried out both before entering into cooperation, as well as in the course thereof. When assessing the risk, the Bank takes into account the materiality of the outsourced activities and analyses the risk of non-performance or improper performance of the service. As part of these analyses, the Bank takes into account the business continuity plans of entities carrying out the outsourced activities and potential abilities to reduce the risk through insurance.

Along with the introduction of retail lending, the Bank launched mechanisms for detection and management of operational risk in this area. The Bank introduced a fraud detection process and mechanisms for recording and analyzing transaction errors and customers' complaints. The Bank monitors any changes affecting the operational risk profile. So far, the data collected does not indicate an increase of the operational risk in the retail banking line. In line with the development of the portfolio of loans granted to individual customers, an increase in losses for this business line can be expected which, however, due to the nature of these activities, should not result in the distribution of operational risk that is characteristic for commercial banks. This phenomenon is subject to on-going monitoring. In connection with the nature of business activities, despite an increase in the retail mortgage loan portfolio, operating losses are recorded mainly in the commercial banking business line.

The Bank has a Business Continuity Plan in place, implemented and tested in 2014. It complies with provisions of the Recommendation D of the Polish Financial Supervision Authority. The purpose of the Plan is to implement mechanisms ensuring the business continuity of mBank Hipoteczny to an extent defined by a list of critical processes in the period of up to five days. The Plan is tested at least twice a year and the list of processes is subject to analysis and update at least every two years. Actions aimed at improving the plan, in accordance with internal regulations adopted, are measured and the Management Board is notified thereof. The Bank implemented events monitoring and notification systems, together with internal security procedures for individual IT systems, for which the IT security risk assessment is performed. Due to the probability of crisis situations in areas related to the Bank's liquidity management, currency risk management and interest rate risk management, the Bank has a "Liquidity Crisis Contingency Plan". Additionally, the Bank also has a "Contingency plan in the event of unexpected, radical changes in prices on the real estate market" in place.

Factors contributing to the increase of the Bank's operational risk exposure:

- numerous changes in the organisational structure,
- number of IT projects and undertakings implemented,
- high staff turnover,
- changes in the profile of operating activities related to the development of the mortgage loan portfolio based on outsourcing agreements concluded, both in the business, as well as in the IT area.

With the extension of the Bank's scope of operations to include the sale of retail loans, the Bank may expect:

- an increase in the number of complaints and claims by individual customers against the Bank,
- a larger number of credit frauds — individual customers trying to obtain loans under false pretences.

The Bank will monitor and analyse any changes affecting the operational risk profile.

Factors stabilising the level of the Bank's exposure to operational risk:

- operational risk management system implemented in the Bank,
- simple organisational structure, lack of subsidiaries,
- small scale and complexity of operations, resulting from the specific nature of mortgage banks,

- lack of e-banking services.
- procedures regulating the process of making outsourcing decisions (analysis of benefits, risks and method of reducing them, business continuity plans and financial standing of the insourcer, as well as ability to perform the services in a timely manner and with good quality),
- the Bank's business continuity plans,
- highly qualified staff,
- effective system of internal control.

2.5 Risk of investing in covered bonds

In the first half of 2015, the risk profile of investments in covered bonds issued by mBank Hipoteczny did not change. These securities constitute financial instruments with a low investment risk, resulting from the required multi-level collateralisation of their issue and trading by the issuer in accordance with the Act on covered bonds and mortgage banks. In addition to ensuring that the Bank meets a number of statutory requirements, taking into account the security of investments in covered bonds under the conditions of slower economic growth, the fact that for many years the Bank has followed a conservative policy of real estate valuation on which the bonds are secured also contributes to high security of this investment. The minimum overcollateralization level of mortgage covered bonds and public sector covered bonds is 10% and 6% respectively.

The increased attractiveness of investments in such securities is also attributed to the fact that covered bonds issued by mortgage banks may constitute collateral for lombard facilities and repo transactions entered into with other banks.

