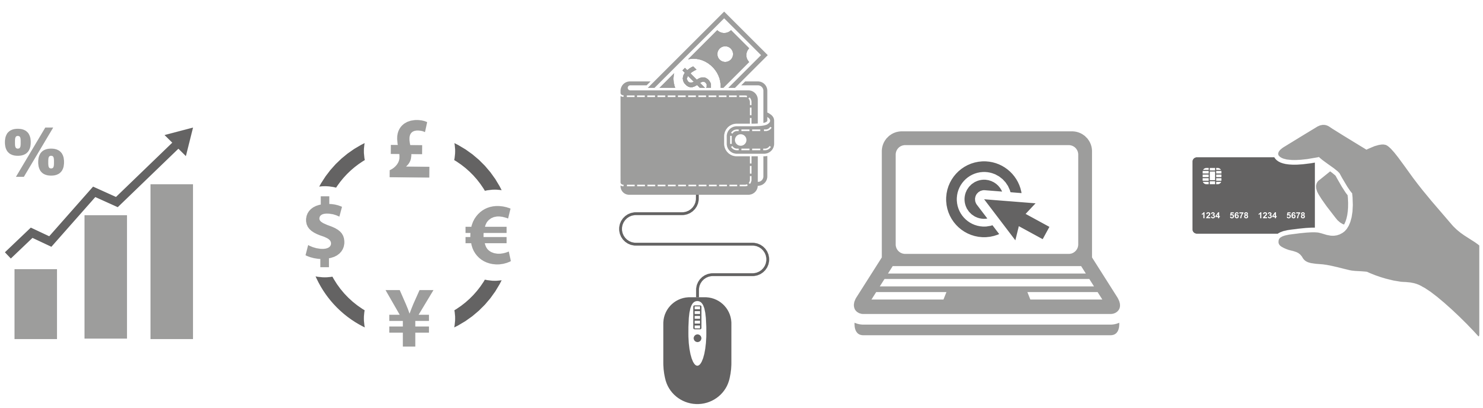
# ANNUAL REPORT 2016

**Komerční banka, a.s.**




NA PARTNERSTVÍ ZÁLEŽÍ

KB

# Survey of Results 2012–2016

According to International Financial Reporting Standards (IFRS)

| Consolidated data (CZK million) | 2016 | 2015 restated[1] | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| **Financial results** | | | | | |
| Net operating income | 31,750 | 31,044 | 30,677 | 30,894 | 32,664 |
| of which Net interest income | 21,067 | 21,357 | 21,423 | 21,207 | 21,969 |
| of which Net fees and commissions | 6,683 | 6,968 | 6,752 | 7,077 | 6,971 |
| Total operating costs | (14,026) | (14,352) | (13,065) | (13,148) | (13,485) |
| Attributable net profit | 13,688 | 12,758 | 12,954 | 12,528 | 13,954 |
| Net profit per share (CZK)[2] | 72.48 | 67.55 | 68.59 | 66.34 | 73.89 |
| **Balance sheet** | | | | | |
| Total assets | 922,737 | 891,556 | 953,261 | 863,980 | 786,836 |
| Loans and advances to customers, net | 580,198 | 532,617 | 494,706 | 473,089 | 451,547 |
| Amounts due to customers | 699,377 | 656,287 | 701,867 | 649,158 | 579,067 |
| Total shareholders' equity | 105,401 | 106,229 | 109,494 | 96,538 | 100,538 |
| **Ratios (%)[3]** | | | | | |
| Return on average equity (ROAE)[4] | 13.42 | 12.22 | 12.95 | 13.09 | 15.77 |
| Return on average assets (ROAA)[5] | 1.51 | 1.38 | 1.43 | 1.52 | 1.81 |
| Net interest margin | 2.53 | 2.60 | not available | not available | not available |
| Cost/income ratio | 44.18 | 46.23 | 42.59 | 42.56 | 41.28 |
| **Capital[6]** | | | | | |
| Capital adequacy (%) | 16.18 | 16.34 | 16.42 | 15.81 | 14.66 |
| Tier 1 ratio (%) | 16.18 | 16.34 | 16.42 | 15.81 | 14.66 |
| Tier 1 | 71,659 | 66,606 | 63,095 | 61,722 | 56,295 |
| Tier 2 | 0 | 0 | 0 | 0 | 0 |
| Total regulatory capital | 71,659 | 66,606 | 63,095 | 59,087 | 53,684 |
| Total risk-weighted assets | 442,865 | 407,642 | 384,186 | 373,796 | 366,107 |
| **Other data** | | | | | |
| Number of employees, average | 8,476 | 8,426 | 8,520 | 8,604 | 8,758 |

| Credit ratings (as of end of February 2017)[7] | Short-term | Long-term |
|---|---|---|
| Standard & Poor's | A-1 | A |
| Moody's | Prime-1 | A2 |
| Fitch | F1 | A- |

1) Comparative information has been restated to reflect the presentation of the current period – see chapter 3.6 Changes in accounting policies and reclassifications in Consolidated Financial Statements.
2) Net profit attributable to shareholders/average number of outstanding shares. Adjusted for the effect of 1-to-5 split of KB shares implemented in April 2016
3) According to the Komerční banka methodology
4) Net profit attributable to shareholders/average shareholders' equity excl. minority interest
5) Net profit attributable to shareholders/average assets
6) According to Basel II methodology during 2012–2013, Basel III since 2014
7) KB was assigned a credit rating by rating agencies registered under Regulation of the European Parliament and Council Regulation (EC) No. 462/2013. KB has considered appointment of rating agencies in accordance with Article 8d of this Regulation and decided not to appoint a rating agency whose market share is smaller than 10%.

Definitions of the Alternative Performance Measures mentioned in this annual report are provided in the respective chapter herein.

| Separate data (CZK million) | 2016 | 2015 restated[1] | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| **Financial results** | | | | | |
| Net operating income | 30,608 | 28,995 | 27,762 | 28,952 | 28,100 |
| of which Net interest income | 20,571 | 19,883 | 18,875 | 18,923 | 17,794 |
| of which Net fees and commissions | 5,979 | 6,287 | 6,370 | 6,672 | 6,990 |
| Total operating costs | (12,710) | (13,113) | (11,871) | (11,790) | (12,008) |
| Net profit | 14,119 | 12,424 | 12,768 | 13,123 | 12,249 |
| **Balance sheet** | | | | | |
| Total assets | 868,065 | 835,526 | 862,766 | 773,892 | 689,457 |
| Loans and advances to customers, net | 527,143 | 484,474 | 449,180 | 423,295 | 396,189 |
| Amounts due to customers | 638,410 | 593,059 | 601,412 | 552,253 | 485,969 |
| Total shareholders' equity | 93,032 | 93,303 | 95,634 | 83,702 | 87,544 |
| **Ratios (%)[2]** | | | | | |
| Return on average equity (ROAE)[3] | 15.15 | 13.15 | 14.24 | 15.33 | 15.31 |
| Return on average assets (ROAA)[4] | 1.66 | 1.46 | 1.56 | 1.79 | 1.82 |
| Net interest margin | 2.34 | n.a. | n.a. | n.a. | n.a. |
| Cost/income ratio | 41.53 | 45.23 | 42.76 | 40.72 | 42.73 |
| **Capital[5]** | | | | | |
| Capital adequacy (%) | 16.91 | 16.66 | 17.05 | 16.01 | 15.32 |
| Tier 1 ratio (%) | 16.91 | 16.66 | 17.05 | 16.01 | 15.32 |
| Tier 1 | 67,263 | 61,665 | 59,151 | 54,944 | 51,228 |
| Tier 2 | 0 | 0 | 0 | 0 | 0 |
| Total regulatory capital | 67,263 | 61,665 | 59,151 | 52,902 | 49,102 |
| Total risk-weighted assets | 397,796 | 370,228 | 346,938 | 330,444 | 320,605 |
| **Other data** | | | | | |
| Number of employees, average | 7,549 | 7,538 | 7,624 | 7,706 | 7,845 |
| Number of points of sale | 392 | 397 | 399 | 399 | 400 |
| Number of clients (thousands) | 1,654 | 1,647 | 1,626 | 1,589 | 1,602 |
| Number of ATMs | 768 | 772 | 754 | 729 | 702 |

1) Comparative information for 2015 has been restated to reflect the presentation of the current period – see chapter 3.6 Changes in accounting policies and reclassifications in Separate Financial Statements
2) According to the Komerční banka methodology
3) Net profit/average shareholders' equity
4) Net profit/average assets
5) According to Basel II methodology during 2012–2013, Basel III since 2014

## Further information

Detailed financial and operational information about Komerční banka Group is available in other publications on KB's website for shareholders and investors **www.kb.cz/en/about-the-bank/investor-relations/index.shtml**. Additional information on corporate social responsibility and ethics at KB is available in the 'About the bank' section at **http://www.kb.cz/en/about-the-bank/about-us/basic-information.shtml**. Information about KB's products and services is accessible from the homepage **www.kb.cz/en**.

This document contains a number of forward-looking statements relating to the targets and strategies of Komerční banka Group. These statements are based on a series of assumptions, both general and specific. As a result, there is a risk that these projections will not be fulfilled. Forward-looking statements are valid only as of the date they are made, and it should not be assumed that they will be revised or updated in the light of new information or future events. Readers are therefore advised not to rely on this information more than is justified, as the Group's future results are liable to be affected by a number of factors and may therefore differ from current estimates.

Readers are advised to take into account factors of uncertainty and risk when basing their investment decisions on information provided in this document.

## Contacts

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Investor Relations
Telephone: (+420) 955 532 155,
955 532 156,
955 532 734
Email: investor_relations@kb.cz

**Loans to clients** (KB Group, gross loans, CZK billion)*


## CZK 595.4 bil. +8.6%

* excluding Other amounts due from customers

**Client deposits** (KB Group, CZK billion)*


## CZK 694.2 bil. +7.4%

* excluding repo operations with clients

**Profit attributable to the Group's equity holders**
(CZK billion)


## CZK 13.7 bil. +7.3%

**Number of standalone Bank clients**


## 1,654,000 clients +0.4%

Komerční banka, a.s.

# ANNUAL REPORT 2016

# Contents

# History

Komerční banka was established in 1990 as a state institution, and in 1992 it was transformed into a joint-stock company. KB's shares have been listed on the Prague Stock Exchange since its inception in 1993, as well as within the RM-System.

In 2001, the state's 60% holding in Komerční banka was purchased by Société Générale. Following privatisation, KB began significantly to develop its activities for individual customers and entrepreneurs while continuing to build on its traditionally strong position in the enterprises and municipalities market.

In developing its retail activities, KB purchased in 2006 the remaining 60% of shares in Modrá pyramida it did not already own. Thereby, Komerční banka attained full control over the Czech Republic's third largest building society. Another important step in extending the offer of financial solutions to our clients was the acquisition in May 2011 of a 50.1% stake in SGEF, a leading provider of asset-backed financing in the Czech Republic and through its branch is active also in Slovakia. In July 2016, KB's subsidiary ESSOX concluded the acquisitions of 100% ownership stakes in the PSA Finance CZ and PSA Finance SK automotive finance companies.

# Société Générale Group

Komerční banka has been an important part of Société Générale Group's international retail banking since October 2001. Société Générale is one of the largest European financial services groups. Based on a diversified universal banking model, SG Group combines financial solidity with a strategy of sustainable growth, and aims to be the reference for relationship banking, recognised on its markets, close to clients, chosen for the quality and commitment of its teams.

Société Générale has been playing a vital role in the economy for 150 years. With more than 145,000 employees, based in 66 countries, SG Group serves 31 million clients throughout the world on a daily basis. Société Générale's teams offer advice and services to individual, corporate and institutional customers in three core businesses:

- Retail banking in France with the Société Générale branch network, Credit du Nord and Boursorama, offering a comprehensive range of multichannel financial services on the leading edge of digital innovation;

- International retail banking, insurance and financial services to corporates with a presence in emerging economies and leading specialised businesses; and

- Corporate and investment banking, private banking, asset management and securities services, with recognised expertise, top international rankings and integrated solutions.

Société Générale is included in the main sustainability indices: DJSI (World and Europe), FTSE4Good (Global and Europe), Euronext Vigeo (World, Europe and Eurozone), ESI Excellence (Europe) from Ethibel, four of the STOXX ESG Leaders indices, and the MSCI Low Carbon Leaders Index.

# Profile of KB

Komerční banka is the parent company of KB Group and is a member of the Société Générale international financial group. KB ranks among the leading banking institutions in the Czech Republic, as well as in Central and Eastern Europe. It is a universal bank providing a wide range of services in retail, corporate and investment banking. Member companies of Komerční banka Group provide additional specialised financial services, such as pension savings and building society schemes, leasing, factoring, consumer lending and insurance. These are accessible through KB's branch network, its direct banking channels, and the subsidiaries' own sales networks. The Bank also provides services in the Slovak Republic through its branch focused on serving corporate clients as well as through selected subsidiaries.

| | Loans to clients (gross loans)* | | Amounts due to customers | |
|---|---|---|---|---|
| CZK billion | 31 December 2016 | 31 December 2015 | 31 December 2016 | 31 December 2015 |
| **KB Group** | **595.4** | **548.2** | **699.4** | **656.3** |
| KB – total (including KB Slovakia) | 539.1 | 496.4 | 638.4 | 593.1 |
| – Individuals | 231.0 | 206.6 | 230.1 | 196.2 |
| – Businesses (including KB Slovakia) | 308.1 | 289.8 | 408.3 | 396.9 |
| – Small businesses | 32.4 | 30.9 | 159.9 | 145.1 |
| – Medium corporates and municipalities | 105.6 | 104.9 | 142.2 | 142.3 |
| – Top Corporates and other (including KB Slovakia) | 170.1 | 154.0 | 106.2 | 109.4 |
| Modrá pyramida | 38.8 | 37.0 | 64.1 | 68.5 |
| ESSOX (including PSA Finance) | 14.8 | 9.3 | n.a. | n.a. |
| Factoring KB | 7.5 | 6.1 | n.a. | n.a. |
| SG Equipment Finance | 25.8 | 24.5 | n.a. | n.a. |
| Bastion | 3.1 | 3.2 | n.a. | n.a. |
| Consolidation and other adjustments | (33.6) | (28.1) | (4.1) | (5.8) |

* excluding Other amounts due from customers

# The Bank's identification details as of 31 December 2016

Komerční banka, a.s., entered in the Commercial Register maintained with the Municipal Court in Prague, Section B, File No. 1360

**Date of registration:**
5 March 1992

**Registered office:**
Prague 1, Na Příkopě 33, building identification number 969, postal code 114 07

**Identification number:**
45317054

**Legal Entity Identifier (LEI):**
IYKCAVNFR8QGF00HV840

**Legal form:**
Public limited company

**Business activities:**

I. The Bank shall carry on business pursuant to Act No. 21/1992 Coll., the Banking Act, as amended. The business activities of the Bank shall include:
   a) acceptance of deposits from the public,
   b) granting of loans,
   c) investing in securities on the Bank's own account,
   d) financial leasing,
   e) making and receiving payments and administration of a clearing system,
   f) issuing of payment instruments, such as payment cards and traveller's cheques,
   g) provision of guarantees,
   h) issuing of letters of credit,
   i) provision of collection services,
   j) provision of investment services including:
      - main investment services of reception and transmission, on behalf of investors, of orders in relation to one or more investment instruments,
      - main investment services of execution of orders on behalf of investors in relation to one or more investment instruments,
      - main investment services of dealing in investment instruments for the Bank's own account,
      - main investment services of managing portfolios of investments in accordance with mandates given by investors on a discriminatory, client-by-client basis where such portfolios include one or more investment instruments,
      - main investment services of underwriting in respect of issues of investment instruments and/or the placing of such issues,
      - ancillary services of safekeeping and administration in relation to one or more investment instruments,
      - ancillary services of safe custody,
      - ancillary services of granting credits or loans to an investor for the purpose of allowing the investor to carry out a transaction in one or more investment instruments wherein the firm granting the credit or loan is involved in the transaction in relation to the investment instrument
      - ancillary services of advice to undertakings on capital structure, industrial strategy and related matters and advice and service relating to mergers and the purchase of undertakings,
      - ancillary services related to underwriting,
      - ancillary services of investment advice concerning one or more investment instruments,
      - ancillary services of foreign-exchange service where these are connected with the provision of investment services;
   k) dealing on the Bank's own account or on the client's account in foreign currencies and gold,
   l) financial brokerage,
   m) foreign exchange operations (purchase of foreign currency),
   n) provision of depository services,
   o) provision of banking information,
   p) renting of safe-deposit boxes,
   q) issuing of mortgage bonds,
   r) activities directly related to those mentioned in paragraphs a) – q).

II. Furthermore, the business activities comprise activities carried out for another as long as these activities relate to the operation of the Bank and to the operation of other banks controlled by it, of financial institutions and of businesses which provide ancillary banking services in the scope specified below:
   a) accounting consultants activities, book-keeping, tax record keeping,
   b) procurement of deals,
   c) advisory and consulting activities, preparation of expert studies and reports,
   d) administration and maintenance of real property,
   e) organisation of specialised courses, training, and other educational programmes including teaching,
   f) provision of software, advisory in information technologies, data processing, hosting and relating activities and web portals,
   g) administration and organisational services.

**Registered capital:**
CZK 19,004,926,000; of which paid up: 100%

**Method of the Company's establishment:**
In accordance with the privatisation project of the state financial institution Komerční banka, with its registered office at Prague, Na Příkopech 28, approved by resolution of the Government of the Czechoslovak Federative Republic No. 1 of 9 January 1992 and No. 109 of 20 February 1992, the National Property Fund of the Czech Republic, as the sole founder, established the public limited company Komerční banka, a.s., based on the Deed of Incorporation of 3 March 1992 under Sec. 172 of the Commercial Code.

**Foreign branch:**
Name: Komerční banka, a.s., pobočka zahraničnej banky
Registered office: Bratislava, Hodžovo námestie 1A,
postal code 811 06, Slovak Republic

# Report of the Board of Directors on the Bank's and Group's business activities and financial position

## Vision and mission

**Long-term mutually beneficial relationships with clients and other stakeholders**
Komerční banka is a universal bank based on a multi-channel model. KB presents to its clients a comprehensive range of financial products and services. Through unceasing innovation, the Bank endeavours to meet its customers' evolving needs while tailoring its offer to suit specific clients.

**To create value for clients, shareholders and employees and to serve the economy**
KB focuses on continuously developing its business activities while prudently managing the related risks. Co-operation with other members of KB Group, with companies from SG Group, and with other, independent partners enables the Bank to provide highly sophisticated products and gives it a flexibility that is indispensable in a constantly changing environment. The excellent know-how and experience of the Group's employees ensure that the products portfolio is fully relevant and competitive. At the same time, Komerční banka is aware of the responsibilities stemming from its position as a leading Czech financial institution.

## Declaration on principles of corporate social responsibility

**Code of conduct**
Komerční banka recognises that only by taking an ethical approach to doing business and providing financial services can it hope to maintain and even strengthen its position in the banking sector. The Bank also acknowledges that a fundamental prerequisite to successfully developing the company consists in professional conduct and behaviour on the part of its employees, as exemplified in particular by fostering and preserving direct and open relationships with clients as well as by fortifying the mutual trust between KB and its clients. Komerční banka expects its employees to be fully aware of and committed to their obligation to act in accordance with the ethical standards set forth in its Code of Ethics – which applies to all KB employees without exception – and to endeavour always to adhere to those standards.

**Corporate governance**
Komerční banka adheres to and voluntarily upholds all the principal standards of corporate governance in compliance with *the Corporate Governance Code* based on the OECD principles as amended in 2004 and issued by the Czech Securities Commission. The Czech wording of the Code as amended is available on the websites of the Ministry of Finance of the Czech Republic at **www.mfcr.cz** and of the Czech National Bank at **www.cnb.cz**.

**Sustainable development**
Komerční banka is aware of the influence that its activities have on the surroundings wherein it operates, and it considers responsible behaviour to be important. Therefore, it adopts adequate measures which on the one hand should eliminate negative influences on the environment and on the other contribute to its protection and improvement. KB monitors the impact of its activities on the environment and identifies those areas upon which it needs to focus. Komerční banka then adopts measures directed to effectively reducing its environmental impact.

# Major events of 2016

## January

KB was recognised as providing the best services for business and export as it was named *Best Trade Finance Bank* in an annual award of Global Finance magazine.

KB Penzijní společnost prepared the supplementary pension savings offer for children. The parents or grandparents can conclude the contract on behalf of the children.

Komerční banka became the first bank on the Czech market to offer start-ups financing for their projects in co-operation with the European Investment Fund. Clients need not document their business histories, and a good business plan is enough for obtaining credit.

Modrá pyramida introduced for its clients dynamic biometric signature, which improves security and efficiency of the contracting process. Biometric signature's introduction was a part of extensive digitalization and automatization of operating processes in Modrá pyramida.

## February

Komerční banka and Worldline SA agreed to form a partnership to provide merchant acquiring and payment processing services to retailers under the brand name KB SmartPay. The alliance combines strengths of Wordline's digital payment products and platform with KB's entrenched relationships with commercial clients.

Finparada.cz named KB as offering the *Financial Product of the Year 2015* in recognising the Trusteer Rapport tool from IBM that the Bank provides free of charge to its clients. The software enhances protection of clients' devices and minimises the risk for abuse of login information for online banking.

At the very same time as the Apple Watch was launched on the Czech market, Komerční banka introduced a new banking application for this smart watch.

Komerční banka joined the largest project geared towards providing assistance to Czech craftsmen: The Year of Crafts 2016, which has been declared by the Association of Small and Medium-Sized Enterprises and Crafts of the Czech Republic.

## March

With support from the European Investment Bank, KB became the only bank in the Czech Republic to begin providing advantageous EuroEnergie loans to help small and medium-sized enterprises finance energy saving projects.

Again co-operating with the European Investment Bank, Komerční banka launched an offer of advantageous financing to firms in the Czech Republic employing young people up to 30 years of age.

Komerční banka extended its co-operation agreement with the Association of Private Farming CZ.

## April

Via acquisition of 100% ownership in PSA Finance Czech Republic and PSA Finance Slovakia  from Banque PSA Finance, ESSOX entered the market of financing new cars. Both acquired companies provide financing for PSA Groupe's Peugeot, Citroën and DS car brands. The two companies have been consolidated in KB Group accounts from 1 July.

At the General Meeting on 22 April, Komerční banka's shareholders ratified the Board of Directors' proposal to approve the reported profit and distribution of the 2015 dividend of CZK 310 per share.

The General Meeting also approved a share split in the ratio of 5:1. The split took legal effect on 25 April 2016 with its entry into the Register of Companies. Shareholders received five new shares with nominal value 100 CZK in place of each old share with nominal value 500 CZK. The split shares began trading on the Prague Stock Exchange on 12 May 2016.

## May

Joining forces with the Association of Small and Medium-Sized Enterprises, KB launched the fourth year of the *Start up!* grant programme for young and beginning entrepreneurs, whereby the Bank provides them with financing, expert advice, as well as financial, legal and marketing support.

## June

The programme of Komerční banka's Global Depositary Receipts (GDRs) registered under ISIN US5004594090 and US5004591021 was terminated as of 3 June 2016,. The adoption of the GDRs for trading at the London Stock Exchange was cancelled on 30 March 2016. The Board of Directors had approved these steps in January. Improvements in the Czech Republic's institutional framework and integration into the European Union's regulatory environment have eliminated the need to provide this additional layer of assurance to investors through listing on a developed stock market.

With the *MojePojištění majetku* (My Property Insurance) policy, Komerční pojišťovna entered the market for residential property, household and household liability insurance. The new product is unique in eliminating the risk of underinsurance. Instead of the client's designating a level of insurance coverage, KP reimburses the full cost of renovation in case of an insured event.

## July

Jana Hanušová, who is also statutory representative of ESSOX, became statutory representative of PSA Finance Czech Republic. Jean-Philippe Vincent became CEO of PSA Finance Czech Republic. Jana Hanušová and Mária Kováčiková were named statutory representatives of PSA Finance Slovakia. Mária Kováčiková also became CEO of the company.

KB was awared third place in the Sodexo *Employer of the Year competition* in the category for companies with more than 5,000 employees.

## August

With effect from 2 August, the Supervisory Board named Jan Pokorný as a new member of Komerční banka's Board of Directors with responsibility for Structured Financing, Top Corporations and Investment Banking. He replaced Karel Vašák, whose mandate expired at this date.

KB became banking partner of the first business incubator of the European Space Agency in the CEE countries. Over the next five years KB will provide preferential credit financing for up to 25 start-up companies focused on employment of space-based technologies into everyday life.

In co-operation with Visa and Worldline, KB introduced a payment card in a mobile phone - MojeMobilní karta - for contactless payments using the Host Card Emulation technology.

A new generation of the Mobilní banka mobile banking application brought to clients more tools, more information about the clients' products both within the Bank itself as well as at KB's subsidiaries, and a more intuitive navigation.

KB launched fully on-line offering of KB Business World credit card for entrepreneurs - without need to visit a branch. The application is processed and necessary documents signed electronically through client's internet banking.

## September

As part of KB SmartPay alliance roll-out, Komerční banka concluded the sale of an 80% stake in its subsidiary Cataps to Worldline SA/NV. Before the sale, Cataps had assumed Komerční banka's activities in credit and debit card payment processing services (merchant acquiring). Clients will see an improved product offer, including expanded card acceptance for web payments and further simplification in using payment services.

KB took third in the Best Bank contest conducted by the daily newspaper Hopodářské noviny and took third place in the *Most Client-Friendly* category. Furthermore, KB took the second place in the category the *Banking Innovator* in recognition of its application for Apple devices.

Komerční banka introduced a new package, Profi účet GOLD (Profi GOLD account), which includes in addition to covering the basic banking needs of large and growing companies as well as all withdrawals from ATMs both domestic and abroad.

## October

CNB introduced stricter recommendations for new mortgages. The loan-to-value (LTV) ratio was reduced from 100% to 95%. Subsequently, the ratio will be cut to 90% from 1 April 2017.

Komerční banka introduced a solution for a new mandatory electronic reporting of sales by merchants in the Czech Republic (EET).

KB and the Association of Small and Medium-sized Enterprises prolonged their co-operation. The major collaborative areas will be support for start-up businesses, easier drawdown of EU subsidies, and assistance to enter successfully into and operate on foreign markets.

Following abolition of the 2nd pillar of the pension system in 2016, pension companies started paying out the clients's savings.

## November

Komerční banka was named the Bank of the Year in the Fincentrum Bank of the Year competition. Albert Le Dirac'h also scored a victory in the category *Banker of the Year*. At the same time, KB second took places in the categories *Most Trusthworthy Bank* and *Online Bank* and third place in the category *Private Bank of the Year*. The success was supported by third place of KB Penzijní společnost in the category *Pension Company of the Year*.

## December

On 1 December, new Consumer Credit Directive took effect. It brings many changes for both consumers and banks in the area of mortgages and consumer lending.

To secure client's mobile devices against malware infections and phishing attacks, KB, as the first bank in the Czech Republic, provided its clients at no charge with a state-of-the-art tool developed by IBM.

## Year 2017

KB announced the sale of its fully owned subsidiary NP 33 (the headquarters building on the street Na Příkopě in Prague).

# Macroeconomic development in 2016[1]

The growth rate of the Czech economy decreased by half in 2016 compared with the extraordinary result of 2015. Supported as it was by both domestic and foreign demand, that expansion was nevertheless broadly based. The one exception was seen in declining investment spending. The Czech economy faced no major macroeconomic imbalances during 2016, and the inflation rate began to realign itself with the inflation target of the Czech National Bank in the final months of the year. The economy achieved record-high figures for the foreign trade surplus and the current account within the balance of payments. Despite the healthy macroeconomic environment, the central bank continued its extremely easy monetary policy and therefore interest rates within the economy remained very low.

Despite increased geopolitical risks in 2016, Czech exporters enjoyed robust external demand and the CZK/EUR rate was stable due to the floor enforced by the central bank. The external trade surplus (as measured by the national methodology) reached a record CZK 183.9 billion, which represents an annual improvement of CZK 52.9 billion. While exports grew by 1.2%, imports even slightly decreased (–0.2%). Smaller imports were due both to lower prices of imported commodities and to a dip in investment imports. The most important export destination remains the European Union, with a share of 84.0%. More specifically, the euro zone accounted for 65.5% of Czech exports in 2016. Among individual countries, Germany is the leader and accounted for 32.2% of exports. The success of foreign trade in goods and services contributed to 2016's overall current account surplus, which, at 1.6% of GDP, was the largest on record.

The structure of GDP shows that increasing net exports helped to offset a decrease in fixed investments, which was quite significant in 2016. The decline results from a high statistical base in 2015, which year marked the last opportunity to draw financing from EU funds for the 2007–2013 programming period. Insufficient readiness of projects financed from public funds and a slow take-off of new programmes for the period 2014–2020 greatly influenced the contraction within the engineering segment (–16.0%) during 2016. Overall, construction output declined in real terms by 7.6% during the year. Building construction was down by 3.3%, especially because developers in Prague are facing administrative obstacles relating to the city's obsolete zoning plan. Lower investment and construction activity also had negative effects on industrial production in 2016. Industrial output climbed by just 2.9%, and that growth was driven especially by the successful automotive industry. Production of motor vehicles rose by 11%. In contrast, due to low commodity prices, mining industry output dropped (–9.0%). Meanwhile, production in the chemical industry (–7.0%) was affected by accidents at the refineries in Kralupy and Litvinov.

Household consumption was the most important driver of the Czech economy in 2016. Consumer sentiment approached record high levels, driven up mainly by favourable labour market development. The employment rate reached an all-time high. Extremely low unemployment – which is becoming in many cases an obstacle to greater investment activity – resulted in upward pressures on wages. Wages growth exceeded 4% in nominal terms during 2016. The rising disposable income led to both higher consumption and savings by households and drove investment into the real estate market, resulting in rising prices for apartments. Growth in retail sales (excluding motor vehicle sales) reached 5.6% in real terms for the year while sales of motor vehicles were up even by 8.6%. The service sector expanded in real terms by 1.2% overall in 2016.

Inflation remained low through almost all of 2016, and average inflation for the year stood at just 0.74%. The final months of the year nevertheless saw a substantial acceleration in the price dynamics. On a year-on-year basis, consumer price inflation reached 2.0% in December. That figure is right on the CNB's inflation target. This rise in inflation was caused by gradual fading of the beneficial shock from low fuel prices, increasing food prices and, last but not least, price growth in core inflation. The rising core inflation reflected the strong consumer demand driven by growth in wages.

The CZK/EUR exchange rate was extremely stable in 2016 with the exception of a few weeks after the referendum on Brexit and after election of the new president in the United States. In a freely floating exchange rate regime, economic growth accompanied by surpluses in foreign trade and on the balance of payments would cause currency appreciation. By continuing its policy of exchange rate commitment through 2016, however, the Czech National Bank defended the Czech crown against strengthening below CZK 27 per euro. Especially in the second half of the year, financial investors started to test the exchange rate commitment and the CNB was forced massively to increase the volume of its currency interventions. Buying of euros by the central bank and expectations for crown appreciation after the end of the exchange rate commitment resulted in a strengthening of the Czech crown on the forward market and lower availability of long-term financing in euros. As a result, the cost of currency hedging increased for Czech exporters and there was a massive inflow of capital from abroad to purchase Czech government bonds.

Especially bonds with short maturity were in huge demand, reflecting bets on a stronger crown and low-cost CZK funding available for foreign investors. Yields on short-term Czech bonds fell to below minus 1%, making them the most expensive bonds in the world. At the long end of the yield curve, yields were declining until September 2016, but then the situation turned around. Higher inflation and growth in yields on foreign bonds ended the trend of ever-declining yields which had existed

1 Sources of primary data in this chapter: Czech Statistical Office, Czech National Bank.

since 2011. Until the end of the summer in 2016, the trend of the CZK swap curve was decreasing, as well, due to the continued decline at the long end. Near the end of the year, this trend reversed, due to higher inflation and higher EUR yields. At the same time, there was speculation about a possible rate cut by the CNB into negative territory and that conjecture influenced the short end. The yield curve was therefore steepening toward the end of the year.

## Main assumptions for 2017

In its baseline scenario, Komerční banka anticipates that the Czech economy will grow in 2017 by 2–3%, thus at a pace similar to that in the previous year. The structure of the economy's dynamics will nevertheless change: after dropping in 2016, fixed investment should gradually recover as public and private investors are set to embark on projects from the new programming period for EU funds. Fixed investments tend to be import-heavy and, consequently, the contribution from net exports to GDP growth will probably turn slightly negative. Inasmuch as 2017 is an election year, the economy will receive fiscal stimulus in the form of increased government spending for public sector wages, social benefits and contributions to the health care system. Household consumption will continue to be the key driver of growth in the Czech economy, underpinned by record high employment rates and rapid growth in wages.

Industrial production should still benefit during 2017 from growing external demand, and the greater fixed investments should have positive impacts as well. Activity and growth in the industrial sector should thus accelerate slightly compared to 2016. The construction sector should pick up modestly in 2017 after dropping significantly in 2016 due to the decrease in public infrastructure investment and administrative obstacles to new construction.

The healthy economy is pushing down the unemployment rate. During 2016 and into the beginning of 2017, various sectors of the economy already were suffering from a lack of workforce. The labour shortage is putting upward pressure on wages. This is expected to lead to an increase in the average nominal wage within the economy by more than 4% in 2017, even slightly exceeding the wages growth recorded in 2016.

Consumer price inflation accelerated sharply at the turn of 2016 and 2017 due to the effect of a low base for food and fuel prices one year earlier. Inflation during 2017 will be influenced to a large extent by import prices. Although anticipated CZK appreciation should have an anti-inflationary effect, expected weakening of the euro vis-à-vis the US dollar, on the other hand, would be pro-inflationary. Overall, CPI should fluctuate around the monetary policy target of 2% for most of 2017.

Rising inflation should prompt the Czech National Bank to exit from the exchange rate floor set for the Czech currency in November 2013. The timing of that exit will depend on the inflation forecast. KB expects that before the exit, the CNB may create a new facility for interbank liquidity with a negative interest rate while limiting entry into existing facilities and clearing accounts with unchanged rates. The measure is likely to be applied only temporarily around the time of exit in order to deter inflow of speculative capital. The measure would move PRIBOR rates down, too. Long-term rates should, however, already reflect the increasing inflation expectations and move up moderately.

The stability in the CZK exchange rate that resulted from the FX floor will vanish with its exit. KB's model for the long-run equilibrium exchange rate indicates potential for the Czech currency to appreciate. On the other hand, because speculative capital will play the key role at the time around the exit, the volatility of the EUR/CZK currency pair can be expected to increase significantly. Sooner or later, arbitrageurs will close their long CZK positions, and that can be associated with risk for a temporary but potentially significant weakening of the Czech currency. The appreciation trajectory should therefore be gradual.

Growth in bank lending should be bolstered by robust confidence among households and businesses, as well as the still favourable financing costs. On the other hand, the recent prudential measures of the Czech National Bank, such as its imposition of a countercyclical capital requirement and a cap on the ratio of mortgage loan volume to value of the collateral (LTV), seek to slow the growth of lending on the market. Short supply of housing units, and especially so in Prague, is seen as another factor limiting growth in mortgage lending. That market is thus expected only slightly to outpace the nominal GDP growth.

Deposit market growth is expected to decelerate significantly, mainly due to reduced government deposits and likely outflows of capital in the second half of 2017 after the CNB's floor regime comes to an end.

Competition on the Czech banking market, which is characterised by excess liquidity, will remain intense. Indeed, it will become even more so due to a proliferation of technology companies offering various financial services and sometimes exploiting the much more relaxed regulation of firms outside the traditional financial sector.

# Strategy and priorities for 2017

Komerční banka is developing a universal-banking model focused upon meeting the financial needs of its clients. This strategy is based on building long-term, mutually beneficial relationships with its clients, thereby allowing the Bank precisely to identify dynamic changes in clients' needs and expectations while constantly adapting its services offer in accordance with this knowledge in order further to boost clients' satisfaction. Within that model, KB's investment banking activities are dedicated to serving clients and are constrained by conservative limits.

In 2017, Komerční banka will continue to develop its client-centric business model. That work builds upon several pillars providing support to that model across the Group:

In an environment marked by margins under pressure due to strong competition, low interest rates and expanded consumer protection initiatives, growth in the volume of business activities is essential for maintaining the revenue base. KB aims to maintain sound development of its client base while focusing especially on increasing the number of active clients. Komerční banka's strong capital, liquidity and operating capability, as well as the improving efficiency of its credit-granting processes, should enable it to continue its growth in lending across the main client segments and product categories and to gain further market share in select areas, including lending to consumers and small businesses. New solutions will be presented to seize opportunities in the corporate segment while effectively utilising the Bank's available capital. In a market where most clients prefer safe investments for their savings, the Group will be offering trustworthy, long-term solutions.

KB seeks to be recognised on the market for delivering simple and value-adding services, providing quality advisory and offering new and relevant products. Inasmuch as payment transactions have already been successfully switched to digital channels, activities in 2017 will mainly focus on developing capabilities for selling financial products via the internet and mobile channels. To assure positive experience for clients, it is essential that availability, reliability and security of internet and mobile banking be strengthened continuously. Because the branch network remains the main base for building mutual relationships with clients, the Bank continues in adapting the design of its branches to enhance the privacy and efficiency of servicing clients. This commercial setup is completed by call centres providing value-added services even during extended hours. KB's customer-friendly approach extends to simplifying client contractual documentation and introducing uncomplicated and advantageous products and bundles. It is manifested, too, in a new marketing communication concept. In order effectively and efficiently to address the differing needs and expectations of various client groups, KB will work take full advantage of the updated client segmentation in retail banking.

Komerční banka's subsidiaries leverage on the Bank's capabilities to distribute their products. When effective to do so, they also develop their own complementary distribution channels. The Bank's largest subsidiary, Modrá pyramida, will focus on growing the production of loans booked on its own balance sheet, further developing its distribution of KB Group products and adjusting its funding costs. ESSOX is pursuing a transformation programme that will allow it to evolve successfully within the expanded possibilities opened up by its recent acquisition of PSA Finance in the Czech Republic and Slovakia and in the changing and competitive industry of non-bank consumer financing. Meanwhile, Komerční pojišťovna, in addition to its traditional life insurance products, will expand within the property insurance sector via the new offer launched in 2016.

To remain competitive in the environment marked by rapid and often disruptive changes, KB's people must embrace a mindset emphasising simplicity and agility. The corporate culture must reflect Komerční banka's core values of team spirit, innovation, commitment and responsibility. In addition to competitive remuneration and professional skills training, KB is developing programmes directed to improving employee motivation. The Group also is investing substantially into improving the competence of relationship managers and equipping them with the most useful information and tools. New digital tools facilitate communication and co-working; goals are shared in order to promote team spirit. Innovation initiatives will be more easily created within KB's new Innovation Lab – a dedicated space to facilitate teaming up with universities, start-ups and fintec companies in an open-minded atmosphere. The internal capabilities will be further supported by advancing data-mining and analyses, mutualisation and sharing of support functions, as well as agile and efficient project development and implementation methodologies.

Cost efficiency is pursued through bolstering productivity and cost discipline. Continuing simplification of processes and upgrading technological equipment within the distribution networks are freeing up capacity for commercial activities and helping to grow the volume of business activities per employee. The fast pace of change in technologies used in the banking industry is captured in Komerční banka's IT transformation programme, whereby selected key elements in the IT infrastructure are progressively updated or replaced. Ongoing change is generally funded from depreciation and amortisation. Consistent sourcing processes allow the Bank to benefit fully from technological progress and changes of relative prices. At the same time, employee remuneration reflects intense labour market competition for talent and the Bank is allocating adequate resources to develop the future growth drivers for the Group's business.

KB's risk management is pursuing a prudent and balanced approach to all types of risks assumed. It aims to support development of the Group's business activities, and that includes sustainably growing its lending activities while reinforcing the Group's market positions. The objective is to ensure profitable lending and market activities across the business cycle while at the same time preserving a sound balance sheet.

As in previous years, the Bank will meet all its regulatory obligations. KB must address new regulatory initiatives in the most efficient manner. The Group will make itself ready to face successfully the regulatory challenges (such as the revised Payment Services Directive) which are changing the landscape of the financial industry.

## Main challenges and risks for the Bank and Group in 2017 and expected developments in the financial situation

Komerční banka Group is a complex undertaking which is naturally subject to a whole array of risks ranging from economic, competitive, regulatory and reputational risks to operational, capacity, counterparty, legal, market and credit risks. It may also be impacted by human error or fraud, insufficiency of skills and experience, or flawed management decisions. Not least, it may incur losses resulting from unforeseen or catastrophic events.

The Group's business model has proven itself robust. Komerční banka's capital and liquidity include adequate buffers to absorb unexpected adverse market developments. Credit-granting standards have been calibrated to assure the Bank's satisfactory performance even in the declining phase of the business cycle. KB's hedging policy mitigates the short-term impact of interest rate fluctuations. Its funding is assured due to its broad and stable base of client deposits. Placements of free liquidity are confined by strict limits, and these are directed mostly to operations with the Czech National Bank and to government bonds. KB's risk management strategy and techniques are further elaborated in the respective chapter of this annual report.

Reflecting Komerční banka's systemic importance on the Czech banking market, its performance is closely linked with that of the Czech economy and, to a lesser extent, the Slovak economy. Both are open economies that are fully integrated into the EU's internal market. Should the Czech economy develop more poorly than expected as of the beginning of 2017, KB's results would be affected negatively. Slower growth in the economy would lead to decelerating growth in business volumes, stagnation or even modest decline in recurring revenues along with a rise in risk costs. Average risk weights of assets would increase, and that could bring a slight weakening in capital adequacy ratios. The Group's operations should remain profitable even in an alternative negative scenario of economic recession. The outlook for the Czech economy remains solid. The main sources of economic uncertainty for 2017 can be identified to include impacts from the CNB's expected removal of the floor under the Czech crown. An abrupt appreciation of the Czech crown would result in a negative shock for the Czech economy, which is heavily dependent on industry and exports. The United Kingdom is expected to begin negotiating its departure from the European Union. Although this can lead to a certain disruption in trade and decrease in EU funds available for the Czech Republic, such probably would not yet occur in 2017. With its 5.3% share of total Czech exports, the UK is the Czech Republic's fourth largest trading partner.[1]

Net interest income is the most important source of KB's revenues. The Bank has in place a long-term hedging policy for interest rate risk which has proven its effectiveness. Nevertheless, the persisting situation of very low interest rates has been affecting KB's interest income negatively. This impact has been offset by rising loan and deposit volumes.

In 2017, Komerční banka's management expects the Group's overall loan portfolio will expand at a year on year rate just slightly slower than in the previous year. The housing loans category will be somewhat affected by limitations established by the CNB, but their effect should not be striking inasmuch as the overall economic conditions should remain favourable. As would be consistent with recent periods, KB aims to outperform the market in expanding its portfolios of consumer loans and loans to small businesses. In corporate segments, the growing economy and recovering fixed investments should support demand for financing even though acquisition and structured deals may not match the high volumes of 2016. The overall deposit volume will be affected by the next step in centralising deposits of certain public corporations within the central bank. Some impact should be expected also from the flows of short-term money around the time of exit from the CZK floor. The increase in deposits should therefore be slower than in 2016.

Based on the above assumptions, net interest income should reach a similar level in 2017 as in the previous year. Should rates decrease significantly from the levels observed at the beginning of the year, pressure on the Group's net interest income would build. Still, thanks to KB's hedging policy, the effect would occur only gradually and relatively slowly.

1 In 2015. Source: Czech Statistical Office

In recent years, KB has reduced prices for many financial services and introduced product bundles with very attractive pricing. This was made possible by technological progress that boosted the overall productivity. It also reflected intense competition from established and new banks and increasingly even from on-line providers of financial services (so-called “fintech” companies). Competition on the market remains intense, but the Bank has been able to grow the number of clients as well as the volumes of loans and assets under management. This can be attributed to the enhanced value of services delivered to clients and KB’s consistent and reasonable pricing strategy. Consequently, the recurring income from fees and commissions should stabilise or even rise slightly in a year-on-year comparison. In September 2016, KB sold an 80% stake in its subsidiary Cataps, which had assumed KB’s card payment processing services (merchant acquiring). Because the respective fee income will not occur in the subsequent periods, reported fees and commissions may decline slightly in 2017. The proliferation of fintech companies presents potential risks, because such firms benefit from lower regulatory burdens compared to banks. Further strengthening of competition among banks themselves might also squeeze margins from banking products.

The upcoming end of the period during which the Czech crown’s appreciation has been prevented by CNB interventions will probably increase demand among clients for hedging of currency and interest rate risks. The prevailing perception that the crown should appreciate after the exit from the floor, however, may make it difficult to find willing counterparties for some hedging trades. The net profit from financial operations will thus again be driven mainly by hedging linked to credit provided to clients, foreign currency transaction traffic, and other financial market services provided to clients. The reported result will be lower by the extraordinary income generated in 2016 from disposal of KB’s stake in VISA Europe.

The Group has been able to manage effectively its operating expenditures in relation to revenues development. The Collective Agreement KB signed in December 2016 with trade unions for the year 2017 embraces the strategic vision also with employees for building long-term partnerships based on trust. Among other changes brought by the agreement, the average salary will increase in 2017 by more than 2% year on year. The number of employees and branches will not change much. Non-personnel expenses will reflect the inflation rate, which is picking up, but this will be offset in part by ongoing efforts for simplification, optimisation and synergies within all operations. Reported operating costs will be lower by the share attributed to the merchant acquiring business which was sold.

A growing economy, low unemployment and low interest rates are favourable conditions for the development of the cost of credit risks. From an already very insignificant level, KB expects only moderate normalisation of provisioning in the retail segments. Similarly to the situation in 2016, corporate provisioning may display certain volatility caused by individual instances of exposures requiring special review.

As of 1 January 2017, KB’s Overall Capital Requirement (OCR) stood at 15.4%. Within this total, the countercyclical buffer reached 0.5%, which level has been confirmed by the CNB also for the period beginning on 1 January 2018. The systemic risk buffer was increased in 2016 to 3% and, according to the relevant regulation, it should be reviewed at least once every two years. The conservation buffer was already at the so-called “fully phased-in” level of 2.5%, which in other countries was to be met by 2019. With a view to the near future, therefore, capital requirements seemed to be relatively stabilised nothwithstanding potential changes resulting from the annual Supervisory Review and Evaluation Process.

In the conditions envisaged at the start of 2017, management expects the Bank’s operations will generate sufficient profit in 2017 to cover the Group’s capital needs ensuing from its growing volume of assets as well as to pay dividends.

# Report on business activities

## Clients of KB Group and their service

At the close of December 2016, KB Group was serving 2.4 million clients on a consolidated basis. Standalone KB recorded 1,654,000 clients (+0.4% year on year), of which 1,398,000 were individuals. The remaining 256,000 customers were comprised of entrepreneurs, businesses and corporations (including municipalities and associations). Modrá pyramida was attending to 491,000 customers, and the number of pension insurance participants at KB Penzijní společnost reached 534,000. ESSOX's services were being used by 201,000 active clients, and services of PSA Finance in the Czech Republic and Slovakia by almost 17,000 clients.

Komerční banka's clients had at their disposal 392 banking branches (including one branch for corporate clients in Slovakia), 768 ATMs (of which 195 were deposit ATMs), plus full-featured direct banking channels supported by two call centres. The number of clients using at least one direct banking channel (such as internet or telephone banking) reached 1,387,000 by the end of December 2016 and corresponds to 83.8% of all clients. Customers held 1,595,000 active payment cards, of which 194,000 were credit cards. The number of active credit cards issued by ESSOX came to 113,000. Modrá pyramida's customers had at their disposal 216 points of sale and approximately 1,000 advisors. SG Equipment Finance (SGEF) was providing its leasing services via nine branches (two of which are in Slovakia), as well as through KB's network.

Komerční banka's business model is founded upon building long-term relationships with customers. KB Group perceives its competitive advantage on the banking market as consisting in the value of partnerships with clients, the ability of its banking advisors to provide high-quality advisory, a wide range of relevant and advantageous financial products, and proximity to clients via the branch network and advanced, secure direct banking.

KB is a universal bank with a multi-channel distribution model. For each segment, the Bank establishes a service model and access channels enabling clients to use digital solutions wherever important for them to do so. Digitalisation of the environment and related changes in client behaviour are also reflected in the way the branch network operates. This primarily concerns the long-term trend of shifting transaction and simple service activities plus sale of selected products to direct channels, especially to mobile banking. At the same time, the branch network continues to be a key channel for advisory, as well as for sales and service regarding such more complex products as mortgages and investments. Branches have and will continue to have an important role in financial advisory provided on the basis of client knowledge and banking advisors' expertise. They also continue to play a very crucial role in cash services.

The comprehensive branch reconstruction project continued during 2016 so that branches correspond better to the clients' changing needs. Emphasis is given to the clients' comfort and privacy in obtaining financial advisory. Eighteen branches received the new design in 2016, bringing to 64 the total number of branches the Bank has reconstructed in the new concept. In 2016, the role of deposit ATMs was markedly intensified as compared to that of standard cash desks at branches. Most large branches are now equipped with deposit ATMs. The Bank expects to continue extending the availability of deposit ATMs in 2017.

This network is further complemented by the subsidiaries' distribution capacities (especially those of Modrá pyramida) and, in the cases of selected products, also by the business partners' networks. Services and products of other KB Group companies are available within their own distribution networks, in the KB branch network, and potentially through the business partners.

Komerční banka adheres strictly to regulatory requirements in all areas of its activities, and it is developing the "know your client" concept, primarily through its banking advisors. Each client has his or her own banking advisor responsible for an assigned portfolio of clients and for developing the relationships with them. KB perceives knowing the client and the client's needs to be an integral part of the business relationship with the customers and a process reflecting the respect, responsibility and trust the Bank has in its clients. Knowledge of clients also provides a basis for the banking advisors to offer appropriate advisory and services corresponding to clients' actual needs. In this sense, the concept is a purely business activity directly influencing the customer experience, and especially at the beginning of the business relationship. Komerční banka is dedicating increased attention to training employees in this area and to continuously updating business processes so that they adequately serve to maximise business efficiency and ensure compliance with evolving regulatory demands.

The fundamental objectives in servicing clients are to ensure a long-term personal approach to each client, provide an offer of key products corresponding to the customer's actual needs, satisfy the clients' distinct needs, and provide individual financial advisory. Komerční banka is developing a system for detailed segmentation of customer relationships. The highest-level segments in the Bank are the following:

- Individuals,
- Small Businesses (the indicative criterion being annual turnover up to CZK 60 million),
- Corporates and Municipalities (annual turnover up to CZK 1.5 billion), and
- Top Corporations (annual turnover greater than CZK 1.5 billion).

A set of sub-segments within these segments is elaborated. In the retail banking segments, Komerční banka modified its service model during 2016 according to the needs of more closely defined customer groups, the objective being to allocate capacities so as most efficiently to meet the different client groups' various expectations.

## Selected business indicators

| Distribution network | 31 December 2016 | 31 December 2015 |
|---|---|---|
| KB branches | 392 | 397 |
| KB business centres | 10 | 10 |
| KB corporate divisions | 5 | 5 |
| MPSS points of sale | 216 | 215 |
| ATMs | 768 | 772 |
| out of which: deposit taking ATMs | 195 | 114 |

| Number of clients | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Komerční banka | 1,654,000 | 1,647,000 |
| – individual clients | 1,398,000 | 1,391,000 |
| – using at least one direct banking channel | 1,387,000 | 1,340,000 |
| Modrá pyradmida | 491,000 | 519,000 |
| KB Penzijní společnost | 534,000 | 545,000 |
| ESSOX | 201,000 | 219,000 |

| Direct channels | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Active direct banking products | 2,120,000 | 1,996,000 |
| KB Payment cards – active | 1,595,000 | 1,618,000 |
| – debit cards | 1,401,000 | 1,417,000 |
| – credit cards | 194,000 | 201,000 |
| ESSOX credit cards – active | 113,000 | 118,000 |

| Loans to clients – gross loans (CZK billion)[1] | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **KB Group** | **595.4** | **548.2** |
| KB – total loan portfolio | 539.1 | 496.4 |
| – Loans to individuals | 231.0 | 206.6 |
| – Volume of KB's mortgages | 207.8 | 185.2 |
| – Volume of KB's consumer and other loans | 23.2 | 21.4 |
| – Loans to small businesses | 32.4 | 30.9 |
| – Loans to medium corporates and municipalities | 105.6 | 104.9 |
| – Loans to top corporates and other loans[2] | 170.1 | 154.0 |
| Modrá pyramida - total loan portfolio | 38.8 | 37.0 |
| ESSOX – total loan portfolio (including PSA Finance) | 14.8 | 9.3 |
| Factoring KB – total loan portfolio | 7.5 | 6.1 |
| SG Equipment Finance – total loan portfolio | 25.8 | 24.5 |
| Bastion – total loan portfolio | 3.1 | 3.2 |
| Consolidation and other adjustments | (33.6) | (28.1) |

1) excluding Other amounts due from customers
2) Including loans provided by KB Slovakia

| Amounts due to customers and assets under management (CZK billion) | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **KB Group deposits** | **699.4** | **656.3** |
| KB deposits | 638.4 | 593.1 |
| – individuals | 230.1 | 196.2 |
| – small business | 159.9 | 145.1 |
| – MEM corporates | 142.2 | 142.3 |
| – top corporates and other deposits[3] | 106.2 | 109.4 |
| Modrá pyramida – building savings | 64.1 | 68.5 |
| Factoring KB | 1.0 | 0.5 |
| Consolidation and other adjustments | (4.1) | (5.8) |
| **Non-bank assets under management** | **151.8** | **139.9** |
| Assets under management in mutual funds[4] | 55.9 | 50.0 |
| Clients' assets managed by KB Penzijní společnost | 48.9 | 45.1 |
| KP life insurance technical reserves[5] | 47.0 | 44.8 |

## Selected operating indicators for Komerční banka

| | 2016 | 2015 |
|---|---|---|
| **Number of active[6] payment cards** | **1,575,000** | **1,618,000** |
| – debit cards | 1,384,000 | 1,417,000 |
| – credit cards | 191,000 | 201,000 |
| Volume of payments using KB cards (in CZK million) | 80,000 | 70,000 |
| Number of payments using KB cards | 102,098,000 | 83,994,000 |
| **Volume of cash withdrawals (in CZK million)** | **252,000** | **251,000** |
| – via ATM | 129,000 | 127,000 |
| – via non-ATM | 123,000 | 125,000 |
| **Volume of cash deposits (in CZK million)** | **300,000** | **311,000** |
| – via ATM | 12,000 | 7,000 |
| – via non-ATM | 288,000 | 303,000 |
| **Number of cash withdrawals** | **29,203,000** | **29,159,000** |
| – via ATM | 27,502,000 | 27,301,000 |
| – via non-ATM | 1,700,000 | 1,859,000 |
| **Number of cash deposits** | **6,889,000** | **7,469,000** |
| – via ATM | 730,000 | 485,000 |
| – via non-ATM | 6,159,000 | 6,984,000 |

3) Including deposits in KB Slovakia, other payables to customers and repo transactions
4) Assets of KB Group clients managed by third party asset managers
5) Komerční pojišťovna is consolidated by equity method.
6) Cards in circulation

## Selected awards

| | |
|---|---|
| **January 2016** | Best Trade Finance Bank from Global Finance magazine |
| **February 2016** | Financial Product of the Year 2015 for the Trusteer Rapport tool from Finparada.cz |
| **March 2016** | Sub-custody services 1st place in the Czech Republic in the category Unweighted in independent survey of Global Investor ISF magazine |
| **May 2016** | The FocusEconomics awards for accuracy of macroeconomic forecasts: |
| | 2nd place in the Best Overall Forecaster – Slovakia |
| | 3rd place in the Best Overall Forecaster – Czech Republic |
| **July 2016** | 3rd place in the Employer of the Year 2016 contest in the category for companies with more than 5,000 employees |
| **September 2016** | In the Best Bank contest conducted by the daily newspaper Hopodářské noviny: |
| | 3rd place in the category Best Bank |
| | 3rd place in the category Most Client-Friendly |
| | 2nd place in the category Banking Innovator |

| | |
|---|---|
| **November 2016** | In the Fincentrum Bank of the Year competition: |
| | 1st place in the category Bank of the Year, Banker of the Year |
| | 2nd place in the category Most Trusthworthy Bank |
| | 2nd place in the category Online Bank |
| | 3rd place in the category Private Bank of the Year |
| | 3rd place for KB Penzijní společnost in the category Pension Company of the Year |
| **January 2017** | In the Finparáda.cz Financial Product of the Year 2016 competition: |
| | KB Privátní správa aktiv 1 – Popular, best mutual fund in the category Short-term investment |
| | 2nd place for Komerční pojišťovna in the category Investment Life Insurance |

for Business clients

Internal efficiency

for Individual clients

Positive environmental, social impacts

## Individuals

Komerční banka is among the three largest banks in the Czech Republic by number of retail clients serviced[1]. Thanks to its long-term focus on advisory, it is perceived as a value-adding bank. In 2016, as in previous years, KB continued to develop its client-oriented approach and its product offer.

It was also due to these activities that Komerční banka won Fincentrum's prestigious award Bank of the Year 2016. Moreover, the Bank again confirmed by its standing in the independent Secure Account Navigator study[2] that it provides among the fairest consumer lending on the Czech market.

The competitive environment continued to intensify during 2016. So-called "new" banks continued actively to acquire new clients and position themselves in contrast to "traditional" banks. The trend of pressure for low prices continued, and especially so in the area of basic banking services. Activity increased across the entire financial services market in terms of the lending offer, loans consolidation, and refinancing. That, in turn, was significantly reflected in lower interest margins. Nevertheless, Komerční banka strengthened its own market position.

KB acquired more than 97,000 new clients in the Individuals segment, bringing the total number to 1,398,000. That represents a year-on-year gain of 0.5%. The Bank also maintains a prominent position in the children and youth segment, with more than 415,000 accounts.

The overall volume of loans from KB to individuals grew year on year by 11.8% to CZK 231.0 billion. Within this total, the portfolio of mortgages to individuals expanded by 12.2% to CZK 207.8 billion and the volume of consumer and other loans from KB to individuals rose by 8.4% to CZK 23.2 billion. Modrá pyramida reported growth of its portfolio by 5.0% to CZK 38.8 billion and the volume of financing by ESSOX including the portfolios of PSA Finance in the Czech Republic and Slovakia acquired in 2016 added 59.1% at CZK 14.8 billion.

Komerční banka is pursuing an objective to reinforce the perception of professionalism, trustworthiness, and modernness as to the services it provides. The Bank does not offer just separate products to individual clients but focuses on professional approach, is a partner in clients' decision-making, and offers advisory and solutions respecting their needs and requirements to the utmost, including the possibility of service through various channels. Each Komerční banka client has his or her own banking advisor who knows the client's needs. The unique Moje Plány (My Plans) application is used to assure this.

In 2016, Komerční banka changed the rules for clients segmentation, its objective being to provide clients with optimal service in accordance with their financial requirements. Specialisation of banking advisors by segments was made more precise in order better to reflect specific client needs. Employees in the teller section, too, received a new sales role as part of the new segmentation. The Bank also offered support in relation to investments in the form of a new role for investment specialists. This strategy exhibited excellent results in a number of areas despite the challenging market environment.

A number of activities continued during 2016 to be focused on innovations while making the product offer simpler and more transparent. The Bank brought to its clients new-generation mobile banking which includes protection for its clients. The new Mobilní banka (Mobile Bank) offers intuitive controls, faster input of payment orders, connection with products of the subsidiary companies, and the possibility to arrange a meeting with the client's bank advisor. In newly reconstructed branches, the arrangement of client zones corresponds to the changes in the approach to financial services. In these branches, among other things, services include remote support from specialists. The first specialised service offered was videoconferencing with an investment specialist.

The Bank also extended its offer of investment and insurance products. The range of investment possibilities was expanded, for example, to include CPR Global Silver Age, an equity fund directing its investments into fields related to the trend seen in the aging global population. In co-operation with Komerční pojišťovna, Komerční banka newly extended its product offer to include its own property and casualty insurance – MojePojištění majetku (MyInsurance for property). In consideration of clients' developing needs and greater need to purchase on-line, Komerční banka increased the number of products which can be obtained in that manner. On-line sales in 2016 accounted for 12% of consumer loans.

The competitive environment will continue to intensify during 2017, due to, among other reasons, the European Union's revised directive on payment operations which is currently being prepared. It is expected that a number of companies, particularly in the IT area, will begin to provide financial services. KB is working to prepare for this new era and to offer attractive solutions to clients which would further increase the added value in the services it provides.

One of the largest tasks for 2017 will be to maintain the trend in acquiring clients and maintaining, and potentially improving, the Bank's position on the market. Komerční banka will continue to simplify its processes while enhancing the quality of the services it provides as well as client comfort.

1 Source: KB's own market research
2 Source: Project of the advisory company EEIP and Charles University

## Private Banking

Komerční banka offers comprehensive Private Banking services to clients with financial assets exceeding CZK 20 million at its branches in Prague, Brno, and Ostrava as well as – if such clients prefer – outside the Bank's business premises. Clients with assets in excess of CZK 3 million have access to selected Private Banking products at 71 regional branches.

Services provided include in particular private portfolio management, a comprehensive range of investment instruments, first-class banking service, as well as real estate and Lombard loans for financing clients' private needs.

Private Banking achieved double-digit growth in the volume of assets under management during 2016. It strengthened its services directed to structuring family assets and multi-generational planning for asset transfer, and it assisted in sales of 36 companies valued at more than CZK 7 billion. Furthermore, it successfully completed subscription of qualified investors' funds investing into income-generating real estate (Realitní fond KB I) and private equity (KB Private Equity fund) on the Czech market. Realitní fond KB I (the real estate fund) focused on acquiring large commercial buildings in downtown Prague. These transactions ranked among the largest on the Czech market. Historically low interest rates also supported strong client demand for financing private projects.

Priorities for 2017 include to further develop portfolio management and investment advisory services, including to offer investment into funds for qualified investors. Private banking will also reinforce internal synergies utilising the global know-how of SG Private Banking's expert centres for open-architecture investment solutions. It will focus, too, on services to owners selling their companies, multi-generational structuring of assets, and building financial asset portfolios.

## Small Businesses

Komerční banka continued in activities aiming to reinforce its market position from the perspectives of client numbers, comprehensiveness of the offer, and market share of financing provided. Further expansion of the offer to and support for start-up entrepreneurs was also a priority.

During 2016, the Bank acquired 18,500 new clients, and the number of small businesses serviced came to nearly 244,000. Start-up entrepreneurs comprised 57% of new clients. The volume of financing provided continued to grow, thus reaching CZK 32.4 billion and representing a year-on-year gain of 4.8%.

The main source of growth can be seen in the increased number and volume of loans processed due to further simplification of processes both in relation to the clients and internally. At the start of the year, KB was the first bank on the market to present unique financing of start-up entrepreneurs using support from EIF and its guarantee programmes Microfinance and COSME. The new Profi loan Start enables provision of a loan to start-up entrepreneurs without a history, purely on the basis of assessing the business plan. During the year, almost 100 loans in a volume exceeding CZK 75 million were approved in this way.

During the year, Komerční banka continued in the Nastartujte se (Start up!) programme, which offers support to start-up entrepreneurs not only in the form of financial grants and access to expert advisory, but also an offer of advantageous services from non-banking partners.

Also in 2016, the Bank continued to co-operate and support the Association of Small and Medium-sized Enterprises and Crafts of the Czech Republic (AMSP) and the Association of Private Farming of the Czech Republic. Long-term co-operation with these partners allows the Bank to more accurately target and tailor its services to the clients' needs on the basis of acquiring feedback and to support the associations' members in various important projects. For example, Komerční banka was a partner of the AMSP Year of Crafts 2016 project wherein its activities and funds supported the activities of 23 professional associations and crafts guilds.

In 2017, Komerční banka will again focus on providing and developing practical solutions for its clients. That means supplying simple services at competitive prices for start-up and small businesses as well as more comprehensive solutions together with advisory from banking advisors for larger and growing companies with broader banking services needs. KB also is preparing to further simplify processes in client financing and to expand the availability of deposit ATMs.

## Corporates and Municipalities

In the Corporates and Municipalities segment, long-term client relationships, knowledge of the clients and their business models, and understanding for the environments within which they operate allow Komerční banka to recognise early changes in the customers' needs and accordingly to propose suitable solutions.

Even though the Czech economy grew in 2016, drawing from EU funds slowed substantially. Companies invested into expanding production capacities, renewing machinery and equipment, and acquiring other businesses. Companies financed current operations using their own growing financial resources, which was also apparent from the rising volume of corporate bank deposits. In the public sector, the lending volume decreased in relation to the slowdown in drawing from EU funds, and public sector deposits diminished after municipalities were forced to transfer some of their deposits to the Czech National Bank.

Komerční banka further strengthened its position during 2016 as the largest bank on the corporate financing market. According to a market survey, 43%[1] of small and medium-sized enterprises used the Bank's services. KB is also one of the two largest banks in public sector financing[2]. It is one of the most important partners for European financial institutions in the Czech Republic, and an exclusive partner in certain of their programmes[3].

A highly competitive environment and low interest rates again prevailed during 2016. Despite the challenging market conditions, the volume of financing provided added 0.6% as compared to the previous year to CZK 105.6 billion. Loans were growing most rapidly in real estate financing, financing of mergers and acquisitions, and for the retail, engineering, and automotive segments. In comparison with 2015, the volume of deposits declined by 0.1% to CZK 142.2 billion. The number of clients in the corporate segment remained stable, with the Bank servicing 10,100 clients at the end of 2016.

In addition to basic and structured financial products, Komerční banka provides its Corporates and Municipalities clients in selected sectors also with related expert advisory. In addition to banking advisors, the clients also have at their disposal specialists on foreign trade, trade finance products, EU subsidies, cash management, and investment banking. The KB Academy educational cycle is also a component of expert advisory.

Komerční banka also strengthened its on-line communication channels during 2016. After the success of the Mobile Bank Business application for mobile phones and tablets using the iOS operating system, Komerční banka extended the application to Android and Windows devices. It also allowed logging into the app by fingerprint and was the first on the market to introduce an app for Apple Watch. The Bank dedicates great attention to internet banking security, which clients value highly. IBM Trusteer Mobile security was newly made a standard part of the app for smartphones and tablets.

The **www.kb.cz** website got a new look that included the Corporates and Municipalities section. With its new organisation by section, visitors will more easily manoeuvre about the website and find those services they truly want and need. Selected sectors and services (EU subsidies and cash management) received spaces of their own where advisory service are available to visitors.

Funds from European financial institutions are designated for financing of publicly and socially beneficial projects and for developing small and medium-sized enterprises. The Bank may provide corporate and municipal clients with loans for such projects under more advantageous conditions. The offer of advantageous financing from European sources was expanded to include the EuroEnergie loan. Businesses can thereby benefit from the guarantee of the European Investment Bank and an advantageous interest rate for financing energy-saving projects.

In 2017, among other things, Komerční banka will co-operate with international financial institutions in providing advantageous financing and additional security. The Bank will continue expanding secure on-line services and communication channels. It will present the KB Advisory Point concept, whereby, in co-operation with advisory companies M.C.TRITON and Grant Thornton Advisory as well as other specialists, the Bank will offer comprehensive solutions and advisory for companies in various areas of their business. A platform will be launched during the year for exchanging and sharing practical and innovative solutions for corporates and municipalities.

## Top Corporations

Komerční banka's strategic objective in the Top Corporations segment is to maintain a leading position in provision of comprehensive banking services and to be the reference bank on the market for providing tailored solutions in the areas of financing, payment system maintenance, provision of bank guarantees, import and export letters of credit, and other services. Komerční banka provides its clients with a wide range of products and services, including highly specialised ones from investment banking as well as export and structured financing. At the same time, it brings clients comprehensive solutions for transactions unique on the banking market. KB's product offer is complemented by the offers from subsidiary and affiliated companies providing leasing, factoring services and supplementary pension insurance. KB clients value in particular the stable sales team for its reliability, professional approach and knowledge. In meeting the needs of top multinational clients, KB co-operates in creating solutions with expertise provided by Société Généralé Group. It also offers clients the possibility to use Société Généralé Group's extensive international network, in particular for export finance solutions, payment services and international cash pooling structures.

The overall macroeconomic situation in the Czech Republic and in Europe was an important factor influencing market trends during 2016. Strong domestic consumption and growing foreign demand had positive effects on the overall economic situation of corporations serviced by Komerční banka. Of course, the entire market had to deal with low interest rates, although the Czech National Bank's long-continuing interventions constituted an equally important factor. All this had a positive impact on the top corporations' demand for operating and investment financing. CNB's interventions and expectations for the discontinuation of those interventions, as well as the Brexit and the US presidential elections, were closely followed events and influenced the behaviour of corporations and their demand for foreign-currency financing, as well as demand for hedging instruments.

1 Source: GfK agency's research
2 Source: KB's own market research
3 Source: KB's own research

Central and Eastern European markets were very appealing also from the perspective of foreign investors. As seen in purchases and sales of companies and demand for acquisition loans, the Czech Republic was among the most attractive countries in the region. Real estate financing is an integral part of the corporate market and 2016 was a record year as measured by the number and volume of such transactions on the market.

Komerční banka has long held a leading place in financing and servicing companies in the Top Corporations segment. Its market share in the area of lending to businesses with turnover exceeding CZK 1.5 billion (as determined by comparing KB's exposure with Czech National Bank data) has long ranged above 25%. Due to its having this position, Komerční banka also has a correspondingly important share in the provision of payment services and other so-called everyday banking services. KB's portfolio of clients in the Top Corporations segment is relatively stable.

The general economic situation had a positive effect also on clients' demand for financing. The volume of loans increased by 9.2% to CZK 136.7 billion. The main growth engines for the loan portfolio were financing of real estate, construction and energy, as well as acquisition financing. Komerční banka was also successful in the market as an arranger of large transactions. Clients benefited from low interest rates, which was reflected also in interest rate hedging transactions. Despite CNB intervention and the Czech crown's stable exchange rate, the Bank executed significant hedging transactions in connection with expected termination of the CNB's interventions and also in relation to exchange rate movements caused by the referendum on the UK's leaving the EU and the results of the US presidential election. The year 2016 was also productive from the perspective of commodity financing, in which segment KB, due to its expertise and co-operation with parent company Société Générale, is among the most active institutions on the market.

Through co-operation within the Société Générale Group, Komerční banka introduced a new product for international companies called SG Intraday Sweeping. It is a form of fully automated cash pooling which will enable connecting to any bank communicating through SWIFT – even outside of the Société Générale Group and in any currency. KB extended corporate clients' possibilities for on-line channels. The Mobile Bank Business app was extended to all smartphone platforms, and it also allows logging in by fingerprint. To reinforce security, IBM Trusteer Mobile became a standard part of the application.

Ambitions for 2017 remain confirmed. Komerční banka will strive to maximise use of synergies within Komerční banka Group and Société Générale Group to achieve clients' satisfaction in providing all financial services. An important matter for clients remains the timing as to the end of the CNB's exchange rate commitment. Komerční banka is prepared to safely guide its clients through this period in connection with hedging their transactions and stabilising their cash flows and profitability. KB banka will continue to monitor the market for new investment opportunities and the related transactions. In connection to the national economy and statements of the Czech government, the Bank expects faster drawing from EU funds, due to which it also anticipates increased investments directed especially to innovative technologies and infrastructure. These, in turn, can bring additional growth in financing.

## Komerční banka, a.s., pobočka zahraničnej banky (KB SK)

KB SK is Komerční banka's sole foreign branch. It operates in Slovakia on the basis of a single banking licence issued by the CNB. KB SK is cultivating its co-operation with top corporations within Slovakia, as well as with those clients of KB and SG groups operating there.

The performance of KB SK naturally reflects the situation on the Slovak market. The euro is KB SK's domestic currency, and therefore excessive liquidity, magnified by the financing support programmes of the European Central Bank, significantly influenced the branch's business results and caused a narrowing of margins from client financing. This effect was compensated, however, by significant annual growth in the total volume of loans. Due to vigilant cost control and low cost of risk, net profit increased substantially. KB SK, sometimes in collaboration with expert teams from Komerční banka and Société Générale, closed several important transactions with clients from the energy, real estate, engineering and automotive industries.

The banking advisor team at KB SK was strengthened during the year such that the Bank maintained its high quality of services for clients. KB SK also invested substantially into its systems and processes to fulfil demanding regulatory requirements. Projects were initiated in the areas of direct sales channels and the struggle against money laundering and financing of terrorism.

The solid performance of the Slovak economy is reinforcing clients' confidence. That should lead in 2017 to growth of fixed investments in businesses and, therefore, to stronger financing demand. In addition to its current offer, KB SK will introduce new products for corporate clients in Slovakia. Continuing focus on efficiency, prudence in lending and complying with regulatory requirements will remain a good recipe for stakeholders' value growth also in 2017.

## Investment Banking

Even though the growth rate was slower than in 2015, economic activity in the Czech Republic nevertheless remained on an upward path during 2016. Household consumption was the main growth driver, and this was further supported by net exports and government consumption. On the other hand, investments recorded a decline due to substantially lower public spending on projects co-financed from EU funds and a slow start-up of the new budgetary period. At the end of 2016, inflation started to accelerate and reached its maximum for the past three years. Volatility on foreign-exchange markets was very low. For most of the year, the CZK/EUR exchange rate remained in a very narrow range just above CZK 27. Only in periods of market and political turmoil (Brexit and presidential candidate Trump's victory) did there occur large fluctuations in the crown's exchange rate. The expected end of the CNB exchange rate commitment stimulated a large influx of funds into the Czech currency. This weighed down foreign-currency forwards and motivated the CNB to intervene further in the market. As a result, financing in crowns became massively less costly and government bond yields at the short end of the yield curve dropped to record-low levels. Yields at the long end of the curve reached their lowest in history during September. Thereafter, increasing inflation and higher yields on the foreign markets caused yields on Czech government bonds to rise at the long end of the yield curve.

KB's investment banking teams achieved very good results in 2016. The Czech and Slovak Corporate Sales Desks put in a solid performance while executing large and sophisticated transactions in interest rate swaps, cross currency swaps and foreign exchange options. By taking an active approach and co-operating professionally with the financial markets division of Société Générale, the Bank succeeded in developing commodity services. Komerční banka also boosted returns due to the eTrading platform, which offers a range of services, including foreign currency conversions, earning returns on idle funds, and currency risk hedging. The Financial Institution Sales Desk executed several corporate bond issues. The sales desks achieved solid results due to the aforementioned foreign exchange volatility and wider spreads. Although the volumes traded were high during the year, trades at the foreign exchange spot market were executed with extremely low volatility and extra-narrow spreads. The higher volume of trades involving foreign clients compensated for the narrow spreads on the bond market and low client activity on the local market.

## Structured Finance

On 1 January 2016, KB established a Structured Financing Arm (SFA) through reorganizing and merging a number of its front office teams into a single, new arm. The SFA is made up of approximately 50 professionals with in-depth knowledge in their respective areas.

The SFA offers structured financing and advisory solutions in a wide range of sectors, including export finance, real estate finance, energy finance, acquisition and leveraged finance, debt syndication and debt capital markets.

This new arrangement aims to strengthen KB's origination and execution capabilities for structured financing transactions in KB's core domestic markets (Czech Republic and Slovakia). It should address the increasing needs of KB clients for sophisticated solutions. The SFA will also enhance co-operation with Société Générale Group on transactions requiring an international execution chain, such as international syndications.

KB's Structured Financing Arm also supports and assists a number of Société Générale Group entities within the CEE region in order to enhance their capacity to provide structured finance solutions to their clients.

In 2017, KB will further develop and strengthen the position of its structured finance on the domestic market as well as in abroad. The skills and experience of KB together with a close and active co-operation with Société Générale Group should help to achieve this goal.

## Transaction and payment services

### Cash payment operations

ATM withdrawals predominated in terms of the number of cash transactions performed, while deposits at branches were the most significant in terms of volume. As a result of continually expanding deposit ATMs, the proportion of deposits at branches is decreasing while deposits through ATMs are increasing, thereby fulfilling the objectives defined by the new KB cash strategy. At the end of 2016, KB was operating 195 deposit ATMs as opposed to 114 in 2015.

In 2016, KB selected an alternative ATM technology supplier and continued developing the services currently offered. At the end of the year, therefore, the Bank introduced, for example, the possibility to make a choice of bank notes when withdrawing money from ATMs and pilot operation of coin deposits via ATMs.

During 2017, KB will launch pilot operation of teller cash recyclers in the branch network. Implementation of this technology will boost the efficiency of KB's internal processes and improve the convenience of its services for clients.

### Non-cash payment operations

Komerční banka is among the three largest players on the Czech market.[1] The Bank recorded a 3% year-on-year rise in the number of domestic non-cash payments, and even 10% greater foreign payments. The share of payments within the Single Euro Payment Area (SEPA) in the total number of foreign payments exceeds 72%.

The Bank recorded an accelerating rate of growth in the number of payments made by clients. In 2016, clients were enabled to input SEPA payments in simplified forms merely by filling in the recipient's account number in the IBAN format, without the necessity to fill in the recipient's bank.

Inspired by clients' requests, modifications were made in internet banking. In addition to simplifying the forms for inputting orders and accelerating their completion, KB extended the times for their submission (in the cases of express domestic payments and urgent foreign payments) and it accelerated the execution of payments (e.g. payments into Komerční banka, a.s., pobočka zahraničnej banky in Slovakia).

During 2017, KB will prepare for fulfilling the requirements of the new Directive on Payment Services in the EU internal market (PSD2), which should allow clients to check their account balances and enter orders from several accounts in different banks at the same time from a single app.

### Payment cards

The Czech card market was strongly influenced during 2016 by the validity of EU regulation. This created strong pressure to optimise the card portfolio and the efficiency of issuing payment cards. This resulted in a decline in the number of payment cards issued. Nevertheless, Komerční Banka continues to rank third on the Czech market with 1.6 million payment cards issued and a market share of 14.1% according to the number of cards issued.[2]

The rapid spread of contactless technology caused an increase in card payment numbers. Total turnover expanded by 14.5% in comparison to 2015.

KB signed a partnership with Worldline, a global payment processor and European leader. Together, we will sell and provide card acceptance services to retailers under the brand name KB SmartPay. This co-operation will bring customers an improved product offer (including broadening of card acceptance on the internet) and further simplification in using payment services.

In the digitalisation area, KB is preparing for the theoretical possibility of performing payments in real time, and in the Czech Banking Association it is leading a work group for instantaneous payments, where standards and technical descriptions for processing instantaneous payments are being defined.

### Trade Finance and Cash Management

KB has long been one of the main players on the trade finance market.[3] Year on year, the Bank recorded a stable number of new sales during 2016, while volume declined mainly in bank guarantees. This trend mirrored the market development. The number of users of the Trade & Finance OnLine app for arranging and managing transactions rose by a substantial 14%.

In cash management, KB benefited from its position on the Czech market and SG's experience in offering local and multinational clients new solutions tailored to their needs. The Bank worked on bringing new tools to the market for cross-border payment solutions, such as Sogecash Web internet banking, intermediation to connect large international companies into the SWIFT network through Sogecash SWIFTNet services, and use of new cash-pooling structures that enable centralising balances on accounts from various banks and in different currencies.

1 Source: statistics from the CNB
2 Source: statistics from the Bank Card Association
3) Source: KB's own research in co-operation with the International Chamber of Commerce CR

# Komerční banka Group

As of 31 December 2016, Komerční banka had 10 subsidiaries and 1 associate, Komerční pojišťovna, where it held a 49% share. KB considers these companies as part of the Group. In addition to its ownership interests in the Group, KB holds a strategic interest of 20% in Czech Banking Credit Bureau, a.s. and of 20% in Cataps, s.r.o.

With the aim to maximise the use of all potential synergy effects, KB Group deepened in 2016 mutual business co-operation within the Group and also with other members of the Société Générale Group operating on the Czech market. Special emphasis is given to improving co-ordination of product development in business areas and in distribution, in procurement, IT and other supporting services. The result should be optimal, comprehensive and effective satisfaction of clients' financial needs.

Information on values and changes in equity investments is provided in the Separate Financial Statements according to IFRS, note no. 24 *'Investments in subsidiaries and associates'*.

