Komisja
Nadzoru
Finansowego

REPORT
on the condition of Polish banks
in 2009

Warsaw, 2010
Polish Financial Supervision Authority

Compilation:
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with cooperation of Banking Sector Analysis Division and the Inspection Department
Banking Sector Supervision Department
Banking Supervision Section
Polish Financial Supervision Authority

Contents

PREFACE

Ladies and Gentlemen,

I would like to present to you another report summarising the past year in banking. Polish financial market emerged from the global crisis unscathed. No institution went bankrupt, and the sector as a whole remained profitable. Capital position of banks is now much better off than a year before, and the conditions of their functioning have also improved.

This does not mean that the sector remained fully resistant to the effects of deterioration in the macroeconomic situation. In particular, the negative balance of reserves and write-offs produced mainly due to the deteriorating quality of loans for households ate up nearly one quarter of profits from banking business. This draws attention to the strong deterioration of results or losses occurring in case of banks and branches of credit institutions, which were pursuing expansionary lending during the economic boom. This shows that the model based on high margin loans awarded without a solid credit rating may be unreliable. Business activity carried out in such a manner is not only contrary to the principle of prudent bank management, threatens the stability of an individual institution as well as the whole sector, but is also incompatible with the ethics of a banker.

For us, last year was a time of hard work in the scope of supervision, analysis, inspection and regulation. I hope that the recommendations prepared during this period - the T Recommendation, reviewed A and I Recommendations - will be incorporated into the necessary minimum of standards of risk management in banks.

I hope you enjoy reading,

Andrzej Stopczyński, Ph.D.
Managing Director
of Banking Supervision Sector

BASIC DATA (increase/decrease or value in the period 12/2009-12/2008)

EMPLOYMENT	- 6 175	(persons)
BRANCH NETWORK	212	(units)
FINANCIAL RESULT	-36.2%	
number of banks declaring a loss	16	(share in the sector assets 7.9%)
BALANCE SHEET TOTAL	2.1%	
LOANS	5.8%	
Households	11.9%	
- consumer	13.2%	
- housing	11.6%	
in PLN	28.1%	
in foreign currencies	4.3%	
Companies	-4.4%	
- current activity	-10.5%	
- real estate	2.8%	
- investment	0.9%	
DEPOSITS	13.4%	
Households	14.8%	
Companies	11.4%	
NON-PERFORMING LOANS	76.1%	(increase in share from 4.5% to 7.5%)
Households	73.5%	(increase in share from 3.5% to 5.5%)
- consumer	86.0%	(increase in share from 6.6% to 10.8%)
- housing	64.3%	(increase in share from 1.0% to 1.5%)
in PLN	53.3%	(increase in share from 2.0% to 2.4%)
in foreign currencies	82.0%	(increase in share from 0.6% to 1.0%)
Companies	79.2%	(increase in share from 6.1% to 11.4%)
LIQUIDITY		
number of banks not conforming to the Resolution 386/2008	11	(share in sector assets 0.3%)
ADEQUACY		
Own funds	15.7%	
number of banks not conforming to the requirements	1	(share in sector assets 0.0%)
Total capital requirement	-2.5%	
Solvency ratio	13.3%	(ratio level)
number of banks with the ratio < 8%	-	

MOST IMPORTANT OBSERVATIONS AND CONCLUSIONS

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- ✓ maintaining the growth of Polish economy, reviving global economy
- ✓ maintaining a stable situation in terms of liquidity,
- ✓ record capital increase and a strong increase in the solvency ratio,
- ✓ significant increase of the deposit base,
- ✓ change in the currency structure of newly granted housing loans (advantage of PLN)
- ✓ expiration of the problem of foreign exchange derivative transactions,
- ✓ revisions of applied loan policies (tightening the criteria)

(-)

- ✓ the level of risk generated by external environment remains heightened,
- ✓ strong deterioration of credit portfolio quality,
- ✓ decline in financial performance by more than 1/3,
- ✓ decrease in funding companies,
- ✓ lowering the rating of certain banks,

Despite the strong deterioration in financial performance, the situation of the banking sector remained stable. At the same time, due to the record increase of the capital base, the stability of the banking sector strongly increased, including the ability to absorb potential losses; the potential for the sector development increased, too. Thus, medium-term prospects of the banking sector development do not raise concerns.

The main source of risks includes external environment and inadequate lending procedures applied by some entities, which generate high risk on the one hand (both for customers, individual institutions and for the whole sector), **and on the other hand, have a negative impact on actions of remaining participants in a market** (competition pressure).

Maintaining the stability of the banking sector requires that banks continue adaptation and preventive measures and that the external environment of banks is stabilised (the latter is difficult, because most risks originate outside Poland).

Necessary and desirable actions on the part of banks:

- ✓ strengthening loan procedures, especially in the area of consumer and housing loans (no further granting of loans which generate high risk), and in particular the need to rapidly implement the recommendations contained in the T Recommendation adopted by the PSFA in February 2010 (including the use of services provided by Credit Reference Agency (BIK) and submitting information about customers' income to this Agency),
- ✓ strengthening of restructuring and debt collection activities,
- ✓ adjustment of risk management to market conditions (ensuring the adequate level of liquid assets and capital buffer),
- ✓ further efforts to obtain long-term funding sources,
- ✓ changing the ways of formulating development strategies of banks, with the aim to ensure their long-term stability rather than maximizing short-and medium-term profits. It is necessary to reconstruct processes and structures of banks (including remuneration systems) to enhance analysis and risk management (especially in medium-and long-term perspective, in order to, among other things, reflect the overall effectiveness of products during the whole period when they remain in the portfolio).

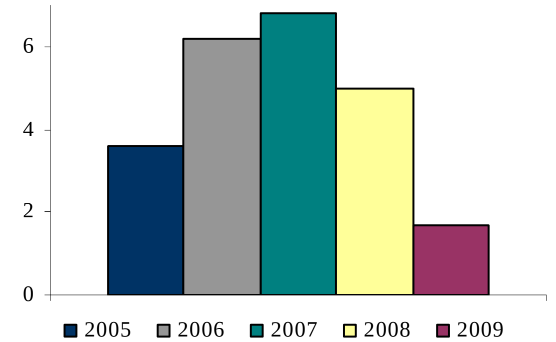
I. EXTERNAL CONDITIONS OF THE OPERATION OF BANKS

Macroeconomic situation

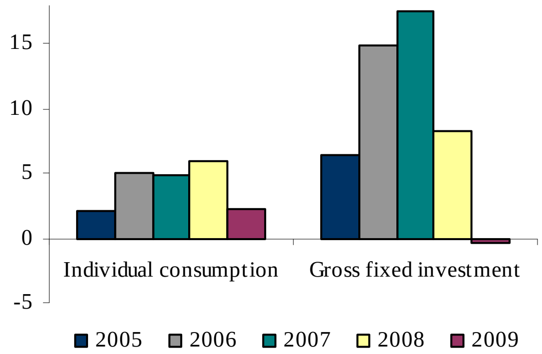
In 2009, the rate of economic growth slowed down drastically, the labour market was significantly weakened and the situation in the public finance sector deteriorated. Unfavourable trends were the consequence of the collapse of the global economy, which, as a result of the financial crisis started in 2007, went into the deepest recession since the end of World War II.

Despite the slowdown, the condition of the Polish economy was better than the economies of other EU countries. Poland turned out to be the only EU country which managed to maintain a positive growth rate in spite of the crisis, while the remaining countries slipped into recession.

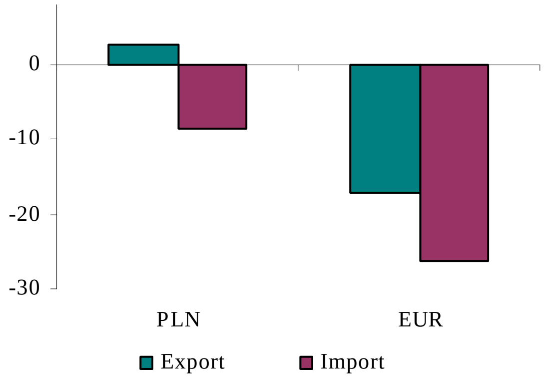
GDP growth rate (%)



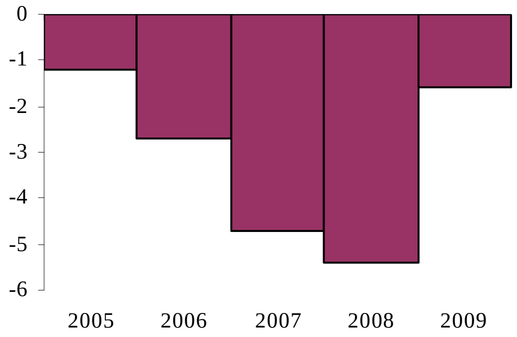
Individual consumption and gross fixed investment (%)



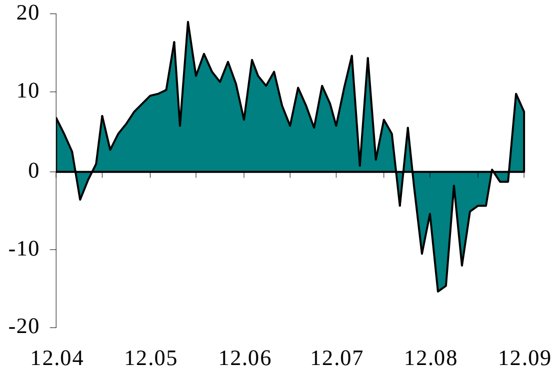
Change in the trade volume - 2009/2008 (%)



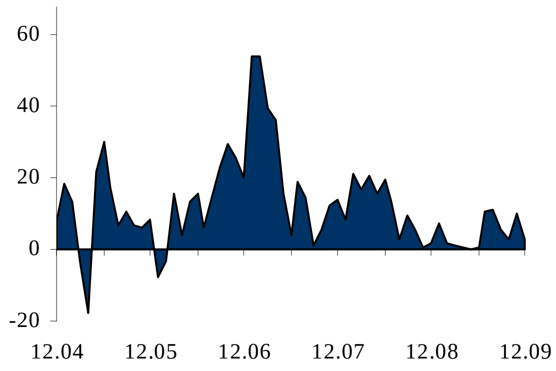
Deficit on current account/GDP (%)



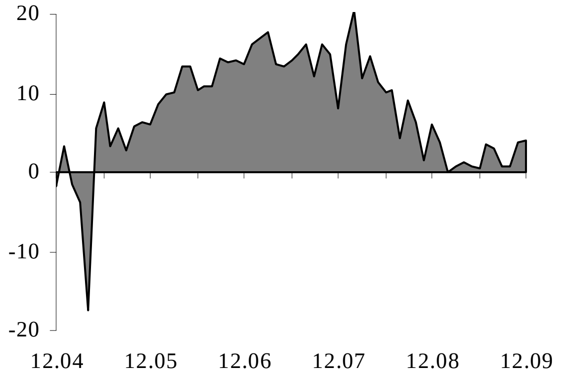
Annual growth rate of industrial production (%)



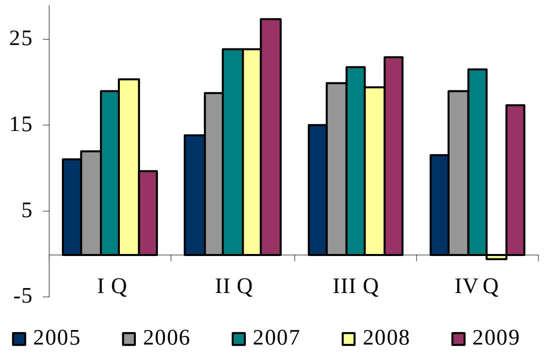
Annual growth rate of construction and assembly production (%)



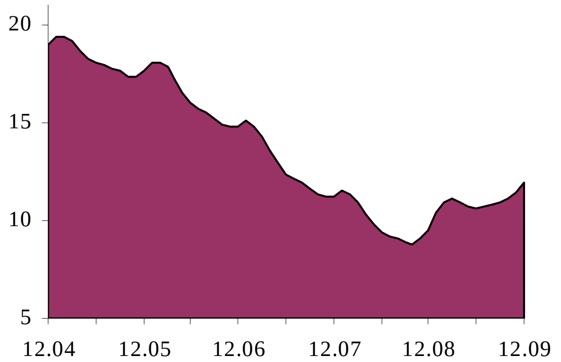
Annual retail sale growth rate (%)



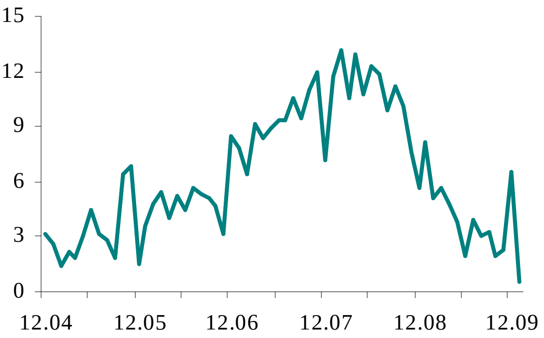
Financial results of the enterprise sector (in billion PLN)



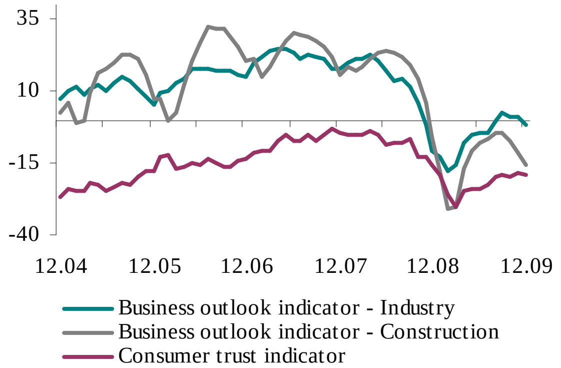
Unemployment rate (%)



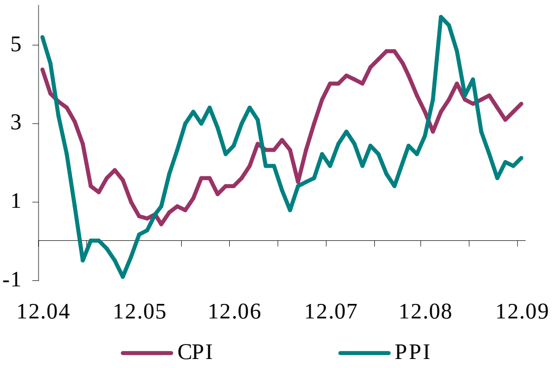
Annual growth rate of remuneration in the enterprise sector (%)



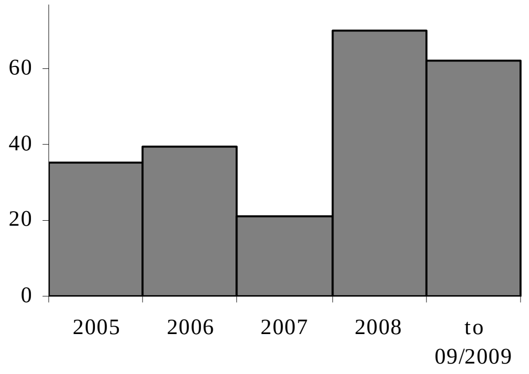
Business outlook indicators



CPI and PPI Inflation (%)



Growth of public finance sector debt (billion PLN)



Public debt/GDP (%)

Source: Central Statistical Office (GUS), Ministry of Finance (MF)

According to the initial estimate of GUS, the Gross Domestic Product increased in 2009 by 1.7% in real terms, which meant a significant decrease in comparison to the growth rate observed in the years 2006-2008 (6.2%, 6.8%, 5.0%). The main reason for the slowdown was the decline in external demand and general deterioration of atmosphere, which led to restrictions of production and private investment. On the other hand, very high gross fixed investment made by the public sector had a stabilising effect on the economy, as well as the PIT reform and high indexation of pension benefits. The adverse impact of global recession on the Polish economy was also to some extent mitigated by the weakening of zloty. Despite the difficult external conditions, the Polish economy managed to avoid recession, and in the second half of the year, the signs of improvement appeared.

Most areas of the economy experienced the decrease in activity. According to preliminary estimates:

- Sold production of industry in 2009 fell by 3.5% (against the increase by 3.6% in 2008 and 10.7% in 2007). The decrease occurred primarily in companies manufacturing investment goods, goods related to energy and supply, while companies producing consumer goods recorded an increase in production. This resulted from the reduction in the portfolio of domestic and foreign orders, excessive inventories, difficulties in obtaining financing and uncertainties about future economic developments. The growth rate of construction and assembly production remained positive despite the strong decline, and amounted to 3.0% (against the increase by 12.1% in 2008 and 15.5% in 2007). Companies dealing with building construction and specialist works recorded a decline, and civil engineering companies recorded a strong increase. The consequence of the decline in economic activity was the low utilization of production capacity [1] and deterioration of mood among companies. After having reached the minimum readings by business indicators in the first quarter of the previous year, they improved during the subsequent periods. However, at the end of the year mood deteriorated again, and the business indicator readings remained within the negative areas (particularly in construction);
- Retail sale increased by 1.3% (in 2008, the growth was 5.0%). The decrease concerned mainly groups of fuels and motor vehicles;
- exports in PLN in current prices increased by 2.7% and imports decreased by 8.5% (negative balance amounted to PLN 37.7 billion, against minus PLN 91.6 billion in 2008). In EUR, exports decreased by 17.1%, and imports by 26.3% (negative balance was EUR 8.7 billion against minus EUR 26.2 billion in 2008). Export growth in terms of PLN resulted from the weakening of zloty (the average exchange rate of EUR against PLN in 2009 amounted to 4.3273 while in 2008 it was 3.5166), which compensated for the reduction in the number of orders and had a positive impact on the situation of exporters. The weakening of zloty combined with the decrease of business activity also resulted in a sharp imports decline, which improved the foreign trade balance on the one hand (it is estimated that the deficit in current turnover decreased from 5.1% of GDP in 2008 to 1.6% in 2009), and on the other hand, it supported the situation of companies manufacturing for the domestic marked (competition limitation). Thus, the strong weakening of zloty observed in the 2nd half of 2008 and at the beginning of 2009 created for the economy a "pillow" which mitigated the crisis phenomena;
- despite the decline in economic activity, the financial result of the enterprise sector amounted to PLN 78.9 billion and was higher by 25.1% than in 2008 At the same time, the percentage of companies declaring after-tax profit slightly increased (from 76.7% to 77.3%) and the total loss of companies declaring a negative financial result decreased (from PLN 22.3 billion to PLN 18.7 billion). Revenues from total business activity increased to a greater extent that their costs (by 1.6% and 0.7%, respectively). The financial result from the sale of products, goods and materials has improved (by 1.4%) as well as the result from the remaining operational activity (by 12.8%). As a result, most economic and financial assessment ratios have improved (the ratio of overall activity costs decreased from 95.8% to 95.0%; net turnover profitability ratio increased from 3.3% to 4.1%). The liquidity of companies has also improved. In spite of favourable results, it should be noted that the key element of the improvement was to decrease the negative result from financial operations (from PLN 17.1 billion to PLN 3.0 billion), which was the result of solving the problem of foreign exchange derivative transactions having a very negative impact on the performance of companies in 2008.

[1] According to estimates, in January 2010 the rate of production capacity utilization in industrial processing was about 72%.

- negative phenomena occurring in the economy translated into gradual deterioration in the labour market. It the end of 2009, the number of registered unemployed amounted to 1 893 thousand and the unemployment rate was 11.9% (compared with 1 474 thousand unemployed and 9.5% at the end of 2008). The average monthly gross salary in the enterprise sector in 2009 was PLN 3 325 (in December PLN 3 652) and was higher by 4.4% than in 2008 (by 1.1% in real terms), but the dynamics of remuneration growth slowed down sharply[2]. Although the situation on the labour market turned out to be more favourable than it had been forecast at the beginning of the last year, however, further deterioration is expected in 2010, being the result of delayed adaptive reactions. Therefore, the decrease in the income situation of some households should be expected in the incoming periods. The negative phenomena resulted in the deterioration of atmosphere among the consumers. Although it has been significantly improving since the second quarter of the last year, it still remains within the area of negative readings;
- despite the decline in economic activity and progressive deterioration in the labour market, the growth rate of prices of consumer goods and services remained at a high level. Consequently, in December last year, inflation measured by CPI (year/year) was 3.5% (compared with 3.3% in December 2008), which means that it is at the the upper boundary of the inflation target deviation band (2.5%). Strong depreciation of zloty in the second half of 2008 and at the beginning of 2009, increase in regulated prices and increased prices of tobacco products and alcoholic beverages contributed to the high level of inflation. In turn, after the acceleration in the first half, the price dynamics of sold production of industry decreased and in December last year PPI (year/year) was 2.1% (compared with 2.7% in December 2008);
- rapid reductions in economic growth combined with the previous reductions of fiscal burden (among other things, the reduction of pension contributions and the introduction of two personal income tax rates) resulted in a significant decrease in tax revenue on the one hand, and the fast accumulation of budget deficit on the other. This resulted in the need to amend the budget act in the second half of the previous year. However, due to the gradual improvement of economic outlook and the resulting restoration of tax revenue (especially indirect taxes), it was possible to limit the scale of the deficit. The inflow of EU funds also had a positive impact on the budget. Finally, the budget deficit amounted to PLN 23.8 billion (compared with PLN 24.3 billion in 2008 and PLN 27.2 billion in the amended budget for 2009)[3]. In spite of relatively good implementation of the budget, the situation in the public finance sector deteriorated even more. According to preliminary estimates, the deficit in the public finance sector in 2009 was about 7.2% of GDP (compared with 3.6% in 2008 and 1.9% in 2007), and the debt of the public finance sector increased from 47.2% in 2008 to about 49.5% in 2009. The consequence of the negative phenomena is a very sharp increase in the budget deficit planned for the year 2010 . (PLN 52.2 billion) and a further increase in the debt of the public finance sector (up to about 53% of GDP). At the same time, since the deficit of the government and self-government institution sector exceed the reference value of 3% of GDP in 2008, the European Commission has initiated the excessive deficit procedure towards Poland, under which Poland is obliged to decrease, by 2012, the annual public finance deficit to the level of 3% of GDP.

Situation on the financial market, monetary policy, reactions of banks

At the beginning of 2009, the aversion to risk continued to increase, which resulted in, among other things, further declines in share markets and the depretiation of currencies from emerging markets. At the end of February and the beginning of March, a fundamental change of atmosphere occurred. This should be associated with actions taken by governments of particular countries and international organisations, as well as with the inflow of information which is better than expected, to the market (mainly in the form of so called leading indicators). As a result, some investors concluded that the most severe phase of the crisis was over and proceeded to buy overestimated assets. This led to a very strong rebound in share markets, increase in prices of raw materials and the gradual strengthening of currencies from emerging markets. Also, the improvement in functioning of the interbank market has been observed, which reflects the gradual rebuilding of trust among the participants of this market, and the decrease in risk premiums reflected in quoting CDS contracts. Investors remained optimistic until the end of the year, which should be associated with the inflow of data to the market, reflecting the recession phenomena being overcome by the global economy. However, there are still concerns about the scale and stability of the improvement.

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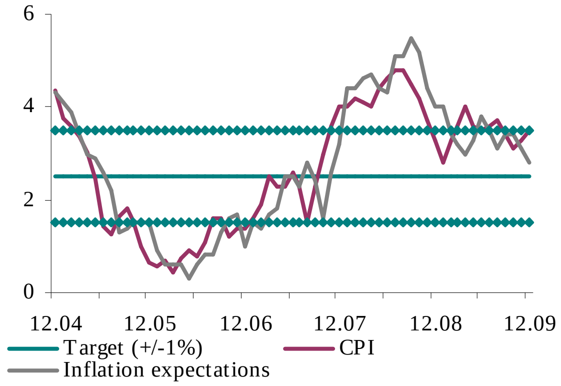
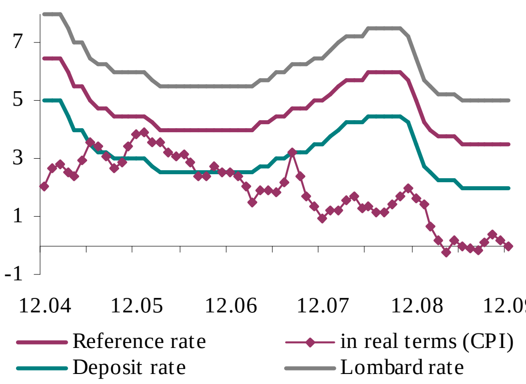
[2] The average gross monthly pension in the non-agricultural public insurance scheme amounted to PLN 1 543 and was higher by 8.7% than in 2008 (by 4.3% in real terms).

[3] Compared with 2008, revenue from indirect taxes rose by 0.9%, and funds from the EU by as much as 117.9%. On the other hand, corporate income tax revenue fell by 11.0% and personal income tax revenue by 7.7%.

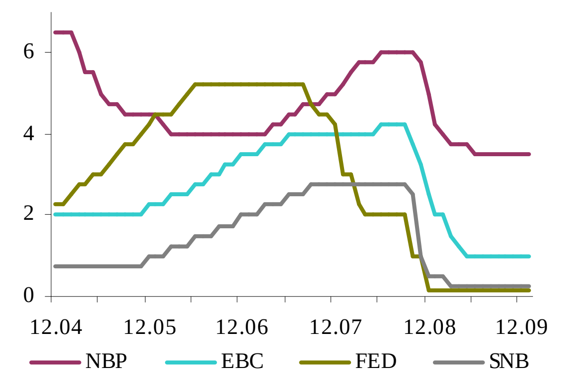
Implementation of the direct monetary policy target (%)



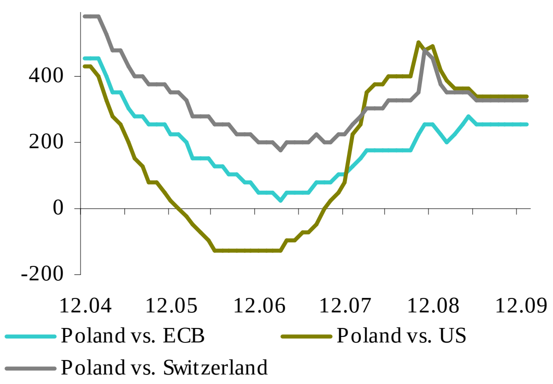
The NBP interest rates (%)



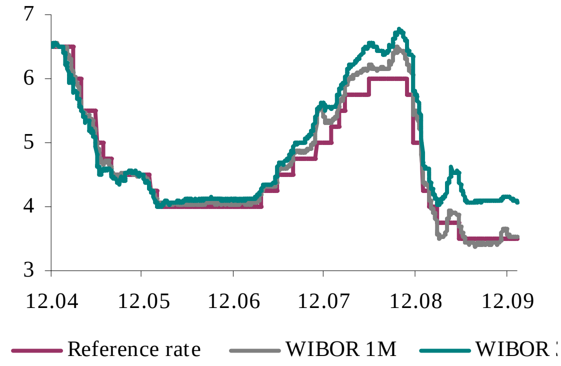
Basic interest rates of central banks (%)



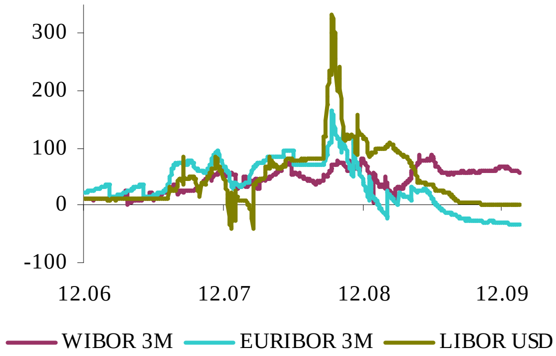
The difference in the levels of reference rates (basis points)



The NBP reference rate and WIBOR rates (%)



Deviation from reference rates (basis points)



Source: GUS, the NBP, EBC, FED, SNB, Bloomberg, independent estimates

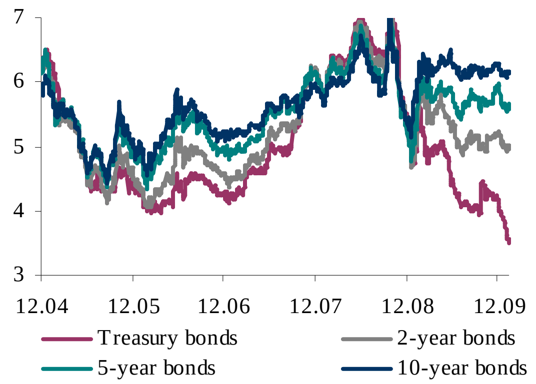
RPP continued to quickly mitigate the monetary policy[4] with the aim to stimulate the weakening economy, (believing at the same time, that the probability for the inflation to fall below the inflation target in a medium period is greater than the probability that inflation will be higher than the target). As a consequence, the NBP interest rates were reduced by 150 basis points[5] and their levels were record low (the reference rate dropped from 5.00% at the end of the previous year to 3.50%). As a result, there was a reduction of disparity between the NBP

[4] „Assumptions of the monetary policy for the year 2009" include the statement that „The basic aim of the monetary policy implemented in 2009 will be - as in the previous years – to strive to maintain inflation at the level of 2.5% in a medium period. At the same time, the monetary policy will be still applied in a way which helps to maintain balanced economic development.".
The basic tool to reach the inflation target are the NBP interest rates, which task is to shape the short-term interest rates of the financial market. This is done by open market operations (on the initiative of the NBP) and deposit and loan operations (on the initiative of banks). The basic rate is the NBP reference rate specifying the minimum profitability of basic operations of NBP which influences the level of short-term market interest rates. The the NBP lombard rate establishes the cost of acquiring money in the NBP (specifying the upper limit of market rate growth *overnight*), and the NBP deposit rate establishes interest on a deposit in the NBP (specifying the lower limit for market rate fluctuations *overnight*).

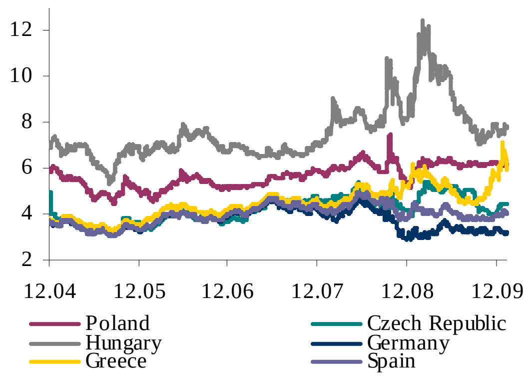
[5] In January by 75 basis points, in February, March and June by 25 basis points.

rates and the rates of main central banks[6], which had previously cut interest rates very aggressively, bringing them to the lowest levels in history.
Monetary Policy Council also lowered the compulsory reserve ratio (from 3.50% to 3.00%), and the NBP continued its activities aiming at improving the situation on the interbank market and stimulating lending. To this aim,the NBP bonds related to the decrease in compulsory reserves were redeemed earlier and the range of instruments applied under the "Trust Package" was expanded, among other things[7].
The measures taken helped rebuild confidence in the market, as evidenced by, inter alia, narrowing the gap between rates in the interbank market and the reference rate of the central bank (a similar phenomenon occurred in global markets). However, the situation on the interbank market is far from being completely normal, which is proved by, among other things, the lack of smooth functioning of operations with long dates of maturity.
Per annum, WIBOR 3M rate, which is the reference rate for most loans in PLN decreased from 6.2% in December 2008 to 4.1% in December 2009.