3. Property market in Poland in the first half of 2015

Residential property market

- the residential real estate sector remained balanced despite a further increase in the number of housing units pending sale. In total, the main cities' offer included approx. 45.5 thousand housing units at the end of the second quarter, of which 19.7% were already completed units;
- transaction prices per square meter of housing in the primary and secondary markets of the largest cities were stable. The Warsaw market saw a decline in prices in the secondary market driven by the sale of a larger number of lower quality or worse location dwellings;
- as a result of high profit margins and rates of return on residential projects, as well as measures undertaken by real estate developers fearing the amendment of the "Real Estate Development Act" proposed by the Office of Competition and Consumer Protection, the number of issued building permits increased (the number of building permits issued in the first quarter of 2015 was 4.5 thousand higher than in the corresponding period of 2014). A slight decline was noted in the number of dwellings under construction (a 0.4 thousand drop on the 2014 Q1 figure) and completed dwellings (a 3.8 thousand decline as compared with the corresponding period of the previous year);
- the stock of unsold housing in Poland's six largest cities increased further in the analysed period (by approx. 700 housing units) following the last quarter's decline;
- the total number of transactions for six markets[1] reached 45.8 thousand units in the last four quarters, approx. 27% more than in record years 2007 and 2013, when approx. 36 thousand apartments were sold in each year;

the demand was high as a result of discounting the effect of interest rate cuts. This worked in the opposite direction than the increase in the own participation level required to obtain a mortgage loan. As a result, the average market time in the six largest cities' primary market increased slightly.

[1] Warsaw, Kraków, Wrocław, Poznań, Gdańsk, Łódź

Commercial property market

- the volume of transactions concluded in the first quarter of 2015 on the commercial property market amounted to EUR 438 million, half of the value achieved in the corresponding period of 2014;
- the share of individual markets was balanced, with small domination of investments in the retail segment which accounted for approx. 35% of the quarterly volume;
- in the second half of 2015, the largest increase in the investors' activity is expected in the retail sector.

Office property

- Warsaw remains the largest office property market in Poland. As at the end of the first quarter of 2015, its resources increased by further 57 thousand m^2 and totaled approx. 4.4 million m^2 of space;
- a high level of new supply under construction (approx. 1.2 million m^2 in Poland) will contribute to an increase in the vacancy rate to which, in particular, older (B class) and less attractively located office buildings will be exposed;
- total volume of transactions signed in the capital in the first quarter amounted to approx. 168 thousand m^2 and was by approx. 30% higher than in the first quarter of 2014;
- the demand for office space in regional markets amounted to 75 thousand m^2 and was slightly lower than in the same period of recent years;
- asking rents remained at a stable level, developers, however, show large flexibility during negotiations concerning non-rent conditions of lease, such as participation in office finishing costs or rent-free periods.

Retail property

- in the recent period, most shopping centres were opened in smaller regional cities, however, currently new projects are expected to be completed in major agglomerations in Poland, located in city centres which will contribute to changes in the retail map of Poland;
- Polish shopping centres are an attractive market for foreign brands;
- consolidation of the food industry and dynamic development of smaller grocery stores (supermarkets and discounts);
- increase in attractiveness of shopping centres through modernisations, extensions, relocation of tenants and introduction of non-trade concepts (e.g. collection points for Internet orders, co-working spaces), "pop-up" stores;
- increased popularity of shopping parks in smaller cities where the construction of shopping centres is not profitable;
- stable level of rents; an increase in prime rents is visible only in the capital;
- low and moderate vacancy rate.

Warehouse property

- increased investors' activity,
- more than half of the existing supply is currently held by four largest players and their partners (Prologis, SEGRO, Logicor and Goodman);
- projects for specific customer still dominant (like pre-let and BTS);
- increased developer interest in speculative projects (properties previously not secured by lease contracts);

- Warsaw remains the largest warehouse market in Poland;
- Poznań, as well as Lower and Upper Silesia are the most dynamically developing warehousing centres;
- the largest demand for new space was visible in Poznań, Wrocław and in Silesia;
- large warehouse space is located around main transit roads and transport hubs.

