



Independent Registered Auditor's Opinion To the General Meeting of Shareholders and the Supervisory Board of Powszechna Kasa Oszczędności Bank Polski SA

We have audited the accompanying financial statements of Powszechna Kasa Oszczędności Bank Polski SA (hereinafter called "the Bank"), with its registered office at 15 Puławska Street, in Warsaw, which comprise the statement of financial position as at 31 December 2011, showing total assets and total equity and liabilities of PLN 188,372,690 thousand; the income statement for the financial year from 1 January to 31 December 2011, showing a net profit of PLN 3,953,622 thousand; the statement of comprehensive income for the period from 1 January to 31 December 2011, showing a total comprehensive income of PLN 4,075,527 thousand; the statement of changes in equity, the statement of cash flows for the financial year and additional information on accounting policies and other relevant matters.

The Bank's Management Board is responsible for preparing the financial statements and a Directors' Report in accordance with the applicable regulations, and for the correctness of the accounting records. The Management Board and Members of the Supervisory Board are required to ensure that the financial statements and **the Director's Report meet the requirements set out in the Accounting Act of 29 September 1994 (uniform text, Journal of Laws of 2009, No. 152, item 1223 with further amendments, hereinafter referred to as "the Act").**

Our responsibility was to perform an audit of the accompanying financial statements and to express an opinion on whether in all material respects the financial statements comply with the applicable accounting policies, whether they present fairly the Bank's **financial position** and results, and whether the accounting records constituting the basis for the preparation of the financial statements are properly maintained.

We conducted our audit in accordance with the following:

- (a) the provisions of Chapter 7 of the Act;
- (b) national auditing standards as issued by the National Chamber of Registered Auditors;
- (c) International Standards on Auditing.

Our audit was planned and performed to obtain reasonable assurance that the financial statements were free of material misstatements and omissions. The audit included examining, on a test basis, accounting documents and entries supporting the amounts and disclosures in the financial statements. The audit also included an assessment of the accounting policies applied by the Bank and significant estimates made in the preparation of the financial statements as well as an evaluation of the overall presentation thereof. We believe that our audit provides a reasonable basis for our opinion.

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**Independent Registered Auditor's Opinion
To the General Meeting of Shareholders and the Supervisory Board of
Powszechna Kasa Oszczędności Bank Polski SA (cont.)**

In our opinion, and in all material respects, the accompanying financial statements:

- (a) present fairly the Bank's **financial** position as at 31 December 2011 and of the results of its operations for the year then ended, in accordance with International Financial Reporting Standards as adopted by the European Union;
- (b) comply in form and content with the applicable laws and the Bank's **Memorandum of Association**;
- (c) have been prepared on the basis of properly maintained accounting records in accordance with the applicable accounting principles (policies).

The information in the Directors' Report for the year ended 31 December 2011 has been prepared in accordance with the provisions of the Decree of the Minister of Finance of 19 February 2009 concerning the publication of current and periodic information by issuers of securities and the conditions of acceptance as equivalent information required by the laws of another state not being a member state ("*the Decree*" – Journal of Laws of 2009, No. 33, item 259) and is consistent with the information presented in the audited financial statements.

Conducting the audit on behalf of PricewaterhouseCoopers Sp. z o.o., Registered Audit Firm No. 144:

Antoni F. Reczek
President of the Management Board

PricewaterhouseCoopers Sp. z o.o.

Principal Registered Auditor
No. 90011

Warsaw, 29 February 2012

Powszechna Kasa Oszczędności Bank Polski SA
Independent Registered Auditor's Report on the financial
statements as at and for the year ended 31 December 2011

**Independent registered auditor's report on the financial statements
To the General Meeting of Shareholders 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 the year ended 31 December 2011

I. General information about the Bank

- (a) The Bank was established in 1919 as Poczta 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, the 16th Registration Department. Currently, the Bank is registered under the number KRS 0000026438, and the District Court for the City of Warsaw, the 13th Business Department of the National Court Register, is the competent registration court.

On 14 June 1993, the Bank was assigned a tax identification number (NIP) 525-000-77-38 for making tax settlements. On 18 April 2000, the Bank was assigned a REGON number 016298263 for statistical purposes.

- (b) As at 31 December 2011 the Bank's registered share capital amounted to PLN 1,250,000 thousand and consisted of 1,250,000,000 ordinary shares, each of PLN 1 par value, including:

- 312,500,000 A-series registered shares;
- 197,500,000 A-series bearer shares
- 105,000,000 B-series bearer shares;
- 385,000,000 C-series bearer shares;
- 250,000,000 D-series bearer shares.

- (c) As at 31 December 2011, the Bank's shareholders were:

Shareholder's name	Number of shares held	Par value of shares held (PLN'000)	Type of shares held (ordinary /preference)	Votes (%)
State Treasury	512,406,277	512,406	ordinary	40.99
Bank Gospodarstwa Krajowego	128,102,731	128,103	ordinary	10.25
Other	609,490,992	609,491	ordinary	48.76
Total:	1,250,000,000	1,250,000		100.00

- (d) 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 in Warsaw (hereinafter called "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 Commission dated 26 August 1991, the Brokerage House of PKO BP SA obtained a licence 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 in the National Depository for Securities.

Powszechna Kasa Oszczędności Bank Polski SA **Independent registered auditor's report on the financial statements** **as at and for the year ended 31 December 2011**

I. General information about the Bank (cont.)

(e) In the audited year, the **Bank's** operations comprised:

- accepting cash deposits payable on demand or on an agreed date and maintaining accounts for such deposits;
- granting loans and cash advances;
- granting and confirming bank guarantees;
- clearing cash transactions;
- issuing cards and conducting transactions with the use of cards;
- conducting forward transactions.

At the same time, the Bank conducts brokerage activities through the Brokerage House of PKO BP SA and fiduciary services through the Fiduciary Office.

(f) During the audited year, the Management Board of the Bank comprised:

Zbigniew Jagiełło	President of the Management Board	throughout the year
Piotr Alicki	Vice-President of the Management Board	throughout the year
Bartosz Drabikowski	Vice-President of the Management Board	throughout the year
Andrzej Kołatkowski	Vice-President of the Management Board	from 9 August 2011
Jarosław Myjak	Vice-President of the Management Board	throughout the year
Jacek Obłąkowski	Vice-President of the Management Board	from 30 June 2011
Jakub Papierski	Vice-President of the Management Board	throughout the year
Krzysztof Dresler	Vice-President of the Management Board	to 30 June 2011
Wojciech Papierak	Vice-President of the Management Board	to 30 June 2011

(g) The Bank has the following related entities:

Bankowe Towarzystwo Kapitałowe SA	- subsidiary
Bankowy Fundusz Leasingowy SA	- subsidiary
Centrum Elektronicznych Usług Płatniczych „eService” SA	- subsidiary
Centrum Finansowe Puławska Sp. z o.o. – in liquidation	- subsidiary
Finansowa Kompania „Prywatne Inwestycje” Sp. z o.o., Ukraine	- subsidiary
Inteligo Financial Services SA	- subsidiary
Kredobank SA, Ukraine	- subsidiary
PKO BP BANKOWY Powszechnie Towarzystwo Emerytalne SA	- subsidiary
PKO BP Finat Sp. z o.o.	- subsidiary
PKO Finance AB, Sweden	- subsidiary
PKO Towarzystwo Funduszy Inwestycyjnych SA	- subsidiary
Fort Mokotów Inwestycje Sp. z o.o.	- subsidiary
Qualia Development Sp. z o.o.	- subsidiary
Centrum Haffnera Sp. z o.o.	- jointly controlled entity
Centrum Obsługi Biznesu Sp. z o.o.	- jointly controlled entity
Bank Pocztowy SA	- associate
Kolej Gondolowa Jaworzyna Krynicka SA	- associate
Poznański Fundusz Poręczeń Kredytowych Sp. z o.o.	- associate
Agencja Inwestycyjna CORP-SA SA	- associate

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I. General information about the Bank (cont.)

and the companies that are members of the capital groups of Bankowe Towarzystwo **Kapitałowe SA**, Bankowy Fundusz Leasingowy SA and Qualia Development Sp. z o.o. as well as indirect jointly controlled entities that are members of the capital group Centrum Haffnera Sp z o.o. and indirect associates that are members of the capital group Bank Pocztowy SA.

- (h) The Bank is an issuer of securities admitted for trading on the Warsaw Stock Exchange. In accordance with the choice of selecting accounting policies permitted by the Accounting Act, the Company has decided to prepare its financial statements in accordance with IFRS as adopted by the European Union since 2005.

The decision to prepare the Bank's financial statements in accordance with these standards was made by the General Shareholders' Meeting in their Resolution No. 28/2005 passed on 19 May 2005.

- (i) As the Parent Company of the Group, the Bank has also prepared consolidated financial statements according to IFRS as adopted by the European Union as at 23 February 2012. **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 statements.**

Powszechna Kasa Oszczędności Bank Polski SA
Independent registered auditor's report on the financial statements
as at and for the year ended 31 December 2011

II. Information about the audit

- (a) The audit of the financial statements as at and for the year ended 31 December 2011 was conducted by PricewaterhouseCoopers Sp. z o.o. having its seat in Warsaw, Al. Armii Ludowej 14, registered audit firm no. 144. The audit was conducted on behalf of the registered audit firm under the supervision of the principal registered auditor Antoni F. Reczek (no. 90011).
- (b) PricewaterhouseCoopers Sp. z o.o. was appointed independent registered auditor to the Bank by Resolution No. 15/2008 of the Supervisory Board dated 28 March 2011 in accordance with paragraph 15, clause 1, item 3 of the Bank's Memorandum of Association.
- (c) PricewaterhouseCoopers Sp. z o.o. and the principal registered auditor conducting the audit are independent of the audited entity within the meaning of art. 56, clause 2-4 of the Act on registered auditors and their council, entities entitled to provide audit of financial statements and public supervision of 7 May 2009 (Journal of Laws 2009, No. 77, item 649, with subsequent amendments).
- (d) The audit was conducted in accordance with an agreement dated 14 April 2011, in the following periods:
- interim audit from 28 October to 22 December 2011;
 - final audit from 9 January to 29 February 2012.

Powszechna Kasa Oszczędności Bank Polski SA

Independent registered auditor's report on the financial statements as at and for the year ended 31 December 2011

III. The Company's results and financial position

The financial statements do not take account of the impact of inflation. The consumer price index (on a December to December basis) amounted to 4.6% in the audited year (3.1% in 2010).