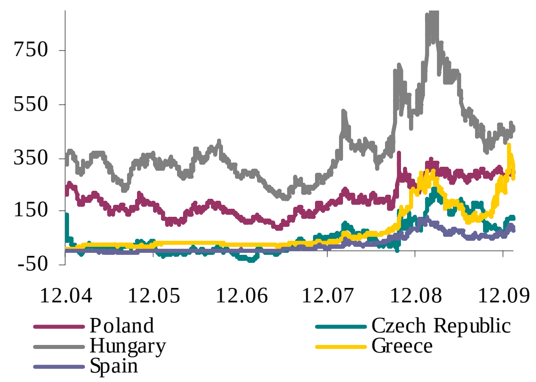
Return on Polish treasury bonds (%)



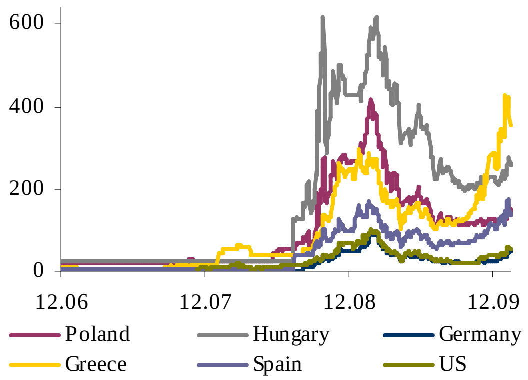
Return on 10-year treasury bonds (%)



Difference in return as compared with Germany (basis points)



Rates of 5-year CDS (basis points)



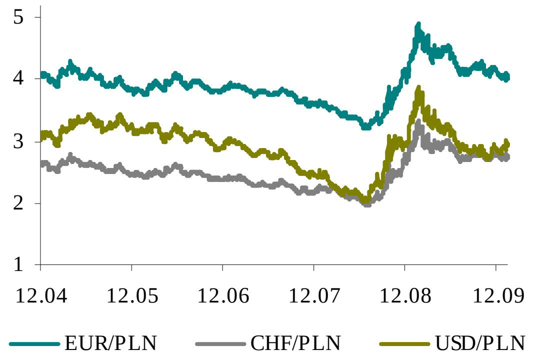
Source: Bloomberg, independent estimates

Treasury bonds market reacted to the changes in monetary policy parameters to a limited extent (mainly bonds with short maturity dates), being mainly under the influence of investors' mood (large fluctuations were observed), their risk assessments and expectations regarding future interest rates. Consequently, while the return on bonds with short maturity dates dropped significantly (average return on 52-week treasury bills in the secondary market fell from 5.7% in December 2008 to 4.2% in December 2009), the return on bonds with long maturity dates increased (average return on 5-year bonds increased from 5.2% to 5.8%, and on 10-year bonds - from 5.6% to 6.2%). The spread between Polish and German 10-year bonds was maintained, or even increased (it was 257 basis points on average in December 2008, and 300 basis points in December 2009). This unfavourable change may be explained by investors' concerns about the state of Polish public finances, as well as the large issues of treasury bonds on a global scale, which means that it is necessary to pay higher costs for the placing of issues. On the other hand, there was a gradual return of foreign investors to the Polish treasury bond market.

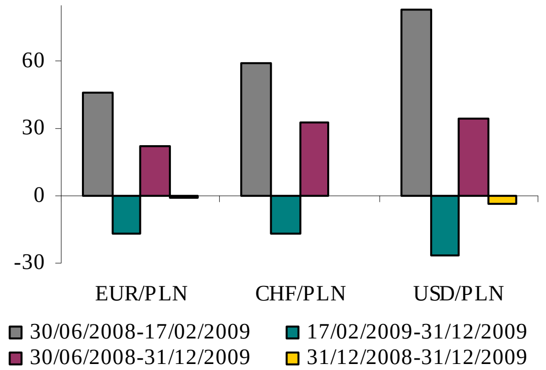
[6] In 2009 r. ECB lowered its base rate from z 2.50% to 1.00%, FED left the 0.00%-0.25% margin unchanged and SNB decreased its margin target to 0.00%-0.75%.
[7] Extension of repo and swap operations, and expansion of the list of securities accepted by the NBP as collateral on these operations.

The consequence of the improved mood in the market was also the decrease in quotation of CDS contracts, which are used to secure a lending risk connected with the issuer of debt securities (to put it simply, the higher CDS rate, the greater probability that the issuer is insolvent). However, despite the improved investment climate, CDS quotations did not return to the period from before the crisis. Moreover, in the last weeks of the previous year, CDS quotations increased again, which should be related the fact that concerns about the condition of public finances and solvency of particular countries escalated again. It should be noted that Poland comes out positively not only against other countries in the region, but also in comparison with some Eurozone countries which faced a strong deterioration of public finances. (including Greece, Spain, Portugal).

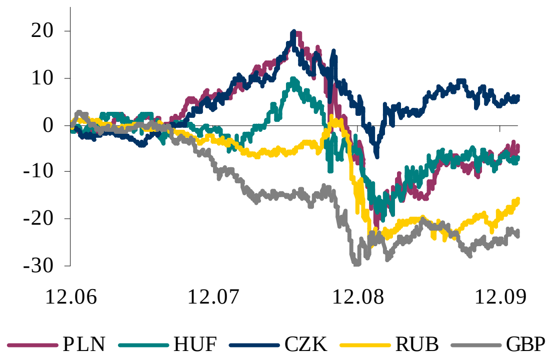
Exchange rate of main currencies against zloty



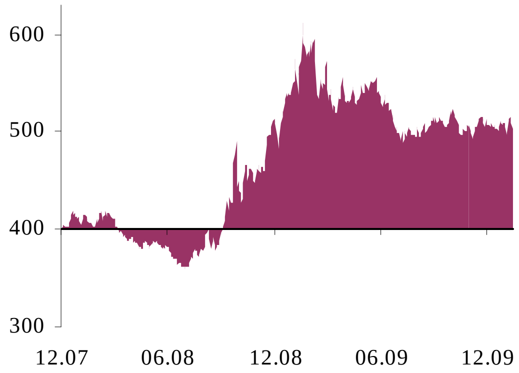
Change of main currencies against zloty



Change of currency exchange rate against EUR (%; 12/2006=100)



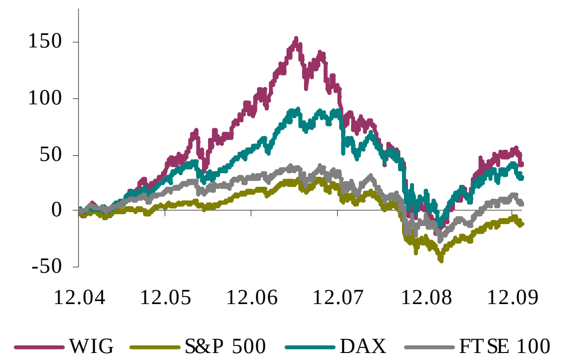
Value of the CHF loan in PLN, for PLN 400 thousand granted in 12/2007



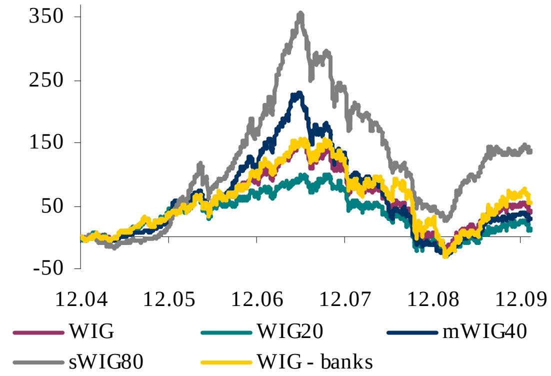
Source: Bloomberg, independent estimates

Situation in the PLN market was characterized by two phases. During the first one which lasted until mid-February, the Polish currency continued to be depreciated, and this caused zloty to fall to the minimum level from the beginning of 2004. It stemmed from a very negative atmosphere in global financial markets and accumulation of negative outlooks for the economies in Central and Eastern Europe. During the second phase, zloty stabilised and was gradually strengthened (particularly against USD), which should be attributed to the general improvement in atmosphere in global markets. The strengthening of zloty was additionally influenced by "media campaign" for the strengthening of the Polish currency, the intervention sale of EU funds directly on the foreign exchange market, acquiring access to IMF flexible credit line by Poland (USD 20.6 billion), which is granted exclusively to countries with strong foundations, as well as economy data indicating that the growth is being sustained. As a result, at the end of 2009, 1 EUR was 4.1018 (compared with 4.1724 at the end of 2008), 1 CHF was 2.7661 (2.8014), and 1 USD was 2.8503 (2.9618), which means that despite the high fluctuations during the year, the exchange rate of PLN at the end of 2009 was close to the rate at end of 2008. Nonetheless, the value of zloty against euro was nearly 20% lower than at the peak of its appreciation (in mid-2008), and by about 25% against CHF and USD. However, despite a negative impact on the situation of some borrowers, companies and on the increase of the foreign debt, the depreciation mitigated the influence of the global recession adverse effects on the Polish economy.

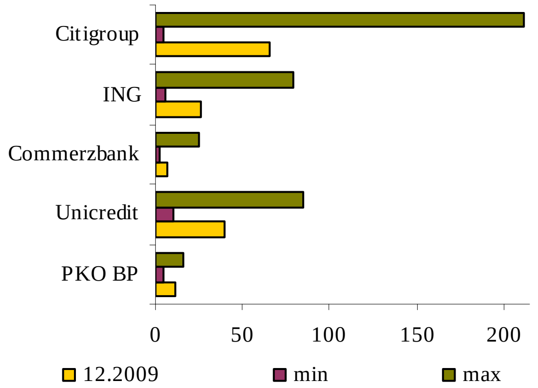
Change of index values from the end of 2004 (%)



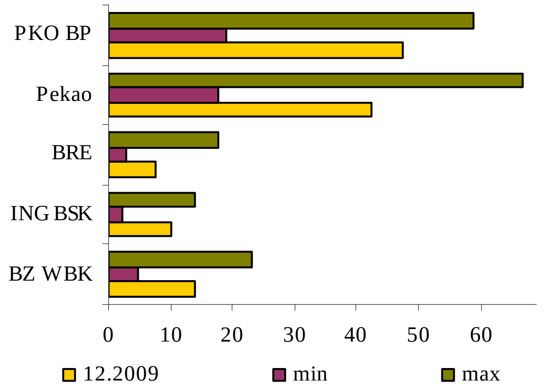
Change of index values from the end of 2004 (%)



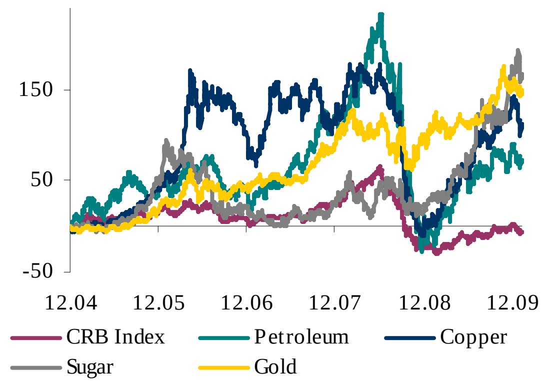
Capitalization (in EUR billion)



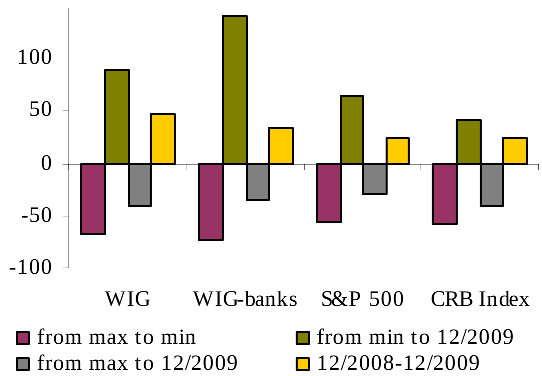
Capitalization of largest banks in Poland (in PLN billion)



Change of index values and raw material prices from the end of 2004 (%)



Change of index values (%)



Source: Bloomberg, GPW (Warsaw Stock Exchange), independent estimates

Until mid-February last year, very strong declines which started in the second half of 2007 continued, and as a result,the whole 2003-2007 market boom disappearedand indexes and share prices reached historical minimum levels or minimum levels which lasted many years. During the peak stage of market decline, WIG lost nearly 70% (WIG-Banki - over 70%) from the historical maximum, and many companies lost over 90% of their market value. At the end of February and the beginning of March, there was a turning point which led to a very strong "rebound", lifting the indexes by more than 80% above the last minimums (WIG-Banki increased by more than 140%). Consequently, this allowed the indexes to make up for the losses from the beginning of the year and finish the year with strong increases as compared with the end of 2008 - WIG increased by 46.9%, WIG20 by 33.5%, mWIG40 by 55.2%, sWIG80 by 61.8% and WIG-Banki by 33.7%. Despite the observed increases, indexes still remain 30% -40% below the historical maxima. However, it should be noted that the pre-crisis prices were prices of the peak phase of the many years' market boom, during which most companies were extremely overvalued. There is currently no way to determine whether the market boom observed since March last year marks the beginning of a new, many years' upward trend or whether it is a very strong reaction to the market decline. Undoubtedly, the risk of investing in share markets has increased. Therefore, information coming from the real economy will be of key importance - it will either provide arguments for the continuation of increases, or renew fears about the scale and sustainability of global economy recovery, and will lead to a significant adjustment of quotations (a characteristic feature of the market boom observed since March last year is no accumulation phase and no deeper adjustments, and a strong rebound in a form of V was a reaction to the declines).

The situation in the commodity markets was strongly correlated with the mood of investors in financial markets as well as information coming from the economy. Therefore, during the first weeks of last year a further reduction was observed (many raw materials reached local minimums at the end of 2008), followed by a very strong reaction which led to price increases of several dozen percent. Apart from mood improvement and positive information coming from the global economy, factors which significantly influenced the growth of raw material prices were the weakening of USD and concerns about future inflation increase.

It should be noted that despite a substantial change in atmosphere on the financial market, there was no significant inflow of resources to investment funds (on a net basis). According to estimates by Online Analysis, a positive balance of payments and withdrawals in the whole year 2009 was only about PLN 3 billion. Therefore, the observed per annum increase in net assets of investment funds - from PLN 73.9 billion at the end of 2008 to93.0billion at the end of 2009 should be associated mainly with the increase in share prices (the value of funds accumulated in investment funds increased from PLN 17.5 billion to PLN 27.1 billion). This may reflect a change of preferences in the ways households invest financial surpluses - they chose classical forms of investing money in a form of bank deposits, as a result of negative experiences of the crisis. Should this change of preferences turn out to be permanent, it will contribute to the growth of deposits in the banking sector, but on the other hand, it will limit revenue of banks from commissions and fees for intermediary in trading on the capital market and managing financial assets.

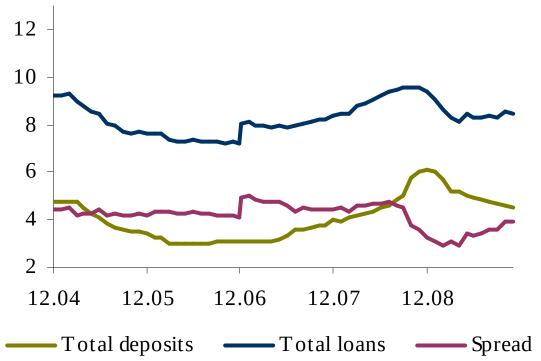
In response to the changes of the NBP interest rates and events on the financial market, banks have made amendments to the deposit and credit policy.

Weighted average interest rates on deposits and loans (%)

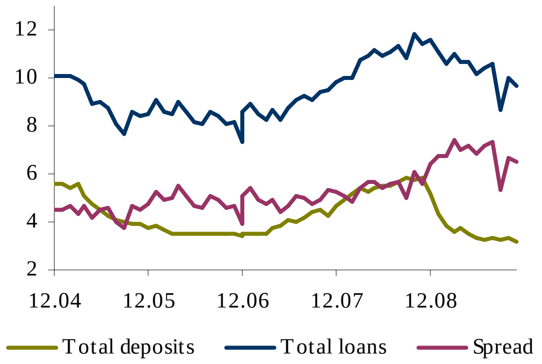
	The interest rate on the status of all contracts OPS				Interest rate on new contracts OPN			
	12/2007	12/2008	12/2009	Change in 2009	12/2007	12/2008	12/2009	Change in 2009
INSTRUMENTY ZŁOTOWE								
Total deposits	3.78	6.02	4.48	-1.54	4.22	5.85	3.17	-2.68
- households	3.47	6.05	4.77	-1.28	4.16	6.52	4.03	-2.49
- companies	4.34	5.94	3.82	-2.12	4.23	5.60	2.99	-2.61
Total loans	8.25	9.59	8.43	-1.16	9.52	11.41	9.66	-1.75
- for households	9.54	10.98	9.90	-1.08	11.55	13.61	12.49	-1.12
- for companies	6.51	7.68	5.90	-1.78	7.19	8.33	6.53	-1.80
Spread	4.47	3.57	3.95	0.38	5.30	5.56	6.49	0.93
Consumer loans								
Total	13.49	14.48	14.45	-0.03	13.72	15.32	15.12	-0.20
including credit cards	16.78	17.81	16.07	-1.74	14.80	15.92	15.11	-0.81
APRC (excluding cards)	x	x	x	x	20.23	22.55	21.77	-0.78
Home loans								
- PLN	6.15	7.92	6.01	-1.91	6.93	8.73	7.00	-1.73
APRC	x	x	x	x	7.48	9.28	7.81	-1.47
- CHF	4.55	4.31	2.18	-2.13	4.63	4.45	3.74	-0.71
APRC	x	x	x	x	4.91	4.59	4.16	-0.43
- EUR	x	x	x	x	6.63	7.09	4.87	-2.22
APRC	x	x	x	x	6.80	7.32	5.28	-2.04

Source: the NBP, independent estimates
x - the NBP does not publish data, APRC (the annual percentage rate of charge) calculated in accordance with the Consumer Credit Act.

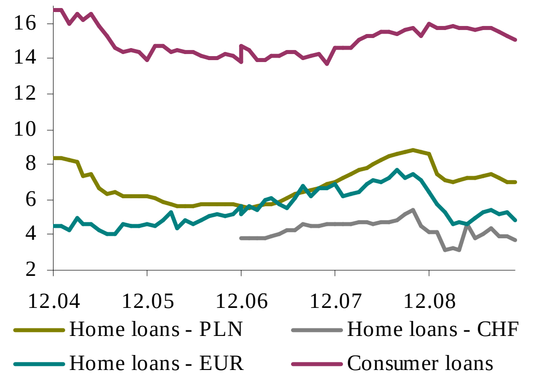
Weighted average interest rates on deposits and loans - OPS (%)



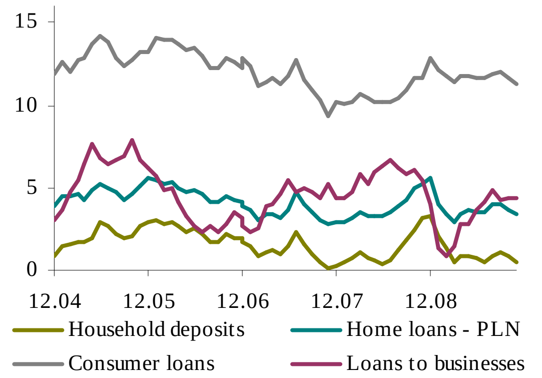
Weighted average interest rates on deposits and loans - OPN (%)



Weighted average interest rates on OPN loans (%)



Real interest rates on OPN deposits and loans (%)



Source: the NBP, GUS, independent estimates

On the basis of data on the status of all contracts (OPS) we may conclude that the weighted average interest rate on term deposits in PLN decreased from 6.0% in December 2008 to 4.5% in December 2009, and loans in PLN - from 9.6% to 8.4% resulting in the increased spread between interest on loans and deposits - from 3.6% to 4.0%. However, the average spread per annum was significantly lower. The average spread in 2009 was 3.4%, while in 2008 it was 4.4%. A strong decrease in the average spread was due to the disturbance in global financial markets and the consequent "deposit war" constituted one of the main reasons for the reduction of the result on interest rate.

When observing changes in the interest rates of new contracts (OPN), it may be concluded that the peak phase of the "deposit war" took place in the fourth quarter of 2008 Banks reduced interest rates in 2009. The average interest rate on deposits made in December 2009 was 3.2% against 5.9% in December 2008 and average interest on newly granted loans decreased from 13.6% to 12.5%. As a result, the spread between lending and deposit interest rates in terms of OPN increased from 5.6% to 6.5%. The spread increase in terms of OPN will be one of the factors that positively influence the growth of interest income in subsequent periods (the size and quality of credit portfolio is ignored here).

On the basis of data in terms of OPN it may also be concluded that changes in the deposit and credit policy of banks were in line, as far as the direction is concerned, with the changes of the monetary policy parameters (the change of the reference rate was 1.50% and taking into account the change made at the end of December 2008, it was 2.25%). However, the interest on deposits was reduced more than the interest on loans.

Situation in Poland compared with other EU countries, main sources of risks

Despite the strong slowdown, the condition of the Polish economy was better than the economies of other EU countries. According to preliminary estimates, EU GDP in 2009 decreased by 4.1% (against the increase by 0.8% in 2008 and 2.9% in 2007). In particular, due to a sharp decline of external demand, Germany, which is the largest economy in Europe, has been suffering a deep recession (estimated decline of GDP in 2009 was 5.0%). The situation in other countries was equally poor, especially in the new member states which reported a very deep recession (from nearly 5% in the Czech Republic to 18% in Lithuania and Latvia).
Poland turned out to be the only EU country which managed to maintain a positive growth rate in spite of the crisis. Growth forecasts in subsequent periods are also better than for most EU countries. Similar disadvantageous trends appear only in the scope of public debt growth in the coming years, although the debt of this sector in relation to GDP is below average levels of EU countries.

Poland in comparison with the EU countries

	GDP EUR billion	GDP growth rate					Deficit of the public finance sector % of GDP			Public debt % of GDP					Unemployment rate	
	2008	2007	2008	2009	2010	2011	2009	2010	2011	2007	2008	2009	2010	2011	2009	2010
EU	12 507	2.9	0.7	-4.2	0.7	1.6	-6.9	-7.5	-6.9	58.7	61.5	73.0	79.3	83.7	9.1	10.3
Euro zone	9 265	2.8	0.6	-4.1	0.7	1.5	-6.4	-6.9	-6.5	66.0	69.3	78.2	84.0	88.2	9.5	10.7
Germany	2 496	2.5	1.3	-5.0	1.2	1.7	-3.4	-5.0	-4.6	65.0	65.9	73.1	76.7	79.7	7.7	9.2
France	1 950	2.3	0.4	-2.2	1.2	1.5	-8.3	-8.2	-7.7	63.8	67.4	76.1	82.5	87.6	9.5	10.2
Great Britain	1 819	2.6	0.5	-4.9	0.6	1.9	-12.1	-12.9	-11.1	44.2	52.0	68.6	80.3	88.2	7.8	8.7
Italy	1 572	1.5	-1.3	-5.0	0.7	1.4	-5.3	-5.3	-5.1	103.5	105.8	114.6	116.7	117.8	7.8	8.7
Spain	1 089	3.6	0.9	-3.6	-0.6	1.0	-11.2	-10.1	-9.3	36.1	39.7	54.3	66.3	74.0	17.9	20.0
Netherlands	596	3.6	2.0	-4.0	0.9	1.6	-4.7	-6.1	-5.6	45.5	58.2	59.8	65.6	69.7	3.4	5.4
Poland	362	6.8	5.0	1.7	2.6	3.2	-6.4	-7.5	-7.6	45.0	47.2	51.7	57.0	61.3	8.4	9.9
Belgium	345	2.9	1.0	-3.1	0.6	1.5	-5.9	-5.8	-5.8	84.2	89.8	97.2	101.2	104.0	8.2	9.9
Sweden	328	2.5	-0.2	-4.9	1.4	2.1	-2.1	-3.3	-2.7	40.5	38.0	42.1	43.6	44.1	8.5	10.2
Austria	282	3.5	2.0	-3.6	1.1	1.5	-4.3	-5.5	-5.3	59.5	62.6	69.1	73.9	77.0	5.5	6.0
Greece	239	4.5	2.0	-2.0	-0.3	0.7	-12.7	-12.2	-12.8	95.6	99.2	112.6	124.9	135.4	9.0	10.2
Denmark	233	1.7	-0.9	-4.9	1.5	1.8	-2.0	-4.8	-3.4	26.8	33.5	33.7	35.3	35.2	4.5	5.8
Finland	184	4.9	1.2	-7.8	0.9	1.6	-2.8	-4.5	-4.3	35.2	34.1	41.3	47.4	52.7	8.5	10.2
Ireland	182	6.0	-3.0	-7.5	-1.4	2.6	-12.5	-14.7	-14.7	25.1	44.1	65.8	82.9	96.2	11.7	14.0
Portugal	166	1.9	0.0	-2.7	0.3	1.0	-8.0	-8.0	-8.7	63.6	66.3	77.4	84.6	91.1	9.0	9.0
Czech Rep.	148	6.1	2.5	-4.8	0.8	2.3	-6.6	-5.5	-5.7	29.0	30.0	36.5	40.6	44.0	6.9	7.9
Romania	140	6.3	7.3	-7.1	0.5	2.6	-7.8	-6.8	-5.9	12.6	13.6	21.8	27.4	31.3	9.0	8.7
Hungary	106	1.0	0.6	-6.3	-0.5	3.1	-4.1	-4.2	-3.9	65.9	72.9	79.1	79.8	79.1	10.5	11.3
Slovakia	65	10.6	6.2	-4.7	1.9	2.6	-6.3	-6.0	-5.5	29.3	27.7	34.6	39.2	42.7	12.3	12.8
Luxembourg	39	6.5	0.0	-3.4	1.1	1.8	-2.2	-4.2	-4.2	6.6	13.5	15.0	16.4	17.7	6.2	7.3
Slovenia	37	6.8	3.5	-7.8	1.3	2.0	-6.3	-7.0	-6.9	23.3	22.5	35.1	42.8	48.2	6.7	8.3
Bulgaria	34	6.2	6.0	-5.0	-1.1	3.1	-0.8	-1.2	-0.4	18.2	14.1	15.1	16.2	15.7	7.0	8.0
Lithuania	32	9.8	2.8	-15.0	-3.9	2.5	-9.8	-9.2	-9.7	16.9	15.6	29.9	40.7	49.3	14.5	17.6
Latvia	23	10.0	-4.6	-18.0	-4.0	2.0	-9.0	-12.3	-12.2	9.0	19.5	33.2	48.6	60.4	16.9	19.9
Cyprus	17	5.1	3.6	-1.7	0.1	1.3	-3.5	-5.7	-5.9	58.3	48.4	53.2	58.6	63.4	5.6	6.6
Estonia	16	7.2	-3.6	-14.1	-0.1	4.2	-3.0	-3.2	-3.0	3.8	4.6	7.4	10.9	13.2	13.6	15.2
Malta	6	3.8	2.1	-1.9	0.7	1.6	-4.5	-4.4	-4.3	62.0	63.8	68.5	70.9	72.5	7.1	7.4

Source: European Economic Forecast Autumn 2009 EC, Interim forecast - February 2010 EC, Eurostat.

The relatively high resistance of the Polish economy to the effects of the global crisis should be explained by the occurrence of several factors:

– First, Polish economy has a relatively large internal market and is less open in comparison with other economies in the region. It also characterised by a relatively high level of diversification (among other things, lack of clear domination of one sector and no large enterprises/conglomerates which decide about the development of the whole economy) and high flexibility of a large part of companies that were able to adapt to difficult external conditions;
– Second, high investment outlays made by the public sector played an important stabilizing role (to a large extent, they replaced the reduction of investment by the private sector), as well as the reduction of PIT rates and high indexation of pension benefits, or earlier lowering of the pension contribution. These actions have a certain similarity to the stimulus packages implemented in other countries and are associated with certain fiscal costs (reflected in the rapid growth of public finance sector debt);
– third, floating exchange rate helped to absorb the external shock - a decline in orders was largely offset by higher proceeds resulting from the weakening of zloty, and some companies reported growth in orders due

to the increase of their competitiveness. At the same time, the depreciation of zloty did not cause significant inflationary tension;

– fourth, Poland is characterized by a low level of "banking" (relatively low development of the financial market) and the local character of the banking system. As a result, the banking sector did not suffer large losses in foreign markets that require involvement of public funds. At the same time, parent companies did not withdraw funding and household deposits experienced strong growth. Moreover, since the importance of financing companies by the banking sector or with funds raised on the capital market is lower than in other countries, restrictions of funding by banks and the downturn at the stock exchange did not have such negative impact as in many other countries. In other words, the channel transferring the crisis phenomena from the financial sector to the economy turned out to be narrower.

Although Polish economy has positively adapted to the external crisis, its future condition depends on developments on a global scale. Although the situation on financial markets improved in 2009 and in the second half-year the economies of USA and EU experienced growth, there are still many risks accumulating which may delay the process of rebuilding the global economy or cause further outbreaks of the crisis.

SELECTED SOURCES OF POTENTIAL MACROECONOMIC RISKS

TRUST CRISIS (atmosphere on markets may easily change)	
FOREIGN	Undisclosed bank losses
	Concern about the strength and durability of the observed recovery and developments in the labour market
	Concern regarding further economic development in the USA
	Strong deterioration of public finances in some countries
	- very large budget deficits the USA and the UK
	- difficult situation in some countries belonging to the the so-called PIIGS group [8]
	Record low interest rates and concern about the consequences of the future tightening of monetary policy (low interest was one of the primary causes of the crisis - are the reason to seek alternative investments which ensure a higher rate of return, "encourage" speculation and bad asset allocation, as well as excessive debt)
	Concern about the future growth of inflation phenomena
DOMESTIC	Concern about the development of macroeconomic situation, including developments on the labour market
	Very high budget deficit
	Rapid growth of debt in the public finance sector

It is difficult to determine which of the risks identified by various observers may actually materialize, and what their implications would be for the global economy. However, one must be aware of them and banks have to take them into consideration when formulating a strategy for the coming years. The most important ones include: concerns about the strength and durability of the observed revival (including the developments on the labour market), rapid growth of budget deficits which poses a risk of causing financial imbalance in some countries, concerns about future consequences of monetary policy being currently implemented, and concerns about increasing losses of banks[9].

[8] The abbreviation is used to identify the group of countries including: Portugal, Italy, Ireland, Greece and Spain. Currently, the country being under the greatest pressure is Greece.

[9] According to IMF estimates, until the end of 2010, bank losses incurred as a result of the crisis could reach USD 2.8 trillion (USA - USD 1.0 trillion, Europe - USD 1.6 trillion, Asia - UDS 0.2 trillion) - see "Global Financial Stability Report," October 2009.

GDP growth rate (year/year) in 2009 and forecast for the years 2010-2011 (%)

	2009	Forecasts					
		EC		IMF		OECD	
		2010	2011	2010	2011	2010	2011
Poland	1.7	2.6	3.2	2.2	4.0	2.5	3.1
EU[10]	-4.2	0.7	1.6	1.0	1.6	0.9	1.7
Germany	-5.0	1.2	1.7	1.5	1.9	1.4	1.9
the USA	-2.4	2.2	20	2.7	2.4	2.5	2.8
Japan	-5.2	1.1	0.4	1.7	2.2	1.8	20
China	8.7	9.6	9.5	10.0	9.7	10.2	9.3

Source: Eurostat, European Commission, IMF, OECD

Currently it is difficult to determine whether a fundamental change in atmosphere in financial markets which occurred in the past year, as well as the revival of the global economy observed since the second half of the previous year mean, that the recession has been permanently overcome and this is the beginning of the path of sustainable, stable growth. Some economists believe that it is too early to speak about the end of the crisis (pointing to the sources of risks mentioned above). However, most international institutions expect a gradual improvement and a permanent overcoming of the crisis without the "second economic trough" effect (this is reflected by, among other things, verifications of earlier forecasts regarding the growth of particular economies). It is being emphasised, however, that the recovery is "fragile" and it is necessary to take radical steps, in particular to create a new architecture of financial markets (including regulation at micro and macro scales) that will ensure stability of the financial system and counteract the formation of "bubbles".
From the point of view of the Polish economy the situation in the EU countries will be of paramount importance, particularly in Germany which is the main trade partner of Poland (over 25% of Polish exports is directed to the German market). Developments in the "emerging market" countries will also have a significant impact, which is due to the fact that many investors include Poland in the same "basket".