4. Development directions and key elements of the Bank's strategy

The mission of mBank Hipoteczny is to develop an effective mechanism for financing the property market by issuing long-term debt securities — covered bonds.

The Bank's visions is a safe, sustained, profitable and long-term growth leading to maintaining strong leading position on the changing and increasingly demanding covered bonds market by utilising 15 years of experience, specialist competences and potential of the mBank brand, as well as strenghting the Bank's position on the growing commercial and housing property financing market.

In June 2015, the Bank adopted an update of its strategy for subsequent years (2016–2019). The main directions of development and strategic objectives specified in the 2013 version of the document remain up-do-date.

The business strategy sets out two main strategic objectives of the Bank for the years 2016–2019:

- building the largest possible portfolio of real estate assets under the applicable risk management strategy, compliant with the covered bond collateral criteria,
- maximum utilisation of covered bonds as a tool for refinancing the portfolio of long-term mortgage loans.

Since 2013, the Bank has been implementing a strategic project based on the model of cooperation with mBank in the area of establishing and refinancing the retail mortgage loan portfolio through the issuance of covered bonds. In September 2013, the Bank began to offer mortgage loans to individual customers through mBank's sales network. This applies to loans that meet the criteria of entry into the register of covered bond collateral and potentially form a basis for their issuance. In the third quarter of 2014, the creation of the new retail mortgage loan portfolio was additionally supported by the implementation of the pooling model under which the Bank started to take over the existing retail loan portfolio of mBank. The first transactions of that type were conducted in September and October 2014.

In the first half of 2015, the Bank continued its activities consisting in creation of a new retail mortgage loan portfolio acquired in cooperation with mBank, improvement of the lending process, acquisition of the retail loan portfolio from mBank under the pooling model (another three pooling transactions) and refinancing this portfolio through the issuance of covered bonds.

Strategy for the sales of commercial property loans

In the years 2016–2019, the Bank will gradually reduce the financing of projects below PLN 10 million and focus on financing undertakings with the value above PLN 10 million (including the limit for derivative transactions) and staying below the credit concentration limit (currently EUR 35 million). The Bank's priority will be to finance commercial property with low investment risk, characterised by high standard, located in large and medium-sized urban areas and to finance only prime locations in smaller urban areas. The Bank will finance in particular real property from the following segments:

- office buildings,
- warehouses,
- retail and service spaces.

The refinancing or financing of purchase of completed, commercialised facilities will be the Bank's main sales objective.

Secondly, the Bank will focus on acquiring the customers from the commercial property developer financing area. These loans will be converted to long-term refinancing loans after the construction phase is completed.

Moreover, in the years 2016–2019, on the basis of the previous experience in the financing of residential projects, the Bank will continue to grant loans for projects from the area of housing developer financing. Loans will be offered to developers with market successes, experience, practice, market awareness and well prepared projects adapted to the market needs. Above all, the Bank will continue to cooperate with developers with whom it has previously successfully implemented housing projects.

Strategy with respect to retail clients

By implementing the strategy for the years 2016–2019, the Bank will develop its operations in the retail area with respect to building a portfolio of mortgage loans for individual customers, both through the sales of new loans, as well as through transfer of the existing loan portfolio from mBank and its refinancing with covered bonds.

The Bank will utilise its own experience, as well as experience of the mBank Group in this market, following criteria for the qualification of loans to be used in the issuance of covered bonds. The mBank Group aspires to increase the share in the financing of the market of mortgage loans for individual customers to approx. 10% by 2019.

Strategy for the refinancing of mBank Hipoteczny

The activity of mBank Hipoteczny in the years 2016-2019 will be financed from six major sources:

- covered bonds, including:
    - covered bonds secured with retail mortgage loans (in PLN),
    - covered bonds secured with commercial mortgage loans (in PLN, EUR),
- own bonds,
- long-term credit facilities (in PLN, EUR),
- term and current deposits, including:
    - from other financial institutions
    - from retail clients,
- a subordinated loan obtained from mBank SA,
- equity.