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

- As at 31 December 2011, total assets amounted to PLN 188,372,690 thousand and they increased by PLN 21,133,771 thousand (i.e. by 13%) compared with the balance as at 31 December 2010.
- The increase was mainly financed with the increase in amounts due to customers of PLN 14,741,626 thousand (i.e. 11%), mainly as a result of an increase in deposits and an increase in liabilities in respect of an issue of debt securities of PLN 3,105,588 thousand (i.e. 100%) as a result of issuing mainly bonds to the Polish market, accompanied by an increase in the balance of amounts due to banks of PLN 1,157,209 thousand, i.e. 28%), and in equity of PLN 1,600,527 thousand (i.e. 8%).
- The main source of financing of assets in 2011 were amounts due to customers (similarly to the prior year). The balance of amounts due to customers amounted to PLN 150,030,681 thousand as at the balance date and represented 80% of the total assets (a decrease of 1 pp compared with the balance as at 31 December 2010). The change in the balance of amounts due to customers was mainly the effect of a considerable growth in amounts due to individuals (an increase of PLN 9,077,028 thousand, i.e. 10%, compared with the balance as at 31 December 2010) and to corporate customers (an increase of PLN 7,889,181 thousand, i.e. 23% compared with the balance as at 31 December 2010), including amounts due in respect of a loan granted by a subsidiary PKO Finance AB of CHF 250,000 thousand (Note 13). The loan is related to the issue of bonds to international markets carried out in 2011 on behalf of the Bank by PKO Finance AB.
- The balance of liabilities in respect of debt securities in issues as at 31 December 2011 was PLN 3,105,588 thousand and related to short-term bonds issued to the Polish market of PLN 2,929,973 thousand and structured bank securities based on the S&P500 index, the price of gold or the price of copper of PLN 175,615 thousand (there were no liabilities in respect of issuing of securities as at 31 December 2010).
- The balance of amounts due to other banks was PLN 5,321,390 thousand as at the balance date (an increase of PLN 1,157,209 thousand, i.e. 28% compared with the prior year) and comprised mainly a consortium loan in Swiss francs received, the amount of which in the Polish currency was PLN 3,443,872 thousand (PLN 2,999,116 thousand as at 31 December 2010 – the 15% increase in the valuation of the loan resulted mainly from a similar increase in the Swiss franc's exchange rate compared with 31 December 2010). There was also an increase in the balances of inter-bank deposits accepted (an increase of PLN 399,877 thousand, i.e. 41%) and current accounts (an increase of PLN 378,038 thousand, i.e. 861%) (Note 12).

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

- As at 31 December 2011, the liabilities due to negative valuation of derivatives amounted to PLN 2,645,281 thousand (PLN 2,404,795 thousand as at 31 December 2010). The increase in the balance as at the balance date was mainly a result of a higher valuation of IRS transactions and currency transactions compared with the balance as at the end of 2010 and it was offset by a drop in the negative valuation on CIRS transactions (Note 4)
- Subordinated liabilities amounted to PLN 1,614,377 thousand as at the balance date (PLN 1,611,779 thousand as at 31 December 2010) and they comprised the valuation of bonds issued by the Bank in 2007 in the nominal amount of PLN 1,600,700 thousand (Note 15).
- The balance of equity as at 31 December 2011 was PLN 22,802,375 thousand (PLN 21,201,848 thousand as at 31 December 2010). The increase in the balance was mainly brought about by the profit generated by the Bank in 2011 of PLN 3,953,622 thousand. At the same time, the Bank earmarked PLN 2,475,000 thousand out of the profit for 2010 for payment of dividend. The remaining portion of the profit for 2010 was earmarked for increasing supplementary capital (by PLN 800,000 thousand) and reserves (by PLN 36,209 thousand) (Note 18).
- The balance of own funds calculated on the regulatory basis was PLN 17,347,921 thousand as at 31 December 2011 (PLN 16,562,906 thousand as at 31 December 2010) and it was PLN 5,712,542 thousand higher than the total capital requirement (PLN 11,635,379 thousand as at the end of 2011). The capital adequacy ratio calculated as at the balance date based on the bank portfolio and the trading portfolio was 11.93% and decreased by 0.06 pp compared with the end of the prior year. The decrease in the capital adequacy ratio resulted mainly from the increase in the capital requirement in respect of credit risk by PLN 860,601 thousand (i.e. by 9%) which was due to the growth of the loan portfolio, offset with the increase in own funds of PLN 785,015 thousand (i.e. 5%), mainly as a result of earmarking a portion of the net profit for reserve capital.
- The higher level of financing was mainly reflected in the PLN 11,125,520 thousand (i.e. 9%) increase in loans and advances to customers **and the PLN 4,292,681 thousand (i.e. 43%)** increase in available-for-sale investment securities. Cash and balances with the central bank also increased by PLN 2,947,718 thousand (i.e. by 48%), financial instruments designated at fair value through profit or loss increased by PLN 1,708,870 thousand, i.e. by 16%) and the positive valuation of derivatives increased by PLN 1,345,385 thousand, i.e. by 78%).
- As at the balance date, loans and advances to customers amounted to PLN 140,058,649 thousand and represented 74% of the total assets (a decrease of 3 pp compared with the end of 2010). The gross balance of the loan portfolio as at 31 December 2011 amounted to PLN 145,041,439 thousand and it increased by PLN 11,842,826 thousand (i.e. by 9%) compared with the balance as at 31 December 2010. The increase resulted mainly from the increase in the balance of mortgage and corporate loans granted to customers from the non-financial sector (an increase of PLN 8,477,904 thousand, i.e. 14% and PLN 4,494,713 thousand, i.e. 12% respectively) (Note 6).

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

- The quality of the loan portfolio as at the balance date measured with the ratio of impaired loans to the total balance of loans and advances to customers deteriorated slightly compared with the end of 2010. As at 31 December 2011, the ratio of impaired loans to the total loans and advances to customers increased by 0.1 pp and amounted to 7.2%. At the same time, the coverage of impaired loans with impairment allowances amounted to 41.7% as at 31 December 2011 and was 1.8 pp higher than as at the end of the prior financial year. The deterioration in the quality of the loan portfolio related mainly to loans to small- and medium-sized enterprises and mortgage loans.
- The balance of available-for-sale investment securities amounted to PLN 14,168,933 thousand as at the balance date and was PLN 4,292,681 thousand (i.e. 43%) higher than as at the end of 2010. The increase related mainly to Treasury bonds (an increase of PLN 2,823,806 thousand, i.e. 51%). There was also an increase in the balances of corporate bonds (of PLN 828,287 thousand, i.e. 55%) and municipal bonds (of PLN 634,183 thousand, i.e. 22%). The entire balance relates to Polish issuers (Note 7).
- The balance of financial assets designated at fair value through profit or loss amounted to PLN 12,467,201 thousand as at the balance date. The increase in the balance (of PLN 1,708,870 thousand, i.e. 16%) resulted mainly from a change in the structure of the balance - the share of short-term NBP bills increased (by PLN 4,596,011 thousand, i.e. by 115%) and the balance of Polish T-bonds was lower than in the prior year (by PLN 3,420,366 thousand, i.e. by 72%) (Note 5).
- Other liquid assets, which comprised cash and balances with the central bank, amounts due from banks, financial assets held for trading and derivative financial instruments increased in aggregate as at the balance date by PLN 4,041,502 thousand (i.e. by 34%), which was mainly the result of an increase in the balance of cash and balances with the central bank (of PLN 2,947,718 thousand i.e. 48%) and in derivative financial instruments (an increase of PLN 1,345,385 thousand, i.e. 78%) (Notes 1-4).
- The Bank's liquidity ratios up to 1 month and up to 3 months, calculated on the basis of data on the maturities of assets and liabilities according to real terms maturity dates amounted to 1.90 and 1.66 respectively (1.98 and 1.80 as at the end of 2010).
- The share of interest-bearing assets in the total assets increased by 0.1 pp compared with the balance as at 31 December 2010 and amounted to 94.1% as at the end of 2011. The loans to deposits ratio (L/D) was on a level of 93.4% as at the end of 2011 (95.3% as at the end of 2010).
- Operating profit amounted to PLN 4,913,931 thousand in 2011 and as PLN 791,014 thousand (19%) higher than in 2010. The operating profit comprised mainly: net interest income of PLN 7,504,969 thousand, net fee and commission income of PLN 2,872,801 thousand and net foreign exchange gains of PLN 331,367 thousand. At the same time, the operating profit was reduced by administrative expenses of PLN 4,058,490 thousand and net impairment allowance and write-downs of PLN 1,812,122 thousand.

Powszechna Kasa Oszczędności Bank Polski SA
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III. The Company's results and financial position (cont.)

- Net interest income amounted to PLN 7,504,969 thousand in 2011 and was PLN 1,121,193 thousand (i.e. 18%) higher than the net interest income generated in 2010. The increase was mainly due to higher interest on loans and advances to customers (an increase of PLN 1,335,089 thousand, i.e. 16%), which was mainly due to a **9% higher volume of the Bank's loan portfolio. In 2011, the interest margin**, calculated as the ratio of net interest income to interest income increased by 1 pp compared with 2010 and amounted to 64% (Note 19). The interest spread, calculated as the difference between the rate of interest income on interest-bearing assets and the price of external financing was 4.2% and it did not change significantly (an increase of 0.2 pp) compared with 2010.
- Net fee and commission income in 2011 was lower than in 2010 and amounted to PLN 2,872,801 thousand (a decrease of PLN 64,758 thousand, i.e. 2%), which was mainly due to lower fee and commission income than in the prior year. Compared with 2010, fee and commission income dropped by PLN 56,607 thousand (a drop of 2% to PLN 3,621,880 thousand). The decrease was mainly related to commission in respect of loan insurance (a drop of PLN 138,002 thousand, i.e. 21%) and was partly offset by an increase in income from payment cards and from loans and advances granted (an increase of PLN 57,237 thousand and PLN 49,934 thousand respectively, i.e. 6% and 10%). At the same time, fee and commission expense increased by PLN 8,151 thousand, i.e. by 1% to PLN 749,079 thousand (Note 20).
- In the audited year, net foreign exchange gains amounted to PLN 331,367 thousand and were PLN 9,981 thousand (i.e. 3%) lower than in 2010. Net foreign exchange gains are a net position of gains of PLN 523,174 thousand (losses of PLN 1,026,841 thousand in 2010) in respect of foreign exchange differences on instruments designated at fair value through profit or loss and losses of PLN 191,807 thousand (gains of PLN 1,368,189 thousand in 2010) in respect of other assets and liabilities and realized foreign exchange differences (Note 23).
- In 2011, administrative expenses were PLN 156,378 thousand, i.e. 4% higher than in the prior year and amounted to PLN 4,058,490 thousand. The increase in employee costs and overheads by a total of 63,694 (i.e. 2%) was accompanied by the increase in payments to the Banking Guarantee Fund of PLN 83,353 thousand, i.e. 156% (Note 25). The general effectiveness of operations calculated as the ratio of costs to income (the C/I ratio) improved in 2011 (the ratio decreased by 2.2 pp to 37.6%). The positive change in the ratio was due to higher income than in 2010 (mainly interest income).
- Net impairment allowances in 2011 amounted to PLN 1,812,122 thousand (PLN 1,767,046 thousand in 2010). The increase in the net impairment allowance (recognized in the income statement) was mainly related to business and mortgage loans to customers - an increase of PLN 156,461 thousand, i.e. 29%) and PLN 120,907 thousand (i.e. 47%) respectively, and it was offset by a decrease in net impairment allowance in respect of consumer loans (a decrease of PLN 146,686 thousand, i.e. 18%). At the same time, the costs of recording provisions for off-balance liabilities were lower by PLN 68,886 thousand, i.e. 66%) in 2011 (Note 24). The cost of risk amounted to 1.3% in 2011 (1.4% in 2010).