To sum up, **external factors are the main source of short-term and medium-term risks for the Polish economy, and thus for the banking sector**, such factors being triggered by the financial crisis which started in 2007 and evolved into the greatest crisis of the global economy since the Great Depression of the 1930s. **In spite of the fundamental change in atmosphere on financial markets, improved functioning of these markets and signs of the global economy entering the path of growth** it should be concluded that **the high level of risk for the Polish banking system is continuously maintained**. As a consequence, this may adversely affect the situation of banks, and banks must take these risks into account when formulating their strategies.

[10] In case of the IMF and OECD forecasts, the data relates to the euro zone.

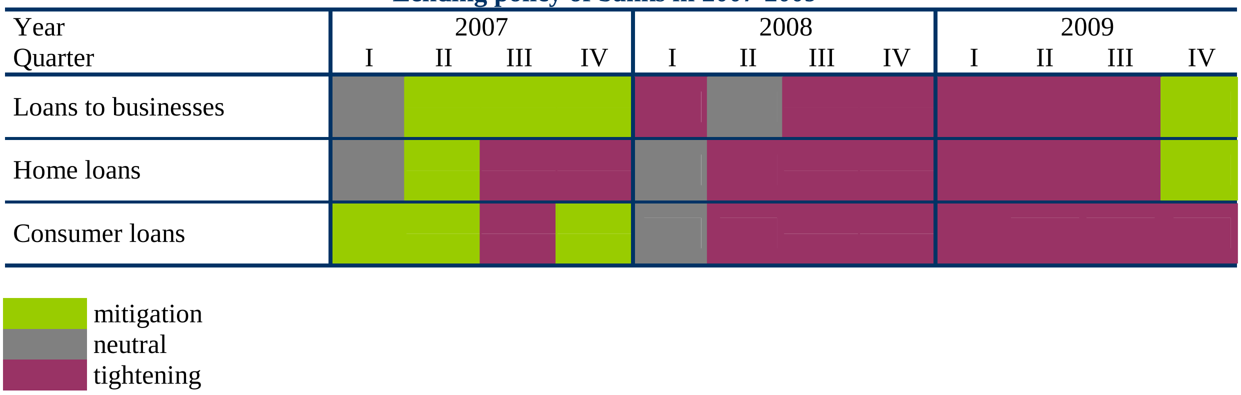
II. MAIN DEVELOPMENT DIRECTIONS, BASIC TRENDS

A strong decline in economic activity, combined with the persistent uncertainty about future development of the situation and aversion to excessive risk-taking translated into decreased activity of the banking sector. As a result **banks have reduced their expansion and concentrated on adjusting business models to the difficult external** conditions.
However, **despite the strong deterioration in financial performance, the situation of the banking sector in 2009 remained stable, and the capital position of banks was strengthened**.

Main items of assets and liabilities of the banking sector (PLN billion)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
BALANCE SHEET TOTAL	586.4	681.8	795.4	1 039.1	1 060.8	21.7	2.1
Assets							
- cash and operations with the NBP	17.8	23.0	28.2	39.4	50.4	11.0	27.9
Receivables from the financial sector	122.3	134.5	125.2	107.2	72.9	-34.3	-32.0
receivables from the non-financial sector	248.6	314.7	421.9	587.6	612.1	24.4	4.2
receivables from the budget sector	21.6	22.8	21.4	24.6	44.5	19.9	80.7
- securities	133.9	142.5	135.6	180.9	211.4	30.4	16.8
Liabilities							
- operations with the NBP	2.5	5.0	3.0	18.1	14.5	-3.7	-20.2
- liabilities to the financial sector	92.3	119.0	158.4	242.2	225.4	-16.8	-6.9
- liabilities to the non-financial sector	337.4	383.9	428.3	506.1	571.8	65.7	13.0
- liabilities to the budget sector	29.5	32.5	44.7	53.5	54.3	0.8	1.5
- equity (funds) and subordinated liabilities	55.0	59.2	68.4	82.3	104.9	22.6	27.5
- net financial result	9.1	10.7	13.6	13.7	8.7	-5.0	-36.2

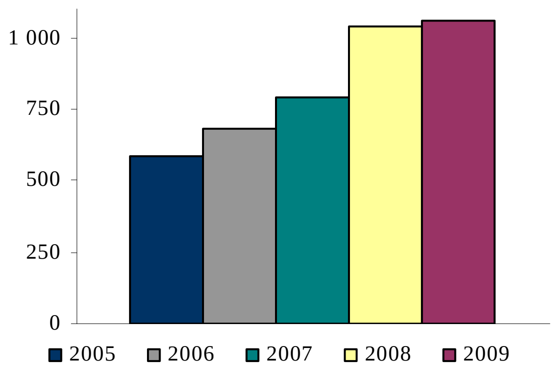
Lending policy of banks in 2007-2009[11]



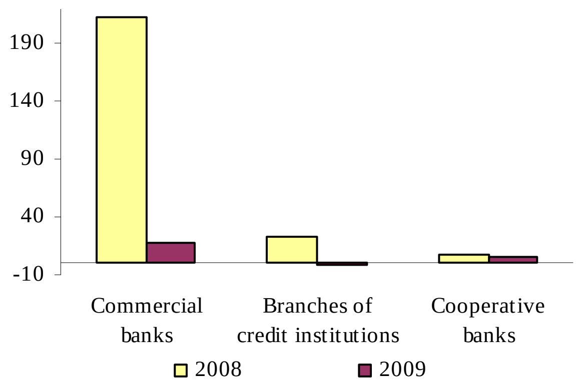
The elevated risk of the sector activity resulted in measures to increase liquidity on the one hand, and on the other, measures aiming at reducing risk exposure (by tightening credit policy, among other things), and increasing the capital buffer. Reduction of exposition to financial sector entities was observed, as well as the increase of safe debt security portfolio (treasury and the NBP) as well as the emphasis on the acquisition of deposits and the increase of the capital base.
In 2009, the balance sheet total of the banking sector increased only by 2.1% (in comparison with 30.6% in 2008[12]). It should be added however, that apart from the negative impact of external conditions, a significant impact on reducing the dynamics was exerted by the decline in the value of balance sheet items related to valuation of derivative instruments held for trading (by PLN 32.5 billion), which was caused by maturity (also due to the restructuring) and the lack of revolving of some of these transactions.

[11] Independent study on the basis of the "Situation on the credit market" by the NBP (based on answers to the questions 1 and 8 of the NBP survey).
[12] A very large increase in the balance sheet total in 2008 was largely derived from the substantial weakening of zloty.

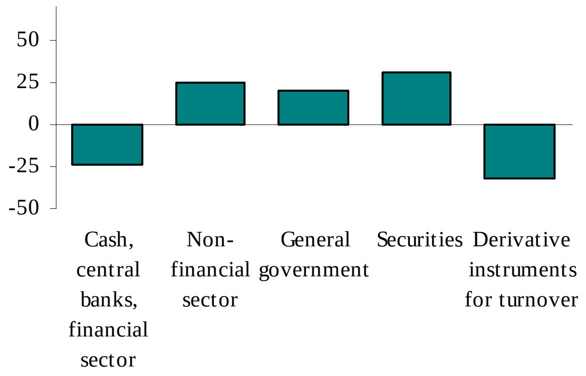
Balance sheet total of the banking sector (PLN billion)



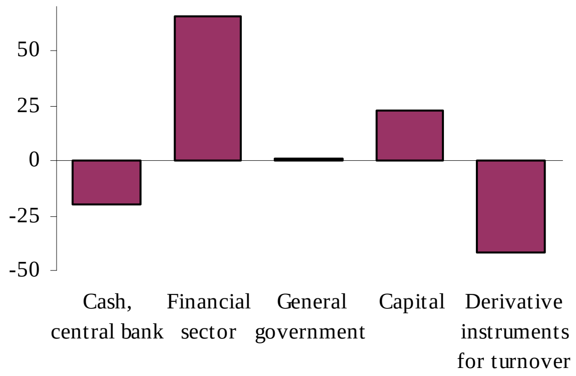
Change of the balance sheet total status (in PLN billion)



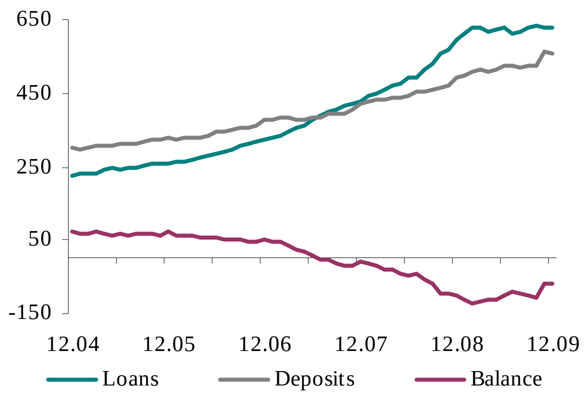
Change in status of the main asset items in 2009 (in PLN billion)



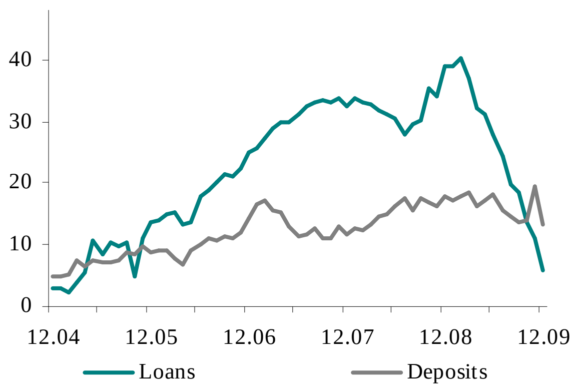
Change in status of the main liability items in 2009 (in PLN billion)



Loans and deposits of the non-financial sector (in PLN billion)



Growth rate of loans and deposits (in PLN billion)



Consequently, **changes in the balance sheet structure of the banking sector occurred**, the most important of which consisted in:

- slight increase in the share of receivables from the non-financial sector (from 56.6% at the end of 2008 to 57.7% at the end of 2009), with the simultaneous strong increase in the share of liabilities to this sector (from 48.7% to 53.9%.) Reducing the negative gap of financing the non-financial sector by half (from PLN 81.5 billion to PLN 41.3 billion) and the increased coverage of loans by deposits (from 83.3% to 89.2%) was a positive consequence of the lending slowdown and the strong growth of the deposit base;
- reducing the share of receivables from the financial sector (from 10.3% to 6.9%), while reducing the share of liabilities to this sector (from 23.3% to 21.3%);
- increasing the share of the security portfolio (from 17.4% to 19.9%);
- increasing the share of equity (funds) (from 7.9% to 9.9%).

It should be added that the low growth dynamics of the balance sheet total concerned commercial banks (increase by 2.0%) and branches of credit institutions (decrease by 3.0%), while the cooperative banking sector reported significant increase (by 9.2%).

The sector structure, employment and distribution channels of banking services, role in the economy

The structure of the banking sector did not change significantly.

Number of banks and branches of credit institutions[13] carrying out operation activities

	2005	2006	2007	2008	2009
Total, including:	649	647	645	649	643
- commercial banks	54	51	50	52	49
- branches of credit institutions	7	12	14	18	18
- cooperative banks	588	584	581	579	576

At the end of the year, 643 banks and branches of credit institutions were carrying out operations:

- the number of commercial banks decreased from 52 to 49 as a result of finalising mergers between GE Money Bank and Bank BPH, Dominet Bank with Fortis Bank and Cetelem Bank of Sygma Bank branch in Poland;
- number of branches of credit institutions remained unchanged (Skandinaviska Enskilda Banken and DEPFA terminated their business activity, and KBL European Private Bankers and Credit Suisse commenced their business activity);
- the number of cooperative banks has decreased from 579 to 576, since several banks merged. Cooperative banks are members of three structures: Bank Polskiej Spółdzielczości (Polish Cooperative Bank - 347), Gospodarczy Bank Wielkopolski (Wielkopolska Province Economic Bank - 151) and Mazowiecki Bank Regionalny (Mazowieckie Province Regional Bank - 77). The largest cooperative bank, i.e. Krakowski Bank Spółdzielczy (Cracow Cooperative Bank) is an exception - this bank functions independently.

The ownership structure of the banking sector measured by a group's share of the sector assets (%)

	2005	2006	2007	2008	2009
Domestic investors:	30.0	30.3	29.1	27.7	31.9
- banks controlled by the Treasury	20.3	19.8	18.3	17.3	20.8
- other commercial banks	4.0	4.3	4.6	5.0	5.3
- cooperative banks	5.7	6.2	6.2	5.4	5.8
Foreign investors:	70.0	69.7	70.9	72.3	68.1
- commercial banks	69.1	66.6	66.6	66.9	63.0
- branches of credit institutions	0.9	3.1	4.3	5.4	5.1

Also, there were no significant changes in the ownership structure of the banking sector, however, the increase in the share of domestic banks is worth noting:

- As in the previous year, domestic investors controlled 10 commercial banks and all cooperative banks (the Treasury controlled four commercial banks - PKO Bank Polski (PKO Bank of Poland), Bank Gospodarstwa Krajowego (National Economy Bank), Bank Pocztowy (Postal Bank) and Bank Ochrony Środowiska (Environmental Protection Bank). Their market share measured by assets, loans and deposits amounted to 31.9%, 31.3% and 34.0%, respectively.
- Foreign investors controlled 39 commercial banks and all branches of credit institutions. Their market share measured by assets, loans and deposits amounted to 68.1%, 68.7% and 66.0%, respectively. There are investors from 18 countries in the banking sector, and the dominant role is played by Italian investors who control 13.3% of the sector assets, followed by German (9.9%), Dutch (8.7%), American (7.4%) and Belgian (5.7%).

The merger between Getin Bank and Noble Bank, finalised in January 2010 may be included in the events which will have the greatest impact on the structure of the banking sector in the nearest future. In addition, we cannot rule out that due to the crisis there will be changes of strategic investors in some banks as a result of their parent banks being taken over (for example, in 2009 BNP Paribas took over a part of the Fortis group), or necessary sales of some foreign assets by parent banks (following independent decisions aiming at improving the financial situation, or forced by the European Commission in relation to granted public support).

13 As defined by the Banking Law Act (art. 4 (1) (17)).

Employment and branch network

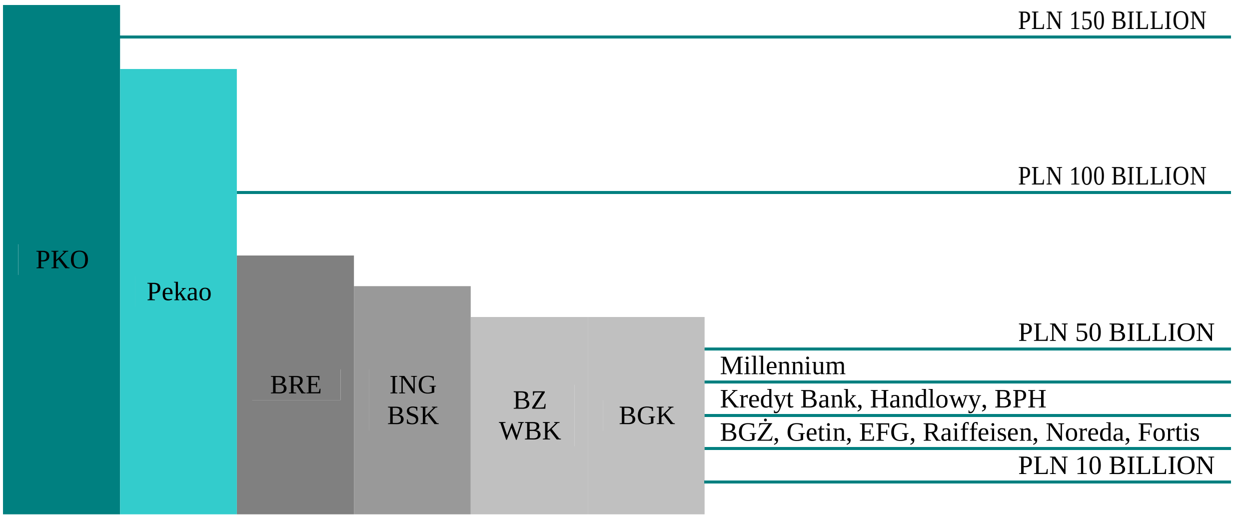
	2005	2006	2007	2008	2009
Employment – total		157 931	167 127	181 191	175 016
- commercial banks		127 201	133 724	145 406	137 941
- branches of credit institutions		1 826	3 300	4 610	5 387
- cooperative banks		28 904	30 103	31 175	31 688
Branch network – total		12 562	13 478	14 678	14 890
- commercial banks		8 592	9 280	10 237	10 229
- branches of credit institutions		171	184	236	245
- cooperative banks		3 799	4 014	4 205	4 416

The deterioration of the banking sector medium-term prospects resulted in, among other things, **the process of adapting the network of sales and employment levels to the new conditions**:

– at the end of 2009, there were 175.0 thousand persons employed in the banking sector, which is less than 6.3 thousand persons in relation to the end of 2008. The decrease in employment was lower than initially expected and occurred primarily in the commercial banking segment, while branches of credit institutions and the cooperative banks sector increased employment (as a whole). The greatest staff reduction was carried out in PKO BP (more than 1,000 employees), BRE Bank, Pekao, Bank Millennium, Kredyt Bank and BZ WBK (600-1000 employees);

– At the end of 2009, the branch network of the banking sector was made up of 14 890 entities, which constitutes an increase by 212 entities. This increase occurred mainly in the cooperative banking sector and the rapidly growing Alior Bank, while most large commercial banks underwent a process of network review and restructuring, resulting in its slight reduction.

Currently, it is difficult to predict trends in the volume of employment and the development of branch networks. On the one hand, overcoming crisis phenomena may lead to a new increase in employment and the development of sales network. On the other hand, the persisting high level of uncertainty as to the further development of the macroeconomic situation and the still high charges for credit risks materialization may lead to the adoption of a conservative business model.



PKO BP and Pekao remain unquestionable **leaders on the market.** Their assets exceed PLN 100 billion and their total share in the banking market exceeds 25%. While in 2007 Pekao overtook PKO BP, which was a consequence of taking over most of Bank BPH (resulting from the acquisition of HVB by UniCredit). PKO BP, however, rapidly rebuilt its leading position and is widening the gap again.[14] It is worth noting that PKO BP, as the first bank in Poland, exceeded the value of the balance sheet total of PLN 150 billion, and its equity is close

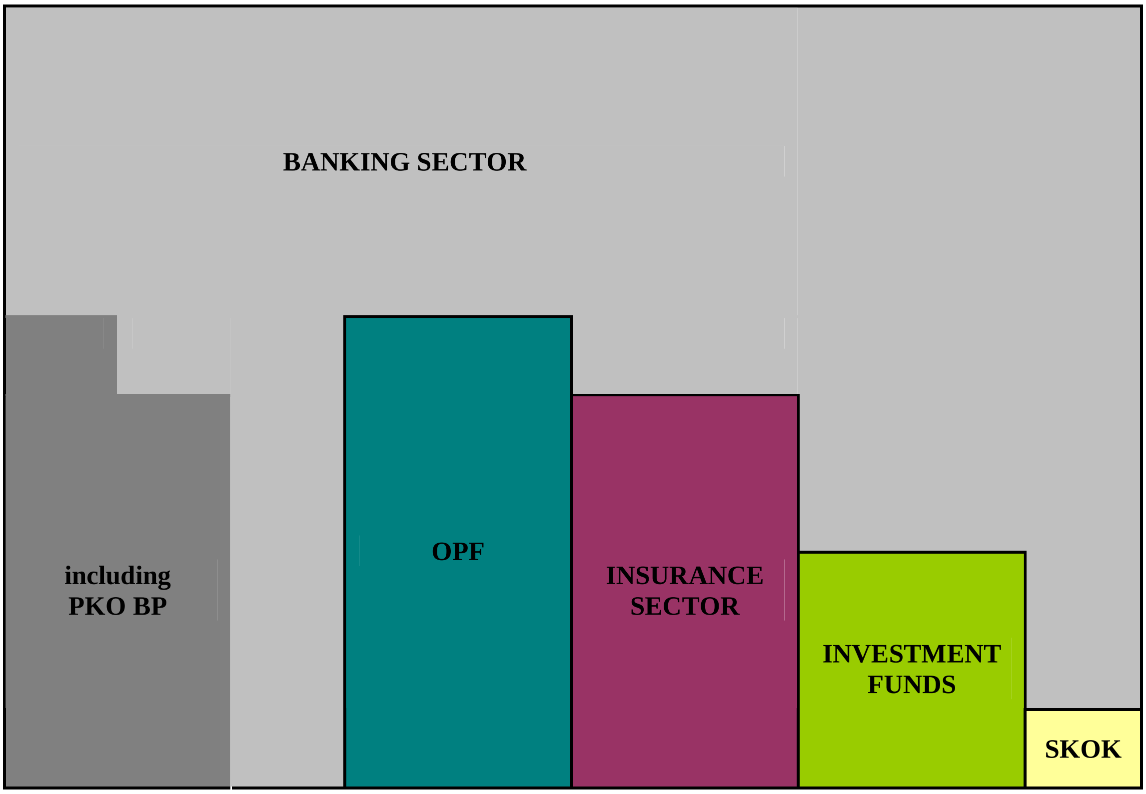
[14] A similar situation occurred in 1999, when three banks controlled by the Treasury was merged with Pekao, which resulted in the abrupt increase of Pekao assets. However, PKO BP substantially outdistanced Pekao in subsequent years.

to PLN 20 billion. Next, there is a group of four banks (BRE, ING BSK, BZ WBK, BGK), whose assets exceed PLN 50 billion and 10 whose assets exceed PLN 20 billion. In total, 16 large and medium banks with assets exceeding PLN 20 billionaccounted for 76.2% of the total market.

Assets of most co-operative banks did not exceed PLN 100 million, and only 9 had the balance sheet total exceeding PLN 500 million. Krakowski Bank Spółdzielczy and Podkarpacki Bank Spółdzielczy remained leaders in this segment. Their assets exceeded PLN 1 billion.

Despite the dominant role of several large banks, the level of concentration of the Polish banking sector remains moderate in comparison with other EU countries. At the end of 2009, the share of the five largest banks in assets, loans and deposits in the banking sector was 44.5%, 42.7% and 53.9%, respectively. This means that compared to the state at the end of 2008, the concentration measured by the CR5 index decreased minimally. Decreased share of the largest banks in total deposits is worth noting - this should be attributed to a fierce fight among medium and small institutions to acquire customers' deposits.

------------------------------- FINANCIAL SECTOR STRUCTURE ---------------------------------



Despite the decrease in the growth rate, **the banking sector remains a key element of the financial system**. At the end of 2009, assets of the whole financial sector (without the NBP) amounted to PLN 1 482.8 billion (compared with PLN 1 398.6 billion at the end of 2008), 70% of which was attributed to the banking sector. Moreover, assets of the largest banks are comparable to the total assets of the other components of the financial system, and the largest investment fund companies and some pension fund companies are controlled by banks. It should be concluded then that the stability of the banking sector is crucial for the stability of the entire financial system.

The consequence of the slow dynamics of the balance sheet total was the decreased share of banking sector assets in GDP, from 85% in 2008 to about 82% in 2009.

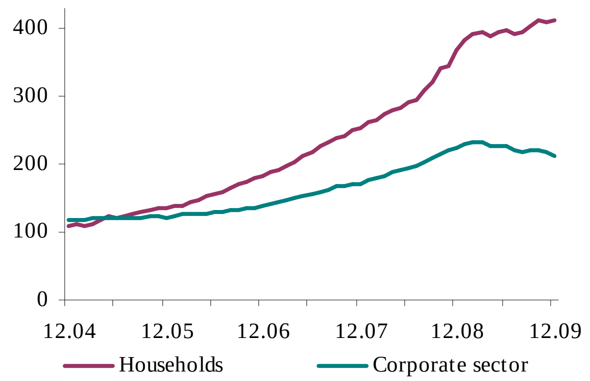
Lending and investment activity

A very large decline in dynamics of **loans for** the non-financial sector and **a change in the currency structure of newly granted loans were characteristic features of 2009**.

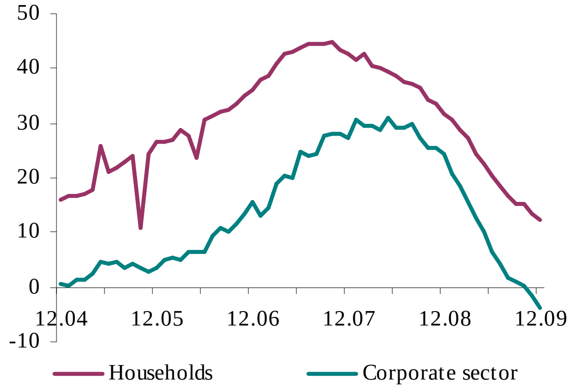
Entity structure of loans for the non-financial sector (in PLN billion, nominal value)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Total, including:	258.5	322.8	427.6	593.4	627.9	34.5	5.8
- households	136.4	183.4	254.2	368.6	412.5	43.9	11.9
- companies	121.2	138.3	171.7	222.6	212.7	-9.8	-4.4
- non-profit institutions	0.9	1.0	1.6	2.2	2.7	0.5	21.2

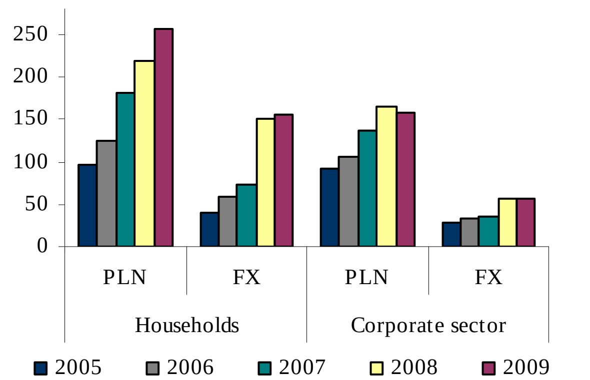
Loans for the non-financial sector (in PLN billion)



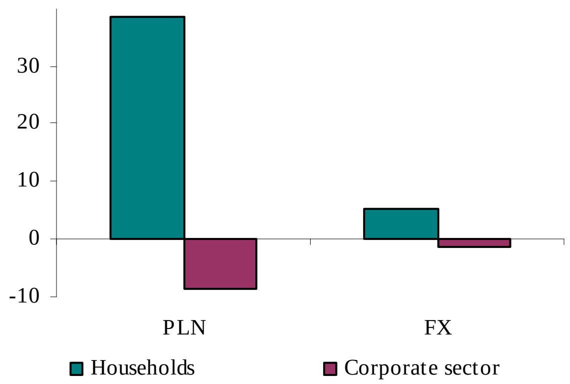
Annual growth rate of loans for the non-financial sector (%)



Currency structure of loans for the non-financial sector (in PLN billion)



Nominal increase of loans in 2009 (in PLN billion)



Nominal value **of loans for the non-financial sector increased by 5.8%**[15], from PLN 593.4 billion at the end of 2008 to PLN 627.9 billion at the end of 2009.
Given that the exchange rates of major currencies were at the end of 2009 almost identical as at the end of 2008, the study does not include the issue of the currency fluctuation impact on the lending dynamics. The variability of PLN exchange rate, however, caused significant fluctuations in loans over the last year.

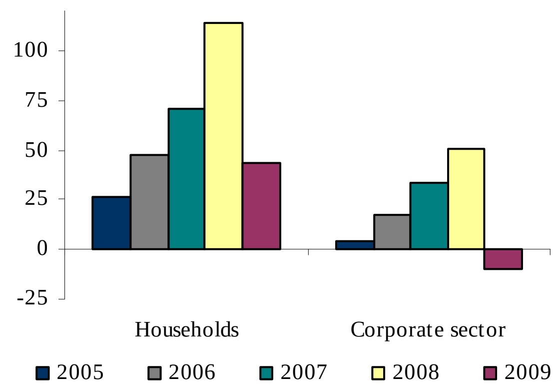
Despite the strong decline in lending dynamics, it is clear that the growth of lending observed in 2006-2008 was impossible to be sustained. Global crisis aside, it should be borne in mind that the peak phase in Polish economy occurred in 2007. In addition, natural barriers such as limited sources of financing lending and capital requirements must be taken into consideration, as well as the impact of the statistical base. Moreover, maintaining dynamics at such a high level as during the boom years posed a risk of creating much tension and imbalance in the economy. One of the negative consequences of the credit boom was a rapid rise in property

[15] It was by 5.0% in commercial banks, by 13.7% in branches of credit institutions and by 12.5% in cooperative banks.

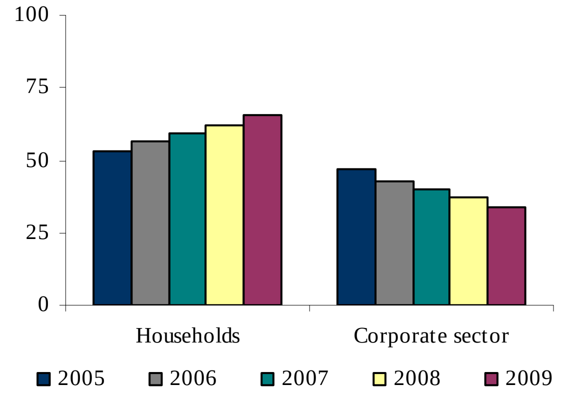
prices due to, among other things, cheap and very easily available loans, which "poured" into the market on an unprecedented scale, which combined with the lack of adequate supply and competition led to strong price increases.

Changing the currency structure of newly granted loans should be considered a positive trend. Per year, the value of loans in PLN increased by 7.9% (PLN 30.4 billion), while the value of foreign currency loans by 2.0% (PLN 4.1 billion). Despite substantial improvements, the share of foreign currency loans in total household debt is still very high and at the end of 2009 it was 37.6% (compared with 40.6% at the end of 2008). The fact which rises concern is that despite the negative experiences of the crisis (including the sudden, very deep depreciation of zloty), some banks are taking action to re-extend foreign currency lending for this group of customers. The high share of foreign currency loans generates additional increase in the system risk associated with the heightened risk of particular customers' insolvency in the event of depreciation of the zloty, and with the management of portfolios of these loans by banks (in case the turmoil in global financial markets occurs again.) Moreover, the high share of foreign currency loans for households is one of the arguments put forward by external analysts, who point to the increased risk of the Polish banking sector, and may have a negative impact on the rating of Poland and individual banks.