## Summary of the results of major companies in Komerční banka Group

| | Group | Total assets | | Shareholders' equity | | Net profit | | Consolidation |
|---|---|---|---|---|---|---|---|---|
| **CZK million, IFRS** | **Holding (%)*** | **2016** | **2015** | **2016** | **2015** | **2016** | **2015** | **method** |
| **Domestic participations** | | | | | | | | |
| Modrá pyramida stavební spořitelna, a.s. | 100 | 84,559 | 88,751 | 6,292 | 7,358 | 883 | 915 | Full |
| Komerční pojišťovna, a.s. | 49 | 55,478 | 53,173 | 2,608 | 2,483 | 410 | 308 | Equity |
| KB Penzijní společnost, a.s. | 100 | 2,049 | 1,693 | 1,602 | 1,367 | 234 | 176 | Full |
| SG Equipment Finance Czech Republic s.r.o. | 50.1 | 28,794 | 28,853 | 4,049 | 3,760 | 289 | 311 | Full |
| ESSOX s.r.o. | 50.93 | 11,648 | 9,868 | 3,634 | 3,935 | 464 | 481 | Full |
| Factoring KB, a.s. | 100 | 8,573 | 7,336 | 1,609 | 1,626 | 78 | 76 | Full |
| Protos, uzavřený investiční fond, a.s. | 100 | 8,093 | 8,677 | 8,061 | 8,623 | 239 | 222 | Full |
| KB Real Estate, s.r.o. | 100 | 987 | 1,013 | 497 | 495 | 2 | 2 | Full |
| VN 42, s.r.o. | 100 | 2,102 | 2,070 | 2,078 | 2,045 | 32 | 31 | Full |
| NP 33, s.r.o. | 100 | 737 | 892 | 724 | 878 | 16 | 16 | Full |
| PSA FINANCE ČESKÁ REPUBLIKA, s.r.o. (100% subsidiary of ESSOX s.r.o.) | 50.93 | 3,067 | n.a. | 757 | n.a. | 12 | n.a. | Full |
| **Foreign participations** | | | | | | | | |
| Bastion European Investments S.A. | 99.98 | 6,185 | 6,348 | 3,118 | 3,184 | 31 | 48 | Full |
| PSA FINANCE SLOVAKIA, s.r.o. (100% subsidiary of ESSOX s.r.o.) | 50.93 | 1,859 | n.a. | 184 | n.a. | 7 | n.a. | Full |

* KB direct and indirect holding

# Basic information on Komerční banka Group's major companies

## Modrá pyramida stavební spořitelna, a.s.

Modrá pyramida is a fully owned subsidiary of KB. This second largest building savings bank in the Czech Republic as measured by loan volume has 16% market share[1]. Main products offered by Modrá pyramida include: state-subsidised savings accounts, bridging loans and building savings loans. Modrá pyramida's distribution network with its approximately 1,000 advisors provides additional products of KB Group such as mortgages and KB bank services, supplementary pension insurance, mutual funds, life insurance etc.

**Financial summary** (CAS[2], CZK thousand)

| | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Total assets | 85,024,701 | 89,103,638 |
| Shareholder's equity | 6,291,859 | 7,357,501 |
| Loans to clients (gross) | 39,001,080 | 37,171,614 |
| Volume of deposits | 76,381,234 | 79,312,458 |
| Net operating income | 1,531,700 | 1,538,947 |
| Net profit | 883,094 | 915,071 |
| Average number of FTEs | 330 | 330 |
| Number of points of sale | 216 | 215 |

**Contact:**
Modrá pyramida stavební spořitelna, a.s.
Bělehradská 128, č. p. 222, 120 21 Prague 2
ID: 60192852
Phone: +420 222 824 111
Email: info@modrapyramida.cz
Internet: www.mpss.cz
www.modrapyramida.cz

## KB Penzijní společnost, a.s.

KB Penzijní společnost is a fully owned subsidiary of KB with core businesses of collecting contributions and managing them in pension funds pursuant to the Supplementary Pension Savings Act and supplementary pension insurance in the Transformed fund. This pension company has by number of participants 16% market share on the supplementary pension savings market (3rd pillar) and 11% market share on the pension insurance market (transformed fund)[3].

**Financial summary** (CAS[2], CZK thousand)

| | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Assets under management[4] | 52,238,529 | 48,551,032 |
| of which in Transformed fund | 49,864,419 | 46,614,720 |
| Shareholder's equity | 1,601,777 | 1,367,441 |
| Net operating income | 361,403 | 295,831 |
| Net profit | 234,400 | 175,568 |
| Average number of FTEs | 47 | 47 |

**Contact:**
KB Penzijní společnost, a.s.
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Phone: +420 955 525 999
E-mail: kbps@kbps.cz
Internet: www.kbps.cz

## SG Equipment Finance Czech Republic s.r.o.

SG Equipment Finance is owned by Komerční banka (50.1%) and SG Equipment Finance International (49.9%). Through KB and its own network of 7 branches in the Czech Republic and 2 in Slovakia, this company provides financing of equipment, agricultural and forestry technology, vehicles for transportation of goods and passengers, high-tech, real estate and special projects by leasing and other financing. SGEF has 18% market share on the leasing market in the Czech Republic measured as volume results based on based on financed amount (not including consumer credit companies)[5].

**Financial summary** (CAS[2], CZK thousand)

| | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Total assets | 29,642,418 | 29,655,399 |
| Shareholders' equity | 3,779,246 | 3,404,523 |
| Volume of new financing | 12,252,728 | 11,496,000 |
| Net operating income | 719,007 | 880,789 |
| Net profit | 374,722 | 577,909 |
| Average number of FTEs | 124 | 121 |

**Contact:**
SG Equipment Finance Czech Republic s.r.o.
nám. Junkových 2772/1, 155 00 Prague 5
ID: 61061344
Phone: +420 955 526 700
E-mail: info@sgef.cz
Internet: www.sgef.cz

1 Source: internal data, Ministry of Finance of the Czech Republic, www.mfcr.cz
2 CAS: Czech Accounting Standards. Not audited.
3 Source: Association of Pension Funds of the Czech Republic, www.apfcr.cz
4 Total volume on client accounts
5 Source: Czech Leasing and Finance Association, www.clfa.cz

## ESSOX s.r.o.

ESSOX is owned by Komerční banka (50.93%) and SG Consumer Finance (49.07%) is a non-bank provider of consumer loans and financial leasing for consumers and performs activities of payment institutions within the scope of payment services under a licence from CNB. ESSOX has a 14% market share in consumer lending provided by companies associated in the Czech Leasing and Finance Association[1]. Main products include financing of consumer goods and automobiles, general-purpose loans and revolving credit (credit card). Through the acquisition of PSA Finance Czech Republic and PSA Finance Slovakia in 2016, ESSOX entered the market of financing new cars.

**Financial summary** (CAS[2], CZK thousand)

| | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Total assets | 11,642,900 | 9,824,268 |
| Shareholders' equity | 3,593,931 | 3,890,221 |
| Amounts due from clients (gross) | 10,093,891 | 9,451,446 |
| Net operating income | 1,090,034 | 1,048,421 |
| Net profit | 468,819 | 464,984 |
| Average number of FTEs | 346 | 341 |

**Contact:**
ESSOX s.r.o.
Senovážné nám. 231/7,
370 21 České Budějovice
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Phone: +420 389 010 111
E-mail: essox@essox.cz
Internet: www.essox.cz

## Factoring KB, a.s.

Factoring KB is a fully owned subsidiary of KB. In the first quarter of 2016, Factoring KB came to be the leading factoring company in the Czech Republic and its market share reached 29% of the factoring portfolio on the Czech market[3]. This biggest factoring company provides through its own and also KB's network the following products: domestic factoring, export factoring, import factoring, modified factoring and receivables management.

**Financial summary** (CAS[2], CZK thousand)

| | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Total assets | 13,976,690 | 12,027,931 |
| Shareholder's equity | 1,609,743 | 1,626,201 |
| Factoring turnover | 37,761,677 | 35,480,496 |
| Amounts due from clients (gross) | 12,869,688 | 10,801,275, |
| Net operating income | 202,495 | 170,554 |
| Net profit | 78,137 | 76,215 |
| Average number of FTEs | 42 | 42 |

**Contact:**
Factoring KB, a.s.
nám. Junkových 2772/1, 155 00 Prague 5
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Phone: +420 955 526 906
E-mail: info@factoringkb.cz
Internet: www.factoringkb.cz

## Komerční pojišťovna a.s.

The shareholders of Komerční pojišťovna are SOGECAP (51%) and Komerční banka (49%). This insurance company has 11% share on the life insurance market (measured by premiums written)[4]. Main products include: saving life insurance, risk life insurance, capital life insurance, investment life insurance, accident insurance, payment card insurance, travel insurance, travel insurance for payment cards, risk life insurance for credit cards and risk life insurance for consumer loans. In 2016, Komerční pojišťovna radically developed its activities by introducing residential real estate and household insurance.

**Financial summary** (CAS[2], CZK thousand)

| | 31.12.2016 | 31.12.2015 |
|---|---|---|
| Total assets | 48,109,578 | 46,687,061 |
| Shareholders' equity | 2,597,615 | 2,983,090 |
| Technical reserves (gross) | 47,449,991 | 45,428,778 |
| Gross premium written | 6,660,083 | 6,577,143 |
| Net profit | 486,960 | 372,781 |
| Average number of FTEs | 180 | 166 |

**Contact:**
Komerční pojišťovna a.s.
Karolinská 1/650, 186 00 Prague 8
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Phone: +420 222 095 999
E-mail: servis@komercpoj.cz
Internet: www.komercpoj.cz

1 Source: Czech Leasing and Finance Association, www.clfa.cz, including PSA Finance CZ
2 CAS: Czech Accounting Standards. Not audited.
3 Source: Czech Leasing and Finance Association, www.clfa.cz
4 Source: Czech Insurance Association, www.cap.cz

# Corporate governance

(A separate part of the annual report pursuant to § 118 (4) (b), (c), (e) and (j) and (5) (a)–(k) and (6) of Act No. 256/2004 Coll., on Capital Market Undertakings, as amended)

Komerční banka adheres to and voluntarily upholds all the principal standards of corporate governance in compliance with the *Corporate Governance Code* based on the OECD principles as amended in 2004 and issued by the Czech Securities Commission. The Czech wording of the Revision of the Code is available on the website of the Ministry of Finance of the Czech Republic at **www.mfcr.cz**.

Komerční banka's Board of Directors respects the aforementioned principles of corporate governance, including the newly introduced European rules unifying corporate governance codes of best practice at the European level, and it reflects the new rules in its internal procedures and regulations.

The Bank applies an open approach to publishing information concerning its financial position, dividend policy, performance, ownership, and corporate management. Financial reports provide a true and fair view of the Bank's accounting and financial position. Shareholders are informed in a timely manner as to the date, location, and agenda of the General Meeting, with the proposals of the individual resolutions and their rationale, including the information on the proposal for the payment of the share in profit and the method of its payment. Shareholders are informed of their rights relating to their participation in the General Meeting, including a description of how to attend the General Meeting, whether in person or on the basis of a power of attorney, and have at their disposal in advance materials concerning the agenda of the General Meeting.

The Bank has a two-tier management system which entails a separation of the executive and control functions. The Board of Directors performs all key functions of the Bank's management. Operational management is divided among the individual members of the Board, and each member of the Board has competence over a certain area of the Bank's activities (functional division). The Board of Directors nevertheless decides collectively at its meetings, which are held regularly at two-week intervals. Under the Bank's Articles of Association, members of the Board are subject to rules and regulations over conflicts of interest even stricter than as defined by Act No. 90/2012 Coll., on Business Corporations. They are obliged to inform the Board of Directors and Supervisory Board of any existing or even potential conflicts of interest relating to functions they perform in any other legal entity and are obliged to abstain from voting on all matters concerning the Bank's relationship to such a legal entity.

The Supervisory Board is a control body supervising the activities of the Board of Directors and of the entire Bank. Two of the Supervisory Board's nine members are independent and three are employee representatives. The Supervisory Board is to establish Audit, Risk, Nominations and Remunerations committees. Members of the Audit Committee are appointed by the General Meeting. The majority of members of the Audit Committee, including the Chairperson, are independent and professionally qualified. The audit committee plays an important role in supervising the Bank's proper management, independence and objectivity of the external auditor, the auditor's conduct of the mandatory audit, effectiveness of the risk management systems (together with the Risk Committee), and mechanisms of internal management and control. The Risk Committee monitors the Bank's approach to risk, its strategy in the risk area, acceptable levels of risk and risk management.

Within its competences, the Supervisory Board ensures that the Board of Directors and Supervisory Board consist of individuals having suitable professional, time of experience, and other qualifications so that both bodies have a balance of expert qualification and experience and that the composition of the Board of Directors and Supervisory Board as a whole is diverse. For this purpose, the Supervisory Board adopted principles for appointing members of the Board of Directors and the Supervisory Board and for the composition and performance of the Board of Directors and Supervisory Board. On a regular, annual basis, the Nominations Committee evaluates the trustworthiness, professional qualifications, professionalism and experience of the individual members of the Board of Directors and Supervisory Board and of the two bodies as a whole.

There were no fundamental changes during 2016 which would adversely influence the aforementioned standards for the Bank's corporate governance. Komerční banka will continue to respect the principles of corporate governance, inasmuch as these best correspond with the Bank's business model as well as the interests of the Bank and its shareholders.

# Shareholders and the General Meeting

Komerční banka's share capital totals CZK 19,004,926,000 and is divided into 190,049,260 ordinary listed shares admitted to trading on the European regulated market, each with a nominal value of CZK 100. All the Bank's shares carry the same rights.

**Major shareholders of Komerční banka owning more than 1% of the share capital as of 31 December 2016**
(per the extract from the issuers register taken from the Central Securities Depository)

| Shareholder | Proportion of share capital |
|---|---|
| Société Générale S.A. | 60.35% |
| Nortrust Nominees Limited | 4.20% |
| Chase Nominees Limited | 3.59% |
| Brown Brothers Harriman | 2.70% |
| State Street Bank and Trust Company | 2.44% |
| Clearstream Banking, S.A. | 2.23% |
| GIC Private Limited | 2.06% |
| J.P. Morgan Bank | 1.09% |
| AGF Investments Inc. | 1.00% |
| Other shareholders | 20.34% |

**Shareholder structure of Komerční banka as of 31 December 2016**
(per the extract from the issuers register taken from the Central Securities Depository)

| | Number of shareholders | Proportion in number of shareholders | Proportion of share capital |
|---|---|---|---|
| **Number of shareholders** | **46,801** | **100.00%** | **100.00%** |
| of which: legal entities | 658 | 1.41% | 96.67% |
| private individuals | 46,143 | 98.59% | 3.33% |
| **Legal entities** | **658** | **1.41%** | **96.67%** |
| of which: from the Czech Republic | 210 | 0.45% | 1.51% |
| from other countries | 448 | 0.96% | 95.16% |
| **Private individuals** | **46,143** | **98.59%** | **3.33%** |
| of which: from the Czech Republic | 41,579 | 88.84% | 3.14% |
| from other countries | 4,564 | 9.75% | 0.18% |

The General Meeting is the supreme body of the Bank. The Regular General Meeting is convened at least once per year, and in no case later than four months from the last day of each accounting period. A quorum of the General Meeting shall be constituted if the attending shareholders hold shares the total nominal value of which exceeds 30% of the Bank's registered capital, provided that voting rights are attached thereto in accordance with generally binding legal regulations and except in cases specified in § 12, para.1 of the Articles of Association. The quorum is confirmed at the time of convening the General Meeting and always before each vote. The General Meeting shall approve resolutions by a majority of votes of the attending shareholders unless legal regulations or the Articles of Association require a qualified majority of votes. The General Meeting's order of business is governed by the agenda stated in the invitation to the General Meeting, which contains proposed resolutions and their justification and further information about the conditions of shareholders' participation, execution of shareholder rights and the main information from the financial statements. At least 30 days prior to the General Meeting, the General Meeting shall be convened by means of a public notice calling the General Meeting, which shall be posted on the Bank's website **www.kb.cz** and on the notice board in the Bank's registered office, as well as published in the Mladá Fronta DNES daily newspaper. All documents relating to corporate governance are published on the Bank's website. Issues not included in the proposed agenda for the General Meeting are decided upon only with the attendance and consent of all the Bank's shareholders. The General Meeting shall be opened by a member of the Board of Directors authorised for this purpose by the Board of Directors or a person designated by the Board of Directors. This member of the Board of Directors also shall conduct the General Meeting until a Chairman of the General Meeting is elected.

Unless otherwise stipulated by law or the Articles of Association, all persons registered in the list of attending shareholders and present at the General Meeting at the time of calling a vote are entitled to vote. The sequence of voting corresponds to the order on the General Meeting's agenda. The casting of votes shall be carried out by means of ballots. Each CZK 100 of the nominal share value represents one vote. Any proposal presented by the Board of Directors shall be voted upon first. Should such proposal of the Board of Directors be accepted by the required majority, other proposals or counter-proposals to this point shall not be voted upon. Other proposals or counter-proposals shall be voted upon in the sequence in which they have been presented. Should such a proposal or counter-proposal be approved in a vote by the General Meeting, other proposals or counter-proposals shall not be voted upon.

**The General Meeting has within its powers to:**

a) decide upon changes to the Articles of Association, with the exception of a change in consequence of an increase in the registered capital by the authorised Board of Directors or a change made on the basis of other legal circumstances;
b) decide upon a change in the amount of the registered capital, except that, unless it is reduced to cover a loss, the registered capital may be reduced only upon prior approval of the Czech National Bank;
c) elect and remove members of the Supervisory Board; elect and remove members of the Audit Committee;
d) approve the Board of Directors' reports regarding the Bank's business activities and the state of its property, at least once per accounting period;
e) decide upon the possibility of setting off a monetary claim of the Bank against a claim to be used for payment of the issue price, including the draft of the relevant contract for set-off;
f) decide upon a change in the class or type of the shares;
g) decide to issue convertible or priority bonds of the Bank;
h) decide to modify the rights attached to individual classes of the shares;
i) approve the regular financial statements, extraordinary financial statements, consolidated financial statements and, as established by law, interim financial statements;
j) decide upon distribution of profit or other of the Bank's funds or coverage of a loss;
k) approve the service contracts with the members of the Supervisory Board and of the Audit Committee;
l) decide on transformation of the Bank, unless the act regulating transformations of companies and co-operatives establishes otherwise, provided that prior consent of the Czech National Bank has been given where so required by law;
m) decide to wind up the Bank with the prior consent of the Czech National Bank;
n) approve proposed distribution of the liquidation balance of the Bank's assets;
o) decide to file for admitting the participation securities of the Bank to trading in the European regulated market or for excluding these securities from trading in the European regulated market;
p) approve the transfer or pledging of an enterprise or such part thereof entailing a substantial change to the existing structure of the enterprise or a substantial change to the business activities of the Bank;
q) charge the Board of Directors to decide upon an increase in the registered capital under the conditions specified by law;
r) decide to acquire the Bank's shares into treasury in accordance with the applicable provisions of the Act on Business Corporations;
s) decide upon elimination or restriction of the pre-emptive right to acquire convertible or priority bonds, elimination or restriction of the pre-emptive right to subscribe for new shares in accordance with the Act on Business Corporations;
t) approve the acquisition or disposal of assets, when the law so requires;
u) decide upon appointment of the auditor to make the statutory audit or to verify other documents if such appointment is required by legal regulations;
v) convey principles and instructions to the Board of Directors of the Bank (with the exception of instructions regarding the business management of the Bank unless provided to the Board of Directors upon its request); and approve principles and convey instructions to the Supervisory Board (with the exception of instructions regarding the statutory duty to check the competence of the Board of Directors);
w) provide its consent regarding a contract for settlement of a loss caused by a breach of the duty of due care on the part of a member of a body of the Bank;
x) decide upon suspending the service of a member of a body of the Bank who declares a conflict of interest under the Act on Business Corporations, or prohibit a member of a body of the Bank from entering into a contract which is not in the Bank's interest;
y) instruct the Supervisory Board to establish the ratio between the fixed and variable parts of a Board member's remuneration to be higher than 100%, while the overall variable part for any Board member shall not exceed 200% of the fixed part of his or her total remuneration;
z) approve a maximum ratio between the fixed and variable parts of an employee's remuneration higher than 100% on the condition that the overall variable part for any individual may not exceed 200% of the fixed part of his or her total remuneration;
aa) decide upon other matters which according to the legally binding legal regulations or the Articles of Association are a part of the powers of the General Meeting.

The results and information from the General Meeting are available on Komerční banka's website **www.kb.cz**.

## Principle resolutions of Komerční banka's Annual General Meeting held in 2016

At the regular General Meeting held on 22 April 2016, 449 shareholders holding shares with nominal value representing 80.84% of the Bank's share capital were present in person or through their representatives.

The General Meeting approved the Board of Directors' report on the Bank's business activities and the state of its property for the year 2015 as well as the annual financial statements of Komerční banka for the year 2015, decided to distribute profit for 2015 in the total amount of CZK 12,423,619,041.87, and decided to pay out dividends in the amount of CZK 310 per share before tax. The Annual General Meeting also:

- approved the consolidated financial statements for the year 2015;
- elected Mr Bořivoj Kačena as a member of the Supervisory Board;
- elected Mr Bořivoj Kačena as a member of the Audit Committee;
- consented to acquisition into treasury of the Bank's ordinary shares with nominal value of CZK 100 under specified conditions;
- appointed the company Deloitte Audit s.r.o., headquartered in Prague, as the Bank's external auditor for 2016 and the company Deloitte Audit s.r.o., headquartered in Bratislava, as the auditor of KB's foreign branch in Slovakia;
- approved amendments to the Bank's Articles of Association implementing especially the share split at a rate of 5:1;
- approved the maximum ratio between the fixed and variable parts of the remuneration of employees in departments performing important investment activities at 200% of the fixed part of their remuneration. The variable part may range from 0% to 200% of the fixed part and may not exceed 200% of the fixed part of the remuneration for any individual.

## Additional information in accordance with § 118 (5), (i), (j) and (k) of the Act on Capital Market Undertakings

Komerční banka is aware of no contracts made between its shareholders as a result of which the transferability of shares or of voting rights would become more complicated. The Bank has entered into no significant contracts which take effect, are altered or terminate if the person or entity in control of Komerční banka changes as a consequence of a takeover bid. Komerční banka has entered into no contract with a member of its Board of Directors or any employee stipulating an obligation for Komerční banka to perform in the event that such person would cease to serve as a member of the Board of Directors or cease to be employed in connection with a takeover bid. The Bank has established no programmes enabling the members of the Board of Directors and employees of the Bank to acquire the Bank's securities, options on these securities or other rights under preferential conditions.

### Information about special rules on the revision of the Bank's Articles of Association

According to the Bank's Articles of Association, decisions on amendments to the Articles of Association are within the powers of the General Meeting. Proposed resolutions for amendments to the Articles of Association and their justification are provided in the invitation to the General Meeting. Proposed changes in the Articles of Association are available for shareholders' inspection at no charge at the Bank's headquarters and on its website for the period established for convening of the General Meeting. The Bank shall notify its shareholders of these rights in the invitation to the General Meeting.

If a shareholder wishes to raise counter-proposals to the proposed changes to the Articles of Association at the General Meeting, the shareholder is obliged to deliver the written wording of such proposal or counter-proposal to the Bank no later than five business days prior to the day of the General Meeting. The Board of Directors shall notify its shareholders of the wording of the counter-proposal along with its viewpoint with regard to it in the manner specified for the convening of the General Meeting.

Decisions on changes in the Articles of Association are made by the General Meeting and carried by two-thirds of those votes of the attending shareholders upon a proposal of the Board of Directors, of the Supervisory Board or of one or more shareholders in accordance with the Act on Business Corporations and the Articles of Association. Decisions on changes in the Articles of Association must be recorded by notarial deed containing the approved text of the wording of changes in the Articles of Association. Komerční banka is obliged to report to the Czech National Bank its intention to make changes in the Articles of Association relating to those particulars which must be stated in the Articles of Association based on a requirement set forth by law.

## Board of Directors

The Board of Directors is the corporate body which manages the Bank's activities. The Board of Directors is charged with business management, including to ensure the proper keeping of the Bank's accounting records, integration of the accounting system and financial reporting, reliability of financial and operating control, smooth conduct of activities and the Bank's performance on the financial market in compliance with the object and plan of its activities. The Board ensures consistent and effective implementation of the risk management, compliance and internal audit functions. The Board of Directors further ensures the creation of a comprehensive and adequate management and control system, ensures its compliance with legal regulations, and is responsible for its continuous functioning and effectiveness. The Board of Directors ensures the establishment and maintenance of the management and control system so as to ensure the adequacy of information and communication in conducting the Bank's operations.

The Board of Directors shall decide upon all matters concerning the Bank unless assigned to the competence of the General Meeting, the Supervisory Board or the Audit Committee by law or by the Articles of Association. The Board of Directors consists of six members, natural persons, who satisfy the conditions established in legal regulations for serving as a member of the

Bank's Board of Directors and who are elected for four-year terms by an absolute majority of all Supervisory Board members at the recommendation of the Nominations Committee. The Nominations Committee ensures the trustworthiness, adequate professional qualifications and experience of the members of the Board of Directors. The professional qualifications, trustworthiness and experience of the members of the Bank's Board of Directors are assessed by the Czech National Bank.

In accordance with the requirement of the Czech National Bank, Komerční banka declares that the members of the Board of Directors of Komerční banka have not in the past 5 years been convicted of any criminal offence and that no charges, accusations or other sanctions have been brought against them by any regulatory body. No bankruptcy, receivership or liquidation has been declared in relation to the stated persons during the past 5 years.

In relation to his or her work in the Bank, no person with executive power has any conflict of interests between the duties of a person with executive power in the Bank and that person's private interests or other duties. Chairman of the Board of Directors Albert Le Dirac'h and members of the Board of Directors Aurélien Viry and Karel Vašák have employment contracts signed with Société Générale S.A. and they are delegated to serve as the Bank's directors.

## Method of performing acts in law on the Bank's behalf

The Board of Directors, as the Bank's authorised body shall act on behalf of the Bank in all matters, either by all members of the Board of Directors jointly or by any two members jointly. The Board has authorised the Chairman of the Board to act on behalf of the Bank in relation to the employees.

## Composition of the Board of Directors as of 31 December 2016

**Albert Le Dirac'h**
Chairman of the Board of Directors (since 2 August 2013)

**Libor Löfler**
Member of the Board of Directors (since 1 April 2015)

**Vladimír Jeřábek**
Member of the Board of Directors (since 1 June 2008, re-elected on 3 June 2016)

**Peter Palečka**
Member of the Board of Directors (since 13 October 1999, re-elected on 8 October 2013)

**Jan Pokorný**
Member of the Board of Directors (since 2 August 2016)

**Karel Vašák**
Member of the Board of Directors (since 1 August 2012, membership terminated as of 1 August 2016)

**Aurélien Viry**
Member of the Board of Directors (since 1 January 2011, re-elected on 2 January 2015, membership terminated as of 30 November 2016)

**Albert Le Dirac'h**
Graduated in management studies from the University of Rennes. Between 1979 and 1980, he worked in the Insurance National Group. He has worked in the Société Générale Group since 1980, first in Paris as an inspector in the SG Inspection department and from 1987 as deputy director and later as director of the Back Office within the Capital Markets Department. From 1995 until 1999, he was Head of Human Resources Management. From 1999 to 2006, he was CEO and a member of the Board of Directors of SGBT Luxembourg. Between 2001 and 2007, he served as Chairman of the Supervisory Board at SG Private Banking Belgium and from 2006 to 2008 as Deputy Head of Human Resources of SG Group. From 2008 to 2012, he was Chairman of the Board of Directors and CEO of Société Générale Morocco headquartered in Casablanca. The Board of Directors of Komerční banka elected Mr Albert Le Dirac'h as Chairman of the Board of Directors and Chief Executive Officer of Komerční banka with direct responsibility for management of the Human Resources, Internal Audit and Marketing and Communication departments, as well as the Strategic Plan. Mr Le Dirac'h is also a member of the supervisory boards of SGEF and Komerční pojišťovna and chairman of the supervisory boards of Modrá pyramida, ESSOX and PSA Finance Slovakia.

**Vladimír Jeřábek**
A graduate from VUT Technical University in Brno, Czech Republic, and from Nottingham Trent University, he has held the positions of economic director and member of the board of directors in several banking institutions and at Zetor, a.s., a producer of agricultural tractors. Upon his arrival to Komerční banka in 1998, Mr Jeřábek was the regional manager responsible for the Brno region and later was in charge of Komerční banka's distribution channels. In February 2007, he was appointed Executive Director of the Distribution Network. He is responsible for the Bank's distribution network serving the Retail and Corporate segments and also for the alternative distribution channels such as internet banking and non-banking channels. The Supervisory Board elected Mr Jeřábek as a member of the Board of Directors in charge of Distribution with effect from 1 June 2008. Moreover, Mr Jeřábek is chairman of the supervisory board of KB Penzijní společnost and a member of the supervisory board of Modrá pyramida.

**Libor Löfler**
A graduate from the University of Economics, Prague, he has spent his entire professional career in the banking industry. Among other positions, he worked at the National Bank of Czechoslovakia,

Investiční banka and Konsolidační banka in the areas of IT projects and financial management. During 1998 and 1999, he worked as the CEO of Konsolidační banka. Since 1999, he has been working for Komerční banka in the areas of finance and the financial group management. He served as Head of Financial Management between 2002 and 2006. From 2006 to 2010, he held the position of Vice-Chairman of Modrá pyramida in charge of credit approval, IT and projects. From 2010 to 2012, he was Deputy Senior Executive Director for Strategy and Finance of Komerční banka. In 2012, he took over as the Executive Director of Strategy and Finance. With effect from 1 April 2015, he was elected by the Supervisory Board as a Member of the Board of Directors of Komerční banka in charge of Strategy and Finance, Transaction and Payment Services, Investment Banking Services, Support Services, Information Technology, Organisation and Change Management and Information Management. Mr Löfler is also a member of the supervisory boards of Modrá pyramida, ESSOX, Komerční pojišťovna and PSA Finance Slovakia. Moreover, Mr Löfler is Chairman of the Board of VISA Czech Republic.

**Peter Palečka**
A graduate of the University of Economics, Bratislava, from 1982 to 1988, Mr Palečka worked in foreign trade enterprises. Between 1989 and 1992, he worked at the Federal Ministry of Foreign Trade of the Czech and Slovak Federative Republic. From 1992 to 1994, he was the Permanent Representative of the Czech and Slovak Federative Republic and then of the Czech Republic to GATT, and from 1995 to 1998 he was the Permanent Representative of the Czech Republic to the World Trade Organization. He joined Komerční banka in 1998 as the director for Strategy. In October 1999, he was elected a member and in April 2000 Vice-Chairman of Komerční banka's Board of Directors. On 5 October 2001, he was re-elected as a member and Vice-Chairman of the Board of Directors. At present, he is a member of the Board of Directors and Corporate Secretary. Mr Palečka is also vice-chairman of the supervisory board and chairman of the audit committee of Modrá pyramida.

**Jan Pokorný**
A graduate of the Czech Technical University Prague, Faculty of Mechanical Engineering, and of post-graduate studies at the University of Economics, Prague, Economics and Management Programme, he received in 2003 the title Executive MBA from the University of Chicago Graduate School of Business. He has been working in Komerční banka Group since 1991. He initially worked in the capital markets area and then was active in KB's London representation, where he focused on investment banking. After returning to the Czech Republic, he held the position of Vice-Chairman of the Board of Investiční kapitálová společnost Komerční banky. During 2003 to 2005, he was Executive Director of the distribution network. Between 2006 and 2009, he was First Vice President for Central and Eastern Europe in SG Private Banking SA, Switzerland. In 2010, he was appointed Chairman of the Board of Directors and CEO of Modrá pyramida stavební spořitelna. As of 1 August 2015, he was appointed Executive Director for Komerční banka's Structured Financing. Effective from 2 August 2016, he was appointed by the Supervisory Board as Member of the Board of Directors responsible for the Structured Financing, Investment Banking and Top Corporations departments. Jan Pokorný is also a member of the Supervisory Board of KB Penzijní společnost.

## Activity report of the Board of Directors

The Board of Directors shall convene at its regular, periodic meetings, usually once every two weeks. Meetings shall be convened and presided over by the Chairman of the Board of Directors or, in his or her absence, by a member of the Board of Directors authorised to do so by the Board of Directors. Should it not be possible to hold a Board of Directors' meeting, a decision may be adopted by voting remotely in accordance with the Articles of Association.

The Board of Directors met at 22 regular and 2 extraordinary meetings in 2016 and held 4 remote votes in accordance with the Bank's Articles of Association. The average meeting length was 1 hour and 50 minutes and with an average participation of 88%. A quorum of the Board of Directors shall be constituted if an absolute majority of the Board members are present. Resolutions of the Board of Directors shall be adopted by an absolute majority of members of the Board of Directors present, except for the election of the Chairman of the Board of Directors, who shall be elected by an absolute majority of all members of the Board of Directors.

In 2016, the Board of Directors discussed the annual financial results of KB Group for the year 2015, as well as KB's consolidated financial statements, separate financial statements, and their footnotes as of 31 December 2015 and prepared under International Financial Reporting Standards (IFRS). The Board of Directors submitted these statements to the Supervisory Board for review and then to the General Meeting for approval. At the same time, it submitted to the Supervisory Board for review the proposed profit distribution for 2015, which was subsequently approved by the General Meeting.

The Board of Directors also discussed additional proposals for the General Meeting, in particular the Report of the Board of Directors on the Bank's Business Activities, the Report on Relations among Related Entities, the conditions for acquiring the Bank's own shares, the proposal for appointment of the external auditor and other matters falling within the competence of the General Meeting. Moreover, it approved the Bank's Annual Report for 2015 and Half-yearly Report for 2016.

The Board of Directors regularly reviewed the quarterly financial results of KB Group. It continuously evaluated the Bank's capital adequacy and also approved the Internal Capital Adequacy Assessment Process (ICAAP) submitted to the Czech National Bank on the basis of Decree No. 163/2014 Coll. on the performance of the activity of banks, credit unions and investment firms. While taking into consideration the test of solvency, it decided on the payment of dividends for the year 2015. It also discussed capital management policy, particularly with respect to new regulatory requirements on banks' capital requirements. In this connection, it approved a dividend policy in relation to the profit for the year 2016. This policy was published along with the results for the third quarter of 2016. Moreover, the Board of Directors discussed reports on the market situation, the development of structural risks for each quarter of the year, as well as the KB Group budget for 2016.

As part of its activities, the Board of Directors regularly assessed all of the Bank's risks. In the field of risk management, it discussed the reports on the development of market and capital risks and the development of lending on capital markets on a monthly basis. At the same time, it discussed and approved limits on market risks, and, within its competence, approved loans to economically connected groups above a specified limit. It also approved the strategy for dealing with clients assigned to the administration of the Asset Valuation and Recovery Department. Moreover, it approved competences in providing loans and dealt with issues on risk management supervision across the entire Group. It approved the document on the level of so-called risk appetite. In the operational risks area, the Board of Directors discussed the regular quarterly reports containing also information on the results of the first-level controls.

Compliance risks were evaluated both in the yearly report for 2015 and the quarterly reports on the development of these risks. At the same time, the Board of Directors approved the 2015 annual evaluation report on KB's system against money laundering and the financing of terrorism. It was informed on new regulations impacting the Bank and needing to be implemented as well as their expected development in the next year. The Board of Directors decided the Bank would commit to the Code of Conduct regulating PRIBOR. It also approved the Group's recovery plan for 2016, in accordance with Directive No. 2014/59/EU and with Act No. 374/2015 on recovery procedures, which was subsequently submitted to the CNB. The Board of Directors updated the list of those employees whose professional activities have a material impact on the Bank's risk profile. It also conducted an annual evaluation as to implementation of the remuneration principles.

In the area of Internal Audit, the Board of Directors discussed a number of documents. It discussed reports on the status of corrective measures as of the end of each quarter of 2016 and was regularly informed of all actions carried out by Internal Audit. Management of corrective measures and their proper implementation were fully addressed. It also discussed the results of risk mapping, based upon which the annual internal audit plan for 2017 and a strategic plan for the period 2017–2021 were established and approved. It discussed, too, measures (and status of their implementation) taken in accordance with the findings presented in the Management Letter which had been prepared and presented to the Board of Directors by the external auditor Deloitte Audit, s.r.o.

The Board of Directors evaluated the overall functioning and efficiency of the Bank's management and control system, which is functional and effective. Furthermore, the Board of Directors addressed reports on the handling of complaints and claims (including complaints sent to the Bank's Ombudsman). The Board of Directors also discussed the Bank's strategic direction for the next year.

The Board of Directors discussed all issues falling within its competence as the sole shareholder in performing duties of the General Meeting in KB Group's subsidiaries, such as approving financial statements, election and remuneration of members of company bodies, amendments to the articles of association, appointment of auditors and other matters.

As part of its activities, the Board of Directors decided on many other issues related to organisational structure, approving directives within various arms or granting powers of attorney. Further steps were taken in the implementation plan for the utilisation of buildings for KB's head office. The new collective bargaining agreement was approved for the next four-year period.

The Board of Directors, as the founder, also discussed the orientation of Komerční banka's Jistota Foundation and it was informed of the Foundation's activities. The Board of Directors approved the financial contribution for the Foundation's activities and also a contribution to the budget of the Debt Advisory Centre. It discussed and approved contractual documentation related to co-operation with the European Investment Bank, Council of Europe Development Bank and European Investment Fund. It also decided on a partnership with Worldline SA/NV in the processing of card payments for merchants. Throughout the year, there was a transfer of part of the Bank's activities (merchant acquiring) to the Bank's subsidiary Cataps, s.r.o. Subsequently, an 80% stake in Cataps, s.r.o. was sold to Worldline.

Great attention was further devoted to corporate governance issues in the context of new developments in Czech legislation and in the context of corporate governance adopted by the parent company Société Générale. The Board of Directors evaluated its own activities in 2015 and submitted its report on those activities for this period to the Supervisory Board. The Board of Directors approved the distribution of competences among individual members and agreed the proposal for amendment of the Bank's Articles of Association, which were subsequently submitted to the General Meeting and at its meeting were approved. The main change that occurred was a splitting of the shares in issued in a ratio of 5:1, and thus a reduction in the nominal value of one share from CZK 500 to CZK 100. The aim of this step was to improve access to the Bank's shares for more investors. The change of Articles of Association also adjusted the position of the Audit Committee as one of the committees established by the Supervisory Board. Furthermore, the Board decided to cancel the listing of global depository receipts on the London Stock Exchange.

## Committees established by the Board of Directors

The Board of Directors establishes specialised committees to which it delegates authority for making decisions in the various activity areas assigned to them. It authorises them to co-ordinate selected activities and to exchange information and opinions. The Board of Directors approves the statutes of these committees, while their members are appointed by the CEO. These committees include the following:

### Project Management Committee (PMC)

The Project Management Committee makes and proposes decisions regarding KB's development activities and their prioritisation (KB's Project Plan), including to initiate, change or terminate important projects, as well as to measure and evaluate projects' contributions. It considers the material content of important projects and their links as well as their use of financial and non-financial resources. Each member of the committee has one vote. If a consensus is not reached, the committee acts based on the decision of its chairperson.

| Members | Positon |
|---|---|
| Albert Le DIRAC'H | Chairman of the Board of Directors, Chief Executive Officer |
| Libor LÖFLER | Member of the Board of Directors, Senior Executive Director, Chief Administrative Officer |
| Vladimír JEŘÁBEK | Member of the Board of Directors, Senior Executive Director, Distribution – Retail and Corporate |
| Jan POKORNÝ | Member of the Board of Directors, Senior Executive Director, TCA, SFA, IB[1] |
| Karel BERAN | Executive Director, Project Organisaton and Management |
| Patrice BEGUE | Executive Director, Marketing and Communication |
| Jiří ŠPERL | Executive Director, Strategy and Finance |
| Antonín PRELL | Executive Director, Information Technology |
| Yann De NANTEUIL | Executive Director, Risk Management |
| Secretary of the Committee: Aleš VEJVODA | |

### Watch Provision List Committee (WPLC)

The Watch Provision List Committee makes and proposes decisions regarding provisions. The Committee is responsible for clients' inclusion into or removal from the Watch Provision List, used for rating clients according to the CNB classification system and for determining the appropriate amount of provisions. The Committee decides on three levels. Each member of the WPLC expresses an opinion on proposals regarding each case discussed. A consensus of all regular members at the respective level is sought so that the final decision assumed by that level reflects the joint position of the risk management and business units. If a consensus is not reached (i.e. at least one of the regular members does not concur), then the case is moved up to the next WPLC level. If within WPLC Level 3 a consensus is not reached, then the final decision is made by the Chief Executive Officer. A higher level WPLC is entitled to review and change any decision of a lower level WPLC.

1 TCA – Top Corporations, SFA – Structured Financing, IB – Investment Banking

| Members – LEVEL 3 | Position |
|---|---|
| Albert Le DIRAC'H | Chairman of the Board of Directors, Chief Executive Officer |
| Yann De NANTEUIL | Executive Director, Risk Management |
| Radek TRACHTA | Executive Director, Top Corporations |
| Vladimír JEŘÁBEK | Member of the Board of Directors, Senior Executive Director, Distribution – Retail and Corporate |
| Jiří ŠPERL | Executive Director, Strategy and Finance |

| Members – LEVEL 2 | Position |
|---|---|
| Yann De NANTEUIL | Executive Director, Risk Management |
| Dušan ORDELT | Manager of Credit Risk Approval |
| Lukáš HORÁČEK | Manager of Loan Consulting |
| Radek TRACHTA | Executive Director, Top Corporations |
| Agness HENN | Deputy Manager of Corporate Credit Portfolio Management |

| Members – LEVEL 1 Pilsen | Position |
|---|---|
| Alena VACÍKOVÁ | Manager of Regional Credit Risk Assessment |
| Anna ŠÍPOVÁ | Head of Loan Portfolio Management – Corporate |
| Petr PARUŽEK | Head of Loan Portfolio Management – Corporate |
| Dana HNOJSKÁ | Head of Loan Portfolio Management – Retail |
| Alena KOTKOVÁ | Head of Loan Portfolio Management – Retail |

| Members – LEVEL 1 Hradec Králové | Position |
|---|---|
| Jiří DĚDEK | Manager of Regional Credit Risk Assessment |
| Alena SLÍPKOVÁ | Head of Loan Portfolio Management – Corporate |
| Vladislav BAREŠ | Head of Loan Portfolio Management – Corporate |
| Michal VOŠVRDA | Head of Loan Portfolio Management – Retail |
| Lenka KALINOVÁ | Head of Loan Portfolio Management – Retail |

| Members – LEVEL 1 Ostrava | Position |
|---|---|
| Lubomír ANDRLA | Manager of Regional Credit Risk Assessment |
| Miroslav SKLENÁŘ | Head of Loan Portfolio Management – Corporate |
| Milena VESELÁ | Head of Loan Portfolio Management – Corporate |
| Renata TOBIÁŠOVÁ | Head of Loan Portfolio Management – Retail |
| Libor LEGNER | Head of Loan Portfolio Management – Retail |

| Members – LEVEL 1 Brno | Position |
|---|---|
| Markéta RIESNEROVÁ | Manager of Regional Credit Risk Assessment |
| Petr LUKÁŠEK | Head of Loan Portfolio Management – Corporate |
| Vladimír MINICH | Head of Loan Portfolio Management – Corporate |
| Vlastimil DVOŘÁK | Head of Loan Portfolio Management – Retail |
| Ilona JARŮŠKOVÁ | Head of Loan Portfolio Management – Retail |

| Members – LEVEL 1 Prague | Position |
|---|---|
| Petr PLAŠIL | Risk manager (Prague Team) |
| Stanislav CHALUPA | Head of Loan Portfolio Management – Corporate |
| Kateřina MIKULÍKOVÁ | Head of Loan Portfolio Management – Corporate |
| Jana PURGEROVÁ | Head of Loan Portfolio Management – Retail |
| Secretary of the Committee: Blanka NEUHÄUSEL KOLÁŘOVÁ | |

### Assets and Liabilities Committee (ALCO)

The Assets and Liabilities Committee makes and proposes decisions regarding asset and liability management in KB. Each member of the committee has one vote. If a consensus is not reached, the committee acts based upon a simple majority of those members present.

| Members | Position |
|---|---|
| Libor LÖFLER | Member of the Board of Directors, Senior Executive Director, Chief Administrative Officer |
| Jiří ŠPERL | Executive Director, Strategy and Finance |
| Yann De NANTEUIL | Executive Director, Risk Management |
| Slawomir KOMONSKI | Executive Director, Investment Banking |
| Ivan VARGA | Manager of Trading and Institutional Sales |
| Tomáš FUCHS | Manager of ALM & Treasury |
| Secretary of the Committee: Tomáš FUCHS | |

### Commercial Committee (CC)

The Commercial Committee makes and proposes decisions in the area of business offers, business strategy and tactics, rates, prices and conditions. It also provides its opinions on selected new products in accordance with its statutes. A consensus of all members is sought. If a consensus is not reached, the committee acts based upon a simple majority of the members present, and, in the event of a tie, the chairperson has the deciding vote.

| Members | Position |
|---|---|
| Albert Le DIRAC´H | Chairman of the Board of Directors, Chief Executive Officer |
| Jan POKORNÝ | Member of the Board of Directors, Senior Executive Director, TCA, SFA, IB[1] |
| Libor LÖFLER | Member of the Board of Directors, Senior Executive Director, Chief Administrative Officer |
| Vladimír JEŘÁBEK | Member of the Board of Directors, Senior Executive Director, Distribution – Retail and Corporate |
| Patrice BEGUE | Executive Director, Marketing and Communication |
| Yann DUMONTHEIL | Executive Director, Retail Banking |
| Jitka HAUBOVÁ | Executive Director, Corporate Banking |
| Jiří ŠPERL | Executive Director, Strategy and Finance |
| Jana ŠVÁBENSKÁ | Executive Director, Transaction and Payment Services |
| Secretary of the Committee: Klára LOUDOVÁ | |

1) TCA – Top Corporations, SFA – Structured Financing, IB – Investment Banking

### Credit Risk Management Committee (CRMC)

The Credit Risk Management Committee makes and proposes decisions regarding credit risk management principles and their implementation. A decision may be taken if at least 50% of all members are present. A consensus of all members is sought. If a consensus is not reached, the committee acts based upon a simple majority of those members present having voting rights. If a majority is not reached, the decision is moved up to the Board of Directors.

| Members | Position |
|---|---|
| Yann De NANTEUIL | Executive Director, Risk Management |
| Jan SEVCIK | Deputy Senior Executive Director, Risk Management |
| Dušan ORDELT | Manager of Credit Risk Approval |
| Lenka DVOŘÁKOVÁ | Manager of Credit Portfolio Management |
| Leoš SOUČEK | Deputy Executive Director for Marketing and Communication |
| Lukáš VOBORSKÝ | Manager of Corporate Credit Analysis |
| Etienne LOULERGUE | Deputy Executive Director, Strategy and Finance |
| Tomáš DOLEŽAL | Manager of Operational Risk |
| Pavol BLAHO | Manager of Risk and Analytics Solutions |
| Milan TŮMA | Manager of Internal Audit |
| Secretary of the Committee: Petr ZDENĚK | |

### Investment Banking New Product Committee (IB NPC)

The Investment Banking New Product Committee makes and proposes decisions on new investment banking products in accordance with its statutes. Its activities include assessing the risks related to new or significantly altered products, establishing the conditions for launching products and monitoring that these conditions are met. A consensus of all members is sought.
If a consensus is not reached, the decision is made by the Chief Executive Officer. If a product is not launched into the market within six months of approval, then the decision is void and the product must be resubmitted to the Committee for new approval.

| Members | Position |
|---|---|
| Yann De NANTEUIL | Executive Director, Risk Management |
| Jan POKORNÝ | Member of the Board of Directors, Senior Executive Director, TCA, SFA, IB[1] |
| Alan COQ | Manager of Capital Markets Risks |
| Dušan ORDELT | Manager of Credit Risk Approval |
| Norbert VANĚK | Manager of Investment Banking Services |
| Tomáš HORA | Head of Investment Products |
| Tomáš SLABOCH | Manager of IT Application Services |
| Tomáš CHOUTKA | Manager of Compliance |
| Jakub DOSTÁLEK | Manager of Tax |
| Tomáš FUCHS | Manager of ALM & Treasury |
| Tomáš DOLEŽAL | Manager of Operational Risk |
| Ida BALUSKOVÁ | Manager of Accounting and Reporting |
| Secretary of the Committee: Norbert VANĚK | |

1) TCA – Top Corporations, SFA – Structured Financing, IB – Investment Banking

### Corporate and Retail Banking New Product Committee (CRB NPC)

The Corporate and Retail Banking New Product Committee makes and proposes decisions on new products other than investment banking products in accordance with its statutes. Its activities include assessing the risks related to new or significantly altered products, establishing the conditions for launching products and monitoring that these conditions are met. A consensus of all members is sought. If a consensus is not reached, the decision is made by the Chief Executive Officer. If a product is not launched to the market within six months of approval, then the decision is void and the product must be resubmitted to the Committee for new approval.

| Members | Position |
|---|---|
| Jan ŠEVČÍK | Deputy Senior Executive Director, Risk Management |
| Patrice BEGUE | Executive Director, Marketing and Communication |
| Tomáš DOLEŽAL | Manager of Operational Risk |
| Yann DUMONTHEIL | Executive Director, Retail Banking |
| Jitka HAUBOVÁ | Executive Director, Corporate Banking |
| Antonín PRELL | Executive Director, Information Technology |
| Leoš SOUČEK | Deputy Executive Director, Marketing and Communication |
| Robert ŠÁROVEC | Deputy Executive Director, Transaction and Payment Services |
| František KUBALA | Deputy Executive Director, Project Organisation and Management |
| Matěj STRANSKÝ | Manager of Supervision and Risk Measurement |
| Etienne LOULERGUE | Deputy Executive Director, Strategy and Finance |
| Radek TRACHTA | Executive Director, Top corporations |
| Secretary of the Committee: Marcela KRÁLOVÁ | |

### Operational Risk Committee (ORC)

The Operational Risk Committee makes and proposes decisions regarding operational risks and safety. For a decision to be taken, at least 50% of all members must be present. A decision must be adopted by a majority of votes of those members present. If a consensus is not reached, the decision is adopted at the Board of Directors level.

| Members | Position |
|---|---|
| Peter PALEČKA | Member of the Board of Directors, Senior Executive Director, Corporate Secretary |
| Tomáš DOLEŽAL | Manager of Operational Risk |
| Tomáš CHOUTKA | Manager of Compliance |
| Martin ZEMEK | Manager of Regional Support Services Management |
| Martin PARUCH | Deputy Senior Executive Director, Distribution – Retail and Corporate, Manager of Network Management Support |
| Etienne LOULERGUE | Deputy Executive Director, Strategy and Finance |
| Robert ŠÁROVEC | Deputy Executive Director, Transaction and Payment Services |
| Pavel POLÁK | Manager of IT Security |
| Sandra DORILLEAU | Manager of Risk Supervision and Prevention |
| Luděk NOVÝ | Head of Risk Management – Retail |
| David KUBĚJ | Manager of Global Strategy and Development |
| Denisa SLÁDKOVÁ | Manager of HR Services Centre |
| Martin BERDYCH | Manager of Legal Services |
| Zuzana MELICHAROVÁ | Head of Top Corporations Business Divisions Support |
| Aleš VEJVODA | Manager of Project Portfolio Management |
| Bohumil ČUČELA | Deputy Executive Director, Internal Audit in KB and CEN region |
| Leoš SOUČEK | Deputy Executive Director, Marketing and Communication |
| Norbert VANĚK | Manager of Investment Banking Services |
| Petr NOVÁK | Manager of Information Management |
| Secretary of the committee: Dušan PAMĚTICKÝ | |

## Information about special rules for the election and recall of members of the Board of Directors

Members of the Board of Directors of Komerční banka are elected by the Supervisory Board upon nomination by its Nominations Committee. A nominee must receive an absolute majority of votes of all Supervisory Board members. Members of the Board of Directors are elected to terms of four years. Only persons fulfilling the conditions for serving as a member of a Board of Directors as specified by the Civil Code, Act on Business Corporations and Banking Act may become members of the Board of Directors. The Nominations Committee ensures the trustworthiness, adequate professional qualifications and experience of the members of the Board of Directors. The Nominations Committee also assesses the balance of competences and experience as well as diversity in the Board's overall composition. The professional qualifications, trustworthiness and experience of the members of the Board of Directors are assessed by the Czech National Bank.

The Supervisory Board has the right to decide at any time to recall a member of the Board of Directors. Such decision is carried if approved by an absolute majority of its members. The Supervisory Board's decision is based on a proposal from the Supervisory Board's Nominations Committee.

## Information about special competences of the Board of Directors under the law regulating legal relations of corporations and co-operatives

The Board of Directors of Komerční banka is the corporate body that decides upon all matters concerning the Bank with the exception of those matters falling within the powers of the General Meeting or of the Supervisory Board.

**It is within the Board of Directors' exclusive competences to:**

a) convene the General Meeting and implement its resolutions;
b) submit to the General Meeting for its approval the annual, extraordinary and consolidated financial statements and the interim financial statements along with a proposal for the distribution of profit (which must be available to the shareholders for inspection at least 30 days prior to the date of the General Meeting) or a proposal for coverage of a loss;
c) submit to the General Meeting proposals for amendments to and changes of the Articles of Association as well as proposals for increasing or decreasing the Bank's registered capital;
d) submit to the General Meeting a report on the Bank's business activities and on the state of the Bank's property at least once for each accounting period, as well as the annual report;
e) decide upon granting and revoking powers of procuration;
f) decide upon the appointment, removal and compensation of selected managers of the Bank;
g) approve acts in connection with the realisation of security instruments for the Bank's claims whose price exceeded CZK 100,000,000 as of the date of the claim's origin if the presumed realisation price thereof is lower than 50% of the security instrument's price ascertained upon entering into the loan agreement;
h) submit to the Supervisory Board for its information quarterly and half-yearly financial statements;
i) decide upon acts which are beyond the scope of the Bank's usual business relationships;
j) define and regularly evaluate the Bank's overall strategy, including the setting of the principles and targets for its fulfilment and ensuring the continued and effective operation of the internal control system;
k) approve the Bank's annual plans and budgets;
l) enter into a contract with an auditor for performing the statutory audit or, as the case may be, for the provision of additional services;
m) inform the Supervisory Board of the General Meeting date no later than within the period specified by the Act on Business Corporations for the General Meeting to be convened;
n) decide upon the issue of bonds of the Bank with the exception of decisions on the issue of bonds for which the decision of the General Meeting is required by law;
o) decide upon an increase in the registered capital if so authorised by the General Meeting;
p) enter into collective agreements;
q) decide upon providing loans or securing debts to persons or entities having a special relationship to the Bank pursuant to the Banking Act;
r) approve the charter and subject of the risk management functions, compliance functions and internal audit functions, as well as the strategic and periodic plan of internal audit;
s) decide about paying out a share in profit based upon fulfilment of conditions established by generally binding legal regulations;
t) approve and regularly evaluate the security principles of the Bank, including the security principles for information systems;
u) decide upon establishing other funds and the rules governing the creation and usage thereof;
v) prepare the report on relations among related entities pursuant to the Act on Business Corporations;
w) approve and regularly evaluate the Bank's organisational structure so that it is functional and efficient, including segregation of duties and preventing potential conflicts of interest;
x) approve the principles of the personnel and remuneration policy;
y) evaluate the overall functioning and effectiveness of the management and control system at least once annually;
z) approve and regularly evaluate the risk management strategy, the strategy relating to the capital and to capital ratios, the strategy for the information and communication system's development, and the strategy for human resources management;
aa) approve and regularly evaluate the principles of the internal control system, including principles aiming to prevent the occurrence of any possible conflict of interest and principles related to compliance and internal audit and security policies; and
bb) discuss the audit report with the auditor.

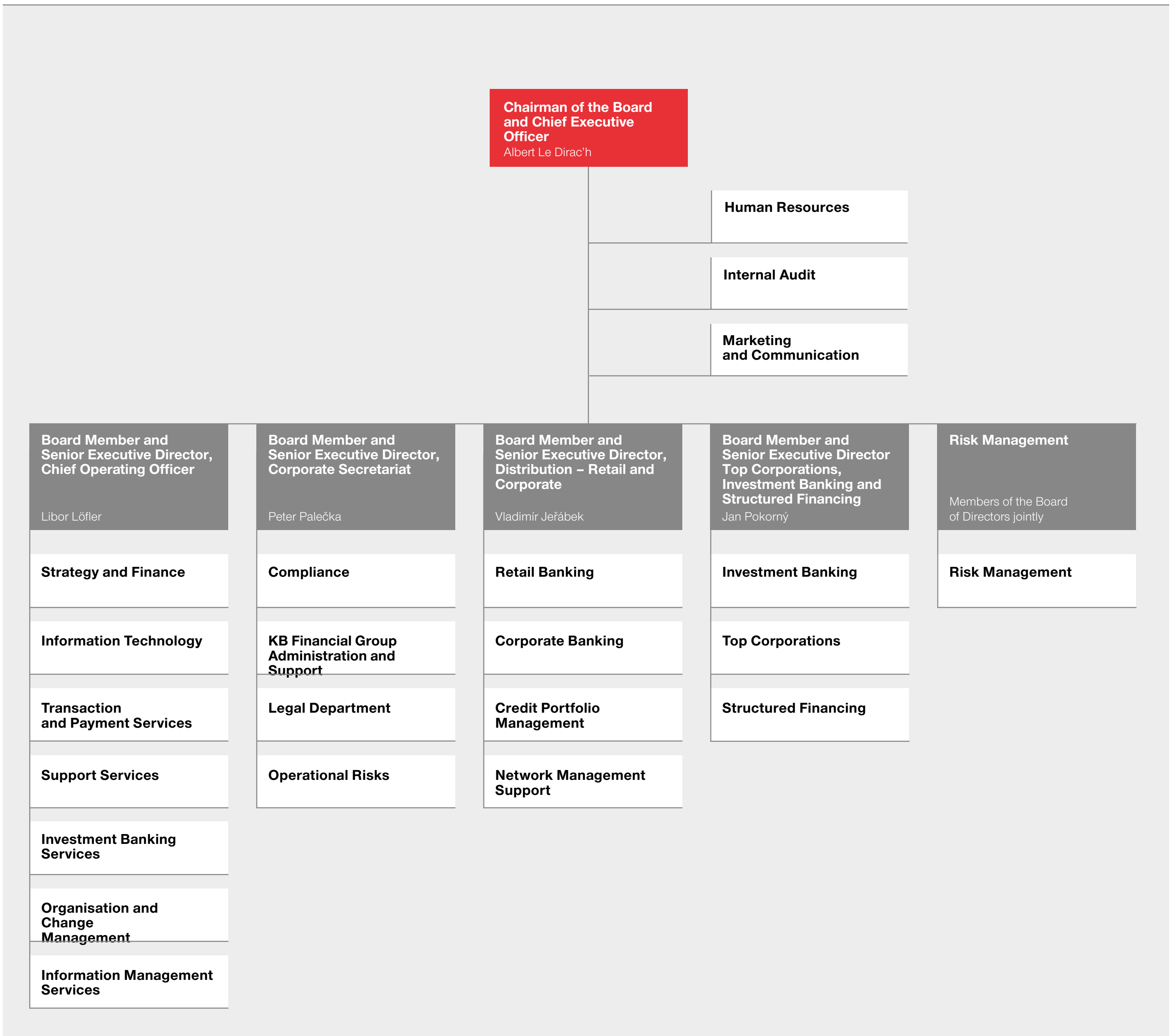
**In addition to the aforementioned, the Board of Directors shall in particular:**

a) manage the activities of the Bank and conduct its business affairs;
b) ensure proper conduct of the Bank's accounting, including the proper administrative and accounting processes;
c) exercise employer's rights;
d) exercise rights in respect to the Bank's property interests flowing from the Bank's ownership holdings;
e) approve the acquisition or disposal of the Bank's fixed assets exceeding CZK 30,000,000 in value as a single case or as a total of related cases; and
f) approve the business continuity plan.

The Board of Directors was not authorised to make a decision on increasing registered capital. Based on the consent of the General Meeting held on 22 April 2016, Komerční banka was authorised to acquire its ordinary shares into treasury. The conditions and information on the acquisition of its own shares are provided in the Acquisition of Treasury Shares chapter of this annual report.

# Organisational chart of Komerční banka

(as of 31 December 2016)



# Supervisory Board

The Supervisory Board is the supervisory authority of the Bank. It supervises the exercise of the Board of Directors' powers, the conduct of the Bank's business activities and the effectiveness and efficiency of the Bank's management and control system as a whole.

The Supervisory Board consists of nine members, who are individuals meeting the statutory requirements for becoming a member of the Bank's Supervisory Board. Two-thirds of them are elected by the General Meeting and one-third by the Bank's employees to terms of four years.

In accordance with the requirement of the Czech National Bank, Komerční banka declares that the members of the Board of Directors of Komerční banka have not in the past 5 years been convicted of any criminal offence and that no charges, accusations or other sanctions have been filed against them by a regulatory authority, except for the member of the Supervisory Board Giovanni Luca Soma, who was fined EUR 15,000 by the Bank of Italy as a member of the Executive Board of Fiditalia for deficiencies in control and organisation to ensure transparency of client conditions. No bankruptcy, receivership or liquidation was declared in relation to the stated persons in the past 5 years.

## Composition of the Supervisory Board

**Jean-Luc Parer**
Chairman of the Supervisory Board (appointed as a substitute member of the Supervisory Board from 27 September 2012 until 24 April 2013 and thereafter elected by the General Meeting; elected Chairman as from 1 May 2013)

**Giovanni Luca Soma**
Vice-Chairman of the Supervisory Board (since 1 May 2013)

**Laurent Goutard**
Member of the Supervisory Board (since 1 May 2013)

**Bořivoj Kačena**
Independent Member of the Supervisory Board (since 29 April 2008, re-elected on 30 April 2012 and on 1 May 2016)

**Petr Laube**
Independent Member of the Supervisory Board (since 8 October 2001, re-elected on 29 April 2005, on 30 April 2009 and on 1 May 2013)

**Sylvie Rémond**
Member of the Supervisory Board (since 23 April 2015)

**Pavel Jelínek**
Member of the Supervisory Board elected by KB's employees (since 1 June 2013)

**Dana Neubauerová**
Member of the Supervisory Board elected by KB's employees (since 29 May 2009, re-elected on 1 June 2013)

**Karel Přibil**
Member of the Supervisory Board elected by KB's employees (since 29 May 2009, re-elected on 1 June 2013)

**Jean-Luc Parer**
A graduate of the Business School HEC Paris and a Master's Graduate of Law, he began working at Société Générale in 1981 in the Inspection Department. From 1991 to 2001, he was head of structured financing within the Investment Banking Division. From 2001 to 2003, he participated in the development of the Debt Finance Department, and from 2003 to 2005 he was responsible for supervising activities in the debt capital markets. In 2005, he became Deputy Director of Debt Finance, and in 2008 he was appointed Director of Capital Markets and Finance. In 2009, he became Director of Global Finance. Since 2012, he has been a member of the Executive Committee of the Société Générale Group, serving as head of the International Banking Division and, since 2013, Head of the International Banking, Financial Services and Insurance Industry Division. Since 2012, he also has been a member of the Supervisory Board of Komerční banka and since 2013, he has been its Chairman.

**Giovanni Luca Soma**
An MBA graduate of the University of Turin, Italy, and a graduate of LUISS University with a degree in business economics, he also holds qualifications to work as a certified auditor and certified public accountant. From 1984 to 1989, he was the manager of Arthur Young Consulting in Rome, Italy. From 1989 to 1994, he worked with Deloitte & Touche Consulting in Milan, Italy. During 1994–1997, he served as Sales and International Services Director of Hyperion Software Inc. Between 1997 and 1998, he served as managing director of GE Capital Insurance and subsequently, during 1998–1999, as Corporate Sales Director for Italy in GE Capital. From 1999 to 2000, he served as CEO of Dial Italia (Barclays Group). During 2000–2005, he served as CEO of ALD Automotive Italy, 2005–2007 as Chairman of ANIASA, the Italian Association of Automotive Leasing and Services Providers, 2006–2008 as Group Regional Director and Deputy CEO of the ALD International Paris, and 2008–2011 as CEO of the ALD International Paris in France. Between December 2012 and September 2013, he was Deputy Head of the International Retail Banking Department and he has become a member of the Group Management Committee of Société Générale. He currently serves as CEO of SG Consumer Finance, France (since 2010) and Deputy Head of IBFS, International Banking and Financial Services (since December 2012). Since 2013, he has been a Member and Vice-Chairman of the Supervisory Board of Komerční banka.

**Laurent Goutard**
A graduate of four-year economics studies at the University of Paris-Dauphine and of the Paris Institute of Political Studies, faculty of public services, with a major in economics, he joined Société Générale in 1986, working first at the General Inspection and then, between 1993 and 1996, as Deputy Managing Director for Large Corporations at the Paris–Opera Branch. During 1996–1998, he was Director of the Corporate Banking Division on the French territory. From 1998 to June 2004, he was a member of the Board of Directors and Chief Executive Officer, later Chairman of the Board of Directors of Société Générale Marocaine de Banques. In 2004, he became Vice-Chairman of the Board of Directors and in 2005 Chairman of the Board of Directors and CEO of Komerční banka. He served in that position until 2009, when he became French Network Director and Delegated Director for Retail Banking of Société Générale in France. Since 2011, he has served as French Network Director and Director for Retail Banking of Société Générale in France. He has been a Member of the Supervisory Board of Komerční banka since 2013.

**Pavel Jelínek**
Having completed studies at the Secondary School of Economics in Chrudim, he began working in Komerční banka in 1993 in various positions in cash processing (as a warden, ATM operator, cashier, deputy manager of cash section). Beginning in 2002, he was commercial clerk, and later he was a relationship manager for individuals, a relationship manager for small businesses and a team leader. Until the end of 2013, he was a relationship manager for top small business clients, and since 2014 he has been a relationship manager for corporations. He has been a member of trade unions at KB since joining the Bank. Since 1994, he has represented employees as chairman of the union's local unit in Pardubice, and at the same time he has been a member of the all-company committee of trade unions at KB. Since 2011, he has been a member of the union's negotiating team for collective negotiation with the employer. Since 2013, he has been a Member of the Supervisory Board of Komerční banka.

**Bořivoj Kačena**
A graduate of the Czech Technical University in Prague (Faculty of Civil Engineering), he started in 1966 to work for Stavby silnic a železnic, n. p. (SSŽ), where he held various positions. From 1978, he worked in SSŽ as director of its branch office 4, and from 1983 as director of the organisation "Investor of Transport Construction" for metro and urban road construction within the Prague Public Transit Company. He became director of the state enterprise SSŽ in November 1988 and its chief executive officer and Chairman of the Board of Directors in 1992. From 2007 to April 2008, he was the Chairman of the Board of Directors of SSŽ. Since 2008, he has been a Member of the Supervisory Board of Komerční banka.

**Petr Laube**
A graduate of the University of Economics, Prague, specialised in foreign trade, he worked during 1974 to 1991 at Polytechna, a foreign trade company for technical co-operation. From 1991 to 1992, he was at Deutsche Bank, A.G. in Nuremberg. Between 1992 and 1993, he worked for Lafarge Coppée, Paris, and since 1993 he was Chief Executive Officer and Chairman of the Board of Directors of Lafarge Cement, a.s., Prague. From 2005, he served as director of the segment electricity, gas and liquid fuels at SG&A at Lafarge, S.A., Paris. From January 2007, he was Chief Executive Officer of Lafarge Cement, a.s., in Ukraine. He has been retired since December 2009. Since 2001, he has been a Member of the Supervisory Board of Komerční banka. Since 2014, he has been Chairman of the Supervisory Board of LafargeHolcim, Česká republika.

**Dana Neubauerová**
Having completed studies at the Secondary School of Economics in Havlíčkův Brod, she has been working in Komerční banka (formerly State Bank of Czechoslovakia) since 1984. She moved over time through a number of positions from data acquisition to liquidation worker, and then from 1991 to 1998 she worked as head of a services department. From June 1998 to 2002, she worked as a commercial clerk for entrepreneurs and until 2006 as the bank advisers team leader. From 1 March 2006, she was appointed director of the Havlíčkův Brod branch, and then was director of the Level 2 Havlíčkův Brod branch from 1 October 2008. From 1 July 2009 to 31 December 2015, she was the director of the Jihlava branch. From 1 January 2016, she is director of the Pelhřimov branch. She has been a union member since joining Komerční banka and served as chairwoman of the union's local unit in Havlíčkův Brod from 1990 to June 2008. Since 2009, she has been a Member of the Supervisory Board of Komerční banka.

**Karel Přibil**
A graduate from the Faculty of Education at Charles University in Prague, he defended his doctoral thesis there in 1986. Since joining Komerční banka in 1993, he has worked in various positions at headquarters – first as a specialist officer, then in 1995 in internal services and from 2003 as a property administration specialist. From 1 March 2006, he has held the office of Chairman of the Trade Union Committee and been a member of other union bodies. He has been a union member since joining Komerční banka and chairman of the union's headquarters unit and a member of KB's Trade Union Committee since the mid-1990s. He also participates in collective bargaining. He has been a Member of the Supervisory Board of Komerční banka since 2009.

**Sylvie Rémond**
A graduate of the Rouen Business School, she joined Société Générale in 1985, working first in the Development Division and then, between 1985 and 1989, as a product manager within the Individual Client Division. During 1989–1992, she worked as an aerospace group credit analyst within the Large Corporate Division. In 1992, she started work within the Structured Finance Department, first in a senior position in the area of acquisition finance, and later, in 2000, in the position of Co-Head of Corporate and Acquisition Finance Syndication. Between 2004 and 2008, she served as Co-head and, between 2008 and 2010, as Head of Credit Risk for Corporate and Investment Banking. During 2010–2014, she served as Deputy Chief Risk Officer. In 2015, she became Co-Head of Corporate and Investment Banking. She is also a member of the Group Management Committee. The General Meeting elected Ms Rémond a Member of the Supervisory Board of Komerční banka with effect from 23 April 2015.

## Activity report of the Supervisory Board

Regular meetings of the Supervisory Board shall be held once per calendar quarter with the possibility of remote voting. A quorum of the Supervisory Board shall be constituted if at least five members of the Supervisory Board are present at the meeting. Resolutions of the Supervisory Board are adopted by an absolute majority of all its members.

In 2016, the Supervisory Board held four regular meetings and one remote vote in accordance with the Bank's Articles of Association. The average meeting length was 1 hour and 20 minutes. The Supervisory Board reviewed the Bank's separate and consolidated financial statements as of 31 December 2015 prepared under International Financial Reporting Standards (IFRS) and recommended that the General Meeting approve both sets of financial statements as proposed by the Bank's Board of Directors.

The Supervisory Board also examined the Board of Directors' proposal for distribution of net profit for the 2015 accounting period and recommended that the General Meeting approve this proposal. Furthermore, it reviewed the Report on Relations among Related Entities for 2015 compiled in accordance with the provisions of § 82 et seq. of Act No. 90/2012 Coll., on Business Corporations and Co-operatives (the Act on Business Corporations) and stated that, based on the presented documents, Komerční banka did not incur during the accounting period from 1 January 2015 to 31 December 2015 any damages resulting from the contracts and agreements made with related entities. At the same time, upon recommendation of the Audit Committee, the Supervisory Board agreed to submit a proposal to the General Meeting to approve Deloitte Audit s.r.o. as the external auditor of the Bank for the year 2016.

During 2016, the Supervisory Board was continuously informed of the Bank's activities and was regularly presented reports and analyses. The Supervisory Board assessed, in particular, the functionality and efficiency of the Bank's internal control systems, concluding that the internal control systems are functional and effective. Moreover, it examined the 2015 annual assessment report on KB's system for anti-money laundering and preventing the financing of terrorism and the annual compliance management report. KB Group's budget for 2016 was submitted for discussion to the Supervisory Board. The Supervisory Board discussed remuneration of the members of the Board of Directors and decided on the amounts of bonuses, the payment of which is subject to the principles (scheme) of deferred bonuses. The Supervisory Board also discussed developments in the areas of employee demographics, sickness rate and overtime. It discussed the annual analysis as to the handling of all complaints sent to KB and its Ombudsman. The Activity Report of the Board of Directors for 2015 also was presented to the Supervisory Board. The Supervisory Board discussed the resignation of one member of the Board of Directors of the Bank and based on the Nominations Committee proposal elected a new member of the Board of Directors.

The Supervisory Board regularly discussed the Bank's quarterly financial results and its position on the market with a view to development of the macroeconomic environment. Furthermore, it discussed the actions of the Internal Audit and their results in individual periods of the year, as well as the internal audit plan for 2017 and the strategic plan for 2017–2021. In the course of its activities, the Supervisory Board continued to rely on the opinion of its Audit, Risk, Remuneration and Nominations committees and was informed of the issues discussed by these committees. The Supervisory Board approved the new version of the Statute of the Audit Committee and the Internal Audit of KB financial Group.

## The Supervisory Board's committees

The Supervisory Board established within its competences the Audit Committee, the Risk Committee, the Nominations Committee and the Remuneration Committee as its advisory and initiative bodies. Committees of the Supervisory Board provide the Supervisory Board with regular reports on their activities and within the areas entrusted to their jurisdiction submit to the Supervisory Board recommendations directed to preparing resolutions for adoption by the Supervisory Board.

### Audit Committee

The Audit Committee was established in accordance with Act No. 93/2009 Coll., on Auditors, as amended. Its powers are stipulated by that act and the statute of the committee. Based on the amendments to the Articles of Association approved by the General Meeting on 22 April 2016, this committee was included among the Supervisory Board committees because of its proportional position in relation to other committees and inasmuch as the committee is composed of Supervisory Board members.

The Audit Committee consists of three members, individuals, who meet the requirements for performing duties of a member of an audit committee set forth by legal regulations and by the Status of the committee. Audit Committee members shall be appointed by the General Meeting from the members of the Supervisory Board for terms of four years. The major members of the Audit Committee, including its Chairman, are independent and professionally qualified.

**Composition of the Audit Committee**
**Petr Laube**
Independent Member of the Audit Committee (since 29 April 2009) and Chairman of the Audit Committee (since 30 September 2010, re-elected on 30 April 2013)

**Jean-Luc Parer**
Member of the Audit Committee (appointed as a substitute member of the Audit Committee from 27 September 2012 to 24 April 2013 and thereafter elected by the General Meeting as from 25 April 2013, membership terminated as of 22 April 2016)

**Giovanni Luca Soma**
Member of the Audit Committee (since 25 April 2013), Vice-Chairman of the Audit Committee (since 3 May 2016)

**Bořivoj Kačena**
Independent member of the Audit Committee (since 23 April 2016)

The Audit Committee meets as a rule once per quarter, but at least four times in a calendar year. A quorum of the Audit Committee shall be constituted if a simple majority of all Audit Committee members attend the meeting. Decisions on all matters discussed by the Audit Committee must receive an absolute majority of votes to be carried. If the votes are equal, the chairperson shall cast the deciding vote. The person in question shall not vote in the proceedings with respect to the election and removal of the Chairman and Vice-Chairman of the Audit Committee.

The Audit Committee held seven regular meetings in 2016. The average meeting length was 60 minutes. The committee performed its monitoring activities and worked closely within the Bank, especially with Internal Audit, Strategy and Finance, Risk Management, and Compliance departments, and also with the external auditor, who kept it informed about the ongoing audit of the Bank.

The committee discussed KB Group's annual financial results for 2015, the consolidated and separate financial statements and notes thereto as of 31 December 2015 prepared under International Financial Reporting Standards (IFRS), and the proposal for distribution of net profit for 2015. In this context, it discussed the scope, strategy and the main areas of external audit of financial statements for 2015, prepared by Deloitte Audit, s.r.o. It further evaluated the independence of the external auditor and recommended that the Supervisory Board submit to the General Meeting for approval a proposal to appoint Deloitte Audit, s.r.o. as the Bank's external auditor for 2016. KB Group's budget for 2016 was presented to the committee for discussion. The committee also regularly discussed Internal Audit's reports on the status of corrective measures and was continuously informed about all of Internal Audit's investigations conducted in individual periods. The committee discussed the Management Letter prepared by the external auditor, Deloitte Audit, s.r.o. It was informed about the external auditor's plan in compiling the financial statements for 2016. Furthermore, the committee examined in detail risk mapping, the annual internal audit plan for 2017, and the strategic plan for 2017–2021.

The Audit Committee regularly discussed at its meetings the Group's financial results for each quarter. Attention was also devoted to the capital adequacy of the Bank and Group. In this context, the committee discussed the Bank's capital management strategy. In particular with respect to new regulatory requirements on capital base, it also discussed the dividend policy in relation to the profit for the year 2016. The Committee was regularly informed about the Bank's functioning in the internal control area and the development of all associated risks that it evaluated. The Committee also discussed an update to its Status and the Status of the KB Group's Internal Audit and elected its Vice-Chairman. The committee discussed the preliminary text of the report on the audit of financial statements for 2016, prepared by Deloitte Audit, s.r.o.

### Risk Committee

The Risk Committee has three members, one of whom is independent. The committee meets according to need, but at least twice per year. A quorum is constituted if a simple majority of all members of the committee is present at the meeting. Resolutions shall be adopted by agreement of an absolute majority of all its members.

**Composition of the Risk Committee**
**Petr Laube**
Independent Member and Chairman of the Risk Committee (from 25 September 2014)

**Jean-Luc Parer**
Member of the Risk Committee (from 25 September 2014)

**Giovanni Luca Soma**
Member of the Risk Committee (from 25 September 2014)

The committee held two regular meetings in 2016. The average length of the sessions was 1 hour and 30 minutes. The committee discussed all issues of the Bank's risk management system including the Bank's credit risk profile. It provided recommendations to the Supervisory Board within the scope of its powers.

### Remuneration Committee

The Remuneration Committee has three members, one of whom is independent. The committee meets according to need, but at least twice per year. A quorum is constituted if a simple majority of all members of the committee is present at the meeting. Resolutions shall be adopted by agreement of an absolute majority of all its members.

**Composition of the Remuneration Committee**
**Jean-Luc Parer**
Chairman of the Remuneration Committee
(from 25 September 2014)

**Giovanni Luca Soma**
Member of the Remuneration Committee
(from 25 September 2014)

**Bořivoj Kačena**
Independent Member of the Remuneration Committee
(from 25 September 2014)

The committee held three regular meetings in 2016 and one remote vote. The average length of the sessions was 1 hour. The committee discussed issues of the deferred bonus scheme and remuneration of KB's employees. It provided recommendations to the Supervisory Board within the scope of its powers. Moreover, it discussed and provided its recommendations for remunerating members of the Board of Directors, and it provided information in relation to updating the remuneration principles. The committee was informed on the progress of collective bargaining and further on the regulatory changes of the CNB and their impacts on KB.

### Nominations Committee

The Nominations Committee has three members, one of whom is independent. The committee meets according to need, but at least twice per year. A quorum is constituted if a simple majority of all members of the committee is present at the meeting. Resolutions shall be adopted by agreement of an absolute majority of all its members.

**Composition of the Nominations Committee**
**Jean-Luc Parer**
Chairman of the Nominations Committee
(from 25 September 2014)

**Giovanni Luca Soma**
Member of the Nominations Committee
(from 25 September 2014)

**Bořivoj Kačena**
Independent Member of the Nominations Committee
(from 25 September 2014)

The committee held a single one-hour regular meeting in 2016 and two remote votes. The committee discussed issues of the Bank's personnel policy and proposed election of members of the Board of Directors. It furthermore evaluated the structure, size, composition and performance of the Board of Directors and Supervisory Board. It discussed the evaluation as to the trustworthiness, competence and experience regarding individual members of the Board of Directors and the Supervisory Board, as well as both of these bodies as a whole.

## Emoluments and benefits to members of the Board of Directors and Supervisory Board

In relation to his or her work in the Bank, no person with executive power has any conflict of interests between the duties of a person with executive power in the Bank and that person's private interests or other duties. Komerční banka has concluded service contracts with all members of the Board of Directors, and these were approved by the Supervisory Board. The contracts are concluded for the term of office of each member of the Board of Directors. The contracts provide no benefits upon termination of service. Certain members of the Board of Directors also have concluded contracts with the Bank's subsidiaries to serve as members of their supervisory boards. In these cases, the contracting parties are as specified in the descriptions of functions within the subsidiaries stated in the section "Composition of the Board of Directors". Chairman of the Board of Directors Albert Le Dirac'h and members of the Board of Directors Aurélien Viry and Karel Vašák have employment contracts signed with Société Générale S.A., and they have been assigned to serve as the Bank's directors.