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

- Gross profitability (calculated as profit before income tax to total income) amounted to 30.7% in the audited year and increased by 2.0 pp compared with the prior year.
- Income tax expense in 2011 amounted to PLN 960,309 thousand (PLN 811,708 thousand in 2010). The effective tax rate amounted to 19.5% in 2011 and was 0.2 pp higher than in 2010.
- As a result, in 2011 the Bank generated a net profit of PLN 3,953,622 thousand which was PLN 642,413 thousand (i.e. 19%) higher than the net profit for 2010. In 2011 net profitability (calculated as net profit to total income) amounted to 24.7% (23.1% in 2010).
- The return on assets (calculated as net profit to average total assets) amounted to 2.2% in 2011 and increased by 0.1 pp compared with 2010. In the audited year, the return on equity amounted to 18.0% and it was 2.0 pp higher than in 2010.

The financial statements of the Bank have been prepared on the going concern basis.

Powszechna Kasa Oszczędności Bank Polski SA
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IV. Discussion of financial statement components

STATEMENT OF FINANCIAL POSITION as at 31 December 2011

ASSETS	Note	31.12.2011	31.12.2010	Change	Change	31.12.2011	31.12.2010
		PLN'000	PLN'000	PLN'000	(%)	Structure (%)	Structure (%)
Cash and balances with the central bank	1.	9,060,280	6,112,562	2,947,718	48	5	4
Amounts due from banks	2.	2,320,198	2,379,239	(59,041)	(2)	1	1
Trading assets	3.	1,311,089	1,503,649	(192,560)	(13)	1	1
Derivative financial instruments	4.	3,065,149	1,719,764	1,345,385	78	2	1
Financial assets designated at fair value through profit and loss	5.	12,467,201	10,758,331	1,708,870	16	7	7
Loans and advances to customers	6.	140,058,649	128,933,129	11,125,520	9	74	77
Investment securities available for sale	7.	14,168,933	9,876,252	4,292,681	43	7	6
Investments in subsidiaries, jointly controlled entities and associates	8.	1,497,975	1,467,507	30,468	2	1	1
Non-current assets held for sale		20,410	19,784	626	3	-	-
Intangible assets	9.	1,522,568	1,528,267	(5,699)	-	1	1
Tangible fixed assets	10.	2,013,314	2,077,140	(63,826)	(3)	1	1
Deferred income tax asset	26.	384,134	462,923	(78,789)	(17)	-	-
Other assets	11.	482,790	400,372	82,418	21	-	-
Total assets		188,372,690	167,238,919	21,133,771	13	100	100

Powszechna Kasa Oszczędności Bank Polski SA
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as at and for the year ended 31 December 2011

IV. Discussion of financial statement components (cont.)

STATEMENT OF FINANCIAL POSITION as at 31 December 2011 (cont.)

LIABILITIES AND EQUITY	Note	31.12.2011	31.12.2010	Change	Change	31.12.2011	31.12.2010
		PLN'000	PLN'000	PLN'000	(%)	Structure (%)	Structure (%)
Amounts due to the central bank		3,454	3,370	84	2	-	-
Amounts due to banks	12.	5,321,390	4,164,181	1,157,209	28	3	3
Derivative financial instruments	4.	2,645,281	2,404,795	240,486	10	1	1
Amounts due to customers	13.	150,030,681	135,289,055	14,741,626	11	80	81
Debt securities in issue	14.	3,105,588	-	3,105,588	100	2	-
Subordinated liabilities	15.	1,614,377	1,611,779	2,598	-	1	1
Other liabilities	16.	2,156,523	1,787,599	368,924	21	1	1
Current income tax liabilities		77,532	61,854	15,678	25	-	-
Provisions	17.	615,489	714,438	(98,949)	(14)	-	-
Total liabilities		165,570,315	146,037,071	19,533,244	13	88	87
Share capital		1,250,000	1,250,000	-	-	1	1
Other capital		17,598,753	16,640,639	958,114	6	9	11
Net profit for the year		3,953,622	3,311,209	642,413	19	2	1
Total equity	18.	22,802,375	21,201,848	1,600,527	8	12	13
Total liabilities and equity		188,372,690	167,238,919	21,133,771	13	100	100

INCOME STATEMENT

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IV. Discussion of financial statement components (cont.)

for the financial year ended 31 December 2011

	Note	2011 PLN'000	2010 PLN'000	Change PLN'000	Change (%)	2011 Structure (%)	2010 Structure (%)
Interest and similar income		11,818,059	10,107,552	1,710,507	17	74	70
Interest expense and similar charges		(4,313,090)	(3,723,776)	(589,314)	16	40	37
Net interest income	19.	7,504,969	6,383,776	1,121,193	18		
Fee and commission income		3,621,880	3,678,487	(56,607)	(2)	23	26
Fee and commission expense		(749,079)	(740,928)	(8,151)	1	7	7
Net fee and commission income	20.	2,872,801	2,937,559	(64,758)	(2)		
Dividend income	21.	94,028	109,895	(15,867)	(14)	-	1
Net income from financial instruments designated at fair value through profit and loss	22.	(78,538)	(56,489)	(22,049)	39	1	1
Gains less losses from investment securities		16,303	71,282	(54,979)	(77)	-	1
Net foreign exchange gains	23.	331,367	341,348	(9,981)	(3)	2	2
Other operating income		110,791	48,012	62,779	131	1	-
Other operating expense		(67,178)	(43,308)	(23,870)	55	-	-
Net impairment allowance and write-downs	24.	(1,812,122)	(1,767,046)	(45,076)	3	15	17
Administrative expenses	25.	(4,058,490)	(3,902,112)	(156,378)	4	37	38
Operating profit		4,913,931	4,122,917	791,014	19		
Income tax expense	26.	(960,309)	(811,708)	(148,601)	18		
Net profit		3,953,622	3,311,209	642,413	19		
Total income		15,992,428	14,356,576	1,635,852	11	100	100
Total expenses		(11,078,497)	(10,233,659)	(844,838)	8	100	100
Profit before income tax		4,913,931	4,122,917	791,014	19		

Selected ratios presenting the Bank's financial position and results

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IV. Discussion of financial statement components (cont.)

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

	2011	2010
Profitability ratios		
Gross profitability (profit before tax/total income)	30.7%	28.7%
Net profitability (net profit / total income)	24.7%	23.1%
ROE (net profit /average net assets) (2)	18.0%	16.0%
Return on assets (net profit /average total assets) (2)	2.2%	2.1%
Cost to income ratio (administrative expenses / profit on banking activities (3)	37.6%	39.8%
Profitability ratio on interest-bearing assets (interest income / average interest-bearing assets) (2)	7.1%	6.7%
Cost of borrowings (interest expense / average interest-bearing liabilities) (2)	2.9%	2.7%
Asset quality ratios		
Interest-bearing assets to total assets (4)	94.1%	94.0%
Impaired loans to total gross loans and advances to customers	7.2%	7.1%
Coverage with impairment allowances of impaired loans and advances to customers	41.7%	39.9%
Cost of risk (5)	1.3%	1.4%
Liquidity ratios		
Liquidity up to 1 month (6)	1.90	1.98
Liquidity up to 3 months (6)	1.66	1.80
Loans to deposits	93.4%	95.3%
Other ratios		
Capital adequacy ratio	11.93%	11.99%
Regulatory equity (PLN'000)	17,347,921	16,562,906
Total capital requirement (PLN'ooo)	11,635,379	11,049,447

(1) The values of the individual ratios may differ from the values presented in the financial statements due to a different calculation method being used.

(2) The average balances of balance items were calculated on the basis of the balances of individual items at the beginning and the end of the current and prior financial year.

(3) The profit on banking activities defined as operating profit less administrative expenses and net impairment allowances.

(4) Interest-bearing assets are defined as balances with the central bank (excluding cash), amounts due from banks and customers, investment securities and securities designated at fair value through profit or loss and held for trading.

(5) The cost of risk calculated by dividing net impairment allowance to be held on loans and advances to customers for the year by the average balance of gross loans and advances to customers.

(6) Liquidity ratios are understood as the ratio of assets receivable to liabilities payable at the actual maturities as at the balance date.

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IV. Discussion of financial statement components (cont.)

Statement of financial position as at 31 December 2011

1. Cash and balances with the central bank

As at 31 December 2011, "Cash and balances with the central bank" amounted to PLN 9,060,280 thousand (PLN 6,112,562 thousand at the end of 2010) and included PLN 6,845,759 thousand of cash maintained by the Bank on an account in the National Bank of Poland (PLN 3,782,717 thousand as at 31 December 2010).

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 held with the NBP as at 31 December 2011 amounted to PLN 4,975,268 thousand (PLN 4,553,482 thousand as at 31 December 2010).

2. Amounts due from banks

The balance of amounts due from banks as at the respective balance dates and the movements therein are presented in the table below:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Placements with other banks	1,914,393	1,501,919	412,474	27
Current accounts	279,622	557,408	(277,786)	(50)
Loans and advances granted	125,777	317,531	(191,754)	(60)
<i>- including: to related entities</i>	<i>119,705</i>	<i>233,476</i>	<i>(113,771)</i>	<i>(49)</i>
Receivables in respect of unsettled transactions	32,385	28,089	4,296	15
Cash in transit	1,731	6,862	(5,131)	(75)
Total	2,353,908	2,411,809	(57,901)	(2)
Impairment allowance in respect of amounts due	(33,710)	(32,570)	(1,140)	4
Total, net	2,320,198	2,379,239	(59,041)	(2)

The decrease in the balance of loans and advances granted (of PLN 191,754 thousand, i.e. 60%) was mainly a result of Kredobank SA repaying a part of the loan granted by the Bank (a drop in the exposure of PLN 113,771 thousand, i.e. 49% compared with the balance as at 31 December 2010). The decrease was partly offset by an increase in the balance of placements with other banks (an increase of PLN 412,474 thousand, i.e. 27%).

As at 31 December 2011, impairment allowance in respect of amounts due from banks was PLN 33,710 thousand and was PLN 1,140 thousand (i.e. 4%) higher than the balance as at 31 December 2010. The balance mainly comprised an allowance for amounts due from banks in respect of transactions in derivative instruments not yet cleared but declared due, in the amount of PLN 32,385 thousand (PLN 28,089 thousand as at 31 December 2010).

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IV. Discussion of financial statement components (cont.)

2. Amounts due from banks (cont.)

Amounts due denominated in foreign currencies represented an equivalent of PLN 1,975,590 thousand, i.e. 84%) of amounts due from banks as at the balance date (PLN 2,168,762 thousand, i.e. 90% of the balance as at 31 December 2010).

3. Financial assets held for trading

As at 31 December 2011, the balance of 'Financial assets held for trading' with a value of PLN 1,311,089 thousand comprised the following items:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Treasury bonds (PLN)	1,219,069	1,483,144	(264,075)	(18)
Treasury bills	49,402	-	49,402	100
Other	42,618	20,505	22,113	108
Total	1,311,089	1,503,649	(192,560)	(13)

The fall in the valuation of financial assets held for trading of PLN 192,560 thousand (i.e. 13%) as at the balance date was due to a decrease in **the Bank's exposure to Polish Treasury bonds** (down PLN 264,075 thousand, i.e. 18%) and it was partly offset by an increase in the **Bank's exposure in Treasury bills (up by PLN 49,402 thousand**, there were none in the portfolio as at 31 December 2010) and other securities (up by PLN 22,113 thousand, i.e. 108%). The portfolio of financial assets held for trading was subject to significant fluctuations as at the end of the individual months of the audited period, reaching the highest balance as at the end of March 2011 (PLN 3,329,249 thousand).

As at 31 December 2011, Polish Treasury bonds represented 93% of the balance of all financial assets held for trading.