By increasing the balance sheet total over the coming years, mBank Hipoteczny will seek to build a structure of assets that will enable the issuing of the largest possible volume of covered bonds, within the limits imposed by applicable regulations.

The Bank plans issues both in PLN and in EUR. In line with the current practice, maturities of individual tranches will be between 5 and 10 years.

5. The Bank's authorities

Shareholders

Shareholding structure of mBank Hipoteczny S.A.

Shareholder's name	Registered share capital in PLN '000	Shares		Voting rights at the General Shareholders' Meeting	
		Number ('000)	%	Number of shares ('000)	%
MLV.45 Sp. z o. o. Sp. komandytowa	208,200	2,082	73.06	2,082	73.06
mBank S.A.	76,800	768	26.94	768	26.94
Total	**285,000**	**2,850**	**100**	**2,850**	**100**

The Bank did not conclude any contracts which could result in a change of the proportion of shares held by existing shareholders and bondholders.

The Bank does not cooperate with international public institutions.

Management Board

As at 30 June 2015, the composition of the Management Board of mBank Hipoteczny was as follows:

- Piotr Cyburt — President of the Management Board
- Marcin Romanowski — Member of the Management Board
- Grzegorz Trawiński — Member of the Management Board
- Marcin Wojtachnio — Member of the Management Board

Mr Grzegorz Trawiński was appointed a Member of the Management Board by resolution of the Supervisory Board on 31 March 2015.

Appointment and dismissal of Member of the Management Board and their powers:

The Supervisory Board appoints and dismisses Members of the Management Board, including the President of the Management Board.
Appointment of two Members of the Management Board, including the President of the Management Board and Member of the Management Board responsible for risk takes place with the consent of the Polish Financial Supervision Authority. The application for such consent is submitted by the Supervisory Board.

The Bank's Management Board handles all matters of the Bank and represents the Bank, e.g. it makes decisions on the issuance of covered bonds and bonds, determining the scope of issue in line with the strategies and annual operating plans approved by the Supervisory Board. The scope of responsibility of the Bank's Management Board includes all matters not reserved for other bodies of the Bank, under the Statute or provisions of the law.

Principles of amending the Articles of Association

In accordance with Article 430 § 1 of the Code of Commercial Partnerships and Companies, an amendment to the Articles of Association requires a resolution of the Shareholders' Meeting and entry in the registry.
In accordance with Article 34(1) of the Banking Law, any amendment to the Bank's Articles of Association requires an authorisation of the Polish Financial Supervision Authority where such amendment relates to:

1) the business name, which should contain the word 'bank' and be distinct from the names of other banks, and indicate whether the bank is a state bank, a joint stock bank, or a cooperative bank;
2) the bank's registered office, objects and scope of activity, taking into account activities referred to in Article 69(2) items 1–7 of the Act on Trading in Financial Instruments of 29 July 2005 which the bank intends to perform in accordance with Article 70(2) of that act;
3) governing bodies and their competence, special consideration being given to the competence of the members of the Management Board, referred to in Art. 22b(1) of the Banking Law, procedures for decision taking, basic organisational structure of the bank, principles of making representations with respect to property rights and obligations, procedures for issuing internal regulations and procedures for adopting decisions with respect to assuming liabilities or disposing assets whose aggregate value in relation to one entity exceeds 5% of own funds;
4) principles for the functioning of the internal control system;
5) own funds and principles for financial management

and share privilege or restrictions with respect to the voting right in a joint stock bank.