### Principles of remuneration for members of the Board of Directors

Remuneration for members of the Board of Directors is in accordance with the EU's Capital Requirements Directive IV and its transposition into Czech law by CNB Decree No. 163/2014 Coll., as amended. The Supervisory Board decides on the amounts of remuneration based upon a proposal from its Remuneration Committee.

Remuneration for members of the Board of Directors consists of fixed and variable parts. The fixed remuneration is paid monthly, and its amount reflects the experience and responsibilities of the respective member of the Board of Directors. The variable part of the remuneration (the annual performance bonus) is not an automatic entitlement, reflects the performance of the member of the Board of Directors during the year, and is closely linked with the results of the Bank. In deciding the amount of the variable remuneration, the Supervisory Board and its Remuneration Committee assess all relevant financial and business indicators, including the development of net profit, market shares, net banking income, costs, and cost of risk. In deciding the amount of the variable remuneration, the Supervisory Board and its Remuneration Committee also take into account the results of an independent evaluation made by Compliance and Risk Management as to the quality of the performance of individual members of the Board of Directors in terms of risk management. The maximum amount of the variable remuneration may not exceed 200% of the basic salary, while variable remuneration greater than 100% of the basic salary is subject to approval by the General Meeting.

The budget for the variable remuneration as a whole is set in accordance with the financial plan for the given fiscal year. In accordance with its strategy, KB takes into account planned year-on-year changes in net operating income, operating expenses, allowances for loan losses and other risks (the cost of risk), and net profit at Komerční banka's separate (unconsolidated) level, excluding the effect of dividends received. The budget for the variable remuneration as a whole is drawn depending on KB's business plan being fulfilled in all its main indicators. It may be decreased by 0–100% depending on fulfilment of the key indicators net banking income, business performance, operating expenses, cost of risk, net profit including exceptional items, capital adequacy and the Bank's liquidity, as well as in accordance with quarterly results and cumulative results from the beginning of the fiscal year.

Payment of the variable remuneration is made with substantial delay in relation to the entire deferred remuneration and a retained part of the non-deferred remuneration. As a result, payment of 70% or 80% of the variable part is delayed. Given the ratio between the variable remuneration and the basic salary, the variable remuneration is paid in two distinct regimes.

If the variable part is greater than 100% of the basic salary and at the same time less than or equal to EUR 300,000, then 70% of the variable part is spread over three years. The first deferred part of 30% is transformed into a non-monetary instrument linked to the price of KB shares and is paid after a deferral period of nine months. Payment of the remaining 40% of the deferred amount is made on a straight-line basis over three years as follows: The first payment is made in March of the year following the year the bonus was awarded (N+1). The remaining two parts are transformed into non-monetary instruments linked to the price of KB shares, awarded in March of years N+2 and N+3, and always paid after a deferral period of nine months. The non-deferred part of the variable remuneration amounting to 30% of the awarded amount is paid in March of the year the bonus was awarded (year N).

If the variable part is greater than EUR 300,000, then 80% of the variable part is spread over three years. The first deferred part of 20% is transformed into a non-monetary instrument linked to the price of KB shares and is paid after a retention period of nine months. Payment of the remaining 60% of the deferred amount is made on a straight-line basis over three years, similarly as in the aforementioned case. The non-deferred part of the variable remuneration amounting to 20% of the awarded amount is paid in March of the year the bonus was awarded (N).

Settlement (payment) of the part of the bonus linked to the KB share price is in cash. Members of the Board of Directors may not hedge price movements of the non-monetary instruments. The variable remuneration awarded need not be paid in part or in full in cases where a member of the Board of Directors exposes the Bank to a level of risk above that considered acceptable by the Bank, where his or her conduct causes material damage to the Bank, or where he or she materially breaches the Bank's internal regulations (e.g. by behaving unethically) or legal regulations. The bonus also need not be paid in the case that it was awarded based upon deliberately incorrect or misleading information.

The reference price of the non-monetary instrument is determined as the arithmetic mean of the daily closing prices for KB shares on the Prague Stock Exchange (PSE) in the 20 days preceding the record date. In 2016, the record date for determining the initial reference price of the non-monetary instrument was 13 March. The number of non-monetary instruments awarded to members of the Board of Directors was calculated as of this date. In 2016, the next record date for determining the final amount for payment of the respective variable remuneration according to the number of non-monetary instruments awarded and KB share price on the PSE was 13 December 2016. Both record dates were fixed by the Remuneration Committee of the Supervisory Board.

In addition to the aforementioned remuneration, those members of the Board of Directors having Czech citizenship are entitled to the following additional remuneration:

a) above-standard health care (Santé Silver Card);
b) meal vouchers valued at CZK 85 per day at no cost to the employees;
c) contribution valued at CZK 6,700 per employee per year for recreation, sport, health, culture and personal development for use through the cafeteria plan;
d) amount in total value of CZK 1,200 per year for employees with physical disabilities, and the value of CZK 600 per year for employees over 55 years of age through the cafeteria plan;
e) contributions to supplementary pension insurance or supplementary pension savings in the amount of 3.5% of the base for social security and state employment policy contributions;
f) contribution to capital life insurance in the amount of CZK 650 per month;
g) contribution for the purchase of employee shares in the Global Employee Share Ownership Programme of Société Générale;
h) premium conditions for retail banking products and services provided by Komerční banka to its employees;
i) financial support for long-term illness;
j) risk life insurance; and
k) social assistance in exceptional circumstances.

Members of the Board not having Czech citizenship and who are deputed to the Czech Republic are eligible for these additional benefits:
a) above-standard health care (Santé Silver Card);
b) meal vouchers valued at CZK 85 per day at no cost to the employees;
c) contribution valued at CZK 6,700 per employee per year for recreation, sport, health, culture and personal development for use through the cafeteria plan;
d) amount in total value of CZK 1,200 per year for employees with physical disabilities, and the value of CZK 600 per year for employees over 55 years of age through the cafeteria plan;
e) contribution for the purchase of employee shares in the Global Employee Share Ownership Programme of Société Générale; and
f) premium conditions for retail banking products and services provided by Komerční banka to their employees.

In contrast to the members of the Board of Directors with Czech citizenship, members temporarily delegated to the Czech Republic are entitled to remuneration relating to their stay abroad (e.g. covering costs for moving and transport at the start and end of their assignments; accommodation costs; insurance, including health insurance and social security; support during the immigration process; traveling costs within a defined budget; and tuition fees for children).

In order to carry out their duties as well as for private use, the Bank provides members of the Board of Directors with: a company car, contributions to fuel costs, a mobile telephone with an unlimited voice and data tariff, and a personal computer.

The value of all in-kind and monetary payments to the members of the Board of Directors is given in the section "Information on monetary and in-kind income to members of the Board of Directors and the Supervisory Board".

## Principles of remuneration for members of the Supervisory Board

Remuneration for members of the Supervisory Board consists of a fixed monthly part and a part dependent on the members' attendance at meetings. Remuneration is set by decision of the General Meeting. In accordance with a resolution of the annual General Meeting held on 17 June 2004, remuneration for members' attendance at Supervisory Board meetings is limited to a maximum of six meetings per year.

Members of the Supervisory Board elected by employees are additionally entitled as employees of the Bank to a basic monthly salary and other compensation in lieu of salary according to their employment contracts pursuant to the Labour Code.

Members of the Supervisory Board who fulfil established conditions are entitled by their employment with KB under the same conditions as other KB employees to the following additional remuneration:
a) meal vouchers valued at CZK 85 per day at no cost to the employees;
b) contribution valued at CZK 6,700 per employee per year for recreation, sport, health, culture and personal development for use through the cafeteria plan;
c) amount in total value of CZK 1,200 per year for employees with physical disabilities, and the value of CZK 600 per year for employees over 55 years of age through the cafeteria plan;
d) employees receive contributions to supplementary pension insurance or supplementary pension savings in the amount of 2% of selected wage components from which is calculated the contribution for social security and state employment policy contributions, the minimum amount of the employer contribution being CZK 400 per month;
e) contribution to capital life insurance in the amount of CZK 650 per month;
f) contribution for the purchase of employee shares in the Global Employee Share Ownership Programme of Société Générale;
g) premium conditions for retail banking products and services provided by Komerční banka to their employees;
h) financial support in case of long-term illness;
i) 2 paid days off and 1 additional, unpaid day off for employees who are employed continuously for 7 years or more in Komerční banka, this benefit not being transferable to the next calendar year;
j) risk life insurance; and
k) social assistance in exceptional circumstances.

Komerční banka has concluded service contracts with all members of the Supervisory Board, and these were approved by the General Meeting held on 30 April 2014. The contracts are concluded for the term of office of each member of the Supervisory Board. The contracts provide no benefits upon termination of service. Information on all in-kind and monetary payments to the members of the Supervisory Board is given in the following section.

## Information on monetary and in-kind income to members of the Board of Directors

The total value of remuneration to members of the Board of Directors in 2016 is net of overlapping inclusion of full-year remuneration of newly elected and outgoing members. It includes all monetary and in-kind income received in 2016 by current and former members of the Board of Directors. Furthermore, all bonuses awarded (but not necessarily paid) in 2016 are also included:

**Board of Directors**
**(in total seven current and former members)**

| | Total CZK | Of which for performance of Board responsibilities | Of which for employment |
|---|---|---|---|
| A | 29,888,020 | 29,888,020 | 0 |
| B | 867,373 | 867,373 | 0 |
| C | 21 980,020 | 21,980,020 | 0 |
| D | 0 | 0 | 0 |
| E | 0 | 0 | 0 |
| F | 5,644,908 | 5,644,908 | 0 |
| **TOTAL** | **58,380,321** | **58,380,321** | **0** |

Note:
A. total amount of remuneration paid and remuneration recognised but not yet paid for services performed in the given fiscal year;
B. remuneration and benefits received from any company within the KB Group;
C. bonuses to members of the Board of Directors awarded in 2015 regardless of when individual parts become due;
D. remuneration to members of the audit committee;
E. paid or payable compensation for former members of the Board of Directors in connection with termination of their activities during the given fiscal year; and
F. total estimated value of non-monetary income considered as remuneration not included in points (A) to (E).

The management of KB is convinced that the aforementioned net summary most faithfully describes the trend of remuneration for the given group of the Bank's representatives.

In accordance with Act No. 256/2004 Coll., on Capital Market Undertakings, as subsequently amended, Komerční banka also releases information on all monetary and in-kind income received during the 2015 financial reporting period by members (including former members) of the Board of Directors from Komerční banka and from entities controlled by the Bank. The data are published in a structure similar to that from the provisions of Section III, point 5.3 of the European Commission Recommendation of 14 December 2004 (2004/913/EC):
A. total amount of remuneration paid for services performed in the given fiscal year;
B. remuneration and benefits received from any company within the KB Group;
C. remuneration paid in the form of profit sharing and/or bonuses;
D. significant additional remuneration paid for special services beyond the scope of usual duties;
E. paid or payable compensation for former members of the Board of Directors in connection with termination of their activities during the given fiscal year; and
F. total estimated value of non-monetary income considered as remuneration not included in points (A) to (E).

**Board of Directors**
**(in total ten current and former members)**

| | Total CZK | Of which for performance of Board responsibilities | Of which for employment |
|---|---|---|---|
| A | 29,888,020 | 29,888,020 | 0 |
| B | 867,373 | 867,373 | 0 |
| C | 23,301,997 | 23,301,997 | 0 |
| D | 0 | 0 | 0 |
| E | 0 | 0 | 0 |
| F | 5,751,474 | 5,751,474 | 0 |
| **TOTAL** | **59,808,864** | **59,808,864** | **0** |

The table above presents in the aforementioned structure all compensation received during 2016 by the members of the Board of Directors of Komerční banka, including compensation received in 2016 by former members as deferred payments (in total nine current and former members of the Board of Directors). If no value is shown, then no such compensation was made within the given year to the member by Komerční banka or entities controlled by KB.

## Information on monetary and in-kind income to members the Supervisory Board

In accordance with Act No. 256/2004 Coll., on Capital Market Undertakings, as subsequently amended, Komerční banka also releases information on all monetary and in-kind income received during the 2015 financial reporting period by members (including former members) of the Supervisory Board from Komerční banka and from entities controlled by the Bank. The data are published in a structure similar to that from the provisions of Section III, point 5.3 of the European Commission Recommendation of 14 December 2004 (2004/913/EC):
A. total amount of remuneration paid for services performed in the given fiscal year, including remuneration for meeting attendance approved by the General Meeting of shareholders;
B. remuneration and benefits received from any company within the Group (note: KB Financial Group) – concerns only members who are employees;
C. remuneration paid in the form of profit sharing and/or bonuses – concerns only members who are employees;
D. significant additional remuneration paid for special services beyond the scope of usual duties;
E. paid or payable compensation for former members of the Supervisory Board in connection with termination of their activities during the given fiscal year; and
F. total estimated value of non-monetary income considered as remuneration not included in points (A) to (E) – concerns only members who are employees.

### Supervisory Board (in total nine members)

| | Total CZK | Of which for performance of responsibilities | Of which for employment |
|---|---|---|---|
| A | 4,806,421 | 3,382,500 | 1,423,921 |
| B | 64,543 | 0 | 64,543 |
| C | 318,360 | 0 | 318,360 |
| D | 300,000 | 300,000 | 0 |
| E | 0 | 0 | 0 |
| F | 133,829 | 0 | 133,829 |
| **TOTAL** | **5,623,153** | **3,682,500** | **1,940,653** |

The table above presents in the aforementioned structure the compensation received during 2016 by the members of the Supervisory Board of Komerční banka for performing the duties of a member of the Supervisory Board or the Audit Committee. If no value is shown for a given category, then no such compensation was made within the given year to the member of the Supervisory Board of Komerční banka.

## Information on shares and share options held by members of the Board of Directors and the Supervisory Board and by related persons

The following table provides information on the numbers of shares issued by Komerční banka that were held as of 31 December 2016 by members of the Board of Directors and members of the Supervisory Board and related persons, as well as information on options and comparable investment instruments whose values are linked to the price of KB shares and which were concluded by or on behalf of the listed persons.

| 31 December 2016 | Shares | Options |
|---|---|---|
| Members of the Board of Directors in 2016 (total) | 17,000 | 0 |
| Members of the Supervisory Board in 2016 (total) | 19,295 | 0 |
| Related persons (total) | 0 | 0 |

No members of the Board of Directors or members of the Supervisory Board were contractual parties to any option or similar contract concerning comparable investment instruments whose values are linked to KB shares, nor were any such contracts concluded on their behalf.

PROFILE OF KB
STRATEGY AND RESULTS
CORPORATE GOVERNANCE
CORPORATE SOCIAL RESPONSIBILITY
RISK MANAGEMENT

# Corporate social responsibility

Responsibility is the basis of every partnership, and it is also Komerční banka's priority in relation to our clients, employees, shareholders and the broader society. Komerční banka's principles of corporate social responsibility (CSR) are consistent with its fundamental values, even as the Bank's business strategy regards this to be a condition for long-term success.

Corporate social responsibility ensures that Komerční banka's long-term interests are being served in a responsible manner while duly considering the expectations of its major stakeholders and complying with all regulations. This responsibility is advanced in the economic, environmental and social areas, it is made an integral aspect of the entire organisation, and its observation and implementation at all levels are supported through a variety of activities.

Komerční banka, as part of the Société Générale Group, conducts its business with the utmost respect for the values and principles expressed in the following documents:

- the Universal Declaration of Human Rights and its associated covenants (namely, the International Covenant on Civil and Political Rights and the International Covenant on Economic, Social and Cultural Rights),
- the main conventions of the International Labour Organisation,
- the UNESCO World Heritage Convention, and
- the OECD (Organisation for Economic Co-operation and Development) Guidelines for Multinational Enterprises.

## Corporate governance and organisation, internal control

KB employs a clear and transparent governance structure, fortified with strong and independent control functions. The Bank's governance structure is defined in its Articles of Association. The Board of Directors is responsible for directing the business of the Bank. Control functions at the highest level are conducted by the Supervisory Board and the Audit Committee, and these are bolstered within KB by Internal Audit and a comprehensive, formalised system of first-level controls. Responsible risk management operates within Komerční banka as an independent function.

## Ombudsman

In 2004, Komerční banka became the first financial institution in the Czech Republic to establish a position of independent ombudsman. Should KB's clients not be satisfied with how their complaints had been resolved by a branch or the Complaint Management Department, they can take them to the ombudsman. JUDr. Joseph Franciscus Vedlich, LLM has served in this position since 2009. The institution of the independent ombudsman can be utilised by clients across a total of seven companies within KB Group. In 2016, the ombudsman was contacted by 169 Komerční banka Group clients. The Ombudsman resolved 28 cases which fell within his competence for resolving complaints and claims in the third instance and in accordance with the Charter of the Ombudsman.

## Five strategic pillars of corporate social responsibility

Socially responsible activities and procedures are a natural part of KB's everyday activities. KB's corporate social responsibility principles are built on five pillars:

- responsible banking,
- solidarity-based banking offer,
- responsible employer,
- environment and responsible sourcing,
- civil society.

## Responsible banking

### Ethics

Komerční banka recognises that only by taking an ethical approach to the way it does business and provides banking services can it hope to maintain and improve its position on the competitive banking market over the long term. The requirements for ethical and professional conduct apply not only to the Bank as an entity but to every employee individually. The entire KB Group has for a number of years been implementing corporate rules of conduct and principles of ethical behaviour in relation to its employees. These rules ensue both from the general obligations laid down in regulatory rules and standards of professional conduct applicable in the banking field. The prescribed responsibility consists mainly of rules against conflict of interest, in regard to accepting gifts, against misuse of position, and against misuse of confidential information.

### Measures against corruption

Maintaining these rules and zero tolerance to any forms of corruption represent the basic standard and operating principle of socially responsible business as declared by KB Group. Only through consistent application of ethical principles in performing its business activities can Komerční banka preserve and strengthen its long-term position on the competitive market wherein it operates.

The rules and principles of ethical behaviour and professional conduct, including rules adopted for the struggle against corruption and bribery, are anchored in the Bank's internal regulations. The employees regularly undertake training focusing on the basic principles in all areas concerned. Employees are reminded regularly about the most important rules, and their adherence to these rules is regularly checked. In these areas, KB insists upon zero tolerance for any fraudulent or unfair conduct. Among other things, the Bank focuses on providing and receiving gifts and other advantages and participation at various social and other events. Special attention is also dedicated to tenders. Through anti-corruption clauses in contractual provisions, Komerční banka also prescribes certain obligations for ethical behaviour among its suppliers and intermediaries.

### Measures against money laundering and financing of terrorism

When entering into and conducting business relationships with clients, Komerční banka rigorously applies the “know your client” process. It declines to work with any person or entity refusing to co-operate in verifying identification or conducting in-depth control. Nor does it work with untrustworthy persons or entities. The Bank carries out no transaction or payment instructions for a client which would bear signs of possible risk of money laundering or terrorist financing. Moreover, the Bank never enters into transactions which can lead to violations of international sanctions programmes.

The Bank exerts maximum effort to obstruct its being misused for purposes of money laundering or financing of terrorism. To this end, rules, methods and controls are applied in accordance with legal regulations and with the standards and requirements of the Société Générale financial group. The preventive system in this field is continuously validated and updated. Information is regularly shared with all employees of the Bank in the forms of reports, training courses or e-learning.

Unethical conduct and corruption as well as inconsistent practices in prevention of money laundering and financing of terrorism could bring the Bank a great deal of risk and unfavourable consequences, in particular conflicts with supervisory bodies and other institutions, but also, for example, possible sanctions and remediation measures and even criminal prosecution of those persons responsible or of the legal entity as a whole. If realised, these risks could bring loss of reputation and goodwill in relation to clients and the general public, loss of clients, financial losses, and in an extreme case even a possible existential threat in the form of a loss of licence.

### Limitation of trading with potential negative impact on the quality of life and social environment

Komerční banka, as part of the Société Générale financial group, respects business limits pertaining to provision of banking services and products for trading in weapons, ammunition and other goods and technologies which comprise military materiel. The limitations pertain also to individual private and state entities and entire business groups the business activities of which in the weapons industry are considered intransparent. Regarding environmental and social responsibility, Komerční banka also follows other specific sector rules of the Société Générale financial group governing provision of financial products in areas which may crucially influence the quality of the natural and social environment. These sectors are mainly mining and further processing of fossil fuels, dams and water power plants, as well as renewable sources of energy.

Thereby, Komerční banka tries to eliminate risks resulting from financing of illegal and unethical activities as well as such activities which are dangerous for the society as a whole. This concerns especially activities in such areas as human cloning for reproductive purposes, tobacco products, distilled alcoholic beverages, production and trading with weapons and munitions, gambling clubs, casinos, IT projects focusing on non-permitted areas including internet gambling and pornography, and such projects with an objective to allow illegal access to electronic data networks or illegal downloading of data.

## Solidarity-based banking offer

KB provides funding under slightly better conditions, such as at reduced interest rates for loans or more advantageous collateral requirements, to activities having positive social impact. Komerční banka provides several "solidarity" products in co-operation with international financial institutions.

### Deposits and special programmes

KB maintains current accounts used for the purposes of charity, environmental protection or for complete transparency.

These accounts, for instance, offer the possibility of selecting an easy-to-remember account number inasmuch as they often are used for funds collection in public fundraising. Moreover, there are "transparent" accounts that enable complete public access to the transaction history. This service is available free of charge and is most often used by various foundations and foundation funds, socially beneficial organisations, various associations, municipalities, political entities, associations of residential unit owners and housing co-operatives, as well as any other entities that wish to be completely transparent in their financial dealings. As of the end of 2016, KB was administering 575 transparent accounts.

In relation to environmental protection, the Bank also offers an escrow account that serves as a current account for depositing funds to create reserves for purposes specified by law. These include land reclamation, management of waste heaps and reclamation following a heap's closure, requirements in the event of a mining accident, electronics waste disposal, pond dredging, forest-growing activities, and nuclear waste management.

KB provides an advantageous business package, Profi-account, to starting-up entrepreneurs for up to 4 years. To associations of residential unit owners and housing co-operatives, it provides the advantageous Profi-account without any time limit.

Each holder of an A card or Lady card can send a reward from non-cash transactions in the amount of 1% to benefit the Nadace Jistota Foundation. The client can easily set the amount of contributions via internet banking.

**EuroPremium Young:** In co-operation with the European Investment Bank (EIB), this project supports small and medium-sized companies (up to 3,000 employees), which may have an additional discount on loan interest rates if they employ young people under 30 years or age. Companies offering internships and traineeships to young people can qualify.

**COSME, Microfinance:** Beginning entrepreneurs can obtain financing with lower collateral requirements thanks to the guarantee of the European Investment Fund. COSME provides a guarantee of 50%. It is designed for entrepreneurs with no more than three years of business history. Microfinance provides an 80% guarantee and gives preference to entrepreneurs providing positive social impacts. Advantages are for beginning entrepreneurs who started their businesses on a part-time basis, who were previously unemployed, or who have low-income jobs. People disadvantaged in the labour market may also qualify, such as those returning to work after parental leave, disabled persons, migrants or people belonging to a national minority. Beginning entrepreneurs under 30 or over 55 years of age may be given advantageous conditions.

**EuroEnergy:** Projects leading to reduced energy consumption can obtain a combination of such benefits as lower interest rates and more lenient collateral requirements. The European Investment Bank provides advantageous financing for these projects and also guarantees up to 80% of losses. Non-financial benefits of reduced $CO_2$ emissions also are taken into account when considering energy savings in accordance with the EIB methodology.

**Providing microcredit:** KB has pledged to adhere to the EU's European Code of Good Conduct for Microcredit Provision in the context of its co-operation with the European Investment Fund. The Code aims to standardise the norms, procedures and conduct of microcredit providers. It contains a set of standards in relation to transparent determination of the cost of credit, providing complete statements, and resolving customer complaints. Further, it includes, among others, an anti-discrimination policy and policies for protecting client data, implementing internal audit and managing risks.

## Responsible employer

### Key data on employees

| Average recalculated number of employees during year | 2016 | 2015 |
|---|---|---|
| – KB Group | 8,476 | 8,426 |
| – Komerční banka | 7,549 | 7,538 |
| – of which in Slovakia | 38 | 38 |
| – of which in Czech Republic | 7,511 | 7,500 |
| – of which at headquarters | 3,949 | 3,878 |
| – of which in the distribution network | 3,562 | 3,622 |

| Age structure of employees (KB, Czech Republic, as of end of year) | | |
|---|---|---|
| <30 | 17% | 17% |
| 31–40 | 27% | 28% |
| 41–50 | 32% | 32% |
| 50+ | 23% | 23% |
| **Employees by type of employment contract** | | |
| – Full-time | 93% | 93% |
| – Part-time | 7% | 7% |
| **Employees by period of employment** | | |
| – Permanent employment | 85% | 86% |
| – Other employment (temporary, limited assignment, other) | 15% | 14% |
| **Employees' qualifications** | | |
| – University | 44% | 43% |
| – Secondary school | 54% | 54% |
| – Other education | 2% | 3% |
| **Proportion of men and women** | | |
| – Men | 33% | 33% |
| – Women | 67% | 67% |
| **Proportion of women in leadership positions (including team leaders)** | 52% | 53% |
| **Number of employees on maternal and parental leave** | 711 | 737 |
| **Illness rate** | 3.02% | 2.90% |
| **Number of employees with disabilities** | 72 | 76 |

A key aspect of Komerční banka's strategic vision is to pursue the creation of longstanding partnerships with its employees. In doing so, Komerční banka presumes there to be a professional relationship that stems from mutual trust, respect, communication, equality of opportunity, and the availability of attractive professional and career development prospects. These values are shared across the Group.

Concerning the legislative framework, Komerční banka and the entire Group are subject to the same legal conditions and standards as apply to any other employer in the Czech Republic. Its activities are supervised by the Czech National Bank, which may apply other regulatory measures, for example in relation to employee education and remuneration. Regulations of Société Générale and international standards can also have an influence. Fulfilment of all legal standards, decrees and regulations is subject to regular or random control, and failure to uphold these standards can be sanctioned in accordance with the valid regulations.

### Work safety and working conditions

To the full extent of law, KB ensures its employees' occupational safety as well as health and fire protection (hereinafter referred to as OSH and FP) concerning possible risks that would endanger their lives and health when performing their work. It provides its employees with sufficient and adequate information and instructions on OSH and providing first aid. The Bank also ensures respect for the prohibition of smoking and consumption of alcoholic beverages at work. Management employees at all levels are responsible that the employer's obligations in this area are honoured. These tasks are an equal and integral part of their work obligations. The employer provides work-related medical services through EUC Premium and regular employee training in OSH and FP according to the relevant legal standard. Komerční banka regularly organises checks and employee training in these areas while documenting and recording the results.

Komerční banka is also modernising the environment within its branches in accordance with both safety and health requirements as well as regarding the social environment and state-of-the-art technologies.

### Right to information and to social negotiation

All information designated for employees is in various ways shared openly within KB Group. For each employee, the main source of information is his or her superior. Since 2016, an Employee section has been in operation within the new KB intranet. All necessary information from the human resources area is accessible there and is regularly updated. Employees can call the Moje HR (My HR) telephone line, submit their inquiries by e-mail or contact HR Business Partners and consultants.

The right of KB employees to social bargaining is exercised through the KB Trade Unions Organisation. KB is in regular contact with representatives of the trade unions organisation, and collective bargaining is ongoing every year. The results of the negotiations with the trade unions organisation at the end of 2016 is the Collective Agreement, newly concluded for the period 2017–2020.

The right to information is based in the Collective Agreement. The full negotiations between the employer and the trade unions organisation are published to all employees and including the full wording of the Collective Agreement.

### Employee health

Komerční banka has for several year been systematically attentive to the health of its employees. KB continued – and further developed – its Moje Vitalita programme during 2016. It aims to support high performance from KB employees by looking after their physical and mental well-being. Physical well-being was given special focus this year, and the programme featured Health Days across the Czech Republic.

**Supporting employees in difficult life situations**
KB respects all its employees' human and social rights. Any form of discrimination is prohibited. Over the long term, KB has been forthcoming to its employees who happen to be in difficult life situations. This support is implemented in various ways, and it considers the life situation an employee is facing (for example through flexibly adjusting work time, reduced working hours, home office, financial support, unpaid vacation). Every situation is assessed and resolved individually.

Support of employees in difficult life situations is based on the Collective Agreement and the corresponding implementation rules. Any drawing of financial aid is recorded by the employer.

**Gender diversity**
The principles of equal opportunities and non-discrimination are among Komerční banka's basic principles as an employer. Employees are hired on the basis of their experience and competence, and the same approach is applied with regard to internal mobility. Moreover, KB applies a diversified approach to the individual employee groups based upon their needs and current situations. This approach can impact the offer of educational programmes for certain groups (graduates, managers, sales positions, specialists).

Another specific group of employees consists of those on maternity and parental leave (ML/PL). Their successful reintegration into the workflow is among Komerční banka's important goals. KB is in contact with these employees also during the maternity and parental leave; they are invited to networking events and, in case of mutual interest and needs, co-operation during the leave is established. After return from ML/PL, employees may take advantage of reduced work responsibilities, home office or flexible work hours, if allowed by the type of operation and job character.

The principle of equal treatment is anchored in KB's basic documents, such as the Code of Ethics and the Rules of Employment. Employees and managers conducting recruitment are trained about discrimination and in the basics of the Employment Code. The proportion of employees reintegrated after returning from ML/PL is regularly monitored and included into the managerial reporting.

**Equal conditions in employment**
Komerční banka applies the principle of non-discrimination in selecting employees. It is crucial in a manner such that the expectations from the position and job description are in accordance with the knowledge, competencies and expectations of each individual applicant. A specific population upon which we want to focus attention during 2017 is that of handicapped applicants with disabilities. Their employment will be supported by newly formed positions. KB also initiated co-operation with the Foundation Fund for Employment of Persons with Medical Disabilities which has focused on supporting this group over the long term.

Recruitment employees are trained in recruiting applicants with disabilities, and regular monitoring of this area has been established.

**Seeking and acquiring talent**
Again in 2016, Komerční banka co-operated actively with universities and student organisations. Within its support to the development of higher education within the Czech Republic, Komerční banka continued sponsorship support of state universities all across Czech Republic which has been going on for several years. The Bank actively co-operated in particular with the University of Economics, Prague; Masaryk University in Brno and Czech Technical University in Prague (ČVUT). Components of the co-operation with ČVUT in Prague, and specifically with the Faculty of Information Technology, included not only support of research but also development of new ideas in the innovations area of today's digital world through Komerční banka's Innovation LAB. Additional active co-operation with university students occurred in the forms of such collective gatherings on employment opportunities as trade fairs and workshops with current topics, as well as putting forward and critiquing diploma theses, and offering possible participation in internships at Komerční banka's headquarters or branches. Among the student organisations supported last year were AIESEC and ASA.

Co-operation with schools is ensured through a contractual agenda. Budget drawing is regularly monitored and strategy in this area is regularly revised.

**Employee education and career development**
KB's human resources strategy is geared to developing long-term partnerships with employees. This is supported through education, among other things. KB Group employees have access to a broad range of educational activities and programmes even as strong emphasis is given to the principle that the employee should take individual responsibility for his or her career development.

As in previous years, the Bank devoted particular effort to the development of those employees in direct contact with clients within the branch network. Special attention was given to the development of managers and high-potential employees, who are participants of the Strategic Talent Management programme.

The M'Academy management academy focuses on enhancing long-term, personalised skills in the areas of human resources development, responsibility, innovation and the pro-client approach. Other integration and development programmes have traditionally been dedicated to new employees (StartinG), university graduates (ConnectinG and ConnectinG+) and future top managers (ChallenginG).

Komerční banka continues in co-operation on development programmes with parent company Société Générale. KB employees have the opportunity to develop their skills and abilities in an international environment.

### Fair remuneration

Remuneration is formulated to support the Bank's overall strategy as well as its specific business and financial objectives, to preclude the taking of unnecessary risks and careless conduct, to support cost efficiency and to strengthen KB's value from the perspectives of both employees and shareholders. In pursuing a remuneration policy that is designed to be both healthy and business-sensitive, Komerční banka builds upon the following core principles:

- ***Internal fairness*** is about equal remuneration for individual employees performing equally in the same job under the same transparent conditions.
- ***External competitiveness*** is achieved with the assistance of regular market surveys.
- ***Reflecting risks*** means ensuring that remuneration at KB remains consistent with, and supportive of, healthy and efficient risk management. Remuneration compliant with this principle does not encourage risk-taking beyond those risk levels tolerated by the Bank.

The remuneration structure is supported by three fundamental pillars:

- ***Basic pay for work performed.***

The pay of any employee is determined in respect of the demands of his or her particular position, especially in terms of required knowledge, experience and skills, as well as corresponding responsibilities.

- ***Flexible performance-dependent pay component.***

In addition to the basic pay, a variable pay component scheme is in place for all employees. It rewards contributions in achieving corporate, team and individual targets.

- ***Employee benefits that support employees' sense of belonging within Komerční banka Group.***

These benefits reflect the Bank's desire to be a responsible employer while offering choice to employees. The structure and level of the available benefits are subject to an annually reviewed agreement ensuing from collective negotiation.

### Corporate values and The Leadership Model

Inasmuch as corporate culture is a stone in the foundation for achieving long-term success in business, KB is applying a new definition of its corporate values which are shared across SG Group.

Those updated core values are: **team spirit, innovation, commitment and responsibility**. The values contribute to the basis of an updated model for managers and employees' conduct, known as "The Leadership Model". It is built on the following five pillars:

- Client satisfaction,
- Innovation in creativity and change management,
- Responsibility,
- Our teams' commitment, and
- Team spirit with a strong sense of achieving results together.

The updated corporate values are progressively being reflected in all associated processes, and particularly in recruitment, assessment, remuneration and education.

## The environment and responsible sourcing

In relation to environmental protection, Komerční banka meets all its legal obligations. The Bank is particularly active in areas of waste management, which means by reducing paper consumption through progressive digitalization of documents as well as proper and considerate treatment of waste. In co-operation with the Bank's individual departments, KB ensures separation, transportation, and disposal of all types of waste (including batteries and small electrical appliances). As part of environment protection, KB issues internal directives and provides advisory services to internal clients. Of course, this includes co-operation also with supervisory bodies. This results in a well-established system for sorting and disposal of all types of waste as well as compliance with Komerční banka's legal obligations.

KB monitors its consumption of electricity and other resources while working systematically to reduce their consumption and to use them efficiently. As a result of systematic work to reduce energy consumption, stable annual savings of ca CZK 1.5 million were realised due in part to introducing lighting based upon LED technologies.

The main risk in the environmental area is Komerční banka's negative impact on the environment and related sanctions from regulatory bodies. KB has introduced regular reporting to monitor the amounts of waste according to individual categories (paper, plastic, etc.). Energy consumption is evaluated on a monthly basis. In accordance with legal obligations, an energy audit of KB was performed during 2016. The audit demonstrated the Bank's good approach while also identifying further opportunities for improvement.

### Relationships with suppliers

In its relationships with suppliers, Komerční banka shares best practices for protecting the environment, protecting social and human rights, and respecting the principles of sustainable development. As a subsidiary of Société Générale, KB implements the principles of sustainable development into its processes. The Bank does so because it is convinced of its responsibility in the area of sustainable economic and social development and takes the view that the practices contribute also to its risk management effort.

The commitment to sustainable development by Société Générale, Komerční banka's parent company, was confirmed by its signing the Statement of Commitment by Financial Institutions on Sustainable Development from 27 November 2001 under the patronage of the United Nations. It also joined the United Nations Global Compact from 16 May 2003.

In the spirit of this joint commitment, Komerční banka is extending this dialogue and transparency to relationships with its suppliers (sharing and improving best practices with respect to the environment, social and human rights, etc.). Komerční banka participates in the Ethical Sourcing Programme that is in force across the Société Générale Group. Each supplier with which KB enters into a contractual relationship undertakes to observe the principles set forth in this programme, and KB reserves the right to conduct an independent audit.

## Civil society

An integral part of KB's social responsibility consists in sponsoring, philanthropy and employee social involvement. In the sponsoring area, KB continues supporting important cultural entities, including the National Theatre in Prague and the National Gallery. Sponsoring of non-professional sport again focuses on floorball events and firefighting sport. Successful co-operation continues also with the Prague Zoo. Charity and sponsoring activities constitute a favourite and well-visible part of Komerční banka's CSR concept. Meanwhile, Komerční banka's Jistota Foundation has been operating for more than 20 years.

### Sponsoring

In its sponsoring strategy, Komerční banka focuses on supporting culture, non-professional sport and education. The Bank is partnering with institutions, projects and events with society-wide impact. It emphasises in particular the exceptional human, social or artistic dimensions of the projects it supports. KB particularly cherishes its long-term partnerships.

Komerční banka has been active in sponsoring and charity since the beginning of its existence. For almost that long its name has been connected with the National Theatre, the most prestigious cultural institution in the country. For the second year, KB has been supporting also the National Gallery in Prague. With help from KB, children and youths up to 18 years of age and students up to 26 years of age have free admission there. The bank has also traditionally co-operated with the French Film Festival, which presents some of the best French film productions and co-productions and is seen as one of the most prominent film festivals in the Czech Republic.

In sponsoring sport, Komerční banka focuses primarily on projects that bring joy and entertainment to the broadest segment of society. Therefore, it has long supported Czech floorball and also firefighting sport, both of which are physically demanding, highly popular with fans, and correspond to KB's Partnership Matters motto. KB has been a sponsor of the Czech Republic's national championship in firefighting sport since 2012. The successful partnership with the Prague Zoo also continues.

### Philanthropy and community involvement

Employees of the Group are actively involved in many volunteer activities each year, and especially in the fields of charity work and environmental protection.

Several large charitable projects were organised and supported at all levels within the Bank during 2016. Employees also participated in several smaller events that took place at the level of individual banking departments or branches.

*Blood donation*

The traditional blood donation event was held within KB on the occasion of World Blood Donor Day. Blood collection took place at the headquarters in Prague, where donors numbered more than 100, as well as in Brno, Ostrava, České Budějovice, Ostrava, Pilsen, Olomouc and Liberec. The KB effort yielded in total 57 litres of blood within the Czech Republic.

*Collection of old mobile phones*

Another of Komerční banka's activities has been to collect old mobile phones and electronic devices in co-operation with the organisation Retela. An event was launched on 22 April, which is Earth Day. For each mobile phone donated, CZK 10 was given to Jedlička's Institute for the Disabled, which cares for physically disabled children. The collected equipment was dismantled by specialised companies employing disabled people. Collected in total were 1,773 mobile phones plus 240 kg of other electrical equipment. Through their collection efforts, employees reduced environmental burdens corresponding to 2,811 kg of $CO_2$ emissions and savings equal to 53,012 litres of drinking water and 17,146 km of car driving distance. The phone collections brought Jedlička's Institute for the Disabled a contribution of CZK 17,730, and dismantling of the collected equipment provided 283 hours of work to handicapped employees.

*Biking to work*

Through the Auto*Mat initiative, the popular Bike to Work competition event was organised for the six year in a row. Komerční banka employees again participated, with 224 participants signed up in 69 teams. This marked an increase by 22 teams compared to the previous year. The event involved 27 Bohemian and Moravian towns. New in 2016 was the opening of a category for walkers, runners, riders on scooters and skateboarders in addition to cyclists. Each participant had to ride, run or walk a route at least 1.5 km long. KB Group employees rode, ran or walked a total of 43,569 km to reduce $CO_2$ emissions by four tonnes.

*Clothing collection*
During September 2016, a clothing collection was organised by KB and earmarked for the Borůvka Praha non-profit organisation. Part of the clothing was sold and the proceeds were used to support jobs for handicapped people. The rest was provided to those in need or processed into nonwoven fabric. Approximately 900 kilograms of clothing were donated.

*Employee photograph auction*
KB employees were also involved in the annual auction of photographs taken by employees. Registered in 2016 were 229 photos. Selected photos were printed in large format, framed and auctioned off by the employees. The auction's proceeds of CZK 36,500 were donated to the Jistota Foundation. A calendar was created from the best photos, and proceeds from sales of nearly 100 calendars came to nearly CZK 60,000.

*Breakfast for Jistota Foundation*
The principle of the Breakfast for Jistota Foundation is to prepare a breakfast for colleagues that they can buy when they arrive to work and thereby contribute to a good cause. During 2016, several departments in KB organised six breakfasts within the headquarters building in Prague, as well as in Liberec, Zlín, České Budějovice, Brno and at branches in Mladá Boleslav, Hradec Králové, Ostrava, Pilsen, Brno and České Budějovice. Nearly CZK 430,000 was collected for donation to Jistota Foundation through these events.

*Jistota Foundation Week*
During this week, the Jistota Foundation organised lectures focused on various topics in relation to caring for the disabled or elderly people. The Foundation also repeated the successful clothing collection drive. A floorball tournament which joined sponsoring with charity was a big success. The event was held at the Sportovní hale Děkanka in Prague in co-operation with the Czech Floorball Association, which professionally organised a tournament for the Bank. Six teams including 41 employees of the Bank participated in the tournament. Each team paid an entry fee, and these fees, totalling CZK 8,200, were donated to the Jistota Foundation.

*Movember*
For several years now, Komerční banka has been joining the Movember event in support of prostate cancer research. It did so again this past November. Male employees demonstrate their support for the event by growing moustaches, the campaign's symbol. The campaign appeals to men to have preventive medical check ups. Through the efforts of KB employees, 227 men signed up for the check-up in response to the appeal and the Movember collection all across KB yielded CZK 3,200 in donations.

**Charity works and Komerční banka's Jistota Foundation**
The aims of charity are actively to support projects and activities for the greater development of civil society, to support education and actively to support health projects with a social character, including support for integrating individuals into society.

The Foundation continued its support for hospice facilities and for organisations directed to activities for children and adults with health or social disadvantages. Athletes with disabilities received CZK 485,000, as the Foundation supported the Czech Wheelchair Rugby Union, Wheelchair Athletics, and Sport without Prejudice. In another project, the Foundation provided CZK 788,120 to maintain and renew baby boxes for abandoned newborns.

The Jistota Foundation pledged to provide nearly CZK 2,300,000 over the next three years to The House of Three Wishes organisation to help children in crisis situations and more than CZK 750,000 to NAUTIS, an organisation working with people with autism. During 2016, these amounts were drawn in the amounts of CZK 229,277 by NAUTIS and CZK 810,000 by The House of Three Wishes. The House of Three Wishes also received CZK 241,552 raised through the traditional golf tournament. Those funds will be used in caring for children and families in crisis.

The Foundation decided also to reinforce contemporary trends in hospice care by supporting a newly established Centre for Palliative Care with the amount of CZK 250,000. Similarly, the home-care hospice known as The Way Home is promised backing of CZK 360,000 over the next two years. In 2016, the Foundation also agreed on support to these entities for the next period. The Way Home is to receive CZK 400,000 over two years and the Centre for Palliative Care is to receive CZK 263,220 during one year.

For the fourth year, KB Group employees supported the Matters of the Heart project through their volunteer activities. Seven projects in total were funded to the tune of CZK 638,318.

Komerční banka is the most important donor to the Foundation, annually contributing CZK 7 million. The Jistota Foundation has established collaboration also with Komerční banka's associated and subsidiary companies in 2013. Since that time, Penzijní společnost KB, Komerční pojišťova, SGEF, Modrá pyramida, KB Factoring and ALD Automotive, too, have contributed significant sums to individual projects of the Foundation. The contributions of KB Group employees are important for the Foundation, whether by regular or one-off contributions or through participation in the Foundation's collection events, such as Breakfast for Jistota Foundation, the charity golf tournament, collections during staff meetings of employees of KB and other events.

# Risk management

## Risk governance

### Main principles of risk management in KB Group

Risk management at Komerční banka is based on an integrated concept that takes into account the advanced risk management standards of the Société Générale Group together with the statutory and regulatory norms as defined and required by the Czech National Bank and other regulatory bodies. Komerční banka's corporate governance standards assure that the risk management function is independent of commercial and operational functions.

Credit risk management, including management of Komerční banka's market risks and counterparty risks arising from financial market activities and recovery of the Bank's receivables as well as management of related information systems, is carried out within the Risk Management Arm of KB. The Risk Management Arm closely co-operates with risk management at KB subsidiaries and supervises their activities. Operational risk, legal risk and compliance risk are managed within the Corporate Secretariat. Management of interest rate risk and foreign exchange risk in the banking book is conducted within the Strategy and Finance Arm.

### Overall risk management strategy

Through its risk management strategy, KB Group continues to pursue a prudent and balanced approach to all types of risks assumed, i.e. credit, market and liquidity risks, as well as regulatory, legal, operational and environmental risks. At the same time, it aims to support development of the Group's business activities, including sustainable growth of its lending activities and reinforcing the Group's market positions.

The objective is to ensure profitable credit and market activities across the business cycle and, at the same time, to preserve a sound balance sheet with strong capital and liquidity ratios. To this end, advanced risk management tools, including statistical tools, are continuously enhanced and analytical and risk management skills are maintained at high levels for both risk management and business staff.

A general target of KB's risk management is to harmonise risk management processes and tools throughout the Group. The Bank enables shared access to selected tools within the credit risk system for designated subsidiaries, thereby providing a unified credit risk view and harmonising the credit risk approach.

The Group continues in regular stress testing of its portfolio as an integral part of its risk management. Stress-testing results in 2016 confirmed that KB Group would meet the regulatory requirements for capital adequacy even in the case of a negative development in the Czech economy.

### Risk appetite

KB Group risk appetite is outlined in the KB Group Risk Appetite Statement, which since 2015 has been prepared in compliance with Financial Stability Board recommendations. It defines at aggregated level all risks that KB Group is ready to accept or intends to avoid and defines a prudent and balanced approach to them, namely in relation to

- credit risk, including concentration risk;
- market risk, liquidity and structural risk, including interest rate risk in the banking book and FX risk; as well as
- operational risk, compliance and reputation risk.

The KB Group Risk Appetite Statement is elaborated with the aim of ensuring consistency among the risk-taking capacity, capital adequacy, and the business and financial targets. The level of the Group's risk appetite and its risk management strategy are fully aligned.

The Risk Appetite Statement is revised annually or, according to need, more frequently.

# Regulatory development

## IFRS 9

KB is already well advanced in implementing the IFRS 9 requirements with which it will be obliged to comply from the beginning of 2018. It will utilise SG Group IFRS 9 methodology with a few local adjustments. Great attention is being devoted to assuring provisions calculations in accordance with IFRS 9 will be consistent with the risk-weighted assets calculation (the same statistical models will be used in both calculations) and the regular stress testing approach (forward-looking predictions in the IFRS 9 calculations will be the same as those used in the regular stress testing). Technical implementation should be completed by the end of the second quarter of 2017 and will be based on utilising existing IT tools. A parallel regular run of the IFRS 9 provisions calculation is expected to be started in the first quarter of 2017.

# Credit risk

## Credit risk development

Credit risk remained at a satisfactory level during 2016. Further improvement occurred in the Retail segment, which was positively influenced by the Czech economy's good performance and accompanying rise in household consumption and in real estate prices. The Corporate segment remained healthy overall, although its cost of risk results in 2016 were affected by a few isolated cases.

KB regards its current level of net provisioning as satisfactory. The Group's cost of risk increased to 32 basis points in 2016 from 21 basis points in 2015, driven solely, as mentioned above, by a few isolated cases in the Corporate segment.

The proportion of defaulted loans decreased year over year to 3.8% from 4.2%.

## Principal activities in 2016

KB Group concentrated during 2016 especially on the following activities in the credit risk area:

- preparing KB Group for new regulatory requirements (IFRS 9, AnaCredit, EMIR, regulations in the area of mortgage loans, etc.),
- implementing the optimised risk management function in KB Group with a focus on aligning and interconnecting subsidiaries' risk management processes with those of the Bank,
- further developing the risk tools in the area of small business financing,
- strengthening the concentration management framework and the borrowing base and receivables management processes in the corporate segment,
- optimising approval authorities setting within both KB Group and in relation to SG,
- fine-tuning the new collection system that had been introduced in 2015's second half, and
- updating key risk models to reflect the latest observations of portfolio development while maintaining sufficient margins across the entire business cycle.

## Credit risk management tools

**Credit risk assessment and monitoring**
Client credit risk is managed on the basis of comprehensively assessing clients' risk profiles from quantitative (financial) and qualitative viewpoints using advanced scoring and rating models along with individual approval by competent risk or business managers. The system of approval authorities is set up to reflect the risk profiles of the counterparties and the levels of competencies required for their assessment.

No credit exposure can be originated until internal credit limits for the client and transaction have been first duly established.

All KB scoring, rating and Basel (e.g. Loss Given Default, Probability of Default) models are back-tested at least annually and any deterioration triggers corrective measures.

**Credit fraud prevention**
Komerční banka uses an automated system for detecting individual credit frauds and also for co-ordinated reactions to credit fraud attacks. The system is fully integrated into KB's main applications. Anti-fraud tools and processes are continuously adjusted according to the market situation.

**Classification**
The Bank classifies all its assets originating from financing activities into five categories according to Czech National Bank Decree No. 163/2014 Coll. while taking into account both quantitative criteria (payment discipline, financial statements) and qualitative criteria (in-depth client knowledge, client's behaviour and history). The contagion principle is implemented in classifying co-applicants and guarantors in relation to defaulted receivables.

**Real estate valuation**
In compliance with Czech regulations and Basel III rules, the valuation and monitoring of real estate collaterals accepted by the Bank as security for corporate and retail loan exposures are delegated to a dedicated independent unit. This unit is a part of the Risk Management Arm and co-operates with a broad group of external valuation experts.

Komerční banka continuously monitors both residential and commercial real estate markets and regularly revalues the real estate collaterals it holds. The Bank utilises appropriate techniques (individual or statistical) for this purpose in order to react adequately to market developments.

**Recovery activities**
The Bank closely monitored changes in the legal environment, analysed their impacts in the area of receivables collection, and ensured their proper reflection in KB processes.

The inflow of clients into recovery has been relatively stable, influenced mainly by good macroeconomic conditions and clients' financial situations. This inflow was affected also by several insolvencies of large subjects commenced during 2016.

Given the size of the portfolio in recovery, KB continued in optimising its recovery capacity and performance by using external capacities as well as regular auction sales to selected investors of unsecured and secured retail receivables portfolios.

**Credit concentration risk management**
Komerční banka's credit concentration risk is actively managed as a part of overall credit risk management utilising standard tools. The Bank maintains its objective of taking on no excessive credit concentration risk. Credit concentration risk management procedures cover individual counterparties as well as economically connected groups, countries, selected industry sectors and collateral providers. A system of internal limits is established so that the Bank complies with the regulatory limits set in respect to concentration risk.

## Provisioning and its adequacy

**Main principles of provisioning**
Depending on the business segment, materiality, risk profile and specificity of the receivables, provisions are calculated either (i) on the basis of statistical models developed in conformity with Basel requirements and in compliance with IFRS rules and which are regularly updated based on the latest loss observations and new risk drivers reflecting the phase of the business cycle; or (ii) taking into account the present value of expected future cash flows while considering all available information, including the estimated value of collateral and expected duration of the recovery process; or (iii) based upon the expected loss approach.

Since 2013, the provisioning approach has been gradually harmonised with SG standards. Harmonisation is focused on both the Corporate and Retail segments. Komerční banka also performs regular back-testing of provisioning models to carefully monitor their quality and to identify in a timely manner any potential deterioration.

# Market risk

## Capital markets risks management

Market risk and counterparty risk on market transactions in KB Group's financial markets activities is managed by a dedicated Capital Markets Risks Department. This department reports directly to the Bank's Chief Risk Officer and is fully independent of business units. It operates within the framework of Société Générale Group's Market Risk Division. Methodologies for measuring risks and control procedures are thus aligned with the best practices of Société Générale.

## Market risk management methods for the trading portfolio

Several types of measures are used for assessing risks in Komerční banka's trading portfolio:

- Value-at-Risk (VaR) is calculated using historical scenarios with a 99% confidence level and 1-day time horizon. The reliability of the VaR model's results is back-tested while checking the daily P&L against the VaR. KB's Board of Directors is regularly informed about the results of the back-testing.
- The impacts of low-probability events not covered by VaR are assessed using various stress-testing methods and scenarios.
- Volume and sensitivity metrics are used to measure exposure to all relevant risk factors (e.g. FX, interest rate, basis, flight-to-quality, commodities, and credit spread risks).

Market risk limits are approved by two members of the KB Board of Directors (Senior Executive Director Risk Management, Senior Executive Director Top Corporations) after being validated by SG's Market Risk Division.

The Bank uses enhanced valuation techniques for derivatives while taking into account whether a given derivative is concluded with or without collateral agreement and thus reflecting the cost of liquidity.

Komerční banka is not exposed to volatility risk on its market book, as all option derivatives are traded on a back-to-back basis.

## Counterparty risk on financial markets activities

A market transaction may be concluded with a counterparty only on validated products and if approved limits exist for this counterparty. Counterparty limits for financial markets operations are monitored on a daily basis. Any breach of such limits is immediately reported to the relevant level of management within the Bank.

The measurement of counterparty risk arising from derivative products is based on the Credit Value at Risk (CVaR) indicator. This indicator is calculated using Monte Carlo simulation while taking into account netting and collateral effect. With a 99% confidence level, CVaR quantifies the potential future replacement costs of a transaction with a client in case of such client's default.

# Operational risk

The overall strategy for operational risk management is determined by the Operational Risk Committee, which also adopts appropriate steps in case of any negative development in the operational risk area and approves principal changes in the insurance programme utilised for mitigating impacts of operational risk events.

KB has been applying the Advanced Measurement Approach (AMA) to operational risk management and capital requirement calculation since 2008. Capital requirement calculation is performed using a central model of Société Générale. In addition to the standard tools utilised within the AMA approach, such as collecting data on actual operational risk losses, risk control self-assessment, key risk indicators, and scenario analysis, KB also has implemented a system of permanent supervision composed of daily and formalised controls. The headquarters department uses the group instrument GPS (Group Permanent Supervision) to manage and report on these formalised controls. This enables better documentation and monitoring of individual controls. The concept of permanent supervision, which is in line with the principles of the Group, was strengthened in 2016 by introducing a "second stage of controls" aimed at independent verification of the settings and performance of the formalised controls. The process of risk self-assessment has been closely linked to the risk mapping performed by Internal Audit since 2012, thus promoting a consistent approach across the Bank to those risks assessed. Moreover, Komerční banka has been continuously improving its efficiency in collecting information on internal operational risk events while also enhancing the detail of information gathered for each such event. In 2016, Komerční banka Group recorded 590 operational risk events in a final amount of CZK 88.1 million. In a year-on-year comparison, this represents a 27% decrease in the number of losses and slight increase in terms of total loss volumes. In terms of loss volumes, fraud and other criminal acts constitute the most significant long-term risk category.

KB expends considerable effort and resources in the fight against fraud. Within the Bank, there are several teams and systems specifically focused upon preventing and fighting against various types of fraud. During 2016, KB significantly strengthened its ability to detect suspicious and/or fraudulent transactions occurring through direct banking channels (Mojebanka, Mobile Bank, Profibanka, etc.). The Bank has also strengthened measures aimed at prevention, early identification and subsequent investigations of internal fraud.

Co-operation within consolidated operational risk management has been deepened among KB Group companies. Within KB Group, the AMA approach is already used in four Group companies. In addition to the Bank itself, these include two non-banking entities, SGEF and ESSOX, as well as Modrá pyramida.

## Business continuity

Business continuity management consists in developing Komerční banka's structures, procedures and resources intended to cope with extraordinary situations in order to reduce potential damaging impacts these may have on the Bank; protect the entity's employees, clients, assets and activities; and enable it to continue providing basic services and thus to protect KB's reputation, business assets, brands, products, processes and know-how while limiting the impact on KB's financial situation and strength. KB has developed banking business continuity plans for all main vital and critical processes. These plans are regularly updated and tested. The system is subject to regular reviews by external and internal auditors, as well as regulatory authorities.

## Cyber and Information Security

The goal of risk management in the area of cyber and information security is to ensure that the key pillars of information security – confidentiality, integrity, availability and non-repudiation – are properly maintained. Sound management of the mentioned pillars provides adequate security for clients and for the Bank's internal environment. Komerční banka is well aware today of both the continually increasing number of threats originating from the cyber environment and sophisticated new attack vectors. New types of attacks on clients and on bank information systems have potential to go so far as to violate the Bank's cyber and information security. We recognise that the greatest risks originate from the external environment and include risks the likes of fraud, attacks on our clients, penetrating the Bank's information systems, and loss of electronic services availability. Furthermore, Komerční banka is aware of threats that can originate from inside the Bank's organisation, where the greatest risks are associated with internal fraud, misuse of access rights, and potential leakage of banking or other internal information.

Strict application of preventative security policies ensures proper risk management in the area of cyber and information security. These policies are based on several key foundation sources, including Czech Republic and EU laws and regulations, internal Société Générale policies, and the family of ISO/IEC 2700x norms. In implementing the information security management system, the Bank regularly performs risk assessment for its information and IT assets. Assessment results are fully integrated with the overall risk control self-assessment (RCSA) practice.

With the aim to improve its management of identified digital risks, Komerční banka implemented in 2016 the GRC-Archer system. This system centrally manages and controls identified risks from the digital world. KB invested considerable effort and resources during 2016 into projects and initiatives directed to implementing security measures mitigating the aforementioned risks. The Bank implemented technical preventive measures on the network infrastructure, completed its system of advanced protection for payments and transactions processing, and strengthened its control on assigned access rights. It also invested into improving all employees' security awareness through approved yearly education plans.

In 2014, Komerční banka was designated as a processor of critical state infrastructure based on Act No. 181/2014 Coll., on Cyber Security. Accordingly, the Bank implemented new measures in 2016 to meet the requirements of that law. With the goal to further mitigate risks associated with client security, Komerční banka continually pursued its "Securely together" initiative that aims to communicate directly to its clients threats currently existing and the principles of safe behaviour in the digital world. Meanwhile, KB is educating clients and offering them guidance in case of digital emergency. Komerční banka continued also in maintaining its dedicated security website (https://www.kb.cz/security). The Bank further extended the offer for clients to use the IBMTrusteer Rapport security tool. This tool is focused upon protecting from such specific threats as fake and harmful websites (phishing) and malware and upon preventing attempts to detect passwords (e.g. keylogging). Trusteer Rapport was offered originally to clients of internet banking, but in 2016 the offer was augmented with newly developed protection for mobile banking clients on the Android platform.

Komerční banka continually monitors a defined set of key risk indicators, such as number of security exceptions, number and criticality of open vulnerabilities, and number of security incidents. None of those KRIs monitored have deviated over the long term from their approved levels. The Bank neither recorded nor reported during 2016 any cybersecurity incident as per the definition stated in Act No. 181/2014 Coll., on Cyber Security.

## Compliance risk

Compliance risk consists in the potential for breach of regulatory rules and standards, principles of ethical behaviour and, last but not least, internal regulations to be upheld within KB Group and to which the Group is committed and which it has defined on the basis of regulatory rules and general principles. When such risk event comes to pass, this represents possible consequences for the Bank in terms of legal action taken by regulatory agencies and institutions or clients of the Bank, additional risk of financial penalties, damages or remediation costs, and further risk for loss of reputation and goodwill among clients and the general public and thus more possible financial losses.

The Compliance Department is an important part of the Bank's management and control system. It has clearly defined functions and powers to identify these risks and prevent their being realised, particularly consisting in monitoring compliance with established rules and procedures. All KB employees are obliged to follow the rules for management of compliance risk on the basis of internal regulations, and senior employees are required to ensure their continuous education.

To manage compliance risk, KB has established a set of rules and processes within the control and management system. The Bank is scrupulously attentive to their observance. These rules and processes are embedded in the Bank's internal regulations, regarding the content of which employees are regularly reminded and their compliance is regularly controlled.

For the purposes of risk management, the Bank carried out a series of activities ranging from monitoring pending regulatory rules, through co-ordination of their implementation within the Bank, the creation of internal regulations and procedures, and to follow-up inspection and consulting.

The Bank has developed a wide basis of internal regulations within risk management whereby it focuses primarily on preventing violations of regulatory and ethical rules and on minimising the associated risks. The main areas include especially:

- preventing risks of money laundering and financing of terrorism,
- corruption and accepting gifts,
- financial markets,
- distribution and advertising of products,
- payment operations,
- protection of banking secrecy,
- consumer protection,
- client data protection,
- competition and
- rules for the regulation of advertising.

In these areas, the Bank provides training to relevant groups of employees and informs them regarding new regulatory developments. The purpose of this training is to ensure compliance with regulatory requirements while maintaining general awareness about the main principles and rules of conduct which both the Bank and its employees must observe. The Bank provides advisory and support in the aforementioned areas across all KB Group companies.

In the context of compliance risk management, KB insists upon a zero tolerance for fraudulent and dishonest conduct of any sort, as well as for any infringement of the pertinent regulatory and ethical rules, either consciously or through negligence. Special attention is given also to reputational risks that must be taken into account within the context of the Bank's activities.

A number of mechanisms have been put into place to minimise the risks of regulatory non-compliance by the Bank and its employees. In addition to the mentioned training courses, monitoring compliance with the rules is among the most important of these. The results of that monitoring are regularly reviewed, especially in terms of the effectiveness of the implemented rules but also with a view to the proper settings for the individual controls. At the same time, the Bank records findings and conclusions from inspections carried out by regulatory institutions. This includes monitoring the implementation of corrective action where a regulatory institution's inspection has found a discrepancy. Furthermore, individual regulatory inconsistencies identified through normal bank operations are recorded and carefully evaluated. Based on such findings, consideration always is given to measures for preventing these. All these activities and identified indicators are evaluated on a regular basis and reported to the Board of KB.

## Komerční banka's most important compliance risk management activities during 2016

In the area of preventing money laundering and financing of terrorism, the Compliance Department focused during 2016 on analysing the impacts ensuing from adoption of an amendment to Act No. 253/2008 Coll., on Certain Measures against the Legalization of Proceeds from Criminal Activity and the Financing of Terrorism, particularly in connection with the requirements to adjust internal procedures relating to client due diligence and creating an internal risk assessment system for individual client segments and businesses.

New control mechanisms were created during 2016 to strengthen preventive measures in the implementation of international sanctions programmes within KB Group. They contributed to broader engagement with the monitored transactions executed through the Bank and enabled a more expert approach to risk management in this area.

Another priority was to implement both local and international regulatory requirements. The scope and complexity of the new regulation, as well as a high degree of legal uncertainty arising from it, places considerable demands on the Bank's capacities and make it difficult to establish compliance through its systems and processes. The short time between learning the final form of the requirements until the effective date of the legal regulation made their implementation very challenging.

In the area of consumer protection during 2016, projects were being implemented for new regulatory requirements on the providing of consumer loans for residential property and for payment system requirements relating to the EU's Payment Accounts Directive and amendment to the EU's Payment Services Directive. A project to implement a new EU regulation on the protection of personal data also was launched.

The Compliance Department participated in implementing requirements in the area of prudential banking regulation, and especially regarding the EU directive on deposit insurance and on a new EU regulation concerning crisis management of banks.

There were considerable changes in the capital markets area. During the summer of 2016, essential requirements were implemented regarding the Market Abuse Directive II and Market Abuse Regulation (MAD II and MAR). KB began implementation work also in the regulation of key information related to the EU's regulation on Packaged Retail and Insurance-Based Investment Products (PRIIPS). At the end of 2016, the effective date of this regulation was delayed for one year due to significant ambiguity in its interpretation. There was likewise such a shift for the Regulation on Markets in Financial Instruments and the Markets in Financial Instruments Directive II (MiFIR and MiFID II), which will be transposed into the Act on Capital Market Undertakings. Implementation of EU legislation (regard the capital markets and other areas) remains the main task of the Compliance Department for 2017.

## Governing law

As an issuer of publicly traded securities, during 2016 Komerční Banka was governed in its activities particularly by the following laws:

- Act No. 21/1992 Coll., the Banking Act;
- Act No. 256/2004 Coll., on Capital Market Undertakings;
- Act No. 90/2012 Coll., on Business Corporations and Co-operatives;
- Act No. 145/2010 Coll., on Consumer Credit (effective until November 30, 2016);
- Act No. 257/2016 Coll., on Consumer Credit (effective from 1 December 2016);
- Act No. 284/2009 Coll., the Payment Systems Act;
- Act No. 38/2004 Coll., on Insurance Intermediaries and Independent Loss Adjusters and on Amending the Trade Licensing Act;
- Act No. 253/2008 Coll., on Certain Measures against the Legalisation of Proceeds from Criminal Activity and the Financing of Terrorism;
- Act No. 69/2006 Coll., on Implementation of International Sanctions;
- Act No. 563/1991 Coll., on Accounting;
- Act No. 101/2000 Coll., on Personal Data Protection;
- Act No. 143/2001 Coll., on Protection of Economic Competition;
- Act No. 136/2011 Coll., on the Circulation of Banknotes and Coins;
- Act No. 190/2004 Coll., on Bonds;
- Act No. 240/2013 Coll., on Investment Companies and Investment Funds;
- Act No. 89/2012 Coll., the Civil Code;
- Act No. 277/2013, on Foreign Exchange Activities;
- Act No. 634/1992 Coll., on Consumer Protection;
- Regulation (EU) No. 596/2014, on Market Abuse;

- Regulation (EU) No. 575/2013 on Prudential Requirements for Credit Institutions and Investment Firms and Related Implementing Regulations of the European Commission; and
- Regulation (EU) No. 648/2012 on OTC Derivatives, Central Counterparties and Trade Repositories (EMIR).

## Legal risk

Managing legal risk consists in minimising uncertainty associated with enforcement and interpretation of legal acts, agreements, regulations and laws. KB Group applies a variety of techniques, procedures and tools, including regular monitoring of drafted and adopted legislation, close co-operation within the legal teams of KB Group, a system of continuous education of and specialisation among lawyers, detailed documentation and evaluation of outputs and, last but not least, a set of corresponding control mechanisms to manage legal risks.

In addition to standard legal functions within such various areas as contract, banking and corporate law, the main tasks of KB's lawyers during 2016 consisted in reworking a part of contractual documentation for retail banking related to implementation of the Consumer Credit Act and preparatory work on implementing the Payment Services Directive (PSD II) and Payment Accounts Directive (PAD).

### Significant legal disputes

With respect to its overall financial situation, Komerční banka considers as significant all litigations involving principal amounts exceeding CZK 10 million and any bankruptcy proceeding in which the Bank is a creditor with a claim exceeding CZK 50 million.

As of 31 December 2016, KB Group was a party to 8 significant legal proceedings as a plaintiff. The principal that was the subject of these legal proceedings totalled CZK 632.4 million. KB Group was a bankruptcy creditor with a claim exceeding CZK 50 million in 29 bankruptcy proceedings. The total of claims filed in relation to these proceedings was CZK 6.9 billion. As of 31 December 2016, KB Group was a party to a total of 9 significant legal proceedings as a defendant. The principal that was the subject of these legal proceedings totalled CZK 707.7 million.

As of 31 December 2016, KB was a party to a total of 8 significant legal proceedings as a plaintiff. The total principal that was the subject of these lawsuits was CZK 698.6 million. KB was a creditor in 29 bankruptcy proceedings as of 31 December 2016 in which it had a claim exceeding CZK 50 million. The total of KB's claims in these cases was CZK 6.9 billion. As of 31 December 2016, KB was a party to a total of 8 significant legal proceedings as a defendant. The principal that was the subject of these legal proceedings totalled CZK 617.9 million.

Information concerning the provisions created for litigations in which the Bank is a defendant is stated in the Notes to the Separate Financial Statements according to IFRS, Note 36 – "Commitments and contingent liabilities".

In 2016, ESSOX continued resolving claims of a larger number of clients to refund fees paid for concluding consumer loan agreements and to set the level of interest on the respective loans at the CNB's discount rate inasmuch as the claimants considered that disclosure of the contractual parameters in the contracts' documentation had not been in accordance with Appendix 3 of the Consumer Credit Act. ESSOX used all its procedural rights to prove that in concluding the consumer loan agreements it had complied with the Consumer Credit Act, which fact was supported by the relevant courts deciding the cases.

## Internal audit

The main tasks of KB Internal Audit include to assess the functionality and effectiveness of risk management, control processes and the Bank's corporate governance, as well as contribute to improving the organisation's overall operational effectiveness.

KB Internal Audit is integrated into the organisation of the global division of Internal Audit within the SG Group. In addition to conducting audits at KB, it also provided coverage for KB Group subsidiaries and SG Group entities in the Central European region.

The strategic goals of Internal Audit are primarily focused on covering major risks and the most important activities of the Group, including fulfilment of all regulatory requirements. Internal Audit's engagements are driven by the annual audit plan prepared mainly on the basis of assessments of the risks and priority areas (such as embargoes and sanctions). In 2016, 69 audits were carried out, 20 of which were performed in KB Group subsidiaries and two of which were conducted across the KB Group as a whole, including the Bank itself. The 47 audits performed within the Bank covered both the distribution network and head office units, as well as selected companies providing KB with important services (outsourcing). In total, 402 recommendations addressing issues identified by audit engagements were implemented within KB Group during 2016, of which 26 were given significant priority. The Bank proper continued to have the lowest number of long-term unresolved recommendations. As of the year's end, 10 recommendations had been outstanding for more than 18 months.

In its regular report to KB's Board of Directors, the Audit Committee and Supervisory Board, Internal Audit evaluated the Bank's internal control system and declared it effective. A review of the remuneration system in KB, which focused mainly on the fulfilment of CRD IV requirements, was performed for the fifth time and covered also Komerční banka's subsidiaries. No significant findings were revealed.

Using a methodology shared across the entire SG Group, the plan for 2017 draws upon outcomes from a risk assessment and the five-year audit cycle.

## Information on internal control and approach to risks in the process of accounting and preparing financial statements

The Bank uses a number of tools in several areas to ensure true and accurate presentation of facts in the accounting and proper compilation of financial statements. These begin with tools for proper recording of individual transactions, include various controls, and finally involve preparing the statements and their control.

The tools used for proper recording of transactions, events, trades and the like in accounting include, in particular, the selection of appropriate systems (applications) for their recording and processing, thorough testing during their implementation, maximum automation of all repetitive processes, and managing of access rights to individual systems. Setting up systems, processes and controls is always formally governed by the Bank's internal regulations.

Compliance of those accounting methods employed with IFRS in particular is ensured by an independent department that regularly monitors developments in these standards and other regulatory rules, analyses effects ensuing therefrom, and implements the standards in co-operation with relevant departments. For more information on the rules used, see Notes to the Financial Statements, Note 3 "Principal accounting policies" and Note 41 "Risk management and financial instruments".

The Bank utilises a system of defining responsibilities for individual ledger accounts (the so-called ownership system) under which a particular employee authorised to transact with the account and an employee responsible for account analysis are assigned to each account of the general ledger. The control over account analysis includes, in particular, the duty to specify at any time the account balance and to monitor its balance and movements, as well as responsibility for documentary stock-taking of accounts. The control over account analysis also involves reconciliation of data in supporting systems relating to the data in the general ledger at specified regular intervals.

The area of control tools may be divided into two parts: control as to the accuracy of input data and follow-up control over the consistency and integrity of the functioning and accounting of the individual systems. Control over the accuracy of input data is performed especially in the Distribution and Transaction and Payment Services arms within the First Level Control system which constitutes the basis of the Bank's internal control system. The First Level Control system establishes the control activities of the management employees so that there occurs oversight over operational risks arising from the activities of the relevant departments; monitoring of the quality, effectiveness and reliability of the established work procedures; verification of the employees' compliance with the applicable regulations and procedures; and determination of corrective measures in cases when deficiencies are identified.

Follow-up control is carried out in particular by an independent department of the Accounting and Reporting Division which expressly checks the data in the accounting by means of analytical procedures. The main analytical procedures may be classified as control over data consistency as of the current date with the development in the past, consistency between financial and non-financial data (numbers of transactions, trades, etc.), and consistency between the changes in the balance sheet and income statement. The changes in the development of individual items of the financial statements or directly in the general ledger accounts are regularly analysed, and these changes are subsequently reconciled to the changes in trades, prices for services provided and market data, or to changes attributable to one-off items.

An automated system is used to process most financial statements. In most cases, detailed data from source systems is used for their creation and this data is reconciled with the general ledger while at the same time the accuracy of the data in the general ledger is checked.

The effectiveness of internal controls is evaluated by a newly established independent Second Level Control system that examines design and operating effectiveness of both First Level Controls and operational controls. Key risk indicators (such as number of manual transactions, or number and volume of various reconciliation gaps) are also regularly followed up and evaluated in the Bank while their values are kept at very low risk levels in the long term. The internal control system in the financial reporting area is also regularly evaluated by Internal Audit.

# Financial risks

In addition to credit and non-financial risks, the Group is exposed to risks related to changes in interest and exchange rates and liquidity of assets (financial risks). The process of managing financial risks aims to hold risks undertaken to a minimum while also facilitating the Group's organic development. The methods for identifying, measuring and managing risks in the areas of foreign exchange and interest rates are typically based on the requirement to minimise the impact on earnings. KB's Asset and Liability Management & Treasury (ALM & Treasury) Department methodically oversees the processes for asset and liability management within all the individual entities of KB Group. The respective transactions are subject to approval by the Assets and Liabilities Committee (ALCO). ALCO, whose membership includes, among others, members of Komerční banka's senior management, approves rules and methods used in managing the aforementioned risks. It also oversees the levels of risk taken on and the proposed hedging transactions that the Bank executes in order to reduce risk. All ALM activities fully comply with the rules of the Czech regulatory authorities and with relevant international banking regulations.

## Price setting

The process of product price setting is organised on two levels. The first involves the economic principle of determining a proper benchmark in terms of current market conditions and at the level of Komerční banka's portfolio (by ALCO). The second is to determine the price for the customer in view of a combination of marketing objectives and product parameters from the client perspective (by the Commercial Committee). ALM & Treasury provides tools and supports the Bank's business network in valuing transactions, setting client rates, and determining exchange rate spreads. The price-setting strategy is to offer clients products bearing competitive interest rates while always taking into account those costs connected with the price of liquidity and hedging against interest rate risk. In that manner, margins and financial stability are preserved even despite possible changes in market conditions.

## Interest rate risk in the banking book

Interest rate risk constitutes the risk of possible financial loss or negative changes in the Group's net interest income due to movements in market interest rates. KB Group has divided its business activities according to their nature into the banking book and market book. Transactions executed with clients through the branch network typically fall within the banking book while operations on the interbank market belong in the market book. Interest rate risk is measured and managed separately for the banking and market books. With regard to interest rate risk in the banking book, the parent company (i.e. Komerční banka) and Modrá pyramida are the most significant members of the Group. The Group manages its banking book interest rate risk using standard methods (gap analysis, interest rate sensitivity analysis) and a more sophisticated method called Earnings at Risk, which is based on a stochastic evaluation of the volatility of future interest income. The aim of the Group is to minimise banking book risk and not at all to speculate on interest rate changes. To this end, the Group has established prudent limits, which were not exceeded in 2016. KB uses such standard market instruments for hedging against interest rate risk as interest rate swaps and forward rate agreements, as well as investing into securities. All hedging and investment transactions are immediately entered into the Bank's front office system, where they are recorded and priced.

As of 31 December 2016, securities were for the most part held by the Group in the available-for-sale (AFS) and held-to-maturity (HTM) portfolios. In both cases, the Group does not acquire these securities with the intention to sell them before maturity. The selection of portfolio for a given investment is ultimately driven by the need to limit volatility in the volume of regulatory capital otherwise stemming from the Basel III regulatory concept, wherein the revaluation difference of the AFS portfolio is included into the regulatory capital. This means that the reported volume of regulatory capital may be unexpectedly influenced not only due to worsening of the credit quality of the issues but also because of movements in market interest rates. On the other hand, investments in the HTM portfolio cannot be hedged against interest rate risk due to limitations set by rules of hedge accounting. Interest rate derivatives (used for hedging risk in the banking book) are accounted for in accordance with the valid accounting regulations (including IAS 39) in order to achieve the most accurate accounting presentation. KB has worked out a detailed strategy of interest rate risk management that includes descriptions of which derivatives are allowed, how these may be used, and the procedures for their accounting valuations.

## Foreign exchange risk in the banking book of KB Group

Foreign exchange risk is defined as the risk of potential loss to the Group due to fluctuations in currency exchange rates. The Group's foreign exchange risk is measured and managed on a daily basis, and its position is controlled by a system of limits. The strategy is to minimise the impact of foreign exchange risk in the banking book, which means essentially to achieve neutral foreign exchange positions. For the purposes of hedging these, the Bank uses such standard instruments as FX spot and FX forward operations. Within the Group, foreign exchange risk is concentrated especially in Komerční banka itself. The maximum open foreign exchange position of the Group's banking book in 2016 was less than 0.12% of the Group's capital, and thus it was essentially negligible. Part of foreign exchange risk management also involves KB's ability to respond quickly to market developments so as to prevent the conclusion of economically disadvantageous transactions. Komerční banka uses an automatic system for continuously monitoring the development of market rates, and it changes those rates used in client transactions once the market movement reaches a predetermined threshold.

# Capital and liquidity

## Regulatory framework

Komerční banka is subject to supervision by the Czech National Bank (CNB), and, since November 2014, the Société Générale Group is supervised by the European Central Bank.

The regulatory requirements in the European Union are established within the Basel III capital framework through Regulation No. 575/2013 on prudential requirements for credit institutions and investment firms (the Capital Requirements Regulation, or “CRR”) and by Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (Capital Requirements Directive 4, or “CRD IV”). CRD IV was transposed into Czech law by an amendment to the Banking Act and publication of CNB Decree No. 163/2014 Coll. The new regulation establishes, above all, the newly conceived capital ratios as well as more stringent requirements mainly on regulatory capital, liquidity, risk-weighted exposures and overall corporate governance.

The Basel III rules did not change the processes of capital adequacy management, but they were reflected in those processes’ parameters, particularly with regard to implementing an additional combined capital buffer above the 8% minimum required capital. The regulatory methodology stabilised in 2016 (esp. stacking order of capital buffers) and consequently the additional Pillar II buffer of 1.5% over the minimum required capital ratio of 8.0% is applied to the Bank, which means the required TSCR (i.e. total SREP) capital ratio is 9.5%. The combined capital buffer of 5.0% is applied on top of the TSCR capital ratio and it results in the required overall capital ratio of 14.5% for year 2016 (increased by 0.1% in comparison with the previous year). The combined capital buffer consists of the capital conservation buffer of 2.5% and the systemic risk buffer of 2.5%; the countercyclical buffer was not effectively applied. As from 1 January 2017, the regulator increased the required overall capital ratio by 90 basis points to 15.4%. Within the increase, +0.5% is the increased systemic risk buffer, +0.5% is the newly imposed countercyclical buffer, and −0.1% is the decreased capital requirement within Pillar II. The Bank meets the required level of the overall capital ratio with adequate reserve because its capital ratio stands well above the minimum required level.

## Consolidated capital and risk-weighted assets

Total shareholders’ equity comprises the following main items: share capital, reserve funds and retained earnings. Shareholders’ equity decreased year over year by 0.8% to CZK 105.4 billion. The generation of net profit was offset by payment of the annual dividend (KB paid out CZK 11.7 billion in May 2016). Revaluation gains on cash flow hedges were lower due to increase of market interest rates at the end of 2016. The revaluation of the AFS portfolio (which represents primarily reinvestment of client deposits) declined as a result of recognising the payment received for KB’s stake in VISA Europe Ltd. within ‘Net gains from financial operations’ and amortisation of the revaluation differences on securities reclassified from the AFS to HTM portfolio in 2014. As of 31 December 2016, KB held in treasury 1,193,360 of its own shares. This is equivalent to 238,672 shares before the share split in 2016 and constitutes 0.63% of the registered capital. These shares had been acquired in previous years at a cost of CZK 726 million. The split of shares was approved by the General Meeting in order to reduce the price of each individual share and thus make the shares of the Bank more accessible to a greater number of investors. The Bank did not acquire its own shares during 2016. The acquisition of its own shares had been authorised by the General Meeting, particularly for purposes of managing KB’s capital adequacy.

Consolidated regulatory capital for the capital adequacy calculation stood at CZK 71.7 billion as of 31 December 2016. KB Group’s regulatory capital was composed solely of Core Tier 1 equity. The capital adequacy (as well as the Core Tier 1 capital ratio under Basel III standards) stood at 16.2%. The regulatory capital base includes a contribution from a part of the revaluation reserve recognised within the equity account. This item, which pertains to disposable securities in the AFS portfolio and which since 1 January 2015 under the valid rules has been included into the regulatory capital, amounted to CZK 1.5 billion. It increased the capital adequacy ratio by 35 basis points.