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IV. Discussion of financial statement components (cont.)

4. Derivative financial instruments

The balance of receivables in respect of positive fair value of derivatives increased by PLN 1,345,385 thousand (i.e. by 78%) compared with the end of 2010 and amounted to PLN 3,065,149 thousand as at 31 December 2011. The liabilities in respect of negative fair value of derivatives amounted to PLN 2,645,281 thousand and they increased by PLN 240,486 thousand (i.e. by 10%) compared with the end of 2010. The above balances comprised the following items:

	31.12.2011 Assets PLN'000	31.12.2011 Liabilities PLN'000	31.12.2010 Assets PLN'000	31.12.2010 Liabilities PLN'000
Interest rate swaps	2,399,482	2,378,165	1,586,292	2,252,113
- including CIRS:	419,640	421,039	126,219	687,977
Currency forwards	557,624	195,991	80,560	126,585
Options	106,492	70,112	46,397	25,382
Other	1,551	1,013	6,515	715
Total	3,065,149	2,645,281	1,719,764	2,404,795

The movements in the above-mentioned balances as at 31 December 2011 compared with the balances as at 31 December 2010 are presented in the table below:

	Change Assets PLN'000	Change Assets %	Change Liabilities PLN'000	Change Liabilities %
Interest rate swaps	813,190	51	126,052	6
- including CIRS	293,421	232	(266,938)	(39)
Currency forwards	477,064	592	69,406	55
Options	60,095	130	44,730	176
Other	(4,964)	(76)	298	42
Total	1,345,385	78	240,486	10

In 2011, there was an increase in both the positive and negative fair values of derivatives. The most significant change related to the increase in the positive fair value of interest rate transactions and currency forwards and was due to (among other things) the increase in the nominal amounts of the transactions concluded (an increase of PLN 157,708,950 thousand, i.e. 36% and PLN 23,845,195 thousand, i.e. 95% respectively).

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IV. Discussion of financial statement components (cont.)

4. Derivative financial instruments (cont.)

Beginning from 2009, the Bank has applied hedge accounting (a macro cash flow hedge) in accordance with IAS 39 F6.2 – F6.3. In 2011, the Bank established one new hedging relationship:

- A hedge of the cash flow volatility on floating interest rate loans in CHF as a result of the interest rate risk, using IRS transactions. In connection with establishing the new hedging relationship in 2011, a net amount of PLN 28,415 thousand was recognized in the statement of comprehensive income.

In addition, the Bank continued to use the hedging relationships created in the previous years:

- a hedge of the cash flow volatility on mortgage loans denominated in CHF and negotiated deposits in PLN as a result of the interest rate risk and the exchange risk, using CIRS transactions – due to the strategy being pursued in 2011, a net amount of PLN 45,337 thousand was recognized in the statement of comprehensive income;
- a hedge of the cash flow volatility on floating interest rate loans in EUR as a result of the interest rate risk, using IRS transactions – due to the strategy being pursued in 2011, a net amount of PLN 70,325 thousand was recognized in the statement of comprehensive income;
- a hedge of the cash flow volatility on floating interest rate loans in PLN as a result of the interest rate risk, using IRS transactions – due to the strategy being pursued in 2011, a net amount of PLN 184 thousand was recognized in the statement of comprehensive income.

In total, as a result of applying hedge accounting the Bank recognized PLN 144,261 thousand deferred tax (PLN 98,648 thousand net of deferred income tax in 2010) in the statement of comprehensive income. At the same time, the Bank recognized the ineffective portion of cash flow hedges of PLN 64,342 thousand in the income statement (PLN 82,879 thousand in 2010) (Note 22).

At the same time, the amount of PLN (1,112,235) thousand was cleared to net profit out of comprehensive income (PLN 267,292 thousand in 2010) (Note 19).

In accordance with the Bank's accounting policies, the measurement of derivative hedging transactions is decomposed and affects the following items:

- foreign exchange differences on revaluation of the nominal amount – net foreign exchange gains;
- interest accrued as at the balance date – net interest income;
- mark-to-market – revaluation reserve and net gain/(loss) on financial instruments designated at fair value (the ineffective part).

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IV. Discussion of financial statement components (cont.)

4. Derivative financial instruments (cont.)

As at the balance date, the net fair value measurement of derivative transactions designated as hedges as part of two hedging relationships applied by the Bank based on these instruments amounted to PLN 174,327 thousand:

	Assets 31.12.2011 PLN'000	Liabilities 31.12.2011 PLN'000	Net 31.12.2011 PLN'000
Fair value measurement, including:	313,182	67,845	381,027
- measurement until the date of introducing hedge accounting (net income/loss from financial instruments designated at fair value)	111,117	(100,373)	10,744
- measurement from the date of introducing hedge accounting (revaluation reserve)	202,065	168,218	370,283
Foreign exchange differences on revaluation of the nominal amount (net foreign exchange gains/losses); Interest accrued (net interest income)	74,732 129,011	(453,863) 43,420	(379,131) 172,431
Total	516,925	(342,598)	174,327

As at 31 December 2010, the net measurement to fair value of derivative transactions designated as hedges amounted to PLN (402,062) thousand:

	Assets 31.12.2010 PLN'000	Liabilities 31.12.2010 PLN'000	Net 31.12.2010 PLN'000
Fair value measurement, including:	114,394	202,271	316,665
- measurement until the date of introducing hedge accounting (net income/loss from financial instruments designated at fair value)	140,855	(101,320)	39,535
- measurement from the date of introducing hedge accounting (revaluation reserve)	(26,461)	303,591	277,130
Foreign exchange differences on revaluation of the nominal amount (net foreign exchange gains/losses); Interest accrued (net interest income)	(74,055) 113,582	(822,521) 64,267	(896,576) 177,849
Total	153,921	(555,983)	(402,062)

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IV. Discussion of financial statement components (cont.)

5. Financial instruments designated at fair value through profit and loss

The balance of 'Financial instruments designated at fair value through profit and loss' increased by PLN 1,708,870 thousand (i.e. by 16%) compared with the end of 2010 and amounted to PLN 12,467,201 thousand as at 31 December 2011. The portfolio comprised the following categories of securities:

	31.12.2011	31.12.2010	Change	Change
	PLN'ooo	PLN'ooo	PLN'ooo	(%)
NBP bills	8,593,791	3,997,780	4,596,011	115
Treasury bills	2,180,148	1,893,058	287,090	15
Polish Treasury bonds (PLN)	1,318,278	4,738,644	(3,420,366)	(72)
Municipal bonds (EUR)	143,973	128,849	15,124	12
Polish Treasury bonds (EUR)	122,089	-	122,089	100
Municipal bonds (PLN)	108,922	-	108,922	100
Total	<u>12,467,201</u>	<u>10,758,331</u>	<u>1,708,870</u>	<u>16</u>

The increase in the balance of financial instruments designated at fair value through profit and loss resulted mainly from increasing the Bank's exposure in short-term securities – compared with the end of 2010, the balances of NBP bills and Treasury bills increased by PLN 4,596,011 thousand (i.e. 115%) and PLN 287,090 thousand (i.e. 15%) respectively. The increase was partly offset by a drop in the balance of Treasury bonds (a decrease of PLN 3,420,366 thousand, i.e. 72% compared with the balance as at 31 December 2010). The most significant increase of the Bank's exposure in NBP bills took place in December 2011 – an increase in the balance of PLN 3,595,066 thousand compared with the previous month.

All the financial instruments designated at fair value through profit and loss were issued by Polish entities. As at the balance date, instruments quoted on organized stock exchanges represented 11% of the balance (29% as at the end of 2010).

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IV. Discussion of financial statement components (cont.)

6. Loans and advances to customers

In 2011 the portfolio of loans and advances to customers, measured by reference to the gross value of loans granted, increased by PLN 11,842,826 thousand (i.e. 9%) compared with the balance as at 31 December 2010 and amounted to PLN 145,041,439 thousand.

The analysis of the structure and quality of the loan portfolio is presented in the points below.

a) Structure of the Bank's loan portfolio by type of loans

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Financial sector (excluding banks)	3,220,155	4,252,926	(1,032,771)	(24)
corporate loans	3,220,155	4,252,926	(1,032,771)	(24)
Non-financial sector	136,754,855	125,095,189	11,659,666	9
mortgage loans	70,880,841	62,402,937	8,477,904	14
corporate loans	41,625,770	37,131,057	4,494,713	12
consumer loans	24,248,244	25,561,195	(1,312,951)	(5)
Public sector	5,066,429	3,850,498	1,215,931	32
corporate loans	5,066,429	3,849,854	1,216,575	32
mortgage loans	-	644	(644)	(100)
Total loans and advances, gross	145,041,439	133,198,613	11,842,826	9
Impairment allowance	(4,982,790)	(4,265,484)	(717,306)	17
Total loans and advances, net	140,058,649	128,933,129	11,125,520	9

As at the balance date, PLN 33,984,423 thousand (i.e. 23%) of gross loans were amounts due in foreign currencies (PLN 29,852,907 thousand, i.e. 22% as at 31 December 2010), of which 72% related to the Swiss franc (76% as at 31 December 2010).

After eliminating the effect of foreign exchange rate increases, the increase of the gross loan portfolio in 2011 would amount to PLN 7.8 billion (i.e. 6%), of which a drop of PLN 1.6 billion (i.e. 6%) would relate to mortgage loans denominated in CHF.

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IV. Discussion of financial statement components (cont.)

6. Loans and advances to customers (cont.)

b) The Bank's loan portfolio in terms of quality

	31.12.2011	31.12.2010	31.12.2011	31.12.2010
	PLN'000	PLN'000	Structure	Structure
			%	%
Impaired loans and advances	10,395,779	9,490,018	7.2	7.1
Loans and advances not impaired, gross	134,645,660	123,708,595	92.8	92.9
Total loans and advances, gross	145,041,439	133,198,613	100.0	100.0
Impairment allowances on impaired loans	(4,330,276)	(3,785,602)	86.9	88.7
Impairment allowances for incurred but not reported losses (IBNR)	(652,514)	(479,882)	13.1	11.3
Total impairment allowances for loans and advances	(4,982,790)	(4,265,484)	100.0	100.0
Total loans and advances, net	140,058,649	128,933,129		

As at the end of 2011, the share of impaired loans in the total loan portfolio increased slightly compared with the end of 2010 and amounted to 7.2% (7.1% as at 31 December 2010). At the same time, the coverage ratio of impairment allowances to impaired loans increased and amounted to 41.7% (39.9% as at 31 December 2010).

The deterioration in the quality of the loan portfolio related mainly to loans to small and medium enterprises and mortgage loans. The sale of the impaired loans portfolio is a significant part of managing impaired loans. The sales carried out in 2011 (mainly in the area of consumer loans) limited the growth of the impaired loans ratio (had there been no sales of the portfolio in 2011, the ratio of impaired loans as at the end of 2011 would amount to 8.0%).

The total gross carrying amount of the impaired loans sold in 2011 was PLN 1,342,488 thousand (the net amount was PLN 361,610 thousand).

The share of allowances for incurred but not reported impairment (IBNR) in the total allowances was higher than in the prior year - as at the balance date, the allowance amounted to PLN 652,514 thousand (13.1% of the total allowances), whereas in the prior year it amounted to PLN 479,882 thousand (11.3% of the total allowances). This was a result, among other things, of changing the methodology for calculating impairment allowances in respect of mortgage loans and periodic updating of the parameters applied in the calculation of the allowances.