Increase of loans for the non-financial sector (in PLN billion)



Share in loans for the non-financial sector (%)



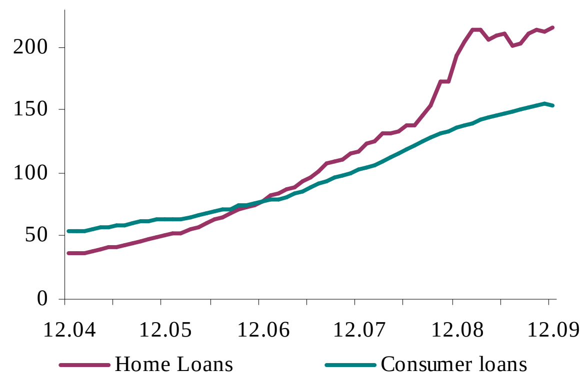
As in previous years, loans for households were characterised by the highest rate of growth - in 2009 they increased by 11.9%, while loans for companies fell by 4.4%. **At the end of 2009, the share of loans for households in the credit portfolio increased to 65.7%** (from 62.1% at the end of 2008), **and in case of loans for companies, it decreased to 33.9%** (from 37.5%). Lending to non-profit institutions was only peripheral to the operations of banks (at the end of 2009 it accounted for the mere 0.4% of the credit portfolio).
It should be added that the actual value of lending to the enterprise sector was lower, since some part of newly granted loans were loans related to the settlement of foreign exchange derivative transactions (exchanging obligations for a loan)

Leaving aside the issue of loan increase caused by the change of obligations subject to the settlement of foreign exchange derivative transactions, it may be concluded that the majority of commercial banks and branches of credit institutions decided to increase lending. Out of 16 large and medium banks with assets exceeding PLN 20 billion, only 5 limited the lending, while others increased it (by over 10% in 4 of them). It is also worth noting that only 11% of banks in the section of cooperative banks reduced their funding levels, and the remaining banks increased them - half of them by more than 10%.

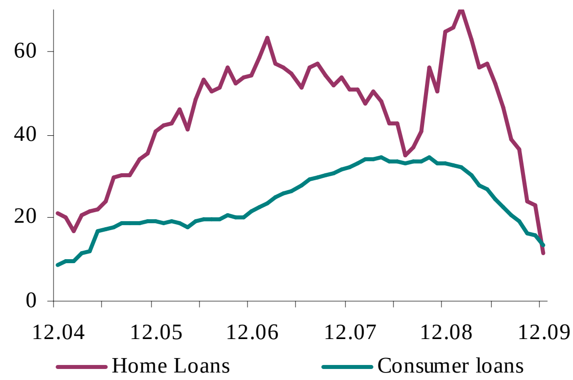
Entity-related structure of household loans (in PLN billion; nominal value)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Total, including:	136.4	183.4	254.2	368.6	412.5	43.9	11.9
- housing	50.7	78.2	117.7	194.0	216.4	22.4	11.6
including in foreign currencies	32.2	50.0	65.1	134.9	140.7	5.8	4.3
- consumer, including	63.8	77.5	102.5	136.5	154.5	18.0	13.2
overdraft	14.6	15.2	17.7	20,7	22.7	20	9.5
credit cards	4.2	5.8	8.9	12.7	15.0	2.3	18.3
other	45.0	56.5	75.9	103.0	116.8	13.7	13.3
- other	21.9	27.7	34.0	38.1	41.6	3.4	9.0

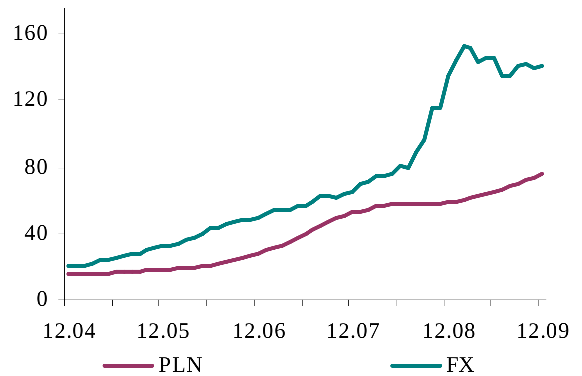
Household loans (in PLN billion)



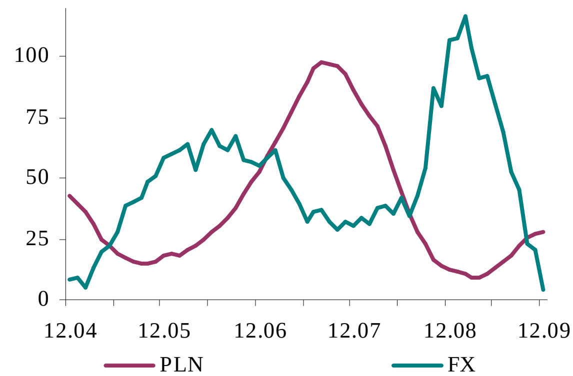
Annual growth rate of household loans (%)



Home loan structure (in PLN billion)



Annual growth of home loans (%)



Household loans increased by 11.9%[16] from PLN 368.6 billion at the end of 2008 to PLN 412.5 billion at the end of 2009, and the value of loans in PLN increased by 17.6% (PLN 38.6 billion), and currency loans by 3.5% (PLN 5.3 billion).

The portfolio of home loans increased by 11.6% (from PLN 194.0 billion to PLN 216.4 billion), which means a sharp decline in dynamics in comparison with previous years. But in the second half of the year, another revival occurred in the market (the growth of loans in the third and fourth quarter exceeded PLN 5 billion). The decline in dynamics resulted from several factors occurring at the same time, most important of which were the tightening of lending policies by banks, uncertainty about economic developments (fear of loss or reduction of income sources in the future) and reduced demand while waiting for lower prices. Moreover, the record dynamics in 2008 was largely derived from the depreciation of the zloty. We should also add that contrary to fears, banks did not cease to lend, survey shows the opposite - the number of open credit agreements on a net

[16] In commercial banks they increased by 11.3% (by 44.7% in 2008), in branches of credit institutions by 23.8% (136.5%), and in cooperative banks by 10.5% (13.1%).

basis increased by 141.9 thousand, while in 2008 the increase was 129.3 thousand. This indicates indirectly that the decline in housing prices caused the increased availability of household loans.

At the same time there has been a substantial and positive change in the currency structure of newly granted loans. As a result of tightening the lending policy, the value of loans in PLN increased by 28.1% (by PLN 16.6 billion), and the value of currency loans increased only by 4.3% (PLN 5.8 billion). This led to the increase in the share of loans in PLN (from 30.5% to 35.0%) and the decrease in the share of currency loans (from 69.5% to 65.0%). Despite this change, the share of currency loans is still very high and generates additional risk for the activity and stability of banks. Therefore, measures are required to improve the currency structure of the portfolio.

Considerable**tightening of the lending policy** occurred in the fourth quarter of 2008, and it was continued, to a lesser extent, unti the third quarter of 2009 r. It was based on increasing margins, increasing the level of required own contribution, increasing non-interest costs of loans, shortening the maximum lending period and tightening conditions regarding required collateral. At the same time, most banks ceased to grant foreign currency loans or subjected them to "prohibitive" margins which had the same effect. Banks also tightened the rules for calculating credit capacity, requirements regarding documents providing information on the income of a borrower and the rules of real estate valuation. Therefore, it may be said that all the elements of the lending policy were tightened, although the extent of such tightening was different for individual banks. Measures taken by banks should be considered **beneficial from the point of view of the stability of the banking sector**, and thus the economy.

On the other hand, in the fourth quarter last year the lending policy was relaxed, but the extent of this was described as slight by the banks. It concerned mainly the reduction of margins, other conditions were relaxed to a lesser extent. Gradually, banks started returning to granting loans denominated in foreign currencies. The mitigation was caused by increased optimism regarding the economic outlook and the situation on the housing market, i.e. increasing stabilization of prices and a significant increase in demand. The improvement of the capital situation and increasing pressure of competitors were also important factors. While some degree of mitigation may be understood, several issues give rise to concern:

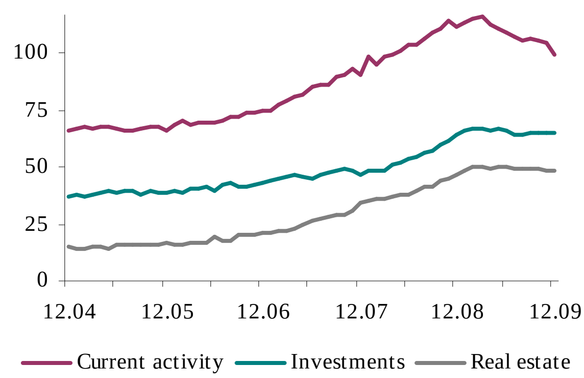
- gradual return to broader funding in foreign currencies;
- the fact that the essential reason for the decision to ease the credit policy was competition pressure;
- increasing the level of LTV by banks and emergence of offers which enable to take a loan with LTV 100% or above (the risk is reduced to some extent by the insurance system).

Despite the continuous weakening of the economy and decline of customers' mood, the value **of consumption loans increased by 13.2%** (from PLN 136.5 billion at the end of 2008 to PLN 154.5 billion at the end of 2009). As in previous periods, debt on credit cards was growing the fastest (by 18.3%). The high growth rate of this debt may be associated with the fast development of these products and their strong promotion in previous periods. On the other hand, a sharp increase in non-performing loans (by nearly PLN 1 billion) may indicate that some borrowers use credit cards to pay other obligations.
The relatively high growth occurred despite the steady tightening of credit policy in this area. It consisted in increasing margins, non-interest costs of loans, limiting the availability of simplified procedures of credit capacity analysis (including documenting a borrower's income with an income declaration) and tightening collateral procedures. The main reasons for tightening the lending policy were negative prospects of macroeconomic development and declined quality of consumer loan portfolio, and at the same time, the importance of the first factor in the first quarter did not constitute a significant reason (increased optimism regarding economic outlook).
In the first quarter of 2010, banks expect a further tightening of lending policy in this segment, together with the simultaneous growth in demand for these loans.

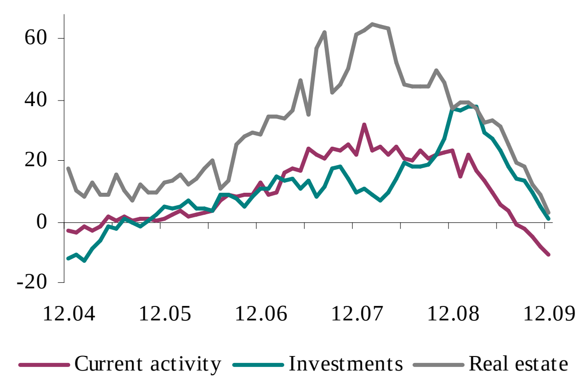
Entity-related structure of enterprise loans (in PLN billion; nominal value)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Total, including:	121.2	138.3	171.7	222.6	212.7	-9.8	-4.4
- current activity	66.1	74.4	90.6	111.5	99.7	-11.8	-10.5
- investment loans	38.6	42.7	46.8	64.1	64.7	0.6	0.9
- real estate financing	16.6	21.3	34.3	47.0	48.3	1.3	2.8

Loans for corporate sector (in PLN billion)



Annual growth rates (%)



Adverse changes occurring in the macroeconomic environment on the one hand resulted in banks tightening their lending policies, and on the other, reducing demand for loans by some businesses. Consequently, the value of loans granted to the enterprise sector decreased by 4.4%[17] (from PLN 222.6 billion at the end of 2008 to PLN 212.7 billion at the end of 2009). The reduction of the financing level would be higher if not for the exchange of some liabilities resulting from foreign exchange derivative transactions to loans.

The greatest decrease occurred in the area of loans for daily operations (by 10.5%), while in the case of investment loans and loans for real estate financing, a marginal increase was reported (by 0.9% and 2.8%, respectively). However, it should be noted that retaining the positive dynamics of investment loans and loans for real estate financing was probably related to releasing subsequent tranches as part of loans granted in previous periods.

The tightening of the lending policy for enterprises was carried out until the third quarter of the previous year and included all areas, with most banks deciding to raise margins and the level of credit security. Moreover, some banks reduced the maximum credit limits. According to banks, the most important reason for tightening lending policies was the negative outlook on economic prospects. In addition, many banks indicated that the declined quality of the loan portfolio was the reason for the tightening.

In the fourth quarter of the previous year, due to the improved prospects of economic growth, most banks did not change the lending criteria, and the criteria for granting loans to small and medium-sized enterprises, as well as short-term loans for large companies were slightly relaxed. However, some banks claim that the development prospects remain unfavourable and require further tightening of the lending criteria and conditions.

In the first quarter of 2010, banks expect a slight relaxation of criteria for granting short-term loans, and on the other hand, a slight tightening in the case of long-term loans.

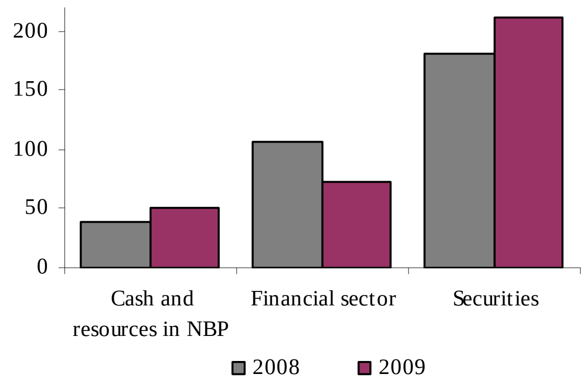
However, the low dynamics of enterprise lending was caused not only by the tightened lending policies of banks, **but also by the decreased demand for loans** from companies, which, in view of the decline in demand (domestic and foreign), were limiting production and verifying investment plans.

According to the economic climate analysis carried out by the NBP, in the course of the year the companies were showing a gradual increase in optimism as to the prospects for development. Low demand remained the main obstacle to the development (however, this barrier was being gradually lowered), followed by the fluctuation of exchange rates and increased competition. Despite the growing optimism regarding forecasts for demand, orders

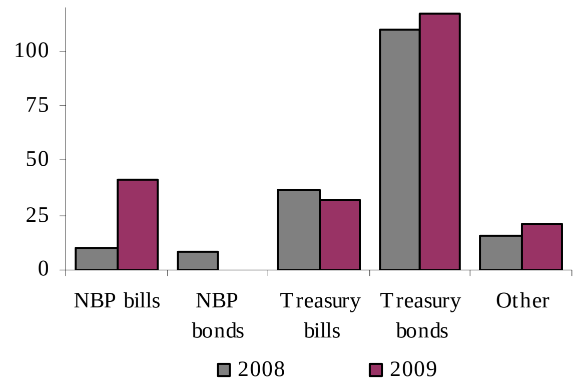
[17]In commercial banks they decreased by 5.1% (increased by 29.4% in 2008), in branches of credit institutions by 6.1% (increase by 40.3% in 2008), and in cooperative banks they increased by 19.1% (22.9%).

and production, most companies are still planning to limit employment, reduce the dynamics of remuneration increase and refrain from making investments.
It seems that the strong decline in credit dynamics observed during the previous year (including the decline in loans for daily operations) may be, in some part, a result of a gradual upturn. In the face of difficulties in obtaining loans, some companies decided to reduce the level of bank financing and increase the share of own resources. This is proved by the studies carried out by the NBP, which show that in the first quarter of 2010, most companies are going to reduce the level of bank financing.

Cash, NBP, financial sector, securities (in PLN billion)

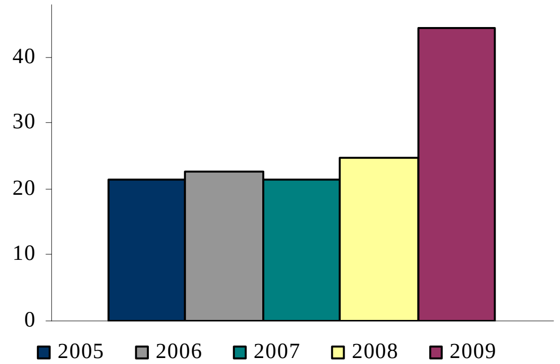


Security portfolio structure (in PLN billion)

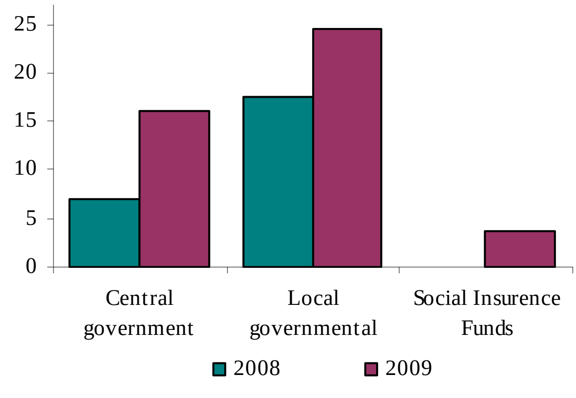


Last year, there were significant **shifts in the structure of most liquid assets**. On the one hand, the decrease in mutual trust between financial institutions, which constituted the "aftermath" of the crisis translated into a decrease in receivables from the financial sector by as much as 32.0% (from PLN 107.2 billion at the end of 2008 to PLN 72.9 billion at the end of 2009). Changes introduced by the PSFA resolution no 382/2008 on detailed rules and conditions for considering exposure when determining the observance of the exposure concentration limit and the limit of large exposures (...). This draws attention to the strong decline in receivables from non-residents (from PLN 44.3 billion to PLN 23.1 billion), which indirectly indicates that there can be no question of financing foreign parent companies by Polish banks. On the other hand, banks increased the level of funds deposited in cash departments and the National Bank of Poland by 27.9% (from PLN 39.4 billion to PLN 50.4 billion). At the same time, despite the early redemption of the NBP bonds in January last year (maturing in 2012 and related to the reduction of the minimum reserve ratio in 1999) banks increased the security portfolio by 16.8% (from PLN 180.9 billion at the end of last year to PLN 211.4 billion). The increase resulted mainly from the increased portfolio of the NBP money bills, and to a lesser extent, treasury bonds, which constituted a safe "liquidity buffer" to ensure "income without risk." Despite a substantial increase in the status of the security portfolio, their share in assets (19.9%) remained at a relatively low level compared to the period before the credit boom. It is also worth noting that despite the mutual shifts, the total share of funds accumulated in cash departments, the NBP, and receivables from the financial sector and the security portfolio remained at the level existing at the end of 2008 and amounted to 31.5%.

Receivables from the budget sector (in PLN billion)



Debt structure of the budget sector (in PLN billion)

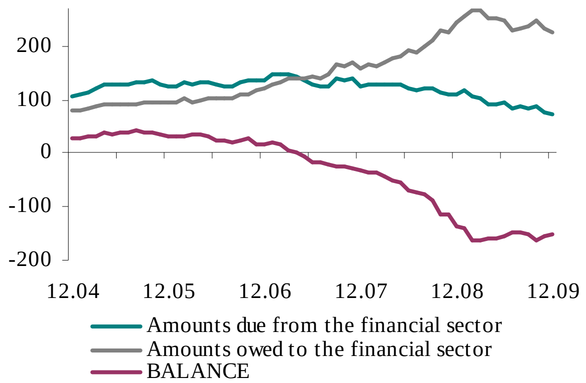


In 2009, there was also a rapid increase of debt in the sector of government and self-government institutions. Receivables of banks on account of this increased by as much as 80.7% (from PLN 24.6 billion at the end of 2008 to PLN 44.5 billion at the end of 2009). The strong growth of debt in the budget sector was a result of lowering the dynamics of own income which was a consequence of the decline in economic activity, and the simultaneous increase of expenditure connected with, among other things, co-financing projects with the use of EU funds. Consequently, the increase in receivables from government institutions amounted to 133.1% (from PLN 6.9 billion to PLN 16.1 billion) and receivables from self-government institutions were 39.8% (from PLN 17.5 billion to PLN 24.5 billion). Adopting an insufficient subsidy for the Social Insurance Fund in the Budget Act had also a significant impact. As a result, the Fund was forced to take a loan in the banking sector (debt increase from PLN 0.0 billion to PLN 3.8 billion) and borrow from the state budget.

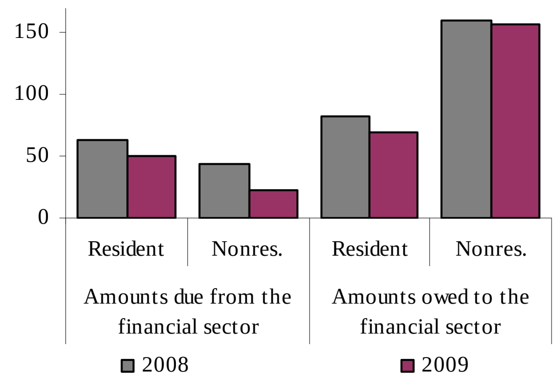
Sources of financing business activity

While in the previous years the development of business activity was financed mainly through the accumulation of commitments toward the financial sector and deposits of non-financial sector entities, in 2009 the main sources of growth were the strong growth of the deposit base and capitals.

Liabilities to the financial sector (in PLN billion)



Change of liability status (in PLN billion)



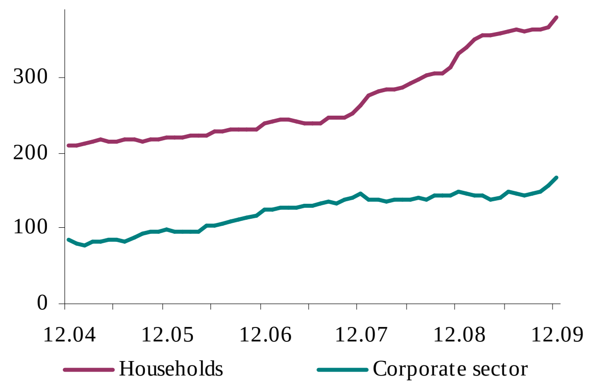
Liabilities to the financial sector decreased by 6.9% (from PLN 242.2 billion at the end of 2008 to PLN 225.4 billion at the end of 2009). Considerable decrease in liabilities to residents (by 16.6%) catches attention, while liabilities to non-residents fell marginally and it was actually caused by the minimal strengthening of the zloty (by 2.0%). In conjunction with the aforementioned strong decrease in liabilities to the financial sector, this may indirectly prove that the mutual distrust between the entities of the financial sector persists. At the same time the data indicates that despite the fears there are no signs of limiting funding from foreign investors. The greater decline of receivables than liabilities caused an increase in negative balance in the settlements of banks with this sector (from PLN 135.1 billion at the end of 2008 to PLN 152.5 billion at the end of 2009).

The increase of negative balance in settlements of banks with the financial sector, which has been observed during recent years, derived from the rapid development of small and medium-sized banks and branches of credit institutions. Since the deposit base is poorly developed, they utilized funds from the financial market, or used the support of foreign parent companies. Also some large banks, despite fairly well-developed deposit bases, made use of funds from the financial market in order to extend lending and increase their market share. The consequence of this phenomenon was the deteriorated structure of financing sources and increased sensitivity of the banking sector to the situation existing on national and global financial markets. However it should be noted, that a large proportion of non-resident funds is derived from parent institutions (it is often 50% -100%) and is of a long-term nature. Thus, the risk is limited (most of the parent companies declare that they would support liquidity and provide funds for the development of Polish subsidiaries). However, given the experiences of the crisis, banks should continue their efforts to obtain stable and diversified sources of funding.

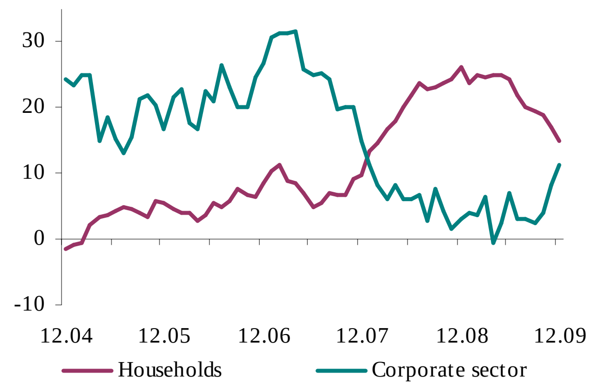
Entity-related structure of non-financial sector deposits (in PLN billion; nominal value)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Total, including:	329.1	375.6	419.3	494.1	560.0	66.0	13.4
- households	219.9	238.8	262.4	330.8	379.7	48.9	14.8
- enterprises	99.2	125.9	144.8	149.1	166.0	16.9	11.4
- non-profit institutions	10.0	10.9	12.1	14.2	14.3	0.2	1.1

Non-financial sector deposits (in PLN billion)



Annual growth rate of non-financial sector deposits (%)

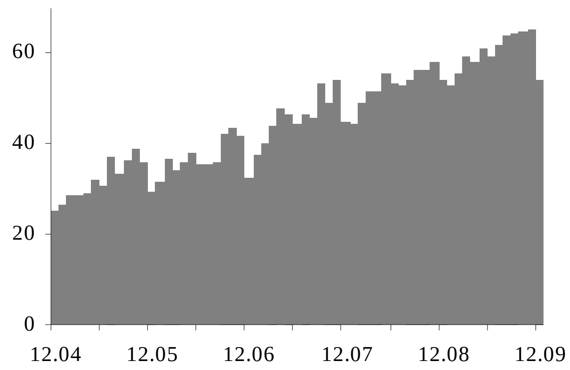


Deposits of the non-financial sector increased by 13.4% from PLN 494.1 billion at the end of 2008 to PLN 560.0 billion at the end of 2009 r.[18] The increase of household deposits was the main determinant of growth.

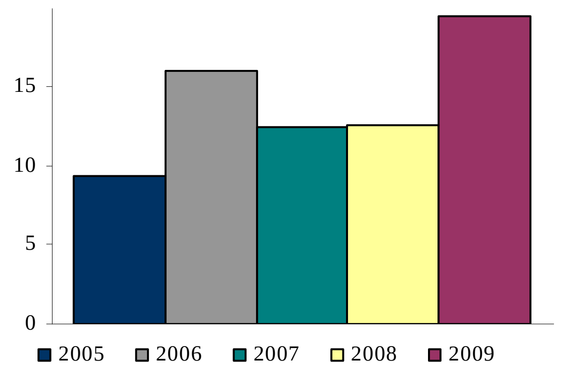
- **household deposits increased by 14.8%** (from PLN 330.8 billion to PLN 379.7 billion). This growth resulted from making the deposit offers of banks more attractive ("deposit war"), as well as the increased declines in the stock market during the first two months of the previous year, as a consequence of which some funds were continued to be withdrawn from investment funds and deposited also in the banking system. The growth determinants could be also found in the decision of some households to increase savings in case their financial situation deteriorates following the expansion of the global crisis (increasing savings at the expense of current consumption and investments in tangible assets or risky assets.) However, with the end of the year, there was a distinct weakening of the deposit growth rate. In this case, determinants opposite to these mentioned before occurred, i.e. clear decrease in the attractiveness of bank deposits combined with a strong rebound at the share market, gradual deterioration in the labour market (lower and lower dynamics of remuneration increase and a growing unemployment rate), or a gradual increase in expenditure of some households associated with better prospects of their own financial situation. Consequently, the primary growth in deposits occurred in January and February last year (by a total of nearly PLN 20 billion). A strong increase was also reported in December (over PLN 13 billion), which should be attributed, inter alia, to the payment of awards and bonuses, which in the previous year were paid in November;
- **deposits in the enterprise sector increased by 11.4%** (from PLN 149.1 billion to PLN 166.0 billion). Contrary to household deposits, the growth dynamics of enterprise deposits was very low at the beginning of the year (until October, the level of enterprise deposits was lower than at the end of 2008). This resulted from the declining financial situation of many companies and the tightening of lending policies by banks, which caused companies to make a greater use of their own resources in order to finance current operations and investment. In the fourth quarter of the previous year, the growth rate of enterprise deposits clearly accelerated (the value of deposits rose by nearly PLN 20 billion), which resulted from a gradual economic recovery and, consequently, an increase of liquid funds held by businesses. As a result, a significant per annum increase in deposits of this sector was reported.

[18]By 13.3% in commercial banks, 25.5% in branches of credit institutions and by 10.4% in cooperative banks.

Liabilities to the budget sector (in PLN billion)



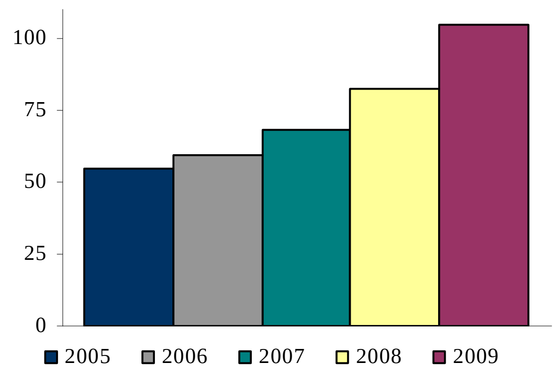
Issue of own debt securities (in PLN billion)



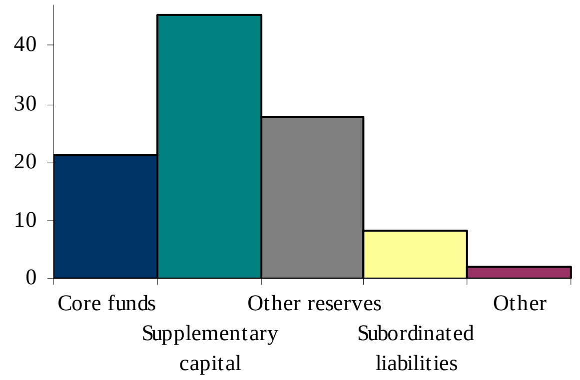
For most of the year, the status of funds deposited in bank accounts by entities of the government and self-government institution sector was significantly higher than at the end of 2008. However, due to large withdrawals made in December last year (over PLN 10 billion) the per annum increase in deposits of this sector was only 1.5% (from PLN 53.5 billion at the end of 2008 to PLN 54.3 billion at the end of 2009). This should be combined with the accumulation of some expenditure and a decrease in the level of deposits, which is characteristic of this month.

In 2009, there was a strong increase (55.6%) of liabilities subject to the issue of own securities, resulting from a very large issue of these securities carried out in the last quarter of the previous year by BGK (it was connected with issuing bonds to finance the construction of road infrastructure worth about PLN 7 billion, by Krajowy Fundusz Drogowy (National Road Fund), located in BGK). As a result, the total value of banks' obligations in this respect increased to PLN 19.4 billion (from PLN 12.4 billion at the end of 2008). However, these funds were still a marginal source of financing operations of banks (the item represented 1.9% of the balance sheet total of the sector). Only 23 banks chose for this type of funding, and it was significant only in case of two mortgage banks (about half of the balance sheet total) and the above-mentioned BGK (a share of several percent in the balance sheet total).
In this context it should be added that the lack of long-term financing in PLN is a problem for the sector (there are instruments such as mortgage bonds, but their market is shallow.)

Equity and subordinated liabilities (in PLN billion)



Equity structure at the end of 2009 (PLN billion)



Equity (funds) and subordinated liabilities of the banking sector **increased by as much as 27.4%** from PLN 82.6 billion at the end of 2008 to PLN 105.2 billion at the end of 2009.[19] The increase in funds resulted mainly from increasing common equity[20] (by PLN 5.3 billion), the supplementary capital[21] (by PLN 7.2 billion) and

[19]By 28.0% in commercial banks (from PLN 77.4 billion to PLN 99.0 billion), 18.8% in cooperative banks (from PLN 5.2 billion to PLN 6.2 billion).
[20]A share fund in cooperative banks.
[21]A reserve fund in cooperative banks.

other reserve capitals (by PLN 8.6 billion). The impact of other items was definitely less important (subordinated liabilities increased by PLN 1.2 billion, the general risk fund and the revaluation fund increased by about PLN 0.9 billion).