Komerční banka uses two advanced approaches for calculating capital requirements related to individual types of risk: the “Advanced Internal Ratings-Based” (AIRB) approach for credit risk (except for KB SK, which uses the Standardised Approach) and the "Advanced Measurement Approach" (AMA) for operational risk.

The volume of the Group's risk-weighted assets (RWA) stood at CZK 442.9 billion as of 31 December 2016, compared to CZK 407.6 billion as of 31 December 2015. RWA for credit risk (including credit valuation adjustments) constituted 86%, operational risk 10%, and market risk 4% of the total RWA. Increase of RWA was caused by growth of exposure across main client segments during 2016 and a moderate increase in average risk weights. The average risk weight for credit risk rose moderately to 39.7% as of 31 December 2016 compared to 37.8% a year earlier, driven by growth in average risk weight for Corporations segments.

*Information on consolidated capital and risk-weighted assets for calculation of capital adequacy (in CZK million)*

### Reconciliation of accounting and regulatory capital

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **Items from Statement of Financial Position – Total shareholders' equity** | **105,400** | **106,229** |
| Share capital | 19,005 | 19,005 |
| Share premium | 150 | 154 |
| Other equity | 405 | 369 |
| Accumulated Other comprehensive income | 14,672 | 17,576 |
| Reserve funds | 4,670 | 4,670 |
| Retained earnings for the previous periods | 49,705 | 48,607 |
| Own shares | (726) | (726) |
| Net profit for the period | 13,688 | 12,758 |
| Non-controlling interest | 3,831 | 3,816 |
| **Total adjustments to CET1** | **(33,741)** | **(39,623)** |
| Gains/(losses) on hedging instruments (cash flow hedging) | (11,379) | (12,653) |
| Additional value adjustment | (186) | (239) |
| Goodwill | (3,752) | (3,752) |
| Other intangible assets, net of tax | (3,648) | (3,642) |
| Insufficient coverage of expected credit losses (lack of provisions) | (1,522) | (1,255) |
| Unusable profit * | (7,529) | (11,783) |
| Non-controlling interest | (3,831) | (3,815) |
| Other transitional adjustments to CET 1 ** | (1,894) | (2,484) |
| **Total capital** | **71,659** | **66,606** |
| **Tier 1 capital** | **71,659** | **66,606** |
| **Core Tier 1 (CET1) capital** | **71,659** | **66,606** |

* Capital adequacy ratio as of 31 December 2016 assuming retained earnings adjusted for Board of Directors' dividend proposal disclosed on 3 November 2016 (55.0% payout ratio).

** As part of gradual phase-in of Basel III rules, the regulatory capital from 1 January 2015 includes a part of the AFS revaluation reserve related to disposable securities in the AFS portfolio. As a result, Total capital and Core Tier 1 adequacy are higher by 35 bps as of 31 December 2016.

### Consolidated risk-weighted assets

| | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **Total risk-weighted assets** | **442,865** | **407,642** |
| **for credit risk** | **376,885** | **341,985** |
| for credit risk pursuant to the Standardised Approach in IRB | 83,919 | 68,034 |
| for credit risk pursuant to the IRB Approach | 292,965 | 273,951 |
| **for settlement risk** | **0** | **4** |
| **for position, foreign exchange and commodity risks** | **20,321** | **20,576** |
| **for operational risk** | **42,327** | **42,270** |
| **for credit valuation adjustment** | **3,333** | **2,807** |

*Information in accordance with Decree 163/2014 on an individual basis (in CZK million)*

| Reconciliation of accounting and regulatory capital | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **Items from Statement of Finacial Position – Total shareholders' equity** | **93,031** | **93,303** |
| Share capital | 19,005 | 19,005 |
| Share premium | 134 | 134 |
| Other equity | 371 | 347 |
| Accumulated Other comprehensive income | 14,136 | 16,881 |
| Reserve funds | 4,188 | 4,188 |
| Retained earnings for the previous periods | 41,804 | 41,050 |
| Own shares | (726) | (726) |
| Net profit for the period | 14,119 | 12,424 |
| **Total adjustments to CET1** | **(25,768)** | **(31,638)** |
| Gains/(losses) on hedging instruments (cash flow hedging) | (11,538) | (12,836) |
| Additional value adjustment | (186) | (239) |
| Other intangible assets, net of tax | (3,214) | (3,202) |
| Insufficient coverage of expected credit losses (lack of provisions) | (1,548) | (1,266) |
| Unusable profit | (7,529) | (11,783) |
| Other transitional adjustments to CET 1 | (1,753) | (2,312) |
| **Total capital** | **67,263** | **61,665** |
| **Tier 1 capital** | **67,263** | **61,665** |
| **Core Tier 1 (CET1) capital** | **67,263** | **61,665** |

| Capital requirements | 31 December 2016 | 31 December 2015 |
|---|---|---|
| **Total capital requirements** | **31,824** | **29,619** |
| **for credit risk pursuant to the Standardised Approach in IRB** | **3,047** | **2,617** |
| Exposures to central governments or central banks | | 2 |
| Exposures to regional governments or local authorities | | |
| Exposures to public sector entities | 5 | 13 |
| Exposures to international development banks | | |
| Exposure to international organisations | | |
| Exposures to institutions | 16 | 15 |
| Exposures to corporates | 1,693 | 1,246 |
| Retail exposures | | |
| Exposures secured by real estate | | |
| Exposures in default | 15 | 3 |
| Exposure associated with particularly high risks | | |
| Exposure to covered bonds | | |
| Items representing securitisation positions | | |
| Exposures to institutions and businesses with short-term credit rating | | |
| Exposures in the form of units of shares or shares in collective investment undertakings | | |
| Equity exposure | 1,318 | 1,338 |
| Other items | | |
| **for credit risk pursuant to the IRB Approach** | **24,225** | **22,453** |
| Exposures to central governments or central banks | 823 | 809 |
| Exposures to institutions | 2,207 | 2,357 |
| Exposures to corporates | 13,171 | 11,875 |
| Retail exposures | 7,309 | 6,572 |
| Equity exposure | 42 | 200 |
| Items representing securitisation positions | 0 | 0 |
| Other assets that are non-credit obligation | 673 | 640 |
| **for position risk** | **1,505** | **1,461** |
| **for large exposures exceeding the limits** | | |
| **to currency risk** | | |
| **to settlement risk** | | **0** |
| **to commodity risk** | **121** | **186** |
| **to operation risk** | **2,926** | **2,902** |

| Capital and ratios (%) | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Capital ratio for common equity Tier 1 | 16.91 | 16.66 |
| Capital ratio of Tier 1 capital | 16.91 | 16.66 |
| Capital ratio for total capital | 16.91 | 16.66 |
| Return on average assets (ROAA) | 1.59 | 1.45 |
| Return on average equity Tier 1 (ROAE) | 22.38 | 20.46 |
| Assets per employee in CZK thousand | 113,280 | 109,005 |
| Administrative costs per employee in CZK thousand | 1,456 | 1,339 |
| Profit or loss after tax per employee in CZK thousand | 1,843 | 1,621 |

## Capital management

The Bank manages its capital adequacy to ensure its sufficient level while allowing for organic business growth and for potentially adverse macroeconomic developments. Under the applicable Basel III regulation of capital adequacy, in addition to the usual reporting of the capital adequacy ratio (so-called Pillar I), regulatory demands comprise also fulfilling conditions for evaluating required economic capital, stress testing and capital planning (so-called Pillar II, or the internal capital adequacy assessment process). To determine the required economic capital, the Group has selected a method close to the regulatory procedures applied for Pillar I. That has resulted in there being very similar levels of necessary economic and regulatory capital.

Given the fact that Basel III capital requirements (and particularly the required capital buffers) are still being developed, the Bank is continuously assessing the impact of their changes in the process of capital planning. As the national regulatory authority, the CNB oversees KB's compliance with capital adequacy requirements on standalone and consolidated bases. During 2016, the Bank met all regulatory requirements. On a regular basis, KB also compiles and reports to the CNB mandatory information regarding its system of internal capital adequacy assessment.

## Stress testing

As an essential part of its risk management under Pillar II, KB regularly simulates hypothetical macroeconomic scenarios involving potential adverse external macroeconomic conditions. On this basis, it estimates impacts upon its financial result and the risk profile of the Bank's business in a medium-term horizon. It subsequently generates expectations for the development of RWA (i.e. capital requirements) and financial results. The results of stress testing are among the inputs considered in determining the Bank's dividend policy. In the liquidity risk area, client behaviour and its effect on the deposit base are modelled on the basis of stress scenarios such that any possible outflow of liquidity would be very securely covered. Consistent with development of the legal framework in France and the USA, liquidity risk management was centralised into the Assets and Liabilities Management Department, under which the Treasury Desk of the Bank was assigned, and this was reflected in the new name of the department.

The results of stress testing in 2016 confirmed that KB is resistant to impacts from potential unexpected adverse developments in the Czech economy.

# Liquidity and funding

KB Group's strong liquidity position is founded upon the various types of customer deposits that it holds and the fact that the Group does not substantially use secondary financing. Thanks to the stability of its large deposit base, the Group had no need to modify the structure of its balance sheet in response to external economic developments by reducing certain types of exposures or seeking to obtain other types of funding. KB Group's strong creditworthiness is supported by its stable financial results, as well as the level of capital adequacy it has achieved. As a result, it has an excellent loans-to-deposits ratio of 83.0%. KB also would meet by a large margin the currently anticipated 3% required leverage ratio. This indicator confirms Komerční banka's solid position and its adequate room for further business growth.

## Funding of KB Group

Client deposits in the volume of CZK 692 billion (not including Other payables to clients) comprise a crucial part (approximately 75%) of the Group's total liabilities and shareholders' equity. Current accounts made up the largest proportion of client deposits within the Group (72%). In addition to its broad and stable base of client deposits, KB Group has other possible funding sources, including debt securities issues and loans taken. Due to its long-term liquidity surplus, Komerční banka did not increase in 2016 the volume of issued debt securities. As of the end of 2016, the total nominal amount of mortgage bonds and other debt securities placed outside KB Group reached CZK 10.8 billion.

## Liquidity management

Liquidity risk management focuses primarily on the ability of the Bank and entire Group to meet their payment obligations at all times. This includes maintaining adequate cash volumes as well as balances on nostro accounts and the mandatory minimum reserves account while not unnecessarily adding to the Bank's costs or restraining its business activities. Liquidity is maintained by rigorous cash flow management. A liquidity snapshot broken down by currency (CZK and foreign) is monitored based on indicators measuring the incoming and outgoing cash flows within particular time horizons.

Behaviour of the client deposit base and clients' use of financing are modelled (including under stress scenarios) in order to maintain a very high certainty of covering possible outflows of funds. Sufficient liquidity is managed using a system of limits. To achieve these, KB uses on- and off-balance sheet transactions on the interbank market. The Group is prudent in its strategy and uses medium- and long-term instruments which allow it to stabilise both volumes and associated costs while at the same time reflecting changes in costs when setting prices.

The Group maintains high liquidity at all times. It covered all its liabilities during 2016 from its internal sources without any problems, and the use of additional secondary funding remained limited. As of 31 December 2016, the Group was not drawing liquidity from central banks. The Group's liquidity cushion is a combination of investments in government bonds and reverse repo operations with the CNB.

With the introduction of Basel III regulation, two new measures were implemented: the Liquidity Coverage Ratio (LCR) and the Net Stable Funding Ratio (NSFR). Both these regulatory indicators are simplified versions similar to those used by KB Group to measure its liquidity. Since the beginning of 2012, KB Group's LCR ratio has been consolidated into SG Group reporting and simultaneously it is reported to the CNB, the local regulator. The estimated levels of LCR and NSFR indicators have long been well above the required 100%.

# Comments on the IFRS consolidated financial results

Komerční banka Group recorded a consolidated and audited attributable net profit of CZK 13,688 million for 2016 under International Financial Reporting Standards (IFRS). This represents a 7.3% increase in comparison with 2015.

## Profit and loss statement

*Note: As from 1 January 2016, Komerční banka reclassified certain items in the income statement and statement of financial position in accordance with IFRS to better reflect the substance of those items and recommendations of the European Banking Authority.*

*Specifically, the contribution to the Deposit Insurance Fund has been reclassified from 'Net interest income' to 'General administrative expenses' and the contribution to the Investor Compensation Fund (supported by securities brokers) has been reclassified from 'Net fees and commissions' to 'General administrative expenses'. In addition, the balances of depository bills of exchange have been reclassified from 'Amounts due to customers' to 'Securities issued'.*

*The comments provided above and below are on a like-for-like basis. Results for the year 2016 and the comparable period 2015 are presented in accordance with the reporting methodology applied from 2016.*

Komerční banka's reported net operating income for 2016 was up by 2.3% to CZK 31,750 million. This growth was markedly influenced by a gain booked in the second quarter from payment received for KB's share in VISA Europe Ltd. in the amount of CZK 959 million. The net banking income excluding this one-off gain reached CZK 30,791 million, down 0.8% year over year.

Net interest income was down by 1.4% to CZK 21,067 million. The growth in the volumes of loans and deposits influenced the result positively. There was also a small contribution from the PSA Finance businesses, consolidated since 1 July 2016. Market interest rates were even lower than in the previous year through most of 2016. Because that weighed upon yields from reinvestment of deposits, net interest income from deposits declined even though the volume of deposits expanded. Net interest income from loans increased due to growth in the volume of financing even as interest spreads on lending products narrowed slightly due to competitive pressure. This effect was more pronounced in consumer lending. The net interest margin, computed as the ratio of net interest income to interest-earning assets reported on the balance sheet, narrowed to 2.5% in 2016 from 2.6% one year earlier.

Net fees and commissions were down by 4.1% to CZK 6,683 million. The number of electronic, card as well as foreign transactions increased, but the reported transaction fee income declined due to a gap in revenues which can be attributed to Cataps, KB's provider of merchant acquiring services, a majority stake of which was sold at the end of the third quarter. Fee income from deposit products was smaller as KB paid out more rewards within the MojeOdměny (MyRewards) loyalty programme and the number of accounts at Modrá pyramida diminished somewhat. Fees for loan services were down as a result of higher commissions paid for mortgages and for consumer loans from ESSOX and also due to previously cancelling retail loan administration fees. Fees from cross-selling rose while the volume of assets under management continued to grow. Fees from specialised financial services declined slightly, affected by diminished demand for bank guarantees due to weaker construction activity, smaller numbers of public tenders, and reduced use of trade finance instruments linked to a drop in corporate clients' trading with some countries. On the other hand, fees from some services grouped into this category, such as for custody and depository, did record growth.

Net gains from financial operations rose by 47.0% to CZK 3,837 million. Even excluding the contribution from the VISA Europe transaction, the result was higher by 10.3%. Income was underpinned by demand from corporate clients for hedging of currency and interest rate risks. This was driven by a presumption that the floor under the Czech crown's exchange rate with the euro is nearing its end, by heightened volatility in prices of financial derivatives, as well as by the growing volume of financing provided to clients which have opted to hedge the risk of future interest rate fluctuations. The fees and commissions from FX transactions were boosted by increasing foreign transactions turnover.

Other income rose by 49.5% to CZK 163 million. In 2016, other income primarily comprised revenues from intermediation and property rental.

Operating expenditures decreased by 2.3% to CZK 14,026 million. The drop is due to revaluation of buildings recognised on the line 'Depreciation, impairment and disposal of assets' in 2015 with a negative impact of CZK 418 million. Excluding this one-off item, operating costs were almost stable (+0.7%). Within this total, personnel expenses were higher by 3.5%, at CZK 7,029 million. The average number of employees rose by 0.6% to 8,476, partly due to the acquisitions. General administrative expenses (excluding the regulatory funds) were down by 0.7% to CZK 4,374 million. Savings were achieved across all main areas except for marketing and information technologies. The cost of contributions to the regulatory funds (Deposit Insurance Fund, Resolution Fund and Investor Compensation Fund of securities brokers) decreased by 3.6% to CZK 880 million. The category 'Depreciation, impairment and disposal of fixed assets' was down by 22.2% to CZK 1,743 million. Excluding the aforementioned revaluation of buildings, the line item was smaller by 4.3%, mainly due to completed amortisation of certain software.

Reported profit before allowances for loan losses, provisions for other risk, profit on subsidiaries and income tax for 2016 was higher by 6.2%, at CZK 17,724 million. Were non-recurring items[1] to be excluded, it would have declined by 2.0%.

The cost of risk increased by 69.1% to CZK 1,818 million from 2015's low figure. This translates into 32 basis points in relative terms as measured over the average volume of the lending portfolio. Provisioning in retail segments remained marginal, reflecting the very good repayment discipline of clients and successful recovery performance. The cost of risk in corporate segments was influenced by creation of provisions for a few isolated cases.

Income from shares in associated undertakings (essentially Komerční pojišťovna) was up by 32.7% to CZK 203 million.

Profit attributable to exclusion of companies from consolidation (related to the sale of a stake in Cataps in the third quarter) reached CZK 727 million.

In the fourth quarter of 2016, KB concluded acquisition accounting for PSA Finance CZ and SK, with a small difference between the net value of assets of the acquired companies and the purchase price.

Income taxes rose by 6.1% to CZK 2,799 million.

At CZK 14,074 million, KB Group's consolidated net profit for the year 2016 was higher by 7.2% in comparison with the prior year. Of this amount, CZK 386 million was profit attributable to holders of minority stakes in KB's subsidiaries (+3.2% versus the year earlier).

Other comprehensive income, which derives from hedging of cash flows, hedging of currency risk for foreign net investments, and profits and losses from financial assets available for sale, net of tax, reached CZK -2,893 million in comparison with CZK -3,588 million in 2015.

The Group's comprehensive income for 2016 amounted to CZK 11,181 million, up by CZK 1,637 million year on year.

## Statement of financial position

*Note: As of 1 January 2016, Komerční banka reclassified depository bills of exchange from 'Amounts due to customers' to 'Securities issued'. The figures have been reclassified retrospectively. As a result of the reclassification, the item 'Amounts due to customers' as of 31 December 2015 contracts by CZK 10.1 billion and the item 'Securities issued' expands by the same amount.*

### Assets

As of 31 December 2016, KB Group's total assets had grown by 3.5% year on year to CZK 922.7 billion. Excluding the value of the acquired assets of PSA Finance CZ and SK, the Group's total assets would have grown by 2.9% to CZK 917.8 billion.

Cash and current balances with central banks dropped by 12.5% to CZK 112.2 billion. The main component of this item comprises the volume of obligatory minimum reserves at central banks.

Amounts due from banks added 8.3% to reach CZK 51.8 billion.

Financial assets measured at fair value through profit or loss went up by 1.8% to CZK 29.7 billion. That line comprises the Group's trading portfolio.

Total net loans and advances picked up by 8.9% year on year to reach CZK 580.2 billion (or by +8.1% to CZK 575.5 billion when excluding PSA Finance CZ and SK). The gross amount of client loans and advances rose by 8.6% to CZK 595.4 billion (+7.7% to CZK 590.6 billion excluding PSA Finance CZ and SK).

1 Non-recurring items excluded in 2015: Revaluation of buildings held for sale (impact net of tax CZK −399 million). In 2016: gain from reimbursement for KB's stake in VISA Europe Ltd. (impact net of tax CZK 777 million), gain related to sale of Cataps (impact net of tax CZK 728 mil.).

The loan portfolio's quality has improved compared to 2015. The share of standard loans climbed to 94.6% (CZK 560.5 billion) while the proportion of loans rated watch was 1.6% (CZK 9.3 billion). Loans under special review (substandard, doubtful and loss) comprised 3.8% of the portfolio, with volume of CZK 22.4 billion. The volume of provisions created for loans reached CZK 15.6 billion. That was 1.6% less than in the prior year.

The portfolio of securities available-for-sale (AFS) diminished by 5.8% to CZK 39.4 billion. Within this portfolio, debt securities comprised CZK 39.2 billion. These included CZK 20.2 billion in Czech government bonds and foreign government bonds of CZK 7.9 billion.

The volume of securities in the held-to-maturity (HTM) portfolio shrank by 2.4% to CZK 65.5 billion. Within this portfolio, Czech government bonds constituted CZK 54.3 billion and foreign government bonds CZK 11.2 billion.

The net book value of tangible fixed assets declined by 2.6% to CZK 6.7 billion, while that of intangible fixed assets added 0.5% to reach CZK 3.9 billion.

Goodwill, which primarily derives from the acquisitions of Modrá pyramida, SGEF and ESSOX, remained unchanged at CZK 3.8 billion.

**Liabilities**

Total liabilities were 4.1% higher in comparison with the prior year and reached CZK 817.3 billion.

Amounts due to banks decreased in 2016 by 3.7% to CZK 54.1 billion. This item represents primarily amounts drawn to cover the Group's short-term liquidity needs in certain currencies.

The total volume of 'Amounts due to customers' was up by 6.6% to CZK 699.4 billion. Excluding volatile repo operations with clients, the overall volume of deposits within KB Group rose by 7.4% year on year to CZK 694.2 billion.

The volume outstanding of issued securities decreased by 37.3% to CZK 13.4 billion. An overview of issued bonds is provided in the chapter Securities issued by KB.

Provisions increased by 47.6% to CZK 1.7 billion. This line item does not include allowances for loan losses, which are reflected at the item 'Loans and advances to customers'. It includes provisions for contractual commitments and provisions for other credit commitments, comprising provisions for off-balance sheet commitments and provisions for undrawn loan facilities.

**Shareholders' equity**

Shareholders' equity decreased year over year by 0.8% to CZK 105.4 billion. The generation of net profit was offset by payment of the annual dividend (KB paid out CZK 11.7 billion in May). Revaluation gains on cash flow hedges were lower due to increase of market interest rates at the end of 2016. The revaluation of the AFS portfolio (which represents primarily reinvestment of client deposits) declined as a result of recognising the payment received for KB's stake in VISA Europe Ltd. within 'Net gains from financial operations' and amortisation of the revaluation differences on securities reclassified from the AFS to HTM portfolio in 2014. KB's share capital remained stable at CZK 19.0 billion.

The cash flow hedging, which reflects the change in the fair value of hedging derivatives, decreased by 10.1% from CZK 12.7 billion at the end of 2015 to CZK 11.4 billion at the end of 2016 and the available-for-sale portfolio revaluation reserve declined by 31.0% in the same period from CZK 5.0 billion to CZK 3.4 billion.

Revaluation of hedging derivatives and the portfolio of securities available-for-sale provides only a limited picture for determining the balance sheet value, as, in accordance with accounting standards, assets and liabilities hedged by derivatives are valued on an accrual basis. Therefore, the book value of the hedging reserve and the value of the hedged assets and liabilities are generated on the basis of different accounting regulations. Similarly, the portfolio of securities available-for-sale is managed to correspond with the development of liabilities having stable interest yields. These, however, are not revalued on a mark-to-market basis.

## Expenses on research and development

In 2016, Komerční banka had outlays through operating expenses of CZK 185 million for research and development. Most of these outlays were related to development studies and implementation of individual projects, particularly in the area of information technologies and systems, including development of internet applications.

# Financial and non-financial investments

### Financial investments made by the Bank* (balance as of the end of the year)

| CZK million, IFRS | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Bonds and treasury bills | 103,260 | 100,900 |
| Shares | 182 | 675 |
| Emissions allowances | 1,839 | 2,800 |
| Equity investments in subsidiary and associated undertakings** | 21,535 | 22,177 |
| **Total** | **126,816** | **126,552** |

Note: *See also the Notes to the Separate Financial Statements prepared in accordance with IFRS, notes no. 17 Financial assets at fair value through profit or loss, no. 18 Available-for-sale financial assets, no. 19 Assets held for sale and no. 22 Held-to-maturity investments.
**Including investment in Held for sale portfolio

### Main investments – excluding financial investments* (balance as of the end of the year)

| CZK million, IFRS | 31 December 2016 | 31 December 2015 |
|---|---|---|
| Tangible fixed assets | 4,664 | 4,444 |
| Intangible fixed assets | 3,428 | 3,427 |
| **Total tangible and intangible fixed assets** | **8,092** | **7,871** |
| Tangible fixed assets held under financial leases | 0 | 0 |

Note: * Net book value of investments. See also Notes to the Separate Financial Statements according to IFRS, notes no. 25 – Intangible fixed assets and 26 – Tangible fixed assets.

### Main ongoing investments – excluding financial investments

In 2016, the Bank made non-financial investments in a total of CZK 1.8 billion. Most of this amount was invested in the area of information technologies (CZK 1 billion) for acquisition and development of software and hardware. A significant part of the total amount was invested into development and reconstruction of branch network, real estate owned by the Bank and ATMs. All of the non-financial investments were made in the Czech Republic and Slovakia and were financed from internal resources.

### Main investments planned by the Bank – excluding financial investments

The investments planned by Komerční banka for 2017 should not exceed CZK 2.2 billion and will be financed from own sources. The Bank will continue to invest mainly into maintenance and development of the distribution network, into quality of provided services and operational efficiency, including investments into information technologies. The Bank's investment plans may be adjusted in accordance with developments in the economic environment.

# Description of real estate owned by KB Group

Komerční banka Group manages real estate used especially to conduct those business activities for which it is licensed under the applicable legal regulations.

### Summary of the real estate managed by KB Group:

| As of 31 December 2016 | Number | Of which owned by KB Group |
|---|---|---|
| Buildings in the Czech Republic | 603 | 105 |
| Buildings in the Slovak Republic | 2 | 0 |
| **Total** | **605** | **105** |

Note: See also the Notes to the Consolidated Financial Statements prepared in accordance with IFRS, notes no. 19 – Assets held for sale and 26 – Tangible assets.

# Trademarks, licences and sublicenses

In 2016, Komerční banka used trademarks for labelling its products and services both in the Czech Republic and the Slovak Republic. Those trademarks used were registered with appropriate intellectual property authorities in the Czech Republic and Slovak Republic.

With the Czech Intellectual Property Office Komerční banka registered a total number of 186 trademarks. In case of a further 6 trademarks, a registration process has been initiated but the process has not yet been completed. In the Slovak Republic, 7 trademarks are registered with the Industrial Property Office of the Slovak Republic.

Within the KB Group, Komerční banka provides to certain of its subsidiaries licenses for its trademarks. In some cases, Komerční banka, is also a licence and sub-licensee, typically from providers of IT services.

# Definitions of the mentioned Alternative Performance Measures

**Housing loans:** mortgages to individuals provided by KB + loans to clients provided by Modrá pyramida;

**Cost of risk in relative terms:** annualised 'Allowances for loan losses' divided by the average of 'Gross amount of client loans and advances', year to date;

**Gross amount of client loans and advances:** 'Gross amount of client loans and advances' minus 'Other amounts due from customers';

**Average of Gross amount of client loans and advances:** ('Gross amount of client loans and advances' minus 'Other amounts due from customers' as of the year end X plus 'Gross amount of client loans and advances' minus 'Other amounts due from customers' as of the year end X-1) divided by 2;

**Net interest margin (NIM):** 'Net interest income' minus 'Dividend income' divided by average interest-earning assets (IEA) year to date (IEA comprise 'Amounts due from banks', 'Cash and current balances with central banks' ['Current balances with central banks' only], 'Net loans and advances to customers', 'Financial assets at fair value through profit or loss' (debt securities only), 'Financial assets available for sale' [debt securities only], 'Investments held to maturity' [debt securities only]). Data for 2015 are reported in accordance with the 2016 reporting methodology (i.e. cost of Deposit Insurance Fund is not included in the category 'Net interest income');

**Reconciliation of 'Net interest margin' calculation, (CZK million, consolidated):**

| *(Source: Profit and Loss Statement)* | FY 2016 | FY 2015 |
|---|---|---|
| **Net interest income (excl. Income from dividends)** | **21,065** | **21,355** |

| *(Source: Balance Sheet)* | 31 Dec 2016 | 31 Dec 2015 | 31 Dec 2014 |
|---|---|---|---|
| Amounts due from banks + Cash and current balances with central banks (Amounts due from central banks only) | 155,016 | 164,778 | 205,022 |
| Loans and advances to customers, net | 580,198 | 532,617 | 494,706 |
| Financial assets at fair value through profit or loss (debt securities only) | 9,606 | 7,872 | 18,765 |
| Financial assets available for sale (debt securities only) | 39,238 | 41,189 | 42,032* |
| Investments held to maturity (debt securities only) | 65,462 | 67,083 | 69,449 |
| **Interest-bearing assets** | **849,520** | **813,540** | **829,974*** |
| **Average interest-bearing assets, year to date** | **831,530** | **821,757** | |
| **NIM year to date, annualised** | **2.5%** | **2.6%** | |

Note: *Excluding financial assets held in the Transformed Fund.

**Net loans to deposits:** 'Net loans and advances to customers' divided by total 'Amounts due to customers'. Data for 2015 are reported in accordance with the 2016 reporting methodology (i.e. depository bills of exchange are not included in the category 'Amounts due to customers');

**Cost to income ratio:** 'Operating costs' divided by 'Net banking income'. Data for 2015 are reported in accordance with the 2016 reporting methodology (i.e. the cost of Deposit Insurance Fund and of Investor Compensation Fund are included in 'General administrative expenses');

**Return on average equity (ROAE):** annualised 'Net profit attributable to equity holders' divided by the quantity average group 'Shareholders' equity' less 'Minority equity', year to date;

**Average group 'Shareholders' equity' less 'Minority equity':** (group 'Shareholders' equity' less 'Minority equity' as of the year end X minus group 'Shareholders' equity' less 'Minority equity' as of the year end X-1) divided by 2;

**Return on average assets (ROAA):** annualised 'Net profit attributable to equity holders' divided by average 'Total assets', year to date.

# Consolidated Financial Statements prepared in accordance with International Financial Reporting Standards as adopted by the European Union as of 31 December 2016

# Consolidated Statement of Income and Consolidated Statement of Comprehensive Income for the year ended 31 December 2016

## Consolidated Statement of Income for the year ended 31 December 2016

| (CZKm) | Note | 2016 | Restated 2015 |
|---|---|---|---|
| Interest income and similar income | 5 | 26,757 | 28,622 |
| Interest expense and similar expense | 5 | (5,692) | (7,267) |
| Dividend income | 5 | 2 | 2 |
| **Net interest income and similar income** | | **21,067** | **21,357** |
| Net fee and commission income | 6 | 6,683 | 6,968 |
| Net profit/(loss) on financial operations | 7 | 3,837 | 2,610 |
| Other income | 8 | 163 | 109 |
| **Net operating income** | | **31,750** | **31,044** |
| Personnel expenses | 9 | (7,029) | (6,793) |
| General and administrative expenses | 10 | (5,254) | (5,319) |
| Depreciation, amortisation, impairment and disposal of assets | 11 | (1,743) | (2,240) |
| **Total operating expenses** | | **(14,026)** | **(14,352)** |
| **Profit before allowances for loan losses, provisions for other risk, profit on subsidiaries and income tax** | | **17,724** | **16,692** |
| Allowances for loan losses | 12 | (1,843) | (1,306) |
| Provisions for other risk expenses | 12 | 25 | 231 |
| **Cost of risk** | | **(1,818)** | **(1,075)** |
| Income from share of associated undertakings | | 203 | 153 |
| Profit/(loss) attributable to exclusion of companies from consolidation | | 727 | 0 |
| Gain on a bargain purchase | | 37 | 0 |
| **Profit before income tax** | | **16,873** | **15,770** |
| Income tax | 13 | (2,799) | (2,638) |
| **Net profit for the period** | 14 | **14,074** | **13,132** |
| Profit attributable to the Non-controlling owners | | 386 | 374 |
| Profit attributable to the Group's equity holders | | 13,688 | 12,758 |
| **Earnings per share/diluted earnings per share (in CZK)** | 15 | **72.48** | **67.55*** |

* Adjusted for the effect of 1-to-5 split of KB shares implemented in April 2016 – see Note 2 Events for the period ended 31 December 2016. The previously reported value of earning per share (before the split) for the year 2015 was CZK 337.77.

## Consolidated Statement of Comprehensive Income for the year ended 31 December 2016

| (CZKm) | Note | 2016 | 2015 |
|---|---|---|---|
| **Net profit for the period** | 14 | **14,074** | **13,132** |
| **Items that will not be reclassified to the Statement of Income** | | | |
| Remeasurement of retirement benefits plan, net of tax | 39 | (93) | (16) |
| **Items that may be reclassified subsequently to the Statement of Income** | | | |
| Cash flow hedging | | | |
| – Net fair value gain/(loss), net of tax | 40 | 1,959 | 136 |
| – Transfer to net profit/(loss), net of tax | 40 | (3,233) | (3,402) |
| Foreign exchange gain/(loss) on hedge of a foreign net investment | | (4) | 0 |
| Foreign exchange difference on translation of a foreign net investment | | 4 | (5) |
| Net value gain/(loss) on available-for-sale financial assets, net of tax | 41 | (1,536) | (273) |
| Net value gain/(loss) on available-for-sale financial assets, net of tax (associated undertakings) | 24 | 10 | (28) |
| **Other comprehensive income for the period, net of tax** | | **(2,893)** | **(3,588)** |
| **Total comprehensive income for the period, net of tax** | | **11,181** | **9,544** |
| Comprehensive income attributable to the non-controlling owners | | 386 | 374 |
| Comprehensive income attributable to the Group's equity holders | | 10,795 | 9,170 |

The accompanying Notes form an integral part of these Consolidated Financial Statements.

# Consolidated Statement of Financial Position as of 31 December 2016

| (CZKm) | Note | 31 December 2016 | Restated 31 December 2015 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and current balances with central banks | 16 | 112,241 | 128,336 |
| Financial assets at fair value through profit or loss | 17 | 29,709 | 29,198 |
| Positive fair value of hedging financial derivatives | 42 | 22,331 | 23,701 |
| Available-for-sale financial assets | 18 | 39,420 | 41,864 |
| Assets held for sale | 19 | 906 | 385 |
| Amounts due from banks | 20 | 51,771 | 47,799 |
| Loans and advances to customers | 21 | 580,198 | 532,617 |
| Revaluation differences on portfolios hedge items | | 32 | 18 |
| Held-to-maturity investments | 22 | 65,462 | 67,083 |
| Current tax assets | | 86 | 367 |
| Deferred tax assets | 34 | 78 | 70 |
| Prepayments, accrued income and other assets | 23 | 4,919 | 4,436 |
| Investments in associates | 24 | 1,280 | 1,219 |
| Intangible assets | 25 | 3,886 | 3,867 |
| Tangible assets | 26 | 6,666 | 6,844 |
| Goodwill | 27 | 3,752 | 3,752 |
| **Total assets** | | **922,737** | **891,556** |
| **LIABILITIES AND EQUITY** | | | |
| Amounts due to central banks | | 1 | 1 |
| Financial liabilities at fair value through profit or loss | 28 | 18,167 | 19,494 |
| Negative fair value of hedging financial derivatives | 42 | 9,428 | 10,055 |
| Amounts due to banks | 29 | 54,124 | 56,230 |
| Amounts due to customers | 30 | 699,377 | 656,287 |
| Revaluation differences on portfolios hedge items | | 762 | 610 |
| Securities issued | 31 | 13,423 | 21,403 |
| Current tax liabilities | | 360 | 83 |
| Deferred tax liabilities | 34 | 3,830 | 4,584 |
| Accruals and other liabilities | 32 | 16,150 | 15,419 |
| Provisions | 33 | 1,714 | 1,161 |
| **Total liabilities** | | **817,336** | **785,327** |
| Share capital | 35 | 19,005 | 19,005 |
| Share premium and reserves | | 82,565 | 83,408 |
| Non-controlling interest | | 3,831 | 3,816 |
| **Total equity** | | **105,401** | **106,229** |
| **Total liabilities and equity** | | **922,737** | **891,556** |

The accompanying Notes form an integral part of these Consolidated Financial Statements.

These Consolidated Financial Statements were approved by the Board of Directors on 7 March 2017.

Signed on behalf of the Board of Directors:

**Albert Le Dirac'h**
Chairman of the Board of Directors and Chief Executive Officer

**Libor Löfler**
Member of the Board of Directors and Chief Operating Officer

## Consolidated Statement of Changes in Equity for the year ended 31 December 2016

| (CZKm) | Share capital | Capital funds and retained earnings/* | Remeasurement of retirement benefits plan | Cash flow hedging | Translation of a foreign net investment | Available-for-sale financial assets | Total equity | Non-controlling interest | Total equity, including non-controlling interest |
|---|---|---|---|---|---|---|---|---|---|
| **Balance as of 31 Dec 2014** | **19,005** | **64,734** | **(22)** | **15,980** | **6** | **6,660** | **106,363** | **3,131** | **109,494** |
| Deconsolidation of Transformed Fund** | 0 | 0 | 0 | (61) | 0 | (1,427) | (1,488) | 0 | (1,488) |
| Treasury shares, other | 0 | 151 | 0 | 0 | 0 | 0 | 151 | 549 | 700 |
| Payment of dividends | 0 | (11,783) | 0 | 0 | 0 | 0 | (11,783) | (238) | (12,021) |
| **Transactions with owners** | **0** | **(11,632)** | **0** | **0** | **0** | **0** | **(11,632)** | **311** | **(11,321)** |
| Profit for the period | 0 | 12,758 | 0 | 0 | 0 | 0 | 12,758 | 374 | 13,132 |
| Other comprehensive income for the period, net of tax | 0 | (28)*** | (16) | (3,266) | (5) | (273) | (3,588) | 0 | (3,588) |
| **Comprehensive income for the period** | **0** | **12,730** | **(16)** | **(3,266)** | **(5)** | **(273)** | **9,170** | **374** | **9,544** |
| **Balance as of 31 Dec 2015** | **19,005** | **65,832** | **(38)** | **12,653** | **1** | **4,960** | **102,413** | **3,816** | **106,229** |
| Treasury shares, other | 0 | 145 | 0 | 0 | 0 | 0 | 145 | 4 | 149 |
| Payment of dividends | 0 | (11,783) | 0 | 0 | 0 | 0 | (11,783) | (375) | (12,158) |
| **Transactions with owners** | **0** | **(11,638)** | **0** | **0** | **0** | **0** | **(11,638)** | **(371)** | **(12,009)** |
| Profit for the period | 0 | 13,688 | 0 | 0 | 0 | 0 | 13,688 | 386 | 14,074 |
| Other comprehensive income for the period, net of tax | 0 | 10*** | (93) | (1,274) | 0 | (1,536) | (2,893) | 0 | (2,893) |
| **Comprehensive income for the period** | **0** | **13,698** | **(93)** | **(1,274)** | **0** | **(1,536)** | **10,795** | **386** | **11,181** |
| **Balance as of 31 Dec 2016** | **19,005** | **67,892** | **(131)** | **11,379** | **1** | **3,424** | **101,570** | **3,831** | **105,401** |

* Capital funds and retained earnings consist of other funds created from profit in the amount of CZK 4,670 million (2015: CZK 4,670 million), share premium, treasury shares and share-based transactions in the amount of CZK -171 million (2015: CZK -203 million), net profit from the period in the amount of CZK 13,688 million (2015: CZK 12,758 million) and retained earnings in the amount of CZK 49,705 million (2015: CZK 48,607 million).

** As of 1 January 2015, Transformovaný fond KB Penzijní společnost, a.s. (Transformed Fund) was deconsolidated from the consolidating group of Komerční banka (refer to Note 2).

*** This amount represents the gain from the revaluation of available-for-sale financial assets (the impact of the consolidation of an associated company using the equity method).

The accompanying Notes form an integral part of these Consolidated Financial Statements.

## Consolidated Statement of Cash Flows for the year ended 31 December 2016

| (CZKm) | 2016 | Restated 2015 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Interest received | 24,026 | 26,084 |
| Interest paid | (4,287) | (6,191) |
| Fee and commission received | 7,915 | 8,542 |
| Fee and commission paid | (1,407) | (1,709) |
| Net cash received from financial operations | 2,399 | 1,735 |
| Other receipts | 110 | 100 |
| Cash payments to employees and suppliers, and other payments | (12,450) | (11,489) |
| **Operating cash flow before changes in operating assets and operating liabilities** | **16,306** | **17,072** |
| Amounts due from banks | (3,331) | 11,309 |
| Financial assets at fair value through profit or loss | (507) | 12,660 |
| Loans and advances to customers | (43,765) | (39,621) |
| Other payments received | 118 | (550) |
| **(Increase)/decrease in operating assets** | **(47,485)** | **(16,202)** |
| Amounts due to banks | (6,192) | 7,813 |
| Financial liabilities at fair value through profit or loss | (1,329) | (3,979) |
| Amounts due to customers | 43,952 | 6,855 |
| Other payments made | 145 | 3,358 |
| **Increase/(decrease) in operating liabilities** | **36,576** | **14,047** |
| Net cash flow from operating activities before taxes | 5,397 | 14,917 |
| Income tax paid | (2,335) | (2,696) |
| **Net cash flow from operating activities** | **3,062** | **12,221** |
| **CASH FLOWS FROM INVESTMENT ACTIVITIES** | | |
| Dividends received | 154 | 142 |
| Purchase of held-to-maturity investments | (6,005) | (3,369) |
| Maturity of held-to-maturity investments* | 8,640 | 6,454 |
| Purchase of available-for-sale financial assets | (1,353) | (4,525) |
| Sale and maturity of available-for-sale financial assets * | 3,762 | 5,963 |
| Purchase of tangible and intangible assets | (2,089) | (1,921) |
| Sale of tangible and intangible assets | 57 | 41 |
| Purchase of investments in subsidiaries and associates | (885) | 0 |
| Sale of investments in subsidiaries and associates | 727 | 0 |
| Effect of acquisition of companies | (157) | 0 |
| **Net cash flow from investment activities** | **2,851** | **2,785** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Dividends paid | (11,735) | (11,750) |
| Dividends paid to non-controlling interest | (375) | (238) |
| Securities issued | 0 | 794 |
| Securities redeemed* | (9,874) | (16,501) |
| Increase in share capital and share premium | 0 | 549 |
| **Net cash flow from financing activities** | **(21,984)** | **(27,146)** |
| **Net increase/(decrease) in cash and cash equivalents** | **(16,071)** | **(12,140)** |
| Cash and cash equivalents at the beginning of the year | 126,132 | 138,698 |
| Foreign exchange differences on cash and cash equivalents at beginning of year | 2 | (7) |
| Deconsolidation of Transformed Fund | 0 | (419) |
| **Cash and cash equivalents at the end of the year** (refer to Note 36) | **110,063** | **126,132** |

* The amount also includes coupons received and paid.

The accompanying Notes form an integral part of these Consolidated Financial Statements.

# Notes to the Consolidated Financial Statements as of 31 December 2016

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# 1 Principal activities

The Financial Group of Komerční banka, a.s. (henceforth the "Group") consists of Komerční banka, a.s. (the "Bank") and 12 subsidiaries and three associated undertakings. The parent company of the Group is the Bank which is incorporated in the Czech Republic as a joint-stock company. The principal activities of the Bank are as follows:

I. Providing loans, advances and guarantees in Czech crowns and foreign currencies;
II. Acceptance and placement of deposits in Czech crowns and foreign currencies;
III. Providing current and term deposit accounts in Czech crowns and foreign currencies;
IV. Providing banking services through an extensive branch network in the Czech Republic;
V. Treasury operations in the interbank market;
VI. Servicing foreign trade transactions;
VII. Investment banking.

The Bank generates the preponderant proportion of the Group's income and represents substantially all of the assets and liabilities of the Group.

The registered office address of the Bank is Na Příkopě 33/969, 114 07 Prague 1.

In addition to its operations in the Czech Republic, the Group has operations in Slovakia through its foreign branch (Komerční banka, a.s., pobočka zahraničnej banky) and in Belgium through its subsidiary (Bastion European Investments S.A).

The Bank's ordinary shares are publicly traded on the Prague Stock Exchange. Société Générale S.A. is the Bank's majority shareholder, holding 60.35% (2015: 60.35%) of the Bank's issued share capital.

*The main activities of the Bank's subsidiary companies as of 31 December 2016:*

| Company's name | Direct holding % | Group holding % | Principal activity | Registered office |
|---|---|---|---|---|
| KB penzijní společnost, a.s.* | 100.0 | 100.0 | Financial services | Prague |
| Modrá pyramida stavební spořitelna, a.s. | 100.0 | 100.0 | Building society | Prague |
| Protos, uzavřený investiční fond, a.s. | 83.65 | 100.0 | Investments | Prague |
| Factoring KB, a.s. | 100.0 | 100.0 | Factoring | Prague |
| Bastion European Investments S.A. | 99.98 | 99.98 | Financial services | Brussels |
| KB Real Estate s.r.o. | 100.0 | 100.0 | Support services | Prague |
| NP 33, s.r.o. | 100.0 | 100.0 | Support services | Prague |
| VN 42, s.r.o. | 100.0 | 100.0 | Support services | Prague |
| SG Equipment Finance Czech Republic s.r.o. | 50.1 | 50.1 | Industry financing | Prague |
| ESSOX s.r.o. | 50.93 | 50.93 | Consumer loans, leasing | České Budějovice |
| PSA FINANCE ČESKÁ REPUBLIKA, s.r.o. | 0.0 | 50.93 | Consumer loans, leasing | Prague |
| PSA FINANCE SLOVAKIA, s.r.o. | 0.0 | 50.93 | Consumer loans, leasing | Bratislava |

* As of 1 January 2015, the Transformovaný fond KB Penzijní společnost, a.s. (Transformed Fund) was deconsolidated from the Group.

*The main activities of the Bank's associated undertakings as of 31 December 2016:*

| Company's name | Direct holding % | Group holding % | Principal activity | Registered office |
|---|---|---|---|---|
| Komerční pojišťovna, a.s. | 49.0 | 49.0 | Insurance | Prague |
| Czech Banking Credit Bureau, a.s. | 20.0 | 20.0 | Data collection for credit risk assessments | Prague |
| Cataps, s.r.o. | 20.0 | 20.0 | Financial services | Prague |

## 2 Events for the year ended 31 December 2016

**Dividends declared in respect of the year ended 31 December 2015**

At the General Meeting held on 22 April 2016, the shareholders approved a dividend for the year ended 31 December 2015 of CZK 310 per share before tax. The dividend was declared in the aggregate amount of CZK 11,783 million and the remaining balance of the net profit was allocated to retained earnings. The dividends were paid out in Czech crowns. Moreover, the Group paid out CZK 375 million in dividends to non-controlling owners of ESSOX s.r.o.

**Announcement on the Bank‘s share split**

The General Meeting held on 22 April 2016 approved a split of the Bank's shares in the ratio of 5:1. The split took legal effect on 25 April 2016 with its entry into the Register of Companies. Shareholders received five new shares with nominal value CZK 100 in place of each old share in the nominal value of CZK 500. Trading of the split shares on the Prague Stock Exchange was started on 12 May 2016.

**Changes in the Bank's financial group**

In March 2016, the Bank concluded an agreement on the sale of its interest in Cataps, s.r.o. with Worldline SA/NV based upon which the Bank transferred its merchant acquiring into Cataps, s.r.o. and subsequently sold its 80% stake in Cataps, s.r.o. Both steps were performed in September 2016. The selling price for the 80% stake in Cataps, s.r.o. was CZK 727 million. The remaining 20% stake in Cataps, s.r.o. was valued at CZK 8 million and reclassified as *'Assets held for sale'* due to the expected sale of this company.

In April 2016, the Bank's subsidiary ESSOX s.r.o. concluded agreements to acquire 100% ownership stakes in PSA FINANCE ČESKÁ REPUBLIKA, s.r.o. and in PSA FINANCE SLOVAKIA, s.r.o. from members of the Paris-based Banque PSA Finance group. The acquisitions were finalised in July 2016 after obtaining all required regulatory approvals.

In May 2016, the equity in Bastion European Investments S.A. was decreased by EUR 3.5 million (equivalent to CZK 100 million). The decrease was initiated solely by the Bank as the majority shareholder of Bastion European Investments S.A.

In June 2016, the Bank's investment into subsidiary NP 33, s.r.o., valued at CZK 405 million, was reclassified as *'Assets held for sale'* due to expected sale of this company.

In November 2016, the Bank decided to decrease share capital and to dissolve the reserve and statutory funds of NP 33, s.r.o., that amount totalling to CZK 170 million. The process of decreasing the share capital was finalised in December 2016.

In December 2016, the Bank decreased the capital of its subsidiary Protos, uzavřený investiční fond, a.s. through decreasing the reserve fund by CZK 450 million. The share of the Bank in this decrease was CZK 376 million, which reflects the Bank's 83.65% ownership share. The remaining ownership is held by Factoring KB, a.s., which is fully owned by the Bank.

## 3 Principal accounting policies

The principal accounting policies adopted in the preparation of these Consolidated Financial Statements are set out below.

### 3.1 Statement of compliance with IFRS

The Consolidated Financial Statements are prepared pursuant to and comply with International Financial Reporting Standards (hereafter only "IFRS") as adopted by the European Union and effective for the annual period beginning on 1 January 2016.

The presented Consolidated Financial Statements for the year ended 31 December 2016 are prepared on the basis of current best estimates. The management of the Group believes that these present a true and fair view of the Group's financial results and financial position using all relevant and available information as of the financial statements date.

## 3.2 Underlying assumptions of the Consolidated Financial Statements

### 3.2.1 Accrual basis

The Consolidated Financial Statements are prepared on an accrual accounting basis (i.e. the effects of transactions and other events are recognised when they occur and are reported in the Consolidated Financial Statements for the period to which they relate).

The exception is the Consolidated Statement of Cash Flows, which is prepared on a cash basis (i.e. it presents cash inflows and outflows during the reporting period without regard to the period to which each transaction relates).

### 3.2.2 Going concern

The Consolidated Financial Statements are prepared on the assumption that the Group is a going concern and will continue in operation for the foreseeable future. The Group has neither the intention nor the need to liquidate or materially curtail the scale of its operations.

### 3.2.3 Reporting period

The Group reports for a 12-month period which is identical to the calendar year.

## 3.3 Basis of preparation

### 3.3.1 Presentation currency

The Consolidated Financial Statements are presented in Czech crowns (hereafter only "CZK"), which constitute the Group's presentation currency. The balances shown are stated in CZK million unless indicated otherwise.

### 3.3.2 Historical cost

The Consolidated Financial Statements are prepared under the historical cost convention, except for available-for-sale financial assets, financial assets and liabilities at fair value through profit or loss and hedging derivatives and hedge items in fair value hedge accounting, whose items are measured at fair value.

Assets held for sale are measured at the lower of their (i) fair value less cost to sell, or (ii) carrying amount just prior to reclassification into *'Assets held for sale'*.

### 3.3.3 Significant accounting judgements and estimates

In applying the accounting policies for the purpose of preparing the Consolidated Financial Statements in accordance with IFRS, it is necessary for the Group's management to use professional judgement and make estimates and assumptions. These impact upon reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities as of the financial statements date and the reported amounts of revenues and expenses during the reporting period. These estimates and judgements are based on the information available as of the financial statements date and they relate especially to the determination of:

- Fair values in the Statement of Financial Position of financial instruments not quoted in an active market which are classified as financial assets or liabilities at fair value through profit or loss, hedging derivatives or available-for-sale financial assets (refer to Note 3.5.5);
- The value of intangible assets, except goodwill (refer to Note 3.5.9);
- The amount of impairment of assets (refer to Notes 3.5.5, 3.5.9 and 3.5.10);
- Provisions recognised under liabilities (refer to Note 3.5.11);
- The initial value of goodwill for each business combination (refer to Note 3.5.10);
- The amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies (refer to Note 3.5.7); and
- Assessment of the substance of participation interest in Group entities (refer to Note 3.3.4).

Information about the key judgements and assumptions concerning the future and other key sources of estimation uncertainty as of the financial statements date that have a significant risk of causing material adjustment to the carrying values of assets and liabilities are disclosed in individual notes as appropriate.

### 3.3.4 Basis of consolidation

The Consolidated Financial Statements incorporate the financial statements of the Bank and of its subsidiaries. A subsidiary is an entity over which the Bank has control, i.e. the Bank is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. When assessing the control the Group considers all relevant facts and circumstances while taking into account particularly voting rights, potential voting rights  and contractual arrangements. This assessment may require usage of accounting judgements. Subsidiaries are consolidated using the full method of consolidation from the date when the Bank obtains control to the date when the Bank ceases to exercise control over such entity.

The financial statements of the consolidated subsidiaries used to prepare the Consolidated Financial Statements were prepared as of the Bank's financial statements date and using consistent accounting policies. The assets and liabilities of foreign subsidiaries and branches are translated into the Bank's presentation currency at the rate of exchange as of the Bank's financial statements date, and their items of income and expense are translated at the monthly average exchange rates for the respective month of a given transaction. Exchange differences arising on translation are taken directly to a separate component of equity. The consolidation principles are unchanged as against the previous year. All intragroup transactions, balances, income and expenses were eliminated in full.

Investments in associates are presented in the Consolidated Financial Statements using the equity method. An associate is an entity in which the Bank has significant influence, i.e. it directly or indirectly owns 20% to 50% of voting rights but it does not exercise control. Equity accounting involves recognising in the Consolidated Statement of Income and in the Consolidated Statement of Comprehensive Income the Group's share of the associates' profit or loss for the period and comprehensive income for the period. The Group's interest in the associates in the Statement of Financial Position is initially recognised at cost and adjusted thereafter for the post-acquisition change in the investor's share of net assets of the investee.

## 3.4 Application of new and revised IFRS

### 3.4.1 Standards and interpretations newly applied by the Group in the current period

The following standards, interpretations and amendments were newly applied by the Group as from 1 January 2016. They have no impact in the current period (and/or prior period).

| Standard | Impact/Comments |
|---|---|
| **Annual Improvements to IFRS 2010–2012 Cycle*** | Annual Improvements amend seven standards in a total of eight points predominantly with the objective of removing unintentional inconsistencies in individual standards or redundant or confusing references and improving wording or updating out-of-date terminology. |
| **Defined Benefit Plans: Employee Contributions (Amendments to IAS 19 Employee Benefits)*** | The amendment defines principles for recognition of employee contributions within defined benefit plans distinguishing the procedures for contributions the amounts of which are not dependent upon length of service and those the amounts of which are so dependent. |
| **Accounting for Acquisition of Interests in Joint Operations (Amendments to IFRS 11 Joint Arrangements)** | The amendments provide guidance on the accounting for acquisition of interests in existing joint operations in which the activity constitutes a business as defined in IFRS 3 Business Combinations. It also applies to the formation of a joint operation if, and only if, an existing business is contributed to the joint operation on its formation. The acquirer is required to apply, to the extent of its share, the principles of business combination accounting and disclosures in IFRS 3 and other IFRS, if not conflicting with the guidance in IFRS 11. |
| **Annual Improvements to IFRS 2012–2014 Cycle** | Annual Improvements amend four standards in a total of five points predominantly with the objective of removing unintentional inconsistencies in individual standards or redundant or confusing references and improving wording or updating out-of-date terminology. |
| **Disclosure Initiative (Amendments to IAS 1 Presentation of Financial Statements)** | Given that the amendments clarify existing requirements in IAS 1 which do not directly affect an entity's accounting policies or accounting estimates, there is no need under the transitional provisions to disclose the information otherwise required by IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. |
| **Investment Entities: Applying the Consolidation Exception (Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities and IAS 28 Investments in Associates and Joint Ventures)** | The amendments to IFRS 10 and IAS 28 further clarify application of the consolidation exception to entities in group structures involving investment entities. |

* The European Commission has approved Annual Improvements to IFRS 2010–2012 Cycle and Defined Benefit Plans: Employee Contributions (Amendments to IAS 19 Employee Benefits) for reporting periods beginning on or after 1 February 2015. According to the IASB, both documents are effective already for reporting periods beginning on or after 1 July 2014.

### 3.4.2 Issued standards and interpretations not applied for the current period

Although the following standards, interpretations and amendments had been issued, they are not yet effective for the reporting period beginning on 1 January 2016 and the Group has decided not to adopt them early. The Group has decided not to adopt early the standards and interpretations which were already approved by the European Commission.

Currently, the Group does not anticipate that their application will significantly impact the Group's financial position and financial performance for the reporting period, with the exception of IFRS 9 Financial Instruments and IFRS 16 Leases.

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments supersedes the existing standard IAS 39. It introduces a new approach to the classification and measurement of financial assets, a new impairment methodology and new hedge accounting rules for micro hedges. Accounting and rules for macro hedging were separated from the IFRS 9 project. The IASB is still working on developing a new macro hedging model, the first discussion paper was issued in April 2014.

The application of the new classification and measurement methodology means that financial assets must be classified upon initial application of the standard based on both the entity's business model for managing the financial assets (held to collect, held to collect and sell, other business models) and the financial asset's contractual cash flow characteristics, i.e. applying of the "solely payment of principal and interest" test (SPPI). Financial assets will be newly measured at amortised cost, at fair value through profit or loss, or at fair value through other comprehensive income. In general no impact, with the exception mentioned below, is expected for debt instruments classified in the current portfolio as held-to-maturity, loans and receivables and fair value through profit or loss. Debt instruments classified in the portfolio of available-for-sale are expected to be newly measured at amortised cost rather than at fair value through other comprehensive income, as meeting both criteria: hold to collect business model and SPPI characteristics. With respect to equity instruments classified in the portfolio of available-for-sale, the Group will need to decide whether it will measure these through profit or loss or whether it will use the FVOCI option and thus recognise changes in their fair value in other comprehensive income. The decision for the existing instruments is expected to be made during 2017 but not later than at initial application of the standard. As at 1 January 2018, the remaining unamortised revaluation reserve in Other Comprehensive Income from the reclassification in 2014 of certain debt securities from the available-for-sale to held-to-maturity portfolio and also the revaluation reserve from available-for-sale debt instruments newly measured at amortised costs will be both removed from equity and adjusted against the fair value of the financial assets. Similarly, the related deferred tax will be in both cases removed from equity. Any potential difference in approach to amortization of revaluation reserve subsequent reclassifications to held-to-maturity would be recognized in retained earnings under IFRS 9.

The application of the new impairment methodology, superseding the current IAS 39 incurred loss model, means earlier recognition of expected credit losses from the point at which financial instruments originate or are acquired. The Group is going to utilise Société Générale Group IFRS 9, always considering the materiality of the portfolio or entity. For portfolios covered by an advanced approach to capital adequacy (IRBA), great attention is dedicated to assuring the consistency of provisions calculations according to IFRS 9 with the risk-weighted assets calculation (the usage of the same statistical models in both calculations) and regular stress-testing approach (forward-looking predictions in IFRS 9 calculations to be the same as in the regular stress testing). Overall, the Group will use a consistent approach in all key areas, mainly in classification of financial instruments in stages/buckets. The Group is already well advanced in the implementation of the IFRS 9 requirements that it will be obliged to apply from the beginning of 2018. Technical implementation should be finished by the end of the second quarter of 2017 and will be based on the utilization of existing IT tools. The Bank also supports subsidiaries in implementing IFRS 9 and updating current interfaces necessary for preparing the Consolidated Financial Statements. Parallel regular running of IAS 39 and IFRS 9 provisions calculation is expected to be started in the second quarter of 2017.

For the transitional purposes, the Group will use the relief from restating prior periods. Any differences from the initial application of the standard will be recognised in equity.

As regards hedge accounting, IFRS 9 provides entities with an accounting policy choice: either to continue to apply existing requirements in IAS 39 until the macro hedging project is finalised or to apply the requirements of IFRS 9. The Group assumes to apply IFRS 9, but it does not expect any significant changes.

IFRS 16 Leases

IFRS 16 Leases replaces the current standard IAS 17. The new standard will fundamentally change the accounting from the lessee's point of view when ceasing to distinguish between finance leases and operating leases, and instead introducing a single on-balance sheet accounting model. This will be applicable for almost all leases with the optional exceptions for short-term leases and leases for which the underlying asset is of low value. The accounting by lessors under the new standard is substantially unchanged from today's accounting in IAS 17.

The Bank has already carried out the initial assessment and identified potential areas to be impacted by the application of the new IFRS 16 requirements. The Bank as a lessee under operating lease of office buildings and branches, in particular, will need to recognise those leases on the balance sheet causing an increase of assets (right-of-use assets) and liabilities (lease liabilities). Processes and systems need to be evaluated to comply with the increased disclosure requirements.

The Bank will also need to assess the potential effects of IFRS 16 on capital adequacy requirements and resolution fund contribution. So far, however, inasmuch as the prudential regulator has not expressed its view on how the right-of-use asset will be treated for regulatory purposes, developments in this area need to be monitored.

A further area of interest may include the Bank as a lender or financial services provider. For clients reporting under IFRS that have entered into significant lease contracts currently classified as operating leases, the transition to IFRS 16 will have a significant impact on their financial statements and key financial metrics, based on the recognition of new assets and liabilities, and the differences in timing and classification of lease expenses. The impacts on clients credit assessment or risk evaluation need to be considered. Based, however, on the current status wherein the number of IFRS clients is immaterial and due to the fact that these clients are mostly large and therefore expert rating is provided, we do not expect significant impacts in this area.

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures) | The amendment clarifies the accounting treatment for sale or contribution of assets between an investor and its associates or joint ventures. It resolves a current inconsistency between the existing requirements in IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures on how to calculate any gain or loss arising from this transaction. The accounting treatment depends on whether the non-monetary assets as subject of the transaction constitute a "business", as defined in IFRS 3 Business Combinations. In such case, the gain or loss is recognised in full. | The effective date of 1 January 2016 was withdrawn and deferred indefinitely.<br>Early adoption continues to be permitted.<br>EU postponed |
| Recognition of Deferred Tax Assets for Unrealised Losses (Amendments to IAS 12 Income Taxes) | The amendments to IAS 12 clarify how to account for a deferred tax asset that is related to debt instruments measured at fair value for accounting purposes and at cost for tax purposes in circumstances in which changes in the market interest rate decrease the fair value below cost. This applies irrespective of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use. The amendments also clarify that the carrying amount of an asset does not limit the estimation of probable future taxable profits. | 1 January 2017<br>EU not yet endorsed |
| Disclosure Initiative (Amendments to IAS 7) | The amendments require disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The following changes shall be disclosed (to the extent necessary): changes from financing cash flows, changes arising from obtaining or losing control of subsidiaries or other businesses, the effect of changes in foreign exchange rates, changes in fair values and other changes. | 1 January 2017<br>EU not yet endorsed |
| Annual Improvements to IFRS 2014–2016 Cycle | Annual Improvements amend three standards predominantly with the objective of removing unintentional inconsistencies in individual standards or redundant or confusing references and improving wording or updating out-of-date terminology. | 1 January 2017 (amendment to IFRS 12)<br>1 January 2018 (amendments to IFRS 1 and IAS 28)<br>EU not yet endorsed |
| Classification and Measurement of Share-based Payment Transactions (Amendments to IFRS 2) | The amendments relate to three areas: the accounting for the effects of vesting conditions on cash-settled share-based payment transactions, the classification of share-based payment transactions with net settlement features for withholding tax obligations, the accounting for modification of a share-based payment transaction that changes its classification from cash-settled to equity-settled. | 1 January 2018<br>EU not yet endorsed |

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| IFRS 15 Revenue from Contracts with Customers – new standard | The new standard supersedes current revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.<br><br>It outlines a single comprehensive model for accounting and disclosure of revenue arising from contracts with customers to provide goods or services, regardless of the industry or the type of transaction. For the banking sector, the following areas in particular may be affected: credit card loyalty schemes, pricing mechanisms including variable amounts, distinct goods or services in multi-element arrangements, up-front fees at or near contract inception.<br><br>The Bank is assessing the potential impact on its financial statements. However, as the Bank's main business lies outside the scope of IFRS 15, our expectation is that it will not be significant. | 1 January 2018 |
| Clarifications to IFRS 15 Revenue from Contracts with Customers | The amendments clarify IFRS 15 in three areas (identifying performance obligations, principal versus agent considerations and licensing application guidance) and provide two additional practical expedients for transition purposes (completed contracts under the full retrospective transition approach and modified contracts). | 1 January 2018<br>EU not yet endorsed |
| IFRS 16 Leases – new standard | The new standard, superseding IAS 17 Leases and related interpretation, establishes principles for the recognition, measurement, presentation and disclosure of leases for both: the lessee and the lessor.<br><br>From the lessee's point of view, the standard newly provides a single on-balance sheet accounting model. Lessees are required to recognise assets and liabilities (so-called right-of-use assets and lease liabilities) for all leases unless the lease term is 12 months or less or the underlying asset is of a low value, in which case the lessees have an accounting policy choice to apply a method similar to operating leases under IAS 17. The right-of-use asset is treated similarly as are other non-financial assets; it is depreciated in accordance with the requirements in IAS 16 Property, Plant and Equipment and tested for impairment under IAS 36 Impairment of Assets. The lease liability is initially measured at the present value of the lease payments payable over the lease term, discounted at the rate implicit in the lease if that can be readily determined. If that rate cannot be readily determined, the lessee shall use its incremental borrowing rate.<br><br>Lessors continue to classify leases as operating or finance, with an accounting approach substantially unchanged from IAS 17. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of the underlying asset. Otherwise a lease is classified as an operating lease. For a finance lease, the lessor recognises finance income over the lease term, based on a pattern reflecting a constant periodic rate of return on the net investment. The net investment in the lease (lease receivable) is subject to the derecognition and impairment requirements in IFRS 9 Financial Instruments. For operating leases, the lessor recognises lease income on either a straight-line basis or another systematic basis that is more representative of the pattern in which benefit from use of the underlying asset is diminished. | 1 January 2019<br>EU not yet endorsed |

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| IFRS 9 Financial Instruments – new standard | In July 2014, the final version of IFRS 9 was issued, replacing the current IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. It introduces a new approach to the classification and measurement of financial assets, a new impairment methodology and new hedge accounting rules for micro hedges. Accounting and rules for macro hedging were separated from the IFRS 9 project and are part of a separate project (Discussion Paper, April 2014). The new IFRS 9 shall be applied retrospectively except for micro hedge accounting.<br><br>The classification and measurement of financial assets depends on assessment of both a financial asset's contractual cash flow characteristics and the entity's business model for managing the financial asset. The resulting measurement categories are:<br>• Amortised cost;<br>• Fair value through other comprehensive income; and<br>• Fair value through profit or loss.<br><br>In comparison to IAS 39, the embedded derivatives in financial assets are no longer bifurcated.<br><br>In respect to financial liabilities, IFRS 9 retains almost all of the existing requirements from IAS 39 except changes in the entity's own credit risk for financial liabilities designated at fair value through profit or loss using the fair value option, which are newly presented in other comprehensive income.<br><br>The impairment requirements in the new standard are based on an expected credit loss model. For all financial assets in the scope of IFRS 9 that are not accounted for at fair value through profit or loss and excluding also equity instruments, entities are required to recognise from origination throughout the life of an asset either 12-month expected credit losses or lifetime expected credit losses, when credit risk significantly increases after initial recognition. The measurement of expected credit losses should reflect a probability-weighted outcome, the time value of money and reasonable and supportable information.<br><br>In November 2013, new requirements related to general hedge accounting (micro hedge accounting) were added to IFRS 9. These requirements align hedge accounting more closely with risk management, which means that more of an entity's risk management activities may qualify for hedge accounting and more designations of groups of items as hedged items are possible. The new model does not fundamentally change the types of hedging relationships or the requirement to measure and recognise ineffectiveness under IAS 39. However, there is only a prospective effectiveness test remaining that is newly based on objective (focus on the economic relationship between the hedged item and the hedging instrument) replacing the range of 80–125%. As a consequence of the new general hedge accounting rules in IFRS 9, additional hedge accounting disclosure requirements were introduced into IFRS 7 Financial Instruments: Disclosures. | 1 January 2018 |
| Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4) | The amendments to IFRS 4 address the different effective dates of IFRS 9 Financial Instruments and the forthcoming new Insurance Contracts Standard.<br><br>The amendments introduce two options for entities that issue insurance contracts within the scope of IFRS 4:<br>(a) Overlay approach permitting insurers to reclassify from profit or loss to other comprehensive income an amount equal to the difference between the amount reported in profit or loss for designated financial assets applying IFRS 9 and the amount that would have been reported in profit or loss for those assets if the insurer had applied IAS 39; and<br>(b) Temporary exemption from IFRS 9 for insurers whose activities are predominantly connected with insurance.<br><br>The application of both approaches is optional and an entity is permitted at the beginning of any annual period to irrevocably stop applying them before the new insurance contracts standard is applied. | 1 January 2018<br>EU not yet endorsed |

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| IFRIC 22 Foreign Currency Transactions and Advance Consideration | Following IAS 21 The Effects of Changes in Foreign Exchange Rates, the interpretation addresses the accounting for foreign currency transactions when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognises the related asset, expense or income.<br><br>For the purposes of determining the exchange rate to use on initial recognition of the related asset, expense or income IFRIC 22 specifies the transaction date as the date of initial recognition of non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. | 1 January 2018<br>EU not yet endorsed |

### 3.4.3 Standards and interpretations not yet endorsed by the European Union

The European Commission decides on the applicability of IFRS issued by the IASB within the European Union by Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

As of the issuance date of these Consolidated Financial Statements, IFRS as adopted by the European Union does not differ from IFRS, except for provisions of IAS 39 prohibiting fair value hedge accounting applied to interest rate hedging on a portfolio basis for banking deposits which has not been approved by the European Union (i.e. in the European Union this hedging is permitted). Should the full version of IAS 39 requirements be applied, the impact would be insignificant, as the Group does not use interest rate hedging on a portfolio basis for banking deposits.

Those effective or issued standards and interpretations and/or amendments thereto not approved by the European Commission are highlighted in the previous section herein.

## 3.5 Principal accounting policies

### 3.5.1 Transactions in foreign currencies

#### *3.5.1.1 Functional and presentation currency*

The functional currency of the Group's entities operating in the Czech Republic (i.e. the currency of the primary economic environment in which the Group operates) is the Czech crown.

The Group has a branch in the Slovak Republic and a subsidiary, Bastion European Investments S.A., in Belgium. These both have the euro as their functional currency and are considered as foreign operations from a financial reporting point of view.

#### *3.5.1.2 Transactions and balances translation*

Transactions realised in foreign currency (i.e. in a currency other than the functional currency) are translated into the functional currency as of the date of initial recognition using the spot foreign exchange rate announced by the bank authority (hereafter only the "BA") for the respective foreign currency. Depending on the functional currency the BA means the Czech National Bank (hereafter only the "CNB") for the Czech crown and the European Central Bank for the euro.

At the end of the reporting period all balance sheet line items denominated in foreign currency are translated into the functional currency, depending on their nature, as follows:

I. Foreign currency monetary items are translated using the closing rate (foreign exchange rate announced by the BA at the end of the reporting period);
II. Non-monetary items that are measured at historical cost are translated using the BA's foreign exchange rate at the date of the transaction; and
III. Non-monetary items that are measured at fair value in a foreign currency are translated using the BA's foreign exchange rate at the date when the fair value was determined.

Gains and losses related to the translation of foreign currency items at the end of the reporting period as well as those related to their settlement are recognised as gains or losses of the period in which they occur and are presented in the line *'Net profit/(loss) on financial operations'*.

However, where a gain or loss from a fair value change in a non-monetary item denominated in foreign currency is recognised directly in Other Comprehensive Income, related foreign exchange rate differences are recognised in the same way. These non-monetary items include equity instruments. Also recognised in Other Comprehensive Income are foreign exchange rate differences related to the fair value revaluation of debt instruments classified as available-for-sale (excluding the effective portion of their fair value hedges and excluding foreign exchange rate differences related to changes in their amortised cost) and non-derivative financial liabilities (current accounts, deposits) used as hedging items for the cash flow hedge of foreign currency risk and the hedge of a net investment in a foreign operation.

For consolidation purposes the results and financial position of entities whose functional currency is different from the Group's presentation currency are translated into this currency using the following procedures:

I. Assets and liabilities are translated using the closing rate (exchange rate announced by the CNB at the end of the reporting period);
II. Income and expenses presenting profit or loss are translated using the average rate for the period (monthly average of exchange rates announced by the CNB during the period);
III. All resulting exchange differences are recognised in other comprehensive income and presented in the line *'Share premium and reserves'* being part of *'Capital funds and retained earnings'*.

### 3.5.2 Recognition of income and expenses

#### *3.5.2.1 Net interest income and similar income*

Interest income and expense related to interest-bearing instruments, except for instruments classified as financial assets or financial liabilities at fair value through profit or loss and interest hedging derivatives, are recognised on an accrual basis in the Statement of Income in the lines *'Interest income and similar income'* and *'Interest expense and similar expense'* using the effective interest rate (refer to 3.5.5.7 Effective interest rate method). Interest income and expense related to interest rate hedging derivatives are recognised in the lines described on an accrual basis using the contractual interest rate of the corresponding derivative. Late fee income is recognised at the date of its payment and presented in the line *'Interest income and similar income'*.

Dividend income is recognised when the Group's right to receive a dividend payment is established and is presented in the line *'Dividend income'*.

#### *3.5.2.2 Net fee and commission income*

The recognition of income from fees and commissions depends on the purpose for which a fee was assessed and the basis of accounting for any associated financial instrument. In accordance with the substance of fees and nature of services for which they are assessed, the Group distinguishes the following three categories of fees:

- Fees and commissions that comprise an integral component of the effective interest rate of a financial instrument are recognised in the line *'Interest income and similar income'*;
- Fees and commissions for services provided – income from these is recognised as revenue when services are provided and it is presented in the line *'Net fee and commission income'*;
- Fees and commissions for the execution of an act – income from these is recognised as revenue when the act has been completed and is also presented in the line *'Net fee and commission income'*.

#### *3.5.2.3 Net profit/(loss) on financial operations*

This line includes net profit/loss on financial operations, which means realised and unrealised gains/losses on securities held for trading; security derivatives; currency, interest rate and trading commodity derivatives; foreign exchange transactions; foreign assets and liabilities retranslation to the functional currency; and realised gains/losses on available-for-sale financial assets.

In this line there is also recognised interest income and expense related to interest-bearing instruments classified as financial assets or financial liabilities at fair value through profit or loss.

### 3.5.3 Cash and cash equivalents

Cash comprises cash on hand and cash in transit.

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment purposes. This item also includes obligatory minimum reserves. The Group can freely transact with the amount of these reserves under the assumption that average obligatory minimum reserves are maintained within the given maintenance period established by the CNB.

In preparing its Statement of Cash Flows for the period, the Group includes into cash and cash equivalents the cash and current balances with central banks at the beginning and end of the period and current amounts due from and to banks.

### 3.5.4 Fair value and hierarchy of fair value

Fair value is the price that would be received in selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability or, in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or most advantageous market must be accessible to the Group.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Group classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements of asset or liability measured at fair value. The hierarchy of fair values has the following three levels:

- *Level 1:* inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- *Level 2:* inputs are inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly; and
- *Level 3:* inputs are unobservable inputs for the asset or liability.

The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

The fair value is included in the hierarchy according to the lowest classified significant input used in its determination. Significant input information is that information which has a significant impact on the total fair value of the asset or liability.

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis (i.e. those for which measurement at fair value is required or permitted in the statement of financial position at the end of each reporting period), the Group determines whether transfers have occurred between levels in the hierarchy by re-assessing the categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the date of the event or change in circumstances that caused the transfer.

### 3.5.5 Financial instruments

#### *3.5.5.1 Dates of recognition and derecognition*

All regular way purchases or sales of financial assets are recognised using settlement date accounting. The settlement (collection) date is the day on which the financial instrument is delivered (cash payment).

When settlement date accounting is applied, the financial asset is recognised in the Statement of Financial Position on the day of receipt of a financial instrument (sending of cash) and derecognised on the day of its delivery (collection of cash).

For financial assets measured at fair value, however, an acquired financial asset is measured to reflect changes in its fair value from the purchase trade date to the purchase settlement date according to its categorisation into an individual portfolio (i.e. either in profit or loss or in other comprehensive income).

All purchases and sales of financial instruments that do not meet the "regular way" settlement criterion in the marketplace concerned are treated as financial derivatives. The Group recognises financial derivatives in the Statement of Financial Position at the trade date. Financial derivatives are derecognised at their maturity.

The Group recognises a financial liability in the Statement of Financial Position when it becomes a party to the contractual provisions of the instrument and it is removed from the Statement of Financial Position when it is extinguished (i.e. in circumstances where a contractually defined obligation is fulfilled, cancelled or expires).

### *3.5.5.2 Initial measurement of financial assets and financial liabilities*

When a financial asset or financial liability is initially recognised, the Group measures it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of that instrument.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price (i.e. the fair value of the consideration given or received).

The transaction costs include mainly fees and commissions paid to brokers, dealers and agents.

Also, financial guarantee contracts issued are initially recognised at fair value, being the premium received, in the Statement of Financial Position in the line ***'Accruals and other liabilities'***. The guarantees are subsequently measured as of the financial statements date at the higher of the amount initially recognised less, when appropriate, cumulative amortisation recognised in profit or loss (in the Statement of Financial Position in the line ***'Accruals and other liabilities'***), and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee (in the Statement of Financial Position in the line ***'Provisions'***). The premium received is recognised in the Statement of Income in the line ***'Net fee and commission income'*** on a straight-line basis over the life of the guarantee. The creation of provisions is recognised in the Statement of Income in the line ***'Allowances for loan losses'***.

### *3.5.5.3 "Day 1" profit or loss*

In determining whether fair value at initial recognition equals the transaction price, the Group takes into account factors specific to the transaction and to the asset or liability.

The Group trades no financial instruments on an inactive market. On active markets the Group trades financial instruments only for the quoted price in the active market. For this reason, there is no difference between the transaction price and the fair value of the financial asset or financial liability that is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique whose variables include only data from observable markets (a "Day 1" profit or loss).

### *3.5.5.4 Financial assets and liabilities classification and subsequent measurement*

Financial assets and liabilities held by the Group are classified upon initial recognition into appropriate portfolios of financial instruments in accordance with the characteristics of a given instrument, the Group's intention as of the acquisition date, and pursuant to the Group's financial instrument investment strategy as follows:

I. Financial assets and liabilities at fair value through profit or loss;
II. Held-to-maturity investments;
III. Loans and receivables;
IV. Available-for-sale financial assets; or
V. Financial liabilities at amortised cost.

The Group does not make use of an option to designate a financial asset or liability upon initial recognition as a financial instrument at fair value through profit or loss (the so-called "Fair Value Option").

*(i) Financial assets and liabilities at fair value through profit or loss*
The Group designates as financial assets at fair value through profit or loss securities held for trading and derivatives that are assets (i.e. financial instruments acquired by the Group for the purpose of generating a profit from short-term fluctuations in prices). These financial assets are recognised in the Statement of Financial Position in the line ***'Financial assets at fair value through profit or loss'***.

Securities designated as held for trading include equity and debt securities, treasury bills, bills of exchange and participation certificates. The trading derivative financial instruments used by the Group include currency and commodity forwards, currency and interest rate swaps, derivatives on securities and emission allowances and options.

Financial liabilities at fair value through profit or loss include liabilities from securities sold and trading derivatives that are liabilities and are recognised in the Statement of Financial Position in the line ***'Financial liabilities at fair value through profit or loss'***.

Unrealised gains and losses, as well as realised gains and losses arising from the fair value measurement of financial assets and liabilities, interest and dividends are recognised as income in the Statement of Income in the line ***'Net profit/(loss) on financial operations'***. These financial assets are not tested for impairment because the change of fair value is recognised directly in profit or loss.

*(ii) Held-to-maturity investments*
Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group has the positive intent and ability to hold to maturity and which do not meet the definition of loans and receivables (i.e. are quoted on an active market).

Held-to-maturity investments are subsequently measured at amortised cost using the effective interest rate method less any impairment loss through the use of an allowance account. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that is an integral components of the effective interest rate. The amortisation is included in ***'Interest income and similar income'*** in the Statement of Income. When an impairment of assets is identified, the Group recognises allowances in the Statement of Income in the line ***'Allowance for impairment of securities'***.

If the Group were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than due to an isolated event that is beyond the Group's control, which is non-recurring and could not reasonably have been anticipated by the Group due to a significant decrease of a client's credit worthiness, changes in tax laws, major business combination or major disposition (including sale of a segment), changes in legislative requirements, a significant increase in regulatory capital requirements or significant increase in risk weights for held-to-maturity investments to calculate the capital adequacy), the entire portfolio would have to be reclassified as ***'Available-for-sale financial assets'***. Furthermore, the Group would be prohibited from classifying any financial asset as ***'Held-to-maturity investments'*** for the following two years.

*(iii) Loans and receivables*
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than:
- Assets that the Group intends to sell immediately or in the near term, which are classified as held for trading, as well as those that the Group upon initial recognition designates as at fair value through profit or loss;
- Assets that the Group upon initial recognition designates as available-for-sale; or
- Assets for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration (e.g. asset-backed securities or a fixed rate interest-only strip created in a securitisation and subject to prepayment risk), which are classified as available-for-sale financial assets or as financial assets at fair value through profit or loss.