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IV. Discussion of financial statement components (cont.)

6. Loans and advances to customers (cont.)

b) The Bank's loan portfolio in terms of quality (cont.)

The reconciliation of the change in the balance of impairment allowances for loans and advances to customers in the balance sheet and the net impairment allowances as at 31 December 2011 is presented below (in PLN'000):

	<u>consumer loans</u>	<u>mortgage loans</u>	<u>corporate loans</u>	<u>Total</u>
Impairment allowances on loans and advances to customers in the balance sheet as at 31 December 2010	(1,499,403)	(907,343)	(1,858,738)	(4,265,484)
Net impairment allowance on loans recognized in the income statement	(662,408)	(379,039)	(689,949)	(1,731,396)
Other changes	(11,802)	(38,775)	(13,027)	(63,604)
Decrease in impairment allowances due to the derecognition of assets not affecting the income statement	<u>722,545</u>	<u>90,183</u>	<u>264,966</u>	<u>1,077,694</u>
Impairment allowances on loans and advances to customers in the balance sheet as at 31 December 2011	<u>(1,451,068)</u>	<u>(1,234,974)</u>	<u>(2,296,748)</u>	<u>(4,982,790)</u>

Other changes comprised mainly currency translation differences on impairment allowance on foreign currency loan exposures.

The decrease in impairment allowances due to the derecognition of assets refers mainly to the sale of loan portfolio.

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IV. Discussion of financial statement components (cont.)

7. Investment securities available for sale

As at 31 December 2011, the balance of "Investment securities available for sale" increased by PLN 4,292,681 thousand (i.e. 43%) compared with the balance as at 31 December 2010 and amounted to PLN 14,168,933 thousand (PLN 9,876,252 thousand as at 31 December 2010).

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Polish Treasury bonds	8,310,429	5,486,623	2,823,806	51
Municipal bonds	3,458,356	2,824,173	634,183	22
Corporate bonds	2,322,398	1,494,111	828,287	55
Listed equity instruments	39,357	60,866	(21,509)	(35)
Other	38,393	10,479	27,914	266
Total	14,168,933	9,876,252	4,292,681	43

The change in the balance as at the balance date was mainly due to an increase in the balance of long-term securities: Treasury bonds, as well as corporate and municipal bonds (up PLN 2,823,806 thousand, i.e. 51%, PLN 828,287 thousand, i.e. 55% and PLN 634,183 thousand, i.e. 22% respectively).

The balance of corporate and municipal bonds comprised bonds issued by companies and local authorities for which the Bank acted as the underwriter. The material increase in the balance of corporate and municipal bonds was due to new issues being carried out in the last month of 2011 (an increase of PLN 337,506 thousand, i.e. 17% and PLN 331,642 thousand, i.e. 11% respectively).

All the investment debt securities available for sale were issued by Polish entities.

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IV. Discussion of financial statement components (cont.)

8. Investments in subsidiaries, jointly controlled entities and associates

As at 31 December 2011, the balance of investments in subsidiaries, jointly controlled entities and associates amounted to PLN 1,497,975 thousand and was PLN 30,468 thousand higher than as at 31 December 2010.

In accordance with IAS 27.37a, the Bank measures its subsidiaries, jointly controlled entities and associates at cost less of impairment allowances.

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Subsidiaries	1,329,357	1,274,182	55,175	4
- value at cost	1,763,746	1,708,571	55,175	3
- impairment allowance	(434,389)	(434,389)	-	-
Jointly controlled entities	61,869	61,869	-	-
- value at cost	61,869	61,869	-	-
- impairment allowance	-	-	-	-
Associates	106,749	131,456	(24,707)	(19)
- value at cost	148,029	148,029	-	-
- impairment allowance	(41,280)	(16,573)	(24,707)	149
Shares in subsidiaries, jointly controlled entities and associates	1,497,975	1,467,507	30,468	2

The increase in the balance of investments in subsidiaries, jointly controlled entities and associates was caused mainly by an increase in the Bank's interest in Centrum Finansowe Puławska Sp. z o.o. – in liquidation, aimed at early repayment of the Company's liability in respect of the Bank (an increase of PLN 39,000 thousand compared with the balance as at 31 December 2010) and purchasing 100% interest from its subsidiaries in PKO BP Finat Sp. z o.o. (an increase in interest of PLN 11,693 thousand compared with 31 December 2010).

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IV. Discussion of financial statement components (cont.)

8. Investments in subsidiaries, jointly controlled entities and associates (cont.)

The Bank's key investments in subsidiaries, jointly controlled entities and associates as at 31 December 2011 are described in the table below:

	Gross amount	Impairment allowance	Net amount	Structure
	PLN'000	PLN'000	PLN'000	(%)
Subsidiaries	1,763,746	(434,389)	1,329,357	89
KREDOBANK SA	935,619	(423,723)	511,896	34
PKO BP BANKOWY PTE SA	205,786	-	205,786	14
PKO Towarzystwo Funduszy Inwestycyjnych SA	186,989	-	186,989	13
Other	435,352	(10,666)	424,686	28
Jointly controlled entities	61,869	-	61,869	4
Centrum Haffnera Sp. z o.o.	44,371	-	44,371	3
Other	17,498	-	17,498	1
Associates	148,029	(41,280)	106,749	7
Bank Pocztowy SA	146,500	(39,780)	106,720	7
Other	1,529	(1,500)	29	-
Shares in subsidiaries, jointly controlled entities and associates	1,973,644	(475,669)	1,497,975	100

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IV. Discussion of financial statement components (cont.)

9. Intangible assets

As at the balance date, intangible assets amounted to PLN 1,522,568 thousand and were PLN 5,699 thousand (i.e. 0.4%) lower than as at 31 December 2010. The analysis of this balance is presented in the table below:

	31.12.2011	31.12.2010	Change	Change
	PLN'ooo	PLN'ooo	PLN'ooo	(%)
Software	2,775,173	2,411,233	363,940	15
Other intangible assets (including capital expenditure)	130,560	301,931	(171,371)	(57)
Total gross	2,905,733	2,713,164	192,569	7
Accumulated amortization	(1,365,148)	(1,166,880)	(198,268)	17
Impairment allowances	(18,017)	(18,017)	-	-
Total, net	1,522,568	1,528,267	(5,699)	-

As at 31 December 2011, the most significant component of intangible assets was the Integrated **Information System ("ZSI")**, which net book value amounted to PLN 707,925 thousand (PLN 701,470 thousand as at 31 December 2010). The capital expenditure on ZSI in the audited year amounted to PLN 68,827 thousand (PLN 82,916 thousand in 2010).

In the audited year the balance of impairment allowances did not change compared with the balance as at 31 December 2010. The value of allowance relating to the unused functionalities of the ZSI system did not change in the audited year and amounted to PLN 15,373 thousand as at the balance date.

The wear and tear of intangible assets measured with the ratio of accumulated amortization to gross carrying amount amounted to 47% (43% as at 31 December 2010).

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IV. Discussion of financial statement components (cont.)

10. Tangible fixed assets

As at the balance date the net carrying amount 'Tangible fixed assets' amounted to PLN 2,013,314 thousand and dropped by PLN 63,826 thousand (i.e. 3%) compared with the balance as at 31 December 2010.

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Land and buildings	2,081,141	2,077,369	3,772	-
Machinery and equipment	1,887,837	1,969,206	(81,369)	(4)
Fixed assets under construction	133,508	82,838	50,670	61
Means of transport	1,373	2,902	(1,529)	(53)
Investment properties	793	793	-	-
Other	385,401	404,230	(18,829)	(5)
Tangible fixed assets, gross	4,490,053	4,537,338	(47,285)	(1)
Accumulated depreciation	(2,476,596)	(2,441,817)	(34,779)	1
Impairment allowances	(143)	(18,381)	18,238	(99)
Tangible fixed assets, net	2,013,314	2,077,140	(63,826)	(3)

As at the balance date, the gross value of tangible fixed assets dropped by PLN 47,285 thousand (i.e. 1%) compared with the end of the prior year. The drop in the balance related mainly to sales and scrapping of machinery and equipment of PLN 177,889 thousand.

Compared with the balance as at 31 December 2010, impairment allowances dropped by PLN 18,238 thousand (i.e. 99%) in the audited year, mainly as a result of writing off fixed assets under construction (an impairment allowance of PLN 17,246 thousand as at 31 December 2010).

The wear and tear of tangible fixed assets measured with the ratio of accumulated depreciation to gross tangible fixed assets amounted to 55% (54% as at 31 December 2010).

Tangible fixed assets are valued at cost less accumulated depreciation and impairment allowances.

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IV. Discussion of financial statement components (cont.)

11. Other assets

The value of other assets increased by PLN 82,418 thousand (i.e. 21%) and amounted to PLN 482,790 thousand as at the balance date. The balance comprised the following asset categories:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Settlements of payment card transactions	166,051	208,760	(42,709)	(20)
Settlements of financial instruments (a)	143,845	47,279	96,566	204
Receivables from customers	39,237	28,031	11,206	40
Receivables from other transactions with financial and non-financial entities	26,538	11,088	15,450	139
Accruals and prepayments	22,862	28,219	(5,357)	(19)
Inventory related to utilization, auxiliary operations and investment	20,160	13,047	7,113	55
Receivables due from unsettled transactions related to derivatives	90,689	116,147	(25,458)	(22)
Receivables from the State budget due to distribution of court fee stamps	3,350	9,311	(5,961)	(64)
Receivables and settlements of securities turnover	1,730	8,020	(6,290)	(78)
Other (b)	138,979	97,979	41,000	42
Total, gross	653,441	567,881	85,560	15
Impairment allowance (c)	(170,651)	(167,509)	(3,142)	2
Total, net	482,790	400,372	82,418	21

- (a) As at the balance date, settlements of financial instruments comprised mainly settlement of the premium paid in respect of the purchase of currency options of PLN 41,574 thousand (PLN 18,537 thousand as at 31 December 2010).
- (b) As at 31 December 2011 the item 'Other' comprised mainly receivables due to shortages and losses with a gross value of PLN 50,356 thousand, i.e. 38% of the balance (PLN 27,426 thousand, i.e. 23% of the balance as at 31 December 2010).
- (c) The balance of other assets as at 31 December 2011 was decreased by impairment allowances of PLN 170,651 thousand (PLN 167,509 thousand as at 31 December 2010). They comprised mainly allowances on receivables due to unsettled, negotiated currency exchange transactions and transactions in derivatives of PLN 84,698 thousand (PLN 102,475 thousand as at 31 December 2010) and in respect of shortages and losses of PLN 48,488 thousand (PLN 25,773 thousand as at 31 December 2010).

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IV. Discussion of financial statement components (cont.)

12. Amounts due to banks

As at 31 December 2011, the amounts due to banks increased compared with the end of 2010 (an increase of PLN 1,157,209, i.e. 28%) and comprised the following components:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Loans and advances received	3,443,872	2,999,116	444,756	15
Bank deposits	1,372,635	972,758	399,877	41
Current accounts	421,939	43,901	378,038	861
Other money market deposits	82,944	93,662	(10,718)	(11)
Amounts due to repurchase agreement	-	54,744	(54,744)	(100)
Total	5,321,390	4,164,181	1,157,209	28

The increase in loans and advances as at 31 December 2011 was caused by an increase in the valuation of the loan granted to the Bank in the amount of 950,000 Swiss francs by a consortium of Polish and foreign banks in 2007 for a period of five years with an option to extend it (an increase of PLN 444,756 thousand, i.e. 15%). This increase was caused mainly by a change in the CHF/PLN exchange rate (an increase from 3.16 as at the end of 2010 to 3.63 as at the end of 2011). As at 31 December 2011 the share of the balance of the loan received by the Bank in total amounts due to banks was 65% (72% as at 31 December 2010).