Such a strong increase in funds was influenced by three events:

- following the activities of PSFA, the NBP and the management boards of banks, it was possible to convince shareholders that it would be appropriate to retain almost the entire profit for 2008 in banks. ;
- The Treasury recapitalized BGK;
- at the end of the previous year, there was a successful mega issue of shares by PKO BP (the bank acquired over PLN 5 billion)

As a result of these activities, a strong growth of the capital base of the Polish banking sector occurred, which on the one hand ensures its stability and ability to absorb potential losses, and on the other, creates a secure base for a safe extension of lending.

In the near future, the distribution of profits for 2009 will have a significant impact on equity growth, as well as the substantial issue of shares carried out by Bank Millennium and planned by BRE Bank.

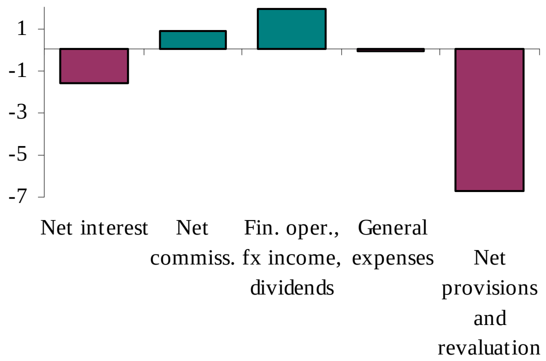
III. FINANCIAL RESULT AND OPERATIONAL EFFICIENCY

The weakening of economy had a strong negative impact on the banking sector financial performance in 2009.

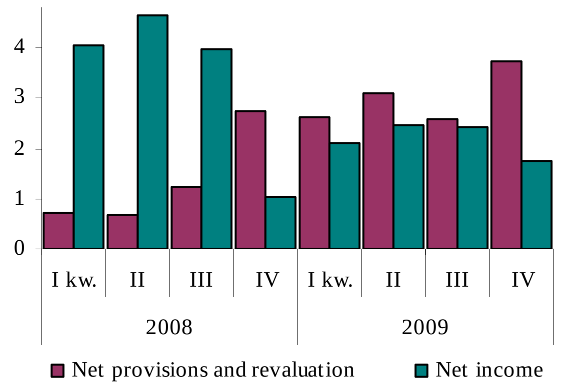
Selected items from the profit and loss account (in PLN billion)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Net interest income	18 542	20 702	24 339	30 089	28 516	-1 573	-5.2
income	34 130	35 006	43 231	60 199	57 621	-2 578	-4.3
costs	15 588	14 304	18 892	30 110	29 105	-1 006	-3.3
Commission income	7 537	9 142	10 998	11 512	12 368	856	7.4
Income from shares and other securities	802	1 107	967	1 505	1 735	230	15.3
Gains / losses on financial operations	880	1 171	1 448	-757	3 865	4 622	-610,5
Foreign exchange result	3 858	3 010	3 665	5 962	3 032	-2 929	-49.1
Income on banking operations	31 619	35 131	41 416	48 311	49 517	1 206	2.5
Other income and operating expenses	627	618	1 063	1 011	676	-335	-33.1
Administrative costs of a bank	17 549	18 997	21 772	24 850	24 943	93	0.4
remunerations	8 096	8 825	10 067	11 461	11 350	-110	-1.0
Depreciation	2 329	2 184	2 290	2 339	2 533	194	8.3
Net provisions and revaluation	1 581	1 667	1 713	5 322	12 004	6 681	125.5
write-offs	11 063	10 726	11 679	17 084	33 248	16 164	94.6
solutions	9 482	9 059	9 966	11 762	21 245	9 483	80.6
Gross profit	10 934	13 030	16 700	16 787	10 715	-6 073	-36.2
Net income	9 110	10 697	13 642	13 658	8 708	-4 951	-36.2

Changes in earnings - 2009/2008 (PLN billion)



Quarterly reserve balance and net result of the sector (in PLN billion)



According to preliminary data **the net income** of the banking sector in 2009 was PLN 8,7 billion, which means **a decline by 36.2%** (PLN 5,0 billion) in comparison to 2008 (the net income in individual quarters of 2009 was: PLN 2.1 billion; PLN 2.4 billion, PLN 2.4 billion and PLN 1.7 billion).
The poor performance of banks was due to a very sharp increase in write-offs resulting from the declined financial situation of some borrowers, as well as the declined interest income (to a little extent, it was also caused by a slight increase in operational costs). Other areas of activity had a positive impact on the performance of banks.

Out of 643 banks and branches of credit institutions engaged in a business activity, only 110 of them reported improved results compared to 2008 (mostly co-operative banks), and the performance of others has declined (the result was lower by more than half in 71 banks).

Despite the strong deterioration of performance, only **16 banks recorded a net** loss (8 commercial banks and 8 branches of credit institutions). Moreover, some losses by branches of credit institutions and two commercial banks can be largely associated with their early stage of development, and therefore they were bearing high operational costs that were not yet fully covered by the generated revenue. On the other hand, the total loss of these 16 institutions was as much as PLN 1.7 billion, which should be considered a very high amount considering the fact that these entities concentrated only 7.9% of the sector assets (the total profit of banks having a positive financial result amounted to PLN 10.4 billion). It should also be noted that there was a large concentration of losses (in 6 institutions, the loss was from more than PLN 100 million to over PLN 400 million).

The income on banking operations increased 2.5% (from PLN 48.3 billion in 2008 to PLN 49.5 billion in 2009).

The low growth dynamics of income on banking operations was decided by **the interest income decreasing by 5.2%** (from PLN 30.1 billion to PLN 28.5 billion).
The decline in the interest income resulted from the lowered interest income realized on operations with the non-financial sector. On the one hand it was **the consequence of deposits growing faster than loans, and the "deposit war"**, which caused a strong decrease in the interest range of loans and deposits in terms of OPS (the average range decreased from 4.4% in 2008 to 3.4% in 2009). However on the other hand, this was also due to **the low margins on loans granted during the credit boom (especially home loans) and the increase in non-performing receivables**, which were not generating income. As a result, the interest income received from the non-financial sector fell by 0.7% (from PLN 41.4 billion to PLN 41.0 billion), while the interest expenses paid to the non-financial sector increased by 12.3% (from PLN 16.1 billion to PLN 18.1 billion). Consequently, the income on operations with this sector decreased by 9.4% (from PLN 25.2 billion to PLN 22.9 billion). The negative trends in the interest income were strengthened by the increase in debt to the financial sector observed during last periods, which, in combination with a large decline in receivables from this sector, led to a negative growth of income realized on operations with this sector (from PLN minus 3.0 billion to PLN minus 3.7 billion). While banks recorded an increase in the interest income from securities held (from PLN 8.6 billion to PLN 9.9 billion) and the decrease in negative income on operations with the budget sector (from PLN minus 0.8 billion to PLN minus 0.6 billion) but it did not compensate for the deterioration of the first two items. It can therefore be concluded, that one of the main reasons for the decline in the interest income was **the expansionary strategy of banks during the earlier periods, consisting in a very large increase of lending which was not supported with an appropriate growth of stable sources of financing** adequate in terms of term and currency structure and **operating on very low margins in order to obtain the greatest possible share in the market**.
However, we need to mention a distinct improvement in the interest income in the second half of the previous year, which should be attributed to the "deposit war" coming to an end, and to the increase in credit margins (the interest income in subsequent quarters was PLN 6.9 billion, PLN 6.6 billion, PLN 7.4 billion, PLN 7.7 billion, respectively).

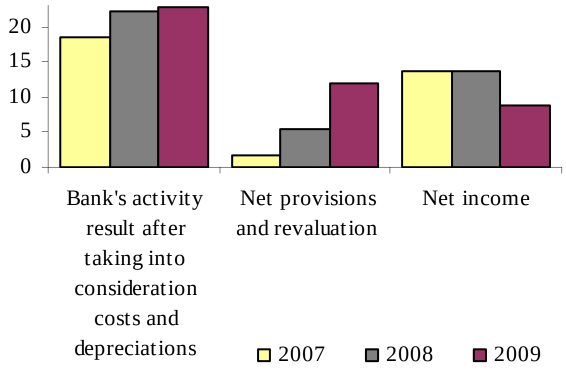
Income on commission increased by 7.4% (from PLN 11.5 billion to PLN 12.4 billion). The increase was caused by raising commissions and charges for most banking services last year. The gradual improvement of the economic situation on the capital market also had a positive impact on its formation (the improvement influenced the growth of income from the sale of units in investment funds, charges for asset management and from acting as an intermediary in the sales of financial instruments), as well as the increase in household loans.

The remaining income from banking operations (income from shares, financial operations and foreign exchange items) strongly increased by 28.7% (from PLN 6.7 billion to PLN 8.6 billion). This should be linked to, inter alia, the increase in revenues from dividends and the successful solving of the issue of foreign exchange derivative transactions, which had a strong negative impact on the performance in 2008.

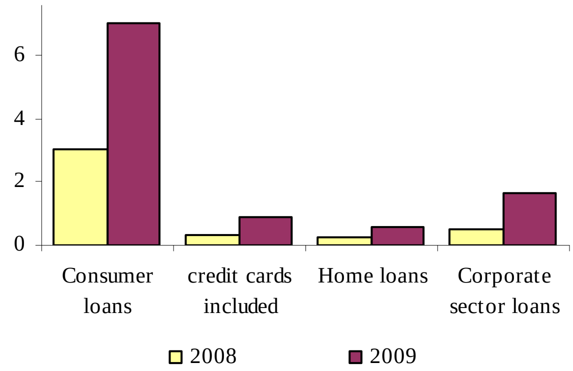
Banks were trying to eliminate the unfavourable changes in the performance of the banking business by seeking **cost savings**. As a result, general expenses (PLN 24.9 billion) **increased only by 0.4%**. 3.4% growth of the other costs item had an effect towards cost increase (from PLN 11.0 billion to PLN 11.4 billion). The other costs include the costs of building maintenance and renting as well as other material costs, which should be linked to, inter alia, a slight extension of the sales network. On the other hand, although during a significant part of the year the level of employment remained higher than in 2008 (it was lower than in the corresponding period of 2008 only at the end of September 2009), the personnel costs, including social security costs and other benefits for employees decreased by 2.0% (from PLN 13.8 billion to PLN 13.5 billion).
As a consequence of the high cost discipline and the gradual improvement of performance, the general expenses ate up 50.4% of the income from banking business realized in 2009, as compared to 51.4% in 2008.

Depreciation costs (PLN 2.5 billion) increased by 8.3% but still accounted for a small part of the income from banking business (5.1%).

Selected items of the income statement (PLN billion)



Selected balances of write-offs for loans (in PLN billion)

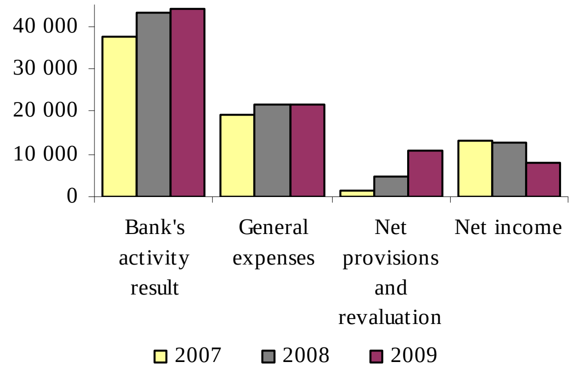


The main reason for a strong decline in financial results was more than a twofold increase in a negative balance of reserves/write-offs on account of impairment from PLN 5.3 billion in 2008 to PLN 12.0 billion in 2009 (net write-offs in subsequent quarters amounted to: PLN 2.6 billion, PLN 3.1 billion, PLN 2.6 billion and PLN 3.7 billion, respectively). As a result, reserves / write-offs ate up as much as 24.5% from banking business, while in 2008 it was 11.0%, and in 2007 it was only 4.1%. On the one hand, the scale of write-offs reflects the impact of the global crisis on the situation of some borrowers, and on the other hand, it indicates **weaknesses in risk management** enhanced by the excessive market expansion in the previous periods (including competing in terms of risk acceptance).

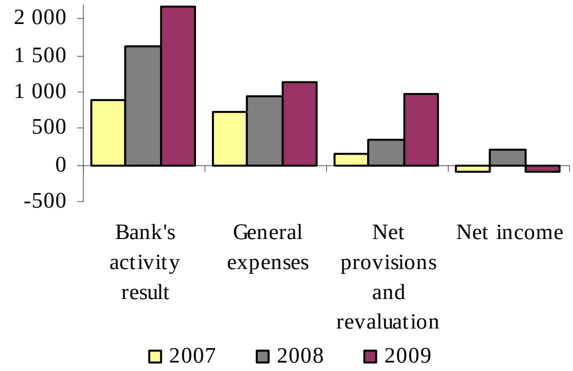
Such a large increase in negative balance of write-offs was caused primarily by a very large increase in net write-offs related to loans granted to retail clients (from PLN 3.3 billion to PLN 7.6 billion). **Situation regarding consumer loans was the worst** (the growth of the negative balance from PLN 3.0 billion to PLN 7.1 billion, including an increase regarding credit cards, from PLN 0.3 billion to PLN 0.9 billion). This resulted to a large extent from the aggressive strategy of several small and medium-sized banks and branches of credit institutions, which in the recent periods were carrying out the lending policy with the aim to obtain the greatest market share (a group of these banks accounted for almost 45% of total net write-offs made in the entire sector while their share in the assets of the sector was less than 20%). However, a significant increase in write-offs on account of house loans is also noticeable (from PLN 0.2 billion to PLN 0.6 billion).

The impact of deteriorated financial condition of some corporate clients was definitely smaller but also significant. The disproportion of the negative balance of write-offs between the corporate sector and retail sector draws attention here. While the growth of non-performing loans in the corporate sector (PLN 10.7 billion) was higher than in case of households (PLN 9.5 billion), the negative balance of reserves created for corporate clients was much lower. In the absence of a proper conservative approach in estimating future cash flows from these exposures, they may be the source of additional write-offs.

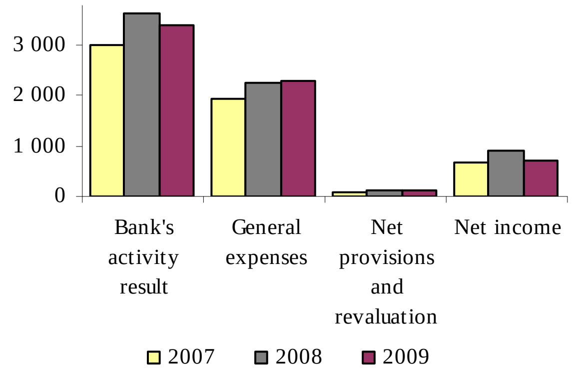
Income structure (in PLN million) - COMMERCIAL BANKS



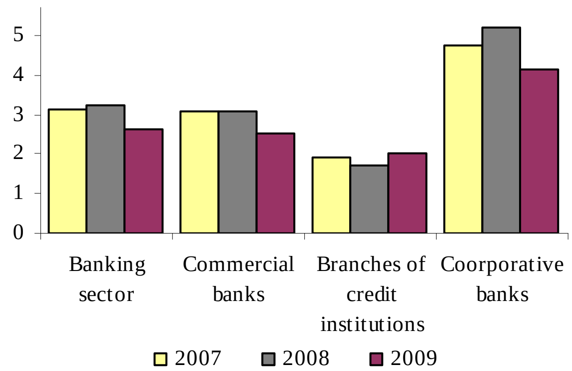
Income structure (in PLN million) - BRANCHES OF CR. INST.



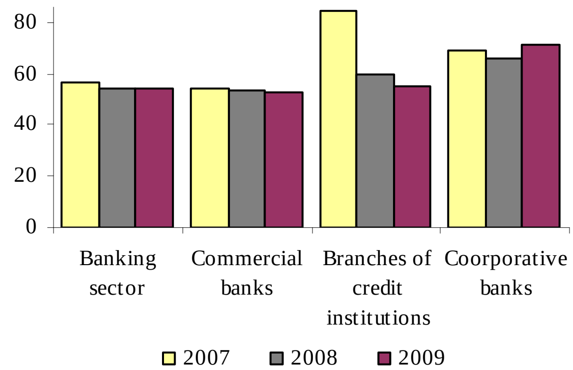
Income structure (in PLN million) - COOPERATIVE BANKS



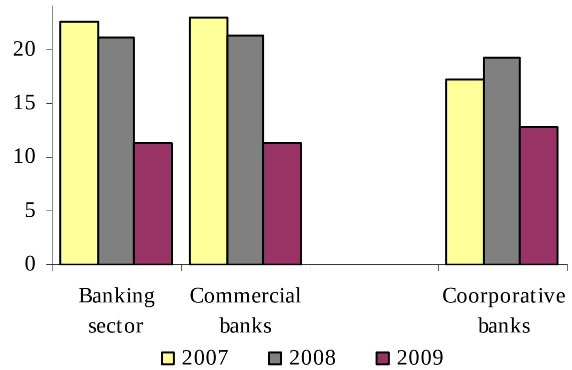
NIM[22] – interest margin (%)



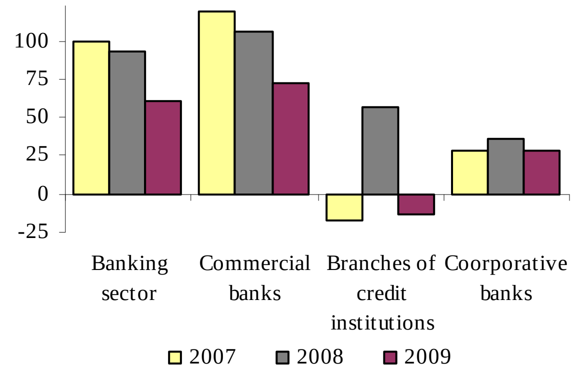
C/I[23] – operational costs ratio (%)



ROE[24] – rate of return on equity (%)



Gross profit / 1 employee (in PLN thousand)



[22]Relation of interest income to average assets.
[23]Relation of operational costs (activities and depreciation) to the income from banking business corrected by the result of the remaining revenues and operational costs.
[24]Relation of net financial income to average basic capital.

Given the different groups of banks:

- net income of commercial banks decreased by 35.5% (from PLN 554.5 million to PLN 8 099 million). This was caused by the more than twofold increase of the negative balance of reserves / write-offs (from PLN 4 854 million to 10 922 million), while the result from banking business increased (by 2.1%), the general costs fell (by 0.7%). It should be noted, however, that the picture of this group is not homogeneous. Strong deterioration of financial results of several institutions which in previous periods were characterized by very aggressive strategies, had a negative impact on the performance of the entire group. These strategies aimed at increasing market share as fast as possible, particularly the segment of household loans. In 2009, the risk taken by these institutions materialised and their financial results "collapsed" (net profits fell by more than half, or losses occurred). On the other hand, banks with more conservative management models, which during the previous periods had been implementing the strategies of stable, sustainable development, managed to handle the crisis phenomena quite well. As it turned out, this model of business worked well "at the age of the crisis" and has generated positive results so far (some entities reported an improvement in financial results as compared to 2008);
- branches of credit institutions recorded a net loss (PLN 90 million), compared to a profit (PLN 203 million) recorded in the previous year. This happened despite the increase in the income from banking business (33.6%) as a result of the increased scale of operations (on the other hand, it led to an increase in general costs by 21.2%). Such a large deterioration in performance was the result of aggressive development strategies of some branches, as a result of which they incurred very high costs of write-offs / reserves on account of bad loans (increase from PLN 349 million to PLN 973 million). It should however be borne in mind that, similar to the entire sector, the picture of this group is not uniform and some of the branches reach positive or very good results;
- the net financial result of the cooperative banking sector decreased by 22.4% (from PLN 900 million to PLN 698 million). Unlike other groups, the decrease in performance was not caused by increased write-offs / reserves (the negative balance decreased from PLN 120 million to PLN 109 million), but it was the result of the decline in the performance of banking business (6.6%) and a slight increase in general costs (by 2.4%). The decline in interest income (by as much as 35.3%) resulted from the reductions in the NBP interest rates (this influenced, iter alia, a reduction of income from preferential loans which account for nearly 30% of the total loan portfolio of this group of banks and are linked to the interest rates of the NBP) and from the "deposit war", which, while causing the outflow of deposits to commercial banking, forced the increase of deposit rates in order to stop it. In turn, the performance of cooperative banks was stabilized by the more conservative and local nature of activities, and the inflow of EU funds improving the income situation of many rural households which constitute a key customer base.

The accumulation of adverse events translated into a significant worsening of effectiveness measures of the banking sector. In particular, due to the reductions in the NBP interest rates, "deposit war" and the growth of unsupported loans, the interest margin declined (from 3.2% in 2008 to 2.6% in 2009). The decrease in ROE (from 22.1% to 11.3%) was also the consequence of the declined performance of banks. However, when analysing this ratio, it should be noted that the deterioration of this measure was also influenced by a positive phenomena, that is, a large increase in equity (causing a greater denominator). At the same time, strict cost control helped to minimally improve the operating costs ratio (from 54.1% to 54.0%).

To sum up, there was a significant deterioration in the financial performance of the banking sector in 2009, but it did not weaken the stability of this sector.
To a large extent, it was caused by the crisis which is"sweeping" through the global economy. However, the deterioration was caused also by the low quality of management in some banks and branches of credit institutions, and this requires substantial improvement. In particular, a negative impact on the image of the entire sector was exerted by a group of several entities, which in the previous period were characterized by extremely aggressive market strategies, also based on mitigating risk acceptance criteria.

IV. MAIN RISK AREAS

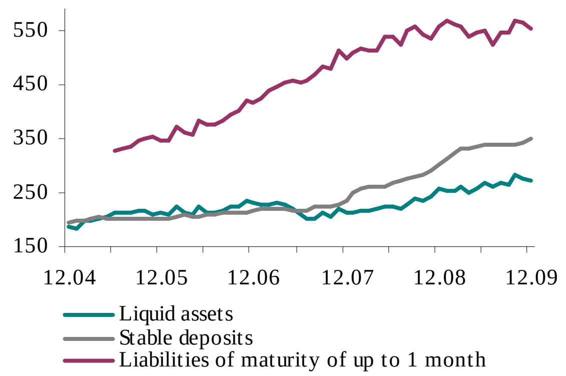
Liquidity risk

The liquidity of the banking sector remains at a satisfactory level. Unadjusted contractual payment dates of assets and liabilities, limited trust and aversion to risk resulting in the weakening of the interbank market functioning remain the main sources of risk.

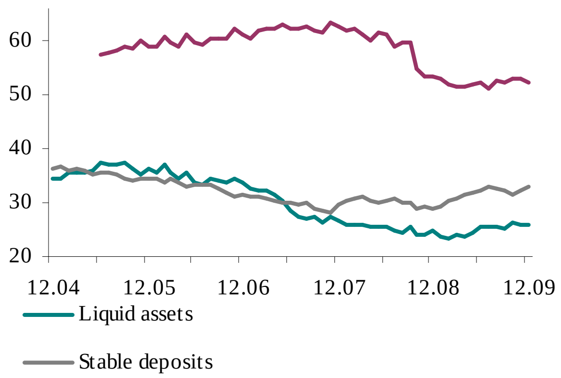
Number of banks and branches of credit institutions violating the Resolution 386/2008 at the end of a month

	01/09	02/09	03/09	04/09	05/09	06/09	07/09	08/09	09/09	10/09	11/09	12/09
Commercial banks	3	2	4	2	2	1	1	3	3	4	2	1
Branches of credit institutions	1	1	1	1	1	1	1	1	1	1	1	0
Cooperative banks	7	5	5	12	9	11	6	9	10	10	6	10
Total share in the sector assets (%)	2.7	0.4	4.7	0.3	0.7	0.3	0.2	0.3	0.4	0.4	0.3	0.3

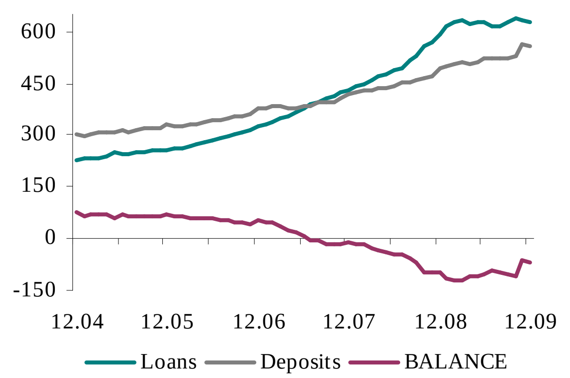
Selected measures of the banking sector liquidity (in PLN billion)



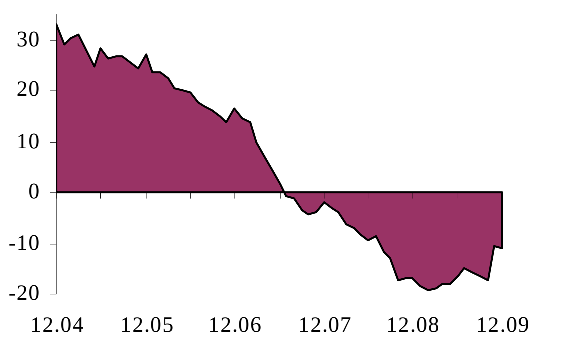
Share in the balance sheet total of the banking sector (%)



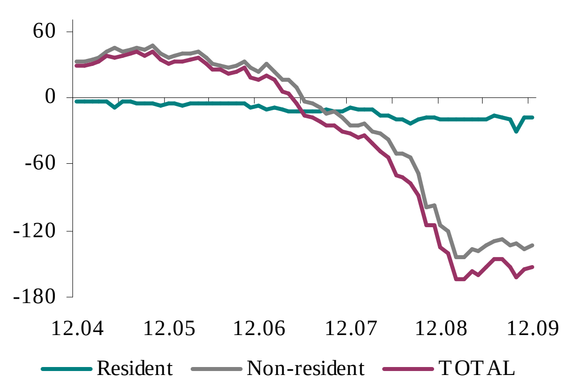
Loans and deposits of the non-financial sector (in PLN billion)



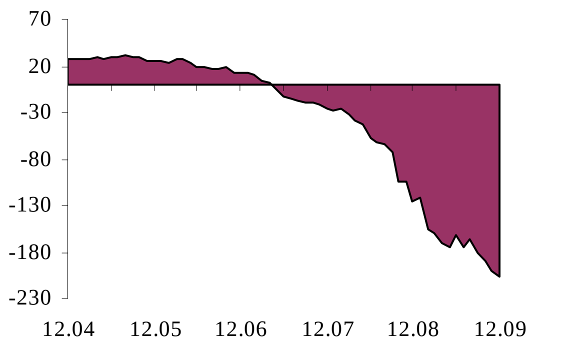
Financial deficit (balance of loans and deposit / loans %)



Balance of receivables and liabilities to the fin. sector (in PLN billion)



Finance deficit (balance of receivables and liabilities / receivables %)



Based on ongoing monitoring, it can be concluded that **the scope of the banks' observance of the PSFA Resolution no 386/2008 regarding the establishment of liquidity standards binding for banks is satisfactory**. Occurring violations are usually incidental (with exceptions) and generally concern small cooperative banks or branches of credit institutions.

Thanks to the strong growth in deposit base coupled with suppressing the growth rate of lending, the following was also observed:

- a significant increase in the balance sheet total of stable deposits (from 29.0% at the end of 2008 to 32.9% at the end of 2009);
- improving the relation of loans to deposits (from 120.1% to 112.1%, resulting in the reduction of the negative finance deficit from 16.7% to 10.8%);
- increase in the share of liquid assets in the balance sheet total (from 24.8% to 25.8%), due to, inter alia, a significant increase in the portfolio of money bills and treasury bonds, which provided liquidity on the one hand, on the other, they are instruments with a much smaller credit risk;
- a slight decrease in the share of liabilities due, to one month in the balance sheet total (from 53.3% to 52.1%).

By contrast, adverse events include:

- sustained decline in trust between financial market participants (despite significant improvements in relation to the climax of the current crisis), which is reflected in the interbank market by, among other things, shortening transaction terms, reducing mutual limits, and thus leads to difficulties in managing liquidity,
- increasing the negative balance in settlements of the banking sector with the financial sector (from PLN 134.7 billion at the end of 2008 to PLN 152.3 billion at the end of 2009. ; in case of residents, the negative balance decreased from PLN 19.0 billion to PLN 18.6 billion, and in case of non-residents it increased from PLN 115.7 billion to PLN 133.7 billion). The increased negative balance was due to the previously described reduction in deposits of Polish banks abroad (exchange into other liquid assets). Moreover, as mentioned before, a large part of non-resident funds (even 50%-100%) is derived from parent companies and is often of a long-term nature. This results in reducing the risk of liquidity, although it makes the situation a subsidiary dependant on the financial situation of the parent company. We should also add that in case of most entities controlled by foreign financial institutions, the parent companies have declared support for the liquidity, and so far these institutions aid the Polish entities if necessary (even though they have their own financial problems.) Therefore, as long as the situation of a parent company does not fundamentally deteriorate, there should be no problems with supporting Polish subsidiaries, especially as failing to provide such assistance would expose these institutions to a reputational risk;
- declined value of the loan portfolio, resulting in the increased risk to the timely repayment of obligations by customers, which may adversely affect current liquidity of individual banks.

To sum up, it may be concluded that **the current situation of the banking sector in the scope of liquidity is satisfactory, and the main sources of risk are**: persisting, **limited level of mutual trust** between the the financial market participants, failing to adjust contractual liquidity dates of assets and liabilities, together with no currency adjustment, significant finance deficit in the scope of operations with the financial sector, **deteriorated quality of the loan portfolio** and **uncertainty regarding the future situation of parent companies**. Therefore, **actions to increase the stability of funding sources and strategy preparation, which are well integrated into external environment, are still desirable**. This is particularly important in view of declarations made by banks regarding the increase in activity.

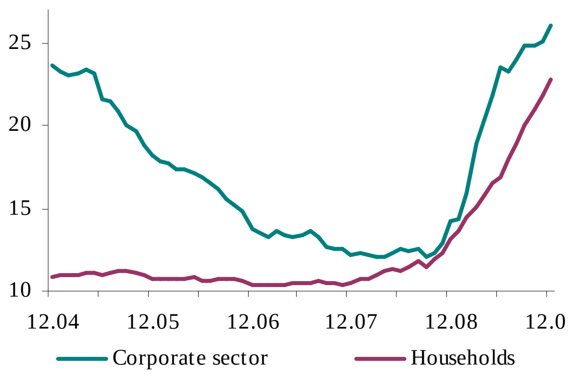
Credit risk

Receivables from the non-financial sector remain the main source of the credit risk - they represent 98.8% of all non-performing receivables, whereas non-performing receivables from the financial sector constitute merely 1.0%, and from the budget sector - 0.2%.

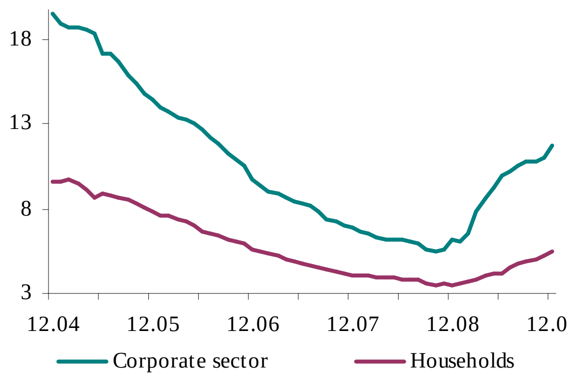
Non-performing receivables from the non-financial sector (in PLN billion, nominal value)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Total non-performing receivables	29.0	24.2	22.7	27.4	48.8	21.4	77.9
- commercial banks	27.8	23.0	21.6	25.8	45.8	20.0	77.3
- branches of credit institutions	0.3	0.4	0.2	0.7	1.8	1.1	157.9
- cooperative banks	0.9	0.9	0.9	0.9	1.2	0.3	34.6

Total non-performing receivables from the non-fin. sect. (in PLN billion)



Total share of receivables of a given group (%)



Non-performing loans from the non-financial sector (in PLN billion)

„Under observation" loans from the non-financial sector (in PLN billion)

Significant deterioration in the macroeconomic situation combined with a sharp increase in lending observed in 2006-2008 and carried out with the excessive relaxation of lending standards, led to the strong increase in non-performing receivables from the non-financial sector. Total non-performing receivables[25] increased by 77.4% from PLN 27.4 billion at the end of 2008 to PLN 48.8 billion at the end of 2009. At the same time their share in total receivables increased from from 4.5% to 7.6%.