Loans and receivables are subsequently measured at amortised cost using the effective interest rate method less any impairment loss through the use of an allowance account. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are integral components of the effective interest rate. The amortisation is included in the line ***'Interest income and similar income'*** in the Statement of Income. When impairment of assets is identified, the Group recognises allowances in the Statement of Income in the line ***'Allowance for loan losses'***.

Financial assets designated as loans and receivables are reported in the Statement of Financial Position in the line ***'Amounts due from banks'*** or in the line ***'Loans and advances to customers'***, as appropriate for the type of debtor.

*(iv) Available-for-sale financial assets*
Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as financial assets at fair value through profit or loss, loans and receivables, or held-to-maturity investments. This portfolio comprises equity securities and debt securities, asset-backed securities and participation certificates.

Available-for-sale financial assets are subsequently measured at fair value and at the end of each reporting period tested to determine whether there is any objective evidence that a financial asset or group of financial assets is impaired. Unrealised gains or losses from the fair value measurement of these assets are recognised within Other Comprehensive Income in the line ***'Net value gain/(loss) on available-for-sale financial assets, net of tax'***) until their sale, maturity or impairment as well as fair value changes arising from changes in foreign exchange rates. Gains or losses from changes in foreign exchange rates on debt instruments are recognised in the Statement of Income in the line ***'Net profit/(loss) on financial operations'*** except for exchange gains or losses related to fair value revaluation that are recognised within Other Comprehensive Income. When the available-for-sale financial asset is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the Statement of Income in the line ***'Net profit/(loss) on financial operations'***.

Accrued interest income for debt securities is recognised in the Statement of Income line ***'Interest income and similar income'***. Dividend income arising from equity securities is recognised when the right for dividends is established and reported in the Statement of Income in the line ***'Dividend income'***.

*(v) Financial liabilities at amortised cost*
Financial liabilities at amortised cost include non-derivative financial liabilities with fixed or determinable payments and are recognised according to the type of counterparty in the lines ***'Amounts due to central banks', 'Amounts due to banks', 'Amounts due to customers', 'Securities issued'*** and ***'Subordinated debt'***.

Financial liabilities at amortised cost are subsequently measured at amortised cost using the effective interest rate method. Interest expense is recognised in the Statement of Income in the line ***'Interest expense and similar expense'***.

In the event of the repurchase of its own debt securities, the Group derecognises these securities (i.e. the item ***'Securities issued'*** is decreased). Gains and losses arising as a result of repurchasing the Group's own debt securities are recognised as of the date of their repurchase in the Statement of Income in the line ***'Net interest income'*** as an adjustment to the interest paid from its own bonds.

*3.5.5.5 Reclassification of financial assets*
The Group does not reclassify any financial assets after initial recognition into the ***'Financial assets at fair value through profit or loss*** portfolio. In rare circumstances, if non-derivative financial assets at fair value through profit or loss are no longer held for the purpose of selling or repurchasing in the short term, the financial assets may be reclassified out of the portfolio and be classified into the ***'Available-for-sale financial assets'***, or ***'Held-to-maturity investments'*** portfolio.

The Group may also reclassify a non-derivative trading asset out of the ***'Financial assets at fair value through profit or loss'*** portfolio and into the ***'Loans and receivables'*** portfolio if it meets the definition of loans and receivables and the Group has the intention and ability to hold the financial asset for the foreseeable future or until maturity. In certain rare circumstances, the Group may also reclassify financial assets out of the ***'Available-for-sale financial assets'*** portfolio and into the ***'Loans and receivables'*** portfolio if they meet the definition of loans and receivables and the Group has the intention and ability to hold the financial assets for the foreseeable future or until maturity. Fixed income securities quoted on an active market can be reclassified out of the ***'Available-for-sale financial assets'*** portfolio and into the ***'Held-to-maturity investments'*** portfolio if the Group's intention or ability to hold these securities has changed or upon expiry of the deadline during which securities were not permitted to be classified as securities held-to-maturity. Reclassifications are recorded at fair value at the date of reclassification, which becomes the new amortised cost.

The Group may reclassify financial assets or a significant amount out of the ***'Held-to-maturity investments'*** portfolio into the ***'Available-for-sale financial assets'*** portfolio or ***'Loans and receivables'*** portfolio, doing so without triggering the so called "tainting rules", in cases when the given assets are near to maturity, the Group has received almost the entire original principal of the given financial asset or there has occurred a unique and exceptional event that is outside of the Group's control and the Group could not have expected it. Such unique cases include in particular a significant decrease of a client's creditworthiness, changes in tax laws or in legal requirements, a business combination or the sale of a part of the business (segment), a significant increase in regulatory capital requirements or a significant increase in risk weights for held-to-maturity investments used in calculating the capital adequacy.

For a financial asset reclassified out of the ***'Available-for-sale financial assets'*** portfolio, any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the effective interest rate. Any difference between the new amortised cost and the expected cash flow is also amortised over the remaining life of the asset using the effective interest rate. If the asset is subsequently determined to be impaired, then the amount recorded in equity is recycled to profit or loss. Reclassification is at the election of management and is determined on an instrument-by-instrument basis.

### *3.5.5.6 Determination of a financial instrument's fair value and its hierarchy*

For the determination and categorisation of a financial instrument's fair value, the Group treats a security as quoted if quoted market prices are readily and regularly available from a stock exchange, dealers, securities traders, industrial groups, valuation services or regulatory authorities and if these prices represent current and regular market transactions under ordinary conditions.

If there are no quoted prices in an active market for the financial asset, the Group uses other values that are observable, directly or indirectly, from the markets for its measurement, such as:

I. Quoted prices for similar assets or liabilities in active markets;
II. Quoted prices for identical or similar assets or liabilities in markets that are not active (i.e. there are few recent transactions, prices quotations are not based on current information, etc.);
III. Inputs other than quoted prices (e.g. inputs based on interest rates, yield curves, implied volatilities, credit spreads, etc.); or
IV. Inputs derived principally from, or corroborated by, observable market data.

Where the inputs for the determination of a financial instrument's fair value are not observable in a market due to the fact that there is no or only minimal activity for that asset/liability, the Group uses for fair value measurement inputs that are available but not directly observable within a market and which in the Group's view reflect assumptions that market participants take into account when pricing the financial instrument.

The fair value of debt securities for which an observable market price is not available is estimated using an income approach (the present value technique taking into account the future cash flows that a market participant would expect to receive from holding the instrument as an asset) and the fair value of unquoted equity instruments is estimated using an income approach or market approach (using prices and other relevant information generated by a market). The fair values of financial derivatives are obtained from quoted market prices, discounted cash flow models or option pricing models and they are adjusted for the credit risk of the counterparty or the Group's own credit risk, as appropriate.

The existence of published price quotations in an active market is normally the best evidence of fair value. The appropriate quoted market price for an asset held or liability to be issued is usually the current bid price and for an asset to be acquired or liability held, the asking price.

The Group manages the group of financial assets and financial liabilities on the basis of the entity's net exposure to a particular market risk. It uses mid-market prices as the basis for establishing fair values for the offsetting risk positions and applies the bid or asking price to the net open position as appropriate.

When measuring the fair value of a financial asset or group of financial assets, the Group incorporates into the valuation an adjustment for the risk of default of the counterparty, a so-called credit valuation adjustment (CVA).

### *3.5.5.7 Effective interest rate method*

The effective interest rate is the rate which exactly discounts the estimated future cash payments or receipts through the expected life of a financial instrument.

When calculating the effective interest rate, the Group estimates cash flows considering all contractual terms of the financial instrument and includes any fees and incremental costs that are directly attributable to the instrument and constitute an integral component of the effective interest rate, but it does not take into consideration future credit losses.

The effective interest rate method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the relevant period.

### *3.5.5.8 Forborne loans*

Forborne exposures are debt contracts in respect of which forbearance measures have been granted to the debt or and for which the discontinuation conditions are not met. Forbearance measures consist of concessions to a debtor facing or about to face difficulties in meeting its financial commitments. The concession refers to either modification of terms and conditions (e.g. changes in payment schedule, interest rate reductions, penalty interest waivers) or refinancing. Once the terms have been renegotiated, any impairment is measured using the original effective interest rate as calculated before the modification of terms. Renegotiated loans are continuously reviewed by the Group to ensure that all criteria are met and that future payments are likely to occur. The renegotiated loans continue to be subject to impairment assessment, calculated based on their future cash flows discounted by the loans' original effective interest rates.

### *3.5.5.9 Impairment of financial assets*

At the end of each reporting period, the Group assesses on a regular basis whether there is any objective evidence that a financial asset or group of financial assets is impaired, the only exception being securities at fair value through profit or loss.

Objective evidence that a financial asset or group of assets is impaired includes observable evidence that comes to the attention of the Group and proving the significant deterioration of a debtor's (issuer's) financial health, breach of contract (default in interest or principal payment), high probability of bankruptcy or other financial reorganisation, or proving a measurable decrease in the estimated future cash flow due to adverse changes in industry conditions.

In addition to the aforementioned events, objective evidence of impairment for an investment in an equity instrument includes information about significant changes with an adverse effect that have taken place in the technological, economic or legal environment in which the issuer operates and significant or prolonged decline in the fair value of the instrument below its cost. The determination of what constitutes a significant or prolonged decline is a matter of circumstances that requires application of the Group management's judgement. As indicators of possible significant or prolonged decline, the Group regards unrealised loss in respect of instrument acquisition cost or the fact that the quoted price of the instrument has been below its carrying amount during every trading date for several months. Furthermore, the Group considers the business model and strategy related to the instrument and supportive indicators as the financial situation of the issuer and its development perspective or regulatory requirements.

If there is objective evidence that an impairment loss on a financial instrument has been incurred, the Group calculates an impairment loss and recognises it in the respective item in the Statement of Income.

For a financial asset classified in portfolios carried at amortised cost (i.e. ***'Held-to-maturity investments'*** and ***'Loans and receivables'*** portfolios), the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flow discounted at the financial asset's original effective interest rate. Estimations of future cash flows for loans are based on expected cash flows from the economic activities of the client and the possible realisation of loan collateral.

The Group uses one of the three methods to assess the amount of allowances (refer to Note 41(A)). For larger, individually significant loans classified as default (Substandard, Doubtful and Loss loans based on the Czech National Bank's classification) the allowances are assessed on an individual basis requiring management to monitor the borrower's repayment abilities individually, including the estimated value from the collateral foreclosure and expected duration of the recovery process etc. These allowances are calculated using discounted expected future cash flows.

For smaller, individually not significant impaired loans where the loans are homogeneous in nature (for example the consumer and mortgage loans to individuals and smaller corporate portfolios) the allowances are calculated by models using historical delinquency statistics.

Portfolio allowances are calculated for losses that have been incurred but have not been identified. Portfolio allowances are held against non-impaired loans across all segments and calculated using models based on probabilities of default and loss given default until the impairment event occurs and individual or model allowances for impaired loans are recognised.

Historical loss experience is adjusted on the basis of currently observable data to reflect new loss observations and to have better discrimination ability (i.e. to reflect the effects of current conditions on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently). The methodology and assumptions used for estimating the future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The carrying amount of an asset is reduced through the use of an allowance account, the creation of which is recognised in the Statement of Income in the line ***'Allowance for loan losses'*** or ***'Allowance for impairment of securities'***. If, in a subsequent period, the amount of the impairment loss decreases, the previously recognised impairment loss is correspondingly reversed.

When it can be reasonably anticipated that clients will be unable to fulfil their obligations to the Group in respect of such loans, loss loans are written off and recognised in the Statement of Income in the line ***'Allowance for loan losses'***. Subsequent recoveries are credited to the Statement of Income in ***'Allowance for loan losses'*** if previously written off. If the Group collects an amount greater than that written off subsequent to the write-off of the loan, the difference is reported through ***'Interest income and similar income'***.

For a ***'Available-for-sale financial assets'*** and in the case of objective evidence of their impairment, a cumulative loss that had been recognised in Other Comprehensive Income is reclassified to the Statement of Income and recognised in the line ***'Allowance for impairment of securities'*** for debt instruments and in the line ***'Net profit/(loss) on financial operations'*** for equity instruments. The amount of the loss is measured as the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that financial asset previously recognised in the Statement of Income. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the Statement of Income, the impairment loss is reversed, with the amount of the reversal recognised in the Statement of Income. The Group cannot reverse any impairment loss recognised in the Statement of Income for an equity instrument.

#### *3.5.5.10 Repurchase agreements*

The Group accounts for contracts to sell and buy back financial instruments (so-called "repos" or "reverse repos") based on their substance as the receiving or granting of a loan with a corresponding transfer of financial instruments as collateral.

Under repurchase transactions ("repos"), the Group only provides securities held in the portfolio of ***'Financial assets or financial liabilities at fair value through profit or loss'*** or in the ***'Available-for-sale financial assets'*** portfolio that are recorded in the Statement of Financial Position in the same lines. The corresponding liability arising from a loan received is recognised in the line ***'Amounts due to banks'*** or ***'Amounts due to customers'***, as appropriate.

Securities purchased under reverse repurchase agreements ("reverse repos") are recorded in the off-balance sheet, where they are remeasured at fair value. The corresponding receivable arising from the provided loan is recognised as an asset in the Statement of Financial Position according to the counterparty type in the line ***'Amounts due from banks'*** or ***'Loans and advances to customers'***.

The Group is allowed to provide securities received in reverse repo transactions as collateral or sell them even in the absence of default by their owner. These securities continue to be recorded in the off-balance sheet and measured at fair value. The corresponding liability arising from the loan received is included in ***'Amounts due to banks'*** or ***'Amounts due to customers'***, as appropriate. The Group has the obligation to return these securities to its counterparties.

The differences between the sale and repurchase prices in respect of repo and reverse repo transactions are treated by the Group as interest, and it is accrued evenly to expenses and income over the life of the repo agreement using the effective interest rate method.

In regard to the sale of a security acquired as collateral under a reverse repo transaction, the Group derecognises from the off-balance sheet evidence the security acquired under the reverse repo transaction and recognises in the Statement of Financial Position an amount payable from a short sale that is remeasured at its fair value. This payable is included in ***'Financial liabilities at fair value through profit or loss'***.

*3.5.5.11 Derivatives and hedge accounting*

A derivative is a financial instrument or other contract having all three of the following characteristics:

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other market variable;
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and
- It is settled at a future date.

At the inception of a financial derivative contract, the Group designates the derivative instrument as either held for trading or hedging.

Held for trading derivatives are classified into a portfolio of ***'Financial assets or financial liabilities at fair value through profit or loss'*** based on whether the fair value is positive or negative (refer to 3.5.5.4 Financial assets and liabilities classification and subsequent measurement).

Hedging derivatives are derivatives that the Group uses to hedge against interest rate and foreign exchange rate risks to which it is exposed as a result of its financial market transactions. The Group designates a derivative as hedging only if the criteria set out under IFRS are met at the designation date, i.e. if, and only if, all of the following conditions are met:

- There is compliance with the Group's risk management objective and strategy in undertaking the hedge;
- At inception of the hedge there is formal designation and documentation of the hedging relationship which includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk;
- The hedge is expected to be highly effective at inception and throughout the period;
- The effectiveness of the hedge can be reliably measured; and
- Changes in the fair value or cash flows of the hedged item are almost fully offset by changes in the fair value or cash flows of the hedging instrument and the results are within a range of 80% to 125%.

Hedging derivatives are accounted for according to the type of hedging relationship, which can be one of the following:

I. Hedging of an exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment, that is attributable to a particular risk and that could affect profit or loss (fair value hedge); or
II. Hedging of an exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction and that could affect profit or loss (cash flow hedge); or
III. Hedging of a net investment in a foreign operation.

Changes in the fair value of a derivative that is designated and qualified as a fair value hedge are recognised in the Statement of Income line ***'Net profit/(loss) on financial operations'***. Changes in the fair value of a hedged item are recognised in the Statement of Financial Position as a component of the carrying amount of the hedged item and in the Statement of Income line ***'Net profit/(loss) on financial operations'***.

It is on this basis that the Group hedges the interest rate risk and foreign currency risk of financial assets (loans with fixed interest rates and debt instruments classified as available-for-sale) and interest rate risk of deposits, repos, mortgage bonds issued, as well asselected portfolios of building savings. The effectiveness of a hedge is regularly tested through prospective and retrospective tests on a quarterly basis.

If the hedge no longer meets the criteria for hedge accounting or the hedging instrument expires or is sold, terminated or exercised, the entity revokes the designation and an adjustment to the carrying amount of the hedged interest-bearing financial instrument is amortised to profit or loss over the period until the maturity of the hedged item.

In connection with the reclassification of certain debt securities from the ***'Available-for-sale financial assets'*** portfolio and into the ***'Held-to-maturity investments'*** portfolio, the Group revoked the designation of respective interest rate swaps as fair value hedges and prospectively classifies them as a cash flow hedge of interest rate risk associated with selected portfolios of assets or liabilities.

Changes in the fair value of hedging derivatives classified as cash flow hedges and that prove to be highly effective in relation to the hedged risks are recognised in the line ***'Cash flow hedging'*** in Other Comprehensive Income and they are transferred to the Statement of Income and classified as income or expense in the periods during which the hedged items affect the Statement of Income. The ineffective portion of a hedge is charged directly to the Statement of Income in the line ***'Net profit/(loss) on financial operations'***.

It is on this basis that the Group hedges the interest rate risk and currency risk associated with selected portfolios of assets or liabilities or individually significant assets or liabilities. The effectiveness of a hedge is regularly tested through prospective and retrospective tests on a quarterly basis.

If the hedge no longer meets the criteria for hedge accounting, the hedging instrument expires or is sold, terminated or exercised, the entity revokes the designation and the cumulative gain or loss on the hedging instrument that has been recognised in Other Comprehensive Income for the period when the hedge was effective remains in equity until the forecast transaction occurs.

If the forecast transaction is no longer expected to occur, the gain or loss accumulated as other comprehensive income is reclassified to profit or loss.

The Group additionally hedges against the foreign exchange rate risk arising from the net investment in the subsidiary Bastion European Investments S.A. Foreign currency deposits are used as a hedging instrument. Foreign exchange rate differences arising from its retranslation are included in Other Comprehensive Income.

Financial derivatives constituting economic hedges under the Group's risk management positions but not qualifying for hedge accounting under the specific rules of IAS 39 are treated as derivatives held for trading.

The fair values of derivative instruments held for trading and hedging purposes are disclosed in Note 42(C).

#### *3.5.5.12 Embedded derivatives*

In some cases, a derivative, such as an option for an earlier redemption of a bond, is a component of a hybrid (combined) financial instrument that also includes a non-derivative host contract. The embedded derivative is separated and accounted for as a derivative if, and only if, all of the following conditions are met:

- The embedded derivative as a separate instrument meets the definition of a derivative;
- The economic characteristics and risks of the embedded derivative are not closely related to those of the host contract; and
- The host contract is not measured at fair value with fair value changes recognised in the Statement of Income.

### 3.5.6 Assets held for sale

The line ***'Assets held for sale'*** represents assets for which the Group expects that their carrying amounts will be recovered principally through sale transactions rather than through continuing use. These assets are available for immediate sale in their present condition, they are actively marketed for sale at a price that is reasonable in relation to their current fair value, and their sale is highly probable, that is to say that a plan to sell and leading to the location of a buyer has been initiated. The Group expects that the sale of assets will be completed, the market situation permitting, within one year from the date of the asset's classification as ***'Assets held for sale'***.

Assets held for sale are measured at the lower of:

- The carrying amount of the respective asset at the date of its classification as ***'Assets held for sale'***; or
- Fair value less estimated costs to sell (e.g. cost of expert valuation reports, legal or financial advisory services, the estimates of which are based on historical experience, as well as real estate transfer tax for real estate).

Assets designated as ***'Assets held for sale'*** are no longer depreciated.

The Group recognises an impairment loss on assets held for sale in the line ***'Depreciation, amortisation, impairment and disposal of assets'*** if their selling price less estimated costs to sell is lower than their carrying value. Any subsequent increase in the selling price less costs to sell is recognised as a gain but not in excess of the cumulative impairment loss that has been recognised either during the time when the assets were classified as held for sale or before their reclassification into the line ***'Assets held for sale'*** (i.e. during the period when the asset had been held for supplying the Group's services or for administrative purposes).

## 3.5.7 Income tax

### *3.5.7.1 Current income tax*

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those valid as of the Statement of Financial Position date.

Current income tax is recognised in the Statement of Income, or, as the case may be, in the Statement of Other Comprehensive Income if it relates to an item directly taken into other comprehensive income.

The Group does not set off current tax assets and current tax liabilities unless it has a legally enforceable right to set off the recognised amounts and intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

### *3.5.7.2 Deferred income tax*

Using the balance sheet liability method, deferred income tax is recorded for temporary differences arising between the tax bases of assets and liabilities and their carrying values presented in the Statement of Financial Position. Deferred income tax is determined using tax rates valid or substantially enacted for the periods in which the Group expects to realise the deferred tax asset or to settle the deferred tax liability. A deferred tax asset is recognised to the extent that it is probable that future taxable profit will be available against which the tax asset can be used.

Deferred income tax is recognised in the Statement of Income, or, as the case may be, in the Statement of Other Comprehensive Income if it relates to an item directly taken into other comprehensive income (such as deferred income tax related to changes in the fair value of available-for-sale financial assets or in relation to a cash flow hedge).

The Group offsets deferred income tax assets and deferred income tax liabilities only if it has a legally enforceable right to set off current tax assets against current tax liabilities and deferred tax assets and deferred tax liabilities relate to income tax levied by the same taxation authority and relate to the same taxable entity.

The largest temporary differences relate to tangible and intangible assets, loans and receivables, hedging derivatives, available-for-sale financial assets and retirement benefits.

## 3.5.8 Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Group as lessor

***Operating leases***

The Group presents assets that are the subject of an operating lease in the appropriate lines within the Statement of Financial Position according to the nature of those assets and uses for them accounting policies applied to the relevant asset class.

Leasing payments received from operating leases are recognised as the Group's income on a straight-line basis over the term of the relevant lease and is presented in the line ***'Other income'***.

*Finance leases*
When assets held are subject to a finance lease, the net investment in the lease is recognised as ***'Loans and advances to customers'*** while the assets themselves are not recognised. The difference between the gross receivable and the present value of the receivable is recognised as deferred interest income.

Lease income is recognised over the term of the lease, reflecting a constant periodic rate of interest on the remaining balance of the receivable, and is presented in the line ***'Interest income and similar income'***.

The Group as lessee
*Operating leases*
Lease payments under an operating lease are recognised on a straight-line basis over the lease term and are presented in the line ***'Generaland administrative expenses'***. Possible penalty payments due to the early termination of a lease are recognised in the reporting period in which the lease was terminated.

*Finance leases*
At the commencement of a lease term, an asset held under a finance lease is recognised in the appropriate line within the Statement of Financial Position in accordance with the nature of the asset and simultaneously a liability is recognised in an amount equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments. Subsequently, the Group uses the same accounting policies for these assets as for its own property presented in the same line as the leased asset. If the legal ownership of the asset held under finance lease is not transferred to the lessee by the end of the lease term, however, the asset is depreciated on a straight-line basis over the lease term.

The Group divides lease payments between amortisation recognised as the reduction of the outstanding liability and a finance charge recognised in the Statement of Income as ***'Interest expense and similar expense'***. The finance charge is allocated so as to produce a constant periodic rate of interest on the remaining balance of the liability during the entire lease period.

### 3.5.9 Tangible and intangible assets (except goodwill)
Intangible assets include principally software and internally generated intangible assets (mainly software). Tangible assets include plant, property and equipment that are used by the Group in supplying its services and for administrative purposes and that are used for longer than one reporting period.

Tangible and intangible assets are measured at the historical acquisition cost less accumulated impairment losses (allowances) and, in the case of depreciated assets less accumulated depreciation and increased by technical improvements. The historical acquisition cost comprises the purchase price and any costs directly attributable to asset acquisition such as delivery and handling costs, installation and assembly costs, advisory fees, and administrative charges. The acquisition cost of internally generated intangible assets comprises external expenses and internal personnel expenses related to an internal project's development phase. The Group capitalises no expenses related to the research phase.

Tangible and intangible assets are depreciated from their acquisition costs on a straight-line basis over their useful lives. Cars under finance leases are depreciated from acquisition cost less estimated residual value, which is determined on the basis of the purchase price following expiration of the lease as established in the lease contract. The Group assumes no residual value for other assets. Depreciation and amortisation are reported in the Statement of Income on the line ***'Depreciation, amortisation, impairment and disposal of assets'***.

The Group does not depreciate land and works of art, Tangible and intangible assets in the course of construction and technical improvements are depreciated only once they have been brought into a condition fit for use.

*During the reporting period, the Group used the following useful lives in years:*

| | 2016 | 2015 |
|---|---|---|
| Machinery and equipment | 4 | 4 |
| Information technology – notebooks, servers | 4 | 4 |
| Information technology – desktop computers | 6 | 6 |
| Fixtures, fittings and equipment | 6 | 6 |
| Vehicles | 5 | 5 |
| ATMs | 10 | 10 |
| Selected equipment of the Group | 8 | 8 |
| Energy machinery and equipment | 12/15 | 12/15 |
| Distribution equipment | 20 | 20 |
| Buildings and structures | 40 | 40 |
| Buildings and structures – selected components: | | |
| – Heating, air-conditioning, windows, doors | 20 | 20 |
| – Lifts, electrical installations | 25 | 25 |
| – Facades | 30 | 30 |
| – Roofs | 20 | 20 |
| – Residual value of buildings and technical improvements without selected components | 50 | 50 |
| Technical improvements on leasehold assets | According to the lease term | According to the lease term |
| Intangible results of development activities (assets generated internally as component of internal projects) | According to the useful life, typically 5 | According to the useful life, typically 5 |
| Licences – software | 5 | 5 |
| Other rights of use | According to contract | According to contract |

At the end of each reporting period, the Group assesses whether there exists any indication that a tangible or intangible asset can be impaired. Indicators of possible impairment include information about a significant decline in an asset's market value, significant changes within the technological, market, economical or legal environment, obsolescence or physical damage to an asset, or change in the manner in which the asset is used. Where any such indicator exists, the Group estimates the recoverable amount of the asset concerned (i.e. the higher amount of its fair value less costs to sell in comparison with the asset's carrying value). If the asset's carrying amount is greater than its recoverable amount, the Group reduces its carrying amount to its recoverable amount and presents the recognised impairment loss in the line ***'Depreciation, amortisation, impairment and disposal of assets'***.

Repairs and maintenance are charged directly to the Statement of Income when they occur.

### 3.5.10 Goodwill

Recognised goodwill arises on the acquisition of a subsidiary. For subsidiaries acquired until 2010, it represents the excess of the acquisition cost (including acquisition-related costs) for the interest acquired by the Group over the net fair value of the acquired assets, liabilities and contingent liabilities at the acquisition date. For subsidiaries acquired from 2010, it represents the difference between the fair value of the transferred consideration and the amount of any non-controlling interest measured at the present proportionate share in the recognised amounts of the subsidiary's identifiable net assets at fair value on one side and the net of the identifiable assets and the liabilities assumed both at fair value on the other side. Acquisition-related costs are recognised in profit or loss.

Goodwill is initially recognised at the cost of acquisition and subsequently at cost net of possible impairment losses. Once recognised, impairment losses on goodwill are not reversed.

The Group tests goodwill for impairment on an annual basis as of 30 September or more frequently if there is indication that the goodwill may be impaired. If the recoverable amount of the tested cash-generating unit (typically the acquired enterprise taken as a whole) is lower than its carrying value, the Group recognises an impairment of the cash-generating unit which is primarily allocated against the goodwill and subsequently against the value of other assets (against other impaired assets and/or on a pro-rata basis).

For the purpose of calculating the recoverable amount, the Group calculates value in use as the present value of the future cash flow to be generated by a cash-generating unit from its continuing use in the business. The Group estimates future cash flow on the basis of 3-year financial plan for the cash-generating unit that is approved by management. Cash flows represent income after tax of cash-generating units available for distribution to owners. The discount rate used is the cost of capital calculated using the capital asset pricing model. This method is based on a risk-free interest rate grossed up by a risk premium determined according to the underlying activities of the cash-generating unit. Inasmuch as all respective subsidiaries are located in the Czech Republic and their functional currency is the Czech crown, no other premium is added. For the period beyond the medium-term financial plan the projected cash flows are calculated in perpetuity based on constant cash flows being the net operating income after taxes and including a steady growth rate derived as an average from the 3-year financial plan. Key assumptions used in the preparation of the financial plan are consistent with market estimations (GDP, interest rate, inflation) and with past experience.

Upon the sale of a subsidiary, the appropriate goodwill balance is reflected in the profit or loss on the sale.

Most acquisitions give rise to positive goodwill. However, occasionally the net of the identifiable assets acquired and the liabilities assumed both at fair value may exceed the aggregate of the fair value of the transferred consideration and the amount of any non-controlling interest measured at the present proportionate share in the recognised amounts of the subsidiary identifiable net assets at fair value. The amount is than referred to as gain on bargain purchase (negative goodwill) and the resulting gain is recognised in profit or loss at the acquisition date. Prior to recognising the gain, however, the Group reassess whether it has correctly identified all of the assets acquired and liabilities assumed and reviews the procedures used for their measurement and the measurement of non-controlling interest in the acquiree and the consideration transferred.

### 3.5.11 Provisions

Provisions are recognised when and only when:

- The Group has a present obligation (legal or constructive) as a result of a past event;
- It is probable that settlement of the obligation will cause an outflow of resources causing a decrease of economic benefits; and
- A reliable estimate can be made of the amount of the obligation. Provisions for legal disputes are estimated on the basis of the amount sought by the plaintiff, including accrued interest and fees.

Provisions are measured at the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditure expected to be required to settle the obligation. The discount rate is a pre-tax rate reflecting current market assessments and the risks specific to the liability. Provision increases related to the passage of time are recognised as interest expense.

Among others, the Group recognises provisions for credit-related commitments which do not meet the criteria for recognition in the Statement of Financial Position. These provisions cover estimated losses from credit-related commitments into which the Group enters in the normal course of its business and that are recorded in the off-balance sheet. These commitments include primarily guarantees, avals, uncovered letters of credit, irrevocable commitments to extend credit, undrawn loan commitments, and approved overdraft loans. Provisions for credit-related commitments are created on the same basis as are allowances for loan portfolios (refer to Note 33).

### 3.5.12 Employee benefits

#### *3.5.12.1 General*

The Group provides its employees with retirement benefits and disability benefits. The employees are entitled to receive retirement or disability benefits if they are employed by the Group until their retirement age or if they are entitled to receive a disability pension but only if they were employed within the Group for a minimum defined period.

Estimated benefit costs are recognised on an accruals basis through a provision over the employment term using an accounting methodology that is similar to the methodology used in respect of defined benefit pension plans. In determining the parameters of the model, the Group refers to the most recent employee data (the length of employment with the Group, age, gender, average salary) and estimates made on the basis of monitored historical data about the Group's employees (expected reduction of the current staffing levels) and other estimates (the amounts of bonuses, anticipated increase in salaries, estimated amounts of social security and health insurance contributions, discount rate).

These provisions are presented in the line ***'Provisions'***. The changes in provisions are disaggregated into three components that are presented as follows:

I. Service cost (i.e. additional liability that arises from employees providing service during the period) is presented in the line ***'Personnel expenses'***;
II. The interest expense on the net benefit liability is presented in the line ***'Personnel expenses'*** and
III. Other changes in the value of the defined benefit obligation, such as changes in estimates, are presented within Other Comprehensive Income in the line ***'Remeasurement of retirement benefits plan, net of tax'***.

The use of a provision is presented in the line ***'Personnel expenses'***.

The Group additionally provides short-term benefits to its employees, such as contributions to retirement pension insurance and capital life insurance schemes. The Group recognises the costs of these contributions as incurred in the line ***'Personnel expenses'*** (refer to Note 9).

The Group has the following share plans and deferred compensation schemes:

### *3.5.12.2 Deferred bonus payments*

In accordance with European regulation (Capital Requirements Directive III; No. 2010/76/EU) the Group implemented a new compensation scheme for employees whose professional activities have a material impact on the Group's risk profile. For employees identified in accordance with the CRD III regulation, the performance-linked remuneration is split into two components: (i) a non-deferred component which is paid in the following year, and (ii) a deferred component which is spread over three years. The amounts of the two components are further split between bonuses paid in cash and bonuses paid in cash equivalent of the Société Générale S.A. share price or in cash equivalent of the Komerční banka, a.s. share price (indexed bonuses). Both bonuses are subject to presence and performance conditions:

- In the case of bonuses paid in the cash equivalent of the Société Générale S.A. share price, the performance condition is based on the profitability of the Société Générale Group;
- In the case of bonuses paid in cash and bonuses paid in cash equivalent of the Komerční banka, a.s. share price, the performance condition is based on the profitability of the Komerční banka Group. Moreover, for investment banking employees there is the condition that the Group's net investment banking operating income be higher than zero.

Indexed bonuses qualify as cash-settled share-based transactions. The liability is measured at the end of each reporting period until settled at the fair value of the shares of Société Générale S.A. or Komerční banka, a.s multiplied by numbers of shares granted and it is spread over the vesting period.

The amount of bonuses finally vested is calculated as the number of Société Générale S.A. shares or Komerční banka, a.s shares multiplied by their price fixed as the volume-weighted average of the last 20 closing trading prices prior to the first business day following the end of the applicable retention period.

Deferred cash bonuses (i.e. bonuses paid to employees more than 12 months after the end of the reporting period in which the employees render the related services) are considered as long-term employee benefits and the related expense is recognised over the vesting period in the line 'Personnel expenses'.

### *3.5.12.3 Free share plan*

In November 2010, the Group awarded all its employees rights to 40 free shares of Société Générale S.A. upon the achievement of two performance conditions and completing a specific period of employment.

The allotment of the shares proceeded in two tranches:

- The first tranche accounted for 40% of the planned allocation (i.e. 16 shares) and it was contingent on the Société Générale S.A. Group's achieving a positive net income in 2012 (the initial criterion of at least 10% return of equity, net of tax was changed by decision of the Société Générale Board of Directors based on agreement of the General Shareholders' Meeting held on 22 May 2012). The Group's employees received those shares on 31 March 2015;
- The second tranche accounted for 60% of the planned allocation (i.e. 24 shares) and it was contingent on customer satisfaction increasing between 2010 and 2013 in the Société Générale S.A. Group's three core businesses (French Networks, International Retail Banking, Corporate and Investment Banking). This condition having been met the Group's employees received those shares on 31 March 2016.

The second and final tranche having been allocated this free share plan was completed in 2016.

To enhance loyalty and motivation to contribute to the long-term growth in the value of the Société Générale Group, the Group can award some of its key employees further free shares (deferred share plan). These free shares are subject to a vesting condition (i.e. presence in the Group at the end of vesting period which is 4 years) and for certain beneficiaries are also subject to the condition that the Société Générale Group records positive net income.

Expenses related to the free share and deferred share plans provided by Société Générale to the Group´s employees are recognised in the Group´s financial statements as equity-settled share-based payment transactions. The fair value of these instruments, measured using the arbitrage model at the grant date, is spread over the vesting period and recorded in the lines ***'Personnel expenses'*** and ***'Share premium and reserves'*** under equity. At the end of each accounting period, the number of these instruments is adjusted in order to take into account performance and service conditions and adjust the overall cost of the plan as originally determined. Expenses recognised under ***'Personnel expenses'*** from the start of the plan are then adjusted accordingly.

### 3.5.13 Share capital

*Dividends on ordinary shares*
Dividends on ordinary shares are recognised as a liability and deducted from equity at the time they are approved by the Group's shareholders.

*Treasury shares*
When the Group acquires its own equity instruments, the consideration paid, and including any attributable transaction costs, is recognised as a deduction from the line ***'Share premium and reserves'*** under equity. Gains and losses on sales of treasury shares are recognised in equity and presented as well in the line ***'Share premium and reserves'***.

### 3.5.14 Contingent assets, contingent liabilities and off-balance sheet items

In addition to transactions giving rise to the recognition of assets and liabilities in the Statement of Financial Position, the Group enters into transactions through which it generates contingent assets and liabilities. The Group maintains contingent assets and liabilities as off-balance sheet items. The Group monitors these transactions inasmuch as they represent a substantial proportion of its activities and materially impact the level of risks to which the Group is exposed (they may increase or decrease other risks, for instance, by hedging assets and liabilities reported in the Statement of Financial Position).

A contingent asset/liability is defined as a possible asset/liability that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly under the Group's control.

A contingent liability also exists in the case of a present obligation where an outflow of resources embodying economic benefits probably will not be required to settle the obligation or the amount of the obligation cannot be measured reliably. Contingent liabilities include, for example, irrevocable loan commitments, commitments arising from bank guarantees, bank acceptances, letters of credit and warrants.

In addition to contingent assets and contingent liabilities, the off-balance sheet includes assets arising from valuables and securities custody and fiduciary activities and related obligations to return these to customers (e.g. Assets under Management).

Off-balance sheet items include also nominal values of such interest and foreign currency instruments as forwards, swaps, options and futures. More information regarding derivative operations is presented in note 3.5.5.11 Derivatives and hedge accounting.

### 3.5.15 Operating segments

Operating segments are reported in accordance with internal reports regularly prepared and presented to the Bank's Board of Directors, which is considered the "chief operating decision maker" (i.e. a person or group of persons that allocates resources and assesses the performance of individual operating segments of the Group).

The Group has the following operating segments:

- ***Retail Banking:*** includes the provision of products and services to individuals (i.e. predominantly current and savings accounts, term deposits, building savings, pension insurance, overdrafts, credit card loans, personal loans and mortgages);
- ***Corporate Banking:*** includes the provision of products and services to corporate entities (i.e. current accounts, term deposits, revolving loans, business loans, mortgages, leasing, foreign currency and derivative products, syndicated and export financing, and guarantee transactions);
- ***Investment Banking:*** involves trading in financial instruments; and
- ***Other:*** consists of the head office of the Bank.

The Investment Banking segment does not reach quantitative limits for obligatory reporting. The management of the Group nevertheless believes that the information concerning this segment is useful for users of the Financial Statements and thus reports this segment separately.

As the principal activity of the Group is the provision of financial services, the Board of Directors of the Bank assesses the performance of operating segments predominantly according to net interest income. For this reason, interest income and interest expense of individual operating segments are not reported separately but on a net basis.

In addition, the Group monitors net fee and commission income, net profit/(loss) on financial operations, and other income predominantly including income from the lease of non-residential premises by segments. Other profit and loss items are not monitored by operating segments.

The Group does not monitor total assets or total liabilities by segment.

The information on the items of net operating income is provided to the Board of Directors of the Bank using valuations identical to those stated in the Group's financial accounting records.

The Group has no client or group of related parties for which the income from transactions would account for more than 10% of the Group's total income.

### 3.5.16 Regulatory requirements

The Group is subject to the regulatory requirements of the CNB and other institutions. These regulations include limits and other restrictions pertaining to minimum capital adequacy requirements, classification of loans and off-balance sheet commitments, and creation of allowances to cover credit risk associated with the Group's clients, as well as with its liquidity, interest rate and foreign currency positions.

## 3.6 Changes in accounting policies and reclassifications

From 1 January 2016, the following changes were made in reporting of several items for better presentation of their nature, and to conform with the recommendations of the European Banking Authority and the Group's principales. Comparative information has been restated to reflect the presentation of the current period. The reconciliation of the lines is shown in the tables below.

*Reconciliation of lines in the Statement of Income for the year ended 31 December:*

| | As reported | Restated | |
|---|---|---|---|
| **(CZKm)** | **2015** | **2015** | **Reference** |
| Interest expense and similar expense | (8,168) | (7,267) | 1 |
| Net fee and commission income | 6,956 | 6,968 | 2 |
| General and administrative expenses | (4,406) | (5,319) | 1, 2 |

1. Contribution to the Deposit Insurance Fund in the amount of CZK 901 million was reclassified from the line ***'Interest expense and similar expense'*** to the line ***'General and administrative expenses'***.

2. Contribution to the Investor Compensation Fund in the amount of CZK 12 million was reclassified from the line ***'Net fee and commission income'*** to the line ***'General and administrative expenses'***.

*Reconciliation of lines in the Statement of Financial Position as of 31 December:*

| | As reported | Restated | As reported | Restated | |
|---|---|---|---|---|---|
| **(CZKm)** | **31 Dec 2015** | **31 Dec 2015** | **31 Dec 2014** | **31 Dec 2014** | **Reference** |
| Amounts due to customers | 666,407 | 656,287 | 701,867 | 689,204 | 1 |
| Securities issued | 11,283 | 21,403 | 22,584 | 35,247 | 1 |

1. Depository bills of exchange in the amount of CZK 10,120 million (2014: 12,663 million) were reclassified from the line ***'Amounts due to customers'*** to the line ***'Securities issued'***.

*Reconciliation of lines in the Statement of Cash Flow for the year ended 31 December:*

| | As reported | Restated | |
|---|---|---|---|
| **(CZKm)** | **2015** | **2015** | **Reference** |
| Interest paid | (7,092) | (6,191) | 1 |
| Fee and commission paid | (1,721) | (1,709) | 2 |
| Cash payments to employees and suppliers, and other payments | (10,576) | (11,489) | 1, 2 |
| Amounts due to customers | 4,312 | 6,855 | 3 |
| Securities redeemed | (13,958) | (16,501) | 3 |

1. Contribution to the Deposit Insurance Fund in the amount of CZK 901 million was reclassified from the the line 'Interest paid' to the line ***'Cash payments to employees and suppliers, and other payments'***.

2. Contribution to the Investor Compensation Fund in the amount of CZK 12 million was reclassified from the the line ***'Fee and commission paid'*** to the line ***'Cash payments to employees and suppliers, and other payments'***.

3. The cash operations from Depository bills in the amount 2,543 million was reclassified from the line ***'Amounts received from customers'*** to the line ***'Securities redeemed'***.

## 4 Segment reporting

| | Retail banking | | Corporate banking | | Investment banking | | Other | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|
| **(CZKm)** | **2016** | **2015** | **2016** | **2015** | **2016** | **2015** | **2016** | **2015** | **2016** | **2015** |
| Net interest income and similar income | 12,363 | 12,256 | 7,084 | 7,258 | 85 | 120 | 1,535 | 1,723 | 21,067 | 21,357 |
| Net fee and commission income | 4,418 | 4,619 | 2,062 | 2,125 | (40) | (29) | 243 | 253 | 6,683 | 6,968 |
| Net profit/(loss) on financial operations | 912 | 876 | 1,437 | 1,311 | 456 | 432 | 1,032 | (9) | 3,837 | 2,610 |
| Other income | 75 | 64 | 7 | 1 | 116 | 110 | (35) | (66) | 163 | 109 |
| **Net operating income** | **17,768** | **17,815** | **10,590** | **10,695** | **617** | **633** | **2,775** | **1,901** | **31,750** | **31,044** |

Given the specifics of banking activities, the Board of Directors of the Bank (the chief operating decision maker) is provided with information on income, recognition of allowances, write-offs and income tax only for selected segments, rather than consistently for all segments. For this reason, this information is not reported for segments.

As most of the income of segments arises from interest and, in assessing the performance of segments and deciding on allocation of resources for segments, the Board of Directors primarily refers to net interest income, the interest for segments is reported on a net basis, i.e. reduced by interest expense.

Transfer prices between operating segments are based on transfer interest rates representing actual market interest rate conditions, including a liquidity component reflecting the existing opportunities to acquire and invest financial resources.

The Group's income is primarily - more than 99% (2015: more than 98%) - generated on the territory of the Czech Republic.

## 5 Net interest income and similar income

*Net interest income and similar income comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Interest income and similar income | 26,757 | 28,622 |
| Interest expense and similar expense | (5,692) | (7,267) |
| Dividend income | 2 | 2 |
| **Net interest income and similar income** | **21,067** | **21,357** |
| Of which net interest income and similar income from | | |
| – Loans and advances | 16,702 | 17,072 |
| – Held-to-maturity investments | 1,767 | 2,000 |
| – Available-for-sale financial assets | 700 | 1,036 |
| – Financial liabilities at amortised cost | (1,921) | (2,775) |
| – Hedging financial derivatives | 3,817 | 4,022 |
| – Dividends | 2 | 2 |
| **Total** | **21,067** | **21,357** |

*'Interest income and similar income'* includes interest on Substandard, Doubtful and Loss loans due from customers of CZK 398 million (2015: CZK 433 million).

*'Interest income and similar income'* also includes accrued interest income from hedging financial derivatives of CZK 7,589 million (2015: CZK 8,497 million) and *'Interest expense and similar expense'* includes interest expenses from hedging financial derivatives of CZK 3,772 million (2015: CZK 4,475 million). Net interest income from these derivatives amounts to CZK 3,817 million (2015: CZK 4,022 million). Hedging financial derivatives are used to hedge both the fair value and future cash flows.

In 2016, the Group recorded as part of *'Net interest income and similar income'* also negative interest income and expense from selected client's deposits in selected currencies, from selected repo transactions, loro and nostro accounts, and margin accounts deposited at banks. The total amount recognised is not material.

## 6 Net fee and commission income

*Net fee and commission income comprises the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Deposit product fee and commission income | 909 | 1,050 |
| Loan fee and commission income | 1,277 | 1,302 |
| Transaction fee and commission income | 3,450 | 3,936 |
| Cross-selling fee income | 1,246 | 1,203 |
| Specialised financial services fee and commission income | 895 | 935 |
| Other fee and commission income | 137 | 126 |
| **Total fee and commission income** | **7,914** | **8,552** |
| Deposit product fee and commission expense | (153) | (146) |
| Loan fee and commission expense | (244) | (196) |
| Transaction fee and commission expense | (573) | (963) |
| Cross-selling fee expense | (90) | (92) |
| Specialised financial services fee and commission expense | (103) | (94) |
| Other fee and commission expense | (68) | (93) |
| **Total fee and commission expenses** | **(1,231)** | **(1,584)** |
| **Total net fee and commission income** | **6,683** | **6,968** |

*'Net fee and commission income'* comprises fee income arising from trust and other fiduciary activities in the amount of CZK 567 million (2015: CZK 496 million) and fee expense for these services in the amount of CZK 67 million (2015: CZK 13 million).

## 7 Net profit/(loss) on financial operations

*Net profit/(loss) on financial operations comprises the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Net realised gains/(losses) on securities held for trading | (282) | 335 |
| Net unrealised gains/(losses) on securities held for trading | (336) | 166 |
| Net realised gains/(losses) on securities available-for-sale | 959 | 0 |
| Net realised and unrealised gains/(losses) on security derivatives | 780 | (343) |
| Net realised and unrealised gains/(losses) on interest rate derivatives | 330 | 159 |
| Net realised and unrealised gains/(losses) on trading commodity derivatives | 23 | 32 |
| Net realised and unrealised gains/(losses) on foreign exchange operations | 1,161 | 1,109 |
| Net realised gains/(losses) on foreign exchange from payments | 1,202 | 1,152 |
| **Total net profit/(loss) on financial operations** | **3,837** | **2,610** |

* This line also includes impacts of derivative trades in emission allowances.

For the year ended 31 December 2016, the line ***'Net realised gains/(losses) on securities available-for-sale'*** includes the net gain from the sale of an equity stake in Visa Europe Limited in the amount of CZK 959 million (refer to Note 18).

A loss of CZK 227 million (2015: gain of CZK 492 million) on the fair value of interest rate swaps for interest rate risk hedging is included in ***'Net realised and unrealised gains/(losses) on interest rate derivatives'***. This amount matches the loss arising from retranslation of hedged loan receivables, available-for-sale financial assets, deposits or repos and issued mortgage bonds reported in the same line.

## 8 Other income

The Group reports ***'Other income'*** in the amount of CZK 163 million (2015: CZK 109 million). In both 2016 and 2015, ***'Other income'*** was predominantly composed of income from services provided to the Société Générale Group entities as well as property rental income.

## 9 Personnel expenses

*Personnel expenses comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Wages, salaries and bonuses | 5,027 | 4,850 |
| Social costs | 2,002 | 1,943 |
| **Total personnel expenses** | **7,029** | **6,793** |
| Physical number of employees at the end of the period* | 8,615 | 8,575 |
| Average recalculated number of employees during the period* | 8,476 | 8,426 |
| **Average cost per employee (CZK)** | **829,283** | **806,195** |

* Calculation according to Czech Statistical Office methodology.

***'Social costs'*** include costs of CZK 89 million (2015: CZK 89 million) paid by the Group to the employees' retirement pension insurance scheme and costs of CZK 44 million (2015: CZK 44 million) incurred in contributing to the employees' capital life insurance scheme.

*Indexed bonuses*

In 2016, the total amount relating to bonuses indexed on the Komerční banka share price recognised in *'Personnel expenses'* was CZK 45 million (2015: CZK: 32 million) and the total amount of CZK 55 million (2015: CZK 49 million) was recognised as a liability. These amounts do not include the costs of social and health insurance and retirement pension insurance paid by the Group. Net loss from hedging indexed bonuses by fair value hedge and cash flow hedge derivatives was CZK 7 million (2015: net gain of CZK 11 million). The total number of Société Générale shares according to which bonuses indexed on the Société Générale share price are calculated is 0 shares (2015: 6,232 shares). The total number of Komerční banka shares according to which bonuses indexed on the Komerční banka share price are calculated is 18,570 shares (2015: 16,572 shares).

*The changes in the numbers of shares were as follows:*

| | 2016 | | 2015 | |
|---|---|---|---|---|
| **(in shares)** | **SG shares** | **KB shares** | **SG shares** | **KB shares** |
| **Balance as of 1 January** | **0** | **16,572** | **6,232** | **17,310** |
| Paid out during the period | 0 | (8,690) | (6,232) | (5,840) |
| Presumed number of newly guaranteed shares | 0 | 10,688 | 0 | 5,102 |
| **Balance as of 31 December** | **0** | **18,570** | **0** | **16,572** |

*Free shares and deferred share plans*

For 2016, the total amount relating to the free shares programme and deferred share plans recognised in *'Personnel expenses'* is CZK 24 million (2015: CZK 64 million).

*The changes in the numbers of shares were as follows:*

| | 2016 | | 2015 | |
|---|---|---|---|---|
| **(in shares; EUR)** | **Number of shares** | **Average price** | **Number of shares** | **Average price** |
| **Balance as of 1 January** | **353,142** | **35.10** | **475,568** | **35.17** |
| Granted during the year | 52,647 | 29.55 | 44,798 | 33.02 |
| Forfeited during the year | (19,162) | 37.19 | (11,121) | 35.04 |
| Exercised during the year | (242,546) | 34.09 | (156,103) | 34.47 |
| **Balance as of 31 December** | **144,081** | **31.58** | **353,142** | **35.10** |

## 10 General and administrative expenses

*General and administrative expenses comprise the following:*

| **(CZKm)** | **2016** | **2015** |
|---|---|---|
| Insurance | 76 | 89 |
| Marketing and representation | 641 | 608 |
| Sale and banking products expenses | 297 | 311 |
| Other employees expenses and travelling | 142 | 140 |
| Real estate expenses | 1,036 | 1,050 |
| IT support | 1,094 | 1,051 |
| Equipment and supplies | 143 | 143 |
| Telecommunications, postage and data transfer | 258 | 281 |
| External consultancy and other services | 563 | 583 |
| Resolutions and similar funds | 880 | 913 |
| Other expenses | 124 | 150 |
| **Total general and administrative expenses** | **5,254** | **5,319** |

## 11 Depreciation, amortisation, impairment and disposal of assets

*Depreciation, amortisation, impairment and disposal of assets comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Tangible and intangible assets depreciation and amortisation (refer to Notes 25 and 26) | 1,757 | 1,796 |
| Impairment and disposal of fixed assets | (14) | 444 |
| **Total depreciation, amortisation, impairment and disposal of assets** | **1,743** | **2,240** |

The net gain of *'Impairment and disposal of fixed assets'* in the total amount of CZK 14 million (2015: net loss of CZK 444 million) include the impairment loss/reversal on assets held for sale.

## 12 Cost of risk

### Allowance for loan losses and provisions for other credit commitments

*'Allowances for loan losses'* in the total amount of CZK 1,843 million (2015: CZK 1,306 million) include a net loss from allowances and provisions for loan losses in the amount of CZK 2,192 million (2015: CZK 1,712 million) and a net gain from loans written off and transferred in the amount of CZK 349 million (2015: CZK 420 million).

*The balances and movements of allowances and provisions for loans as of 31 December 2016 were as follow:*

| (CZKm) | As of 1 Jan 2016 | Effect of acquisition of companies | Charge | Release | Write off and transfer | Foreign exchange | As of 31 Dec 2016 |
|---|---|---|---|---|---|---|---|
| Portfolio allowances for loans to banks (refer to Note 20) | (18) | 0 | (26) | 24 | 0 | 0 | (20) |
| Specific allowances for loans to banks (refer to Note 20) | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Portfolio allowances for loans to customers (refer to Note 21) | (1,200) | (6) | (649) | 550 | 0 | 0 | (1,305) |
| – Individuals | (472) | (6) | (221) | 166 | 0 | 0 | (533) |
| – Corporates* | (728) | 0 | (428) | 384 | 0 | 0 | (772) |
| Specific allowances for loans to customers (refer to Note 21) | (14,618) | (101) | (8,681) | 7,054 | 2,081 | (2) | (14,267) |
| – Individuals | (7,190) | (49) | (1,506) | 1,603 | 783 | 0 | (6,359) |
| – Corporates* | (7,428) | (52) | (7,175) | 5,451 | 1,298 | (2) | (7,908) |
| Specific allowances for other amounts due from customers (refer to Note 21) | (16) | 0 | (1) | 1 | 5 | 0 | (11) |
| Provisions for guarantees and other credit-related commitments (refer to Note 32) | (783) | 0 | (1,484) | 1,026 | 0 | 0 | (1,241) |
| – Individuals | (13) | 0 | (27) | 30 | 0 | 0 | (10) |
| – Corporates* | (770) | 0 | (1,457) | 996 | 0 | 0 | (1,231) |
| Specific allowances for other assets (refer to Note 23) | (251) | 0 | (15) | 9 | 14 | 0 | (243) |
| **Total** | **(16,886)** | **(107)** | **(10,856)** | **8,664** | **2,100** | **(2)** | **(17,087)** |

* This item also includes allowances and provisions for loans granted to individual entrepreneurs.

*The balances and movements of allowances and provisions for loans as of 31 December 2015 were as follow:*

| (CZKm) | As of 1 Jan 2015 | Deconsolidation of Transformed fund | Charge | Release | Write off and transfer | Foreign exchange | As of 31 Dec 2015 |
|---|---|---|---|---|---|---|---|
| Portfolio allowances for loans to banks (refer to Note 20) | 0 | 0 | (19) | 1 | 0 | 0 | (18) |
| Specific allowances for loans to banks (refer to Note 20) | 0 | 0 | 0 | 0 | 0 | 0 | 0 |
| Portfolio allowances for loans to customers (refer to Note 21) | (971) | 0 | (931) | 701 | 0 | 1 | (1,200) |
| – Individuals | (225) | 0 | (497) | 250 | 0 | 0 | (472) |
| – Corporates* | (746) | 0 | (434) | 451 | 0 | 1 | (728) |
| Specific allowances for loans to customers (refer to Note 21) | (17,863) | 0 | (7,137) | 5,758 | 4,739 | (115) | (14,618) |
| – Individuals | (6,873) | 0 | (3,200) | 2,421 | 463 | 0 | (7,190) |
| – Corporates* | (10,989) | 0 | (3,937) | 3,337 | 4,276 | (115) | (7,428) |
| Specific allowances for other amounts due from customers (refer to Note 21) | (16) | 0 | (5) | 5 | 0 | 0 | (16) |
| Provisions for guarantees and other credit-related commitments (refer to Note 32) | (702) | 0 | (940) | 855 | 0 | 4 | (783) |
| – Individuals | (11) | 0 | (36) | 34 | 0 | 0 | (13) |
| – Corporates* | (691) | 0 | (904) | 821 | 0 | 4 | (770) |
| Specific allowances for other assets (refer to Note 23) | (255) | 14 | (20) | 5 | 5 | 0 | (251) |
| **Total** | **(19,807)** | **14** | **(9,052)** | **7,325** | **4,744** | **(110)** | **(16,886)** |

* This item also includes allowances and provisions for loans granted to individual entrepreneurs.

### Provisions for other risk expenses

The net gain of ***'Provisions for other risk expenses'*** of CZK 25 million (2015: CZK 231 million) consists mainly of the charge for provisions of CZK 9 million (2015: CZK 14 million) and the release and use of provisions of CZK 37 million (2015: CZK 287 million) for legal disputes, together with the net costs incurred by the Group as a result of the outcome of legal disputes of CZK 3 million (2015: CZK 42 million).

Additional information on the provisions for other risk expenses is provided in Note 33.

## 13 Income tax

*The major components of corporate income tax expense are as follow:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Tax payable – current year, reported in profit or loss | (2,918) | (2,535) |
| Tax paid – prior year | 20 | 16 |
| Deferred tax (refer to Note 34) | 99 | (96) |
| Hedge of a deferred tax asset against foreign currency risk | 0 | (23) |
| **Total income tax** | **(2,799)** | **(2,638)** |

*The items explaining the difference between the Group's theoretical and effective tax rates are as follow:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| **Profit before income tax** | **16,873** | **15,770** |
| Theoretical tax calculated at a tax rate of 19% (2015: 19%) | 3,206 | 2,996 |
| Tax on pre-tax profit adjustments | 113 | 23 |
| Non-taxable income | (1,754) | (1,934) |
| Expenses not deductible for tax purposes | 1,491 | 1,540 |
| Use of tax losses carried forward | (44) | (34) |
| Tax allowance | (2) | (2) |
| Tax credit | 0 | 0 |
| Hedge of a deferred tax asset against foreign currency risk | 0 | 23 |
| Movement in deferred tax | (99) | 96 |
| Tax losses | 0 | 0 |
| Other | (23) | 0 |
| Impact of various tax rates of subsidiary undertakings | (30) | (25) |
| Tax effect of share of profits of associated undertakings | (39) | (29) |
| **Income tax expense** | **2,819** | **2,654** |
| Prior period tax expense | (20) | (16) |
| **Total income tax** | **2,799** | **2,638** |
| Effective tax rate | 16.59% | 16.73% |

Non-taxable income primarily includes dividends, tax-exempt interest income and the release of tax non-deductible allowances and provisions. Expenses not deductible for tax purposes include primarily the recognition of tax non-deductible allowances and provisions and tax non-deductible operating expenses. Tax on pre-tax profit adjustments primarily represents an adjustment of the IFRS result to the Czech Accounting Standards (CAS).

The corporate tax rate for the year ended 31 December 2016 is 19% (2015: 19%). The Group's tax liability is calculated based upon the accounting profit while taking into account tax non-deductible expenses and tax-exempt income or income subject to a final withholding tax rate.

As of 31 December 2016, the Group records unused tax losses in the amount of CZK 304 million (2015: CZK 636 million).

*These tax losses can be used in the following time horizon:*

| (CZKm) | 1 year | 2 years | 3 years | 4 years | 5 years |
|---|---|---|---|---|---|
| In the amount of | 304 | | | | |

Further information about deferred tax is presented in Note 34.

## 14 Distribution of net profit

For the year ended 31 December 2016, the Group generated a net profit of CZK 14,074 million (2015: CZK 13,132 million). Distribution of profits for the year ended 31 December 2016 will be approved by the general meetings of the Group companies.

The Bank's Board of Directors will propose to the Supervisory Board a dividend payment in the amount of CZK 40 per share (2015: CZK 62 per share, which equals the amount of CZK 310 per share before shares were split), which represents a total of CZK 7,602 million (2015: CZK 11,783 million). The proposal is subject to the Supervisory Board's approval and subsequently to the approval of the General Shareholders' Meeting.

In accordance with a resolution of the General Shareholders' Meeting held on 22 April 2016, the aggregate balance of the net profit of CZK 13,132 million for the year ended 31 December 2015 was allocated as follows: CZK 11,783 million was paid out in dividends and the remaining balance of the net profit was allocated to retained earnings. The dividends were paid out in Czech crowns.

Moreover, the Group paid out dividends to non-controlling owners in the total amount of CZK 375 million (2015: CZK 238 million), of which CZK 375 million (2015: CZK 238 million) was paid to the non-controlling owners of ESSOX s.r.o.

## 15 Earnings per share

Earnings per share of CZK 72.48 (2015: CZK 67.55 per share) have been calculated by dividing the net profit attributable to the Group's equity holders of CZK 13,688 million (2015: CZK 12,758 million) by the number of shares in issue, that is, 190,049,260, decreased by the average number of treasury shares held by the Group during the period, which was 1,193,360 (2015: 1,193,360 shares).

## 16 Cash and current balances with central banks

*Cash and current balances with central banks comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Cash and cash values | 8,996 | 11,357 |
| Current balances with central banks | 103,245 | 116,979 |
| **Total cash and current balances with central banks** (refer to Note 36) | **112,241** | **128,336** |

Obligatory minimum reserves in the amount of CZK 94,340 million (2015: CZK 89,701 million) are included in ***'Current balances with central banks'*** and they bear interest. As of 31 December 2016, the interest rate was 0.05% (2015: 0.05%) in the Czech Republic and 0.00% (2015: 0.05%) in the Slovak Republic.

## 17 Financial assets at fair value through profit or loss

As of 31 December 2016 and 2015, the ***'Financial assets at fair value through profit or loss'*** portfolio includes only securities and positive fair values of derivative financial instruments held for trading. Upon initial recognition, the Group has not designated any financial assets as ***'Financial assets at fair value through profit or loss'***.

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Securities | 11,445 | 10,672 |
| Derivative financial instruments | 18,264 | 18,526 |
| **Total financial assets at fair value through profit or loss** | **29,709** | **29,198** |

For detailed information on derivative financial instruments included in the held for trading portfolio, refer to Note 42(C).

*Trading securities comprise the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Fair value | Cost* | Fair value | Cost* |
| **Emission allowances** | **1,839** | **1,766** | **2,800** | **2,379** |
| Fixed income debt securities | 6,594 | 6,477 | 4,509 | 4,390 |
| Variable yield debt securities | 2,140 | 2,127 | 1,026 | 1,022 |
| Bills of exchange | 872 | 871 | 186 | 185 |
| Treasury bills | 0 | 0 | 2,151 | 2,150 |
| **Total debt securities** | **9,606** | **9,475** | **7,872** | **7,747** |
| **Total trading securities** | **11,445** | **11,241** | **10,672** | **10,126** |

* Acquisition cost for shares, participation certificates and emission allowances; amortised acquisition cost excluding coupon for debt securities.

The Group's portfolio of trading securities includes treasury bills issued by the Czech Ministry of Finance at fair value of CZK 0 million (2015: CZK 2,151 million).

As of 31 December 2016, the portfolio of trading securities includes securities at fair value of CZK 10,516 million (2015: CZK 8,213 million) that are publicly traded on stock exchanges and securities at fair value of CZK 929 million (2015: CZK 2,459 million) that are not publicly traded on stock exchanges (they are traded on the interbank market).

*Emission allowances at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Emission allowances** | | |
| – Other currencies | 1,839 | 2,800 |
| **Total emission allowances** | **1,839** | **2,800** |

*Emission allowances at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Emission allowances issued by:** | | |
| – Foreign financial institutions | 1,839 | 2,800 |
| **Total emission allowances** | **1,839** | **2,800** |

*Debt trading securities at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Variable yield debt securities** | | |
| – Czech crowns | 2,140 | 640 |
| – Other currencies | 0 | 386 |
| **Total variable yield debt securities** | **2,140** | **1,026** |
| **Fixed income debt securities (including bills of exchange and treasury bills)** | | |
| – Czech crowns | 6,636 | 4,909 |
| – Other currencies | 830 | 1,937 |
| **Total fixed income debt securities** | **7,466** | **6,846** |
| **Total trading debt securities** | **9,606** | **7,872** |

*Debt trading securities at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Debt trading securities issued by:** | | |
| – State institutions in the Czech Republic | 8,857 | 5,628 |
| – Foreign state institutions | 658 | 2,044 |
| – Financial institutions in the Czech Republic | 59 | 146 |
| – Foreign financial institutions | 15 | 0 |
| – Other entities in the Czech Republic | 17 | 54 |
| **Total trading debt securities** | **9,606** | **7,872** |

*Bonds issued by Foreign state institutions designated as financial assets at fair value through profit or loss:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Country of issuer** | **Fair value** | **Fair value** |
| European Investment Bank | 62 | 52 |
| Poland | 0 | 1 |
| Slovakia | 596 | 1,991 |
| **Total** | **658** | **2,044** |

Of the debt securities issued by State institutions in the Czech Republic, CZK 7,807 million (2015: CZK 3,106 million) consist of securities eligible for refinancing with the CNB.

## 18 Available-for-sale financial assets

*Available-for-sale financial assets comprise the following:*

| (CZKm) | 31 Dec 2016 Fair value | 31 Dec 2016 Cost* | 31 Dec 2015 Fair value | 31 Dec 2015 Cost* |
|---|---|---|---|---|
| **Shares and participation certificates** | **182** | **177** | **675** | **1** |
| Fixed income debt securities | 25,577 | 22,721 | 27,095 | 23,984 |
| Variable yield debt securities | 13,661 | 13,224 | 14,094 | 13,563 |
| **Total debt securities** | **39,238** | **35,945** | **41,189** | **37,547** |
| **Total available-for-sale financial assets** | **39,420** | **36,122** | **41,864** | **37,548** |

* Acquisition cost for shares and participation certificates; amortised acquisition cost excluding coupon for debt securities.

As of 31 December 2016, the *'Available-for-sale financial assets'* portfolio includes securities at fair value of CZK 39,238 million (2015: CZK 40,225 million) that are publicly traded on stock exchanges and securities at fair value of CZK 182 million (2015: CZK 1,639 million) that are not publicly traded.

As of 31 December 2016, the *'Available-for-sale financial assets'* portfolio includes bonds at fair value of CZK 1,348 million (2015: CZK 0 million) that are used as collateral for intraday facilities in central banks.

In 2016, the Group sold a stake in Visa Europe Limited, the net gain from the sale for the Group amounted to CZK 959 million (refer to Note 7).

*Shares and participation certificates available-for-sale at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Shares and participation certificates** | | |
| – Other currencies | 182 | 675 |
| **Total shares and participation certificates available-for-sale** | **182** | **675** |

*Shares and participation certificates available-for-sale at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Shares and participation certificates available-for-sale issued by:** | | |
| – Other foreign entities | 182 | 675 |
| **Total shares and participation certificates available-for-sale** | **182** | **675** |

*Debt securities available-for-sale at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Fixed income debt securities** | | |
| – Czech crowns | 18,773 | 20,337 |
| – Other currencies | 6,804 | 6,758 |
| **Total fixed income debt securities** | **25,577** | **27,095** |
| **Variable yield debt securities** | | |
| – Czech crowns | 10,951 | 11,375 |
| – Other currencies | 2,710 | 2,719 |
| **Total variable yield debt securities** | **13,661** | **14,094** |
| **Total debt securities available-for-sale** | **39,238** | **41,189** |

*Debt securities available-for-sale at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Debt securities available-for-sale issued by:** | | |
| – State institutions in the Czech Republic | 20,222 | 20,376 |
| – Foreign state institutions | 7,935 | 7,919 |
| – Financial institutions in the Czech Republic | 10,259 | 12,062 |
| – Foreign financial institutions | 822 | 832 |
| – Other entities in the Czech Republic | 0 | 0 |
| – Other foreign entities | 0 | 0 |
| **Total debt securities available-for-sale** | **39,238** | **41,189** |

*Debt securities available-for-sale issued by Foreign state institutions comprise the following:*

| (CZKm) | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| Country of issuer | Fair value | Cost* | Fair value | Cost* |
| Poland | 788 | 676 | 786 | 676 |
| Romania | 1,900 | 1,833 | 1,904 | 1,889 |
| Slovakia | 4,117 | 3,327 | 4,067 | 3,338 |
| European Investment Bank | 1,130 | 1,000 | 1,162 | 1,000 |
| **Total** | **7,935** | **6,836** | **7,919** | **6,903** |

* Acquisition cost for shares and participation certificates amortised acquisition cost excluding coupon for debt securities.

Of the debt securities issued by State institutions in the Czech Republic, CZK 20,222 million (2015: CZK 20,375 million) consist of securities eligible for refinancing with the CNB.

**Reclassification of certain debt securities held in the portfolio of Available-for-sale financial assets**

During the first quarter of 2014, the Group reviewed the accounting recognition of certain debt securities issued by State institutions held in the portfolio of *'Available-for-sale financial assets'* (hereafter only "AFS") on the basis of the Group's changing its intention for their classification. The Group concluded that all regulatory and accounting requirements, as well as internal limits, were satisfied for recognition of the debt securities in the nominal value of CZK 56,596 million in the portfolio of *'Held-to-maturity investments'* (hereafter only "HTM") and decided to reclassify the respective securities from AFS to HTM. The securities were reclassified at fair value. The corresponding unrealised gains and losses in equity of CZK 5,011 million as of the reclassification date are retained in Other Comprehensive Income. Such amounts are amortised over the remaining life of the security (refer to Note 41).

## 19 Assets held for sale

As of 31 December 2016, the Group reported assets held for sale at a carrying amount of CZK 906 million (2015: CZK 385 million) mainly comprising buildings and land owned by the Group which the management of the Group decided to sell as a component of a plan to optimise the distribution network and equipment obtained by taking possession of leasing collateral. Depreciation of these assets has been discontinued since their classification as assets held for sale. As of 31 December 2016, the Group recognised allowances against assets held for sale of CZK 402 million (2015: CZK 418 million).

As of 31 December 2016, *'Assets held for sale'* also includes investments in associates classified as assets held for sale at a carrying amount of CZK 8 million (2015: CZK 0 million), refer to Note 24.

# 20 Amounts due from banks

*Balances due from banks comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Current accounts with other banks (refer to Note 36) | 1,043 | 536 |
| Debt securities | 8,049 | 8,255 |
| Loans and advances to banks | 13,077 | 12,278 |
| Advances due from central bank (reverse repo transactions) | 8,100 | 9,900 |
| Term placements with other banks | 21,522 | 16,848 |
| **Total amounts due from banks, gross** | **51,791** | **47,817** |
| Portfolio allowances for loans to banks (refer to Note 12) | (20) | (3) |
| Specific allowances for loans to banks (refer to Note 12) | 0 | (15) |
| **Total allowances for loans to banks** | **(20)** | **(18)** |
| **Total amounts due from banks, net** | **51,771** | **47,799** |

*Advances due from the CNB and other banks under reverse repurchase transactions are collateralised by treasury bills issued by the CNB and other debt securities, the fair values of which are as follow:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Treasury bills | 8,004 | 9,726 |
| Debt securities issued by state institutions | 167 | 426 |
| Shares | 0 | 607 |
| Investment certificates | 0 | 83 |
| **Total** | **8,171** | **10,842** |

### Securities acquired as loans and receivables

As of 31 December 2016, the Group maintains in its portfolio bonds at an amortised cost of CZK 8,049 million (2015: CZK 8,255 million) and a nominal value of CZK 7,901 million (2015: CZK 7,997 million), of which bonds with a nominal value 2,099 million (2015: CZK 2,099 million) and EUR 79 million (2015: EUR 79 million) are issued by Financial institutions in the Czech Republic and CZK 705 million (2015: CZK 705 million) are by Foreign financial institutions.

# 21 Loans and advances to customers

*Loans and advances to customers comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Loans to customers | 591,146 | 544,009 |
| Bills of exchange | 243 | 302 |
| Forfaits | 815 | 272 |
| **Total loans and advances to customers excluding debt securities and other amounts due to customers, gross** | **592,204** | **544,583** |
| Debt securities | 3,193 | 3,654 |
| Other amounts due from customers | 384 | 214 |
| **Total loans and advances to customers, gross** | **595,781** | **548,451** |
| Portfolio allowances for loans to customers (refer to Note 12) | | |
| – Individuals | (532) | (342) |
| – Corporates* | (773) | (275) |
| Specific allowances for loans to customers (refer to Note 12) | | |
| – Individuals | (6,368) | (7,320) |
| – Corporates* | (7,899) | (7,881) |
| **Total allowances for loans to customers** (refer to Note 12) | **(15,572)** | **(15,818)** |
| Specific allowances for other amounts due from customers (refer to Note 12) | (11) | (16) |
| **Total allowances for loans and other amounts due from customers** | **(15,583)** | **(15,834)** |
| **Total loans and advances to customers, net** | **580,198** | **532,617** |

* This item also includes allowances for loans granted to individual entrepreneurs.

As of 31 December 2016, loans and advances to customers include accrued interest of CZK 1,175 million (2015: CZK 1,248 million), of which CZK 495 million (2015: CZK 576 million) relates to interest from overdue receivables.

As of 31 December 2016, loans provided to customers under reverse repurchase transactions in the amount of CZK 6 million (2015: CZK 819 million) are collateralised by securities with a fair value of CZK 4 million (2015: CZK 1,177 million).

*As of 31 December 2016, the loan portfolio of the Group (excluding Debt securities and Other amounts due from customers) is comprised of the following, as broken down by classification:*

| (CZKm) | Gross receivable | Collateral applied | Net exposure | Allowances | Carrying value |
|---|---|---|---|---|---|
| Standard | 560,453 | 258,770 | 301,683 | (697)* | 559,756 |
| Watch | 9,346 | 3,961 | 5,385 | (608)* | 8,738 |
| Substandard | 5,895 | 3,050 | 2,845 | (2,167) | 3,728 |
| Doubtful | 2,088 | 961 | 1,127 | (727) | 1,361 |
| Loss | 14,422 | 1,505 | 12,917 | (11,373) | 3,049 |
| **Total** | **592,204** | **268,247** | **323,957** | **(15,572)** | **576,632** |

* This item includes portfolio allowances (due to losses incurred but not reported).

*As of 31 December 2015, the loan portfolio of the Group (excluding Debt securities and Other amounts due from customers) was comprised of the following, as broken down by classification:*

| (CZKm) | Gross receivable | Collateral applied | Net exposure | Allowances | Carrying value |
|---|---|---|---|---|---|
| Standard | 512,644 | 237,901 | 274,743 | (617)* | 512,027 |
| Watch | 8,742 | 3,367 | 5,375 | (583)* | 8,159 |
| Substandard | 7,172 | 3,550 | 3,622 | (2,577) | 4,595 |
| Doubtful | 2,029 | 1,246 | 783 | (654) | 1,375 |
| Loss | 13,996 | 1,082 | 12,914 | (11,387) | 2,609 |
| **Total** | **544,583** | **247,146** | **297,437** | **(15,818)** | **528,765** |

* This item includes portfolio allowances (due to losses incurred but not reported).

*Set out below is a breakdown of loans by sector (excluding Debt securities and Other amounts due from customers):*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Food industry and agriculture | 17,083 | 16,903 |
| Mining and extraction | 4,543 | 5,948 |
| Chemical and pharmaceutical industry | 6,700 | 6,114 |
| Metallurgy | 10,219 | 10,764 |
| Automotive industry | 11,950 | 10,526 |
| Manufacturing of other machinery | 9,565 | 8,958 |
| Manufacturing of electrical and electronic equipment | 4,392 | 3,575 |
| Other processing industry | 11,510 | 8,240 |
| Power plants, gas plants and waterworks | 19,706 | 17,319 |
| Construction industry | 10,868 | 10,498 |
| Retail | 15,901 | 14,134 |
| Wholesale | 29,350 | 28,092 |
| Accommodation and catering | 1,564 | 1,451 |
| Transportation, telecommunication and warehouses | 23,045 | 24,764 |
| Banking and insurance industry | 24,841 | 19,963 |
| Real estate | 51,307 | 43,070 |
| Public administration | 27,931 | 32,235 |
| Other industries | 33,726 | 31,605 |
| Individuals | 278,003 | 250,424 |
| **Total loans to customers** | **592,204** | **544,583** |

The majority of loans - more than 90% (2015: more than 90%) - were provided to entities on the territory of the Czech Republic.

*Set out below is an analysis of the types of collateral held in support of loans and advances to customers as stated in the Consolidated Statement of Financial Position:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| (CZKm) | Total client loan collateral* | Discounted client loan collateral value** | Applied client loan collateral value*** | Total client loan collateral* | Discounted client loan collateral value** | Applied client loan collateral value*** |
| Guarantees of state and governmental institutions | 3,097 | 2,328 | 2,325 | 2,613 | 2,262 | 2,254 |
| Bank guarantee | 14,961 | 14,183 | 14,086 | 14,635 | 13,925 | 13,540 |
| Guaranteed deposits | 8,505 | 8,384 | 7,710 | 9,064 | 8,956 | 7,811 |
| Pledge of real estate | 449,258 | 292,686 | 215,319 | 407,379 | 262,467 | 192,656 |
| Pledge of movable assets | 13,053 | 2,082 | 1,279 | 12,971 | 1,263 | 1,214 |
| Guarantee by legal entity | 30,114 | 19,895 | 13,808 | 32,665 | 20,907 | 14,256 |
| Guarantee by individual (natural person) | 2,821 | 275 | 260 | 3,357 | 354 | 329 |
| Pledge of receivables | 29,046 | 1,578 | 15 | 42,657 | 626 | 0 |
| Insurance of credit risk | 11,628 | 11,054 | 11,045 | 13,955 | 13,258 | 13,128 |
| Other | 3,977 | 3,263 | 2,400 | 2,979 | 2,199 | 1,958 |
| **Nominal value of collateral** | **566,460** | **355,728** | **268,247** | **542,275** | **326,217** | **247,146** |

* The nominal value of the collateral is determined based on internal rules of the Group (e.g. internal property valuation, the current value of collateral, the market value of securities, etc.).
** The nominal value of the collateral is reduced by a coefficient taking into account the time value of money, the cost of selling the collateral, the risk of declining market prices, the risk of insolvency, etc.
*** The applied collateral value is the discounted collateral value reduced to the actual balance of the collateralised exposure.

Pledges on industrial real estate represent 10% of total pledges on real estate (2015: 10%).

### Debt securities designated as loans and receivables

As of 31 December 2016, the Group holds in its portfolio bonds at an amortised cost of CZK 2,759 million (2015: CZK 2,749 million) and a nominal value of CZK 2,697 million (2015: CZK 2,687 million), of which bonds with a nominal value of CZK 450 million (2015: CZK 450 million) are issued by State institutions in the Czech Republic, CZK 1,744 million (2015: CZK 1,790 million) by Other entities in the Czech Republic and EUR 16 million (2015: EUR 17 million) and CZK 68 (2015: CZK 0 million) by Other foreign entities. Additionally, the Group holds in this portfolio bills of exchange at an amortised cost of CZK 388 million (2015: CZK 878 million) and a nominal value of CZK 389 million (2015: CZK 880 million), of which bills of exchange in the nominal value of CZK 210 million (2015: CZK 80 million) are issued by State institutions in the Czech Republic and CZK 179 million (2015: CZK 800 million) by Other entities in the Czech Republic. The portfolio is hedged using fair value hedge derivatives with a positive fair value of CZK 46 million (2015: CZK 27 million).

### Forborne loans and advances to customers

*Forborne loans and advances to customers as of 31 December 2016*

| (CZKm) | Neither past due nor impaired | Past due not impaired | Impaired | Total forborne | Allowances | Collateral applied |
|---|---|---|---|---|---|---|
| Individuals | 1,211 | 221 | 1,608 | 3,040 | 705 | 2,107 |
| Corporates* | 447 | 14 | 2,519 | 2,980 | 1,392 | 1,151 |
| **Total** | **1,658** | **235** | **4,127** | **6,020** | **2,097** | **3,258** |

* This item also includes loans granted to individual entrepreneurs.

*Forborne loans and advances to customers as of 31 December 2015*

| (CZKm) | Neither past due nor impaired | Past due not impaired | Impaired | Total forborne | Allowances | Collateral applied |
|---|---|---|---|---|---|---|
| Individuals | 741 | 84 | 1,509 | 2,334 | 482 | 1,752 |
| Corporates* | 226 | 27 | 2,237 | 2,490 | 1,378 | 776 |
| **Total** | **967** | **111** | **3,746** | **4,824** | **1,860** | **2,528** |

* This item also includes loans granted to individual entrepreneurs.