Additionally, the increase in the balance was due to an increase in bank deposits of PLN 399,877 thousand, i.e. 41%, specifically due to an increase in foreign currency deposits (an increase of PLN 380,938 thousand, i.e. 64%) and an increase in the balance of current accounts of PLN 378,038 thousand, i.e. 861% compared with the balance as at 31 December 2010.

As at the balance date, the balance of amounts due to banks comprised foreign currency liabilities (83% as at 31 December 2010).

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IV. Discussion of financial statement components (cont.)

13. Amounts due to customers

As at the balance date, amounts due to customers were PLN 150,030,681 thousand and were PLN 14,741,626 thousand (i.e. 11%) higher than at the end of 2010:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Amounts due to retail clients	103,424,136	94,347,108	9,077,028	10
Term deposits	54,897,173	47,744,721	7,152,452	15
Current accounts and overnight deposits	48,054,921	46,308,729	1,746,192	4
Other money market deposits	472,042	293,658	178,384	61
Amounts due to corporate entities	42,784,326	34,895,145	7,889,181	23
Term deposits	24,012,372	18,039,764	5,972,608	33
Current accounts and overnight deposits	11,187,998	11,139,468	48,530	-
Loans and advances received	6,453,092	5,020,400	1,432,692	29
Amounts due to repurchase agreement	644,005	446,175	197,830	44
Other money market deposits	486,859	249,338	237,521	95
Amounts due to State budget entities	3,822,219	6,046,802	(2,224,583)	(37)
Current accounts and overnight deposits	2,241,309	2,689,361	(448,052)	(17)
Term deposits	1,516,981	3,349,821	(1,832,840)	(55)
Other money market deposits	63,929	7,620	56,309	739
Total amounts due to customers	150,030,681	135,289,055	14,741,626	11

In 2011 the structure of amounts due to customers changed – the share of term deposits increased (54% of the balance) which was partly offset by a drop in current accounts (40% of the balance).

As at the balance date, loans and advances received included advances from the subsidiary PKO Finance AB (Sweden) of CHF 250,000 thousand and funds of EUR 800,000 thousand obtained from the issue of the Bank's bonds under the EMTN program earmarked for international markets.

12% of the balance comprised liabilities denominated in foreign currencies (an increase of 3 pp. compared with the balance as at 31 December 2010).

In 2011, the Bank continued to increase its deposit base. In order to achieve this object the Bank actively sought new funds by introducing new products addressed to retail customers (savings books, term deposit with daily interest capitalization, Deposit 3+3 and Deposit 6+6), as well as by offering negotiated deposits for corporate entities.

As at 31 December 2011 the value of the loan to deposit ratio (L/D) dropped and amounted to 93.4% (95.3% as at 31 December 2010).

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IV. Discussion of financial statement components (cont.)

14. Debt securities in issue

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Financial instruments measured at amortized cost – bank bonds issued	2,929,973	-	2,929,973	100
Financial instruments designated at fair value through profit or loss – bank securities issued	175,615	-	175,615	100
Total	<u>3,105,588</u>	<u>-</u>	<u>3,105,588</u>	<u>100</u>

In 2011 under the Bond Issue Program (the issue limit was set at PLN 5 billion) the Bank issued three-month zero-coupon bonds denominated in PLN. As at 31 December 2011 the Bank had bond liabilities in the nominal amount of PLN 2,250,000 thousand, at a discount rate of 5.27% issued in November 2011 and bonds in the nominal amount of PLN 700,000 thousand, at a discount rate of 5.32% issued in December 2011.

Moreover, in 2011 the Bank offered its customers structured bank securities based on the S&P500 index, price of copper and gold. As at 31 December 2011 **the Bank's liabilities** in respect of the securities issued amounted to PLN 175,615 thousand (no respective liability as at 31 December 2010). In accordance with IAS 39.11A (a) the Bank does not separate the embedded derivative from the underlying contract and measures the whole instrument at fair value through profit or loss.

15. Subordinated liabilities

The balance of subordinated liabilities as at 31 December 2011 of PLN 1,614,377 thousand (PLN 1,611,779 thousand as at 31 December 2010) comprised bonds issued by the Bank in 2007 with a total nominal value of PLN 1,600,700 thousand maturing on 30 October 2017 (with the option of early redemption in 2012).

The bonds were issued on the basis of the Act on Bonds dated 29 June 1995 with a view to **increasing the Bank's supplementary funds in accordance with art. 127 par. 3, clause 2b** of the Banking Law, pursuant to a decision of the Banking Supervision Authority No. 91 dated 5 December 2007 (the reserve capital is increased by the nominal value of the bonds).

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IV. Discussion of financial statement components (cont.)

16. Other liabilities

As at 31 December 2011, other liabilities amounted to PLN 2,156,523 thousand and increased by PLN 368,924 thousand (i.e. 21%) compared with the end of 2010. The balance comprised:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Deferred income	277,150	312,480	(35,330)	(11)
Accounts payable	241,918	236,504	5,414	2
Other liabilities relating to:	1,637,455	1,238,615	398,840	32
Interbank settlements	580,998	174,854	406,144	232
liabilities relating to settlements of security transactions	279,204	181,456	97,748	54
liabilities relating to investment activities and internal operations	182,955	196,671	(13,716)	(7)
Liabilities arising from social and legal transactions	141,261	277,830	(136,569)	(49)
liabilities arising from foreign currency activities	140,546	131,849	8,697	7
financial instruments settlement	82,861	39,851	43,010	108
liabilities due to suppliers	54,794	46,965	7,829	17
liabilities related to payment cards	32,972	20,187	12,785	63
liabilities due to insurance companies	24,821	25,465	(644)	(3)
liabilities due to UOKIK (the Competition and Consumer Protection Office)	16,597	22,310	(5,713)	(26)
liabilities related to sales of value marks	12,626	14,375	(1,749)	(12)
settlement of acquisition of machines and materials, works and services regarding the construction of tangible assets and their usage	10,265	4,613	5,652	123
liabilities arising from transactions with financial and non-financial entities	10,102	21,121	(11,019)	(52)
Other	67,453	81,068	(13,615)	(17)
Total	<u>2,156,523</u>	<u>1,787,599</u>	<u>368,924</u>	<u>21</u>

As at 31 December 2011, interbank settlements had the largest share in other liabilities (27%) and amounted to PLN 580,998 thousand showing an increase of PLN 406,144 thousand (i.e. 232%) compared with the balance as at 31 December 2010 and liabilities related to the settlement of security transactions (13%) amounted to PLN 279,204 thousand an increase by PLN 97,748 thousand (i.e. 54%) compared with the balance as at 31 December 2010.

The increase in the balance as at 31 December 2011 resulted mainly from an increase in interbank settlements of PLN 406,144 thousand, i.e. 232%, in connection with the larger balance of transfers awaiting settlement, ordered by the customers after the end of the session, which will be completed on the following business day.

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IV. Discussion of financial statement components (cont.)

17. Provisions

As at as at 31 December 2011, provisions comprised the following items:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Provision for retirement benefits and anniversary bonuses	426,973	410,723	16,250	4
Provision for liabilities and guarantees granted	111,769	216,137	(104,368)	(48)
Provisions for legal claims	2,254	6,311	(4,057)	(64)
Other provisions	74,493	81,267	(6,774)	(8)
Total	615,489	714,438	(98,949)	(14)

The drop in the balance of provisions as at the end of 2011 resulted mainly from a decrease in the level of provisions for liabilities and guarantees granted of PLN 104,368 thousand (i.e. 48%). This drop was mainly the result of the utilization of the provision for valuation the guarantee of repayment of dues granted in 2010 to the subsidiary Kredobank SA in the amount of PLN 155,534 thousand in connection with the payment of compensation in respect of the guarantee of PLN 144,956 thousand.

The provision for retirement pension benefits and for anniversary bonuses was based on the calculations of an independent actuary included in the report from February 2012. The report was prepared on the basis of balances as at the balance date.

As at 31 December 2011 “**Other provisions**” related among other things to the restructuring provision (PLN 63,636 thousand). The restructuring provision covers future liabilities in respect of compensations and severance payments to employees whose employment contracts will be terminated for reasons unrelated to the employees. In accordance with IAS 37.72, **the Bank's employment restructuring plan** is the basis for creating this provision.

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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	Financial assets available for sale	Cash flow hedges	General Banking Risk Fund	Other reserves	Total other capital	Retained earnings	Net profit	TOTAL
	PLN'000	PLN'000	PLN'000	PLN'000	PLN'000	PLN'000	PLN'000	PLN'000	PLN'000	PLN'000
As at 31.12.2010	1,250,000	12,098,111	(28,808)	217,924	1,070,000	3,283,412	16,640,639	-	3,311,209	21,201,848
Change in the value of instruments available for sale net of deferred tax	-	-	(22,356)	-	-	-	(22,356)	-	-	(22,356)
Hedge accounting	-	-	-	144,261	-	-	144,261	-	-	144,261
Net profit for 2011	-	-	-	-	-	-	-	-	3,953,622	3,953,622
Transfer of retained earnings	-	-	-	-	-	-	-	3,311,209	(3,311,209)	-
Transfer from net profit to capital	-	800,000	-	-	-	36,209	836,209	(836,209)	-	-
Transfer from net profit to dividends	-	-	-	-	-	-	-	(2,475,000)	-	(2,475,000)
As at 31.12.2011	1,250,000	12,898,111	(51,164)	362,185	1,070,000	3,319,621	17,598,753	-	3,953,622	22,802,375

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IV. Discussion of financial statement components (cont.)

18. Equity (cont.)

On 30 June 2011, the General Shareholders' Meeting of Powszechna Kasa Oszczędności Bank Polski SA passed a resolution relating to the appropriation of profit for 2010, in the amount of PLN 3,311,209 thousand, according to which PLN 800,000 thousand was to be transferred to reserve capital, PLN 36,209 thousand was to be transferred to other reserves and PLN 2,475,000 thousand to be paid out as dividend.

As at 31 December 2011, the Bank's share capital amounted to PLN 1,250,000 thousand and consisted of 1,250,000,000 ordinary shares, with a par value of PLN 1 each, including:

- 312,500,000 series A registered shares;
- 197,500,000 series A bearer shares;
- 105,000,000 series B bearer shares;
- 385,000,000 series C bearer shares;
- 250,000,000 series D bearer shares;

The Bank's own funds calculated in accordance with the Banking Law and Resolution no. 325/2011 of the Polish Financial Supervision Authority, amounted to PLN 17,347,921 thousand as at 31 December 2011 (PLN 16,562,906 thousand as at 31 December 2010) and were PLN 5,712,542 thousand higher than the total capital requirements (PLN 11,635,379 thousand as at the end of 2011). As at 31 December 2011, the capital adequacy ratio calculated on the basis of the banking and trading portfolio amounted to 11.93% (11.99% as at 31 December 2010).