Supervisory Board

The composition of the Supervisory Board of mBank Hipoteczny S.A. as at 30 June 2015:

- Cezary Kocik – Chairman of the Supervisory Board
- Hans-Dieter Kemler – Deputy Chairman of the Supervisory Board
- Joerg Hessenmueller – Member of the Supervisory Board
- Lidia Jabłonowska-Luba – Member of the Supervisory Board
- Michał Popiołek – Member of the Supervisory Board
- Dariusz Solski – Member of the Supervisory Board
- Mariusz Tokarski – Member of the Supervisory Board

On 11 April 2014, the Supervisory Board was appointed for the ninth term of office by the Annual General Meeting of mBank Hipoteczny S.A. in the above composition, except for Mr Mariusz Tokarski. Mr Mariusz Tokarski was appointed a Member of the Supervisory Board on 3 July 2014 and a Member of the Audit Committee on 16 July 2014.

In accordance with paragraph 14, item 5 of the Memorandum of Association of mBank Hipoteczny S.A., the General Shareholders' Meeting decides, by resolution, on appointing and recalling Members of the Supervisory Board and establishing the terms of their remuneration.

In accordance with paragraph 3, item 9 of the Rules and Regulations of the Supervisory Board of mBank Hipoteczny S.A., the Supervisory Board is responsible for determining the terms of contracts and remuneration for Members of the Bank's Management Board.

The Supervisory Board has two Committees: the Audit Committee and the Risk Committee.

Audit Committee

As at 30 June 2015, the composition of the Audit Committee was as follows:

- Joerg Hessenmueller – Chairman of the Committee
- Hans-Dieter Kemler – Member of the Committee
- Dariusz Solski – Member of the Committee
- Mariusz Tokarski — Member of the Committee

Duties of the Audit Committee include:

- monitoring the financial reporting process,
- monitoring the performance of internal control, internal audit and risk management systems,
- monitoring the performance of financial auditing activities,
- monitoring the independence of the statutory auditor and the entity authorised to audit financial statements.

In the first half of 2015, one meeting of the Audit Committee took place – on 22 April.

Risk Committee

As at 30 June 2015, the composition of the Risk Committee was as follows:

- Lidia Jabłonowska-Luba – Chairwoman of the Committee
- Joerg Hessenmueller – Member of the Committee
- Hans-Dieter Kemler – Member of the Committee
- Michał Popiołek – Member of the Committee

Duties of the Risk Committee include:

- recommending to the Supervisory Board whether to approve or reject the Bank's operating strategy and the principles of cautious and sound management,
- supervision over risk management at the Bank,
- supporting the Supervisory Board in the exercise of supervision over the compliance of the Bank's policy with regard to risk assumption with the Bank's strategy and financial plan,
- recommending to the Supervisory Board whether to approve or reject the Bank's internal procedures for the processes of internal capital estimation, capital management and capital planning,
- recommending to the Supervisory Board whether to approve or reject transactions between the Bank and the members of the Bank's authorities,
- supervision over cooperation of the Bank with the Commerzbank AG group with respect to consolidated supervision over risk and information exchange.

In the first half of 2015, two meetings of the Risk Committee took place – on 27 March and 3 June.

6. Other information

Loans, deposits and interest rates

Basic floating interest rates applied by the Bank are based on the LIBOR and EURIBOR interest rates for foreign currency loans and on the WIBOR rate for loans in PLN. The interest rate applied for a loan on a given day is equal to the Bank's margin specified in the agreement and the base rate.

Related party transactions

MLV 45 sp. z o.o. spółka komandytowa is the direct parent entity of mBank Hipoteczny S.A. mBank S.A. is the parent entity of MLV 45 sp. z o.o. spółka komandytowa (formerly: BRE Holding Sp. z o.o.). Commerzbank AG is the ultimate parent company. Commerzbank AG is the direct parent entity of mBank S.A.

All the transactions between the Bank and its related entities were, according to the Management Board, typical and routine transactions concluded on arm's length terms, and their nature and terms resulted from the current operating activities conducted by the Bank. Transactions with related entities concluded in the normal course of operating activities include loans, deposits, liabilities in respect of debt securities in issue and derivative transactions.