*The carrying value of forborne assets in comparison with the loan portfolio of the Group (excluding Debt securities and Other amounts due from customers):*

| | | | 31 Dec 2016 | | | 31 Dec 2015 |
|---|---|---|---|---|---|---|
| (CZKm) | Gross receivable | Forborne assets | Share in gross receivable | Gross receivable | Forborne assets | Share in gross receivable |
| Individuals | 275,528 | 3,040 | 1.10 % | 247,860 | 2,334 | 0.94 % |
| Corporates* | 316,676 | 2,980 | 0.94 % | 296,723 | 2,490 | 0.84 % |
| **Total** | **592,204** | **6,020** | **1.02 %** | **544,583** | **4,824** | **0.89 %** |

* This item also includes loans granted to individual entrepreneurs.

*Portfolio and specific allowances for forborne assets:*

| | | | 31 Dec 2016 | | | 31 Dec 2015 |
|---|---|---|---|---|---|---|
| (CZKm) | Portfolio allowances | Specific allowances | Total | Portfolio allowances | Specific allowances | Total |
| Individuals | 15 | 690 | 705 | 8 | 474 | 482 |
| Corporates* | 36 | 1,356 | 1,392 | 8 | 1,370 | 1,378 |
| **Total** | **51** | **2,046** | **2,097** | **16** | **1,844** | **1,860** |

* This item also includes loans granted to individual entrepreneurs.

## Finance lease

Within the Group, ESSOX s.r.o., PSA FINANCE ČESKÁ REPUBLIKA, s.r.o., PSA FINANCE SLOVAKIA, s.r.o. and SG Equipment Finance Czech Republic s.r.o. engage in providing lease services. Assets leased under lease arrangements at ESSOX s.r.o. primarily include new passenger and utility vehicles with an average lease instalment period of 60 months (2015: 60 months) and technology with an average lease instalment period of 0 months (2015: 37 months). At PSA FINANCE ČESKÁ REPUBLIKA, s.r.o., leased assets primarily include vehicles with an average lease instalment period of 60 months. At PSA FINANCE SLOVAKIA, s.r.o., leased assets primarily include motor vehicles with an option to buy the leased item with an average lease instalment period of 43 months. At SG Equipment Finance Czech Republic s.r.o. leased assets primarily include trucks, tractors and buses with an average lease instalment period of 63 months (2015: 64 months), agricultural vehicles and machines with an average lease instalment period of 62 months (2015: 59 months), machine technology with an average lease instalment period of 66 months (2015: 61 months), air transport equipment with an average lease instalment period of 0 months (2015: 100 months), hardware and software technology with an average lease instalment period of 43 months (2015: 51 months) and real estate with an average lease instalment period of 9 years (2015: 11 years).

*Loans and advances to customers – leasing*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Due less than 1 year | 4,805 | 4,431 |
| Due from 1 to 5 years | 9,003 | 7,549 |
| Due over 5 years | 531 | 453 |
| **Total** | **14,339** | **12,433** |

*Future interest (the difference between gross and net investment in the lease) on lease contracts is:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Due less than 1 year | 317 | 324 |
| Due from 1 to 5 years | 423 | 415 |
| Due over 5 years | 22 | 23 |
| **Total** | **762** | **762** |

As of 31 December 2016, the provisions recognised against uncollectible lease receivables amount to CZK 529 million (2015: CZK 289 million).

## 22 Held-to-maturity investments

*Held-to-maturity investments comprise the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **(CZKm)** | **Carrying value** | **Cost*** | **Carrying value** | **Cost*** |
| Fixed income debt securities | 65,462 | 64,176 | 67,083 | 65,578 |
| **Total held–to-maturity investments** | **65,462** | **64,176** | **67,083** | **65,578** |

* Amortised acquisition cost excluding coupon.

As of 31 December 2016, the ***'Held-to-maturity investments'*** portfolio includes bonds of CZK 64,176 million (2015: CZK 63,486 million) that are publicly traded on stock exchanges and bonds of CZK 0 million (2015: CZK 3,597 million) that are not publicly traded.

As of 31 December 2016, the ***'Held-to-maturity investments'*** portfolio includes bonds of CZK 107 million (2015: CZK 0 million) that are used as collateral for derivative deals with central counterparty.

*Fixed income debt securities held-to-maturity comprise the following:*

| **(CZKm)** | **31 Dec 2016** | **31 Dec 2015** |
|---|---|---|
| **Fixed income debt securities** | | |
| – Czech Crowns | 51,393 | 53,265 |
| – Foreign currencies | 14,069 | 13,818 |
| **Total fixed income debt securities** | **65,462** | **67,083** |

*Fixed income debt securities held-to-maturity, allocated by issuer, comprise the following:*

| **(CZKm)** | **31 Dec 2016** | **31 Dec 2015** |
|---|---|---|
| **Fixed income debt securities issued by:** | | |
| – State institutions in the Czech Republic | 54,295 | 56,224 |
| – Foreign state institutions | 11,167 | 10,859 |
| **Total fixed income debt securities** | **65,462** | **67,083** |

*Debt securities held-to-maturity issued by Foreign state institutions comprise the following:*

| **(CZKm)** | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **Country of Issuer** | **Fair value** | **Cost*** | **Fair value** | **Cost*** |
| Slovakia | 2,822 | 3,096 | 5,146 | 4,812 |
| Poland | 7,938 | 7,818 | 6,023 | 5,778 |
| **Total** | **10,760** | **10,914** | **11,169** | **10,590** |

* Amortised acquisition cost excluding coupon.

## 23 Prepayments, accrued income and other assets

*Prepayments, accrued income and other assets comprise the following:*

| **(CZKm)** | **31 Dec 2016** | **31 Dec 2015** |
|---|---|---|
| Prepayments and accrued income | 722 | 560 |
| Settlement balances | 223 | 343 |
| Receivables from securities trading | 78 | 337 |
| Other assets | 3,896 | 3,196 |
| **Total prepayments, accrued income and other assets** | **4,919** | **4,436** |

*'Other assets'* include receivables of CZK 668 million (2015: CZK 698 million) from the state budget consisting of contributions to participants in the construction savings scheme and to holders of pension insurance policies, allowances for operating receivables for other debtors in the amount of CZK 243 million (2015: CZK 251 million), and in particular also advances provided and receivables for other debtors.

## 24 Investments in associates and non-controlling interests in subsidiaries

*Investments in associates comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Investments in associated undertakings | 1,280 | 1,219 |
| **Total investments in associates** | **1,280** | **1,219** |

In March 2016, the Bank concluded an agreement on the sale of its interest in Cataps, s.r.o. with Worldline SA/NV based upon which the Bank transferred its merchant acquiring into Cataps, s.r.o. and subsequently sold its 80% stake in Cataps, s.r.o. Both steps were performed in September 2016. The remaining 20% stake in Cataps, s.r.o. at CZK 181 million was reclassified as *'Assets held for sale'* due to expected sale of this company.

*The following companies are associated undertakings of the Group as of 31 December 2016:*

| (CZKm) | | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|---|
| **Associates** | **%** | **Cost of investment** | **Share of net assets** | **Cost of investment** | **Share of net assets** |
| Komerční pojišťovna, a.s. | 49.00 | 837 | 1,278 | 837 | 1,217 |
| Czech Banking Credit Bureau, a.s.* | 20.00 | 0 | 2 | 0 | 2 |
| **Total investments in associates** | | **837** | **1,280** | **837** | **1,219** |

| Associates classified in Held for sale portfolio | % | Cost of investment | Share of net assets | Cost of investment | Share of net assets |
|---|---|---|---|---|---|
| Cataps, s.r.o. | 20.00 | 8 | 181 | x | x |
| **Total investments in associates**** | | **845** | **1,461** | **837** | **1,219** |

* The cost of investment for CBCB – Czech Banking Credit Bureau, a.s. is CZK 240 thousand.
** Including associates classified in held for sale portfolio.

| (CZKm) | | | | 31 Dec 2016 |
|---|---|---|---|---|
| **Associates** | **Assets** | **Liabilities** | **Operating income** | **Profit** |
| Komerční pojišťovna, a.s. | 55,478 | 52,870 | 821 | 410 |
| Czech Banking Credit Bureau, a.s. | 25 | 14 | 121 | 9 |
| Cataps, s.r.o. | 1,125 | 357 | 48 | 38 |

| (CZKm) | | | | 31 Dec 2015 |
|---|---|---|---|---|
| **Associates** | **Assets** | **Liabilities** | **Operating income** | **Profit** |
| Komerční pojišťovna, a.s. | 53,173 | 50,690 | 679 | 308 |
| Czech Banking Credit Bureau, a.s. | 18 | 5 | 117 | 11 |

*Movements in share of associated undertakings:*

| (CZKm) | Komerční pojišťovna, a.s. | Czech Banking Credit Bureau, a.s. | Cataps, s.r.o. | Total |
|---|---|---|---|---|
| As of 1 January 2015 | 1,232 | 2 | 0 | 1,234 |
| Dividend payment | (138) | (2) | 0 | (140) |
| Share of profit | 151 | 2 | 0 | 153 |
| Share of revaluation on available-for-sale assets | (28) | 0 | 0 | (28) |
| **As of 31 December 2015** | **1,217** | **2** | **0** | **1,219** |
| Dividend payment | (150) | (2) | 0 | (152) |
| Share of profit | 201 | 2 | 0 | 203 |
| Revaluation of investment | 0 | 0 | 181 | 181 |
| Share of revaluation on available-for-sale assets | 10 | 0 | 0 | 10 |
| **As of 31 December 2016** | **1,278** | **2** | **181** | **1,461** |

*Main financial information about the subsidiary that has non-controlling interest are following:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| (CZKm) | Assets | Liabilities | Profit | Assets | Liabilities | Profit |
| SG Equipment Finance Czech Republic s.r.o.* | 28,794 | 24,745 | 268 | 28,875 | 25,098 | 278 |
| ESSOX s.r.o.** | 11,571 | 7,937 | 458 | 9,780 | 5,845 | 481 |
| PSA FINANCE ČESKÁ REPUBLIKA, s.r.o.** | 3,067 | 2,310 | 29 | x | x | x |
| PSA FINANCE SLOVAKIA, s.r.o.** | 1,859 | 1,675 | 8 | x | x | x |

* Non-controlling interest of SG Equipment Finance Czech Republic s.r.o. subsidiary amounts to 49.9%.
** Non-controlling interest of ESSOX s.r.o., PSA FINANCE ČESKÁ REPUBLIKA, s.r.o. and PSA FINANCE SLOVAKIA, s.r.o. subsidiary amounts to 49.1%.

*Movements of non-controlling interests:*

| (CZKm) | SG Equipment Finance Czech Republic s.r.o. | ESSOX s.r.o. | PSA FINANCE ČESKÁ REPUBLIKA, s.r.o. | PSA FINANCE SLOVAKIA, s.r.o. | Total |
|---|---|---|---|---|---|
| As of 1 January 2015 | 1,199 | 1,932 | X | X | 3,131 |
| Dividend payment | 0 | (238) | X | X | (238) |
| Profit / loss | 138 | 236 | X | X | 374 |
| Share based payment | (1) | 1 | X | X | 0 |
| Increasing of shareholders' equity | 549 | 0 | X | X | 549 |
| Cash flow hedging | 0 | 0 | X | X | 0 |
| **As of 31 December 2015** | **1,885** | **1,931** | **X** | **X** | **3,816** |
| Dividend payment | 0 | (375) | 0 | 0 | (375) |
| Profit / loss | 134 | 224 | 21 | 7 | 386 |
| Share based payment | 1 | 3 | 0 | 0 | 4 |
| Increasing of shareholders' equity | 0 | 0 | 0 | 0 | 0 |
| Cash flow hedging | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **2,020** | **1,783** | **21** | **7** | **3,831** |

Additional information about the Group's equity investments is presented in Notes 1 and 2.

## 25 Intangible assets

*The movements in intangible assets were as follow:*

| (CZKm) | Internally generated assets* | Software | Other intangible assets | Acquisition of assets | Total |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| As of 1 January 2015 | 10,159 | 2,660 | 56 | 819 | 13,694 |
| Additions | 673 | 327 | 0 | 1,274 | 2,274 |
| Disposals/transfers | (20) | (132) | (25) | (1,000) | (1,177) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| As of 31 December 2015 | 10,812 | 2,855 | 31 | 1,093 | 14,791 |
| Effect of acquisition of companies | 0 | 2 | 0 | 0 | 2 |
| Additions | 902 | 200 | 0 | 1,116 | 2,218 |
| Disposals/transfers | 0 | (29) | (2) | (1,102) | (1,133) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **11,714** | **3,028** | **29** | **1,107** | **15,878** |
| **Accumulated amortisation and allowances** | | | | | |
| As of 1 January 2015 | (7,745) | (2,138) | (53) | 0 | (9,936) |
| Additions | (947) | (194) | (1) | 0 | (1,142) |
| Disposals | 20 | 115 | 23 | 0 | 158 |
| Impairment charge | 0 | (4) | 0 | 0 | (4) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| As of 31 December 2015 | (8,672) | (2,221) | (31) | 0 | (10,924) |
| Effect of acquisition of companies | 0 | (1) | 0 | 0 | (1) |
| Additions | (902) | (192) | 0 | 0 | (1,094) |
| Disposals | 0 | 29 | 3 | 0 | 32 |
| Impairment charge | 0 | (3) | 0 | (2) | (5) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **(9,574)** | **(2,388)** | **(28)** | **(2)** | **(11,992)** |
| **Net book value** | | | | | |
| As of 31 December 2015 | 2,140 | 634 | 0 | 1,093 | 3,867 |
| **As of 31 December 2016** | **2,140** | **640** | **1** | **1,105** | **3,886** |

* Internally generated assets comprise mainly software.

During the year ended 31 December 2016, the Group expended CZK 185 million (2015: CZK 144 million) on research and development (when conditions for capitalisation were not met) through a charge to *'Operating expenses'*. As of 31 December 2016, the Group recognised allowances against intangible assets of CZK 9 million (2015: CZK 4 million). These allowances primarily included allowances charged in respect of software.

## 26 Tangible assets

*The movements in tangible assets were as follow:*

| (CZKm) | Land | Buildings | Machinery, furniture and fixtures and other | Acquisition of assets | Total |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| As of 1 January 2015 | 358 | 12,442 | 5,179 | 276 | 18,255 |
| Reallocation from/to assets held for sale | (29) | (1,587) | 0 | 0 | (1,616) |
| Additions | 0 | 216 | 271 | 649 | 1,136 |
| Disposals/transfers | 0 | (108) | (586) | (487) | (1,181) |
| Foreign exchange rate difference | 0 | 0 | 1 | 0 | 1 |
| As of 31 December 2015 | 329 | 10,963 | 4,865 | 438 | 16,595 |
| Effect of acquisition of companies | 0 | 0 | 4 | 0 | 4 |
| Reallocation from/to assets held for sale | (5) | (692) | (17) | 0 | (714) |
| Additions | 0 | 106 | 345 | 906 | 1,357 |
| Disposals/transfers | 0 | (10) | (234) | (560) | (804) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **324** | **10,367** | **4,963** | **784** | **16,438** |
| **Accumulated depreciation and allowances** | | | | | |
| As of 1 January 2015 | 0 | (6,373) | (4,216) | 0 | (10,589) |
| Reallocation of accumulated depreciation of assets held for sale | 0 | 839 | 0 | 0 | 839 |
| Additions | 0 | (357) | (296) | 0 | (653) |
| Disposals | 0 | 88 | 568 | 0 | 656 |
| Impairment charge | 0 | 0 | (5) | 0 | (5) |
| Foreign exchange rate difference | 0 | 0 | 1 | 0 | 1 |
| As of 31 December 2015 | 0 | (5,803) | (3,948) | 0 | (9,751) |
| Effect of acquisition of companies | 0 | 0 | (2) | 0 | (2) |
| Reallocation of accumulated depreciation of assets held for sale | 0 | 415 | 14 | 0 | 429 |
| Additions | 0 | (368) | (293) | (2) | (663) |
| Disposals | 0 | 8 | 245 | 0 | 253 |
| Impairment charge | 0 | 9 | (47) | 0 | (38) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **0** | **(5,739)** | **(4,031)** | **(2)** | **(9,772)** |
| **Net book value** | | | | | |
| As of 31 December 2015 | 329 | 5,160 | 917 | 438 | 6,844 |
| **As of 31 December 2016** | **324** | **4,628** | **932** | **782** | **6,666** |

As of 31 December 2016, the Group recognised allowances against tangible assets of CZK 45 million (2015: CZK 7 million). These allowances primarily included allowances charged in respect of computer equipment.

## 27 Goodwill

*Goodwill by individual companies as of 31 December 2016 was as follows:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Modrá pyramida stavební spořitelna, a.s. | 3,388 | 3,388 |
| ESSOX s.r.o. | 163 | 163 |
| SG Equipment Finance Czech Republic s.r.o. | 201 | 201 |
| **Total goodwill** | **3,752** | **3,752** |

The management is of the view that reasonable potential changes in the key assumptions for Modrá pyramida stavební spořitelna, a.s. upon which the recoverable amount is based would not cause it to fall below the carrying amount given the fact that the value in use is significantly greater than the carrying amount. Impairment of goodwill is considered unlikely.

## 28 Financial liabilities at fair value through profit or loss

As of 31 December 2016 and 2015, the *'Financial liabilities at fair value through profit or loss'* portfolio includes only liabilities arising from short sales of securities and negative fair values of financial derivative instruments held for trading. Upon initial recognition, the Group has not designated any financial liabilities as *'Financial liabilities at fair value through profit or loss'*.

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Sold securities | 160 | 305 |
| Derivative financial instruments | 18,007 | 19,189 |
| **Total financial liabilities at fair value through profit or loss** | **18,167** | **19,494** |

For detailed information on financial derivative instruments included in the portfolio for trading, refer to Note 42(C).

## 29 Amounts due to banks

*Amounts due to banks comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Current accounts (refer to Note 36) | 3,220 | 2,740 |
| Amounts due to banks | 50,904 | 53,490 |
| **Total amounts due to banks** | **54,124** | **56,230** |

*The fair values of securities and treasury bills used as collateral for repurchase loans are as follow:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Carrying value | Fair value | Carrying value | Fair value |
| Financial assets at fair value through profit or loss | 403 | 403 | 0 | 0 |
| Available-for-sale financial assets | 758 | 758 | 0 | 0 |
| Held-to-maturity investments | 4,888 | 4,862 | 0 | 0 |
| Securities received as collateral | 0 | 0 | 117 | 117 |
| **Total** | **6,049** | **6,023** | **117** | **117** |

## 30 Amounts due to customers

*Amounts due to customers, by type of deposit, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Current accounts | 496,353 | 449,672 |
| Savings accounts | 160,632 | 163,600 |
| Term deposits | 29,828 | 26,215 |
| Amounts received from customers | 5,198 | 9,699 |
| Other payables to customers | 7,366 | 7,101 |
| **Total amounts due to customers** | **699,377** | **656,287** |

The fair value of securities and treasury bills used as collateral for repurchase loans received from customers was CZK 5,217 million (2015: CZK 9,709 million), comprising securities received as collateral.

*Amounts due to customers, by type of customer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Private companies | 220,756 | 225,460 |
| Other financial institutions, non-banking entities | 21,480 | 29,626 |
| Insurance companies | 5,615 | 2,542 |
| Public administration | 577 | 2,141 |
| Individuals | 287,931 | 258,260 |
| Individuals – entrepreneurs | 30,498 | 29,435 |
| Government agencies | 77,309 | 70,581 |
| Other | 16,665 | 15,579 |
| Non-residents | 38,546 | 22,663 |
| **Total amounts due to customers** | **699,377** | **656,287** |

## 31 Securities issued

*Securities issued comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Mortgage bonds | 11,030 | 11,283 |
| Depository bills of exchange | 2,393 | 10,120 |
| **Total securities issued** | **13,423** | **21,403** |

The Group issues mortgage bonds to fund its mortgage activities.

*Mortgage bonds according to their remaining time to maturity break out as follows:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| In less than one year | 0 | 0 |
| In one to five years | 1,745 | 1,761 |
| In five to ten years | 1,007 | 1,008 |
| In ten to twenty years | 0 | 0 |
| More than twenty years | 8,278 | 8,514 |
| **Total debt securities** | **11,030** | **11,283** |

*The securities issued detailed above include the following mortgage bonds issued by the Group:*

| Name | Interest rate | Currency | Issue date | Maturity date | 31 Dec 2016 CZKm | 31 Dec 2015 CZKm |
|---|---|---|---|---|---|---|
| HZL Komerční banky, a.s., CZ0002001753 | Rate of the interest swap sale in CZK for 10 years plus 150 bps | CZK | 21 Dec 2007 | 21 Dec 2037 | 8,278 | 8,514 |
| HZL Komerční banky, a.s., CZ0002002801 | 2.55% | CZK | 21 Dec 2012 | 21 Dec 2022 | 1,745 | 1,008 |
| HZL Komerční banky, a.s., CZ0002003064 | 6M PRIBOR plus 50 bps | CZK | 14 Mar 2013 | 14 Mar 2018 | 1,007 | 1,761 |
| **Total mortgage bonds** | | | | | **11,030** | **11,283** |

Six-month PRIBOR as of 31 December 2016 was 35 bps (2015: 37 bps).
The value of the interest rate swap CZK sale average for ten years as of 31 December 2016 was 88 bps (2015: 103 bps).

## 32 Accruals and other liabilities

*Accruals and other liabilities comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Accruals and deferred income | 344 | 237 |
| Settlement balances and outstanding items | 1 | 0 |
| Payables from securities trading and issues of securities | 3,305 | 2,790 |
| Payables from payment transactions | 6,633 | 6,981 |
| Other liabilities | 5,867 | 5,411 |
| **Total accruals and other liabilities** | **16,150** | **15,419** |

Deferred fees from banking guarantees are reported in *'Accruals and deferred income'* in the amount of CZK 19 million (2015: CZK 19 million).

*'Other liabilities'* mainly include liabilities arising from the supplies of goods and services and employee arrangements (including estimated balances).

## 33 Provisions

*Provisions comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Provisions for contracted commitments (refer to Note 12 and 37) | 473 | 378 |
| Provisions for other credit commitments (refer to Note 12) | 1,241 | 783 |
| **Total provisions** | **1,714** | **1,161** |

The provisions for other credit commitments are held to cover credit risks associated with credit commitments issued. The provisions for contracted commitments principally comprise the provisions for ongoing contracted contingent commitments, legal disputes, self-insurance and the retirement benefits plan.

*Set out below is an analysis of the provisions for other credit commitments:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Provision for off-balance sheet commitments | 1,206 | 728 |
| Provision for undrawn loan facilities | 35 | 55 |
| **Total** (refer to Note 12) | **1,241** | **783** |

*Movements in the provisions for contracted commitments were as follow:*

| (CZKm) | Retirement benefits plan | Provisions for loyalty and jubilee bonuses | Other provisions for contracted commitments | Total |
|---|---|---|---|---|
| Balance as of 1 January 2015 | 178 | 3 | 465 | 646 |
| Charge | 13 | 0 | 97 | 110 |
| Release | 0 | (1) | (340) | (341) |
| Use | (13) | 0 | (49) | (62) |
| Accrual | 3 | 0 | 0 | 3 |
| Remeasurement | 20 | 0 | 0 | 20 |
| Foreign exchange difference | 0 | 0 | 2 | 2 |
| **Balance as of 31 December 2015** | **201** | **2** | **175** | **378** |
| Charge | 13 | 1 | 38 | 52 |
| Release | 0 | (1) | (54) | (55) |
| Use | (10) | 0 | (12) | (22) |
| Accrual | 4 | 0 | 0 | 4 |
| Remeasurement | 115 | 0 | 0 | 115 |
| Foreign exchange difference | 0 | 0 | 1 | 1 |
| **Balance as of 31 December 2016** | **323** | **2** | **148** | **473** |

## 34 Deferred tax

Deferred tax is calculated from temporary differences between the tax bases and carrying values using tax rates effective in the periods in which the temporary tax difference is expected to be realised.

*Net deferred tax assets are as follow:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Banking provisions and allowances | 0 | 0 |
| Allowances for assets | 0 | 0 |
| Non-banking provisions | 69 | 60 |
| Difference between accounting and tax net book value of assets | (1) | 1 |
| Leases | 6 | 5 |
| Remeasurement of retirement benefits plan – equity impact (refer to Note 39) | 0 | 0 |
| Revaluation of hedging derivatives – equity impact (refer to Note 40) | 0 | 1 |
| Revaluation of available-for-sale financial assets – equity impact (refer to Note 41) | 0 | 0 |
| Other temporary differences | 4 | 3 |
| **Net deferred tax assets** | **78** | **70** |

*Net deferred tax liabilities are as follow:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Banking provisions and allowances | 284 | 184 |
| Allowances for assets | 77 | 81 |
| Non-banking provisions | 87 | 141 |
| Difference between accounting and tax net book value of assets | (1,036) | (941) |
| Leases | (58) | (100) |
| Remeasurement of retirement benefits plan – equity impact (refer to Note 39) | 31 | 9 |
| Revaluation of hedging derivatives – equity impact (refer to Note 40) | (2,668) | (2,971) |
| Revaluation of available-for-sale financial assets – equity impact (refer to Note 41) | (701) | (1,034) |
| Other temporary differences | 154 | 47 |
| **Net deferred tax liabilities** | **(3,830)** | **(4,584)** |

*Movements in the net deferred tax assets/(liabilities) were as follow:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| **Balance as of the beginning of the period** | **(4,514)** | **(5,215)** |
| Effect of acquisition of companies | 6 | 0 |
| Movement in the net deferred tax – profit and loss impact (refer to Note 13) | 99 | (96) |
| Movement in the net deferred tax – equity impact (refer to Notes 39, 40 and 41) | 657 | 797 |
| **Balance as of the end of the period** | **(3,752)** | **(4,514)** |

## 35 Share capital

The Bank's share capital, entered in the Register of Companies on 11 February 2000, amounts to CZK 19,004,926,000. Based on a decision of the Annual General Meeting held on 22 April 2016, the Bank split its shares in the rate of 5:1, which means that the number of the shares increased by splitting the existing shares into 190,049,260 ordinary bearer shares issued as uncertificated securities with a nominal value of CZK 100 each (ISIN: CZ0008019106). The number of shares authorised is the same as the number of shares issued. The share capital is fully paid up.

The Bank's shares are publicly traded on stock markets in the Czech Republic managed by the market organisers Burza cenných papírů Praha, a.s. (the Prague Stock Exchange) and RM-SYSTÉM, česká burza cenných papírů a.s. (the Czech Stock Exchange). Their transferability is not restricted.

Rights are attached to the ordinary shares in accordance with Act No. 90/2012 Coll., on Business Corporations and Co-operatives. No special rights are attached to the shares. Shareholders' voting rights are governed by the nominal value of their shares. The voting rights can only be eliminated on statutory grounds. The Bank cannot exercise voting rights attached to its own shares.

Shareholders are entitled to share in the Bank's profit (dividend) approved for distribution by the Annual General Meeting based on the Bank's financial results and in accordance with the conditions stipulated by generally binding legal regulations.

The right to payment of the dividend is time-barred from four years after its declared payment date. Pursuant to a resolution of the Annual General Meeting held in 2009, the Board of Directors will not plead the statute of limitations in order to bar by lapse of time the payment of dividends for the duration of 10 years from the date of dividend payment. After the lapse of 10 years from the date of dividend payment, the Board of Directors is obliged to plead the statute of limitations and to transfer the unpaid dividends to the retained earnings account.

In the event of a shareholder's death, his or her legal heir shall be entitled to exercise all rights attached to the shares. Upon the Bank's liquidation and dissolution, the means of liquidation are governed by the relevant generally binding legal regulations. The proposal for the distribution of the liquidation balance among shareholders is approved by the Annual General Meeting in proportion to the nominal values of the shares held by the Bank's shareholders.

*Set out below is a summary of the entities that hold more than 1% of the Bank's issued share capital as of 31 December 2016:*

| Name of the entity | Ownership percentage |
|---|---|
| SOCIETE GENERALE S.A. | 60.35% |
| NORTRUST NOMINEES LIMITED | 4.20% |
| CHASE NOMINEES LIMITED | 3.59% |
| BROWN BROTHERS HARRIMAN | 2.70% |
| STATE STREET BANK AND TRUST COMPANY | 2.44% |
| CLEARSTREAM BANKING, S.A. | 2.23% |
| GIC PRIVATE LIMITED | 2.06% |
| J.P. MORGAN BANK | 1.09% |
| AGF INVESTMENTS INC. | 1.00% |

Société Générale S.A., being the only entity with a qualified holding in the Group, and moreover as the parent company, is a French company limited by shares incorporated by a Deed approved through the issuance of a Decree on 4 May 1864, and is licensed as a bank. Under the legislative and regulatory provisions relating to financial institutions, notably the articles of the Monetary and Financial

Code, the Company is subject to commercial laws, in particular Articles 210-1 et seq, of the French Commercial Code, as well as its Articles of Association.

As of 31 December 2016, the Bank held 1,193,360 of its own share in treasury at a cost of CZK 726 million (2015: 1,193,360 treasury shares which equals the number of 238,672 shares before shares split at a cost of CZK 726 million).

**Capital management**

The Basel III rules, known in EU regulation as CRR/CRD IV, effective from 2014, did not change the process for managing Group's regulatory capital adequacy, but they were taken into consideration when setting the parameters of that process as concerns in particular application of the combined capital buffer and additional Pillar 2 buffer on top of the minimum required capital ratio of 8.0%. The regulatory methodology was stabilised in 2016 (in particular the stacking order of capital buffers), and consequently an additional Pillar 2 buffer of 1.5% over the minimum required capital ratio of 8.0% is applied to the Group. That means the total SREP (supervisory review and evaluation process) capital requirement (TSCR) is 9.5%. The combined capital buffer of 5.0% is applied on top of the TSCR capital ratio resulting in the required overall capital ratio of 14.5% for the year 2016 (an increase by 0.1% in comparison with the previous year). The combined capital buffer consists of the capital conservation buffer of 2.5% and the systemic risk buffer of 2.5%. A countercyclical buffer was effectively not applied. Inasmuch as its capital ratio stands well above the minimum required level, the Group meets the required level of the overall capital ratio with an adequate reserve.

The Group manages its capital adequacy to ensure its sufficient level in an environment of changing regulatory requirements while allowing organic business growth and for potentially adverse macroeconomic development. Under the Basel III capital adequacy regulation, just as under the previous Basel II regulation, in addition to the usual reporting of the capital ratio (Pillar 1), the Group must meet the requirements for evaluating required economic capital, stress testing and capital planning (Pillar 2). To determine the required economic capital, the Group has selected methods close to the regulatory procedures applied for Pillar 1. Consequently, the necessary levels of economic and regulatory capital are very similar.

The Group regularly simulates future developments under Pillar 2 based on the assumption of possible adverse external macroeconomic conditions that may either directly affect the Group's profit or have implications resulting in deterioration in the Group's transactions' risk profile.

The Group compiles hypothetical macroeconomic scenarios on the basis of which it estimates medium-term impacts on earnings and on transactions' risk profiles. On this basis, the Group acquires views as to the changing volume of the risk-weighted assets (i.e. capital requirements), financial results, and, while also taking into account the outlook for dividend payments, the level of the Group's capital adequacy ratio.

The results of such stress testing are among those factors considered in determining the Group's dividend policy, which is the primary tool for capital adequacy management in such a situation that the Group's capital is entirely classified as Common Equity Tier 1 capital.

The Group's capital principally consists of the following balances: share capital, reserve funds and retained earnings.

The Group did not purchase its own shares into treasury during 2016 and as of 31 December 2016 the Group holds in total 1,193,360 treasury shares at a total cost of CZK 726 million which equals the number of 238,672 treasury shares before shares split. These had been purchased in previous years (2015: 238,672 treasury shares at a total cost of CZK 726 million). The purchase of treasury shares had been approved by the Bank's General Meeting especially for the purpose of managing the Group's capital adequacy.

With regard to the fact that the capital requirements of the Basel III regulation (particularly the capital buffers, typically the countercyclical buffer) can vary over time and a part of the implementation of regulatory rules and the regulation itself are still being developed, the Group continuously monitors and evaluates the forthcoming changes in regulatory requirements affecting the capital and capital adequacy and it analyses their potential impact within the capital planning process.

The CNB, as the local regulatory authority, oversees the Group's compliance with the capital adequacy on both separate and consolidated bases. During the past year, the Group complied with all regulatory requirements. Moreover, the Group regularly prepares the regulatory report on Pillar 2 (i.e. internal capital adequacy assessment process) and submits it to the CNB.

## 36 Composition of cash and cash equivalents as reported in the Statement of Cash Flows

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 | Change in the year |
|---|---|---|---|
| Cash and current balances with central banks (refer to Note 16) | 112,241 | 128,336 | (16,095) |
| Amounts due from banks – current accounts with other banks (refer to Note 20) | 1,043 | 536 | 507 |
| Amounts due to central banks | (1) | (1) | 0 |
| Amounts due to banks – current accounts (refer to Note 29) | (3,220) | (2,740) | (480) |
| **Cash and cash equivalents at the end of the year** | **110,063** | **126,131** | **(16,068)** |

## 37 Commitments and contingent liabilities

### Legal disputes

The Group conducted a review of legal proceedings outstanding against it as of 31 December 2016. Pursuant to the review of significant litigation matters in terms of the risk of losses and litigated amounts, the Group has recorded a provision of CZK 23 million (2015: CZK 43 million) for these legal disputes (refer to Note 33). The Group has also recorded a provision of CZK 43 million (2015: CZK 46 million) for costs associated with a potential payment of appurtenances on the pursued claims.

As of 31 December 2016, the Group conducted a review of legal proceedings it had filed against other entities. The Group has been notified that certain parties against which it is taking legal action may file counterclaims against it. The Group will contest any such claims and, taking into consideration the opinion of its internal and external legal counsel, believes that any asserted claims made will not materially affect its financial position. No provision has been made in respect of these matters.

### Commitments arising from the issuance of guarantees

Commitments from guarantees represent irrevocable assurances that the Group will make payments in the event that a customer cannot meet its obligations to the third parties. These assurances carry the same credit risk as do loans, and therefore the Group makes provisions for these instruments (according to a customer's credit worthiness) on the same basis as is applicable to loans.

### Capital commitments

As of 31 December 2016, the Group had capital commitments of CZK 367 million (2015: CZK 458 million) in respect of current capital investment projects.

### Commitments arising from the issuance of letters of credit

Documentary letters of credit are written irrevocable commitments by the Group on behalf of a customer (mandatory) authorising a third party (beneficiary) to draw drafts on the Group up to a stipulated amount under specific terms and conditions. The Group records provisions for these instruments (according to a customer's creditworthiness) on the same basis as is applicable to loans.

### Commitments to extend credit, undrawn loan commitments and overdrafts and approved overdraft loans

Principal off-balance sheet exposures include undrawn limits under framework agreements to provide financial services, approved overdraft loans, undrawn loan commitments, issued commitments to extend credit and unutilised facilities. The primary purpose of commitments to extend credit and framework agreements is to ensure that funds are available to a customer as required. Commitments to extend credit represent unused portions of authorisations to extend credit in the forms of loans or guarantees. In accordance with the IFRS definition of a conditioned commitment, the Group distinguishes between irrevocable and revocable commitments to extend credit and framework agreements. The irrevocability of commitments, framework agreements of undrawn loan commitments, unutilised overdrafts and approved overdraft loans results from contractual terms and conditions of the credit agreements (i.e. their use is not contingent upon customers' maintaining other specific credit standards). For irrevocable commitments or framework agreements, undrawn loan commitments, unutilised overdrafts and approved overdraft loans, the Group recognises a provision when required (according to a customer's credit worthiness) in accordance with the same algorithm as for loans.

*Financial commitments and contingencies comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Non-payment guarantees including commitments to issued non-payment guarantees | 36,248 | 35,358 |
| Payment guarantees including commitments to issued payment guarantees | 14,939 | 12,716 |
| Committed facilities and unutilised overdrafts | 9,476 | 14,351 |
| Undrawn credit commitments | 62,644 | 48,082 |
| Unutilised overdrafts and approved overdraft loans | 15,674 | 13,309 |
| Unutilised limits under framework agreements to provide financial services | 9,445 | 10,820 |
| Open customer/import letters of credit uncovered | 755 | 566 |
| Standby letters of credit uncovered | 1,091 | 1,336 |
| Confirmed supplier/export letters of credit | 22 | 52 |
| **Total commitments and contingencies** | **150,294** | **136,590** |

The risk associated with off-balance sheet credit commitments and contingent liabilities is assessed on the same basis as is that of loans to customers, taking into account the financial position and activities of the entity to which the Group issued the guarantee and the collateral obtained. As of 31 December 2016, the Group recorded provisions for these risks in the amount of CZK 1 241 million (2015: CZK 783 million). Refer to Note 33.

*Set out below is a breakdown of financial commitments and contingencies by sector:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Food industry and agriculture | 10,356 | 8,259 |
| Mining and extraction | 668 | 419 |
| Chemical and pharmaceutical industry | 3,622 | 3,432 |
| Metallurgy | 4,692 | 5,251 |
| Automotive industry | 1,501 | 1,350 |
| Manufacturing of other machinery | 7,749 | 7,283 |
| Manufacturing of electrical and electronic equipment | 2,468 | 1,894 |
| Other processing industry | 2,014 | 1,564 |
| Power plants, gas plants and waterworks | 4,674 | 7,231 |
| Construction industry | 31,989 | 32,866 |
| Retail | 3,731 | 2,966 |
| Wholesale | 7,865 | 7,840 |
| Accommodation and catering | 400 | 417 |
| Transportation, telecommunication and warehouses | 9,292 | 9,429 |
| Banking and insurance industry | 7,760 | 4,106 |
| Real estate | 3,300 | 2,885 |
| Public administration | 4,201 | 3,143 |
| Other industries | 13,308 | 12,642 |
| Individuals | 30,704 | 23,613 |
| **Total commitments and contingencies** | **150,294** | **136,590** |

The majority of commitments and contingencies originate on the territory of the Czech Republic.

*Set out below is an analysis of the types of collateral held in support of financial commitments and contingencies:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| **(CZKm)** | **Total commitments and contingencies collateral*** | **Discounted commitments and contingencies collateral value**** | **Applied commitments and contingencies collateral value***** | **Total commitments and contingencies collateral*** | **Discounted commitments and contingencies collateral value**** | **Applied commitments and contingencies collateral value***** |
| Guarantees of state and governmental institutions | 658 | 523 | 523 | 0 | 0 | 0 |
| Bank guarantee | 1,651 | 1,515 | 1,475 | 975 | 918 | 873 |
| Guaranteed deposits | 2,223 | 2,210 | 2,108 | 2,161 | 2,131 | 2,003 |
| Pledge of real estate | 11,810 | 7,318 | 6,040 | 10,122 | 6,173 | 5,030 |
| Pledge of movable assets | 84 | 8 | 8 | 226 | 22 | 22 |
| Guarantee by legal entity | 6,540 | 1,988 | 1,821 | 7,452 | 5,247 | 5,034 |
| Guarantee by individual (natural person) | 50 | 10 | 10 | 65 | 6 | 6 |
| Pledge of receivables | 1,939 | 0 | 0 | 3,317 | 0 | 0 |
| Insurance of credit risk | 1,560 | 1,476 | 1,476 | 2,097 | 1,925 | 1,925 |
| Other | 21 | 0 | 0 | 22 | 0 | 0 |
| **Total nominal value of collateral** | **26,536** | **15,048** | **13,461** | **26,437** | **16,422** | **14,893** |

* The nominal value of the collateral is determined based on internal rules of the Group (e.g. internal property valuation, the current value of collateral, the market value of securities).
** The nominal value of the collateral is reduced by a coefficient taking into account the time value of money, the cost of selling of the collateral, the risk of declining market prices, the risk of insolvency, etc.
*** The applied collateral value is the discounted collateral value reduced to the actual balance of the collateralised exposure.

In accordance with Act No. 427/2011, on Supplementary pension saving, and in accordance with the statutes of Transformovaný fond KB Penzijní společnost, a.s. (hereafter only the "Fund") created after 1 January 2013, KB Penzijní společnost, a.s. guarantees at least a zero return for clients on an annual basis and must ensure that the value of assets in the Fund is always equal to or greater than the value of liabilities. Otherwise, KB Penzijní společnost, a.s. is required to contribute to the Fund assets necessary to adjust the difference at latest within 30 days after the end of the quarter in which such fact was identified. These transferred assets constitute a special capital fund of the Fund and are primarily used to cover losses of the current year or accumulated losses from prior periods.

In accordance with the Fund's conservative strategy and based on sensitivity analysis, the usage of the guarantee is not probable in the near future as of the financial statements date.

## 38 Related parties

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party on making financial or operational decisions. As of 31 December 2016, the Group was controlled by Société Générale S.A., which owns 60.35% of its issued share capital.

A number of banking transactions are entered into with related parties in the normal course of business. These specifically include loans, deposits, transactions with derivative financial instruments and other types of transactions. These transactions are carried out on an arm's length basis.

### Amounts due to and from the Group companies

As of 31 December 2016, the Group had deposits of CZK 1,677 million (2015: CZK 1,253 million) due to the associate Komerční pojišťovna, a.s. The positive fair value of financial derivatives in relation to the associate Komerční pojišťovna, a.s. amounted to CZK 1,521 million (2015: CZK 1,911 million) and the negative fair value to CZK 46 million (2015: CZK 47 million). Book value of mortgage bonds issued by Bank was CZK 806 million (2015: CZK 807 million) and interest expense from mortgage bonds amounted to CZK 20 million (2015: CZK 20 million).

Interest income from financial derivatives of Komerční pojišťovna, a.s. to the Group amounted to CZK 853 million (2015: CZK 1,241 million) and interest expense on financial derivatives totalled CZK 566 million (2015: CZK 946 million). Interest expense from deposits amounted to CZK 1 million (2015: CZK 1 million), fee income of the Group arising from intermediation totalled CZK 380 million (2015: CZK 309 million), fee expense amounted to CZK 68 million (2015: CZK 62 million), insurance expenses came to CZK 18 million (2015: CZK 24 million) and other income totalled CZK 15 million (2015: CZK 12 million).

### Amounts due to and from the Société Générale Group entities

*Principal balances due from the Société Générale Group entities include the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Total | Of which derivatives | Total | Of which derivatives |
| ALD Automotive s.r.o. (Czech Republic) | 5,146 | 0 | 3,820 | 0 |
| ALD Automotive s.r.o. (Slovak Republic) | 370 | 0 | 648 | 0 |
| BRD – GROUPE Société Générale SA | 30 | 0 | 0 | 0 |
| PJSC Rosbank | 146 | 0 | 67 | 0 |
| SG Bruxelles | 137 | 0 | 2 | 0 |
| SG Expressbank | 15 | 0 | 10 | 0 |
| SG Marocaine de Banques | 4 | 0 | 0 | 0 |
| SG New York | 498 | 0 | 0 | 0 |
| SG Paris | 9,724 | 4,311 | 9,527 | 4,230 |
| SG S.A. oddzial w Polsce | 2 | 0 | 1 | 0 |
| SG Zurich | 176 | 0 | 0 | 0 |
| SGA Société Générale Acceptance | 2,989 | 0 | 3,098 | 0 |
| Société Générale Algerie | 0 | 0 | 2 | 0 |
| Société Générale China Limited | 3 | 0 | 19 | 0 |
| Société Générale – Splitska Banka d.d | 11 | 0 | 5 | 0 |
| Société Générale International Limited | 473 | 0 | 3 | 0 |
| **Total** | **19,724** | **4,311** | **17,202** | **4,230** |

*Principal balances owed to the Société Générale Group entities include the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Total | Of which derivatives | Total | Of which derivatives |
| ALD Automotive s.r.o. (Česká Republika) | 368 | 0 | 186 | 0 |
| BRD – GROUPE Société Générale SA | 8 | 0 | 3 | 1 |
| Crédit du Nord | 7 | 0 | 0 | 0 |
| Inter Europe Conseil | 0 | 0 | 2 | 0 |
| PEMA Praha, spol. s r.o. | 101 | 0 | 13 | 0 |
| SG Amsterdam | 47 | 0 | 46 | 0 |
| SG Banques au Liban | 1 | 0 | 14 | 0 |
| SG Bruxelles | 50 | 0 | 0 | 0 |
| SG ISSUER | 1 | 0 | 0 | 0 |
| SG Frankfurt | 8 | 0 | 1 | 0 |
| SG London | 13 | 0 | 11 | 0 |
| SG New York | 1 | 0 | 2 | 0 |
| SG Paris | 22,965 | 7,025 | 25,604 | 6,925 |
| SG Private Banking /Suisse/ S.A. | 184 | 0 | 280 | 0 |
| SG S.A. oddzial w Polsce | 1 | 0 | 3 | 0 |
| SG Zurich | 0 | 0 | 1 | 0 |
| SGSS Nantes | 3 | 0 | 0 | 0 |
| Société Générale Bank & Trust | 178 | 0 | 978 | 0 |
| Société Générale – Splitska Banka d.d | 1 | 0 | 1 | 0 |
| SOGEPROM Česká republika, s.r.o. | 5 | 0 | 6 | 0 |
| **Total** | **23,942** | **7,025** | **27,151** | **6,926** |

Amounts due to and from the Société Générale Group entities principally comprise balances of current and overdraft accounts, nostro and loro accounts, issued loans, interbank market loans and placements, deposited margins in favour of the counterparty and fair values of derivatives.

As of 31 December 2016, the Group also carried off-balance sheet exposures to the Société Générale Group entities, of which off-balance sheet nominal assets and liabilities amounted to CZK 348,641 million (2015: CZK 257,090 million) and CZK 323,315 million (2015: CZK 250,973 million), respectively. These amounts principally relate to currency spots and forwards, interest rate forwards and swaps, options, commodity derivatives, emission allowances and guarantees for credit exposures.

As of 31 December 2016 and 2015, the Group also carried other amounts due to and from the Société Générale Group entities which are not significant.

During the year ended 31 December 2016, the Group had total income of CZK 22,435 million (2015: CZK 20,485 million) and total expenses of CZK 19,243 million (2015: CZK 18,969 million) in relation to Société Générale Group entities. That income includes income from interbank deposits, fees from transactions with securities, profit from financial operations and interest income on hedging derivatives. Expenses comprise those of interbank deposits, a loss from financial operations, interest expense on hedging derivatives and expenses related to the provision of management, consultancy and software services.

### Remuneration and amounts due from members of the Board of Directors and Supervisory Board

*Remuneration paid to the members of the Board of Directors and Supervisory Board during the years was as follows:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Remuneration to the Board of Directors members* | 58 | 61 |
| Remuneration to the Supervisory Board members** | 6 | 5 |
| **Total** | **64** | **66** |

* Remuneration to the Board of Directors members includes wages paid during the year ended 31 December 2016 to the current and former directors under mandate and management contracts and other compensation and benefits granted in 2016. It also includes a part of bonuses awarded in 2016. The remuneration includes as well benefits arising to the Bank's employees under a collective bargaining agreement.

** Remuneration to the Supervisory Board members includes amounts paid during the year ended 31 December 2016 to the current and former members of the Supervisory Board. Amounts for the Supervisory Board members elected by employees additionally include income paid to them under their employment arrangement with the Bank. The remuneration also includes benefits arising to the Bank's employees under a collective bargaining agreement.

| | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Number of the Board of Directors members at the end of the period | 5 | 6 |
| Number of the Supervisory Board members at the end of the period | 9 | 9 |

In respect of loans and guarantees as of 31 December 2016, the Group recorded receivables from loans granted to members of the Board of Directors and Supervisory Board totalling CZK 15 million (2015: CZK 21 million). During 2016, draw-downs of CZK 1 million (2015: CZK 10 million) were made under the loans granted. Loan repayments during 2016 amounted to CZK 1 million (2015: CZK 11 million). The increase of loans in 2016 is affected by new members already having loans in the amount of CZK 6 million. The amount of loans of resigning members amounted to CZK 12 million as of 31 December 2015.

## 39 Movements in the remeasurement of retirement benefits plan in the equity

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Remeasurement of retirement benefits plan as of 1 January | (47) | (27) |
| Deferred tax asset/(liability) as of 1 January | 9 | 5 |
| **Balance as of 1 January** | **(38)** | **(22)** |
| **Movements during the year** | | |
| Gains/(losses) from remeasurement of retirement benefits plan | (115) | (20) |
| Deferred tax | 22 | 4 |
| | **(93)** | **(16)** |
| Remeasurement of retirement benefits plan as of 31 December | (162) | (47) |
| Deferred tax asset/(liability) as of 31 December (refer to Note 34) | 31 | 9 |
| **Balance as of 31 December** | **(131)** | **(38)** |

## 40 Movements in the revaluation of hedging instruments in the equity

In accordance with IAS 39, certain derivatives were designated as hedges. The changes in fair values of cash flow hedges are recorded in a separate line of equity in the hedging reserve.

### Balance of hedging instruments in equity at the beginning of the period

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Cash flow hedge fair value as of 1 January | 15,623 | 19,652 |
| Deferred tax asset/(liability) as of 1 January | (2,970) | (3,733) |
| **Balance as of 1 January** | **12,653** | **15,919** |
| **Movements during the year** | | |
| Gains/(losses) from changes in fair value | 2,417 | 172 |
| Deferred tax | (458) | (36) |
| | **1,959** | **136** |
| Transferred to interest income/expense | (3,999) | (4,193) |
| Deferred tax | 761 | 798 |
| | **(3,238)** | **(3,395)** |
| Transferred to net profit/loss on financial operations | 1 | 0 |
| Deferred tax | 0 | 0 |
| | 1 | 0 |
| Transferred to personnel expenses | 5 | (8) |
| Deferred tax | (1) | 1 |
| | **4** | **(7)** |
| Cash flow hedge fair value as of 31 December | 14,047 | 15,623 |
| Deferred tax asset/(liability) as of 31 December (refer to Note 34) | (2,668) | (2,970) |
| **Balance as of 31 December** | **11,379** | **12,653** |

## 41 Movements in the revaluation of available-for-sale financial assets in the equity

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Reserve from fair value revaluation as of 1 January | 5,994 | 6,298 |
| Deferred tax asset/(liability) as of 1 January | (1,034) | (1,065) |
| **Balance as of 1 January** | **4,960** | **5,233** |
| **Movements during the year** | | |
| Gains/(losses) from changes in fair value | (181) | 681 |
| Deferred tax | 12 | (156) |
| | **(169)** | **525** |
| (Gains)/losses from reclassified financial assets (refer to Notes 18) | (728) | (985) |
| Deferred tax | 139 | 187 |
| | **(589)** | **(798)** |
| (Gains)/losses from the sale | (960) | 0 |
| Deferred tax | 182 | 0 |
| | **(778)** | **0** |
| Reserve from fair value revaluation as of 31 December | 4,125 | 5,994 |
| Deferred tax asset/(liability) as of 31 December (refer to Note 34) | (701) | (1,034) |
| **Balance as of 31 December** | **3,424** | **4,960** |

# 42 Risk management and financial instruments

## (A) Credit risk

### Assessment of borrower's credit rating

The assessment of credit risk is based on quantitative and qualitative criteria, which leads to a rating assignment. The Group uses several types of ratings, depending on the type and profile of the counterparty and the types of transactions. As a result, specific ratings are assigned to both the Group's clients and to specific clients transactions. The same process of rating assignment is applied in relevant cases to respective guarantors and sub-debtors, which enables better assessment of the quality of accepted guarantees and collaterals.

In 2016, the Group focused on updating selected credit risk models in order to optimally reflect the current macroeconomic situation and goals set by the Group as well as on increasing of effectiveness in monitoring the risk profiles of individual client portfolios and the quality of tools and models for credit risk management.

As in previous years, the results of regular stress testing played an important role, allowing more precise estimates of the expected intensity of credit risk for the ensuing periods and thus optimisation of the Group's credit risk management tools and more accurate estimation of expected future losses.

### *(a) Business clients and municipalities*

For entrepreneurs, corporate clients and municipalities, the Group uses the obligor rating (expressed on the 22-grade Société Générale rating master scale) with the aim to evaluate the counterparty's Probability of Default (PD) and the Loss Given Default (LGD) rating to assess the quality of available guarantees and collaterals and to evaluate the potential loss from counterparty transactions. These models are also used for regular updates of Expected Loss (EL) and Unexpected Loss (UL) for all client exposures reported in accordance with the Basel III requirements.

For large and medium-sized clients, the obligor rating is the combination of the financial rating based primarily on the data in the financial statements and an economic rating obtained through the evaluation of non-financial information relating to a particular client.

In the entrepreneurs and small companies segment, the obligor rating is the combination of financial, non-financial and personal data, data on client behaviour within the Group and information from external credit bureaus. When clients are funded via simple products, the setting of the rating is alternatively limited to the evaluation of data on clients' behaviour within the Group (behavioural rating).

In the municipalities segment, the obligor rating is the combination of the financial rating based on the data in the financial statements and of an economic rating acquired through the assessment of non-financial information relating to a specific municipality.

The Group is also using dedicated rating model for housing co-operatives and association of owners. A special model for real estate developers and investors is currently in the validation phase.

### *(b) Ratings for banks and sovereigns*

For banks, other financial institutions (namely insurance companies, brokers and funds) and for sovereigns (central banks and central governments), the Group uses the economic rating models developed by Société Générale.

### *(c) Ratings for individual clients*

The Group uses two types of ratings with the aim to evaluate the default risk for individuals: (1) the application rating, which results from an evaluation of clients' personal data, data on the behaviour within the Group, and data available from external credit bureaus; and (2) a behavioural rating which is based on evaluation of information on the clients' behaviour within the Group. The application rating is primarily used for active applications of clients for funding, while the behavioural rating (which includes the calculation of indicative limits for simple products with low exposure) is used for active offers of funding by the Group. The behavioural rating of clients is concurrently used as an input for regular updates of the probability of default of all client exposures reported in accordance with the Basel III requirements.

*(d) Internal register of negative information*

The Group maintains an internal register of negative information. The register integrates the maximum quantity of available internal and external negative information on subjects related to the credit process. It includes algorithms for evaluating the negative information and contributes substantially to protecting the Group from risky entities.

*(e) Credit bureaus*

The evaluation of data from credit bureaus is one of the principal factors impacting the assessment of applications for client funding, and especially so in the retail client segments.

*(f) Credit fraud prevention*

The Group uses an automated system for the detection of credit frauds and also for co ordinated reactions to credit fraud attacks. The system is fully integrated with the Group's main applications. The system was updated in 2016 to reflect current market trends mainly in financing of the Individuals segment. Further upgrade of processes and controls preventing credit fraud in the small business segment will be performed in 2017.

### Credit concentration risk

The Group's credit concentration risk is actively managed as a part of overall credit risk management utilising standard tools, credit risk assessment, setting of internal limits, use of risk mitigation techniques, producing of sector analyses and stress testing. The Group maintains its objective not to take on any excessive credit concentration risk. Credit concentration risk management procedures cover individual counterparties as well as economically connected groups, countries, selected industry sectors and collateral providers. The system of internal limits is established so that the Group complies with the regulatory limits set by legislation in respect of concentration risk. Refer to Notes 21 and 37 for quantitative information about credit concentration risk.

*The Group's maximum credit exposure as of 31 December 2016:*

| | Total exposure | | | Collateral applied | | |
|---|---|---|---|---|---|---|
| (CZKm) | Statement of financial position | Off-balance sheet* | Total credit exposure | Statement of financial position | Off-balance sheet* | Total collateral |
| **Current balances with central banks** | **103,245** | **x** | **103,245** | **0** | **x** | **0** |
| **Financial assets at fair value through profit or loss** | **29,709** | **x** | **29,709** | **0** | **x** | **0** |
| **Positive fair value of hedging financial derivatives** | **22,331** | **x** | **22,331** | **0** | **x** | **0** |
| **Available-for-sale financial assets** | **39,420** | **x** | **39,420** | **0** | **x** | **0** |
| **Amounts due from banks** | **51,791** | **1,141** | **52,932** | **10,901** | **54** | **10,955** |
| **Loans and advances to customers** | **595,781** | **149,153** | **744,934** | **268,247** | **13,407** | **281,654** |
| – Individuals | 275,528 | 30,590 | 306,118 | 200,334 | 4,053 | 204,387 |
| of which: mortgage loans | 207,823 | 16,150 | 223,973 | 172,421 | 3,965 | 176,386 |
| consumer loans | 27,938 | 2,273 | 30,211 | 4,941 | 4 | 4,945 |
| constructions savings scheme loans | 36,345 | 5,053 | 41,398 | 22,971 | 85 | 23,056 |
| – Corporates** | 316,676 | 118,563 | 435,239 | 67,913 | 9,354 | 77,267 |
| of which: top corporate clients | 136,723 | 74,786 | 211,509 | 36,036 | 4,309 | 40,345 |
| – Debt securities | 3,193 | x | 3,193 | 0 | x | 0 |
| – Other amounts due from customers | 384 | x | 384 | 0 | x | 0 |
| **Revaluation differences on portfolios hedge items** | **32** | **x** | **32** | **0** | **x** | **0** |
| **Held-to-maturity investments** | **65,462** | **x** | **65,462** | **0** | **x** | **0** |
| **Total** | **907,771** | **150,294** | **1,058,065** | **279,148** | **13,461** | **292,609** |

* Undrawn amounts, commitments, guarantees, etc.
** This item also includes loans provided to individual entrepreneurs.

The maximum credit exposure is presented on a gross basis (i.e. without the impact of allowances).

*The Group's maximum credit exposure as of 31 December 2015:*

| | Total exposure | | | Collateral applied | | |
|---|---|---|---|---|---|---|
| (CZKm) | Statement of financial position | Off-balance sheet* | Total credit exposure | Statement of financial position | Off-balance sheet* | Total collateral |
| **Current balances with central banks** | **116,979** | **x** | **116,979** | **0** | **x** | **0** |
| **Financial assets at fair value through profit or loss** | **29,198** | **x** | **29,198** | **0** | **x** | **0** |
| **Positive fair value of hedging financial derivatives** | **23,701** | **x** | **23,701** | **0** | **x** | **0** |
| **Available-for-sale financial assets** | **41,864** | **x** | **41,864** | **0** | **x** | **0** |
| **Amounts due from banks** | **47,817** | **1,575** | **49,392** | **14,573** | **269** | **14,842** |
| **Loans and advances to customers** | **548,451** | **135,015** | **683,466** | **247,146** | **14,624** | **261,770** |
| – Individuals | 247,860 | 23,490 | 271,350 | 180,120 | 3,213 | 183,333 |
| of which: mortgage loans | 185,151 | 11,673 | 196,824 | 153,097 | 3,094 | 156,191 |
| consumer loans | 24,680 | 2,346 | 27,026 | 4,632 | 17 | 4,649 |
| constructions savings scheme loans | 34,416 | 2,563 | 36,979 | 22,311 | 63 | 22,374 |
| – Corporates** | 296,723 | 111,525 | 408,248 | 67,026 | 11,411 | 78,437 |
| of which: top corporate clients | 125,160 | 70,943 | 196,103 | 34,682 | 7,385 | 42,067 |
| – Debt securities | 3,654 | x | 3,654 | 0 | x | 0 |
| – Other amounts due from customers | 214 | x | 214 | 0 | x | 0 |
| **Revaluation differences on portfolios hedge items** | **18** | **x** | **18** | **0** | **x** | **0** |
| **Held-to-maturity investments** | **67,083** | **x** | **67,083** | **0** | **x** | **0** |
| **Total** | **875,111** | **136,590** | **1,011,701** | **261,719** | **14,893** | **276,612** |

* Undrawn amounts, commitments, guarantees, etc.
** This item also includes loans provided to individual entrepreneurs.

The maximum credit exposure is presented on a gross basis (i.e. without the impact of allowances).

### Classification of receivables

The Group classifies its receivables arising from financial activities into five categories in accordance with CNB Regulation No. 163/2014. The Standard and Watch categories represent non-default while Substandard, Doubtful and Loss represent default. The classification reflects both quantitative criteria (payment discipline, financial data) and qualitative criteria (e.g. in-depth client knowledge). The classification of individuals reflects also the default sharing principle for co-debtors and guarantors of defaulted receivables in accordance with the Basel III principles.

The structure of the credit portfolio according to the classification is regularly reported to the CNB and to investors.

When forbearance measures are granted, the forborne exposures receive default status (i.e. are classified as Substandard, Doubtful or Loss according to the CNB classification). The forbearance classification discontinues after fulfilment of the pre-defined conditions:

I. In the first place, after 12 months reclassification to the performing forborne exposures (i.e. those classified as Standard or Watch) is possible based on an analysis of the debtor's financial condition;
II. Followed by a minimum 2-year probation period.

In addition, proper payments must be made throughout the probation period (i.e. the material days past due with materiality being set identically as for defaulted receivables), must not exceed 30 days. Otherwise the exposure is downgraded back into default status.

### Characteristics of receivables that are not classified

Pursuant to the regulation issued by the CNB, the Group does not classify other amounts due from customers. These amounts consist of non-credit receivables that principally originated from the payment system, fraudulent withdrawals, bank cheques, receivables associated with purchases of securities (on behalf of clients) that have not been settled, and receivables that arise from business arrangements that do not represent financial activities, specifically receivables arising from outstanding rental payments on non-residential premises, sale of real estate and prepayments made.

### Allowances for receivables

Depending on the client segment, materiality, risk profile and specificity of the receivables, allowances are calculated either: (i) taking into account the present value of expected future cash flows while considering all available information, including the estimated value of collateral foreclosure and the expected duration of the recovery process; or (ii) according to models using historical delinquency statistics regularly updated based on the latest loss observations and new risk drivers reflecting the phase of the business cycle; or (iii) using models based on probabilities of default and loss given default until the impairment event occurs and an individual or model allowances for impaired loans are recognised.

*The following table shows the split of customer loans (Substandard, Doubtful and Loss) based on the type of assessment:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Individually | Statistical model | Individually | Statistical model |
| Individuals | 1,942 | 7,847 | 2,127 | 9,216 |
| Corporates* | 10,032 | 2,584 | 10,107 | 1,747 |
| **Total** | **11,974** | **10,431** | **12,234** | **10,963** |

* This item also includes loans granted to individual entrepreneurs.

*As of 31 December 2016, the Group reported the following loans not past due and past due loans not impaired:*

| | Loans | Past due loans, not impaired | | | | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | not past due | 1 to 29 days | 30 to 59 days | 60 to 89 days | 90 days to 1 year | Over 1 year | Total | Total |
| **Banks** | | | | | | | | |
| – Standard | 49,839 | 179 | 0 | 0 | 0 | 0 | 179 | 50,018 |
| – Watch | 1,773 | 0 | 0 | 0 | 0 | 0 | 0 | 1,773 |
| **Total** | **51,612** | **179** | **0** | **0** | **0** | **0** | **179** | **51,791** |
| **Customers** | | | | | | | | |
| – Standard | 555,997 | 4,220 | 116 | 120 | 0 | 0 | 4,456 | 560,453 |
| – Watch | 7,959 | 746 | 506 | 135 | 0 | 0 | 1,387 | 9,346 |
| **Total** | **563,956** | **4,966** | **622** | **255** | **0** | **0** | **5,843** | **569,799** |

*As of 31 December 2015, the Group reported the following loans not past due and past due loans not impaired:*

| | Loans | Past due loans, not impaired | | | | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | not past due | 1 to 29 days | 30 to 59 days | 60 to 89 days | 90 days to 1 year | Over 1 year | Total | Total |
| **Banks** | | | | | | | | |
| – Standard | 45,529 | 0 | 0 | 0 | 0 | 0 | 0 | 45,529 |
| – Watch | 2,288 | 0 | 0 | 0 | 0 | 0 | 0 | 2,288 |
| **Total** | **47,817** | **0** | **0** | **0** | **0** | **0** | **0** | **47,817** |
| **Customers** | | | | | | | | |
| – Standard | 508,156 | 3,940 | 468 | 80 | 0 | 0 | 4,488 | 512,644 |
| – Watch | 7,076 | 293 | 1,183 | 189 | 1 | 0 | 1,666 | 8,742 |
| **Total** | **515,232** | **4,233** | **1,651** | **269** | **1** | **0** | **6,154** | **521,386** |

The amount of the collateral applied in respect of past due loans not impaired was CZK 2,610 million (2015: CZK 2,766 million).

### Loan collateral

The Group uses collateral as one of its techniques for mitigating credit risk. The risk management related to collateralisation is performed by departments within the Risk Management Arm independently of the Group's business lines.

The Group has fully implemented in its internal system the rules for assessing collateral's eligibility according to CNB Regulation No. 163/2014. In compliance with the CNB validation the Group uses the Advanced Internal Ratings-Based (A-IRB) approach. For clients of the Slovak branch, the Group uses the Standardised (STD) approach for assessing collateral eligibility.

The recognised value of collateral is set based on the Group's internal rules for collateral valuation and discounting. The methods used in defining values and discounts take into account all relevant risks, the expected cost of collateral sale, length of sale, the historical experience of the Group, as well as collateral eligibility according to the CNB regulation, bankruptcy/insolvency rules and other regulations. Specifically, for all real estate collateral, which is the most common type of collateral, the Group uses independent valuations performed or supervised by a dedicated specialised department. Collateral values reflected in the calculation of capital requirements and other processes (regulatory exposure management, granting process, creation of provisions and reserves) involve the fulfilment of collateral eligibility according to CNB Regulation No. 163/2014.

The Group (except for the Slovak branch) uses the on-line connection to the Real Estate Register for reviewing and acquiring data on pledged real estates in granting mortgages or other loans secured by real estate and for regular monitoring of selected events that may put the Group's pledge right to real estate at risk.

### Real estate collateral valuation

Activities related to the valuation of real estates obtained as collaterals for corporate and retail loans are independent from the Group's business processes. The valuation process is managed and controlled by a specialised internal department which co-operates with various external valuation experts.

In 2016, together with the principal activity involving real estate valuation, the Group focused mainly upon ongoing monitoring of the real estate market with the aim to promptly identify any adverse development and to take appropriate measures as required. The Group monitors both the residential and commercial real estate markets. An integral component of that monitoring is the revaluation of selected real estates depending on the Basel III requirements. As a result of the statistical monitoring of market prices for residential real estates, adjustment is performed regularly.

### Recovery of receivables from borrowers

The Group continuously responded to the changing legal environment and its impact on the collection of receivables. Given the size of the portfolio in recovery, the Group is continuously improving the efficiency and process of recovery. These efforts also involve intensified and enhanced use of external recovery capacities. During 2016, the Group continued in regular sales of uncollateralised retail receivables to selected qualified investors so that the maximum achievable recovery rate is obtained.

The Group paid increased attention to the application of the Insolvency Act and its impact on the process of collecting receivables from retail and corporate clients. The Group plays an active role in the insolvency process, from the position of secured creditor, creditors' committee member or representative of creditors, whether in bankruptcy proceedings or in reorganisations, which are used by the Group depending on the debtor's circumstances and the attitudes of other creditors.

### Credit risk hedging instruments

The Group has not entered into any credit derivative transactions to hedge or reallocate its credit exposures.

### Credit risk of financial derivatives

The daily calculation of counterparty risk associated with financial derivatives is based on the Credit Value at Risk (CVaR) indicator. This indicator projects the potential adverse development of the market value of a derivative and the potential loss that the Group may incur if the counterparty fails to fulfil its obligations. The maximum potential exposure is calculated at the 99% probability level and depends on the current market value and type of derivative product, the remaining time until maturity of the derivative transaction, as well as the nominal value and volatility of the underlying assets.

As of 31 December 2016, the Group was exposed to a credit exposure of CZK 23,021 million (2015: CZK 30,945 million) on financial derivative instruments (expressed in CVaR). This amount represents the gross replacement cost at market rates as of 31 December 2016 for all outstanding agreements. The netting agreement and parameters of collateral agreement are taken into account where applicable.

The Group puts limits on exposures to counterparties from financial derivatives in order to avoid excessive credit exposures to each clients which could arise from movements in market prices. On a daily basis, the Group monitors compliance with limits. If these are exceeded, an appropriate alert is triggered and action is taken when relevant. In the event that the limit breach is triggered by the deliberate action of a dealer ("active limit breach"), such behaviour is penalised. The Board of Directors is informed about active limit breaches on a regular basis.

## (B) Market risk

### Segmentation of the Group's financial operations

For market risk management purposes, the Group's activities are internally separated into two books: the Market Book and the Structural Book. The Market Book consists of transactions initiated by the investment banking activities and the treasury desk (interbank and individually priced deposits/loans, repos/reverse repos, securities classified as held for trading, derivatives originated by investment banking). The Structural Book consists principally of business transactions (lending, accepting deposits, amounts due to and from customers), hedging transactions within the Structural Book, and other transactions not included in the Market Book.

### Products generating market risk

Products that are traded by the Group and generate market risks include interbank loans and deposits, currency transactions (spots, swaps, forwards), interest rate instruments (interest rate swaps, cross currency swaps, forward rate agreements, interest rate futures and futures on debt securities), government and corporate bonds, bills of exchange programmes and cash and carry exposure in emission allowances.

More complex derivatives (options, commodity derivatives, structured derivatives) which are being sold to clients, are immediately offset on the market by doing "back-to-back" trades in the interbank market mostly with Société Générale. This ensures that the Group is not exposed to market risks associated with these derivatives (e.g. volatility risk, correlation risk).

### Market risk in the Market Book

The Group has developed a complex system of market risk limits with the objective of limiting potential losses due to movements in market prices by limiting the size of the risk exposure.

Since 2016, in addition to measuring and limiting the market risk at the level of Market Book as whole, the Group measures and limits the market risks for the trading activities and the treasury activities separately.

The Group monitors compliance with all limits on a daily basis, and if these are exceeded the Group takes corrective action to reduce the risk exposure. The Board of Directors is informed on a quarterly basis about developments in the exposure to market risk.

In order to measure market risks inherent in the activities of the Market Book, the Group uses the one-day historical 99% Value-at-Risk (hereafter only "VaR") concept. VaR is calculated using full revaluation of the position by means of historical market price scenarios. This method reflects correlations between various financial markets and underlying instruments on a non-parametric basis, inasmuch as it uses scenarios simulating one-day variations of relevant market parameters over a period of time limited to the past 260 business days. The resulting 99% VaR indicator captures the loss that would be incurred after eliminating the 1% of the most unfavourable occurrences. This estimate is calculated as the average of the second and the third largest potential losses out of the 260 considered scenarios.

The VaR for a one-day horizon with a confidence level of 99% was CZK -16 million as of 31 December 2016 (2015: CZK -16 million). The average VaR was CZK -16 million in 2016 (2015: CZK -17 million).

The accuracy of the VaR model is validated through a back-testing calculation, whereby actual trading results and hypothetical results (i.e. results excluding deals closed during the day) are compared with the VaR results. Actual results should not exceed VaR more frequently than 1% of days within a given period.

In addition, the Group performs stress tests on a daily basis which capture losses potentially generated by larger shocks. These stress events have a lower probability of occurrence than do VaR scenarios, and they measure potential losses relevant to the risk exposure in the Market Book. Several types of stress tests for foreign exchange, interest rate and $CO_2$ allowance cash and carry exposures are used. These are developed either based on actual crisis situations in the past (such as the Greek crisis in 2010) or from a hypothetical crisis that could negatively influence the performance of the Market Book.

Additional specific metrics such as sensitivities to market parameters or size of exposure are used to obtain a detailed picture of risks and strategies.

The Group complies with the Société Générale Group's VaR and stress tests methodology and uses Group's software for market risk management.

**Market risk in the Structural Book**
The Group manages foreign exchange risk so as to minimise risk exposures. In order to achieve this, the foreign exchange position of the Structural Book is measured on a daily basis and subsequently hedged under established rules. For the purpose of hedging foreign exchange positions within the Structural Book, the Group uses standard currency instruments in the interbank market, such as currency spots and forwards.

Interest rate risk within the Structural Book is monitored and measured using a static gap analysis, sensitivity of interest income to a parallel shift of the yield curve, and Earnings at Risk (hereafter only "EaR") for net interest income. The EaR indicator shows the maximum departure of the planned net interest income level from the initial value that is attributable to the movements in interest rates over a one-year time horizon and at the 99% confidence level.

The indicators are monitored separately for CZK, USD, EUR, and the sum of other foreign currencies.

The indicator of the Group's sensitivity to a change in market interest rates is measured upon the assumption of an instantaneous, one-off and adverse parallel shift of the market yield curve by 1% p.a. It is determined as the present value of the costs of closing out the Group's open interest rate position after the adverse change of interest rates occurred. As of 31 December 2016, the CZK interest rate risk sensitivity was CZK -875 million (2015: CZK -904 million), the EUR sensitivity was CZK 206 million (2015: CZK 139 million), the USD sensitivity was CZK 18 million (2015: CZK 25 million) and for other currencies it was CZK -4 million (2015: CZK -74 million) for the hypothetical assumption of a 1% change in market interest rates. The Group is limited by this indicator and the level of the limit is determined to be approximately 2% of capital.

In order to hedge against interest rate risk within the Structural Book, the Group uses both standard derivative instruments available in the interbank market (such as forward rate agreements and interest rate swaps) and appropriate investments into securities or a favourable selection of interest rate parameters for other assets and liabilities.

### (C) Financial derivatives

The Group operates a system of market risk and counterparty limits which are designed to restrict disproportionate exposures due to movements in market prices and counterparty concentrations. The Group also monitors adherence to all limits on a daily basis and follows up on any breaches of these limits and takes corrective action to reduce the risk exposure.

The following tables set out nominal and fair values of financial derivative instruments categorised as held for trading and hedging.

*Financial derivative instruments designated as held for trading are as follow:*

| | 31 Dec 2016 Nominal value | | 31 Dec 2015 Nominal value | | 31 Dec 2016 Fair value | | 31 Dec 2015 Fair value | |
|---|---|---|---|---|---|---|---|---|
| **(CZKm)** | **Assets** | **Liabilities** | **Assets** | **Liabilities** | **Positive** | **Negative** | **Positive** | **Negative** |
| **Interest rate instruments** | | | | | | | | |
| Interest rate swaps | 647,406 | 647,406 | 581,225 | 581,225 | 8,954 | 9,341 | 8,685 | 9,435 |
| Interest rate forwards and futures* | 2,986 | 2,986 | 23,107 | 23,107 | 1 | 0 | 2 | 2 |
| Interest rate options | 39,957 | 39,957 | 7,532 | 7,532 | 58 | 58 | 33 | 33 |
| **Total interest rate instruments** | **690,349** | **690,349** | **611,864** | **611,864** | **9,013** | **9,399** | **8,720** | **9,470** |
| **Foreign currency instruments** | | | | | | | | |
| Currency swaps | 203,110 | 203,209 | 166,808 | 166,682 | 1,966 | 2,017 | 1,058 | 966 |
| Cross currency swaps | 135,311 | 135,313 | 125,518 | 125,602 | 4,438 | 3,986 | 5,697 | 5,384 |
| Currency forwards | 52,186 | 51,845 | 29,885 | 29,761 | 377 | 295 | 294 | 229 |
| Purchased options | 66,709 | 66,895 | 58,646 | 59,099 | 1,276 | 0 | 984 | 0 |
| Sold options | 66,895 | 66,709 | 59,098 | 58,646 | 0 | 1,276 | 0 | 983 |
| **Total currency instruments** | **524,211** | **523,971** | **439,955** | **439,790** | **8,057** | **7,574** | **8,033** | **7,562** |
| **Other instruments** | | | | | | | | |
| Forwards on emission allowances | 4,194 | 4,052 | 4,570 | 4,978 | 400 | 260 | 68 | 472 |
| Commodity forwards | 4,162 | 4,162 | 2,590 | 2,590 | 148 | 145 | 68 | 66 |
| Commodity swaps | 9,079 | 9,079 | 13,912 | 13,912 | 622 | 605 | 1,588 | 1,570 |
| Purchased commodity options | 424 | 424 | 356 | 356 | 24 | 0 | 49 | 0 |
| Sold commodity options | 424 | 351 | 356 | 356 | 0 | 24 | 0 | 49 |
| **Total other instruments** | **18,283** | **18,068** | **21,784** | **22,192** | **1,194** | **1,034** | **1,773** | **2,157** |
| **Total** | **1,232,843** | **1,232,388** | **1,073,603** | **1,073,846** | **18,264** | **18,007** | **18,526** | **19,189** |

* Fair values include only forwards. Regarding futures the Group places funds on a margin account which is used on a daily basis to settle fair value changes. Receivables arising from these margin accounts are reported within other assets.

*Financial derivative instruments designated as held for trading are shown below at nominal values by remaining contractual maturity as of 31 December 2016:*

| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| **Interest rate instruments** | | | | |
| Interest rate swaps | 96,165 | 365,099 | 186,142 | 647,406 |
| Interest rate forwards and futures* | 2,986 | 0 | 0 | 2,986 |
| Interest rate options | 946 | 37,082 | 1,929 | 39,957 |
| **Total interest rate instruments** | **100,097** | **402,181** | **188,071** | **690,349** |
| **Foreign currency instruments** | | | | |
| Currency swaps | 200,604 | 2,506 | 0 | 203,110 |
| Cross currency swaps | 18,271 | 65,241 | 51,799 | 135,311 |
| Currency forwards | 40,265 | 11,921 | 0 | 52,186 |
| Purchased options | 38,442 | 28,267 | 0 | 66,709 |
| Sold options | 38,538 | 28,357 | 0 | 66,895 |
| **Total currency instruments** | **336,120** | **136,292** | **51,799** | **524,211** |
| **Other instruments** | | | | |
| Forwards on emission allowances | 2,281 | 1,913 | 0 | 4,194 |
| Commodity forwards | 4,162 | 0 | 0 | 4,162 |
| Commodity swaps | 7,059 | 2,020 | 0 | 9,079 |
| Purchased commodity options | 402 | 22 | 0 | 424 |
| Sold commodity options | 402 | 22 | 0 | 424 |
| **Total other instruments** | **14,306** | **3,977** | **0** | **18,283** |
| **Total** | **450,523** | **542,450** | **239,870** | **1,232,843** |

* The remaining contractual maturity of forward rate agreements (FRA) and futures covers the period to the fixing date when off-balance sheet exposures are reversed.

*Financial derivative instruments designated as held for trading are shown below at nominal values by remaining contractual maturity as of 31 December 2015:*

| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| **Interest rate instruments** | | | | |
| Interest rate swaps | 112,230 | 307,440 | 161,555 | 581,225 |
| Interest rate forwards and futures* | 23,107 | 0 | 0 | 23,107 |
| Interest rate options | 88 | 6,436 | 1,008 | 7,532 |
| **Total interest rate instruments** | **135,425** | **313,876** | **162,563** | **611,864** |
| **Foreign currency instruments** | | | | |
| Currency swaps | 165,242 | 1,566 | 0 | 166,808 |
| Cross currency swaps | 17,825 | 48,643 | 59,050 | 125,518 |
| Currency forwards | 26,129 | 3,756 | 0 | 29,885 |
| Purchased options | 31,865 | 26,781 | 0 | 58,646 |
| Sold options | 32,366 | 26,732 | 0 | 59,098 |
| **Total currency instruments** | **273,427** | **107,478** | **59,050** | **439,955** |
| **Other instruments** | | | | |
| Forwards on emission allowances | 1,610 | 2,960 | 0 | 4,570 |
| Commodity forwards | 2,590 | 0 | 0 | 2,590 |
| Commodity swaps | 12,090 | 1,822 | 0 | 13,912 |
| Purchased commodity options | 145 | 211 | 0 | 356 |
| Sold commodity options | 145 | 211 | 0 | 356 |
| **Total other instruments** | **16,580** | **5,204** | **0** | **21,784** |
| **Total** | **425,432** | **426,558** | **221,613** | **1,073,603** |

* The remaining contractual maturity of forward rate agreements (FRA) and futures covers the period to the fixing date when off-balance sheet exposures are reversed.