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IV. Discussion of financial statement components (cont.)

Income statement for the year ended 31 December 2011

19. Net interest income

In 2011 net interest income amounted to PLN 7,504,969 thousand and increased by PLN 1,121,193 thousand (i.e. 18%) compared with 2010. The balance comprised the following items:

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Interest income:	11,818,059	10,107,552	1,710,507	17
Income from loans and advances to customers	9,581,320	8,246,231	1,335,089	16
Income from hedging financial instruments	814,275	649,116	165,159	25
Income from securities designated at fair value through profit or loss	561,826	494,702	67,124	14
Income from investment securities	557,750	437,053	120,697	28
Income from placements with banks	218,682	147,682	71,000	48
Income from trading securities	74,847	128,940	(54,093)	(42)
Other	9,359	3,828	5,531	144
Interest expense:	(4,313,090)	(3,723,776)	(589,314)	16
Interest expense on amounts due to customers	(4,133,424)	(3,586,343)	(547,081)	15
Interest expense on debt securities in issue	(130,568)	(82,191)	(48,377)	59
Interest expense on deposits from banks	(45,684)	(31,218)	(14,466)	46
Premium expense on debt securities available-for-sale debt securities	(1,322)	(3,553)	2,231	(63)
Other expenses	(2,092)	(20,471)	18,379	(90)
Net interest income	7,504,969	6,383,776	1,121,193	18

The increase in interest income of PLN 1,710,507 thousand in 2011 was caused mainly by interest income on loans and advances to customers which was higher than in 2010 (an increase of PLN 1,335,089 thousand, i.e. 16%). This was mainly due to an increase in the portfolio of loans and advances to customers (a net increase of PLN 11,125,520 thousand, i.e. 9% in 2011 (Note 6)) and an increase in reference rates (average annual WIBOR 1M rate in 2011 amounted to 4.37% compared with 3.62% in 2010).

The dynamics of interest expense were similar and amounted to 16%, which translated into an increase in interest expense of PLN 589,314 thousand in 2011. This was mainly the result of higher interest expense on amounts due to customers and costs of issuing own debt securities (an increase of PLN 547,081 thousand, i.e. 15% and PLN 48,377 thousand, i.e. 59%). This increase resulted mainly from the increase in the balance of amounts due to customers (an increase of PLN 14,741,626 thousand, i.e. 11% (Note 13)) and liabilities from issues of securities (an increase of PLN 3,108,186 thousand in the second half of 2011, i.e. 193%).

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IV. Discussion of financial statement components (cont.)

19. Net interest income (cont.)

As a result, the interest margin defined as the ratio of the net interest income to interest income increased by 1 pp. and amounted to 64% in 2011. The interest margin calculated as the difference between the rate of interest income on working assets and the cost of borrowings did not change compared with 2010 and amounted to 4.2% (an increase of 0.2 pp.).

20. Net fee and commission income

In 2011 net fee and commission income amounted to PLN 2,872,801 thousand and dropped by PLN 64,758 thousand (i.e. 2%) compared with the previous year. Net interest income comprised the following items:

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Fee and commission income	3,621,880	3,678,487	(56,607)	(2)
Income from payment cards	1,020,600	963,363	57,237	6
Income from maintenance of bank accounts	903,972	908,208	(4,236)	-
Income from loans and advances granted	574,044	524,110	49,934	10
Income from loan insurance	515,499	653,501	(138,002)	(21)
Income from maintenance of investment funds (including management fees)	187,566	170,269	17,297	10
Income from cash transactions	148,325	165,437	(17,112)	(10)
Income from securities transactions	70,295	73,231	(2,936)	(4)
Income from foreign mass transactions	47,966	44,754	3,212	7
Income from distribution of court fee stamps	18,625	26,255	(7,630)	(29)
Other	132,182	147,700	(15,518)	(11)
Income from fiduciary activities	2,806	1,659	1,147	69
Fee and commission expense	(749,079)	(740,928)	(8,151)	1
Expenses on payment cards	(373,697)	(329,381)	(44,316)	13
Expenses on loan insurance	(133,488)	(150,842)	17,354	(12)
Expenses on acquisition services	(117,603)	(133,935)	16,332	(12)
Expenses on settlement services	(20,971)	(21,071)	100	-
Expenses on fees and commission for operating services rendered by banks	(11,340)	(10,113)	(1,227)	12
Other	(91,980)	(95,586)	3,606	(4)
Net fee and commission income	2,872,801	2,937,559	(64,758)	(2)

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IV. Discussion of financial statement components (cont.)

20. Net fee and commission income (cont.)

In 2011 fee and commission income decreased by PLN 56,607 thousand (i.e. 2%). The decrease resulted mainly from lower (by PLN 138,002 thousand i.e. 21%) income from loan insurance, partly offset by an increase of PLN 57,237 thousand (i.e. 6%) income from payment cards and an increase of PLN 49,934 thousand (i.e. 10%) in income from loans and advances granted. The drop in income from loan insurance resulted mainly from a decrease in the volume of consumer loans granted (a drop in the volume of consumer loans of PLN 1,312,951 thousand, i.e. 5% (Note 6)) and reimbursing customers with commission in connection with the early repayment of loans or renouncement of insurance. The increase in the loan portfolio for other products contributed to the increase in income from loans and advances granted. These commissions are deferred and settled on a straight-line basis, and relate mainly to overdrafts, revolving loans and other credit facilities granted, which do not have a fixed time schedule for repayment. The increase in income from credit cards resulted mainly from an increase in the number of transactions concluded using payment cards of 5.7% compared with the prior year.

Fee and commission expense in 2011 increased slightly, by PLN 8,151 thousand, compared with 2010 (by 1%). This increase was caused mainly by expenses on payment cards being PLN 44,316 thousand (i.e. 13%) higher than in the prior year. The increase was partly offset with a decrease in commission expense from loan insurance (a drop of PLN 17,354 thousand, i.e. 12%) and in acquisition services (a drop of PLN 16,332 thousand, i.e. 12%) as a result of a lower volume of products sold through this channel and lowering commission rates received by agents and intermediaries.

21. Dividend income

In 2011 dividend income amounted to PLN 94,028 thousand and was PLN 15,867 thousand (i.e. 14%) lower than in 2010. This amount comprised mainly dividend paid by PKO Towarzystwo Funduszy Inwestycyjnych SA – PLN 48,200 thousand (PLN 61,209 thousand in 2010), by Centrum Elektronicznych Usług Płatniczych eService SA – PLN 22,200 thousand (PLN 29,000 thousand in 2010) and by Inteligo Financial Services SA – PLN 16,716 thousand (PLN 1,424 thousand in 2010).

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IV. Discussion of financial statement components (cont.)

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

In 2011 the loss on financial instruments at fair value through profit or loss amounted to PLN 78,538 thousand (a loss of PLN 56,489 thousand in the prior year).

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Derivative instruments	(88,585)	(103,782)	15,197	(15)
Debt instruments	7,003	45,847	(38,844)	(85)
Structured Bank securities at fair value through profit or loss	3,630	-	3,630	100
Equity instruments	(612)	1,427	(2,039)	(143)
Other	26	19	7	37
TOTAL	(78,538)	(56,489)	(22,049)	39

The item "Derivative instruments" includes the net realized income and valuation of derivative instruments excluding foreign currency transactions the value of which is recognized in net foreign exchange gains (Note 23).

The loss recognized in 2011 related mainly to the ineffective part of hedging cash flows recognized in the income statement in the amount of PLN 64,342 thousand (PLN 82,879 thousand in 2010) (Note 4).

23. Net foreign exchange gains

In 2011 net foreign exchange gains amounted to PLN 331,367 thousand (PLN 341,348 thousand in 2010) and included gains and losses on revaluation and transactions in assets and liabilities in foreign currencies and fair value measurement of foreign exchange derivatives (FX forward, FX swap, CIRS and currency options). Compared with 2010, net foreign exchange gains dropped by PLN 9,981 thousand (i.e. 3%).

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Currency translation differences resulting from financial instruments designated at fair value through profit and loss	523,174	(1,026,841)	1,550,015	(151)
Other currency translation differences	(191,807)	1,368,189	(1,559,996)	(114)
Total	331,367	341,348	(9,981)	(3)

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IV. Discussion of financial statement components (cont.)

23. Net foreign exchange gains (cont.)

Compared with 2010 the result on the individual components of net foreign exchange gains were reversed. In 2011 the Bank realized net foreign exchange gains on instruments at fair value through profit or loss (a net gain of PLN 523,174 thousand compared with the net loss of PLN 1,026,841 thousand in 2010). This result was mainly determined by the measurement of derivative instruments and resulted mainly from a change in the measurement of CIRS contracts used mainly to manage interest rate risk, which net valuation changed by PLN 560,359 thousand, i.e. 210% (change from negative net value of PLN 266,938 thousand as at the end of 2010 to a positive net value of PLN 293,421 as at the end of 2011 – Note 4).

At the same time, the net loss on other currency translation differences (including the result on revaluation of loans and advances) amounted to PLN 191,807 thousand (a drop of PLN 1,559,996 thousand, i.e. 114% compared with the prior year).

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IV. Discussion of financial statement components (cont.)

24. Net impairment allowance and write-downs

In 2011 the net impairment allowance and write-downs were negative (an excess of impairment allowances set up over those released) and amounted to PLN 1,812,122 thousand (an increase in the negative balance of PLN 45,076 thousand compared with 2010):

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Loans and advances to customers	(1,731,396)	(1,600,714)	(130,682)	8
Provisions for off-balance sheet liabilities	(36,271)	(105,157)	68,886	(66)
Investments in subsidiaries, jointly controlled entities and associates	(24,707)	(15,073)	(9,634)	64
Investment securities - available for sale	(1,924)	800	(2,724)	(341)
Intangible assets	-	(2,644)	2,644	(100)
Non-current assets held for sale	-	(1,281)	1,281	(100)
Tangible fixed assets	984	(29,418)	30,402	(103)
Amounts due from banks	2,815	(4,383)	7,198	(164)
Other	(21,623)	(9,176)	(12,447)	136
Net impairment allowance and write-downs	<u>(1,812,122)</u>	<u>(1,767,046)</u>	<u>(45,076)</u>	3

The change in the balance in 2011 was largely due to an increase in net impairment allowances for corporate loans of PLN 156,461 thousand (i.e. 29%), mainly in connection with the deterioration in the quality of the portfolio of loans to small and medium enterprises and mortgage loans and loans for developers – an increase of PLN 120,907 thousand (i.e. 47%), which was partly offset by a drop in net impairment allowances for consumer loans (a drop of PLN 146,666 thousand, i.e. 18%). Detailed information on the quality of the loan portfolio is presented in Note 6.

Additionally, in 2011 the Bank decreased the allowance for the valuation of the guarantee granted to the subsidiary Kredobank SA of PLN 155,534 thousand (Note 17), at the same time paying to company respective compensation of PLN 144,956 thousand, and recognised an impairment allowance on the shares of Bank Pocztowy SA in the amount of PLN 24,707 thousand (in 2010 a net write-down of PLN 15,073 thousand) (Note 7).

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IV. Discussion of financial statement components (cont.)