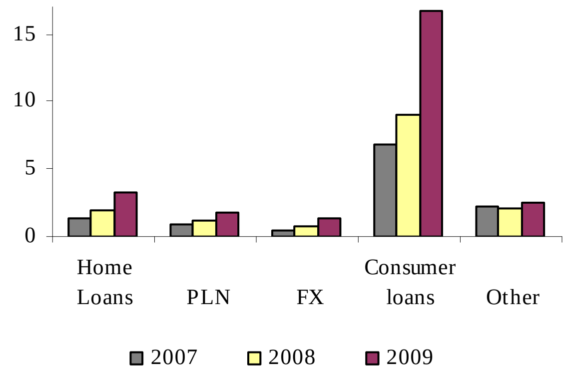
[25]The definition of non-performing receivables is included in the resolution by the Minister of Finance as of 16 December 2008 on the rules for creating reserves on account of risk associated with the banking business. Leaving exceptions aside, non-performing receivables include credit expositions for which the delay in repayment exceeds 3 months (6 months for retail loans) and/or the situation of a borrower indicates that the timely repayment may be at risk. Banks which apply IFRS, identify receivables being at the risk of impairment according to IAS 39, taking into account good practice included in the R Recommendation on the rules of identifying receivables which have lost their value and establishing revaluation write-offs on them. Then, they translate the obtained results into categories, for the reporting purposes, such categories being the closest to the ones defined in the regulation by the Minister of Finance.

What's significant, portfolios which have deteriorated the most were the portfolios of branches of credit institutions (non-performing receivables from the non-financial sector increased by 157.9% and their share in total receivables increased from 2.3% to 5.3%) and commercial banks (increase by 77.3%, increase in the share from 4.8% to 8.0%), while the portfolio quality of cooperative banks remained relatively high (increase by 34.6%, increase in the share from 2.8% to 3.4%.)

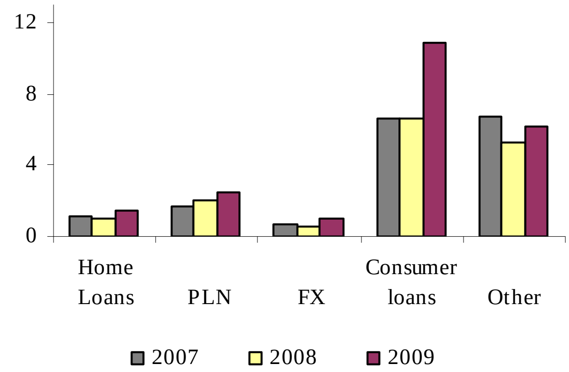
Non-performing loans and their share in portfolio (nominal value; PLN billion; %)

	Value in PLN billion			Change 2009/2008		Share in a given category %		
	2007	2008	2009	in PLN	in %	2007	2008	2009
Total non-performing loans	22.0	26.6	46.8	20.2	76.1	5.1	4.5	7.5
Non-performing household loans	10.4	13.0	22.5	9.5	73.5	4.1	3.5	5.5
- housing	1.4	2.0	3.2	1.3	64.3	1.2	1.0	1.5
PLN	0.9	1.2	1.8	0.6	53.3	1.7	2.0	2.4
foreign currency	0.5	0.8	1.4	0.6	82.0	0.7	0.6	1.0
- consumer	6.7	9.0	16.7	7.7	86.0	6.6	6.6	10.8
overdraft	1.3	1.3	1.8	0.5	36.0	7.4	6.5	8.0
credit cards	0.6	0.9	1.8	1.0	111.5	6.2	6.8	12.1
other consumer	4.9	6.8	13.1	6.3	92.6	6.4	6.6	11.2
- other	2.3	2.0	2.6	0.5	26.8	6.7	5.3	6.1
Non-performing loans from corporate sect.	11.6	13.5	24.3	10.7	79.2	6.7	6.1	11.4
- current operations	7.1	7.2	12.6	5.4	75.4	7.9	6.5	12.7
- investment	2.6	3.6	6.9	3.3	93.6	5.6	5.6	10.7
- real estate	1.8	2.8	4.7	2.0	70.4	5.3	5.9	9.8

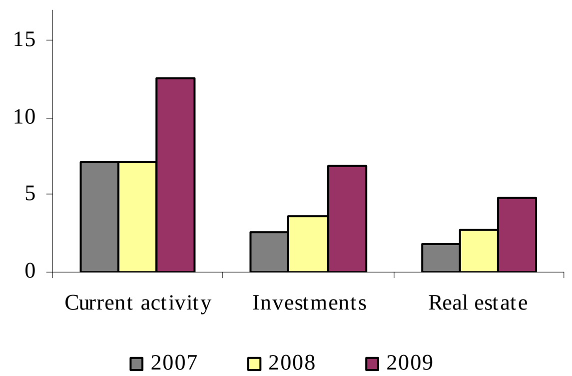
Non-performing household loans (in PLN billion)



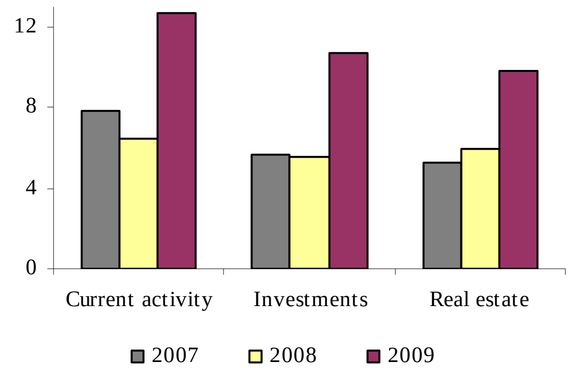
Share of non-performing loans in total loans (%)



Non-performing loans of companies (in PLN billion)



Share of non-performing loans in total loans (%)



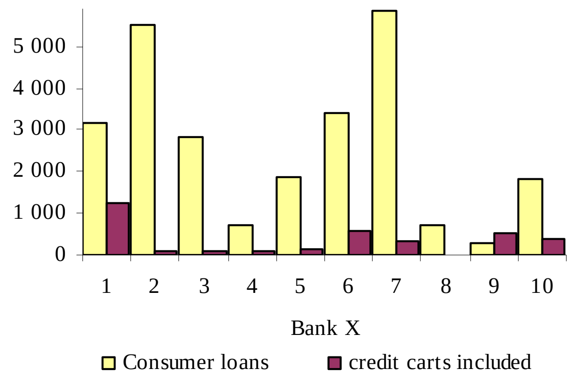
The portfolio of non-performing loans increased by 76.1% (from PLN 26.6 billion at the end of 2008 to PLN 46.8 billion at the end of 2009), and their share in total loans increased from 4.5% to 7.5%.
The value of non-performing loans of the enterprise sector increased by 79.2% (from PLN 13,5 billion to PLN 24.3 billion), **and their share in the portfolio increased from 6.1% to 11.4%**. This should be linked with the deteriorated financial situation of some entities following the difficult external conditions, mistakes made in the development strategy (excessive expansion during a good economic situation), as well as mistakes in a financial management policy (consisting, inter alia, in some entities concluding transactions in foreign exchange derivatives which were improperly selected or did not result from actual needs, but were of a speculative nature and created large losses).

The value of non-performing household loans increased by 73.5% (from PLN 13.0 billion to PLN 22.5 billion), and their **share** in the entire portfolio increased **from 3.5% to 5.5%**:

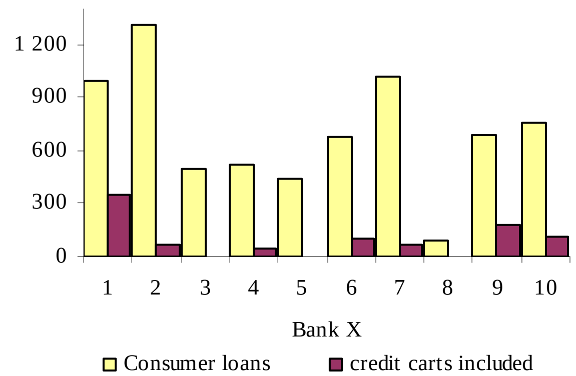
- **the quality of consumer loans decreased the most**. The value of non-performing loans in this group of loans increased by 86.0% (by PLN 7.7 billion), and their **share** in the portfolio **increased from 6.5% to 10.8%**. Further growth of non-performing loans on credit cards and overdraft catches attention, and may indicate that these products are used to settle customers' other obligations (including most likely loans to other banks). It should be noted that in the event of financial problems these loans will probably be the primary source used by households to save the financial liquidity.
  The very strong increase in non-performing loans should be related to the decline in the labour market, overly expansive policy of some banks in earlier periods and the lack of reliable credit investigation and review of credit capacity. This resulted in granting loans to persons who should not receive them (they had already "overborrowed") or granting loans the amount of which exceeded the actual capabilities of given customers. At the same time, due to the low quality of collateral, one must expect that the efficiency of debt recovery in this respect will be limited. There are fears that due to the decline in the labour market, the quality of such loans will further deteriorate in subsequent periods.
  It is worth adding that the consumer loan portfolio is not only generating increasing risk for the banking sector, but is also indicative of the situation in individual households (in case of financial difficulties, loans from this category are impaired in the first place).
- the value of non-performing **home loans** increased by 64.3% (by PLN 1.3 billion), and their **share** in the portfolio **increased from 1.0% to 1.5%** (in case of currency loans - from 0.6% to 1.0%, and loans in PLN - from 2.0% to 2.4%).
  It should be concluded however, that **the relatively high quality of home loans does not reflect the actual scale of risk related to the portfolio of these loans**. First of all, it must be borne in mind that most loans have **a very short history**. Secondly, until the end of February 2009, the portfolio of such loans was characterized by a very high growth dynamics, which "eliminated" the increase of non-performing loans by increasing the value of the entire loan portfolio, so the share of non-performing loans had to be low. Thirdly, a survey shows that **in the second half of 2009 the regular repayment of nearly 12 thousand loans which total value is PLN 2.1 billion was discontinued**. Fourthly, **a strong increase in the average LTV ratio of the banks' credit portfolio raises concern** (loans with LTV exceeding 80% constitute more than half of the loan portfolio), which means that in case of necessary realization of collateral on such a great scale, the claims of some banks will not be satisfied (at the end of 2009, bank portfolios included 21 thousand loans which were more than 30 days in default). Finally, the fact that at the end of 2009 and the beginning of 2010 the lending standards in the area of home loans are being relaxed again (or there are announcements of such relaxation) must be considered unfavourable. Statements issued by banks, claiming that a large proportion of these activities is due to competitive pressure, are worrisome.
  Banks that were granting loans with a very high LTV and a very long credit period, in foreign currencies, while having a very liberal approach towards the credit capacity of a client, that were applying low margins which didn't cover the expected costs of risk, increased cost of financing or the costs of securing credit exposure, are in the greatest danger that the value of their home loan portfolio will deteriorate and they will be exposed to all the resulting negative consequences for their financial performance.

Banks with aggressive development strategies
(changes of selected items in 2007-2009)[26]

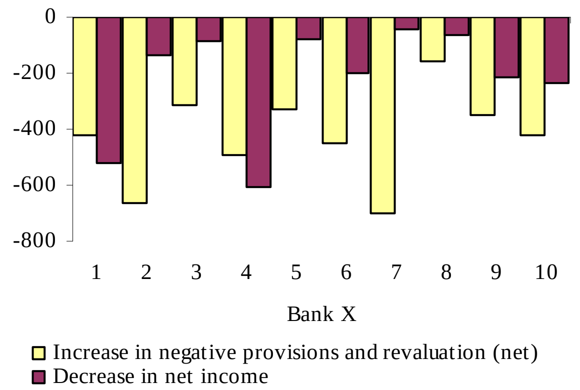
Increase in consumer loans in 2007-2009 (PLN million)



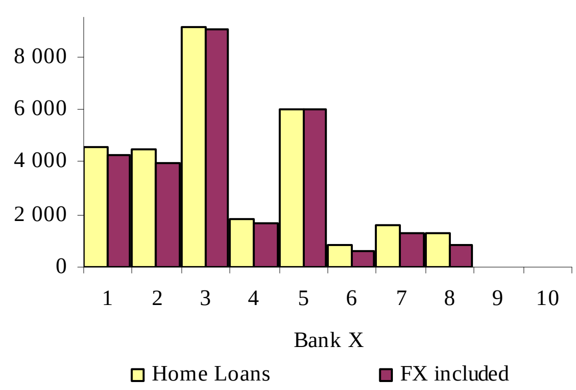
Increase in non-performing consumer loans in 2007-2009 (PLN million)



Change in the net write-offs and net income in 2007-2009 (PLN million)



Increase in house loans in 2007-2009 (PLN million)



As already mentioned, the picture of the banking sector is not homogeneous. The situation of several banks and branches of credit institutions, which in recent years were characterized by aggressive development models in the area of retail banking, had a significant impact on the strong deterioration of the quality of credit portfolio and the sector performance. In 2009, the risk in these banks materialised and the value of credit portfolios sharply deteriorated, which resulted in a rapid growth of write-offs on account of impairment (from the total increase of non-performing consumer loans in the amount of PLN 7.7 billion, this group of banks accounted for as much as PLN 5.4 billion; there are three banks worth mentioning, the ones in which the increase of consumer credit portfolios was about PLN 3-6 billion over the last two years, and the increase of non-performing loans was PLN 1 billion or more). Consequently, the performance of these banks slumped.
Duplicating errors in risk management also in case of other loan portfolios may pose a significant threat to the financial result of these banks (particularly mortgages granted mainly in foreign currencies, the quality of which is now satisfactory).

To sum up, it can be concluded that the quality of credit portfolio of banks strongly deteriorated in 2009, which was caused by both the strong decline of the economy, as well as mistakes in risk management made in the previous periods. Due to the persisting, difficult external conditions, growing unemployment and decreasing remuneration dynamics, there is a fear that the quality of a part of the credit portfolio may decline in the nearest periods, particularly in the area of household loans. On the other hand, as long as the observed process of economic recovery is maintained (or accelerated), one may expect a gradual decrease in pressure on the quality of the credit portfolio, particularly in the area of corporate lending.

[26] Numbers 1, 2, 3, ..., 10 on the x-axis represent selected banks included in a group of banks with aggressive development strategies, ranked according to the amount of the balance sheet total.

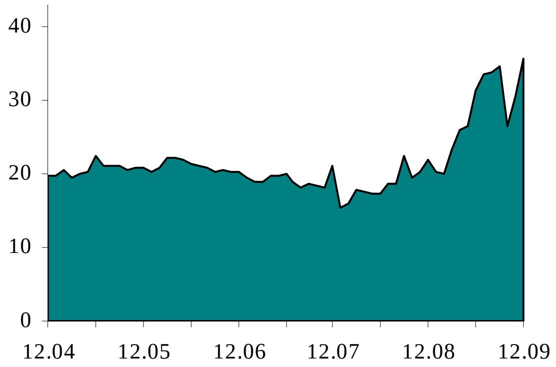
Capital adequacy

On account of the above-mentioned activities by PSFA, the NBP and bank management boards, the capital base of banks and thus the ability to absorb potential losses were strengthened in 2009.

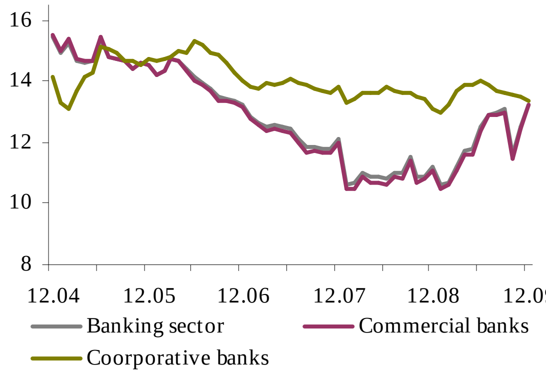
Own funds, total capital requirement and solvency ratio (in PLN billion; %)

	2005	2006	2007	2008	2009	Change 2009/2008	
						in PLN	in %
Banking sector							
Own funds to solvency ratio	46.1	51.6	61.8	77.6	89.7	12.2	15.7
- core funds	45.6	50.3	60.0	74.3	88.4	14.1	18.9
- supplementary funds	3.8	4.3	5.7	8.5	10.4	1.9	21.8
- reductions of core and supplementary funds	3.7	3.4	4.3	5.8	9.4	3.6	62.7
- short-term capital	0.4	0.3	0.3	0.4	0.3	-0.2	-33.6
Total capital requirement	25.3	31.2	40.7	55.5	54.2	-1.4	-2.5
Solvency ratio (%)	14.5	13.2	12.1	11.2	13.3	x	x
Commercial banks							
- own funds	42.9	47.8	57.3	72.4	83.7	11.2	15.5
- total capital requirement	23.6	29.0	38.1	52.4	50.5	-1.9	-3.5
- solvency ratio (%)	14.5	13.2	12.0	11.1	13.2	x	x
Cooperative banks							
- own funds	3.7	3.7	4.5	5.2	6.1	0.9	17.9
- total capital requirement	2.1	2.1	2.6	3.2	3.6	0.5	15.3
- solvency ratio (%)	14.0	14.0	13.8	13.1	13.4	x	x

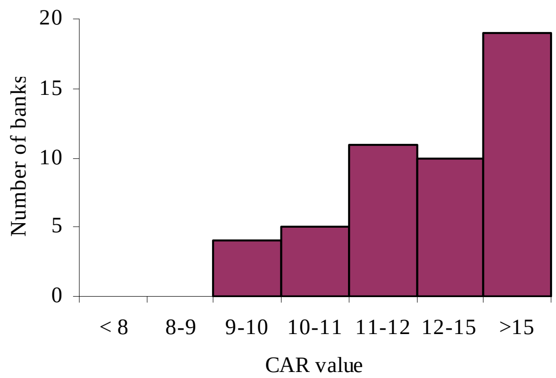
Surplus of own funds over the total requirement (in PLN billion)



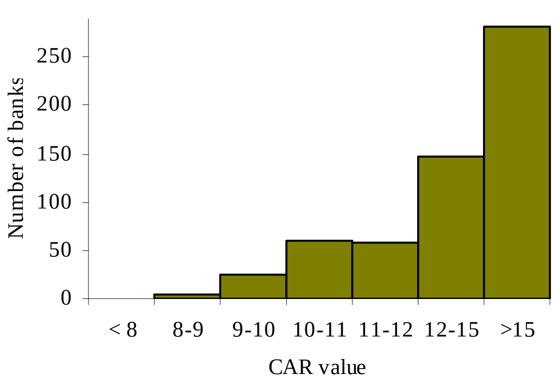
CAR – Solvency ratio (%)



Distribution of commercial banks with regard to CAR



Distribution of cooperative banks with regard to CAR



Own funds of the banking sector increased by 15.7% (from PLN 77.6 billion at the end of 2008 to PLN 89.7 at the end of 2009). The increase in own funds resulted primarily from the increase in core funds, which reached PLN 88.4 billion and were higher by 18.9% than at the end of 2008 (mainly due to retaining almost the entire profit for 2008 in banks, recapitalization of BGK and a very large issue of shares by PKO BP).
All commercial banks met the requirement of minimum own funds at the level of EUR 5 million. In case of the cooperative banking sector, the supervisory action taken and the appreciation of the zloty observed from the mid-February last year caused that at the end of the year only one bank did not meet the required minimum of EUR 1 million (in March last year the number was as much as 93), while the solvency ratio of this bank was more than 8%.

Due to the low dynamics of lending and changes in the structure of assets (such as reducing exposure to the financial sector while increasing the NBP money bills and treasury bonds), the total capital requirement decreased by 2.5% (from PLN 55.5 billion to PLN 54.2 billion). The requirement on account of credit risk constituted 87.2% of the total requirement, the requirement on account of operational risk was 11.0%, and the other requirements accounted for 1.8% only.

The funds held by banks covered the current risk associated with their activity (at the end of last year the surplus of own funds over the total capital requirement amounted to PLN 35.6 billion). At the same time the decrease in the total capital requirement coupled with a strong growth in own funds has caused **a significant increase in the solvency ratio of the banking sector** from 11.2% at the end of 2008 **to 13,3%** at the end of 2009 (in commercial banks from 11.2% to 13, 2%, and in cooperative banks from 13.1% to 13.4%).
At the end of the year, all banks had the solvency ratio in the statutory amount. At the same time only 33 banks (4 commercial and 29 cooperative ones) had a solvency ratio below 10%, but their combined share in the assets of the sector was only 6.3%.

To recapitulate, in 2009 there was **a substantial reinforcement in the capital base of** the Polish banking sector and a significant improvement in terms of capital adequacy. As a consequence, **the stability of the banking sector strongly increased, including the ability to absorb potential losses; the potential for expanding lending was enhanced, too.**
However, taking into account difficult external conditions and the resulting significant risk increase, activities aiming at maintaining the reinforced capital base are desirable.

Conclusions

Based on this description of main risk areas we can conclude that **the current situation as regards the capital base is good, whereas in terms of liquidity it is satisfactory. The credit portfolio quality constitutes the main risk area, since as a result of deterioration in the macroeconomic situation and credit policy applied by some banks it has substantially worsened**.

Ignoring experiences and failure to draw conclusions from recent crisis phenomena seems particularly alarming.

Re-expanding (by some banks) a foreign currency loans offer **arouses concern**. The period 2008-2009 showed the scale of exchange rate volatility and generated risk. It particularly refers to households, nearly all of which have no natural security for their exposures in the form of income received in currencies that are the subject of the loan. It should be noted that even though due to differences in interest rates instalments of foreign currency loans are lower than of similar loans denominated in PLN, yet as a result of a strong weakening of the zloty there has been a steep debt increase for foreign currency loans expressed in PLN (for the majority of customers with a currency loan the amount of debt is higher than for those who have contracted the same obligation in PLN). We cannot assume that results of depreciation of the zloty will be constantly compensated by favourable changes in interest rates.

In some banks **we can observe a return to overly liberal credit policy rules for housing loans** (LTV level).

The banking sector should be prepared for effects of discontinuity in changes in the economic environment by applying an appropriate range of stress tests and actions taken based on their results.

In response to the identified phenomena of loosening credit policy standards for retail loans, and in particular lowering requirements in creditworthiness analysis, **in February 2010 the PFSA adopted the T Recommendation that has to be quickly implemented into the banking practice**.

V. OUTLOOK FOR 2010

In 2009, there was a visible improvement in the situation in the financial market and the global economy gradually recovered. On the other hand, however, numerous potential risks that could severely disrupt or destroy the incoming improvement have still been present. We should be aware that although the activity of the business sector is expected to improve, according to forecasts by economists the situation on the labour market will continue to be under high pressure.

Based on financial plans of commercial banks and branches of financial institutions sent to the Banking Supervision we can expect a moderate pace of banking sector development and a significant improvement in financial results. In particular:

- ♦ banks expect the increase in the balance sheet total by about 11%, which is to be mainly driven by a significant increase in receivables from non-financial (over 16%) and state budget (by about 54%) sectors. Therefore, it seems that there will be a certain shift in banks' activity towards expanding lending for SME sector and the local government sector. Receivables form the financial sector are also expected to rise (by about 7%, whereby deposits at non-residents are to be further reduced and their value should lower by more than 10%). A slight increase should also occur in the securities portfolio (by about 2%). In particular:
  - ✓ loans to households should increase by about 8%, including home loans by about 14%,
  - ✓ loans to business sector should grow by about 15%;

- ♦ the development of activity is to be based mainly on the growth of liabilities to the non-financial sector (by about 12%). To a lesser extent funds for development are to derive from an increase in liabilities to the financial sector (by about 7%, whereby banks expect a decrease in liabilities towards non-residents by more than 20%, which may only partially result from the expected appreciation of the zloty) and growth in liabilities due to the issue of own securities (by about 55%). At the same time liabilities to state budget and local government sectors are to be reduced (by about 4%). In particular:
  - ✓ deposits in the household sector should grow by about 9%
  - ✓ deposits of the business sector should grow by about 5%;

- ♦ as a result of improvement in operating conditions the net financial result is to grow by about 30%. It is to be achieved by a decrease in the negative write-off balance (by about 6%) and a significant improvement in the interest income (by about 13%) and commission income (by about 18%), while maintaining a reduced dynamics for operating costs growth (by about 4%). Nevertheless, it should be noted that nearly one third of reporting institutions expects a deterioration in their results and 11 expects to suffer a financial loss (in 5 entities it is estimated to amount from PLN 50 to 200 million);

- ♦ banks expect an increase in own funds (by about 9%), which is to occur inter alia due to allocating the majority of gains for 2009 to adding funds to capitals. Because of a higher dynamics of lending a slight reduction in the solvency ratio can be expected;

- ♦ despite an improvement in financial results and an increase in capitals, banks expect a further growth of bad loan portfolio, whereby it applies mainly to the portfolio of loans granted to households. In particular, according to banks' estimates:
  - ✓ bad household loans may increase by about 18% (PLN 3.7 billion), with bad home loans increase by about 33% (PLN 1.1 billion).
  - ✓ bad business sector loans may increase by about 6% (PLN 1.5 billion);

- ♦ the improvement in operating conditions induces some banks to slightly increase their employment (by about 1%) and develop a network of partner outlets (by about 10%). The network of own outlets will remain virtually unchanged.

It should be made clear that results of these analysis are a sum of all examined entities' expectations and do not take into account any potential interactions (eg. some entities probably assume that they will take away a part of the market from competitors).
It is also worth to take notice of a few issues. Firstly, expectations of banks regarding changes in receivables and liabilities towards the financial sector indicate that the situation in the interbank market should improve (reluctance to invest funds abroad is still visible, too). Secondly, the banks see a better future for the financial situation in the business sector (the growth in the bad loans portfolio appears to be relatively small). If the

financial situation of some companies effectively improves it may appear that a larger number of provisions gets released than it was initially expected. Thirdly, we should take note of banks' expectations as regards a significant increase in bad home loans portfolio.

To recapitulate, based on banks' financial forecasts (including the above mentioned reservations), we can draw some optimistic conclusions regarding the progress in the situation of the banking sector in 2010. However, we should be aware that the increased risk generated by the environment around banks can exert a negative pressure on their situation.

VI. MAJOR REGULATORY CHANGES AND SUPERVISORY ACTIVITIES

The primary objective of the banking supervision is to ensure the security of funds accumulated on bank accounts and the compliance of banks' activity with provisions of Banking Act, the Act on the National Bank of Poland, statutes and the decision on issuing a permit to establish a bank, as well as compliance of activities conducted by banks in accordance with Art. 70 Par. 2 of the Act of 29 July 2005 on trading in financial instruments with provisions of this Act.

Moreover, in accordance with the Financial Market Supervision Act, the supervision over financial market aims at ensuring the proper functioning of the market, its stability, security and transparency, confidence in the financial market, as well as ensuring protection to the interests of market participants.

Activities undertaken under banking supervision include in particular:

- assessing the financial situation of banks, including examination of their solvency, asset quality, payment liquidity and financial results,
- examining the quality of bank management system, particularly risk management and internal control systems,
- examining the conformity of granted loans, cash loans, letters of credit, bank guarantees and sureties and issued bank securities with regulations applicable in this regard,
- examining collaterals and timeliness of repayments of loans and cash loans,
- examining the compliance with the limits referred to in Art. 71 and Art. 79a of the Banking Act, and assessing the process of identifying, monitoring and controlling exposure concentration, including large exposures,
- examining whether the bank complies with standards defined by FSA for risk acceptable in bank's operation and managing operational risk, including in particular adjusting risk identification and monitoring process as well as reporting on risk to the type and scale of the bank's operation,
- assessing the estimates, maintaining and reviewing the internal capital.

The framework of supervisory policy is determined by the Banking Act, the Financial Market Supervision Act and regulations issued on these grounds by FSA.

Major regulatory changes

The regulatory policy in 2009 aimed at:

- enhancing security and stability of the financial sector,
- continuing actions accounting for experiences related to the financial crisis, aiming at improving the risk management quality in banks and as a result protecting cash deposited on bank accounts,
- ensuring the protection of non-professional market participants.

Objectives of regulatory and prudential policy were implemented by introducing new regulations and modifying regulations that had been applied so far. Furthermore, the objectives were implemented by:

- clarifying and resolving doubts of banks regarding prudential regulations, special rules for bank accounting, financial reporting, including consolidated financial statements of banks,
- developing in cooperation with banks and the NBP changes in banks' supervisory reporting system resulting from changes in the applicable legislation and need for obtaining information from banks for the purposes of the banking supervision,
- developing draft regulations or changes in regulations and prudential recommendations as a part of participation in EU Expert Groups and Basel Committee on Banking Supervision, within the scope covering in particular: capital adequacy, maintaining payment liquidity, criteria for assessing the quality of loans and cash loans, limiting and managing different types of risk such as market risk, concentration risk and operational risk,
- developing proposals for amendments to the Act on Auditors and their Self-Governing Body, entities authorized to examine financial statements and on public supervision as regards rotation of audit firms and key auditors, as well as proposing amendments to draft standards for performing auditor's profession.

In 2009, the following regulations or draft regulations were developed:

Resolution No 314/2009 KNF on other bank's balance sheet items that are included in bank's master funds, their value, scope and conditions for the inclusion of these items in master funds of a bank was developed (the resolution was adopted on 14 October 2009 and entered into force on the same day). The resolution was issued based on Art. 127 Par. 5 (2) (a) of the Banking Act.

Under this resolution the banking supervision allowed to increase bank's own funds after approval from FSA, by including into bank's master funds convertible bonds and long-term bonds which can be redeemed not earlier than after 10 years from the issue and no more than 30 years from the issue (under defined conditions set out in terms of the issue). With regard to long-term bonds it has been stipulated that within the last 10 years of the contract term the amount of funds included into master funds is reduced by 10% in order to avoid a sudden decrease in own funds resulting from the full redemption of bonds (such a solution is consistent with the mechanism of depreciation of subordinated loans provided for in the Banking Act).

The resolution allows including to master funds additionally bonds issued in EUR, CHF and USD in the amount equivalent to their value in Polish zlotys converted at an average exchange rate announced by the NBP.

The resolution sets out specific limits, to the amount of which different types of bonds can be included to master funds, both individually for the issue of particular bond types and as an aggregate limit. The aggregate limit for these instruments in relation to master funds of a bank amounts to 50%, of which 50% is for convertible bonds and 35% for long-term bonds (the amount of these limits was adopted on the basis of the amended Directive 2006/48/EC, which is to be implemented by 31 October 2010 and its rules are to enter in force starting from 31 December 2010).

The term of the resolution is limited to 2 years from the date of its entry into force. The periodic nature of this resolution is a response to the situation on financial markets that resulted from the global financial crisis and the need to enable obtaining a support under conditions when the access to capital has been difficult.

Draft T Recommendation on good practices in risk management for retail credit exposures was adopted in February 2010.