*Financial derivative instruments designated as hedging are as follows:*

| | 31 Dec 2016 Nominal value | | 31 Dec 2015 Nominal value | | 31 Dec 2016 Fair value | | 31 Dec 2015 Fair value | |
|---|---|---|---|---|---|---|---|---|
| **(CZKm)** | **Assets** | **Liabilities** | **Assets** | **Liabilities** | **Positive** | **Negative** | **Positive** | **Negative** |
| Cross currency swaps for cash flows hedging | 42,722 | 43,731 | 39,449 | 41,486 | 354 | 946 | 280 | 1,966 |
| Forwards on stocks for cash flow hedging | 49 | 49 | 49 | 49 | 1 | 1 | 9 | 0 |
| Interest rate swaps for cash flow hedging | 619,884 | 619,885 | 582,625 | 582,625 | 21,099 | 6,031 | 22,671 | 5,957 |
| Interest rate swaps for fair value hedging | 24,116 | 24,116 | 18,585 | 18,585 | 166 | 2,395 | 106 | 2,099 |
| Interest rate swaps for portfolio fair value hedging | 19,350 | 19,350 | 17,650 | 17,650 | 711 | 55 | 635 | 33 |
| **Total** | **706,121** | **707,131** | **658,358** | **660,395** | **22,331** | **9,428** | **23,701** | **10,055** |

*Remaining contractual maturities of derivatives designated as hedging are shown below as of 31 December 2016:*

| **(CZKm)** | **Up to 1 year** | **1 to 5 years** | **Over 5 years** | **Total** |
|---|---|---|---|---|
| Cross currency swaps for cash flow hedging | 8,235 | 33,254 | 1,233 | 42,722 |
| Forwards on stocks for cash flow hedging | 19 | 30 | 0 | 49 |
| Interest rate swaps for cash flow hedging | 104,258 | 297,424 | 218,202 | 619,884 |
| Interest rate swaps for fair value hedging | 0 | 6,289 | 17,827 | 24,116 |
| Interest rate swaps for portfolio fair value hedging | 950 | 10,000 | 8,400 | 19,350 |
| **Total** | **113,462** | **346,997** | **245,662** | **706,121** |

*Remaining contractual maturities of derivatives designated as hedging are shown below as of 31 December 2015:*

| **(CZKm)** | **Up to 1 year** | **1 to 5 years** | **Over 5 years** | **Total** |
|---|---|---|---|---|
| Cross currency swaps for cash flow hedging | 13,276 | 24,940 | 1,233 | 39,449 |
| Forwards on stocks for cash flow hedging | 21 | 28 | 0 | 49 |
| Interest rate swaps for cash flow hedging | 103,896 | 271,687 | 207,042 | 582,625 |
| Interest rate swaps for fair value hedging | 900 | 300 | 17,385 | 18,585 |
| Interest rate swaps for portfolio fair value hedging | 2,050 | 5,450 | 10,150 | 17,650 |
| **Total** | **120,143** | **302,405** | **235,810** | **658,358** |

*Shown below are the undiscounted cash flows from derivatives designated for cash flow hedging according to the periods within which they are expected to affect profit or loss:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| **(CZKm)** | **Up to 1 year** | **1 to 5 years** | **Over 5 years** | **Up to 1 year** | **1 to 5 years** | **Over 5 years** |
| Floating cash flows from cash flow hedging derivatives | (284) | (1,440) | (1,221) | (210) | (1,225) | (1,227) |

The Group treats as hedges only those contracts for which it is able to demonstrate that all criteria set out in IAS 39 for recognising the transactions as hedges have been met.

*During 2016, the Group recorded the following hedges:*

1. Interest rate risk hedging:
   a. The fair values of long-term loans provided and of investments into long-term government securities classified into the ***'Available-for-sale financial assets'*** portfolio and investments into long-term securities classified into the ***'Loans and advances to customers'*** portfolio are hedged by an interest rate swaps and a cross currency swap, respectively;
   b. The fair values of issued long-term mortgage bonds classified into the ***'Securities issued'*** portfolio are hedged by an interest rate swaps;
   c. The fair values of a portfolio of savings accounts from retail clients are hedged by a portfolio of interest rate swaps;
   d. The fair values of fixed rate deposits or repos are hedged by interest rate swaps;
   e. Future cash flows from a portfolio of current assets traded on the interbank market and from loans to clients with variable interest rates are hedged by a portfolio of interest rate swaps or cross currency swaps (cash flows will materialise on an ongoing basis and will also affect the Group's Statement of Income on an ongoing basis);
   f. Future cash flows from a portfolio of short-term liabilities traded on the interbank market and short term liabilities to clients are hedged by a portfolio of interest rate swaps (cash flows will materialise on an ongoing basis and will also affect the Group's Statement of Income on an ongoing basis).

2. Foreign exchange risk hedging:
   a. In selected material cases, the Group hedges the future cash flows of firm commitments arising from the Group's contractual obligations (e.g. contractual payments to third parties in a foreign currency) or receivables of the Group (e.g. dividends). The hedging instrument consists of foreign currency assets (e.g. securities, short-term loans on the interbank market) or foreign currency liabilities (e.g. short-term client liabilities), respectively;
   b. Visa shares transactions – hedging of future cash flows from selling of the Visa Europe stake for cash payment, hedging instruments were foreign currency liabilities (short-term client liabilities), the hedge relationship ended correctly in 2016. Hedging the fair value of newly issued Visa Inc. preferred shares, hedging instruments are foreign currency liabilities (short-term client liabilities).

3. Share price risk hedging:
   a. A portion of the bonus of selected Group employees is paid in cash equivalents of the Société Générale S.A. share price. The risk of change in the Société Générale S.A. share price is hedged at the Société Générale level. Hedging instruments are forwards on stocks. The hedge relationship ended correctly in 2016.;
   b. A portion of the bonus of selected Group employees is paid in cash equivalents of the Komerční banka, a.s. share price. The Group hedges the risk of change in the Komerční banka, a.s. share price. Hedging instruments are forwards on stocks.

4. Hedging of an investment in foreign subsidiaries:
   a. The foreign exchange risk associated with investments in subsidiaries is hedged by selected foreign currency liabilities (e.g. short-term client liabilities).

The Group does not report any instance of hedge accounting being applied to a highly probable forecasted transaction that is no longer anticipated to be effected.

Further information on hedges is provided in Notes 3, 5 and 7 to these Consolidated Financial Statements.

### (D) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The length of time for which the rate of interest is fixed on a financial instrument therefore indicates to what extent that instrument is exposed to interest rate risk. Market developments have led to a situation where interest rates are negative in certain currencies. This fact does not change the essence of interest rate risk measurement and management because the principle of recognising changes in interest rates over time remains unchanged just as the concept of hedging against interest rate risk by matching volumes with changing values within the given period remains valid. Due to legal and technical limitations, methods to prevent negative rates from being applied at the client's level can be applied with the objective of maintaining accordance between a transaction's contractual and economic natures. With respect to ongoing market practice, client deposits are seeing the introduction of deposit fees, which constitute a specific response to the existence of negative market interest rates and which also comply with the requirements given by limitations ensuing from the existing legal framework.

The Group uses internal models for managing interest rate risk. The objective of these models is to describe the expected economic behaviour of the Group's clients when market interest rates fluctuate. It is the policy of the Group's management to manage the exposure to fluctuations in net interest income arising from changes in interest rates through a gap analysis of assets and liabilities in individual groups. Further information about interest rate risk management is provided in Section (B) of this Note.

The table below provides information on the extent of the Group's interest rate exposure based either on the contractual maturity date of its financial instruments or, in the case of instruments that reprice to a market rate of interest before maturity, the next repricing date. Those assets and liabilities that do not have a contractual maturity or a repricing date were grouped into the *'Undefined'* category. The table includes an analysis of other assets and liabilities not within the scope of financial instruments as defined in IAS 32.

| (CZKm) | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Undefined | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and current balances with central banks | 112,241 | 0 | 0 | 0 | 0 | **112,241** |
| Financial assets at fair value through profit or loss | 11,445 | 0 | 0 | 0 | 18,264 | **29,709** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 22,331 | **22,331** |
| Available-for-sale financial assets | 304 | 11,034 | 10,073 | 18,009 | 0 | **39,420** |
| Assets held for sale | 0 | 0 | 0 | 0 | 906 | **906** |
| Amounts due from banks | 38,776 | 7,872 | 2,411 | 2,003 | 709 | **51,771** |
| Loans and advances to customers | 236,283 | 72,161 | 217,356 | 42,516 | 11,882 | **580,198** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 32 | **32** |
| Held-to-maturity investments | 0 | 3,612 | 29,023 | 32,827 | 0 | **65,462** |
| Current tax assets | 0 | 16 | 0 | 0 | 70 | **86** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 78 | **78** |
| Prepayments, accrued income and other assets | 0 | 668 | 0 | 0 | 4,251 | **4,919** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 1,280 | **1,280** |
| Intangible assets | 0 | 0 | 0 | 0 | 3,886 | **3,886** |
| Tangible assets | 0 | 0 | 0 | 0 | 6,666 | **6,666** |
| Goodwill | 0 | 0 | 0 | 0 | 3,752 | **3,752** |
| **Total assets** | **399,049** | **95,363** | **258,863** | **95,355** | **74,107** | **922,737** |
| **Liabilities** | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 160 | 0 | 0 | 0 | 18,007 | **18,167** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 9,428 | **9,428** |
| Amounts due to banks | 36,067 | 8,178 | 0 | 0 | 9,879 | **54,124** |
| Amounts due to customers | 52,073 | 22,049 | 22,053 | 4,899 | 598,303* | **699,377** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 762 | **762** |
| Securities issued | 1,968 | 8,929 | 1,745 | 781 | 0 | **13,423** |
| Current tax liabilities | 0 | 0 | 0 | 0 | 360 | **360** |
| Deferred tax liabilities | 0 | 0 | 30 | 0 | 3,800 | **3,830** |
| Accruals and other liabilities | 227 | 0 | 0 | 0 | 15,923 | **16,150** |
| Provisions | 0 | 0 | 0 | 0 | 1,714 | **1,714** |
| **Total liabilities** | **90,496** | **39,156** | **23,828** | **5,680** | **658,176** | **817,336** |
| **Statement of Financial Position interest rate gap as of 31 December 2016** | **308,553** | **56,207** | **235,035** | **89,675** | **(584,069)** | **105,401** |
| Nominal value of derivatives** | 570,590 | 263,724 | 372,420 | 324,998 | 0 | **1,531,732** |
| **Total off-balance sheet assets** | **570,590** | **263,724** | **372,420** | **324,998** | **0** | **1 531,732** |
| Nominal value of derivatives** | 690,976 | 257,911 | 402,152 | 181,705 | 0 | **1,532,744** |
| Undrawn portion of loans*** | (3,457) | (9,186) | 5,867 | 6,776 | 0 | **0** |
| Undrawn portion of revolving loans*** | (578) | 578 | 0 | 0 | 0 | **0** |
| **Total off-balance sheet liabilities** | **686,941** | **249,303** | **408,019** | **188,481** | **0** | **1,532,744** |
| **Net off-balance sheet interest rate gap as of 31 December 2016** | **(116,351)** | **14,421** | **(35,599)** | **136,517** | **0** | **(1,012)** |
| **Cumulative interest rate gap as of 31 December 2016** | **192,202** | **262,830** | **462,266** | **688,458** | **104,389** | **X** |

* This item principally includes client deposits where the Group has the option to reset interest rates and hence they are not sensitive to interest rate changes.
** Assets and liabilities arising from derivatives include interest rate swaps, interest rate forwards and futures, interest rate options and cross currency swaps.
*** Undrawn loans and revolving loans are reported on a net basis, that is, the Group reports both the expected drawings and repayments within one line. This line does not reflect commitments to extend loans with a fixed repayment schedule or commitments to provide a revolving loan inasmuch as the interest rate has not been determined for such commitments.

| (CZKm) | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Undefined | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and current balances with central banks | 128,336 | 0 | 0 | 0 | 0 | **128,336** |
| Financial assets at fair value through profit or loss | 7,186 | 3,487 | 0 | 0 | 18,525 | **29,198** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 23,701 | **23,701** |
| Available-for-sale financial assets | 4,343 | 8,234 | 17,225 | 12,062 | 0 | **41,864** |
| Assets held for sale | 0 | 0 | 0 | 0 | 385 | **385** |
| Amounts due from banks | 37,615 | 2,147 | 4,559 | 2,674 | 804 | **47,799** |
| Loans and advances to customers | 214,308 | 73,360 | 206,591 | 29,698 | 8,660 | **532,617** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 18 | **18** |
| Held-to-maturity investments | 6,344 | 48 | 19,567 | 41,124 | 0 | **67,083** |
| Current tax assets | 0 | 30 | 0 | 0 | 337 | **367** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 70 | **70** |
| Prepayments, accrued income and other assets | 0 | 698 | 0 | 0 | 3,738 | **4,436** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 1,219 | **1,219** |
| Intangible assets | 0 | 0 | 0 | 0 | 3,867 | **3,867** |
| Tangible assets | 0 | 0 | 0 | 0 | 6,844 | **6,844** |
| Goodwill | 0 | 0 | 0 | 0 | 3,752 | **3,752** |
| **Total assets** | **398,132** | **88,004** | **247,942** | **85,558** | **71,920** | **891,556** |
| **Liabilities** | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 305 | 0 | 0 | 0 | 19,189 | **19,494** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 16 | 0 | 10,039 | **10,055** |
| Amounts due to banks | 43,762 | 6,060 | 0 | 0 | 6,408 | **56,230** |
| Amounts due to customers | 59,845 | 18,093 | 25,950 | 1,609 | 550,790* | **656,287** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 610 | **610** |
| Securities issued | 6,234 | 4,015 | 10,282 | 872 | 0 | **21,403** |
| Current tax liabilities | 0 | 0 | 0 | 0 | 83 | **83** |
| Deferred tax liabilities | 0 | 0 | 37 | 0 | 4,547 | **4,584** |
| Accruals and other liabilities | 262 | 0 | 0 | 0 | 15,157 | **15,419** |
| Provisions | 0 | 0 | 0 | 0 | 1,161 | **1,161** |
| **Total liabilities** | **110,409** | **28,168** | **36,285** | **2,481** | **607,984** | **785,327** |
| **Statement of Financial Position interest rate gap as of 31 December 2015** | **287,723** | **59,836** | **211,657** | **83,077** | **(536,064)** | **106,229** |
| Nominal value of derivatives** | 505,961 | 284,007 | 300,023 | 305,700 | 0 | **1,395,691** |
| **Total off-balance sheet assets** | **505,961** | **284,007** | **300,023** | **305,700** | **0** | **1,395,691** |
| Nominal value of derivatives** | 608,839 | 264,426 | 342,061 | 182,486 | 0 | **1,397,812** |
| Undrawn portion of loans*** | (2,936) | (5,663) | 6,040 | 2,559 | 0 | **0** |
| Undrawn portion of revolving loans*** | 0 | 0 | 0 | 0 | 0 | **0** |
| **Total off-balance sheet liabilities** | **605,903** | **258,763** | **348,101** | **185,045** | **0** | **1,397,812** |
| **Net off-balance sheet interest rate gap as of 31 December 2015** | **(99,942)** | **25,244** | **(48,078)** | **120,655** | **0** | **(2,121)** |
| **Cumulative interest rate gap as of 31 December 2015** | **187,782** | **272,861** | **436,440** | **640,172** | **104,108** | **X** |

* This item principally includes client deposits where the Group has the option to reset interest rates and hence they are not sensitive to interest rate changes.
** Assets and liabilities arising from derivatives include interest rate swaps, interest rate forwards and futures, interest rate options and cross currency swaps.
*** Undrawn loans and revolving loans are reported on a net basis, that is, the Group reports both the expected drawings and repayments within one line. This line does not reflect commitments to extend loans with a fixed repayment schedule or commitments to provide a revolving loan inasmuch as the interest rate has not been determined for such commitments.

*Average interest rates as of 31 December 2016 and 2015 were as follows:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| | **CZK** | **USD** | **EUR** | **CZK** | **USD** | **EUR** |
| **Assets** | | | | | | |
| Cash and current balances with central banks | 0.05% | x | x | 0.04% | x | x |
| Treasury bills | 0.00% | x | x | 0.01% | x | x |
| Amounts due from banks | 0.08% | 1.27% | 0.14% | 0.06% | 0.92% | 0.39% |
| Loans and advances to customers | 2.37% | 2.80% | 1.66% | 2.53% | 2.39% | 1.87% |
| Interest-earning securities | 1.63% | 0.00% | 1.34% | 1.39% | 0.00% | 1.48% |
| **Total assets** | **1.33%** | **1.36%** | **1.14%** | **1.55%** | **1.40%** | **1.37%** |
| **Total interest-earning assets** | **1.76%** | **1.85%** | **1.18%** | **1.80%** | **1.70%** | **1.40%** |
| **Liabilities** | | | | | | |
| Amounts due to central banks and banks | 0.07% | 0.73% | 0.40% | 0.04% | 0.86% | 0.43% |
| Amounts due to customers | 0.16% | 0.03% | 0.02% | 0.04% | 0.02% | 0.05% |
| Debt securities | 3.06% | 0.97% | 0.16% | 3.72% | 1.27% | 0.42% |
| **Total liabilities** | **0.16%** | **0.08%** | **0.16%** | **0.25%** | **0.15%** | **0.17%** |
| **Total interest-bearing liabilities** | **0.17%** | **0.09%** | **0.17%** | **0.26%** | **0.16%** | **0.19%** |
| **Off-balance sheet assets** | | | | | | |
| Nominal value of derivatives (interest rate swaps, options, etc.) | 0.95% | 2.64% | 0.71% | 1.09% | 2.62% | 1.03% |
| Undrawn portion of loans | 1.55% | 0.00% | 1.75% | 1.90% | 2.25% | 1.48% |
| Undrawn portion of revolving loans | 4.90% | 1.29% | 0.29% | 5.62% | x | 0.29% |
| **Total off-balance sheet assets** | **1.18%** | **2.62%** | **0.71%** | **1.32%** | **2.60%** | **1.02%** |
| **Off-balance sheet liabilities** | | | | | | |
| Nominal value of derivatives (interest rate swaps, options, etc.) | 0.71% | 2.32% | 0.63% | 0.79% | 2.23% | 1.04% |
| Undrawn portion of loans | 1.55% | 0.00% | 1.75% | 1.90% | 2.25% | 1.48% |
| Undrawn portion of revolving loans | 4.90% | 1.29% | 0.29% | 5.62% | x | 0.29% |
| **Total off-balance sheet liabilities** | **0.96%** | **2.31%** | **0.63%** | **1.04%** | **2.21%** | **1.03%** |

Note: The above table sets out the average interest rates for December 2016 and 2015 calculated as a weighted average for each asset and liability category.

The 2W repo rate announced by the CNB remained at the level of 0.05% throughout 2016. Czech crown money market rates (PRIBOR) decreased by as much as 0.03% (1–12M). Interest rates in the derivatives market decreased by 0.10-0.17% (2–10Y).

Euro money market rates decreased during 2016 by as much as 0.14% (3–6M) to 0.19% (1Y). Derivative market rates decreased by as much as 0.12% (2Y) to 0.29% (10Y).

Dollar money market rates increased during 2016 by as much as 0.52% (12M), and derivative market rates increased by as much as 0.22% (10Y) to 0.33% (2Y).

*Following is a breakdown of financial assets and liabilities by their exposure to interest rate fluctuations:*

| | 31 Dec 2016 | | | | 31 Dec 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | Fixed interest rate | Floating interest rate | No interest | Total | Fixed interest rate | Floating interest rate | No interest | Total |
| **Assets** | | | | | | | | |
| Cash and current balances with central banks | 0 | 101,539 | 10,702 | **112,241** | 13,800 | 101,201 | 13,335 | **128,336** |
| Financial assets at fair value through profit or loss | 7,466 | 2,140 | 20,103 | **29,709** | 6,846 | 1,026 | 21,326 | **29,198** |
| Positive fair values of hedging financial derivatives | 5 | 0 | 22,326 | **22,331** | 0 | 0 | 23,701 | **23,701** |
| Available-for-sale financial assets | 25,577 | 13,661 | 182 | **39,420** | 27,094 | 14,095 | 675 | **41,864** |
| Amounts due from banks | 9,642 | 41,877 | 252 | **51,771** | 8,160 | 39,556 | 83 | **47,799** |
| Loans and advances to customers | 364,762 | 210,617 | 4,819 | **580,198** | 339,959 | 188,112 | 4,546 | **532,617** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 32 | **32** | 0 | 0 | 18 | **18** |
| Held-to-maturity investments | 65,462 | 0 | 0 | **65,462** | 67,083 | 0 | 0 | **67,083** |
| **Liabilities** | | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | **1** | 1 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 0 | 0 | 18,167 | **18,167** | 0 | 0 | 19,494 | **19,494** |
| Negative fair values of hedging financial derivatives | 1 | 0 | 9,427 | **9,428** | 16 | 0 | 10,039 | **10,055** |
| Amounts due to banks | 25,931 | 27,158 | 1,035 | **54,124** | 13,947 | 42,114 | 169 | **56,230** |
| Amounts due to customers | 61,749 | 632,179* | 5,449 | **699,377** | 65,740 | 583,730* | 6,817 | **656,287** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 762 | **762** | 0 | 0 | 610 | **610** |
| Securities issued | 3,532 | 9,891 | 0 | **13,423** | 172 | 21,213 | 18 | **21,403** |

Note: Individual assets and liabilities are split into the categories of 'Fixed interest rate', 'Floating interest rate', and 'No interest' according to contractual parameters defining the interest rate structure. For this purpose, a fixed interest rate is defined as a rate with a repricing period exceeding one year. Products having no parameters defining their interest rate structure are included in the 'No interest' category.

* This item principally includes client deposits where the Group has the option to reset interest rates and hence they are not sensitive to interest rate changes.

## (E) Liquidity risk

Liquidity risk is a measure of the extent to which the Group may be required to raise funds to meet its commitments associated with financial instruments.

Liquidity risk management is based upon the liquidity risk management system approved by the Bank's Board of Directors. Liquidity is monitored on a bank-wide level, with the Market Book also having a standalone limit. The Group has established its liquidity risk management rules such that it maintains its liquidity profile in normal conditions (basic liquidity scenario) and in crisis conditions (crisis liquidity scenario). As such, the Group has defined a set of indicators for which binding limits are established.

The Group is exposed to daily calls on its available cash resources from derivatives, overnight deposits, current accounts, maturing deposits, loan draw-downs and guarantees. The Group's experiences show that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Group sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of interbank and other borrowing facilities (mainly reverse repo transactions with CNB) that should be in place to cover withdrawals at unexpected levels of demand.

The liquidity risk of the Group is managed as stipulated above (and in particular not on the basis of undiscounted cash flows).

The table below provides a breakdown of assets, liabilities and equity into relevant maturity groupings based on the remaining period from the financial statements date to the contractual maturity date. The table includes an analysis of other assets and liabilities not within the scope of financial instruments as defined in IAS 32.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and current balances with central banks | 17,503 | 0 | 0 | 0 | 0 | 94,738 | **112,241** |
| Financial assets at fair value through profit or loss | 700 | 593 | 1,389 | 4,424 | 1,727 | 20,876 | **29,709** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 22,331 | **22,331** |
| Available-for-sale financial assets | 0 | 20 | 6,137 | 9,993 | 20,696 | 2,574 | **39,420** |
| Assets held for sale | 0 | 0 | 878 | 0 | 0 | 28 | **906** |
| Amounts due from banks | 9,202 | 25,214 | 3,399 | 7,639 | 325 | 5,992 | **51,771** |
| Loans and advances to customers, net | 3,643 | 62,322 | 55,317 | 175,441 | 266,046 | 17,429 | **580,198** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 0 | 32 | **32** |
| Held-to-maturity investments | 0 | 353 | 4,281 | 28,499 | 32,329 | 0 | **65,462** |
| Current tax assets | 0 | 0 | 25 | 0 | 0 | 61 | **86** |
| Deferred tax assets | 0 | 0 | 6 | 0 | 0 | 72 | **78** |
| Prepayments, accrued income and other assets | 120 | 484 | 663 | 0 | 0 | 3,652 | **4,919** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 0 | 1,280 | **1,280** |
| Intangible assets | 0 | 0 | 0 | 0 | 0 | 3,886 | **3,886** |
| Tangible assets | 0 | 0 | 0 | 0 | 0 | 6,666 | **6,666** |
| Goodwill | 0 | 0 | 0 | 0 | 0 | 3,752 | **3,752** |
| **Total assets** | **31,168** | **88,986** | **72,095** | **225,996** | **321,123** | **183,369** | **922,737** |
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 160 | 0 | 0 | 0 | 0 | 18,007 | **18,167** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 9,428 | **9,428** |
| Amounts due to banks | 12,784 | 6,865 | 4,925 | 19,754 | 9,796 | 0 | **54,124** |
| Amounts due to customers | 608,288 | 41,300 | 21,612 | 23,251 | 4,858 | 68 | **699,377** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 0 | 762 | **762** |
| Securities issued | 279 | 1,506 | 629 | 1,741 | 9,268 | 0 | **13,423** |
| Current tax liabilities | 0 | 358 | 0 | 0 | 0 | 2 | **360** |
| Deferred tax liabilities | 0 | 0 | 1 | 29 | 0 | 3,800 | **3,830** |
| Accruals and other liabilities | 13,730 | 749 | 0 | 0 | 0 | 1,671 | **16,150** |
| Provisions | 11 | 171 | 762 | 268 | 4 | 498 | **1,714** |
| Equity | 0 | 0 | 0 | 0 | 0 | 105,401 | **105,401** |
| **Total liabilities** | **635,253** | **50,949** | **27,929** | **45,043** | **23,926** | **139,637** | **922,737** |
| **Statement of Financial Position liquidity gap as of 31 December 2016** | **(604,085)** | **38,037** | **44,166** | **180,953** | **297,197** | **43,732** | **0** |
| Off-balance sheet assets* | 50,043 | 178,351 | 131,043 | 169,546 | 53,033 | 0 | **582,016** |
| Off-balance sheet liabilities* | 58,444 | 199,204 | 186,553 | 214,975 | 57,647 | 16,704 | **733,527** |
| **Net off-balance sheet liquidity gap as of 31 December 2016** | **(8,401)** | **(20,853)** | **(55,510)** | **(45,429)** | **(4,614)** | **(16,704)** | **(151,511)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from FX spot, fixed term and option contracts and payables under guarantees, letters of credit and committed facilities.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and current balances with central banks | 38,268 | 0 | 0 | 0 | 0 | 90,068 | **128,336** |
| Financial assets at fair value through profit or loss | 0 | 1,562 | 2,371 | 2,612 | 635 | 22,018 | **29,198** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 23,701 | **23,701** |
| Available-for-sale financial assets | 0 | 2,480 | 326 | 15,703 | 20,208 | 3,147 | **41,864** |
| Assets held for sale | 0 | 0 | 360 | 0 | 0 | 25 | **385** |
| Amounts due from banks | 2,735 | 26,784 | 2,325 | 8,219 | 1,292 | 6,444 | **47,799** |
| Loans and advances to customers | 4,310 | 54,233 | 61,443 | 155,833 | 239,966 | 16,832 | **532,617** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 0 | 18 | **18** |
| Held-to-maturity investments | 0 | 6,460 | 1,088 | 19,083 | 40,452 | 0 | **67,083** |
| Current tax assets | 0 | 28 | 305 | 0 | 0 | 34 | **367** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 0 | 70 | **70** |
| Prepayments, accrued income and other assets | 389 | 366 | 692 | 0 | 0 | 2,989 | **4,436** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 0 | 1,219 | **1,219** |
| Intangible assets | 0 | 0 | 0 | 0 | 0 | 3,867 | **3,867** |
| Tangible assets | 0 | 0 | 0 | 0 | 0 | 6,844 | **6,844** |
| Goodwill | 0 | 0 | 0 | 0 | 0 | 3,752 | **3,752** |
| **Total assets** | **45,702** | **91,913** | **68,910** | **201,450** | **302,553** | **181,028** | **891,556** |
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 305 | 0 | 0 | 0 | 0 | 19,189 | **19,494** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 16 | 0 | 10,039 | **10,055** |
| Amounts due to banks | 23,126 | 4,685 | 9,087 | 12,167 | 7,165 | 0 | **56,230** |
| Amounts due to customers | 568,376 | 44,705 | 15,803 | 25,822 | 1,565 | 16 | **656,287** |
| Revaluation differences on portfolios hedge items | 0 | 0 | 0 | 0 | 0 | 610 | **610** |
| Securities issued | 8 | 5,715 | 4,418 | 1,756 | 9,506 | 0 | **21,403** |
| Current tax liabilities | 0 | 0 | 62 | 0 | 0 | 21 | **83** |
| Deferred tax liabilities | 0 | 0 | 0 | 38 | 0 | 4,546 | **4,584** |
| Accruals and other liabilities | 12,947 | 747 | 0 | 0 | 0 | 1,725 | **15,419** |
| Provisions | 8 | 110 | 269 | 354 | 1 | 419 | **1,161** |
| Equity | 0 | 0 | 0 | 0 | 0 | 106,229 | **106,229** |
| **Total liabilities** | **604,770** | **55,963** | **29,639** | **40,153** | **18,237** | **142,794** | **891,556** |
| **Statement of Financial Position liquidity gap as of 31 December 2015** | **(559,068)** | **35,950** | **39,271** | **161,297** | **284,316** | **38,234** | **0** |
| Off-balance sheet assets* | 49,522 | 151,449 | 88,241 | 132,405 | 60,284 | 0 | **481,901** |
| Off-balance sheet liabilities* | 56,215 | 174,045 | 139,122 | 170,597 | 64,340 | 16,047 | **620,366** |
| **Net off-balance sheet liquidity gap as of 31 December 2015** | **(6,693)** | **(22,596)** | **(50,881)** | **(38,192)** | **(4,056)** | **(16,047)** | **(138,465)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from FX spot, fixed term and option contracts and payables under guarantees, letters of credit and committed facilities.

The table below contains the remaining contractual maturities of non-derivative financial liabilities and contingent liabilities of the Group based on the undiscounted cash flows as of 31 December 2016.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss (except derivatives) | 160 | 0 | 0 | 0 | 0 | 0 | **160** |
| Amounts due to banks | 14,142 | 10,025 | 7,382 | 24,072 | 10,261 | 0 | **65,882** |
| Amounts due to customers | 608,292 | 41,417 | 21,709 | 24,272 | 5,213 | 136 | **701,039** |
| Securities issued | 279 | 1,518 | 1,155 | 1,850 | 9,295 | 0 | **14,097** |
| Current tax liabilities | 0 | 357 | 1 | 0 | 0 | 2 | **360** |
| Deferred tax liabilities | 0 | 0 | 1 | 29 | 0 | 3,803 | **3,833** |
| Accruals and other liabilities | 13,729 | 788 | 0 | 0 | 0 | 2,141 | **16,658** |
| Provisions | 11 | 171 | 763 | 268 | 4 | 501 | **1,718** |
| **Total non-derivative financial liabilities** | **636,614** | **54,276** | **31,011** | **50,491** | **24,773** | **6,583** | **803,748** |
| Other loans commitment granted | 6,808 | 13,696 | 35,850 | 24,769 | 1,342 | 16,620 | **99,085** |
| Guarantee commitments granted | 1,135 | 7,185 | 19,386 | 20,119 | 3,300 | 84 | **51,209** |
| **Total contingent liabilities** | **7,943** | **20,881** | **55,236** | **44,888** | **4,642** | **16,704** | **150,294** |

The table below contains the remaining contractual maturities of non-derivative financial liabilities and contingent liabilities of the Group based on the undiscounted cash flows as of 31 December 2015.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss (except derivatives) | 305 | 0 | 0 | 0 | 0 | 0 | **305** |
| Amounts due to banks | 23,101 | 4,649 | 9,067 | 12,403 | 7,185 | 0 | **56,405** |
| Amounts due to customers | 568,468 | 45,028 | 15,988 | 27,502 | 1,807 | 16 | **658,809** |
| Securities issued | 140 | 5,767 | 4,636 | 2,907 | 9,972 | 0 | **23,422** |
| Current tax liabilities | 0 | 0 | 62 | 0 | 0 | 21 | **83** |
| Deferred tax liabilities | 0 | 0 | 0 | 38 | 0 | 4,546 | **4,584** |
| Accruals and other liabilities | 12,947 | 747 | 0 | 0 | 0 | 1,725 | **15,419** |
| Provisions | 7 | 110 | 269 | 355 | 1 | 419 | **1,161** |
| **Total non-derivative financial liabilities** | **604,969** | **56,301** | **30,022** | **43,205** | **18,965** | **6,727** | **760,189** |
| Other loans commitment granted | 5,172 | 14,817 | 32,125 | 18,729 | 1,649 | 15,972 | **88,464** |
| Guarantee commitments granted | 1,556 | 7,861 | 17,596 | 18,567 | 2,471 | 75 | **48,126** |
| **Total contingent liabilities** | **6,728** | **22,678** | **49,721** | **37,296** | **4,120** | **16,047** | **136,590** |

## (F) Foreign exchange position

The table below provides an analysis of the Group's main currency exposures. The remaining currencies are shown within *'Other currencies'*. The Group manages its foreign exchange position on a daily basis. For this purpose, the Group has a set of internal limits.

| (CZKm) | CZK | EUR | USD | Other currencies | Total |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash and current balances with central banks | 110,351 | 1,250 | 325 | 315 | **112,241** |
| Financial assets at fair value through profit or loss | 23,884 | 5,505 | 314 | 6 | **29,709** |
| Positive fair values of hedging financial derivatives | 19,747 | 2,333 | 251 | 0 | **22,331** |
| Available-for-sale financial assets | 29,724 | 9,519 | 177 | 0 | **39,420** |
| Assets held for sale | 906 | 0 | 0 | 0 | **906** |
| Amounts due from banks | 15,587 | 25,742 | 9,989 | 453 | **51,771** |
| Loans and advances to customers | 462,360 | 110,710 | 6,297 | 831 | **580,198** |
| Revaluation differences on portfolios hedge items | 32 | 0 | 0 | 0 | **32** |
| Held-to-maturity investments | 51,393 | 14,069 | 0 | 0 | **65,462** |
| Current tax assets | 71 | 15 | 0 | 0 | **86** |
| Deferred tax assets | 42 | 36 | 0 | 0 | **78** |
| Prepayments, accrued income and other assets | 3,991 | 850 | 77 | 1 | **4,919** |
| Investments in subsidiaries and associates | 1,280 | 0 | 0 | 0 | **1,280** |
| Intangible assets | 3,878 | 8 | 0 | 0 | **3,886** |
| Tangible assets | 6,661 | 5 | 0 | 0 | **6,666** |
| Goodwill | 3,752 | 0 | 0 | 0 | **3,752** |
| **Total assets** | **733,659** | **170,042** | **17,430** | **1,606** | **922,737** |
| **Liabilities** | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 14,942 | 2,961 | 258 | 6 | **18,167** |
| Negative fair values of hedging financial derivatives | 7,127 | 2,219 | 82 | 0 | **9,428** |
| Amounts due to banks | 4,082 | 48,607 | 1,379 | 56 | **54,124** |
| Amounts due to customers | 610,872 | 73,655 | 12,246 | 2,604 | **699,377** |
| Revaluation differences on portfolios hedge items | 762 | 0 | 0 | 0 | **762** |
| Securities issued | 13,150 | 19 | 38 | 216 | **13,423** |
| Current tax liabilities | 356 | 4 | 0 | 0 | **360** |
| Deferred tax liabilities | 3,819 | 11 | 0 | 0 | **3,830** |
| Accruals and other liabilities | 13,274 | 2,246 | 494 | 136 | **16,150** |
| Provisions | 1,283 | 328 | 59 | 44 | **1,714** |
| Equity | 105,094 | 307 | 0 | 0 | **105,401** |
| **Total liabilities** | **774,762** | **130,357** | **14,556** | **3,062** | **922,737** |
| **Net FX position as of 31 December 2016** | **(41,103)** | **39,685** | **2,874** | **(1,456)** | **0** |
| Off-balance sheet assets* | 1,287,299 | 502,923 | 147,940 | 16,001 | **1,954,163** |
| Off-balance sheet liabilities* | 1,250,358 | 539,059 | 150,152 | 14,682 | **1,954,251** |
| **Net off-balance sheet FX position as of 31 December 2016** | **36,941** | **(36,136)** | **(2,212)** | **1,319** | **(88)** |
| **Total net FX position as of 31 December 2016** | **(4,162)** | **3,549** | **662** | **(137)** | **(88)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from spot transactions and nominal value of all derivative deals.

| (CZKm) | CZK | EUR | USD | Other currencies | Total |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash and current balances with central banks | 126,081 | 1,764 | 237 | 254 | **128,336** |
| Financial assets at fair value through profit or loss | 20,478 | 8,237 | 482 | 1 | **29,198** |
| Positive fair values of hedging financial derivatives | 21,249 | 2,081 | 371 | 0 | **23,701** |
| Available-for-sale financial assets | 33,616 | 8,246 | 2 | 0 | **41,864** |
| Assets held for sale | 385 | 0 | 0 | 0 | **385** |
| Amounts due from banks | 18,256 | 24,506 | 4,885 | 152 | **47,799** |
| Loans and advances to customers | 433,087 | 90,155 | 8,616 | 759 | **532,617** |
| Revaluation differences on portfolios hedge items | 18 | 0 | 0 | 0 | **18** |
| Held-to-maturity investments | 53,265 | 13,818 | 0 | 0 | **67,083** |
| Current tax assets | 339 | 28 | 0 | 0 | **367** |
| Deferred tax assets | 37 | 33 | 0 | 0 | **70** |
| Prepayments, accrued income and other assets | 3,682 | 411 | 328 | 15 | **4,436** |
| Investments in subsidiaries and associates | 1,219 | 0 | 0 | 0 | **1,219** |
| Intangible assets | 3,867 | 0 | 0 | 0 | **3,867** |
| Tangible assets | 6,840 | 4 | 0 | 0 | **6,844** |
| Goodwill | 3,752 | 0 | 0 | 0 | **3,752** |
| **Total assets** | **726,171** | **149,283** | **14,921** | **1,181** | **891,556** |
| **Liabilities** | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 15,652 | 3,399 | 443 | 0 | **19,494** |
| Negative fair values of hedging financial derivatives | 8,000 | 2,044 | 11 | 0 | **10,055** |
| Amounts due to banks | 14,783 | 37,918 | 3,496 | 33 | **56,230** |
| Amounts due to customers | 576,962 | 65,638 | 11,422 | 2,265 | **656,287** |
| Revaluation differences on portfolios hedge items | 610 | 0 | 0 | 0 | **610** |
| Securities issued | 19,930 | 899 | 313 | 261 | **21,403** |
| Current tax liabilities | 83 | 0 | 0 | 0 | **83** |
| Deferred tax liabilities | 4,577 | 7 | 0 | 0 | **4,584** |
| Accruals and other liabilities | 12,848 | 2,117 | 347 | 107 | **15,419** |
| Provisions | 725 | 391 | 33 | 12 | **1,161** |
| Equity | 102,582 | 3,647 | 0 | 0 | **106,229** |
| **Total liabilities** | **756,753** | **116,060** | **16,065** | **2,678** | **891,556** |
| **Net FX position as of 31 December 2015** | **(30,582)** | **33,223** | **(1,144)** | **(1,497)** | **0** |
| Off-balance sheet assets* | 1,222,235 | 375,250 | 120,140 | 17,797 | **1,735,422** |
| Off-balance sheet liabilities* | 1,192,838 | 410,102 | 118,403 | 16,353 | **1,737,696** |
| **Net off-balance sheet FX position as of 31 December 2015** | **29,397** | **(34,852)** | **1,737** | **1,444** | **(2,274)** |
| **Total net FX position as of 31 December 2015** | **(1,185)** | **(1,629)** | **593** | **(53)** | **(2,274)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from spot transactions and nominal value of all derivative deals.

## (G) Operational risk

Since 2008, the Group has used the Advanced Measurement Approach (AMA) for operational risk management. In addition to standard operational risk instruments used within the AMA approach, such as operational losses collection, Risk Control Self-Assessment (RCSA), Key Risk Indicators (KRI) or Scenario Analysis (SA), the Group developed and deployed also a permanent supervision system consisting of a set of operational everyday controls and a set of formalised periodic controls. The Group is continuously developing all the aforementioned operational risk instruments and supporting continuous development of an operational risk culture throughout all organisational units.

The information collected by the Operational Risks Department is regularly analysed and provided to the Group's management. Based on this information, the management may decide on further strategic steps within the framework of operational risk management. The evaluation of operational risks is also an integral component of the process for new product development and validation.

Co-operation within consolidated operational risk management has been deepened among KB Group companies. The AMA approach has been used in four Group companies, of which two are banking entities (Komerční banka, a.s. and Modrá pyramida stavební spořitelna, a.s.) and two non-banking entities (SG Equipment Finance Czech Republic s.r.o. and ESSOX s.r.o.).

## (H) Legal risk

The Group regularly monitors and evaluates legal disputes filed against it. In order to cover all contingent liabilities arising from legal disputes, the Group establishes a provision equal to the claimed amount in respect of all litigation where it is named as a defendant and where the likelihood of payment has been estimated to exceed 50%. The Group also manages its legal risk through the assessment of legal risks involved in the contracts to which the Group is a party.

## (I) Estimated fair value of assets and liabilities of the Group

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (i.e. an exit price). Where available, fair value estimates are made based on quoted market prices. However, no readily available market prices exist for a significant portion of the Group's financial instruments. In circumstances where quoted market prices are not readily available, the fair value is estimated, as appropriate, using discounted cash flow models or other generally acceptable pricing models. Changes in underlying assumptions, including discount rates and estimated future cash flows, significantly affect these estimates.

In estimating the fair value of the Group's financial instruments, the following methods and assumptions were used.

*(a) Cash and current balances with central banks*
The reported values of cash and current balances with the central bank are generally deemed to approximate their fair value.

*(b) Amounts due from banks*
The estimated fair value of amounts due from banks that mature in 180 days or less approximates their carrying amounts. The fair value of other amounts due from banks is estimated based upon discounted cash flow analysis using interest rates currently offered for investments with similar terms (market rates adjusted to reflect credit risk). The fair value of non-performing amounts due from banks is estimated using a discounted cash flow analysis. The fair value of a loss loan is equal to the appraised value of the underlying collateral.

*(c) Loans and advances to customers*
The fair value of variable yield loans that regularly reprice and which have no significant change in credit risk generally approximates their carrying value. The fair value of loans at fixed interest rates is estimated using discounted cash flow analysis based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality. The fair value of non-performing loans is estimated using a discounted cash flow analysis, including the potential realisation of the underlying collateral.

### *(d) Held-to-maturity investments*

The fair value of the held-to-maturity portfolio is based upon quoted market prices. Where no market prices are available, the fair value is estimated based on discounted cash flow models using the interest rate currently offered as of the financial statements date.

### *(e) Amounts due to central banks, banks and customers*

The fair value of deposits repayable on demand represents the carrying value of amounts repayable on demand as of the financial statements date. The carrying value of term deposits at variable interest rates approximates their fair values as of the financial statements date. The fair value of deposits at fixed interest rates is estimated by discounting their future cash flows using market interest rates. Amounts due to banks and customers at fixed interest rates represent only a fraction of the total carrying value and hence the fair value of total amounts due to banks and customers approximates the carrying values as of the financial statements date.

### *(f) Securities issued*

The fair value of debt securities issued by the Group is based upon quoted market prices. Where no market prices are available, the fair value is estimated using a discounted cash flow analysis.

*The following table summarises the carrying values and fair values of those financial assets and liabilities not presented on the Group's Statement of Financial Position at their fair values:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **(CZKm)** | **Carrying value** | **Fair value** | **Carrying value** | **Fair value** |
| **Financial assets** | | | | |
| Cash and current balances with central banks | 112,241 | 112,241 | 128,336 | 128,336 |
| Amounts due from banks | 51,771 | 53,530 | 47,799 | 49,468 |
| Loans and advances to customers | 580,198 | 596,308 | 532,617 | 548,622 |
| Held-to-maturity investments | 65,462 | 69,585 | 67,083 | 72,264 |
| **Financial liabilities** | | | | |
| Amounts due to central banks | 1 | 1 | 1 | 1 |
| Amounts due to banks | 54,124 | 54,125 | 56,230 | 56,222 |
| Amounts due to customers | 699,377 | 697,488 | 656,287 | 654,939 |
| Securities issued | 13,423 | 10,893 | 21,403 | 20,515 |

*The following table presents the hierarchy of fair values for those financial assets and liabilities not presented on the Group's Statement of Financial Position at their fair values:*

| | 31 Dec 2016 | | | | 31 Dec 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| **(CZKm)** | **Fair value** | **Level 1** | **Level 2** | **Level 3** | **Fair value** | **Level 1** | **Level 2** | **Level 3** |
| **Financial assets** | | | | | | | | |
| Cash and current balances with central banks | 112,241 | 8,997 | 0 | 103,244 | 128,336 | 11,357 | 0 | 116,979 |
| Amounts due from banks | 53,530 | 0 | 0 | 53,530 | 49,468 | 0 | 0 | 49,468 |
| Loans and advances to customers | 596,308 | 0 | 0 | 596,308 | 548,622 | 0 | 0 | 548,622 |
| Held-to-maturity investments | 69,585 | 69,585 | 0 | 0 | 72,264 | 72,264 | 0 | 0 |
| **Financial liabilities** | | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 1 | 1 | 0 | 0 | 1 |
| Amounts due to banks | 54,125 | 0 | 0 | 54,125 | 56,222 | 0 | 0 | 56,222 |
| Amounts due to customers | 697,488 | 0 | 0 | 697,488 | 654,939 | 0 | 0 | 654,939 |
| Securities issued | 10,893 | 0 | 0 | 10,893 | 20,515 | 0 | 0 | 20,515 |

## (J) Allocation of fair values of financial instruments at fair value to the hierarchy of fair values

*Financial assets and financial liabilities at fair value by fair value hierarchy (refer to Note 3.5.4):*

| (CZKm) | 31 Dec 2016 | Level 1 | Level 2 | Level 3 | 31 Dec 2015 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Financial assets at fair value through profit or loss | | | | | | | | |
| – Emission allowances | 1,839 | 1,839 | 0 | 0 | 2,800 | 2,800 | 0 | 0 |
| – Debt securities | 9,606 | 8,501 | 1,105 | 0 | 7,872 | 5,184 | 2,688 | 0 |
| – Derivatives | 18,264 | 401 | 17,863 | 0 | 18,526 | 68 | 18,458 | 0 |
| **Financial assets at fair value through profit or loss** | **29,709** | **10,741** | **18,968** | **0** | **29,198** | **8,052** | **21,146** | **0** |
| **Positive fair value of hedging financial derivatives** | **22,331** | **0** | **22,331** | **0** | **23,701** | **0** | **23,701** | **0** |
| Available-for-sale financial assets | | | | | | | | |
| – Shares and participation Certificates | 182 | 0 | 0 | 182 | 675 | 0 | 0 | 675 |
| – Debt securities | 39,238 | 27,027 | 12,211 | 0 | 41,189 | 28,294 | 12,895 | 0 |
| **Available-for-sale financial assets** | **39,420** | **27,027** | **12,211** | **182** | **41,864** | **28,294** | **12,895** | **675** |
| **Revaluation differences on portfolios hedge items** | **32** | **0** | **32** | **0** | **18** | **0** | **18** | **0** |
| **Financial assets at fair value** | **91,492** | **37,768** | **53,542** | **182** | **94,781** | **36,346** | **57,760** | **675** |
| **Financial liabilities** | | | | | | | | |
| Financial liabilities at fair value through profit or loss | | | | | | | | |
| – Sold securities | 160 | 160 | 0 | 0 | 305 | 305 | 0 | 0 |
| – Derivatives | 18,007 | 261 | 17,746 | 0 | 19,189 | 472 | 18,717 | 0 |
| **Financial liabilities at fair value through profit or loss** | **18,167** | **421** | **17,746** | **0** | **19,494** | **777** | **18,717** | **0** |
| **Negative fair value of hedging financial derivatives** | **9,428** | **0** | **9,428** | **0** | **10,055** | **0** | **10,055** | **0** |
| **Revaluation differences on portfolios hedge items** | **762** | **0** | **762** | **0** | **610** | **0** | **610** | **0** |
| **Financial liabilities at fair value** | **28,357** | **421** | **27,936** | **0** | **30,159** | **777** | **29,382** | **0** |

*Financial assets at fair value – Level 3:*

| | | 2016 | | 2015 |
|---|---|---|---|---|
| (CZKm) | Available-for-sale financial assets | Total | Available-for-sale financial assets | Total |
| **Balance as of 1 January** | **675** | **675** | **2** | **2** |
| Comprehensive income/(loss) | | | | |
| – In Other Comprehensive Income | 303 | 303 | 674 | 674 |
| Purchases | 164 | 164 | 0 | 0 |
| Sales | (960) | (960) | (1) | (1) |
| **Balance as of 31 December** | **182** | **182** | **675** | **675** |

*Shares and participation certificates*

When using an alternative method of valuation based on the price/book value ratio, the fair value is not significantly different from the fair value determined on the basis of the present value of future cash flows which was used for the original valuation.

## 43 Offsetting financial assets and financial liabilities

*The table below provides information about rights of offset and related arrangements for financial instruments as of 31 December 2016:*

| | Assets/liabilities offsetting according to IAS 32 | | | Impact of Master Netting agreement and similar agreement | | |
|---|---|---|---|---|---|---|
| (CZKm) | Gross amount of financial assets/ liabilities* | Gross amount of financial assets/ liabilities set off by financial liabilities/ assets | Net amount of financial assets/ liabilities | Financial instruments recognised in Statement of Financial Position | Cash collateral related to financial instruments | Net amount |
| Positive fair value of derivatives | 40,595 | 0 | 40,595 | 22,719 | 9,817 | 8,059 |
| Negative fair value of derivatives | 27,435 | 0 | 27,435 | 22,719 | 4,234 | 482 |

* This item includes also counterparties with only positive or negative fair value of derivatives.

*The table below provides information about rights of offset and related arrangements for financial instruments as of 31 December 2015:*

| | Assets/liabilities set off according to IAS 32 | | | Amounts which have not been set off | | |
|---|---|---|---|---|---|---|
| (CZKm) | Gross amount of financial assets/ Liabilities* | Gross amount of financial assets/ liabilities set off by financial liabilities/ assets | Net amount of financial assets/ liabilities | Financial instruments recognised in Statement of Financial Position | Cash collateral related to financial instruments | Net amount |
| Positive fair value of derivatives | 42,226 | 0 | 42,226 | 25,065 | 10,667 | 6,494 |
| Negative fair value of derivatives | 29,224 | 0 | 29,244 | 25,065 | 4,179 | 0 |

* This item includes also counterparties with only positive or negative fair value of derivatives.

## 44 Assets in custody and assets under management

*The table below provides information about assets in custody and assets under management:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Cash | Securities | Cash | Securities |
| Assets in custody | 3,305 | 528,431 | 2,789 | 479,433 |
| Assets under management | 0 | 2,137 | 0 | 1,760 |

## 45 Post balance sheet events

### Headquarters building

In March 2017, in line with its long-term strategy of optimising the headquarters buildings, the Group sold one of its headquarters buildings. As of the end of 2016, the building had been classified as held for sale. The result of the transaction will be presented in the line ***'Depreciation, amortisation, impairment and disposal of assets'*** of the Consolidated Statement of Income.

# Separate Financial Statements prepared in accordance with International Financial Reporting Standards as adopted by the European Union as of 31 December 2016

# Separate Statement of Income and Statement of Comprehensive Income for the year ended 31 December 2016

## Separate Statement of Income for the year ended 31 December 2016

| (CZKm) | Note | 2016 | Restated 2015 |
|---|---|---|---|
| Interest income and similar income | 5 | 23,186 | 24,703 |
| Interest expense and similar expense | 5 | (5,337) | (6,518) |
| Dividend income | 5 | 2,722 | 1,698 |
| **Net interest income and similar income** | | **20,571** | **19,883** |
| Net fee and commission income | 6 | 5,979 | 6,287 |
| Net profit/(loss) on financial operations | 7 | 3,833 | 2,665 |
| Other income | 8 | 225 | 160 |
| **Net operating income** | | **30,608** | **28,995** |
| Personnel expenses | 9 | (6,261) | (6,085) |
| General and administrative expenses | 10 | (4,920) | (5,015) |
| Depreciation, amortisation, impairment and disposal of assets | 11 | (1,529) | (2,013) |
| **Total operating expenses** | | **(12,710)** | **(13,113)** |
| **Profit before allowances for loan losses, provisions for other risk, profit on subsidiaries and income tax** | | **17,898** | **15,882** |
| Allowances for loan losses | 12 | (1,884) | (1,327) |
| Provisions for other risk expenses | 12 | 26 | 230 |
| **Cost of risk** | | **(1,858)** | **(1,097)** |
| Profit/(loss) on subsidiaries and associates | 13 | 588 | 0 |
| **Profit before income tax** | | **16,628** | **14,785** |
| Income tax | 14 | (2,509) | (2,361) |
| **Net profit for the period** | 15 | **14,119** | **12,424** |

## Separate Statement of Comprehensive Income for the year ended 31 December 2016

| (CZKm) | Note | 2016 | 2015 |
|---|---|---|---|
| **Net profit for the period** | 15 | **14,119** | **12,424** |
| **Items that will not be reclassified to the Statement of Income** | | | |
| Remeasurement of retirement benefits plan, net of tax | 38 | (93) | (16) |
| **Items that may be reclassified subsequently to the Statement of Income** | | | |
| Cash flow hedging | | | |
| –Net fair value gain/(loss), net of tax | 39 | 1,945 | 232 |
| –Transfer to net profit/(loss), net of tax | 39 | (3,242) | (3,405) |
| Foreign exchange difference on translation of a foreign net investment | | 0 | (2) |
| Net value gain/(loss) on available-for-sale financial assets, net of tax | 40 | (1,354) | 68 |
| **Other comprehensive income for the period, net of tax** | | **(2,744)** | **(3,123)** |
| **Total comprehensive income for the period, net of tax** | | **11,375** | **9,301** |

The accompanying Notes form an integral part of these Separate Financial Statements.

## Separate Statement of Financial Position as of 31 December 2016

| (CZKm) | Note | 31 Dec 2016 | Restated 31 Dec 2015 |
|---|---|---|---|
| **ASSETS** | | | |
| Cash and current balances with central banks | 16 | 103,993 | 116,257 |
| Financial assets at fair value through profit or loss | 17 | 30,482 | 29,889 |
| Positive fair value of hedging financial derivatives | 41 | 21,614 | 23,066 |
| Available-for-sale financial assets | 18 | 31,411 | 32,700 |
| Assets held for sale | 19 | 587 | 360 |
| Amounts due from banks | 20 | 57,983 | 54,589 |
| Loans and advances to customers | 21 | 527,143 | 484,474 |
| Held-to-maturity investments | 22 | 62,425 | 61,003 |
| Current tax assets | | 0 | 303 |
| Deferred tax assets | 33 | 31 | 33 |
| Prepayments, accrued income and other assets | 23 | 3,012 | 2,804 |
| Investments in subsidiaries and associates | 24 | 21,292 | 22,177 |
| Intangible assets | 25 | 3,428 | 3,427 |
| Tangible assets | 26 | 4,664 | 4,444 |
| **Total assets** | | **868,065** | **835,526** |
| **LIABILITIES AND EQUITY** | | | |
| Amounts due to central banks | | 1 | 1 |
| Financial liabilities at fair value through profit or loss | 27 | 18,940 | 20,185 |
| Negative fair value of hedging financial derivatives | 41 | 9,373 | 10,002 |
| Amounts due to banks | 28 | 43,282 | 46,079 |
| Amounts due to customers | 29 | 638,410 | 593,059 |
| Securities issued | 30 | 45,755 | 54,298 |
| Current tax liabilities | | 357 | 0 |
| Deferred tax liabilities | 33 | 3,065 | 3,886 |
| Accruals and other liabilities | 31 | 14,149 | 13,564 |
| Provisions | 32 | 1,701 | 1,149 |
| **Total liabilities** | | **775,033** | **742,223** |
| Share capital | 34 | 19,005 | 19,005 |
| Share premium and reserves | | 74,027 | 74,298 |
| **Total equity** | | **93,032** | **93,303** |
| **Total liabilities and equity** | | **868,065** | **835,526** |

The accompanying Notes form an integral part of these Separate Financial Statements.

These Separate Financial Statements were approved by the Board of Directors on 7 March 2017.

Signed on behalf of the Board of Directors:

**Albert Le Dirac'h**
Chairman of the Board of Directors and Chief Executive Officer

**Libor Löfler**
Member of the Board of Directors and Chief Operating Officer

## Separate Statement of Changes in Equity for the year ended 31 December 2016

| (CZKm) | Share capital | Capital funds and retained earnings* | Remeasurement of retirement benefits plan | Cash flow hedging | Translation of a foreign net investment | Available-for-sale financial assets | Total equity |
|---|---|---|---|---|---|---|---|
| **Balance as of 31 December 2014** | **19,005** | **56,626** | **(22)** | **16,009** | **8** | **4,008** | **95,634** |
| Treasury shares, other | 0 | 151 | 0 | 0 | 0 | 0 | 151 |
| Payment of dividends | 0 | (11,783) | 0 | 0 | 0 | 0 | (11,783) |
| **Transactions with owners** | **0** | **(11,632)** | **0** | **0** | **0** | **0** | **(11,632)** |
| Net profit for the period | 0 | 12,424 | 0 | 0 | 0 | 0 | 12,424 |
| Other comprehensive income for the period, net of tax | 0 | 0 | (16) | (3,173) | (2) | 68 | (3,123) |
| **Comprehensive income for the period** | **0** | **12,424** | **(16)** | **(3,173)** | **(2)** | **68** | **9,301** |
| **Balance as of 31 December 2015** | **19,005** | **57,418** | **(38)** | **12,836** | **6** | **4,076** | **93,303** |
| Treasury shares, other | 0 | 137 | 0 | 0 | 0 | 0 | 137 |
| Payment of dividends | 0 | (11,783) | 0 | 0 | 0 | 0 | (11,783) |
| **Transactions with owners** | **0** | **(11,646)** | **0** | **0** | **0** | **0** | **(11,646)** |
| Net profit for the period | 0 | 14,119 | 0 | 0 | 0 | 0 | 14,119 |
| Other comprehensive income for the period, net of tax | 0 | 0 | (93) | (1,297) | 0 | (1,354) | (2,744) |
| **Comprehensive income for the period** | **0** | **14,119** | **(93)** | **(1,297)** | **0** | **(1,354)** | **11,375** |
| **Balance as of 31 December 2016** | **19,005** | **59,891** | **(131)** | **11,539** | **6** | **2,722** | **93,032** |

* Capital funds and retained earnings consist of other funds created from profit in the amount of CZK 4,189 million (2015: CZK 4,189 million), share premium, treasury shares and share-based transactions in the amount of CZK -221 million (2015: CZK -245 million), net profit from the period in the amount of CZK 14,119 million (2015: CZK 12,424 million) and retained earnings in the amount of CZK 41,804 million (2015: CZK 41,050 million).

The accompanying Notes form an integral part of these Separate Financial Statements.

# Separate Statement of Cash Flows for the year ended 31 December 2016

| (CZKm) | 2016 | Restated 2015 |
|---|---|---|
| **CASH FLOWS FROM OPERATING ACTIVITIES** | | |
| Interest received | 20,691 | 21,797 |
| Interest paid | (3,928) | (5,045) |
| Fee and commission received | 6,868 | 7,566 |
| Fee and commission paid | (885) | (1,288) |
| Net cash received from financial operations | 2,356 | 2,003 |
| Other income receipts | 225 | 168 |
| Cash payments to employees and suppliers, and other payments | (11,459) | (10,382) |
| **Operating cash flow before changes in operating assets and operating liabilities** | **13,868** | **14,819** |
| Amounts due from banks | (3,055) | (510) |
| Financial assets at fair value through profit or loss | (588) | 13,866 |
| Loans and advances to customers | (43,582) | (36,897) |
| Other payments received | 163 | (86) |
| **(Increase)/decrease in operating assets** | **(47,062)** | **(23,627)** |
| Amounts received from banks | (3,163) | 4,155 |
| Financial liabilities at fair value through profit or loss | (1,248) | (5,236) |
| Amounts received from customers | 45,788 | 4,221 |
| Other payments made | 209 | 2,579 |
| **Increase/(decrease) in operating liabilities** | **41,586** | **5,719** |
| Net cash flow from operating activities before tax | 8,392 | (3,089) |
| Income tax paid | (2,025) | (2,462) |
| **Net cash flow from operating activities** | **6,367** | **(5,551)** |
| **CASH FLOWS FROM INVESTMENT ACTIVITIES** | | |
| Dividends received | 2,722 | 1,702 |
| Purchase of held-to-maturity investments | (5,611) | (3,369) |
| Maturity of held-to-maturity investments* | 5,148 | 5,136 |
| Purchase of available-for-sale financial assets | (1,353) | (2,615) |
| Sale and maturity of available-for-sale financial assets* | 2,497 | 5,639 |
| Purchase of tangible and intangible assets | (1,838) | (1,794) |
| Sale of tangible and intangible assets | 56 | 40 |
| Purchase of investments in subsidiaries and associates | 0 | (551) |
| Sale/decrease of investments in subsidiaries and associates | 1,373 | 5,091 |
| **Net cash flow from investment activities** | **2,994** | **9,279** |
| **CASH FLOWS FROM FINANCING ACTIVITIES** | | |
| Dividends paid | (11,735) | (11,750) |
| Securities issued | 0 | 794 |
| Securities redeemed* | (9,976) | (16,342) |
| **Net cash flow from financing activities** | **(21,711)** | **(27,298)** |
| **Net increase/(decrease) in cash and cash equivalents** | **(12,350)** | **(23,570)** |
| Cash and cash equivalents at the beginning of the year | 113,960 | 137,536 |
| Foreign exchange differences on cash and cash equivalents at beginning of year | 2 | (6) |
| **Cash and cash equivalents at the end of the year** (refer to Note 35) | **101,612** | **113,960** |

* The amount also includes coupons received and paid.

The accompanying Notes form an integral part of these Separate Financial Statements.

# Notes to the Separate Financial Statements as of 31 December 2016

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## 1 Principal activities

Komerční banka, a.s. (henceforth the "Bank") is incorporated in the Czech Republic as a joint-stock company. The principal activities of the Bank are as follow:

I. Providing loans, advances and guarantees in Czech crowns and foreign currencies;
II. Acceptance and placement of deposits in Czech crowns and foreign currencies;
III. Providing current and term deposit accounts in Czech crowns and foreign currencies;
IV. Providing banking services through an extensive branch network in the Czech Republic;
V. Treasury operations in the interbank market;
VI. Servicing foreign trade transactions; and
VII. Investment banking.

The registered office address of the Bank is Na Příkopě 33/969, 114 07 Prague 1. The Bank has operations in the Czech Republic and Slovakia through its foreign branch (Komerční banka, a.s., pobočka zahraničnej banky).

The Bank's ordinary shares are publicly traded on the Prague Stock Exchange. Société Générale S.A. is the Bank's majority shareholder, holding 60.35% (2015: 60.35%) of the Bank's issued share capital.

## 2 Events for the year ended 31 December 2016

**Dividends declared in respect of the year ended 31 December 2015**
At the General Meeting held on 22 April 2016 the shareholders approved a dividend for the year ended 31 December 2015 of CZK 310 per share before tax. The dividend was declared in the aggregate amount of CZK 11,783 million and the remaining balance of the net profit was allocated to retained earnings. The dividends were paid out in Czech crowns.

**Announcement on the Bank's share split**
The General Meeting held on 22 April 2016 approved a split of the Bank's shares in the ratio of 5:1. The split took legal effect on 25 April 2016 with its entry into the Register of Companies. Shareholders received five new shares with nominal value CZK 100 in place of each old share in the nominal value of CZK 500. Trading of the split shares on the Prague Stock Exchange was started on 12 May 2016.

**Changes in the Bank's financial group**
In March 2016, the Bank concluded an agreement on the sale of its interest in Cataps, s.r.o. with Worldline SA/NV based upon which the Bank transferred its merchant acquiring into Cataps, s.r.o. and subsequently sold its 80% stake in Cataps, s.r.o. Both steps were performed in September 2016. The selling price for the 80% stake in Cataps, s.r.o. was CZK 727 million. The remaining 20% stake in Cataps, s.r.o., valued at CZK 8 million, was reclassified as *'Assets held for sale'* due to the expected sale of this company.

In April 2016, the Bank's subsidiary ESSOX s.r.o. concluded agreements on acquisitions of 100% ownership stakes in PSA FINANCE ČESKÁ REPUBLIKA, s.r.o. and in PSA FINANCE SLOVAKIA, s.r.o. from members of Banque PSA Finance, based in Paris. The acquisitions were finalised in July 2016 after obtaining all required regulatory approvals.

In May 2016, the equity in Bastion European Investments S.A. was decreased by EUR 3.5 million (equivalent to CZK 100 million). The decrease was initiated solely by the Bank as the majority shareholder of Bastion European Investments S.A.

In June 2016, the Bank's investment into subsidiary NP 33, s.r.o., valued at CZK 405 million, was reclassified as *'Assets held for sale'* due to expected sale of this company.

In November 2016, the Bank decided to decrease share capital and to dissolve the reserve and statutory funds of NP 33, s.r.o., that amount totalling to CZK 170 million. The process of decreasing the share capital was finalised in December 2016.

In December 2016, the Bank decreased the capital of its subsidiary Protos, uzavřený investiční fond, a.s. through decreasing the reserve fund by CZK 450 million. The share of the Bank in this decrease was CZK 376 million which reflects the Bank's 83.65% ownership share. The remaining ownership share is held by Factoring KB, a.s. which is fully owned by the Bank.

# 3 Principal accounting policies

These Financial Statements are separate. The Consolidated Financial Statements are issued as of the same date. As of 31 December 2016, the total consolidated equity is CZK 105,401 million (2015: CZK 106,229 million) and for the year ended 31 December 2016 total consolidated profit is CZK 14,074 million (2015: CZK 13,132 million).

The principal accounting policies adopted in the preparation of these Separate Financial Statements are set out below.

## 3.1 Statement of compliance with IFRS

The Separate Financial Statements are prepared pursuant to and comply with International Financial Reporting Standards (hereafter only "IFRS") as adopted by the European Union and effective for the annual period beginning on 1 January 2016.

The presented Separate Financial Statements for the year ended 31 December 2016 are prepared on the basis of current best estimates. The management of the Bank believes that these present a true and fair view of the Bank's financial results and financial position using all relevant and available information as of the financial statements date.

## 3.2 Underlying assumptions of the Separate Financial Statements

### 3.2.1 Accrual basis

The Separate Financial Statements are prepared on an accrual accounting basis (i.e. the effects of transactions and other events are recognised when they occur and are reported in the Separate Financial Statements for the period to which they relate).

The exception is the Statement of Cash Flows, which is prepared on a cash basis (i.e. it presents cash inflows and outflows during the reporting period without regard to the period to which each transaction relates).

### 3.2.2 Going concern

The Separate Financial Statements are prepared on the assumption that the Bank is a going concern and will continue in operation for the foreseeable future. The Bank has neither the intention nor the need to liquidate or materially curtail the scale of its operations.

### 3.2.3 Reporting period

The Bank reports for a 12-month period which is identical to the calendar year.

## 3.3 Basis of preparation

### 3.3.1 Presentation currency

The Separate Financial Statements are presented in Czech crowns (hereafter only "CZK"), which constitute the Bank's presentation currency. The balances shown are stated in CZK million unless indicated otherwise.

### 3.3.2 Historical cost

The Separate Financial Statements are prepared under the historical cost convention, except for available-for-sale financial assets, financial assets and liabilities at fair value through profit or loss and hedging derivatives and hedge items in fair value hedge accounting, whose items are measured at fair value.

Assets held for sale are measured at the lower of their (i) fair value less cost to sell; or (ii) carrying amount just prior to reclassification into *'Assets held for sale'*.

### 3.3.3 Significant accounting judgements and estimates

In applying the accounting policies for the purpose of preparing the Separate Financial Statements in accordance with IFRS, it is necessary for the Bank's management to use professional judgement and make estimates and assumptions. These impact upon reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities as of the financial statements date and the reported amounts of revenues and expenses during the reporting period. These estimates and judgements are based on the information available as of the financial statements date and they relate especially to the determination of:

- Fair values in the Statement of Financial Position of financial instruments not quoted in an active market which are classified as financial assets or liabilities at fair value through profit or loss, hedging derivatives or available-for-sale financial assets (refer to Note 3.5.5);
- The value of intangible assets (refer to Note 3.5.9);
- The amount of impairment of assets (refer to Notes 3.5.5 and 3.5.9);
- Provisions recognised under liabilities (refer to Note 3.5.10); and
- The amount of deferred tax assets that can be recognised, based upon the likely timing and level of future taxable profits, together with future tax planning strategies (refer to Note 3.5.7).

Information about the key judgements and assumptions concerning the future and other key sources of estimation uncertainty as of the financial statements date that have a significant risk of causing material adjustment to the carrying values of assets and liabilities are disclosed in individual notes as appropriate.

### 3.3.4 Investments in subsidiaries and associates

A subsidiary is an entity in which the Bank has control, i.e. it directly or indirectly owns more than half the voting rights or it has the power to govern the entity in another way. An associate is an entity in which the Bank has significant influence, i.e. directly or indirectly owns 20% to 50% of the voting rights.

Investments in which the Bank directly or indirectly owns less than 20% of the voting rights are classified as *'Available-for-sale financial assets'* and are reported as such.

Investments in subsidiaries and associates are measured at historical cost (i.e. foreign currency investments are translated using the foreign exchange rate at the transaction date) decreased by potential accumulated impairment losses. The Bank assesses regularly at the end of each reporting period whether there is any impairment loss by comparing the carrying values of each investment with its recoverable amount. If the recoverable amount is lower, the Bank recognises the impairment loss through the use of an allowances account. Investments in subsidiaries and associates are presented in the line *'Investments in subsidiaries and associates'*.

## 3.4 Application of new and revised IFRS

### 3.4.1 Standards and interpretations newly applied by the Bank in the current period

The following standards, interpretations and amendments were newly applied by the Bank as from 1 January 2016. They have no impact in the current period (and/or prior period).

| Standard | Impact/Comments |
|---|---|
| **Annual Improvements to IFRS 2010–2012 Cycle*** | Annual Improvements amend seven standards in a total of eight points, predominantly with the objective of removing unintentional inconsistencies in individual standards or redundant or confusing references and improving wording or updating out-of-date terminology. |
| **Defined Benefit Plans: Employee Contributions (Amendments to IAS 19 Employee Benefits)*** | The amendment defines principles for recognition of employee contributions within defined benefit plans distinguishing the procedures for contributions the amounts of which are not dependent upon length of service and those the amounts of which are so dependent. |
| **Accounting for Acquisition of Interests in Joint Operations (Amendments to IFRS 11 Joint Arrangements)** | The amendments provide guidance on the accounting for acquisition of interests in existing joint operations in which the activity constitutes a business as defined in IFRS 3 Business Combinations. It also applies to the formation of a joint operation if, and only if, an existing business is contributed to the joint operation on its formation. The acquirer is required to apply, to the extent of its share, the principles of business combination accounting and disclosures in IFRS 3 and other IFRS, if not conflicting with the guidance in IFRS 11. |
| **Equity Method in Separate Financial Statements (Amendments to IAS 27 Separate Financial Statements)** | The amendment allows an entity to account for investments in subsidiaries, associates and joint ventures in its separate financial statements using the equity method (described in IAS 28) as an alternative to the currently allowable accounting either at cost or as a financial asset in accordance with IAS39/IFRS 9. |

| Standard | Impact/Comments |
|---|---|
| **Annual Improvements to IFRS 2012–2014 Cycle** | Annual Improvements amend four standards in a total of five points predominantly with the objective of removing unintentional inconsistencies in individual standards or redundant or confusing references and improving wording or updating out-of-date terminology. |
| **Disclosure Initiative (Amendments to IAS 1 Presentation of Financial Statements)** | Given that the amendments clarify existing requirements in IAS 1 which do not directly affect an entity's accounting policies or accounting estimates, there is no need under the transitional provisions to disclose the information otherwise required by IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors. |
| **Investment Entities: Applying the Consolidation Exception (Amendments to IFRS 10 Consolidated Financial Statements, IFRS 12 Disclosure of Interests in Other Entities and IAS 28 Investments in Associates and Joint Ventures)** | The amendments to IFRS 10 and IAS 28 further clarify application of the consolidation exception to entities in group structures involving investment entities. |

* The European Commission has approved Annual Improvements to IFRS 2010-2012 Cycle and Defined Benefit Plans: Employee Contributions (Amendments to IAS 19 Employee Benefits) for reporting periods beginning on or after 1 February 2015. According to the IASB, both documents are effective already for reporting periods beginning on or after 1 July 2014.

### 3.4.2 Issued standards and interpretations not applied for the current period

Although the following standards, interpretations and amendments had been issued, they are not yet effective for the reporting period beginning on 1 January 2016 and the Bank has decided not to adopt them early. The Bank has decided not to adopt early the standards and interpretations which were already approved by the European Commission.

Currently, the Bank does not anticipate that their application will significantly impact the Bank's financial position and financial performance for the reporting period, with the exception of IFRS 9 Financial Instruments and IFRS 16 Leases.

<u>IFRS 9 Financial Instruments</u>

IFRS 9 Financial Instruments supersedes the existing standard IAS 39. It introduces a new approach to the classification and measurement of financial assets, a new impairment methodology and new hedge accounting rules for micro hedges. Accounting and rules for macro hedging were separated from the IFRS 9 project. The IASB is still working on developing a new macro hedging model; the first discussion paper was issued in April 2014.

The application of the new classification and measurement methodology means that financial assets must be classified upon initial application of the standard based on both the entity's business model for managing the financial assets (held to collect, held to collect and sell, other business models) and the financial asset's contractual cash flow characteristics, i.e. applying of the "solely payment of principal and interest" test (SPPI). Financial assets will be newly measured at amortised cost, at fair value through profit or loss, or at fair value through other comprehensive income. In general no impact, with the exception mentioned below, is expected for debt instruments classified in the current portfolio as held-to-maturity, loans and receivables and fair value through profit or loss. Debt instruments classified in the portfolio of available-for-sale are expected to be newly measured at amortised cost rather than at fair value through other comprehensive income, as meeting both criteria: hold to collect business model and SPPI characteristics. With respect to equity instruments classified in the portfolio of available-for-sale, the Bank will need to decide whether it will measure these through profit or loss or whether it will use the FVOCI option and thus recognise changes in their fair value in other comprehensive income. The decision for the existing instruments is expected to be made during 2017 but not later than at initial application of the standard. As of 1 January 2018, the remaining unamortised revaluation reserve in Other Comprehensive Income from the reclassification in 2014 of certain debt securities from the available-for-sale to held-to-maturity portfolio and also the revaluation reserve from available-for-sale debt instruments newly measured at amortised costs will be both removed from equity and adjusted against the fair value of the financial assets. Similarly, the related deferred tax will be in both cases removed from equity. Any potential difference in approach to amortization of revaluation reserve subsequent reclassifications to held-to-maturity would be recognized in retained earnings under IFRS 9.

The application of the new impairment methodology, superseding the current IAS 39 incurred loss model, means earlier recognition of expected credit losses from the point at which financial instruments originate or are acquired. The Bank is going to utilise Société Générale Group's IFRS 9 methodology. Great attention is dedicated to assuring the consistency of provisions calculations according to IFRS 9 with the risk-weighted assets calculation (the usage of the same statistical models in both calculations) and regular stress-testing approach (forward-looking predictions in IFRS 9 calculations to be the same as in the regular stress testing). The Bank is already well advanced in the implementation of the IFRS 9 requirements that it will be obliged to apply from the beginning of 2018. Technical implementation should be finished by the end of the second quarter of 2017 and will be based on the utilisation of existing IT tools. Parallel regular running of IAS 39 and IFRS 9 provisions calculation is expected to be started in the second quarter of 2017.

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For the transitional purposes, the Bank will use the relief from restating prior periods. Any differences from the initial application of the standard will be recognised in equity.

As regards hedge accounting, IFRS 9 provides entities with an accounting policy choice: either to continue to apply existing requirements in IAS 39 until the macro hedging project is finalised or to apply the requirements of IFRS 9. The Bank assumes to apply IFRS 9, but it does not expect any significant changes.

IFRS 16 Leases

IFRS 16 Leases replaces the current standard IAS 17. The new standard model will fundamentally change the accounting from the lessee's point of view when ceasing to distinguish between finance leases and operating leases, and instead introducing a single on-balance sheet accounting model. This will be applicable for almost all leases with the optional exceptions for short-term leases and leases for which the underlying asset is of low value. The accounting by lessors under the new standard is substantially unchanged from today's accounting in IAS 17.

The Bank has already carried out the initial assessment and identified potential areas to be impacted by the application of the new IFRS 16 requirements. The Bank as a lessee under operating lease of office buildings and branches, in particular, will need to recognise those leases on the balance sheet causing an increase of assets (right-of-use assets) and liabilities (lease liabilities). Processes and systems need to be evaluated to comply with the increased disclosure requirements.

The Bank will also need to assess the potential effects of IFRS 16 on capital adequacy requirements and resolution fund contribution. So far, however, inasmuch as the prudential regulator has not expressed its view on how the right-of-use asset will be treated for regulatory purposes, developments in this area need to be monitored.

A further area of interest may include the Bank as a lender or financial services provider. For clients reporting under IFRS that have entered into significant lease contracts currently classified as operating leases, the transition to IFRS 16 will have a significant impact on their financial statements and key financial metrics, based on the recognition of new assets and liabilities and the differences in timing and classification of lease expenses. The impacts on clients' credit assessment or risk evaluation need to be considered. Based, however, on the current status wherein the number of IFRS clients is immaterial and due to the fact that these clients are mostly large and therefore expert rating is provided, we do not expect significant impacts in this area.