25. Administrative expenses

Administrative expenses incurred by the Bank amounted to PLN 4,058,490 thousand in 2011 and were PLN 156,378 thousand (i.e. 4%) higher than those incurred in 2010:

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Staff costs	(2,224,040)	(2,197,253)	(26,787)	1
Overheads	(1,184,695)	(1,147,788)	(36,907)	3
Amortization and depreciation	(452,698)	(445,989)	(6,709)	2
Taxes and fees	(60,320)	(57,698)	(2,622)	5
Contribution and payments to Banking Guarantee Fund	(136,737)	(53,384)	(83,353)	156
Total	<u>(4,058,490)</u>	<u>(3,902,112)</u>	<u>(156,378)</u>	<u>4</u>

The increase in administrative expenses in 2011 resulted mainly from an increase in fees paid to the Banking Guarantee Fund (an increase of PLN 83,353 thousand, i.e. 156%) in connection with the change in the contribution to Banking Guarantee Fund, and from an increase in staff costs (of PLN 26,787 thousand, i.e. 1%) and overheads (an increase of PLN 36,907 thousand, i.e. 3%).

The increase in overheads in 2011 was mainly caused by an increase in the expenses on promotional and advertising activities which were PLN 56,688 thousand (i.e. 57%) higher and amounted to PLN 155,555 thousand in 2011, and higher administrative activity costs which increased by PLN 23,727 thousand (i.e. 11%) and amounted to PLN 239,908 thousand in 2011. The increase was partly offset by a decrease in IT activity costs which in 2011 amounted to PLN thousand (PLN 299,404 thousand in 2010).

The increase in staff costs in 2011 was mainly caused by an increase in remuneration expenses which were PLN 22,231 thousand (i.e. 1%) higher and amounted to PLN 1,885,849 thousand in 2011 (PLN 1,863,618 thousand in 2010).

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

	2011	2010
	PLN'000	PLN'000
Administrative expenses	4,058,490	3,902,112
Annual average number of employees	26,444	27,432
Administrative expenses per employee	153	142
Net profit per employee	150	121

The cost to income ratio amounted to 37.6% in the audited year (39.8% in 2010). The improvement in the C/I ratio was mainly caused by an increase in interest income (Note 19). At the same time net profit per employee increased (a 24% increase compared with 2010). Administrative expenses per employee increased, mainly as a result of a drop in the number of employees of 988, i.e. 3.6% (annual average).

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IV. Discussion of financial statement components (cont.)

26. Income tax expense

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

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Deferred income tax	(50,194)	207,922	(258,116)	(124)
Current income tax expense	(910,115)	(1,019,630)	109,515	(11)
Income tax expense disclosed in the income statement	(960,309)	(811,708)	(148,601)	18
Income tax expense disclosed in other comprehensive income	(28,595)	(20,203)	(8,392)	42
Total	(988,904)	(831,911)	(156,993)	19

The effective interest rate amounted to 19.5% in 2011 and was 0.2 pp. lower compared with the prior year.

(a) Deferred income tax

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

	Statement of financial position 31.12.2011	Statement of financial position 31.12.2010	Income statement
	PLN'000	PLN'000	PLN'000
Deferred income tax provision			
Interest capitalized on mortgage loans	190,844	211,576	(20,732)
Interest accrued on receivables	176,076	111,398	64,678
Interest on securities	58,187	44,537	13,650
Valuation of derivatives, including:	94,471	98,859	x
- recognized in the income statement	9,514	47,741	(38,227)
- recognized in other comprehensive income	84,957	51,118	x
Valuation of securities, including:	16,414	-	x
- recognized in the income statement	15,443	-	15,443
- recognized in other comprehensive income	971	-	x
Difference between the carrying and tax value of tangible fixed assets	293,318	258,027	35,291
Gross deferred income tax liability	829,310	724,397	x
- recognized in the income statement	743,382	673,279	70,103
- recognized in other comprehensive income	85,928	51,118	x

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IV. Discussion of financial statement components (cont.)

26. Corporate income tax (cont.)

(a) Deferred income tax (cont.)

	Statement of financial position 31.12.2011	Statement of financial position 31.12.2010	Income statement
	PLN'000	PLN'000	PLN'000
Deferred income tax assets:			
Interest accrued on liabilities	391,527	406,364	(14,837)
Valuation of securities, including:	24,550	57,395	x
- recognized in the income statement	11,580	50,640	(39,060)
- recognized in other comprehensive income	12,970	6,755	x
Adjustment to ESP valuation	211,011	218,000	(6,989)
Impairment allowance	414,558	335,477	79,081
Provision for anniversary, retirement bonuses and other employee benefits	126,714	118,613	8,101
Valuation of derivative instruments	16,093	19,470	(3,377)
Other	28,991	32,001	(3,010)
Gross deferred tax assets	1,213,444	1,187,320	x
- recognized in the income statement	1,200,474	1,180,565	19,909
- recognized in other comprehensive income	12,970	6,755	x
Total effect of temporary differences	384,134	462,923	x
- recognized in the income statement	457,092	507,286	(50,194)
- recognized in the other comprehensive income	(72,958)	(44,363)	
Net deferred tax assets	384,134	462,923	
Net impact of the deferred income tax on the income statement	-	-	(50,194)

Due to the fact that the Bank recognized net deductible differences as at 31 December 2011, it recognized a deferred tax asset of PLN 384,134 thousand (PLN 462,923 thousand as at the end of 2010).

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IV. Discussion of financial statement components (cont.)

26. Corporate income tax (cont.)

(b) Current income tax

In the current financial year, corporate income tax was calculated at a rate of 19% based on profit before tax determined on the basis of IFRS regulations as adopted by the EU, adjusted for non-taxable income and non-deductible costs.

	2011	2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Profit before tax	4,913,931	4,122,917	791,014	19
Current tax at 19%	(933,647)	(783,354)	(150,293)	19
Permanent differences between profit/loss before tax and taxable income, including:				
Other non-deductible costs	(28,613) (10,309)	(28,938) (12,042)	325 1,733	(1) (14)
Allowances reversed/(set up) and positive revaluation which do not constitute taxable income/tax-deductible costs	(36,356)	(37,503)	1,147	3
Dividend income	17,859	20,501	(2,642)	(13)
Other	193	106	87	82
Other differences, including donations	1,951	584	1,367	234
Income tax recognized in the income statement	(960,309)	(811,708)	(148,601)	18
Effective tax rate	19.5%	19.7%	-0.2 pp.	-
Temporary difference resulting from deferred tax recognized in the income statement	(50,194)	207,922	(258,116)	(124)
Current income tax expense	(910,115)	(1,019,630)	109,515	(11)

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IV. Discussion of financial statement components (cont.)

27. Off-balance sheet items

The value of off-balance sheet liabilities granted and received as at 31 December 2011 is shown in the table below:

	31.12.2011	31.12.2010	Change	Change
	PLN'000	PLN'000	PLN'000	(%)
Off-balance sheet liabilities granted, including:	38,075,797	38,188,366	(112,569)	-
Financing granted	30,671,744	29,935,538	736,206	2
Guarantees and warranties granted – nominal value	7,404,053	8,252,828	(848,775)	(10)
Off-balance sheet liabilities received, including:	2,280,636	2,627,052	(346,416)	(13)
Guarantees and warranties received	1,905,208	2,231,427	(326,219)	(15)
Financing received	375,428	395,625	(20,197)	(5)

The insignificant drop in off-balance sheet liabilities granted of PLN 112,569 thousand was caused by a decrease in the nominal value of guarantees and warranties granted of PLN 848,775 thousand (i.e. 10%), which was partly offset by an increase in off-balance sheet liabilities relating to financing of PLN 736,206 thousand (i.e. 2%).

Off-balance sheet liabilities received in 2011 were PLN 346,416 thousand (i.e. 13%) lower than in the prior year.

The item “Guarantees and warranties received” relates mainly to guarantees of loan repayment received, including PLN 1,609,472 thousand relating to State Treasury guarantee of repayment of mortgage loans of the so-called “old portfolio” in accordance with the Act of 29 November 2000 on guaranteeing repayment of specific mortgage loans by the State Treasury (PLN 1,838,551 thousand as at 31 December 2010).

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V. Statements of the independent registered auditor

- (a) The Management Board of the Bank provided all the information, explanations, and representations required by us in the course of the audit 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 Company's accounting policies** were tailored to its needs and ensured the recognition of all events with a material effect on the assessment of its financial position and results, taking into consideration the prudence principle. There were no changes to the accounting policies compared with the previous year.
- (d) The closing balances as at the end of the previous year were correctly brought forward as the opening balances of the current financial year in all material respects.
- (e) The counts of assets and liabilities were carried out and reconciled in accordance with the Accounting Act, and the results were included in the accounting records for the audited year.
- (f) The financial statements of the Bank as at and for the year ended 31 December 2010 were approved by Resolution No. 3/2011 passed **by the General Shareholders' Meeting** on 30 June 2011 filed with the National Court Register in Warsaw on 14 July 2011 and published in *Monitor Polski B* No. 2212 on 16 November 2011.
- (g) The financial statements for the previous year were audited by PricewaterhouseCoopers Sp. z o.o. The registered auditor issued an unqualified opinion.
- (h) We have assessed the operation of the accounting system. Our assessment covered in particular:
 - the accuracy of the documentation relating to business transactions;
 - the fairness, accuracy and verifiability of the books of account, including computerized books of account;
 - the methods used for controlling access to data and the computerized data processing system;
 - the safeguarding of the accounting documentation, books of account, and financial statements.

This assessment, together with our verification of individual items of the financial statements, provides the basis for expressing a general and comprehensive opinion on these financial statements. The audit was not intended to provide a comprehensive opinion on the operations of the said system.

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V. Statements of the independent registered auditor (cont.)

- (i) 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 statement of financial position 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.
- (j) The notes to the financial statements present all significant information required by IFRS as adopted by the European Union.
- (k) **The information in the Directors' Report for the year ended 31 December 2011** has been prepared in accordance with the provisions of the Decree of the Minister of Finance dated 19 February 2009 concerning the publication of current and periodic information by issuers of securities and the conditions of acceptance as equal information required by the law of other state, which is not a member state (Journal of Laws No. 33, item 259 with subsequent amendments) and is consistent with the information presented in the audited financial statements.
- (l) The total capital requirement, together with the requirement concerning the risk of excessive capital exposure, amounted to PLN 11,635,379 thousand as at the balance date. The capital adequacy ratio as at 31 December 2011 amounted to 11.93%. As at the balance date, the Bank complied with the prudence principle in all material respects.



VI. Final information and comments

This report has been prepared in connection with our audit of the financial statements of **Powszechna Kasa Oszczędności Bank Polski SA** with its registered office in Warsaw, **15 Puławska Street**. The financial statements were signed by the Banks's **Management Board** and the person entrusted with maintaining the books of account on 23 February 2012.

This report should be read in conjunction with the **Independent Registered Auditor's** unqualified Opinion to the General Meeting of Shareholders and the Supervisory Board of **Powszechna Kasa Oszczędności Bank Polski SA** dated 29 February 2012, concerning the said financial statements. The opinion on the financial statements expresses 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 account of the impact of the facts noted on the truth and fairness of the financial statements as a whole.

Conducting the audit on behalf of PricewaterhouseCoopers Sp. z o.o., Registered Audit Firm No. 144:

Antoni F. Reczek
President of the Management Board

PricewaterhouseCoopers Sp. z o.o.

Principal Registered Auditor
No. 90011

Warsaw, 29 February 2012 r.