The Recommendation is a response to the identified phenomenon of loosening credit policy standards, in particular: lowering requirements in credit worthiness analysis, excessive and unwarranted extension of crediting period (to reduce the amount of instalments), increasing the LTV ratio. Such situation was revealed by results of inspections carried out in banks and by reports developed by NBP concerning the situation in the credit market. At the same time, banks pointed out to competitive pressure as one of the main causes of loosening their credit policy. Banks were also induced to lower their conditions and criteria for granting loans by an optimistic assessment of the future economic situation, and in the case of housing loans by an ongoing growth in residential property prices (stopped in the second half of 2007). Although as a result of the crisis escalation related to the bankruptcy of Lehman Brothers Bank banks changed their credit policy rules (tightening conditions for customer and transaction approvals), yet not all entities drew relevant conclusions from the materializing risk resulting from the weakness in the crediting process, and not all of them undertook adequate corrective actions. Inconstancy in the approach to the credit risk management in some entities (such as multi-directional changes in approval conditions over a short period) indicated the need to communicate good practices and consolidate positive changes in credit policy rules.

In particular, as regards risk management a bank should take into account the stability and prudence requirement which manifests itself, inter alia, in credit policy rules providing for a long-term risk management perspective, sensitivity to environmental changes and impact on the credit risk level by affecting the choice of bank customers. From this perspective, the practice of risk acceptance process in some banks differs from the so-defined requirements and leads to an excessive risk exposure. The lack of objectivity and necessary conservatism as regards parameters adopted for the assessment of credit capacity and creditworthiness should also be emphasized. The awareness enabling acceptance of a definite risk level is particularly important. This awareness in turn can stem only from knowledge on customers gathered beforehand as a result of credit capacity and creditworthiness assessment. A proper risk identification and measurement as well as determining the level of acceptable risk are a necessary minimum for a proper credit risk management in the bank. By determining the minimum costs of living at the level below the welfare threshold some banks prove to lack the necessary prudence in risk management. While setting a limit to parameters used for creditworthiness assessment banks should provide for their objective nature and justify the level at which they were set by making a reference to amounts confirmed in analysis and researches. It is advisable to maintain the necessary independence of analysis in this scope.

Another example of an excessive liberalism in crediting policy rules is allowing situation where it is accepted that customer's income is overly burdened with debt handling (excessive indebtedness). This practice is particularly worrying as regards groups of customers with the lowest income, who spend the largest share of their income to meet the basic needs.

Identified weaknesses include the assumption made in credit capability and creditworthiness analysis that a customer did not fully use credit limits granted to him by a bank. This approach should be verified in the event of a deterioration in economic conditions (the full economic cycle). Therefore, while assuming that credit limits were not used in full the bank should show the validity of this assumption based on empirical data.

In credit capacity and credit worthiness assessments banks should not disregard liabilities, for the payment of which customers are responsible. As a principle, analysis concerning the value and quality of liabilities as well as customer's revenue should relate to persons liable to repay the credit exposure. Banks should provide such a way of gathering and verifying information in this regard so as to reduce the risk of underestimating the level of the repayment burden. One of the necessary measures in this area is the use of internal and external databases of financial liabilities held by customers, and the history of their handling (based on reciprocity, i.e. also as regards feeding such databases).

The necessity to provide reliable information within the approval process should be stressed, as it is an element directly influencing its quality. Maintaining the credibility of the assessment should result form bank's ability to obtain objective data also from external sources, which would allow verifying declarations and statements made by the borrower. When giving up the necessary requirements in this regard the bank should prove the legitimacy of such an approach based on empirical data.

Given the adverse phenomena (and their materialization, inter alia in the form of a sharp deterioration in the quality of the consumer loan portfolio) and having regard to the safety of the banking sector, the FSA has decided to introduce a recommendation containing a set of good practices in risk management for retail credit exposures. Their implementation should take place at the level of individual bank units and as a part of an integrated approach to risk management for retail credit exposures across the entire bank. Recommendations refer to the following areas:

- management,
- risk control,
- identification, measurement and acceptance of risk,
- securities,
- reporting,
- relationships with customers,
- internal control.

Recommendations enacted by the FSA act as the framework for a proper risk assessment and management of retail credit exposures, and constitute a set of guidelines as regards internal control systems, which should directly and indirectly ensure the integration of these recommendations in all processes related to this type of credit exposures.

FSA expects that these recommendations will be implemented in banks not later than six months from the date of enactment (with exceptions that should be implemented not later than within 10 months).

FSA prepared **draft amendments to the A Recommendation** on managing risk associated with bank transactions concluded on derivatives market and to **the I Recommendation** on managing foreign currency risk in banks as well as rules for banks concerning performing operations burdened with a foreign currency risk.

The A Recommendation was written in 1997, when the derivatives market in Poland was only in the initial phase of development. After more than ten years it became obvious that it is necessary to modify it and adjust to the current state of the market, as well as to make use of experiences originating from crisis phenomena associated with foreign exchange derivatives which occurred between 2008 and 2009. In connection with analysis of these phenomena the Office of the Financial Supervision Authority delivered a letter to chairmen of banks in May last year, which contained a report on involvement of business entities in foreign exchange derivatives transactions, as well as recommendations for sales process and risk management for these instruments.

Based on the analysis concerning the involvement of business entities in f/x derivatives transactions and conclusions from monitoring activities, the banking supervision has prepared a draft amendment to the A Recommendation and the I Recommendation. The proposed changes aim at reducing risk associated with entering into derivatives transactions and changing the manner in which banks inform their customers about risk associated with concluded transactions. In this context, the key is to provide customers with accurate, complete and timely information on transactions concluded by them in derivatives.

The banking supervision believes that implementing provisions of the Recommendation: will limit the credit risk associated with entering into derivatives transactions, should not result in any significant additional costs increase (their potential level depends on the banks' current experience in this regard and the existing internal organization), will not require any major organisational changes.

The I Recommendation was adopted in February 2010 and the A Recommendation in May 2010.

Other supervisory activities

In response to the escalation of crisis phenomena the PFSA has undertaken a number of necessary preventive and adjustment actions in relation to the supervised entities. The banking supervision has immediately responded to signals about problems of capital groups that could be reflected in a situation of their subsidiaries operating in Poland.

Supervisory activities focused on several areas: additional guidelines and recommendations, monitoring activities, meetings with Boards of banks, contacts with home country supervisions, involvement in the work of the Financial Stability Committee. These activities included:

- recommendation to take actions aiming at increasing own funds by adding all gains to banks' capitals and not paying dividends,
- undertaking actions as regards cooperative banks which did not meet the requirement to have their own funds of at the level of 1 million Euro,
- continued monitoring of the involvement of banks significantly exposed to foreign financial entities (information about balance sheet and off-balance sheet amounts),
- continued duty relating to monthly reporting on currency liquidity,
- conducting monitoring and analysis of foreign exchange derivative transactions concluded with non-financial sector entities; cooperation was also held with government authorities to determine the best way to solve the problem of f/x derivative transactions entered into by companies, in terms of unexpected changes in market conditions,
- recommendation to banks on the necessity to review the retail credit risk management system in connection with the phenomenon of "excessive indebtedness" / "credit spiral" and to eliminate weaknesses,
- conducting problem-related and comprehensive inspections and monitoring implementation of post-inspection recommendations,
- continued monitoring related to theimplementation of reorganization proceedings programs,
- analysing and giving opinions on assumptions concerning bank merger processes,
- undertaking necessary individual actions against selected banks within the above mentioned areas, in some cases also system solutions were applied, i.e. FSA communicated a set of recommendations relating to standards of banks' information policy and the sales process of advanced OTC financial products as well as requirements associated with managing by banks risks arising from derivative transactions concluded with non-financial entities.

Meetings with banks were also an important element of supervisory activities. These meeting aimed among others at:

- providing an assessment of the banking sector situation,
- presenting the undertaken inspections and their results,
- pointing out to the fact that banks have to take desirable actions that are expected by the banking supervision and aim at enhancing safety and efficiency of the sector, as well as informing on works planned by the banking supervision related to amending prudential regulations in force and developing new ones, including works undertaken by international EU institutions.

Discussions and possibility to submit postulates to the banking supervision were an important element of these meetings.

In 2009, FSA as the host supervision issued an opinion (conditional approval) for the consolidating supervisor to the proposal made by a bank as regards the application of the Advanced Measurement Approach (AMA). The Authority also issued two approvals for a bank to apply its own own models to determine the delta for options. The current and continuing cooperation with banks and consolidating supervisors was also carried out as regards:

- analysis of proposals and planned applications (and the necessary documentation) concerning issuance of decisions / expressing opinions on approval for the use of statistical methods to calculate capital requirements due to: credit risk (IRB), operational risk (AMA), market risk (including models for calculating the delta for the purposes of calculating the equivalent for OTC options and sensitivity models used to determine the position of the trading book primary instruments for calculating capital requirement due to the general risk of interest rates),
- verification whether banks met the conditions defined in the decision on applying statistical methods for calculating capital requirements for credit risk.
- changing the mode (in relation to the mode defined in the previously issued decision) in which statistical methods for calculating capital requirements for credit risk are implemented.

Direct supervision over banks of analytic and inspection nature

The purpose of the inspection policy implemented in 2009 was the continuation of activities aimed at identifying threats and increased risk areas in banks. Monitoring activities were carried out based on an annual plan of monitoring activities. The plan of inspections in commercial banks has been developed according to the research model based on the supervisory cycle, it also takes into account results of ongoing analysis of economic and financial situation of banks. In turn, for cooperative banks the main criteria taken into account when planning monitoring activities were: the date of the last comprehensive inspection, the degree in which reorganization proceedings were implemented, analytical assessments and forecasts for economic and financial situation, how post-inspection recommendations were implemented and previous supervisory activities applied to the bank.

The list of monitoring activities carried out in 2009

	Comprehensive inspections	Problem-related inspections	Other	Total
Commercial banks and branches of credit institutions				
- the number of monitoring activities	11	6	2	19
- number of man-days	4 595	969	68	5 632
Cooperative banks with assets exceeding 100 million zł				
- the number of monitoring activities	18	7	3	28
- number of man-days	3 970	125	72	4 167
Cooperative banks with assets equal to or less than 100 mln zł				
- the number of monitoring activities	30	14	-	44
- number of man-days	2 947	178	-	3 125

Activities carried out under comprehensive inspections as a standard included examination of the following areas: asset quality, liquidity, interest rate risk, currency operations risk, operational risk, financial result, capital, management - including compliance with the law governing banking activity, statutes and meeting conditions set out the permission to open a bank. Each area was examined and assessed in accordance with the applicable banking supervision methodology. As part of comprehensive inspections an additional task assigned by the Management Board of NBP was executed, too, i.e. control if the required minimum provision was transferred.

In turn, during problem-related inspections selected areas of banks' operation were examined, which in the opinion of the banking supervision could increase banks' operational risk. Issues related to counteracting "money laundering" and terrorist financing as well as implementing recommendations issued after previous inspections were also subject to examination and assessment.

In the course of comprehensive inspections carried out in 2009 in commercial banks a particular attention was drawn to the following issues:

- the way in which banks assessed creditworthiness of their customers,
- managing bank's risk associated with foreign exchange derivatives, including the quality and scope of information that was provided to customers when offering various banking products (especially information about risks arising from transactions),
- calculating capital requirements for credit risk and operational risk, and determining and maintaining by banks internal capital under Pillar II,
- complying with the provisions of Resolution 383/2008 KNF on the bank's risk management process and internal control system,
- managing bank's risk associated with loans to finance real estates, including practical aspects of implementation of provisions of S (II) Recommendation on good practices in credit exposures secured by mortgages,
- managing bank's liquidity risk, including adherence to Resolution 386/2008 KNF - in particular as regards the correctness of the calculation of supervisory liquidity measures and compliance with them,
- conducting bank's stress tests and analysis of their impact on the situation of surveyed banks,
- emergency business plans,
- reliability of information contained in the BION Questionnaire,
- implementing recommendations issued after previous inspections.

Results of inspections conducted in 2009 revealed that not all banks have complied with applicable regulations in a satisfactory degree. The main irregularities related to:

- the process of bank customers' creditworthiness assessment (also as regards derivatives);
- the manner in which the portfolio of credit exposures secured by mortgages is monitored;
- analysis of the impact of exchange rate changes and interest rate changes on credit risk;
- the process of estimating and maintaining the internal capital;
- the business continuity management process;
- the compliance risk management;
- the scope, quality and frequency of banks' management reporting;
- the scope of internal audit activity and effectiveness of controls;
- failure to adjust internal procedures to the existing organizational structure;
- failure to define the acceptable risk tolerance;
- inadequate risk limit systems;
- failure to identify and measure certain types of risk;
- inadequate supervision of the Management Board and Supervisory Board on the risk management process.

The findings resulting from the conducted monitoring activities are included in the record of inspection. Following conducted inspections banks were forwarded PSFA recommendations regarding the the removal of irregularities in order to reduce risk in the banks. Most repeated recommendations were:

in the scope of assets quality:

- ensuring full identification of credit risk associated with loans to private individuals by verifying established assessment rules for creditworthiness of individuals and their periodic monitoring, in particular:
    - implementing the requirement of documenting by the customer income constituting a basis for determining the creditworthiness,
    - establishing realistic minimal costs of living of the borrower (household),
    - determining minimal fixed costs for maintenance of the household, for example, rent, power supply and other fixed expenses,
    - including in the creditworthiness formula the credit liabilities arising from the credit and credit cards limits,
    - taking into account the impact of potential increase of interest rates on on the customers' creditworthiness.
- conducting a comprehensive review of credit exposures, taking into account the applicable provisions, concerning the valuation of assets and the creation of reserves and provisions hedging the suffered risk.
- improving risk management of financing real estate and implementation of the requirements of the Polish Financial Supervision Authority's Resolution No. 391/2008 of 17 December 2008 on issuing the "S" (II) Recommendation on good practices in credit exposures secured by mortgages, in particular by:
    - identification of the risk level associated with financing real estate, including the values and the internal structure of the real estate credit portfolio,
    - conducting time-to-time verification of policy regarding credits secured by mortgages,
    - setting risk controlling limits,
    - separating, in the organizational structure of the bank, functions relating to the analysis of credit applications, risk assessment and credit decision-making,
    - conducting stress tests on the impact of the risk of changes in interest rates on the quality of the portfolio,
    - determining the maximum LTV ratio levels for different types of collaterals,
    - examining LTV ratio level before a credit decision, updating value of the properties and monitoring the level of LTV ratio during the credit agreements and developing procedures determining the rules of bank's procedure in case of increase of the LTV ratio value for individual exposures,
    - monitoring the real estate market, creating a database on real estate constituting collateral for credit agreements,
    - developing detailed internal procedures for the procedures in cases of rapid changes of the collateral value of loans (contingency plan).
- improving risk management of exposure concentrations by:
    - defining the rules for determining and updating the concentration limits,
    - developing assumptions for conducting stress tests,
    - verifying the level and type of set limits, including through the use of results of stress tests,
    - monitoring and reporting of all set limits.

- improving risk management related with the allocation of credit intermediation activities to external economic entities by:
    - determining acceptable level of risk associated with the allocation of credit intermediation to external economic entities, particularly the planned range of operations and limits of risk mitigation,
    - determination of rules of the current assessment of risks arising from the cooperation with such economic entities,
    - determination of the rules of reporting the compliance with internal risk mitigating limits resulting from the collaboration with intermediaries,
    - establishing rules for exercising control over implementation of activities performed by credit intermediaries.

in the scope of liquidity risk:
- developing a plan for obtaining and maintaining stable sources of assets funding,
- supplementing the contingency plan in case of a liquidity crisis and verification of contingency plan assumptions,
- supplementing the conducted liquidity risk measurement and eliminating the irregularities occurring in it,
- improving management of system of limits used to mitigate liquidity risk,
- adjusting rules of supervisory liquidity measurements calculation to the PSFA Resolution No. 386/2008 and complying with supervisory liquidity measurements,
- developing comprehensive management information on liquidity risks.

in the scope of interest rate risk and the exchange operations risk:
- conducting stress tests,
- setting limits for the maximum level of market risk accepted by the bank,
- developing strategic assumptions in the market risk which define the profile of risk and manners of its securing and establishing tolerance for risk,
- adjusting procedures and internal regulations for the functioning organisational structure,
- conducting independent verification of the used methods of measurement of market risk paying special attention to the correctness of the adopted parameters and assumptions, and the completeness and accuracy of used data,
- strengthening the role of internal audit and functional control over the area of market risk,
- supporting the process of market risk management by information systems,
- defining the scope of management information from the market risk prepared for the Supervisory Board and the bank's board,
- mitigating operational risk during the implementation of the dealer transactions to the computerized system,
- improving the quality of currency risk management resulting from transactions related to currency derivatives offered to customers,
- improving the measurement and monitoring of market risk.

in the scope of operational risk:
- implementing/updating Key Risk Indicators (KRI) for the control and operational risk monitoring purposes,
- improving the effectiveness of business continuity management, through:
    - adjusting the business continuity maintenance plan to the changes in the organization of the bank and its external environment,
    - developing and updating contingency plans for all operational units and critical processes and IT systems,
    - conducting time-to-time business continuity plans test,
- improving management information system, including the regular preparation of reports on operational risk for the Supervisory Board.

in the scope of adequacy of capital:
- developing and approving by the bank's board procedure concerning the process of assessing internal capital,
- substantiating and approving of written criteria for recognising individual types of risk as important,
- supplementing the process of assessing internal capital with the omitted material risks,
- maintaining internal capital at a level ensuring the covering all types of material risks present in the activity of the bank,

- implementation of internal procedures for detailed defining the rules for classification of exposures to different classes of exposures, assigning credit risk weights and conducting capital adequacy calculation,
- including all expositions at calculating capital requirement for credit risk,
- implementation of mechanisms ensuring the correct calculation of capital requirement,
- substantiating the process of capital planning,
- developing and approving a bank's capital base development plan.

in the scope of management:

- developing/updating the bank's business strategy and approving it by the Supervisory Board and monitoring the performance of accepted strategic assumptions,
- improving the functioning of the risk management system by:
    - strengthening the supervision of the Supervisory Board and the bank's board over the process of managing individual risks,
    - conducting the comprehensive review of the bank's internal procedures for compliance with the provisions of law governing banking and prudence supervisory recommendations and adjusting to the organizational structure as well as their current updating,
    - implementation of organizational solutions to ensure separation of the measurement, monitoring and risk control functions from operating activity.
- improving the quality of management information system to effectively manage the risk arising in the bank's activity and fulfilling by the bank's board obligation to submit to the Supervisory Board time-to-time information concerning the nature and size of the risk present in the bank's activity, pursuant to the provisions of Article 9 of PFSA Resolution No. 383/2008 of 17 December 2008 on detailed rules for the functioning of risk management system and internal control system and the specific terms of assessing the banks' internal capital and reviewing the process of assessing and maintaining internal capital.
- eliminating the reported violations of the provisions of law, internal procedures and errors in the accounting records and obligatory reporting, as well as ensuring full respect for the provisions in the future,
- improving the effectiveness of functioning of internal control system and internal audit.

Analytical supervision, integrally connected with the inspection one, means the constant monitoring and assessing the situation of the banking sector and individual banks, identifying actual or potential hazards and, if necessary, making interventions. Supervision is based on reports submitted by banks, surveys, meetings with representatives of banks and other available information.
On a quarterly basis a comprehensive analysis of the situation of individual banks and the entire banking sector is performed. Based on the quarterly analysis of economic and financial situation of individual banks they are given a grade in the CAEL system and areas which are likely to be a source of threat and require in-depth examination during the visit are indicated. Simultaneously, under the consolidated supervision the consolidated financial statements of banks, economic and financial situation of holdings and subjects dominant to banks are analysed.
Analytical supervision also includes current examination of the compliance of banks with applicable provisions of law, opinions on bank applications for supervisory body's consent to take action or to obtain rights.

Under the analytical supervision, a wide range of analytical information has been developed ad hoc, including manners of examining creditworthiness, real estate financing and exchange derivatives transactions by banks.

Under the ongoing supervision a constant cooperation with the Ministry of Finance, the Polish National Bank, foreign supervisory bodies and other external institutions were carried out.

POLISH BANKING SECTOR
IN COMPARISON WITH EU COUNTRIES

Polish banking sector in comparison with EU countries - the main characteristics - the results of the ECB survey as of the end of 2008.

	Number of institutions		Number of branches thousand		Number of outlets per 1 million inhabitants		Employment thousand persons		Assets EUR billion		Sector concentration (measured by the participation of 5 biggest banks, in %)		GDP EUR billion		Population million	
	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008
Belgium	104	105	4,8	4,3	464	406	71	65	914	1 272	84	81	290	344	10.4	10.6
Bulgaria	35	30	5.6	6.1	722	794	22	35	13	37	52	57	20	34	7.8	7.7
The Czech Republic	70	54	1.8	2.0	175	191	39	40	87	155	64	62	88	149	10.2	10.4
Denmark	202	171	2.1	2.2	392	399	46	53	630	1 092	67	66	197	232	5.4	5.5
Germany	2 148	1 989	45.3	39,5	549	481	712	686	6 584	7 875	22	23	2 211	2 496	82.5	82.1
Estonia	9	17	0.2	0.3	150	192	4	6	9	22	99	95	10	16	1.4	1.3
Ireland	80	501	0,9	0.9	224	202	36	41	723	1 412	44	56	149	186	4.1	4.4
Greece	62	66	3.4	4.1	308	365	59	66	230	462	65	70	186	243	11.1	11.2
Hiszpania	346	362	40.6	46.1	951	1 010	246	276	1 717	3 381	42	42	841	1 095	42.7	45.6
France	897	728	26.4	39.6	422	618	432	492	4 419	7 225	49	51	1 660	1 950	62.4	64.1
Italy	787	818	31.0	34.1	532	570	336	340	2 276	3 628	26	33	1 392	1 572	58,2	59.9
Cyprus	405	163	1.0	0.9	1 320	1 165	11	13	47	118	57	64	13	17	0.7	0.8
Latvia	23	34	0.6	0.7	252	290	10	14	11	32	62	70	11	23	2.3	.2.3
Lithuania	74	84	0.8	1.0	221	290	7	11	9	27	79	81	18	32	3.4	3.4
Luxembourg	162	152	0.3	0.2	552	469	23	27	695	932	30	27	28	37	0.5	0.5
Hungary	217	197	3.0	3.5	296	350	36	44	x	125	53	55	82	106	10.1	10.0
Malta	16	23	0.1	0.1	247	269	3	4	21	42	79	73	5	6	0.4	0.4
Netherlands	461	302	3,8	3,4	233	208	118	116	1 678	2 235	84	87	491	595	16.3	16.4
Austria	796	803	4.4	4,2	533	509	73	79	635	1 068	44	39	233	282	8.2	8.3
Poland	744	712	8.3	12.9	217	339	150	189	142	263	50	44	204	362	38.2	38.1
Portugal	197	175	5.4	6.4	511	601	53	62	345	482	67	69	144	166	10.5	10.6
Romania	40	43	3.0	7,4	140	344	50	72	23	85	60	54	61	137	21.7	21.4
Slovenia	24	24	0.7	0.7	354	342	12	12	24	49	65	59	27	37	2.0	2.0
Slovakia	21	26	1.1	1.3	207	233	20	21	31	66	67	72	34	65	5.4	5.4
Finland	363	357	1.6	1.7	303	315	25	26	212	384	83	83	152	185	5.2	5.3
Sweden	212	182	2.0	2.0	224	220	44	50	600	900	54	62	288	328	9.0	9.2
Great Britain	407	391	13.4	12.5	224	205	490	496	7 085	8 840	35	37	1 769	1 816	59.8	61.0
EU27	8 902	8 510	211.4	238.1	432	478	3 130	3 335	29 160	42 209	41	44	10 603	12 511	489.8	498.3

Source: “Structural indicators for the EU banking sector”, ECB 2010, independent estimates.
Note: Data for 2009 will be available at the end of 2010

Polish banking sector in comparison with EU countries - selected relationships (%)

	Share in GDP								Relation to the balance sheet total						Relation loans/deposits	
	Assets		Loans		Home loans		Deposits		Loans		Home loans		Deposits			
	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008	2004	2008
Belgium	316	370	105	117	28	25	140	157	33	32	9	7	44	42	75	74
Bulgaria	67	108	36	74	3	12	45	63	54	69	4	11	68	58	79	118
the Czech Republic	99	104	38	52	8	16	67	67	38	50	8	15	68	64	57	78
Denmark	319	470	171	238	86	109	62	82	54	51	27	23	19	18	276	290
Germany	298	316	136	129	43	38	114	123	46	41	14	12	38	39	120	105
Estonia	89	139	60	105	15	39	37	60	68	75	17	28	42	43	162	175
Ireland	485	760	176	259	49	62	122	165	36	34	10	8	25	22	144	157
Greece	124	190	69	91	18	27	90	116	55	48	14	14	72	61	77	78
Spain	204	309	120	181	40	60	104	160	59	59	20	19	51	52	116	114
France	266	371	92	117	26	35	76	86	35	32	10	10	29	23	121	137
Italy	164	231	85	115	13	17	56	76	52	50	8	7	34	33	152	152
Cyprus	366	697	195	321	x	51	236	330	53	46	x	7	65	47	82	97
Latvia	100	140	49	99	12	31	31	58	49	71	12	22	31	41	160	172
Lithuania	47	82	30	65	6	19	31	35	64	79	12	23	66	42	97	186
Luxembourg	2 526	2 541	436	553	34	43	801	718	17	22	1	2	32	28	54	77
Hungary	x	118	x	72	9	14	43	52	x	61	x	12	x	44	x	139
Malta	461	734	192	434	28	39	196	266	42	59	6	5	43	36	98	163
the Netherlands	342	376	173	185	68	63	122	168	51	49	20	17	36	45	142	110
Austria	273	379	127	149	21	25	100	112	47	39	8	7	37	29	127	134
Poland	69	73	33	44	4	13	44	42	47	60	6	18	63	58	75	103
Portugal	240	290	135	170	49	63	101	127	56	58	21	22	42	44	134	133
Romania	38	62	17	37	0	4	25	29	46	60	1	6	65	48	71	126
Slovenia	90	132	53	93	3	9	57	57	59	70	3	7	63	43	94	164
Slovakia	91	101	33	47	7	13	58	62	36	47	7	13	64	62	57	76
Finland	140	208	68	90	27	37	52	61	49	43	20	18	38	29	130	146
Sweden	208	274	105	130	34	39	45	56	50	47	16	14	22	20	232	231
Great Britain	401	487	217	282	55	43	216	285	54	58	14	9	54	58	101	99
EU27	275	337	129	154	36	38	112	134	47	46	13	11	41	40	116	115

Note: The term loans and deposits refers to all loans and deposits not subject to transactions with financial institutions.

STATISTICAL APPENDIX

List of tables

Table 1.1 - Number of banks, employment, network size, market share

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Number of banks	**645**	**649**	**643**	**50**	**52**	**49**	**14**	**18**	**18**	**581**	**579**	**576**
Employment	**167 127**	**181 191**	**175 016**	**133 724**	**145 406**	**137 941**	**3 300**	**4 610**	**5 387**	**30 103**	**31 175**	**31 688**
Branch network	**13 478**	**14 678**	**14 890**	**9 280**	**10 237**	**10 229**	**184**	**236**	**245**	**4 014**	**4 205**	**4 416**
- branches	5 607	6 092	6 378	4 134	4 571	4 808	14	18	18	1 459	1 503	1 552
- other	7 871	8 586	8 512	5 146	5 666	5 421	170	218	227	2 555	2 702	2 864
Market share:												
- assets	100.0	100.0	100.0	89.6	89.2	89.1	4.3	5.4	5.1	6.2	5.4	5.8
- loans to non-financial sector	100.0	100.0	100.0	89.9	89.6	88.8	3.6	5.0	5.4	6.5	5.4	5.8
- non-financial sector deposits	100.0	100.0	100.0	89.4	88.9	88.9	1.9	2.7	2.9	8.8	8.4	8.2
- own funds	100.0	100.0	100.0	92.8	93.3	93.2	x	x	x	7.2	6.7	6.8
- net financial result	100.0	100.0	100.0	95.1	91.9	93.0	-0.7	1.5	-1.0	5.6	6.6	8.0

Table 1.2 - Sector concentration

	5 largest banks			10 largest banks			15 largest banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Employment	**43.0**	**39.8**	**38.9**	**57.0**	**52.0**	**53.6**	**65.3**	**61.5**	**62.3**
Branch network	**41.4**	**39.3**	**38.6**	**51.2**	**47.7**	**49.2**	**55.9**	**54.3**	**55.9**
- branches	47.3	45.6	43.7	62.0	57.5	56.3	64.2	62.5	62.9
- other	37.1	34.8	34.8	43.4	40.8	43.9	49.8	48.5	50.7
Market share:									
- assets	46.6	44.6	44.5	64.5	62.4	63.8	73.9	73.1	74.3
- loans to non-financial sector	44.6	43.1	42.7	60.8	590	59.8	73.3	73.8	73.3
- non-financial sector deposits	56.9	55.3	53.9	72.7	69.8	67.1	79.6	78.5	78.7
- own funds	47.1	47.1	49.0	64.1	63.6	66.4	75.4	74.0	77.3
- net financial result	49.7	61.4	77.8	65.7	75.9	90.2	85.3	82.3	94.0

Table 1.3 - Ownership structure

	Domestic investors			of which: State Treasury			Foreign investors		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Number of banks	**591**	**589**	**586**	**4**	**4**	**4**	**54**	**60**	**57**
Market share:									
- assets	29.1	27.6	31.9	18.3	17.3	20.8	70.9	72.4	68.1
- loans to non-financial sector	29.9	28.6	31.3	19.5	18.5	20.1	70.1	71.4	68.7
- non-financial sector deposits	32.5	32.4	34.0	20.8	20.0	21.2	67.5	67.6	66.0
- own funds	29.9	30.3	32.3	18.9	19.4	21.4	70.1	69.7	67.7
- net financial result	31.6	33.8	43.9	23.2	22.9	31.5	68.4	66.2	56.1

Table 1.4 - Foreign investors by country of origin

	Number of controlled banks and branches of credit institutions			Share in assets (%		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Italy	4	4	4	17.4	13.2	13.3
the Netherlands	4	5	4	10.9	10.8	8.7
Germany	9	10	10	9.3	10.3	9.9
the USA	5	6	5	7.3	8.6	7.4
Belgium	4	4	4	5.6	6.1	5.7
Ireland	2	3	2	5.0	5.3	4.9
France	9	10	9	3.9	4.6	4.6
Portugal	2	3	3	3.9	4.5	4.2
Austria	1	1	1	2.2	2.3	2.0
Sweden	1	1	1	1.3	2.0	2.1
Greece	3	4	3	1.5	1.8	2.2
Spain	2	2	2	1.0	1.0	1.0
Norway	2	1	1	0.7	0.7	0.7
Denmark	2	2	2	0.5	0.5	0.4
Great Britain	2	2	2	0.2	0.3	0.2
Japan	1	1	2	0.2	0.3	0.7
Luxembourg	1	1	1	0	0.0	0.0
- Other	x	0	1	x		0.0
Total	**54**	**60**	**57**	**70.9**	**72.4**	**68.1**
- of which: from EU Member States	45	51	49	62.6	62.8	59.7