Post balance-sheet events

Increase of the Bank's share capital

On 24 July 2015, the Extraordinary General Shareholders' Meeting of BRE Bank Hipoteczny S.A. adopted Resolution No 1 on the increase of the share capital and the exclusion of shareholders from the pre-emptive right to shares pursuant to which the share capital of mBank Hipoteczny S.A. was increased by PLN 14,000 thousand, i.e. to PLN 299,000 thousand, by way of issuing 140,000 ordinary registered shares with a nominal value of PLN 100 each and issue price of PLN 1,000 each. The new shares were offered for subscription to mBank S.A. through private placement. The shares were paid-up in full on 31 July 2015.

Therefore, the Bank's share capital as at the date of signing these condensed interim financial statements amounts to:

- paid up share capital — PLN 299,000 thousand, including paid up and unregistered share capital — PLN 14,000 thousand,
- share premium — PLN 215,856 thousand.

Decision of the Polish Financial Supervision Authority concerning the issue of the Bank's shares of 13 November 2014

In accordance with the decision of the Polish Financial Supervision Authority of 10 July 2015, the Bank, as of the date of the decision, may classify equity instruments in the form of 100,000 ordinary registered shares with a nominal value of PLN 10,000 and issue price of PLN 1,000 each issued on 13 November 2014 into common equity Tier 1, i.e. it may classify the following amounts in common equity Tier 1 in relation to the said issue:

- PLN 10,000 thousand of share capital,
- PLN 89,938 thousand of share premium.

As at 30 June 2015, the Bank's total capital ratio is 12.56%. Had the issue of instruments of 13 November 2014 not been included in common equity Tier 1, the common equity Tier 1 ratio would have amounted to 8.29%, while the Tier 1 capital ratio and the total capital ratio would have remained unchanged as at 30 June 2015.

7. Management representations

Corporate governance

In its activities, the Bank is guided by the principles of corporate governance and good banking practices, which set high standards based on transparency and ethics in business and maintaining balance between the interests of all parties involved in the operation of the Bank.

On 16 December 2014, the Management Board and on 19 January 2015, the Supervisory Board accepted for application the Corporate Governance Principles for Supervised Institutions (the "Principles"), adopted by the Polish Financial Supervision Authority on 22 July 2014, excluding Principles specified in § 8(4), § 25(1), § 29 and § 53-57. The Principles addressed to shareholders shall be presented at the next General Meeting by the Management Board of mBank Hipoteczny S.A.

Correctness and fairness of the presented financial statements

The Management Board of mBank Hipoteczny S.A. represents that according to its best knowledge:

- financial statements and comparable data have been drawn up in accordance with the applicable accounting principles and reflect truly, fairly and clearly the assets and the financial position of mBank Hipoteczny as well as its financial results,
- the Director's report on the operations for the fist half of 2015 presents a true picture of the situation of mBank Hipoteczny, including a description of basic risks and threats.

The process of preparing financial data for reporting is automated and based on the General Ledger of the Bank. Preparation of data in source systems is subject to formalised operational and acceptance procedures. Creating the General Ledger of the Bank takes place within a process covering respective internal controls. Manual adjustments are subject to special controls.

The process of preparing financial statements at mBank Hipoteczny S.A. is carried out by the Financial Reporting Division in the Accounting and Settlement Department. The responsibility for keeping accounting books and administering the model chart of accounts lies with the Accounting and Settlement Department.

Appointment of the registered audit company

The registered audit company auditing the annual financial statements of mBank Hipoteczny was appointed in accordance with the legal regulations. This entity and the registered statutory auditors performing the audit met the requirements regarding the expressing of an unbiased and independent audit opinion, in accordance with the respective legal regulations in force in Poland.

....	....	....	....
Piotr Cyburt	Marcin Romanowski	Grzegorz Trawiński	Marcin Wojtachnio
President of the Management Board	Member of the Management Board	Member of the Management Board	Member of the Management Board