Table 2.1 - Balance sheet (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Balance sheet total	**795 362.1**	**1 039 085.4**	**1 060 758.7**	**712 576.2**	**926 430.3**	**944 588.4**	**33 861.4**	**56 119.1**	**54 454.4**	**48 924.5**	**56 536.0**	**61 715.9**
Assets												
Cash in hand, transactions with central bank	28 214.6	39 413.2	50 399.7	26 630.2	36 447.3	46 917.1	361.0	1 580.7	2 095.8	1 223.4	1 385.2	1 386.8
Amounts due from the financial sector	125 209.6	107 176.8	72 905.3	102 207.0	79 627.5	48 014.0	9 233.1	11 250.7	7 595.6	13 769.4	16 298.5	17 295.7
Amounts due from the non-financial sector, of which:	421 850.9	587 616.0	612 065.6	378 882.7	526 322.1	543 650.4	15 505.1	29 653.3	32 801.4	27 463.0	31 640.6	35 613.8
Amounts due from the general government	21 421.9	24 605.5	44 470.0	19 701.4	22 582.8	41 660.0	5.3	4.8	2.8	1 715.1	2 017.9	2 807.2
Receivables under securities repurchase agreements	5 987.1	9 021.8	12 938.3	5 987.1	8 359.6	12 461.2	0.0	662.2	476.4	0.0	0.0	0.7
Securities, of which:	135 641.4	180 924.5	211 355.0	128 720.0	171 949.0	201 148.4	4 319.4	6 152.4	8 152.2	2 602.0	2 823.1	2 054.4
Tangible fixed assets	21 951.3	25 313.7	24 312.3	19 752.0	22 846.2	21 680.4	330.5	389.1	389.7	1 868.8	2 078.4	2 242.2
Other assets	35 085.4	65 013.9	32 312.4	30 695.7	58 295.8	29 057.0	4 106.9	6 425.9	2 940.3	282.7	292.2	315.1
Liabilities												
Amounts owed to central bank	3 041.1	18 144.7	14 487.3	2 929.1	16 531.4	14 442.0	112.0	1 613.2	45.2	0.1	0.1	0.1
Amounts owed to the financial sector	158 386.8	242 229.1	225 434.6	139 162.1	210 818.2	194 924.9	18 316.3	30 510.9	29 426.3	908.5	900.0	1 083.3
Amounts owed to the non-financial sector	428 250.1	506 088.5	571 802.8	383 272.1	450 639.5	508 797.0	8 023.5	13 520.2	16 774.2	36 954.5	41 928.8	46 231.6
Amounts owed to general government	44 705.6	53 515.6	54 316.5	39 857.0	46 995.1	47 764.2	27.2	114.2	134.4	4 821.4	6 406.4	6 418.0
Payables under securities repurchase agreements	13 261.1	14 716.9	14 333.0	11 877.0	12 467.4	11 996.3	1 384.1	2 249.5	2 336.7	0.0	0.0	0.0
Payables under issue of securities	12 393.0	12 480.1	19 417.4	12 393.0	12 171.9	19 198.7	0.0	308.1	218.7	0.0	0.0	0.0
Other liabilities	53 497.1	95 206.0	46 477.4	46 240.7	86 226.9	39 573.9	6 294.4	7 930.2	5 969.3	961.9	1 048.9	934.2
Reserves for off-balance sheet liabilities	418.4	452.5	570.6	410.0	450.2	568.2	5.5	0.5	0.2	2.8	1.8	2.2
General banking risk reserve	651.2	343.9	372.2	540.2	216.1	224.1	0.0	0.0	0.0	111.0	127.9	148.1
Capital (funds) and subordinated liabilities	68 438.9	82 270.2	104 867.3	64 169.4	77 359.2	99 000.1	-208.6	-310.8	-337.6	4 478.1	5 221.8	6 204.8
Profit (loss) pending approval	10.0	-20.3	-28.1	25.5	0.0	0.0	-15.6	-20.2	-23.4	0.0	0.0	-4.7
Profit (loss) of the current period	12 308.8	13 658.2	8 707.5	11 700.1	12 554.5	8 099.0	-77.5	203.3	-89.9	686.1	900.3	698.4

Note: The result in the current year disclosed in 2007 does not take into account the result of discontinued activities of Bank BPH, which has been demonstrated in the equity of Pekao Bank due to take over most of the bank by Pekao Bank

Table 2.2 – Amounts due from and owed to the financial sector – face value (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Amounts due from the financial sector	**125 711.2**	**107 804.4**	**73 413.6**	**102 701.8**	**80 248.4**	**48 514.3**	**9 234.7**	**11 252.4**	**7 599.8**	**13 774.7**	**16 303.6**	**17 299.4**
Resident	67 569.0	63 536.3	50 282.6	48 878.1	38 205.7	27 056.9	4 916.3	9 027.0	5 926.2	13 774.7	16 303.6	17 299.4
Non-resident	58 142.2	44 268.1	23 131.0	53 823.7	42 042.7	21 457.4	4 318.5	2 225.4	1 673.6	0.0	0.0	0.0
Amounts owed to the financial sector	**158 744.7**	**242 535.7**	**225 666.1**	**139 519.8**	**211 124.5**	**195 156.2**	**18 316.4**	**30 511.0**	**29 426.4**	**908.6**	**900.1**	**1 083.5**
Resident	75 991.5	82 574.7	68 868.9	65 633.2	77 261.2	63 792.0	9 449.7	4 417.4	3 995.9	908.6	896.1	1 081.0
Non-resident	82 753.2	159 961.1	156 797.1	73 886.6	133 863.4	131 364.2	8 866.6	26 093.7	25 430.5	0.0	4.0	2.5

Table 2.3 – Loans and deposits of the non-financial sector – face value (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Total loans	**427 552.9**	**593 378.7**	**627 897.5**	**384 169.9**	**531 461.6**	**557 883.8**	**15 531.7**	**29 848.5**	**33 925.8**	**27 851.4**	**32 068.5**	**36 088.0**
- PLN	319 264.4	386 413.5	416 840.7	279 951.3	338 166.4	362 487.6	11 471.4	16 188.4	18 288.0	27 841.9	32 058.8	36 065.1
- foreign currency	108 288.5	206 965.2	211 056.8	104 218.6	193 295.3	195 396.1	4 060.3	13 660.1	15 637.8	9.5	9.8	22.9
Loans for households	**254 210.0**	**368 578.0**	**412 470.3**	**223 686.8**	**323 735.5**	**360 282.9**	**8 365.5**	**19 781.1**	**24 489.9**	**22 157.7**	**25 061.4**	**27 697.5**
- consumer loans	102 489.7	136 451.0	154 495.1	91 758.9	121 664.7	135 791.3	4 452.8	7 558.5	10 455.0	6 278.0	7 227.8	8 248.9
overdraft	17 721.6	20 739.1	22 710.9	15 752.1	18 404.1	20 044.6	0.3	69.7	71.1	1 969.3	2 265.3	2 595.3
credit cards	8 917.6	12 662.8	14 985.7	8 643.8	12 240.7	13 876.7	269.2	411.7	1 091.3	4.5	10.3	17.8
other	75 850.5	103 049.1	116 798.4	67 363.0	91 019.9	101 870.0	4 183.3	7 077.1	9 292.6	4 304.2	4 952.2	5 635.8
- mortgage loans	117 727.8	193 986.0	216 414.2	112 020.0	180 009.2	200 138.4	3 191.2	10 821.3	12 515.9	2 516.6	3 155.6	3 760.0
PLN	52 595.8	59 079.2	75 674.0	48 673.7	54 485.5	70 466.9	1 405.7	1 438.7	1 451.2	2 516.5	3 155.0	3 756.0
foreign currency	65 132.0	134 906.9	140 740.2	63 346.3	125 523.7	129 671.5	1 785.5	9 382.6	11 064.7	0.1	0.6	4.0
- other real property	4 960.3	5 258.3	6 673.5	3 472.7	3 130.7	4 094.7	150.1	457.7	634.6	1 337.6	1 669.9	1 944.2
- investment	21 331.4	24 092.4	25 383.1	12 707.8	14 723.0	15 396.2	134.4	164.1	192.9	8 489.1	9 205.2	9 794.1
- other	7 700.8	8 790.4	9 504.4	3 727.4	4 207.8	4 862.4	437.0	779.6	691.6	3 536.4	3 803.0	3 950.4
Corporate loans	**171 715.7**	**222 561.5**	**212 712.4**	**159 024.1**	**205 715.6**	**195 180.6**	**7 163.8**	**10 050.6**	**9 435.2**	**5 527.8**	**6 795.3**	**8 096.6**
- current operations	90 583.1	111 489.3	99 729.4	82 522.4	100 865.3	89 218.8	5 263.2	7 330.9	6 574.9	2 797.5	3 293.0	3 935.7
- investment	46 808.8	64 098.1	64 690.7	43 230.6	59 815.6	59 971.8	1 573.1	2 005.3	2 038.4	2 005.1	2 277.2	2 680.5
- real property	34 323.8	46 974.2	48 292.2	33 271.1	45 034.7	45 990.0	327.5	714.4	821.9	725.2	1 225.1	1 480.3
Loans for non-commercial institutions	**1 627.3**	**2 239.2**	**2 714.8**	**1 458.9**	**2 026.2**	**2 420.2**	**2.5**	**1.2**	**0.7**	**165.9**	**211.8**	**293.9**
Farm loans	18 214.9	18 968.5	19 447.1	6 172.6	6 142.7	6 097.5	0.0	0.0	0.0	12 042.3	12 825.8	13 349.5
- preferential	14 915.1	15 006.6	14 809.7	5 755.4	5 552.8	5 539.5	0.0	0.0	0.0	9 159.7	9 453.9	9 270.2
Total deposits	**419 308.0**	**494 051.6**	**560 048.5**	**374 720.1**	**439 393.9**	**497 733.8**	**7 870.1**	**13 129.4**	**16 474.6**	**36 717.8**	**41 528.4**	**45 840.2**
- PLN	362 223.0	439 176.3	504 666.2	319 423.1	386 810.9	444 515.9	6 445.1	11 218.8	14 742.9	36 354.9	41 146.6	45 407.4
- foreign currency	57 085.0	54 875.4	55 382.3	55 297.0	52 583.0	53 217.9	1 425.1	1 910.6	1 731.6	362.9	381.8	432.8
Deposits of enterprises	**144 808.9**	**149 098.5**	**166 028.0**	**135 756.7**	**138 840.0**	**155 138.6**	**5 597.2**	**6 546.4**	**6 500.8**	**3 455.1**	**3 712.1**	**4 388.6**
Deposits of households	**262 399.5**	**330 761.6**	**379 671.5**	**228 064.7**	**287 762.3**	**329 807.6**	**2 213.1**	**6 486.4**	**9 881.7**	**32 121.7**	**36 512.9**	**39 982.2**
Deposits of non-commercial institutions	**12 099.6**	**14 191.6**	**14 349.0**	**10 898.7**	**12 791.6**	**12 787.6**	**59.8**	**96.6**	**92.1**	**1 141.0**	**1 303.4**	**1 469.3**

Note:
In the case of households: consumer loans cover overdraft, credit card debt and other loans and credits, investment loans are the sum of loand for investment and for the purchase of securities, and other include discounted loans, export loans and operating loans.
In the case of enterprises: loans for current operations covers overdraft, discounted loans, export loans, operating loans and other loans and credits, while investment loans are the sum of loans for investment and for the purchase of securities.

Table 2.4 – Securities (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Total	**135 641.4**	**180 924.5**	**211 355.0**	**128 720.0**	**171 949.0**	**201 148.4**	**4 319.4**	**6 152.4**	**8 152.2**	**2 602.0**	**2 823.1**	**2 054.4**
Resident	129 519.5	177 347.0	209 469.6	122 769.0	168 371.5	199 262.9	4 148.5	6 152.4	8 152.2	2 602.0	2 823.1	2 054.4
Non-resident	6 121.9	3 577.5	1 885.4	5 951.0	3 577.5	1 885.4	170.9	0.0	0.0	0.0	0.0	0.0
Equity	1 443.7	1 037.6	6 029.7	1 421.4	1 024.1	6 008.3	0.0	0.0	0.0	22.3	13.4	21.3
Debt	134 020.0	179 750.3	204 923.2	127 188.2	170 821.4	194 773.7	4 319.4	6 152.4	8 152.2	2 512.4	2 776.4	1 997.1
- NBP bills	7 756.0	10 197.8	40 951.7	6 984.8	9 464.1	39 428.1	0.0	0.0	1 249.9	771.2	733.7	273.6
- NBP bonds	8 036.6	8 144.8	0.0	7 966.0	8 073.4	0.0	29.9	43.8	0.0	40.7	27.6	0.0
- Treasury bills	11 436.0	36 940.7	31 806.7	9 997.5	33 759.4	28 904.9	209.3	1 952.0	2 265.3	1 229.2	1 229.3	636.5
- Treasury bonds	92 894.6	109 969.8	117 482.4	88 676.1	105 256.4	112 024.1	3 817.0	4 123.7	4 637.1	401.5	589.7	821.2
- other	13 896.9	14 497.2	14 682.4	13 563.8	14 268.1	14 416.6	263.2	33.0	0.0	69.9	196.1	265.8
Other	177.7	136.7	402.2	110.4	103.4	366.3	0.0	0.0	0.0	67.3	33.2	35.9

Table 2.5 – Capital (funds) and subordinated liabilities (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Total	**68 647.5**	**82 581.0**	**105 204.9**	**64 169.4**	**77 359.2**	**99 000.1**	**x**	**x**	**x**	**4 478.1**	**5 221.8**	**6 204.8**
Core funds	14 366.6	16 063.0	21 316.1	13 742.8	15 436.4	20 628.6	x	x	x	623.8	626.6	687.5
Own stocks	-2.2	-133.6	-145.3	-2.2	-99.3	-101.8	x	x	x	0.0	-34.3	-43.6
Supplementary capital (fund)	31 178.5	38 180.9	45 364.2	27 831.7	34 237.7	40 623.4	x	x	x	3 346.8	3 943.1	4 740.8
Other reserves	9 460.4	10 790.2	18 546.8	9 419.3	10 742.6	18 493.8	x	x	x	41.1	47.7	53.0
General banking risk fund	7 499.6	8 484.4	9 374.7	7 269.5	8 217.9	9 064.2	x	x	x	230.1	266.5	310.6
Profit (loss) brought forward	-13.1	284.6	-322.5	-19.1	284.6	-320.5	x	x	x	6.0	0.0	-2.0
Revaluation reserve	67.3	352.2	1 255.3	-37.9	256.4	1 154.8	x	x	x	105.1	95.7	100.5
Other supplementary funds (CBS/PFSA/Banking Law)	531.1	952.5	940.5	531.1	952.5	940.5	x	x	x	0.0	0.0	0.0
Reserve for risk and expenditures unrelated with core activity	0.0	0.0	0.0	0.0	0.0	0.0	x	x	x	0.0	0.0	0.0
Maturity-adjusted subordinated liabilities	5 152.3	6 940.5	8 149.3	4 991.1	6 704.7	7 875.2	x	x	x	161.2	235.8	274.0
Other subordinated liabilities	434.6	618.9	690.7	407.8	578.4	607.0	x	x	x	26.9	40.4	83.7
Interest on subordinated liabilities	35.1	47.0	34.4	35.0	46.8	34.2	x	x	x	0.1	0.3	0.2

Table 3 – Profit and loss account (PLN million) and performance

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Net interest	**24 339.5**	**30 088.7**	**28 516.1**	**21 669.7**	**26 402.0**	**24 811.0**	**497.6**	**943.3**	**1 294.5**	**2 172.2**	**2 743.4**	**2 410.5**
- income	43 231.4	60 199.1	57 620.9	38 729.0	53 037.7	50 608.6	1 510.5	3 114.8	3 142.2	2 991.9	4 046.7	3 870.2
- costs	18 891.9	30 110.5	29 104.9	17 059.3	26 635.7	25 797.6	1 012.9	2 171.5	1 847.7	819.7	1 303.2	1 459.6
Net commissions	**10 997.7**	**11 512.1**	**12 368.0**	**10 007.0**	**10 185.0**	**11 043.7**	**186.4**	**450.3**	**375.7**	**804.4**	**876.8**	**948.6**
- income	13 895.8	14 902.1	16 017.5	12 529.0	13 140.7	14 226.1	484.9	800.5	763.8	881.9	960.9	1 027.6
- costs	2 898.0	3 389.9	3 649.5	2 522.0	2 955.7	3 182.4	298.5	350.1	388.0	77.5	84.1	79.0
Income from stocks, shares and other securities	966.6	1 505.5	1 735.5	960.7	1 491.5	1 717.3	0.0	0.0	0.0	5.8	14.0	18.1
Result of financial transactions	1 447.9	-757.0	3 864.9	1 548.1	-857.7	3 366.1	-109.7	108.5	492.9	9.5	-7.8	5.8
Foreign exchange result	3 664.8	5 961.8	3 032.5	3 319.5	5 817.0	3 003.2	329.5	119.9	3.1	15.8	24.9	26.2
Profit on banking operations	**41 416.5**	**48 311.0**	**49 516.9**	**37 505.0**	**43 037.6**	**43 941.4**	**903.8**	**1 622.0**	**2 166.2**	**3 007.7**	**3 651.4**	**3 409.2**
Other operating income	1 870.1	1 940.9	1 946.0	1 707.6	1 767.4	1 700.4	47.4	43.6	96.8	115.1	130.0	148.7
Other operating costs	806.9	929.8	1 269.8	676.3	787.7	1 073.6	47.1	41.5	112.6	83.4	100.6	83.6
Result from fair value hedge accounting	-4.3	0.5	14.5	-2.4	0.4	14.4	-2.0	0.0	0.1	0.0	0.0	0.0
Administrative costs	**21 771.9**	**24 849.6**	**24 942.8**	**19 092.9**	**21 667.7**	**21 507.3**	**734.3**	**936.1**	**1 134.8**	**1 944.7**	**2 245.8**	**2 300.7**
- wages and salaries	10 066.7	11 460.6	11 350.5	8 644.2	9 759.2	9 565.4	265.3	354.1	410.7	1 157.1	1 347.3	1 374.4
- insurance and other benefits	2 211.2	2 357.5	2 185.6	1 906.4	2 012.1	1 834.4	51.6	73.2	76.0	253.1	272.2	275.3
- other	9 494.1	11 031.6	11 406.7	8 542.2	9 896.4	10 107.5	417.4	508.7	648.2	534.5	626.4	651.0
Amortisation and depreciation of fixed assets and intangible assets	**2 290.0**	**2 338.8**	**2 532.7**	**2 062.7**	**2 083.5**	**2 254.4**	**66.7**	**77.8**	**95.7**	**160.6**	**177.5**	**182.6**
Net provisions and revaluation	**1 713.0**	**5 322.5**	**12 003.7**	**1 469.9**	**4 853.5**	**10 921.8**	**165.7**	**348.8**	**972.6**	**77.4**	**120.1**	**109.3**
- write-offs for provisions and revaluation	11 679.3	17 084.2	33 248.3	11 128.9	16 293.1	31 805.9	196.5	373.6	1 014.2	353.9	417.5	428.1
of which: for non-performing loans	5 789.6	9 172.0	23 279.8	5 437.2	8 621.2	22 022.8	102.0	274.1	941.6	250.4	276.8	315.3
- release of provisions and revaluation	9 966.2	11 761.7	21 244.6	9 659.0	11 439.5	20 884.1	30.7	24.8	41.6	276.5	297.4	318.9
of which: non-performing loans	4 652.9	5 514.6	13 579.8	4 428.6	5 300.4	13 326.3	19.0	3.4	20.2	205.3	210.8	233.3
Operating result	**16 700.5**	**16 811.7**	**10 728.2**	**15 908.4**	**15 412.9**	**9 899.2**	**-64.7**	**261.5**	**-52.7**	**856.7**	**1 137.3**	**881.8**
Extraordinary profit (loss)	0.1	0.2	-15.1	0.1	0.3	0.2	0.0	0.0	-15.6	0.0	-0.1	0.3
Negative goodwill fully recognised in the financial result	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Share in profits (losses) of subsidiaries	0.3	-28.8	1.8	0.3	-28.8	1.8	0.0	0.0	0.0	0.0	0.0	0.0
Profit (loss) on assets for sale	-1.1	4.4	0.0	-1.1	4.4	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Gross profit (loss)	**16 699.8**	**16 787.5**	**10 714.8**	**15 907.7**	**15 388.8**	**9 901.1**	**-64.7**	**261.5**	**-68.3**	**856.8**	**1 137.2**	**882.0**
Income tax	3 059.9	3 130.1	2 007.0	2 871.1	2 834.8	1 802.2	15.1	58.4	21.5	173.6	237.0	183.3
Other obligatory decreases in profit (increases in loss)	-2.2	-0.8	0.4	-2.5	-0.5		0.0	-0.3		0.2	-0.1	0.4
Net profit (loss)	**13 642.2**	**13 658.2**	**8 707.5**	**13 039.1**	**12 554.5**	**8 099.0**	**-79.8**	**203.3**	**-89.9**	**682.9**	**900.3**	**698.4**
Performance												
Net Interest Margin (%)	3.1	3.2	2.6	3.1	3.1	2.5	1.9	1.7	2.0	4.8	5.2	4.2
Cost-Income Ratio (%)	56.3	54.1	54.0	54.6	53.1	52.6	84.4	59.7	54.6	69.2	66.0	71.4
ROA (%)	1.7	1.6	0.9	1.8	1.6	0.9	-0.1	0.6	-0.1	1.5	1.7	1.2
ROE (%)	22.5	21.1	11.3	22.9	21.2	11.2	x	x	x	17.2	19.3	12.7
Average gross monthly salary (PLN)	5 019.5	5 270.9	5 404.5	5 386.9	5 593.1	5 778.7	6 700.4	6 400.9	6 352.5	3 203.2	3 601.4	3 614.5
Assets / 1 employee (PLN thousand)	4 758.0	5 734.8	6 060.9	5 328.9	6 371.3	6 847.8	10 147.3	12 173.3	10 108.5	1 625.1	1 813.5	1 947.6
Gross profit (loss) / 1 employee (PLN thousand)	100.1	92.7	61.2	119.1	105.8	71.8	-17.5	56.7	-12.7	28.6	36.5	27.8

Table 4 – Non-performing loans (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Non-performing loans	**23 205.5**	**28 096.4**	**49 402.7**	**22 106.0**	**26 481.3**	**46 375.0**	**240.8**	**695.1**	**1 793.0**	**858.7**	**920.0**	**1 234.7**
Financial sector	395.6	565.3	493.4	390.4	559.5	489.9	0.0	0.0	0.0	5.2	5.7	3.6
Non-financial sector	22 712.8	27 434.4	48 812.7	21 621.7	25 827.0	45 791.8	240.8	695.1	1 793.0	850.2	912.3	1 227.9
- enterprises	12 158.8	14 265.6	26 008.7	11 740.0	13 824.7	25 282.4	113.0	73.2	166.2	305.8	367.6	560.2
- households	10 497.9	13 086.0	22 755.3	9 830.6	11 923.9	20 465.1	127.4	621.4	1 626.8	539.8	540.6	663.4
- non-commercial institutions	56.1	82.9	48.7	51.1	78.4	44.3	0.4	0.5	0.0	4.6	4.0	4.3
General government	97.1	96.7	96.5	93.9	94.7	93.3	0.0	0.0	0.0	3.2	2.0	3.2
Share of non-performing loans in total receivables	**4.0**	**3.8**	**6.6**	**4.3**	**4.1**	**7.1**	**1.0**	**1.7**	**4.3**	**2.0**	**1.8**	**2.2**
Financial sector	0.3	0.5	0.7	0.4	0.7	1.0	0.0	0.0	0.0	0.0	0.0	0.0
Non-financial sector	5.2	4.5	7.6	5.5	4.8	8.0	1.5	2.3	5.3	3.0	2.8	3.4
- enterprises	6.9	6.2	11.7	7.1	6.5	12.4	1.6	0.7	1.8	5.5	5.4	6.9
- households	4.1	3.5	5.5	4.4	3.7	5.7	1.5	3.1	6.6	2.4	2.2	2.4
- non-commercial institutions	3.4	3.7	1.8	3.5	3.9	1.8	16.8	39.0	0.0	2.8	1.9	1.5
General government	0.5	0.4	0.2	0.5	0.4	0.2	0.0	0.0	0.0	0.2	0.1	0.1
Non-performing loans for households	**10 377.9**	**12 963.9**	**22 496.4**	**9 718.5**	**11 807.4**	**20 222.9**	**122.5**	**618.4**	**1 611.6**	**536.9**	**538.1**	**662.0**
- consumer loans	6 728.7	8 994.7	16 730.1	6 395.5	8 166.4	15 034.8	116.8	597.0	1 427.3	216.4	231.3	267.9
overdraft	1 319.7	1 341.1	1 824.3	1 278.8	1 296.5	1 767.9	0.0	0.0	0.6	41.0	44.6	55.9
credit cards	555.1	858.6	1 816.2	529.3	828.2	1 669.8	25.8	30.2	146.1	0.1	0.2	0.3
other	4 853.8	6 795.0	13 089.6	4 587.4	6 041.7	11 597.2	91.1	566.7	1 280.7	175.3	186.5	211.7
- mortgage loans	1 361.6	1 953.9	3 211.2	1 327.5	1 901.6	3 111.4	3.8	18.3	46.0	30.4	34.0	53.7
PLN	889.1	1 201.2	1 841.2	856.0	1 162.4	1 775.2	2.7	4.9	12.4	30.4	34.0	53.7
foreign currency	472.6	752.7	1 370.0	471.5	739.2	1 336.3	1.1	13.5	33.7	0.0	0.0	0.0
- other real property	137.2	157.0	223.8	120.3	131.4	177.9	0.0	0.0	0.0	16.9	25.6	45.9
- investment loans	1 184.5	1 134.9	1 378.9	1 034.8	995.5	1 208.2	1.9	3.1	4.4	147.8	136.2	166.4
- other	965.9	723.5	952.4	840.5	612.4	690.5	0.0	0.0	133.9	125.4	111.0	128.1
Share of non-performing loans in total loans												
Total	4.1	3.5	5.5	4.3	3.6	5.6	1.5	3.1	6.6	2.4	2.1	2.4
- consumer loans	6.6	6.6	10.8	7.0	6.7	11.1	2.6	7.9	13.7	3.4	3.2	3.2
overdraft	7.4	6.5	8.0	8.1	7.0	8.8	0.0	0.0	0.8	2.1	2.0	2.2
credit cards	6.2	6.8	12.1	6.1	6.8	12.0	9.6	7.3	13.4	1.7	1.7	1.9
other	6.4	6.6	11.2	6.8	6.6	11.4	2.2	8.0	13.8	4.1	3.8	3.8
- mortgage loans	1.2	1.0	1.5	1.2	1.1	1.6	0.1	0.2	0.4	1.2	1.1	1.4
PLN	1.7	2.0	2.4	1.8	2.1	2.5	0.2	0.3	0.9	1.2	1.1	1.4
foreign currency	0.7	0.6	1.0	0.7	0.6	1.0	0.1	0.1	0.3	0.0	0.0	0.0
- other real property	2.8	3.0	3.4	3.5	4.2	4.3	0.0	0.0	0.0	1.3	1.5	2.4
- investment loans	5.6	4.7	5.4	8.1	6.8	7.8	1.4	1.9	2.3	1.7	1.5	1.7
- other	12.5	8.2	10.0	22.5	14.6	14.2	0.0	0.0	19.4	3.5	2.9	3.2
Hedges and reserves/write-offs for non-perf. loans of the non-fin. sec.												
- hedge value	4 687.1	6 803.4	12 512.9	4 327.6	6 495.9	11 949.5	78.9	12.9	14.6	280.6	294.6	548.8
- basis for the creation of reserves / write-offs	18 025.7	20 631.0	36 299.8	17 294.1	19 331.1	33 842.3	161.9	682.2	1 778.4	569.7	617.6	679.1
- created reserves / write-offs	15 621.1	16 488.9	25 305.2	14 982.8	15 553.8	23 244.3	184.3	465.4	1 565.6	453.9	469.7	495.4

Table 5 – Capital adequacy (PLN million)

	Total banking sector			Commercial banks			Branches of credit institutions			Cooperative banks		
	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009	12/2007	12/2008	12/2009
Total own funds of banks for capital adequacy ratio	**61 764.6**	**77 568.8**	**89 736.6**	**57 304.6**	**72 408.3**	**83 654.9**	**x**	**x**	**x**	**4 460.0**	**5 160.5**	**6 081.7**
- short-term capital	272.9	448.4	297.7	272.9	448.4	297.7	x	x	x	0.0	0.0	0.0
- Tier I capital	60 002.8	74 346.4	88 422.5	55 761.5	69 467.7	82 683.0	x	x	x	4 241.3	4 878.7	5 739.5
- Tier II capital	5 742.4	8 542.4	10 403.4	5 475.5	8 205.3	10 009.3	x	x	x	266.9	337.2	394.1
- deductions from the sum of Tier I and II capital	4 253.6	5 768.4	9 387.0	4 205.4	5 713.0	9 335.2	x	x	x	48.2	55.4	51.8
Breakdown of banks by own funds												
< 3	2	2	0	0	0	0	x	x	x	2	2	0
3 < 10	472	434	387	0	0	0	x	x	x	472	434	387
10 < 20	83	101	136	0	0	0	x	x	x	83	101	136
20 < 50	21	39	47	0	1	1	x	x	x	21	38	46
50 < 100	8	7	7	5	4	1	x	x	x	3	3	6
100 < 200	11	9	10	11	8	9	x	x	x	0	1	1
200 < 500	12	14	13	12	14	13	x	x	x	0	0	0
500 < 1000	7	7	7	7	7	7	x	x	x	0	0	0
1000 < 2000	7	7	7	7	7	7	x	x	x	0	0	0
2000 < 5000	6	9	8	6	9	8	x	x	x	0	0	0
5000 < 10000	1	0	1	1	0	1	x	x	x	0	0	0
> 10000	1	2	2	1	2	2	x	x	x	0	0	0
Total capital requirement	**40 724.8**	**55 537.1**	**54 168.5**	**38 141.2**	**52 385.6**	**50 533.4**	**x**	**x**	**x**	**2 583.6**	**3 151.5**	**3 635.2**
Credit risk	38 552.1	48 537.0	47 259.6	35 986.3	45 825.8	44 119.5	x	x	x	2 565.8	2 711.2	3 140.1
Operational risk	x	5 712.4	5 957.0	x	5 283.2	5 464.8	x	x	x	x	429.1	492.2
Equity and debt securities price risk, commodities and currency risk	468.6	360.2	276.2	466.1	358.4	275.6	x	x	x	2.6	1.8	0.6
Interest rate risk	894.3	728.4	577.8	894.3	728.1	577.8	x	x	x	0.0	0.2	0.0
Excess of large exposure limit	380.6	180.5	61.3	369.4	175.7	60.0	x	x	x	11.2	4.8	1.3
Excess of capital concentration limit	0.0	1.5	0.2	0.0	1.5	0.2	x	x	x	0.0	0.0	0.0
Other	429.2	17.2	36.4	425.1	12.9	35.4	x	x	x	4.0	4.3	1.0
Capital adequacy ratio	**12.1**	**11.2**	**13.3**	**12.0**	**11.1**	**13.2**	x	x	x	**13.8**	**13.1**	**13.4**
Median (Me)	15.2	14.1	14.7	12.1	11.5	13.0	x	x	x	15.5	14.3	14.9
Breakdown of banks by capital adequacy ratio												
< 8	1	5	0	0	2	0	x	x	x	1	3	0
8 < 10	67	50	33	4	13	4	x	x	x	63	37	29
10 < 12	112	147	135	19	16	16	x	x	x	93	131	119
12 < 15	129	157	158	10	5	10	x	x	x	119	152	148
> 15	322	272	299	17	16	19	x	x	x	305	256	280