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| Sale or Contribution of Assets between an Investor and its Associate or Joint Venture (Amendments to IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures) | The amendment clarifies the accounting treatment for sale or contribution of assets between an investor and its associates or joint ventures. It resolves a current inconsistency between the existing requirements in IFRS 10 Consolidated Financial Statements and IAS 28 Investments in Associates and Joint Ventures on how to calculate any gain or loss arising from this transaction. The accounting treatment depends on whether the non-monetary assets as subject of the transaction constitute a "business", as defined in IFRS 3 Business Combinations. In such case, the gain or loss is recognised in full. | The effective date of 1 January 2016 was withdrawn and deferred indefinitely.<br>Early adoption continues to be permitted.<br>EU postponed |
| Recognition of Deferred Tax Assets for Unrealised Losses<br>(Amendments to IAS 12 Income Taxes) | The amendments to IAS 12 clarify how to account for a deferred tax asset that is related to debt instruments measured at fair value for accounting purposes and at cost for tax purposes in circumstances in which changes in the market interest rate decrease the fair value below cost. This applies irrespective of whether the debt instrument's holder expects to recover the carrying amount of the debt instrument by sale or by use. The amendments also clarify that the carrying amount of an asset does not limit the estimation of probable future taxable profits. | 1 January 2017<br>EU not yet endorsed |
| Disclosure Initiative<br>(Amendments to IAS 7) | The amendments require disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The following changes shall be disclosed (to the extent necessary): changes from financing cash flows, changes arising from obtaining or losing control of subsidiaries or other businesses, the effect of changes in foreign exchange rates, changes in fair values and other changes. | 1 January 2017<br>EU not yet endorsed |
| Annual Improvements to IFRS 2014–2016 Cycle | Annual Improvements amend three standards predominantly with the objective of removing unintentional inconsistencies in individual standards or redundant or confusing references and improving wording or updating out-of-date terminology. | 1 January 2017 (amendment to IFRS 12)<br>1 January 2018 (amendments to IFRS 1 and IAS 28)<br>EU not yet endorsed |
| Classification and Measurement of Share-based Payment Transactions<br>(Amendments to IFRS 2) | The amendments relate to three areas: the accounting for the effects of vesting conditions on cash-settled share-based payment transactions, the classification of share-based payment transactions with net settlement features for withholding tax obligations, the accounting for modification of a share-based payment transaction that changes its classification from cash-settled to equity-settled. | 1 January 2018<br>EU not yet endorsed |
| IFRS 15 Revenue from Contracts with Customers – new standard | The new standard supersedes current revenue recognition guidance, including IAS 18 Revenue, IAS 11 Construction Contracts and related interpretations.<br><br>It outlines a single comprehensive model for accounting and disclosure of revenue arising from contracts with customers to provide goods or services, regardless of the industry or the type of transaction. For the banking sector, the following areas in particular may be affected: credit card loyalty schemes, pricing mechanisms including variable amounts, distinct goods or services in multi-element arrangements, up-front fees at or near contract inception.<br><br>The Bank is assessing the potential impact on its financial statements. However, as the Bank's main business lies outside the scope of IFRS 15, our expectation is that it will not be significant. | 1 January 2018 |
| Clarifications to IFRS 15 Revenue from Contracts with Customers | The amendments clarify IFRS 15 in three areas (identifying performance obligations, principal versus agent considerations and licensing application guidance) and provide two additional practical expedients for transition purposes (completed contracts under the full retrospective transition approach and modified contracts). | 1 January 2018<br>EU not yet endorsed |

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| IFRS 9 Financial Instruments – new standard | In July 2014, the final version of IFRS 9 was issued, replacing the current IAS 39 Financial Instruments: Recognition and Measurement and all previous versions of IFRS 9. It introduces a new approach to the classification and measurement of financial assets, a new impairment methodology and new hedge accounting rules for micro hedges. Accounting and rules for macro hedging were separated from the IFRS 9 project and are part of a separate project (Discussion Paper, April 2014). The new IFRS 9 shall be applied retrospectively except for micro hedge accounting.<br><br>The classification and measurement of financial assets depends on assessment of both a financial asset's contractual cash flow characteristics and the entity's business model for managing the financial asset. The resulting measurement categories are:<br>• Amortised cost;<br>• Fair value through other comprehensive income; and<br>• Fair value through profit or loss.<br><br>In comparison to IAS 39, the embedded derivatives in financial assets are no longer bifurcated.<br><br>In respect to financial liabilities, IFRS 9 retains almost all of the existing requirements from IAS 39 except changes in the entity's own credit risk for financial liabilities designated at fair value through profit or loss using the fair value option, which are newly presented in other comprehensive income.<br><br>The impairment requirements in the new standard are based on an expected credit loss model. For all financial assets in the scope of IFRS 9 that are not accounted for at fair value through profit or loss and excluding also equity instruments, entities are required to recognise from origination throughout the life of an asset either 12-month expected credit losses or lifetime expected credit losses, when credit risk significantly increases after initial recognition. The measurement of expected credit losses should reflect a probability-weighted outcome, the time value of money and reasonable and supportable information.<br><br>In November 2013, new requirements related to general hedge accounting (micro hedge accounting) were added to IFRS 9. These requirements align hedge accounting more closely with risk management, which means that more of an entity's risk management activities may qualify for hedge accounting and more designations of groups of items as hedged items are possible. The new model does not fundamentally change the types of hedging relationships or the requirement to measure and recognise ineffectiveness under IAS 39. However, there is only a prospective effectiveness test remaining that is newly based on objective (focus on the economic relationship between the hedged item and the hedging instrument) replacing the range of 80-125%. As a consequence of the new general hedge accounting rules in IFRS 9, additional hedge accounting disclosure requirements were introduced into IFRS 7 Financial Instruments: Disclosures. | 1 January 2018 |
| Applying IFRS 9 Financial Instruments with IFRS 4 Insurance Contracts (Amendments to IFRS 4) | The amendments to IFRS 4 address the different effective dates of IFRS 9 Financial Instruments and the forthcoming new Insurance Contracts Standard.<br><br>The amendments introduce two options for entities that issue insurance contracts within the scope of IFRS 4:<br>(a) Overlay approach permitting insurers to reclassify from profit or loss to other comprehensive income an amount equal to the difference between the amount reported in profit or loss for designated financial assets applying IFRS 9 and the amount that would have been reported in profit or loss for those assets if the insurer had applied IAS 39; and<br>(b) Temporary exemption from IFRS 9 for insurers whose activities are predominantly connected with insurance.<br><br>The application of both approaches is optional and an entity is permitted at the beginning of any annual period to irrevocably stop applying them before the new insurance contracts standard is applied. | 1 January 2018<br>EU not yet endorsed |

| Standard | Summarised content | Effective for reporting period beginning on or after |
|---|---|---|
| IFRIC 22 Foreign Currency Transactions and Advance Consideration | Following IAS 21 The Effects of Changes in Foreign Exchange Rates, the interpretation addresses the accounting for foreign currency transactions when an entity recognises a non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration before the entity recognises the related asset, expense or income.<br><br>For the purposes of determining the exchange rate to use on initial recognition of the related asset, expense or income IFRIC 22 specifies the transaction date as the date of initial recognition of non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. | 1 January 2018<br>EU not yet endorsed |
| IFRS 16 Leases – new standard | The new standard, superseding IAS 17 Leases and related interpretations, establishes principles for the recognition, measurement, presentation and disclosure of leases for both the lessee and the lessor.<br><br>From the lessee's point of view, the standard newly provides a single on-balance sheet accounting model. Lessees are required to recognise assets and liabilities (so-called right-of-use assets and lease liabilities) for all leases unless the lease term is 12 months or less or the underlying asset is of a low value, in which case the lessees have an accounting policy choice to apply a method similar to operating leases under IAS 17. The right-of-use asset is treated similarly as are other non-financial assets; it is depreciated in accordance with the requirements in IAS 16 Property, Plant and Equipment and tested for impairment under IAS 36 Impairment of Assets. The lease liability is initially measured at the present value of the lease payments payable over the lease term, discounted at the rate implicit in the lease if that can be readily determined. If that rate cannot be readily determined, the lessee shall use its incremental borrowing rate.<br><br>Lessors continue to classify leases as operating or finance, with an accounting approach substantially unchanged from IAS 17. A lease is classified as a finance lease if it transfers substantially all the risks and rewards incidental to ownership of the underlying asset. Otherwise a lease is classified as an operating lease. For a finance lease, the lessor recognises finance income over the lease term, based on a pattern reflecting a constant periodic rate of return on the net investment. The net investment in the lease (lease receivable) is subject to the derecognition and impairment requirements in IFRS 9 Financial Instruments. For operating leases, the lessor recognises lease income on either a straight-line basis or another systematic basis that is more representative of the pattern in which benefit from use of the underlying asset is diminished. | 1 January 2019<br>EU not yet endorsed |

### 3.4.3 Standards and interpretations not yet endorsed by the European Union

The European Commission decides on the applicability of IFRS issued by the IASB within the European Union by Regulation (EC) No. 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

As of the issuance date of these Separate Financial Statements, IFRS as adopted by the European Union does not differ from IFRS, except for provisions of IAS 39 prohibiting fair value hedge accounting applied to interest rate hedging on a portfolio basis for banking deposits which has not been approved by the European Union (i.e. in the European Union this hedging is permitted). Should the full version of IAS 39 requirements be applied, the impact would be insignificant, as the Bank does not use interest rate hedging on a portfolio basis for banking deposits.

Those effective or issued standards and interpretations and/or amendments thereto not approved by the European Commission are highlighted in the previous section herein.

## 3.5 Principal accounting policies

### 3.5.1 Transactions in foreign currencies

#### *3.5.1.1 Functional and presentation currency*

The Bank's functional currency (i.e. the currency of the primary economic environment in which the Bank operates) is the Czech crown.

The Bank has a branch in the Slovak Republic and a subsidiary, Bastion European Investments S.A., in Belgium. These both have the euro as their functional currency and are considered as foreign operations from a financial reporting point of view.

#### *3.5.1.2 Transactions and balances translation*

Transactions realised in foreign currency (i.e. in a currency other than the functional currency) are translated into the functional currency at the date of initial recognition using the spot foreign exchange rate announced by the bank authority (hereafter only the "BA") for the respective foreign currency. Depending on the functional currency the BA means the Czech National Bank (hereafter only the "CNB") for the Czech crown and the European Central Bank (hereafter only "ECB") for the euro.

At the end of the reporting period all balance sheet line items denominated in foreign currency are translated into the functional currency, depending on their nature, as follows:

I. Foreign currency monetary items are translated using the closing rate (foreign exchange rate announced by the BA at the end of the reporting period);
II. Non-monetary items that are measured at historical cost are translated using the BA's foreign exchange rate at the date of the transaction; and
III. Non-monetary items that are measured at fair value in a foreign currency are translated using the BA's foreign exchange rate at the date when the fair value was determined.

Gains and losses related to the translation of foreign currency items at the end of the reporting period as well as those related to their settlement are recognised as gains or losses of the period in which they occur and are presented in the line ***'Net profit/(loss) on financial operations'***.

However, where a gain or loss from a fair value change in a non-monetary item denominated in foreign currency is recognised directly in Other Comprehensive Income, related foreign exchange rate differences are recognised in the same way. These non-monetary items include equity instruments. Also recognised in Other Comprehensive Income are foreign exchange rate differences related to the fair value revaluation of debt instruments classified as available-for-sale (excluding the effective portion of their fair value hedges and excluding foreign exchange rate differences related to changes in their amortised cost) and non-derivative financial liabilities (current accounts, deposits) used as hedging items for the cash flow hedge of foreign currency risk and the hedge of a net investment in a foreign operation.

### 3.5.2 Recognition of income and expenses

#### *3.5.2.1 Net interest income and similar income*

Interest income and expense related to interest-bearing instruments, except for instruments classified as financial assets or financial liabilities at fair value through profit or loss and interest hedging derivatives, are recognised on an accrual basis in the Statement of Income in the lines ***'Interest income and similar income'*** and ***'Interest expense and similar expense'*** using the effective interest rate (refer to 3.5.5.7 Effective interest rate method). Interest income and expense related to interest rate hedging derivatives are recognised in the lines described on an accrual basis using the contractual interest rate of the corresponding derivative. Late-fee income is recognised at the date of its payment and presented in the line ***'Interest income and similar income'***.

Dividend income is recognised when the Bank's right to receive a dividend payment is established and is presented in the line ***'Dividend income'***.

#### *3.5.2.2 Net fee and commission income*

The recognition of income from fees and commissions depends on the purpose for which a fee was assessed and the basis of accounting for any associated financial instrument. In accordance with the substance of fees and nature of services for which they are assessed, the Bank distinguishes the following three categories of fees:

- Fees and commissions that comprise an integral component of the effective interest rate of a financial instrument are recognised in the line ***'Interest income and similar income'***;
- Fees and commissions for services provided – income from these is recognised as revenue when services are provided and it is presented in the line ***'Net fee and commission income'***;
- Fees and commissions for the execution of an act – income from these is recognised as revenue when the act has been completed and is also presented in the line ***'Net fee and commission income'***.

#### *3.5.2.3 Net profit/(loss) on financial operations*

This line includes net profit/loss on financial operations, which means realised and unrealised gains/losses on securities held for trading; security derivatives; currency, interest rate and trading commodity derivatives; foreign exchange transactions; foreign assets and liabilities retranslation to the functional currency; and realised gains/losses on available-for-sale financial assets.

In this line there is also recognised interest income and expense related to interest-bearing instruments classified as financial assets or financial liabilities at fair value through profit or loss.

### 3.5.3 Cash and cash equivalents

Cash comprises cash on hand and cash in transit.

Cash equivalents are short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value. Cash equivalents are held for the purpose of meeting short-term cash commitments rather than for investment purposes. This item also includes obligatory minimum reserves. The Bank can freely transact with the amount of these reserves under the assumption that average obligatory minimum reserves are maintained within the given maintenance period established by the CNB.

In preparing its Statement of Cash Flows for the period, the Bank includes into cash and cash equivalents the cash and current balances with central banks at the beginning and end of the period and current amounts due from and to banks.

### 3.5.4 Fair value and hierarchy of fair value

Fair value is the price that would be received in selling an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The fair value measurement is based on the presumption that the transaction to sell the asset or transfer the liability takes place either in the principal market for the asset or liability or, in the absence of a principal market, in the most advantageous market for the asset or liability. The principal or most advantageous market must be accessible to the Bank.

The fair value of an asset or a liability is measured using the assumptions that market participants would use when pricing the asset or liability, assuming that market participants act in their economic best interest.

The Bank classifies fair value measurements using a fair value hierarchy that reflects the significance of the inputs used in making the measurements of asset or liability measured at fair value. The hierarchy of fair values has the following three levels:

- ***Level 1:*** inputs are quoted prices (unadjusted) in active markets for identical assets or liabilities that the entity can access at the measurement date;
- ***Level 2:*** inputs are inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly or indirectly; and
- ***Level 3:*** inputs are unobservable inputs for the asset or liability.

The fair value hierarchy gives the highest priority to quoted prices (unadjusted) in active markets for identical assets or liabilities (Level 1) and the lowest priority to unobservable inputs (Level 3).

The fair value is included in the hierarchy according to the lowest classified significant input used in its determination. Significant input information is that information which has a significant impact on the total fair value of the asset or liability.

For assets and liabilities that are recognised in the financial statements at fair value on a recurring basis (i.e. those for which measurement at fair value is required or permitted in the statement of financial position at the end of each reporting period), the Bank determines whether transfers have occurred between levels in the hierarchy by re-assessing the categorisation (based on the lowest level input that is significant to the fair value measurement as a whole) at the date of the event or change in circumstances that caused the transfer.

### 3.5.5 Financial instruments

#### *3.5.5.1 Dates of recognition and derecognition*

All regular way purchases or sales of financial assets are recognised using settlement date accounting. The settlement (collection) date is the day on which the financial instrument is delivered (cash payment).

When settlement date accounting is applied, the financial asset is recognised in the Statement of Financial Position on the day of receipt of a financial instrument (sending of cash) and derecognised on the day of its delivery (collection of cash).

For financial assets measured at fair value, however, an acquired financial asset is measured to reflect changes in its fair value from the purchase trade date to the purchase settlement date according to its categorisation into an individual portfolio (i.e. either in profit or loss or in other comprehensive income).

All purchases and sales of financial instruments that do not meet the “regular way” settlement criterion in the marketplace concerned are treated as financial derivatives. The Bank recognises financial derivatives in the Statement of Financial Position at the trade date. Financial derivatives are derecognised at their maturity.

The Bank recognises a financial liability in the Statement of Financial Position when it becomes a party to the contractual provisions of the instrument and it is removed from the Statement of Financial Position when it is extinguished (i.e. in circumstances where a contractually defined obligation is fulfilled, cancelled or expires).

#### *3.5.5.2 Initial measurement of financial assets and financial liabilities*

When a financial asset or financial liability is initially recognised, the Bank measures it at its fair value plus, in the case of a financial asset or financial liability not at fair value through profit or loss, transaction costs that are directly attributable to the acquisition or issue of that instrument.

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price (i.e. the fair value of the consideration given or received).

The transaction costs include mainly fees and commissions paid to brokers, dealers and agents.

Also, financial guarantee contracts issued are initially recognised at fair value, being the premium received, in the Statement of Financial Position in the line ***‘Accruals and other liabilities’***. The guarantees are subsequently measured as of the financial statements date at the higher of the amount initially recognised less, when appropriate, cumulative amortisation recognised in profit or loss (in the Statement of Financial Position in the line ***‘Accruals and other liabilities’***), and the best estimate of expenditure required to settle any financial obligation arising as a result of the guarantee (in the Statement of Financial Position in the line ***‘Provisions’***). The premium received is recognised in the Statement of Income in the line ***‘Net fee and commission income’*** on a straight-line basis over the life of the guarantee. The creation of provisions is recognised in the Statement of Income in the line ***‘Allowances for loan losses’***.

#### *3.5.5.3 “Day 1” profit or loss*

In determining whether fair value at initial recognition equals the transaction price, the Bank takes into account factors specific to the transaction and to the asset or liability.

The Bank trades no financial instruments on an inactive market. On active markets, the Bank trades financial instruments only for the quoted price in the active market. For this reason, there is no difference between the transaction price and the fair value of the financial asset or financial liability that is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique whose variables include only data from observable markets (a “Day 1” profit or loss).

### *3.5.5.4 Financial assets and liabilities classification and subsequent measurement*

Financial assets and liabilities held by the Bank are classified upon initial recognition into appropriate portfolios of financial instruments in accordance with the characteristics of a given instrument, the Bank's intention as of the acquisition date, and pursuant to the Bank's financial instrument investment strategy as follows:

I. Financial assets and liabilities at fair value through profit or loss;
II. Held-to-maturity investments;
III. Loans and receivables;
IV. Available-for-sale financial assets; or
V. Financial liabilities at amortised cost.

The Bank does not make use of an option to designate a financial asset or liability upon initial recognition as a financial instrument at fair value through profit or loss (the so-called "Fair Value Option").

#### *(i) Financial assets and liabilities at fair value through profit or loss*

The Bank designates as financial assets at fair value through profit or loss securities held for trading and derivatives that are assets (i.e. financial instruments acquired by the Bank for the purpose of generating a profit from short-term fluctuations in prices). These financial assets are recognised in the Statement of Financial Position in the line ***'Financial assets at fair value through profit or loss'***.

Securities designated as held for trading include equity and debt securities, treasury bills, bills of exchange and participation certificates. The trading derivative financial instruments used by the Bank include currency and commodity forwards, currency and interest rate swaps, derivatives on securities and emission allowances and options.

Financial liabilities at fair value through profit or loss include liabilities from securities sold and trading derivatives that are liabilities and are recognised in the Statement of Financial Position in the line ***'Financial liabilities at fair value through profit or loss'***.

Unrealised gains and losses, as well as realised gains and losses arising from the fair value measurement of financial assets and liabilities, interest and dividends are recognised as income in the Statement of Income in the line ***'Net profit/(loss) on financial operations'***. These financial assets are not tested for impairment because the change of fair value is recognised directly in profit or loss.

#### *(ii) Held-to-maturity investments*

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank has the positive intent and ability to hold to maturity and which do not meet the definition of loans and receivables (i.e. are quoted on an active market).

Held-to-maturity investments are subsequently measured at amortised cost using the effective interest rate method less any impairment loss through the use of an allowance account. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are integral components of the effective interest rate. The amortisation is included in ***'Interest income and similar income'*** in the Statement of Income. When an impairment of assets is identified, the Bank recognises allowances in the Statement of Income in the line ***'Allowance for impairment of securities'***.

If the Bank were to sell or reclassify more than an insignificant amount of held-to-maturity investments before maturity (other than due to an isolated event that is beyond the Bank's control, which is non-recurring and could not reasonably have been anticipated by the Bank due to a significant decrease of a client's creditworthiness, changes in tax laws, major business combination or major disposition (including sale of a segment), changes in legislative requirements, a significant increase in regulatory capital requirements or significant increase in risk weights for held-to-maturity investments to calculate the capital adequacy), the entire portfolio would have to be reclassified as ***'Available-for-sale financial assets'***. Furthermore, the Bank would be prohibited from classifying any financial asset as ***'Held-to-maturity investments'*** for the following two years.

*(iii) Loans and receivables*

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market other than:

- Assets that the Bank intends to sell immediately or in the near term, which are classified as held for trading, as well as those that the Bank upon initial recognition designates as at fair value through profit or loss;
- Assets that the Bank upon initial recognition designates as available-for-sale; or
- Assets for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration (e.g. asset-backed securities or a fixed rate, interest-only strip created in a securitisation and subject to prepayment risk), which are classified as available-for-sale financial assets or as financial assets at fair value through profit or loss.

Loans and receivables are subsequently measured at amortised cost using the effective interest rate method less any impairment loss through the use of an allowance account. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees that are integral components of the effective interest rate. The amortisation is included in the line ***'Interest income and similar income'*** in the Statement of Income. When impairment of assets is identified, the Bank recognises allowances in the Statement of Income in the line ***'Allowance for loan losses'***.

Financial assets designated as loans and receivables are reported in the Statement of Financial Position in the line ***'Amounts due from banks'*** or in the line ***'Loans and advances to customers'***, as appropriate for the type of debtor.

*(iv) Available-for-sale financial assets*

Available-for-sale financial assets are those non-derivative financial assets that are designated as available-for-sale or are not classified as financial assets at fair value through profit or loss, loans and receivables, or held-to-maturity investments. This portfolio comprises equity securities and debt securities, asset-backed securities and participation certificates.

Available-for-sale financial assets are subsequently measured at fair value and at the end of each reporting period tested to determine whether there is any objective evidence that a financial asset or group of financial assets is impaired. Unrealised gains or losses from the fair value measurement of these assets are recognised within Other Comprehensive Income in the line ***'Net value gain/(loss) on available-for-sale financial assets, net of tax'***) until their sale, maturity or impairment as well as fair value changes arising from changes in foreign exchange rates. Gains or losses from changes in foreign exchange rates on debt instruments are recognised in the Statement of Income in the line ***'Net profit/(loss) on financial operations'*** except for exchange gains or losses related to fair value revaluation that are recognised within Other Comprehensive Income. When the available-for-sale financial asset is disposed of, the cumulative gain or loss previously recognised in equity is recognised in the Statement of Income in the line ***'Net profit/(loss) on financial operations'***.

Accrued interest income for debt securities is recognised in the Statement of Income line ***'Interest income and similar income'***. Dividend income arising from equity securities is recognised when the right for dividends is established and reported in the Statement of Income in the line ***'Dividend income'***.

*(v) Financial liabilities at amortised cost*

Financial liabilities at amortised cost include non-derivative financial liabilities with fixed or determinable payments and are recognised according to the type of counterparty in the lines ***'Amounts due to central banks', 'Amounts due to banks', 'Amounts due to customers', 'Securities issued'*** and ***'Subordinated debt'***.

Financial liabilities at amortised cost are subsequently measured at amortised cost using the effective interest rate method. Interest expense is recognised in the Statement of Income in the line ***'Interest expense and similar expense'***.

In the event of the repurchase of its own debt securities, the Bank derecognises these securities (i.e. the item ***'Securities issued'*** is decreased). Gains and losses arising as a result of repurchasing the Bank's own debt securities are recognised as of the date of their repurchase in the Statement of Income in the line ***'Net interest income'*** as an adjustment to the interest paid from its own bonds.

### *3.5.5.5 Reclassification of financial assets*

The Bank does not reclassify any financial assets after initial recognition into the ***'Financial assets at fair value through profit or loss portfolio'***. In rare circumstances, if non-derivative financial assets at fair value through profit or loss are no longer held for the purpose of selling or repurchasing in the short term, the financial assets may be reclassified out of the portfolio and be classified into the ***'Available-for-sale financial assets'***, or ***'Held-to-maturity investments'*** portfolio.

The Bank may also reclassify a non-derivative trading asset out of the ***'Financial assets at fair value through profit or loss'*** portfolio and into the ***'Loans and receivables'*** portfolio if it meets the definition of loans and receivables and the Bank has the intention and ability to hold the financial asset for the foreseeable future or until maturity. In certain rare circumstances, the Bank may also reclassify financial assets out of the ***'Available-for-sale financial assets'*** portfolio and into the ***'Loans and receivables'*** portfolio if they meet the definition of loans and receivables and the Bank has the intention and ability to hold the financial assets for the foreseeable future or until maturity. Fixed income securities quoted on an active market can be reclassified out of the ***'Available-for-sale financial assets'*** portfolio and into the ***'Held-to-maturity investments'*** portfolio if the Bank's intention or ability to hold these securities has changed or upon expiry of the deadline during which securities were not permitted to be classified as securities held-to-maturity. Reclassifications are recorded at fair value at the date of reclassification, which becomes the new amortised cost.

The Bank may reclassify financial assets or a significant amount out of the ***'Held-to-maturity investments'*** portfolio into the ***'Available-for-sale financial assets'*** portfolio or ***'Loans and receivables'*** portfolio, doing so without triggering the so called "tainting rules", in cases when the given assets are near to maturity, the Bank has received almost the entire original principal of the given financial asset or there has occurred a unique and exceptional event that is outside of the Bank's control and the Bank could not have expected it. Such unique cases include in particular a significant decrease of a client's creditworthiness, changes in tax laws or in legal requirements, a business combination or the sale of a part of the business (segment), a significant increase in regulatory capital requirements or a significant increase in risk weights for held-to-maturity investments used in calculating the capital adequacy.

For a financial asset reclassified out of the ***'Available-for-sale financial assets'*** portfolio, any previous gain or loss on that asset that has been recognised in equity is amortised to profit or loss over the remaining life of the investment using the effective interest rate. Any difference between the new amortised cost and the expected cash flow is also amortised over the remaining life of the asset using the effective interest rate. If the asset is subsequently determined to be impaired, then the amount recorded in equity is recycled to profit or loss. Reclassification is at the election of management and is determined on an instrument-by-instrument basis.

### *3.5.5.6 Determination of a financial instrument's fair value and its hierarchy*

For the determination and categorisation of a financial instrument's fair value, the Bank treats a security as quoted if quoted market prices are readily and regularly available from a stock exchange, dealers, securities traders, industrial groups, valuation services or regulatory authorities and if these prices represent current and regular market transactions under ordinary conditions.

If there are no quoted prices in an active market for the financial asset, the Bank uses other values that are observable, directly or indirectly, from the markets for its measurement, such as:

I. Quoted prices for similar assets or liabilities in active markets;
II. Quoted prices for identical or similar assets or liabilities in markets that are not active (i.e. there are few recent transactions, prices quotations are not based on current information, etc.);
III. Inputs other than quoted prices (e.g. inputs based on interest rates, yield curves, implied volatilities, credit spreads, etc.); or
IV. Inputs derived principally from, or corroborated by, observable market data.

Where the inputs for the determination of a financial instrument's fair value are not observable in a market due to the fact that there is no or only minimal activity for that asset/liability, the Bank uses for fair value measurement inputs that are available but not directly observable within a market and which in the Bank's view reflect assumptions that market participants take into account when pricing the financial instrument.

The fair value of debt securities for which an observable market price is not available is estimated using an income approach (the present value technique taking into account the future cash flows that a market participant would expect to receive from holding the instrument as an asset) and the fair value of unquoted equity instruments is estimated using an income approach or market approach (using prices and other relevant information generated by a market). The fair values of financial derivatives are obtained from quoted market prices, discounted cash flow models or option pricing models and they are adjusted for the credit risk of the counterparty or the Bank's own credit risk, as appropriate.

The existence of published price quotations in an active market is normally the best evidence of fair value. The appropriate quoted market price for an asset held or liability to be issued is usually the current bid price and for an asset to be acquired or liability held the asking price.

The Bank manages the group of financial assets and financial liabilities on the basis of the entity's net exposure to a particular market risk. It uses mid-market prices as the basis for establishing fair values for the offsetting risk positions and applies the bid or asking price to the net open position as appropriate.

When measuring the fair value of a financial asset or group of financial assets, the Bank incorporates into the valuation an adjustment for the risk of default of the counterparty, a so-called credit valuation adjustment (CVA).

### *3.5.5.7 Effective interest rate method*

The effective interest rate is the rate which exactly discounts the estimated future cash payments or receipts through the expected life of a financial instrument.

When calculating the effective interest rate, the Bank estimates cash flows considering all contractual terms of the financial instrument and includes any fees and incremental costs that are directly attributable to the instrument and constitute an integral component of the effective interest rate, but it does not take into consideration future credit losses.

The effective interest rate method is a method of calculating the amortised cost of a financial asset or liability and of allocating the interest income or interest expense over the relevant period.

### *3.5.5.8 Forborne loans*

Forborne exposures are debt contracts in respect of which forbearance measures have been granted to the debtor and for which the discontinuation conditions are not met. Forbearance measures consist of concessions to a debtor facing or about to face difficulties in meeting its financial commitments. The concession refers to either modification of terms and conditions (e.g. changes in payment schedule, interest rate reductions, penalty interest waivers) or refinancing. Once the terms have been renegotiated, any impairment is measured using the original effective interest rate as calculated before the modification of terms. Renegotiated loans are continuously reviewed by the Bank to ensure that all criteria are met and that future payments are likely to occur. The renegotiated loans continue to be subject to impairment assessment, calculated based on their future cash flows discounted by the loans' original effective interest rates.

### *3.5.5.9 Impairment of financial assets*

At the end of each reporting period, the Bank assesses on a regular basis whether there is any objective evidence that a financial asset or group of financial assets is impaired, the only exception being securities at fair value through profit or loss.

Objective evidence that a financial asset or group of assets is impaired includes observable evidence that comes to the attention of the Bank and proving the significant deterioration of a debtor's (issuer's) financial health, breach of contract (default in interest or principal payment), high probability of bankruptcy or other financial reorganisation, or proving a measurable decrease in the estimated future cash flow due to adverse changes in industry conditions.

In addition to the aforementioned events, objective evidence of impairment for an investment in an equity instrument includes information about significant changes with an adverse effect that have taken place in the technological, economic or legal environment in which the issuer operates and significant or prolonged decline in the fair value of the instrument below its cost. The determination of what constitutes a significant or prolonged decline is a matter of circumstances that requires application of the Bank management's judgement. As indicators of possible significant or prolonged decline, the Bank regards unrealised loss in respect of instrument acquisition cost or the fact that the quoted price of the instrument has been below its carrying amount during every trading date for several months. Furthermore, the Bank considers the business model and strategy related to the instrument and supportive indicators as the financial situation of the issuer and its development perspective or regulatory requirements.

If there is objective evidence that an impairment loss on a financial instrument has been incurred, the Bank calculates an impairment loss and recognises it in the respective item in the Statement of Income.

For a financial asset classified in portfolios carried at amortised cost (i.e. ***'Held-to-maturity investments'*** and ***'Loans and receivables'*** portfolios), the amount of the loss is measured as the difference between the asset's carrying amount and the present value of the estimated future cash flow discounted at the financial asset's original effective interest rate. Estimations of future cash flows for loans are based on expected cash flows from the economic activities of the client and the possible realisation of loan collateral.

The Bank uses one of the three methods to assess the amount of allowances (refer to Note 41(A)). For larger, individually significant loans classified as default (Substandard, Doubtful and Loss loans based on the Czech National Bank's classification) the allowances are assessed on an individual basis requiring management to monitor the borrower's repayment abilities individually, including the estimated value from the collateral foreclosure and expected duration of the recovery process, etc. These allowances are calculated using discounted expected future cash flows.

For smaller, individually not significant impaired loans where the loans are homogeneous in nature (for example the consumer and mortgage loans to individuals and smaller corporate portfolios) the allowances are calculated by models using historical delinquency statistics.

Portfolio allowances are calculated for losses that have been incurred but have not been identified. Portfolio allowances are held against non-impaired loans across all segments and calculated using models based on probabilities of default and loss given default until the impairment event occurs and individual or model allowances for impaired loans are recognised.

Historical loss experience is adjusted on the basis of currently observable data to reflect new loss observations and to have better discrimination ability (i.e. to reflect the effects of current conditions on which the historical loss experience is based and to remove the effects of conditions in the historical period that do not exist currently). The methodology and assumptions used for estimating the future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience.

The carrying amount of an asset is reduced through the use of an allowance account, the creation of which is recognised in the Statement of Income in the line ***'Allowance for loan losses'*** or ***'Allowance for impairment of securities'***. If, in a subsequent period, the amount of the impairment loss decreases, the previously recognised impairment loss is correspondingly reversed.

When it can be reasonably anticipated that clients will be unable to fulfil their obligations to the Bank in respect of such loans, loss loans are written off and recognised in the Statement of Income in the line ***'Allowance for loan losses'***. Subsequent recoveries are credited to the Statement of Income in ***'Allowance for loan losses'*** if previously written off. If the Bank collects an amount greater than that written off subsequent to the write-off of the loan, the difference is reported through ***'Interest income and similar income'***.

For ***'Available-for-sale financial assets'*** and in the case of objective evidence of their impairment, a cumulative loss that had been recognised in Other Comprehensive Income is reclassified to the Statement of Income and recognised in the line ***'Allowance for impairment of securities'*** for debt instruments and in the line ***'Net profit/(loss) on financial operations'*** for equity instruments. The amount of the loss is measured as the difference between the acquisition cost (net of any principal repayment and amortisation) and current fair value, less any impairment loss on that financial asset previously recognised in the Statement of Income. If, in a subsequent period, the fair value of a debt instrument increases and the increase can be objectively related to an event occurring after the impairment loss was recognised in the Statement of Income, the impairment loss is reversed, with the amount of the reversal recognised in the Statement of Income. The Bank cannot reverse any impairment loss recognised in the Statement of Income for an equity instrument.

### *3.5.5.10 Repurchase agreements*

The Bank accounts for contracts to sell and buy back financial instruments (so-called "repos" or "reverse repos") based on their substance as the receiving or granting of a loan with a corresponding transfer of financial instruments as collateral.

Under repurchase transactions ("repos"), the Bank only provides securities held in the portfolio of ***'Financial assets or financial liabilities at fair value through profit or loss'*** or in the ***'Available-for-sale financial assets'*** portfolio that are recorded in the Statement of Financial Position in the same lines. The corresponding liability arising from a loan received is recognised in the line ***'Amounts due to banks'*** or ***'Amounts due to customers'***, as appropriate.

Securities purchased under reverse repurchase agreements ("reverse repos") are recorded in the off-balance sheet, where they are remeasured at fair value. The corresponding receivable arising from the provided loan is recognised as an asset in the Statement of Financial Position according to the counterparty type in the line *'Amounts due from banks'* or *'Loans and advances to customers'*.

The Bank is allowed to provide securities received in reverse repo transactions as collateral or sell them even in the absence of default by their owner. These securities continue to be recorded in the off-balance sheet and measured at fair value. The corresponding liability arising from the loan received is included in *'Amounts due to banks'* or *'Amounts due to customers'*, as appropriate. The Bank has the obligation to return these securities to its counterparties.

The differences between the sale and repurchase prices in respect of repo and reverse repo transactions are treated by the Bank as interest, and it is accrued evenly to expenses and income over the life of the repo agreement using the effective interest rate method.

In regard to the sale of a security acquired as collateral under a reverse repo transaction, the Bank derecognises from the off-balance sheet evidence the security acquired under the reverse repo transaction and recognises in the Statement of Financial Position an amount payable from a short sale that is remeasured at its fair value. This payable is included in *'Financial liabilities at fair value through profit or loss'*.

### *3.5.5.11 Derivatives and hedge accounting*

A derivative is a financial instrument or other contract having all three of the following characteristics:

- Its value changes in response to the change in a specified interest rate, financial instrument price, commodity price, foreign exchange rate, index of prices or rates, credit rating or credit index, or other market variable;
- It requires no initial net investment or an initial net investment that is smaller than would be required for other types of contracts that would be expected to have a similar response to changes in market factors; and
- It is settled at a future date.

At the inception of a financial derivative contract, the Bank designates the derivative instrument as either held for trading or hedging.

Held for trading derivatives are classified into a portfolio of *'Financial assets or financial liabilities at fair value through profit or loss'* based on whether the fair value is positive or negative (refer to 3.5.5.4 Financial assets and liabilities classification and subsequent measurement).

Hedging derivatives are derivatives that the Bank uses to hedge against interest rate and foreign exchange rate risks to which it is exposed as a result of its financial market transactions. The Bank designates a derivative as hedging only if the criteria set out under IFRS are met at the designation date, i.e. if, and only if, all of the following conditions are met:

- There is compliance with the Bank's risk management objective and strategy in undertaking the hedge;
- At inception of the hedge there is formal designation and documentation of the hedging relationship which includes identification of the hedging instrument, the hedged item or transaction, the nature of the risk being hedged and how the entity will assess the hedging instrument's effectiveness in offsetting the exposure to changes in the hedged item's fair value or cash flows attributable to the hedged risk;
- The hedge is expected to be highly effective at inception and throughout the period;
- The effectiveness of the hedge can be reliably measured; and
- Changes in the fair value or cash flows of the hedged item are almost fully offset by changes in the fair value or cash flows of the hedging instrument and the results are within a range of 80% to 125%.

Hedging derivatives are accounted for according to the type of hedging relationship, which can be one of the following:

I. Hedging of an exposure to changes in fair value of a recognised asset or liability or an unrecognised firm commitment, or an identified portion of such an asset, liability or firm commitment that is attributable to a particular risk and that could affect profit or loss (fair value hedge); or
II. Hedging of an exposure to variability in cash flows that is attributable to a particular risk associated with a recognised asset or liability or a highly probable forecast transaction and that could affect profit or loss (cash flow hedge); or
III. Hedging of a net investment in a foreign operation.

Changes in the fair value of a derivative that is designated and qualified as a fair value hedge are recognised in the Statement of Income line *'Net profit/(loss) on financial operations'*. Changes in the fair value of a hedged item are recognised in the Statement of Financial Position as a component of the carrying amount of the hedged item and in the Statement of Income line *'Net profit/(loss) on financial operations'*.

It is on this basis that the Bank hedges the interest rate risk and foreign currency risk of financial assets (loans with fixed interest rates and debt instruments classified as available-for-sale) and interest rate risk of deposits, repos and mortgage bonds issued. The effectiveness of a hedge is regularly tested through prospective and retrospective tests on a quarterly basis.

If the hedge no longer meets the criteria for hedge accounting or the hedging instrument expires or is sold, terminated or exercised, the entity revokes the designation and an adjustment to the carrying amount of the hedged interest-bearing financial instrument is amortised to profit or loss over the period until the maturity of the hedged item.

In connection with the reclassification of certain debt securities from the *'Available-for-sale financial assets'* portfolio and into the *'Held-to-maturity investments'* portfolio, the Bank revoked the designation of respective interest rate swaps as fair value hedges and prospectively classifies them as a cash flow hedge of interest rate risk associated with selected portfolios of assets or liabilities.

Changes in the fair value of hedging derivatives classified as cash flow hedges and that prove to be highly effective in relation to the hedged risks are recognised in the line *'Cash flow hedging'* in Other Comprehensive Income and they are transferred to the Statement of Income and classified as income or expense in the periods during which the hedged items affect the Statement of Income. The ineffective portion of a hedge is charged directly to the Statement of Income in the line *'Net profit/(loss) on financial operations'*.

It is on this basis that the Bank hedges the interest rate risk and currency risk associated with selected portfolios of assets or liabilities or individually significant assets or liabilities. The effectiveness of a hedge is regularly tested through prospective and retrospective tests on a quarterly basis.

If the hedge no longer meets the criteria for hedge accounting, the hedging instrument expires or is sold, terminated or exercised, the entity revokes the designation and the cumulative gain or loss on the hedging instrument that has been recognised in Other Comprehensive Income for the period when the hedge was effective remains in equity until the forecast transaction occurs.

If the forecast transaction is no longer expected to occur, the gain or loss accumulated as other comprehensive income is reclassified to profit or loss.

The Bank additionally hedges against the foreign exchange rate risk arising from the net investment in the subsidiary Bastion European Investments S.A. Foreign currency deposits are used as a hedging instrument. Foreign exchange rate differences arising from its retranslation are included in Other Comprehensive Income.

Financial derivatives constituting economic hedges under the Bank's risk management positions but not qualifying for hedge accounting under the specific rules of IAS 39 are treated as derivatives held for trading.

The fair values of derivative instruments held for trading and hedging purposes are disclosed in Note 41(C).

*3.5.5.12 Embedded derivatives*

In some cases, a derivative, such as an option for an earlier redemption of a bond, is a component of a hybrid (combined) financial instrument that also includes a non-derivative host contract. The embedded derivative is separated and accounted for as a derivative if, and only if, all of the following conditions are met:

- The embedded derivative as a separate instrument meets the definition of a derivative;
- The economic characteristics and risks of the embedded derivative are not closely related to those of the host contract; and
- The host contract is not measured at fair value with fair value changes recognised in the Statement of Income.

### 3.5.6 Assets held for sale

The line ***'Assets held for sale'*** represents assets for which the Bank expects that their carrying amounts will be recovered principally through sale transactions rather than through continuing use. These assets are available for immediate sale in their present condition, they are actively marketed for sale at a price that is reasonable in relation to their current fair value, and their sale is highly probable, that is to say that a plan to sell and leading to the location of a buyer has been initiated. The Bank expects that the sale of assets will be completed, the market situation permitting, within one year from the date of the assets classification as ***'Assets held for sale'***.

Assets held for sale are measured at the lower of:

- The carrying amount of the respective asset at the date of its classification as ***'Assets held for sale'***; or
- Fair value less estimated costs to sell (e.g. cost of expert valuation reports, legal or financial advisory services, the estimates of which are based on historical experience, as well as real estate transfer tax for real estate).

Assets designated as ***'Assets held for sale'*** are no longer depreciated.

The Bank recognises an impairment loss on assets held for sale in the line ***'Depreciation, amortisation, impairment and disposal of assets'*** if their selling price less estimated costs to sell is lower than their carrying value. Any subsequent increase in the selling price less costs to sell is recognised as a gain but not in excess of the cumulative impairment loss that has been recognised either during the time when the assets were classified as held for sale or before their reclassification into the line ***'Assets held for sale'*** (i.e. during the period when the asset had been held for supplying the Bank's services or for administrative purposes).

### 3.5.7 Income tax

#### *3.5.7.1 Current income tax*

Current tax assets and liabilities for the current and prior years are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those valid as of the Statement of Financial Position date.

Current income tax is recognised in the Statement of Income, or, as the case may be, in the Statement of Other Comprehensive Income if it relates to an item directly taken into other comprehensive income.

The Bank does not set off current tax assets and current tax liabilities unless it has a legally enforceable right to set off the recognised amounts and intends either to settle them on a net basis or to realise the asset and settle the liability simultaneously.

#### *3.5.7.2 Deferred income tax*

Using the balance sheet liability method, deferred income tax is recorded for temporary differences arising between the tax bases of assets and liabilities and their carrying values presented in the Statement of Financial Position. Deferred income tax is determined using tax rates valid or substantially enacted for the periods in which the Bank expects to realise the deferred tax asset or to settle the deferred tax liability. A deferred tax asset is recognised to the extent that it is probable that future taxable profit will be available against which the tax asset can be used.

Deferred income tax is recognised in the Statement of Income, or, as the case may be, in the Statement of Other Comprehensive Income if it relates to an item directly taken into other comprehensive income (such as deferred income tax related to changes in the fair value of available-for-sale financial assets or in relation to a cash flow hedge).

The Bank offsets deferred income tax assets and deferred income tax liabilities only if it has a legally enforceable right to set off current tax assets against current tax liabilities and deferred tax assets and deferred tax liabilities relate to income tax levied by the same taxation authority and relate to the same taxable entity.

The largest temporary differences relate to tangible and intangible assets, loans and receivables, hedging derivatives, available-for-sale financial assets and retirement benefits.

### 3.5.8 Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and rewards of ownership to the lessee. All other leases are classified as operating leases.

The Bank as lessor

*Operating leases*

The Bank presents assets that are the subject of an operating lease in the appropriate lines within the Statement of Financial Position according to the nature of those assets and uses for them accounting policies applied to the relevant asset class.

Leasing payments received from operating leases are recognised as the Bank's income on a straight-line basis over the term of the relevant lease and is presented in the line *'Other income'*.

*Finance leases*

When assets held are subject to a finance lease, the net investment in the lease is recognised as *'Loans and advances to customers'* while the assets themselves are not recognised. The difference between the gross receivable and the present value of the receivable is recognised as deferred interest income.

Lease income is recognised over the term of the lease, reflecting a constant periodic rate of interest on the remaining balance of the receivable, and is presented in the line *'Interest income and similar income'*.

The Bank as lessee

*Operating leases*

Lease payments under an operating lease are recognised on a straight-line basis over the lease term and are presented in the line *'General and administrative expenses'*. Possible penalty payments due to the early termination of a lease are recognised in the reporting period in which the lease was terminated.

*Finance leases*

At the commencement of a lease term, an asset held under a finance lease is recognised in the appropriate line within the Statement of Financial Position in accordance with the nature of the asset and simultaneously a liability is recognised in an amount equal to the fair value of the leased property or, if lower, the present value of the minimum lease payments. Subsequently, the Bank uses the same accounting policies for these assets as for its own property presented in the same line as the leased asset. If the legal ownership of the asset held under finance lease is not transferred to the lessee by the end of the lease term, however, the asset is depreciated on a straight-line basis over the lease term.

The Bank divides lease payments between amortisation recognised as the reduction of the outstanding liability and a finance charge recognised in the Statement of Income as *'Interest expense and similar expense'*. The finance charge is allocated so as to produce a constant periodic rate of interest on the remaining balance of the liability during the entire lease period.

### 3.5.9 Tangible and intangible assets

Intangible assets include principally software and internally generated intangible assets (mainly software). Tangible assets include plant, property and equipment that are used by the Bank in supplying its services and for administrative purposes and that are used for longer than one reporting period.

Tangible and intangible assets are measured at the historical acquisition cost less accumulated impairment losses (allowances) and, in the case of depreciated assets, less accumulated depreciation and increased by technical improvements. The historical acquisition cost comprises the purchase price and any costs directly attributable to asset acquisition such as delivery and handling costs, installation and assembly costs, advisory fees, and administrative charges. The acquisition cost of internally generated intangible assets comprises external expenses and internal personnel expenses related to an internal project's development phase. The Bank capitalises no expenses related to the research phase.

Tangible and intangible assets are depreciated from their acquisition costs on a straight-line basis over their useful lives. Cars under finance leases are depreciated from acquisition cost less estimated residual value, which is determined on the basis of the purchase price following expiration of the lease as established in the lease contract. The Bank assumes no residual value for other assets. Depreciation and amortisation are reported in the Statement of Income on the line *'Depreciation, amortisation, impairment and disposal of assets'*.

The Bank does not depreciate land and works of art. Tangible and intangible assets in the course of construction and technical improvements are depreciated only once they have been brought into a condition fit for use.

*During the reporting period, the Bank used the following useful lives in years:*

| | 2016 | 2015 |
|---|---|---|
| Machinery and equipment | 4 | 4 |
| Information technology – notebooks, servers | 4 | 4 |
| Information technology – desktop computers | 6 | 6 |
| Fixtures, fittings and equipment | 6 | 6 |
| Vehicles | 5 | 5 |
| ATMs | 10 | 10 |
| Selected equipment of the Bank | 8 | 8 |
| Energy machinery and equipment | 12/15 | 12/15 |
| Distribution equipment | 20 | 20 |
| Buildings and structures | 40 | 40 |
| Buildings and structures – selected components: | | |
| – Heating, air-conditioning, windows, doors | 20 | 20 |
| – Lifts, electrical installations | 25 | 25 |
| – Facades | 30 | 30 |
| – Roofs | 20 | 20 |
| – Residual value of buildings and technical improvements without selected components | 50 | 50 |
| Technical improvements on leasehold assets | According to the lease term | According to the lease term |
| Intangible results of development activities (assets generated internally as component of internal projects) | According to the useful life, typically 5 | According to the useful life, typically 5 |
| Licences – software | 5 | 5 |
| Other rights of use | According to contract | According to contract |

At the end of each reporting period, the Bank assesses whether there exists any indication that a tangible or intangible asset can be impaired. Indicators of possible impairment include information about a significant decline in an asset's market value, significant changes within the technological, market, economic or legal environment, obsolescence or physical damage to an asset, or change in the manner in which the asset is used. Where any such indicator exists, the Bank estimates the recoverable amount of the asset concerned (i.e. the higher amount of its fair value less costs to sell in comparison with the asset's carrying value). If the asset's carrying amount is greater than its recoverable amount, the Bank reduces its carrying amount to its recoverable amount and presents the recognised impairment loss in the line ***'Depreciation, amortisation, impairment and disposal of assets'***.

Repairs and maintenance are charged directly to the Statement of Income when they occur.

### 3.5.10 Provisions

Provisions are recognised when and only when:

- The Bank has a present obligation (legal or constructive) as a result of a past event;
- It is probable that settlement of the obligation will cause an outflow of resources causing a decrease of economic benefits; and
- A reliable estimate can be made of the amount of the obligation. Provisions for legal disputes are estimated on the basis of the amount sought by the plaintiff, including accrued interest and fees.

Provisions are measured at the best estimate of the expenditure required to settle the present obligation at the end of the reporting period. Where the effect of the time value of money is material, the amount of a provision is the present value of the expenditure expected to be required to settle the obligation. The discount rate is a pre-tax rate reflecting current market assessments and the risks specific to the liability. Provision increases related to the passage of time are recognised as interest expense.

Among others, the Bank recognises provisions for credit-related commitments which do not meet the criteria for recognition in the Statement of Financial Position. These provisions cover estimated losses from credit-related commitments into which the Bank enters in the normal course of its business and that are recorded in the off-balance sheet. These commitments include primarily guarantees, avals, uncovered letters of credit, irrevocable commitments to extend credit, undrawn loan commitments, and approved overdraft loans. Provisions for credit-related commitments are created on the same basis as are allowances for loan portfolios (refer to Note 32).

## 3.5.11 Employee benefits

### *3.5.11.1 General*

The Bank provides its employees with retirement benefits and disability benefits. The employees are entitled to receive retirement or disability benefits if they are employed by the Bank until their retirement age or if they are entitled to receive a disability pension but only if they were employed within the Bank for a minimum defined period.

Estimated benefit costs are recognised on an accruals basis through a provision over the employment term using an accounting methodology that is similar to the methodology used in respect of defined benefit pension plans. In determining the parameters of the model, the Bank refers to the most recent employee data (the length of employment with the Bank, age, gender, average salary) and estimates made on the basis of monitored historical data about the Bank's employees (expected reduction of the current staffing levels) and other estimates (the amounts of bonuses, anticipated increase in salaries, estimated amounts of social security and health insurance contributions, discount rate).

These provisions are presented in the line ***'Provisions'***. The changes in provisions are disaggregated into three components that are presented as follows:

I. Service cost (i.e. additional liability that arises from employees providing service during the period) is presented in the line ***'Personnel expenses'***;
II. The interest expense on the net benefit liability is presented in the line ***'Personnel expenses'***; and
III. Other changes in the value of the defined benefit obligation, such as changes in estimates, are presented within Other Comprehensive Income in the line ***'Remeasurement of retirement benefits plan, net of tax'***.

The use of a provision is presented in the line ***'Personnel expenses'***.

The Bank additionally provides short-term benefits to its employees, such as contributions to retirement pension insurance and capital life insurance schemes. The Bank recognises the costs of these contributions as incurred in the line ***'Personnel expenses'*** (refer to Note 9).

The Bank has the following share plans and deferred compensation schemes:

### *3.5.11.2 Deferred bonus payments*

In accordance with European regulation (Capital Requirements Directive III; No. 2010/76/EU), the Bank implemented a new compensation scheme for employees whose professional activities have a material impact on the Bank's risk profile. For employees identified in accordance with the CRD III regulation, performance-linked remuneration is split into two components: (i) a non-deferred component which is paid in the following year; and (ii) a deferred component which is spread over three years. The amounts of the two components are further split into bonuses paid in cash and bonuses paid in cash equivalent of the Société Générale S.A. share price or in cash equivalent of the Komerční banka, a.s. share price (indexed bonuses). Both bonuses are subject to presence and performance conditions:

- In the case of bonuses paid in the cash equivalent of the Société Générale S.A. share price, the performance condition is based on the profitability of the Société Générale Group;
- In the case of bonuses paid in cash and bonuses paid in cash equivalent of the Komerční banka, a.s. share price, the performance condition is based on the profitability of the Komerční banka Group. Moreover, for investment banking employees there is the condition that the Bank's net investment banking operating income be higher than zero.

Indexed bonuses qualify as cash-settled share-based transactions. The liability is measured at the end of each reporting period until settled at the fair value of the shares of Société Générale S.A. or Komerční banka, a.s. multiplied by numbers of shares granted and it is spread over the vesting period.

The amount of bonuses finally vested is calculated as the number of Société Générale S.A. shares or Komerční banka, a.s shares multiplied by their price fixed as the volume-weighted average of the last 20 closing trading prices prior to the first business day following the end of the applicable retention period.

Deferred cash bonuses (i.e. bonuses paid to employees more than 12 months after the end of the reporting period in which the employees render the related services) are considered as long-term employee benefits and the related expense is recognised over the vesting period in the line ***'Personnel expenses'***.

### *3.5.11.3 Free share plan*

In November 2010, the Bank awarded all its employees rights to 40 free shares of Société Générale S.A. upon the achievement of two performance conditions and completing a specific period of employment.

The allotment of the shares proceeded in two tranches:

- The first tranche accounted for 40% of the planned allocation (i.e. 16 shares) and it was contingent on Société Générale Group's achieving a positive net income in 2012 (the initial criterion of at least 10% return on equity, net of tax was changed by decision of the Société Générale Board of Directors based on agreement of the General Shareholders' Meeting held on 22 May 2012). The Bank's employees received those shares on 31 March 2015;
- The second tranche accounted for 60% of the planned allocation (i.e. 24 shares) and it was contingent on customer satisfaction increasing between 2010 and 2013 in the Société Générale Group's three core businesses (French Networks, International Retail Banking, Corporate and Investment Banking). This condition having been met the Bank's employees received those shares on 31 March 2016.

The second and final tranche having been allocated this free share plan was completed in 2016.

To enhance loyalty and motivation to contribute to the long-term growth in the value of the Société Générale Group, the Bank can award some of its key employees further free shares (deferred share plan). These free shares are subject to a vesting condition (i.e. presence in the Group at the end of vesting period which is 4 years) and for certain beneficiaries are also subject to the condition that Société Générale Group records positive net income.

Expenses related to the free share and deferred share plans provided by Société Générale to the Bank's employees are recognised in the Bank's financial statements as equity-settled share-based payment transactions. The fair value of these instruments, measured using the arbitrage model at the grant date, is spread over the vesting period and recorded in the lines ***'Personnel expenses'*** and ***'Share premium and reserves'*** under equity. At the end of each accounting period, the number of these instruments is adjusted in order to take into account performance and service conditions and adjust the overall cost of the plan as originally determined. Expenses recognised under the ***'Personnel expenses'*** from the start of the plan are then adjusted accordingly.

### 3.5.12 Share capital

*Dividends on ordinary shares*

Dividends on ordinary shares are recognised as a liability and deducted from equity at the time they are approved by the Bank's shareholders.

*Treasury shares*

When the Bank acquires its own equity instruments, the consideration paid, and including any attributable transaction costs, is recognised as a deduction from the line ***'Share premium and reserves'*** under equity. Gains and losses on sales of treasury shares are recognised in equity and presented as well in the line ***'Share premium and reserves'***.

### 3.5.13 Contingent assets, contingent liabilities and off-balance sheet items

In addition to transactions giving rise to the recognition of assets and liabilities in the Statement of Financial Position, the Bank enters into transactions through which it generates contingent assets and liabilities. The Bank maintains contingent assets and liabilities as off-balance sheet items. The Bank monitors these transactions inasmuch as they represent a substantial proportion of its activities and materially impact the level of risks to which the Bank is exposed (they may increase or decrease other risks, for instance, by hedging assets and liabilities reported in the Statement of Financial Position).

A contingent asset/liability is defined as a possible asset/liability that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events not wholly under the Bank's control.

A contingent liability also exists in the case of a present obligation where an outflow of resources embodying economic benefits probably will not be required to settle the obligation or the amount of the obligation cannot be measured reliably. Contingent liabilities include, for example, irrevocable loan commitments, commitments arising from bank guarantees, bank acceptances, letters of credit and warrants.

In addition to contingent assets and contingent liabilities, the off-balance sheet includes assets arising from valuables and securities custody and fiduciary activities and related obligations to return these to customers (e.g. Assets under Management).

Off-balance sheet items include also nominal values of such interest and foreign currency instruments as forwards, swaps, options and futures. More information regarding derivative operations is presented in note 3.5.5.11 Derivatives and hedge accounting.

### 3.5.14 Operating segments

Operating segments are reported in accordance with internal reports regularly prepared and presented to the Bank's Board of Directors, which is considered the "chief operating decision maker" (i.e. a person or group of persons that allocates resources and assesses the performance of individual operating segments of the Bank).

The Bank has the following operating segments:

- *Retail Banking:* includes the provision of products and services to individuals (i.e. predominantly current and savings accounts, term deposits, overdrafts, credit card loans, personal loans and mortgages);
- *Corporate Banking:* includes the provision of products and services to corporate entities (i.e. current accounts, term deposits, revolving loans, business loans, mortgages, foreign currency and derivative products, syndicated and export financing, and guarantee transactions);
- *Investment Banking:* involves trading in financial instruments; and
- *Other:* consists of the head office of the Bank.

The Investment Banking segment does not reach quantitative limits for obligatory reporting. The management of the Bank nevertheless believes that the information concerning this segment is useful for users of the Financial Statements and thus reports this segment separately.

As the principal activity of the Bank is the provision of financial services, the Board of Directors of the Bank assesses the performance of operating segments predominantly according to net interest income. For this reason, interest income and interest expense of individual operating segments are not reported separately but on a net basis.

In addition, the Bank monitors net fee and commission income, net profit/(loss) on financial operations, and other income predominantly including income from the lease of non-residential premises by segments. Other profit and loss items are not monitored by operating segments.

The Bank does not monitor total assets or total liabilities by segment.

The information on the items of net operating income is provided to the Board of Directors of the Bank using valuations identical to those stated in the Bank's financial accounting records.

The Bank has no client or group of related parties for which the income from transactions would account for more than 10% of the Bank's total income.

### 3.5.15 Regulatory requirements

The Bank is subject to the regulatory requirements of the CNB and other institutions. These regulations include limits and other restrictions pertaining to minimum capital adequacy requirements, classification of loans and off-balance sheet commitments, and creation of allowances to cover credit risk associated with the Bank's clients, as well as with its liquidity, interest rate and foreign currency positions.

## 3.6 Changes in accounting policies and reclassifications

From 1 January 2016, the following changes were made in reporting of several items for better presentation of their nature and to conform with the recommendations of the European Banking Authority and the Group's principles. Comparative information has been restated to reflect the presentation of the current period. The reconciliation of the lines is shown in the tables below.

*Reconciliation of lines in the Statement of Income for the year ended 31 December:*

| | As reported | Restated | |
|---|---|---|---|
| (CZKm) | 2015 | 2015 | Reference |
| Interest expense and similar expense | (7,368) | (6,518) | 1 |
| Net fee and commission income | 6,275 | 6,287 | 2 |
| General and administrative expenses | (4,153) | (5,015) | 1, 2 |

1. Contributions to the Deposit Insurance Fund in the amount of CZK 850 million were reclassified from the line ***'Interest expense and similar expense'*** to the line ***'General and administrative expenses'***.

2. Contributions to the Investor Compensation Fund in the amount of CZK 12 million were reclassified from the line ***'Net fee and commission income'*** to the line ***'General and administrative expenses'***.

*Reconciliation of lines in the Statement of Financial Position as of 31 December:*

| | As reported | Restated | As reported | Restated | |
|---|---|---|---|---|---|
| (CZKm) | 31 Dec 2015 | 31 Dec 2015 | 31 Dec 2014 | 31 Dec 2014 | Reference |
| Amounts due to customers | 603,640 | 593,059 | 601,412 | 588,447 | 1 |
| Securities issued | 43,717 | 54,298 | 55,321 | 68,286 | 1 |

1. Depository bills of exchange in the amount of CZK 10,581 million (2014: 12,965 million) were reclassified from the line ***'Amounts due to customers'*** to the line ***'Securities issued'***.

*Reconciliation of lines in the Statement of Cash Flow for the year ended 31 December:*

| | As reported | Restated | |
|---|---|---|---|
| (CZKm) | 2015 | 2015 | Reference |
| Interest paid | (5,895) | (5,045) | 1 |
| Fee and commission paid | (1,300) | (1,288) | 2 |
| Cash payments to employees and suppliers, and other payments | (9,520) | (10,382) | 1, 2 |
| Amounts due to customers | 1,837 | 4,221 | 3 |
| Securities redeemed | (13,958) | (16,342) | 3 |

1. Contribution to the Deposit Insurance Fund in the amount of CZK 850 million was reclassified from the line ***'Interest paid'*** to the line ***'Cash payments to employees and suppliers and other payments'***.

2. Contribution to the Investor Compensation Fund in the amount of CZK 12 million was reclassified from the line ***'Fee adn commission paid'*** to the line ***'Cash payments to employees and suppliers and other payments'***.

3. The cash operations from depository bills of exchange in the amount of CZK -2,384 million were reclassified from the line ***'Amounts received from customers'*** to the line ***'Securities redeemed'***.

## 4 Segment reporting

| | Retail banking | | Corporate banking | | Investment banking | | Other | | Total | |
|---|---|---|---|---|---|---|---|---|---|---|
| (CZKm) | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 | 2016 | 2015 |
| Net interest income and similar income | 9,963 | 9,900 | 6,544 | 6,727 | 85 | 120 | 3,979 | 3,136 | 20,571 | 19,883 |
| Net fee and commission income | 3,797 | 3,994 | 2,005 | 2,054 | (40) | (29) | 217 | 268 | 5,979 | 6,287 |
| Net profit/(loss) on financial operations | 913 | 877 | 1,432 | 1,312 | 456 | 483 | 1,032 | (7) | 3,833 | 2,665 |
| Other income | 127 | 110 | 23 | 12 | 116 | 110 | (41) | (72) | 225 | 160 |
| **Net operating income** | **14,800** | **14,881** | **10,004** | **10,105** | **617** | **684** | **5,187** | **3,325** | **30,608** | **28,995** |

Given the specifics of banking activities, the Board of Directors of the Bank (the chief operating decision maker) is provided with information on income, recognition of allowances, write-offs and income tax only for selected segments rather than consistently for all segments. For this reason, this information is not reported for segments.

As most of the income of segments arises from interest, and, in assessing the performance of segments and deciding on allocation of resources for segments, the Board of Directors primarily refers to net interest income, the interest for segments is reported on a net basis (i.e. reduced by interest expense).

Transfer prices between operating segments are based on transfer interest rates representing actual market interest rate conditions, including a liquidity component reflecting the existing opportunities to acquire and invest financial resources.

The Bank's income is primarily – more than 99% (2015: more than 98%) – generated on the territory of the Czech Republic.

## 5 Net interest income and similar income

*Net interest income and similar income comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Interest income and similar income | 23,186 | 24,703 |
| Interest expense and similar expense | (5,337) | (6,518) |
| Dividend income | 2,722 | 1,698 |
| **Net interest income and similar income** | **20,571** | **19,883** |
| Of which net interest income and similar income from | | |
| – Loans and advances | 13,543 | 13,994 |
| – Available-for-sale financial assets | 594 | 756 |
| – Held-to-maturity investments | 1,651 | 1,764 |
| – Financial liabilities at amortised cost | (1,648) | (2,254) |
| – Hedging financial derivatives | 3,709 | 3,925 |
| – Dividends | 2,722 | 1,698 |

*'Interest income and similar income'* includes interest on Substandard, Doubtful and Loss loans due from customers of CZK 276 million (2015: CZK 318 million).

*'Interest income and similar income'* also includes accrued interest income from hedging financial derivatives of CZK 7,399 million (2015: CZK 8,189 million) and *'Interest expense and similar expense'* includes interest expense from hedging financial derivatives of CZK 3,690 million (2015: CZK 4,264 million). Net interest income from these derivatives amounts to CZK 3,709 million (2015: CZK 3,925 million). Hedging financial derivatives are used to hedge both the fair value and future cash flows.

*'Dividend income'* includes dividends received from subsidiaries and associates of CZK 2,722 million (2015: CZK 1,703 million). Expenses from hedging financial derivatives used to hedge cash flows from foreign exchange risk for dividends from subsidiaries and associates were CZK 0 million (2015: CZK 5 million).

In 2016, the Bank recorded as part of *'Net interest income and similar income'* also negative interest income and expense from selected clients' deposits in selected currencies, from selected repo transactions, loro and nostro accounts, and margin accounts deposited at banks. The total amount recognised is not material.

## 6 Net fee and commission income

*Net fee and commission income comprises the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Deposit product fee and commission income | 751 | 875 |
| Loan fee and commission income | 962 | 972 |
| Transaction fee and commission income | 3,373 | 3,934 |
| Cross-selling fee income | 742 | 726 |
| Specialised financial services fee and commission income | 900 | 938 |
| Other fee and commission income | 137 | 130 |
| **Total fee and commission income** | **6,865** | **7,575** |
| Deposit product fee and commission expense | (156) | (151) |
| Loan fee and commission expense | (110) | (99) |
| Transaction fee and commission expense | (529) | (941) |
| Cross-selling fee expense | (11) | (1) |
| Specialised financial services fee and commission expense | (62) | (57) |
| Other fee and commission expense | (18) | (39) |
| **Total fee and commission expenses** | **(886)** | **(1,288)** |
| **Total net fee and commission income** | **5,979** | **6,287** |

*'Net fee and commission income'* comprises fee income arising from trust and other fiduciary activities and depository services in the amount of CZK 148 million (2015: CZK 130 million) and fee expense for these services in the amount of CZK 23 million (2015: CZK 19 million).

## 7 Net profit/(loss) on financial operations

*Net profit/(loss) on financial operations comprises the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Net realised gains/(losses) on securities held for trading | (282) | 335 |
| Net unrealised gains/(losses) on securities held for trading | (336) | 166 |
| Net realised gains/(losses) on securities available-for-sale | 959 | 0 |
| Net realised and unrealised gains/(losses) on security derivatives* | 780 | (343) |
| Net realised and unrealised gains/(losses) on interest rate derivatives | 330 | 210 |
| Net realised and unrealised gains/(losses) on trading commodity derivatives | 23 | 32 |
| Net realised and unrealised gains/(losses) on foreign exchange operations | 1,157 | 1,113 |
| Net realised gains/(losses) on foreign exchange from payments | 1,202 | 1,152 |
| **Total net profit/(loss) on financial operations** | **3,833** | **2,665** |

* This line also includes impacts of derivative trades in emission allowances.

For the year ended 31 December 2016, the line *'Net realised gains/(losses) on securities available-for-sale'* includes the net gain from the sale of an equity stake in Visa Europe Limited in the amount of CZK 959 million (refer to Note 18).

A loss of CZK 230 million (2015: gain of CZK 385 million) on the fair value of interest rate swaps for interest rate risk hedging is included in *'Net realised and unrealised gains/(losses) on interest rate derivatives'*. This amount matches the loss arising from retranslation of hedged loan receivables, available-for-sale financial assets, deposits or repos and issued mortgage bonds reported in the same line.

## 8 Other income

The Bank reports *'Other income'* in the amount of CZK 225 million (2015: CZK 160 million). In both 2016 and 2015, *'Other income'* was predominantly composed of income from services provided to the Group's companies and the Société Générale Group entities as well as property rental income.

## 9 Personnel expenses

*Personnel expenses comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Wages, salaries and bonuses | 4,471 | 4,336 |
| Social costs | 1,790 | 1,749 |
| **Total personnel expenses** | **6,261** | **6,085** |
| Physical number of employees at the end of the period* | 7,663 | 7,665 |
| Average recalculated number of employees during the period* | 7,549 | 7,538 |
| **Average cost per employee (CZK)** | **829,381** | **807,243** |

* Calculation according to Czech Statistical Office methodology.

*'Social costs'* include costs of CZK 78 million (2015: CZK 78 million) paid by the Bank to the employees' retirement pension insurance scheme and costs of CZK 42 million (2015: CZK 43 million) incurred in contributing to the employees' capital life insurance scheme.

*Indexed bonuses*
In 2016, the total amount relating to bonuses indexed on the Komerční banka share price recognised in *'Personnel expenses'* was CZK 45 million (2015: CZK 32 million) and the total amount of CZK 55 million (2015: CZK 49 million) was recognised as a liability. These amounts do not include the costs of social and health insurance and retirement pension insurance paid by the Bank. Net loss from hedging indexed bonuses by fair value hedge and cash flow hedge derivatives was CZK 7 million (2015: net gain of CZK 11 million). The total number of Société Générale shares according to which bonuses indexed on the Société Générale share price are calculated is 0 shares (2015: 0 shares). The total number of Komerční banka shares according to which bonuses indexed on the Komerční banka share price are calculated is 18,570 shares (2015: 16,572 shares).

*The changes in the numbers of shares were as follow:*

| | 2016 | | 2015 | |
|---|---|---|---|---|
| (in shares) | SG shares | KB shares | SG shares | KB shares |
| **Balance as of 1 January** | **0** | **16,572** | **6,232** | **17,310** |
| Paid out during the period | 0 | (8,690) | (6,232) | (5,840) |
| Presumed number of newly guaranteed shares | 0 | 10,688 | 0 | 5,102 |
| **Balance as of 31 December** | **0** | **18,570** | **0** | **16,572** |

*Free and deferred share plans*
For 2016, the total amount relating to the free shares programme and deferred share plans recognised in *'Personnel expenses'* was CZK 24 million (2015: CZK 59 million).

*The changes in the numbers of shares were as follow:*

| | 2016 | | 2015 | |
|---|---|---|---|---|
| (in shares; EUR) | Number of shares | Average price | Number of shares | Average price |
| **Balance as of 1 January** | **318,673** | **35.12** | **433,209** | **35.18** |
| Granted during the year | 31,988 | 29.55 | 36,090 | 33.01 |
| Forfeited during the year | (18,996) | 37.19 | (10,537) | 35.12 |
| Exercised during the year | (211,110) | 34.00 | (140,089) | 34.49 |
| **Balance as of 31 December** | **120,555** | **31.62** | **318,673** | **35.12** |

## 10 General and administrative expenses

*General and administrative expenses comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Insurance | 67 | 79 |
| Marketing and representation | 499 | 482 |
| Sale and banking products expenses | 278 | 289 |
| Other employees expenses and travelling | 122 | 119 |
| Real estate expenses | 1,215 | 1,239 |
| IT support | 989 | 955 |
| Equipment and supplies | 121 | 127 |
| Telecommunications, postage and data transfer | 209 | 226 |
| External consultancy and other services | 490 | 535 |
| Resolution and similar funds | 851 | 862 |
| Other expenses | 79 | 102 |
| **Total general and administrative expenses** | **4,920** | **5,015** |

## 11 Depreciation, amortisation, impairment and disposal of assets

*Depreciation, amortisation, impairment and disposal of assets comprise the following:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Tangible and intangible assets depreciation and amortisation (refer to Notes 25 and 26) | 1,543 | 1,573 |
| Impairment and disposal of fixed assets | (14) | 440 |
| **Total depreciation, amortisation, impairment and disposal of assets** | **1,529** | **2,013** |

The net gain of *'Impairment and disposal of fixed assets'* in the total amount of CZK 14 million (2015: net loss of CZK 440 million) include the impairment loss/reversal on assets held for sale.

## 12 Cost of risk

**Allowance for loan losses and provisions for other credit commitments**

*'Allowances for loan losses'* in the total amount of CZK 1,884 million (2015: CZK 1,327 million) include a net loss from allowances and provisions for loan losses in the amount of CZK 2,151 million (2015: CZK 1,741 million) and a net gain from loans written off and transferred in the amount of CZK 267 million (2015: CZK 414 million).

*The balances and movements of allowances and provisions for loans as of 31 December 2016 were as follow:*

| (CZKm) | As of 1 Jan 2016 | Charge | Release | Write off and transfer | Foreign exchange | As of 31 Dec 2016 |
|---|---|---|---|---|---|---|
| Portfolio allowances for loans to banks (refer to Note 20) | (18) | (26) | 24 | 0 | 0 | (20) |
| Specific allowances for loans to banks (refer to Note 20) | 0 | 0 | 0 | 0 | 0 | 0 |
| Portfolio allowances for loans to customers (refer to Note 21) | (1,080) | (416) | 352 | 0 | 0 | (1,144) |
| – Individuals | (390) | (70) | 33 | 0 | 0 | (427) |
| – Corporates* | (690) | (346) | 319 | 0 | 0 | (717) |
| Specific allowances for loans to customers (refer to Note 21) | (10,808) | (8,065) | 6,437 | 1,603 | (3) | (10,836) |
| – Individuals | (4,481) | (1,254) | 1,293 | 510 | 0 | (3,932) |
| – Corporates* | (6,327) | (6,811) | 5,144 | 1,093 | (3) | (6,904) |
| Specific allowances for other amounts due from customers (refer to Note 21) | (1) | 0 | 1 | 0 | 0 | 0 |
| Provisions for guarantees and other credit-related commitments (refer to Note 32) | (783) | (1,484) | 1,026 | 0 | 0 | (1,241) |
| – Individuals | (13) | (27) | 30 | 0 | 0 | (10) |
| – Corporates* | (770) | (1,457) | 996 | 0 | 0 | (1,231) |
| Specific allowances for other assets (refer to Note 23) | (236) | (8) | 8 | 14 | 0 | (222) |
| **Total** | **(12,926)** | **(9,999)** | **7,848** | **1,617** | **(3)** | **(13,463)** |

* This item also includes allowances and provisions for loans granted to individual entrepreneurs.

*The balances and movements of allowances and provisions for loans as of 31 December 2015 were as follow:*

| (CZKm) | As of 1 Jan 2015 | Charge | Release | Write off and transfer | Foreign exchange | As of 31 Dec 2015 |
|---|---|---|---|---|---|---|
| Portfolio allowances for loans to banks (refer to Note 20) | 0 | (19) | 1 | 0 | 0 | (18) |
| Specific allowances for loans to banks (refer to Note 20) | 0 | 0 | 0 | 0 | 0 | 0 |
| Portfolio allowances for loans to customers (refer to Note 21) | (834) | (656) | 409 | 0 | 1 | (1,080) |
| – Individuals | (122) | (332) | 64 | 0 | 0 | (390) |
| – Corporates* | (712) | (324) | 345 | 0 | 1 | (690) |
| Specific allowances for loans to customers (refer to Note 21) | (13,816) | (6,526) | 5,149 | 4,508 | (123) | (10,808) |
| – Individuals | (3,989) | (2,824) | 1,999 | 333 | 0 | (4,481) |
| – Corporates* | (9,827) | (3,702) | 3,150 | 4,175 | (123) | (6,327) |
| Specific allowances for other amounts due from customers (refer to Note 21) | (1) | 0 | 0 | 0 | 0 | (1) |
| Provisions for guarantees and other credit-related commitments (refer to Note 32) | (702) | (940) | 855 | 0 | 4 | (783) |
| – Individuals | (11) | (36) | 34 | 0 | 0 | (13) |
| – Corporates* | (691) | (904) | 821 | 0 | 4 | (770) |
| Specific allowances for other assets (refer to Note 23) | (227) | (18) | 4 | 5 | 0 | (236) |
| **Total** | **(15,580)** | **(8,159)** | **6,418** | **4,513** | **(118)** | **(12,926)** |

* This item also includes allowances and provisions for loans granted to individual entrepreneurs.

### Provisions for other risk expenses

The net gain of *'Provisions for other risk expenses'* of CZK 26 million (2015: net gain of CZK 230 million) consists mainly of the charge for provisions of CZK 6 million (2015: CZK 14 million) and the release and use of provisions of CZK 36 million (2015: CZK 286 million) for legal disputes, together with the net costs incurred by the Bank as a result of the outcome of legal disputes of CZK 4 million (2015: CZK 42 million).

Additional information on the provisions for other risk expenses is provided in Note 32.

## 13 Profit/(loss) on subsidiaries and associates

In March 2016, the Bank concluded an agreement on the sale of its interest in Cataps, s.r.o. with Worldline SA/NV based upon which the Bank transferred its merchant acquiring into Cataps, s.r.o. and subsequently sold its 80% stake in Cataps, s.r.o. Both steps were performed in September 2016. The selling price for the 80% stake in Cataps, s.r.o. was CZK 727 million. The remaining 20% stake in Cataps, s.r.o., valued at CZK 8 million, was reclassified as *'Assets held for sale'* due to the expected sale of this company.

## 14 Income tax

*The major components of corporate income tax expense are as follow:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Tax payable – current year, reported in profit or loss | (2,713) | (2,248) |
| Tax paid – prior year | 28 | 22 |
| Deferred tax (refer to Note 33) | 176 | (112) |
| Hedge of a deferred tax asset against foreign currency risk | 0 | (23) |
| **Total income tax** | **(2,509)** | **(2,361)** |

*The items explaining the difference between the Bank's theoretical and effective tax rates are as follow:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| **Profit before income tax** | **16,628** | **14,785** |
| Theoretical tax calculated at a tax rate of 19% (2015: 19%) | 3,159 | 2,809 |
| Tax on pre-tax profit adjustments | 70 | (24) |
| Non-taxable income | (1,802) | (1,921) |
| Expenses not deductible for tax purposes | 1,281 | 1,386 |
| Tax allowance | (2) | (2) |
| Hedge of a deferred tax asset against foreign currency risk | 0 | 23 |
| Movement in deferred tax | (176) | 112 |
| Other | 7 | 0 |
| **Income tax expense** | **2,537** | **2,383** |
| Prior period tax expense | (28) | (22) |
| **Total income tax** | **2,509** | **2,361** |
| Effective tax rate | 15.09% | 15.97% |

Non-taxable income primarily includes dividends, tax-exempt interest income and the release of tax non-deductible allowances and provisions. Expenses not deductible for tax purposes include primarily the recognition of tax non-deductible allowances and provisions and tax non-deductible operating expenses. Tax on pre-tax profit adjustments primarily represents an adjustment of the IFRS result to Czech Accounting Standards (CAS).

The corporate tax rate for the year ended 31 December 2016 is 19% (2015: 19%). The Bank's tax liability is calculated based upon the accounting profit while taking into account tax non-deductible expenses and tax exempt income or income subject to a final withholding tax rate.

Further information about deferred tax is presented in Note 33.

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## 15 Distribution of net profit

For the year ended 31 December 2016, the Bank generated a net profit of CZK 14,119 million (2015: CZK 12,424 million). The Bank's Board of Directors will propose to the Supervisory Board a dividend payment in the amount of CZK 40 per share (2015: CZK 62 per share, which equals the amount of CZK 310 per share before shares were split), which represents a total amount of CZK 7,602 million (2015: CZK 11,783 million). The proposal is subject to the Supervisory Board's approval and subsequently to the approval of the General Shareholders' Meeting.

In accordance with a resolution of the General Shareholders' Meeting held on 22 April 2016, the aggregate balance of the net profit of CZK 12,424 million for the year ended 31 December 2015 was allocated as follows: CZK 11,783 million was paid out in dividends and the remaining balance of the net profit was allocated to retained earnings. The dividends were paid out in Czech crowns.

## 16 Cash and current balances with central banks

*Cash and current balances with central banks comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Cash and cash values | 8,996 | 11,357 |
| Current balances with central banks | 94,997 | 104,900 |
| **Total cash and current balances with central banks** (refer to Note 35) | **103,993** | **116,257** |

Obligatory minimum reserves in the amount of CZK 93,292 million (2015: CZK 89,122 million) are included in ***'Current balances with central banks'*** and they bear interest. As of 31 December 2016, the interest rate was 0.05% (2015: 0.05%) in the Czech Republic and 0.00% (2015: 0.05%) in the Slovak Republic.

## 17 Financial assets at fair value through profit or loss

As of 31 December 2016 and 2015, the ***'Financial assets at fair value through profit or loss'*** portfolio includes only securities and positive fair values of derivative financial instruments held for trading. Upon initial recognition, the Bank has not designated any financial assets as ***'Financial assets at fair value through profit or loss'***.

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Securities | 11,445 | 10,672 |
| Derivative financial instruments | 19,037 | 19,217 |
| **Total financial assets at fair value through profit or loss** | **30,482** | **29,889** |

For detailed information on derivative financial instruments included in the held for trading portfolio, refer to Note 41(C).

*Trading securities comprise the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Fair value | Cost* | Fair value | Cost* |
| **Emission allowances** | **1,839** | **1,766** | **2,800** | **2,379** |
| Fixed income debt securities | 6,594 | 6,477 | 4,509 | 4,390 |
| Variable yield debt securities | 2,140 | 2,127 | 1,026 | 1,022 |
| Bills of exchange | 872 | 871 | 186 | 185 |
| Treasury bills | 0 | 0 | 2,151 | 2,150 |
| **Total debt securities** | **9,606** | **9,475** | **7,872** | **7,747** |
| **Total trading securities** | **11,445** | **11,241** | **10,672** | **10,126** |

* Acquisition cost for shares, participation certificates and emission allowances; amortised acquisition cost excluding coupon for debt securities.

The Bank's portfolio of trading securities includes treasury bills issued by the Czech Ministry of Finance at fair value of CZK 0 million (2015: CZK 2,151 million).

As of 31 December 2016, the portfolio of trading securities includes securities at fair value of CZK 10,516 million (2015: CZK 8,213 million) that are publicly traded on stock exchanges and securities at fair value of CZK 929 million (2015: CZK 2,459 million) that are not publicly traded on stock exchanges (they are traded on the interbank market).

*Emission allowances at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Emission allowances** | | |
| – Other currencies | 1,839 | 2,800 |
| **Total emission allowances** | **1,839** | **2,800** |

*Emission allowances at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Emission allowances issued by:** | | |
| – Foreign financial institutions | 1,839 | 2,800 |
| **Total emission allowances** | **1,839** | **2,800** |

*Debt trading securities at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Fixed income debt securities (including bills of exchange and treasury bills)** | | |
| – Czech crowns | 6,636 | 4,909 |
| – Other currencies | 830 | 1,937 |
| **Total fixed income debt securities** | **7,466** | **6,846** |
| **Variable yield debt securities** | | |
| – Czech crowns | 2,140 | 640 |
| – Other currencies | 0 | 386 |
| **Total variable yield debt securities** | **2,140** | **1,026** |
| **Total trading debt securities** | **9,606** | **7,872** |

*Debt trading securities at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Debt trading securities issued by:** | | |
| – State institutions in the Czech Republic | 8,857 | 5,628 |
| – Foreign state institutions | 658 | 2,044 |
| – Financial institutions in the Czech Republic | 59 | 146 |
| – Foreign financial institutions | 15 | 0 |
| – Other entities in the Czech Republic | 17 | 54 |
| – Other foreign entities | 0 | 0 |
| **Total trading debt securities** | **9,606** | **7,872** |

*Bonds issued by Foreign state institutions designated as financial assets at fair value through profit or loss:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Country of issuer** | **Fair value** | **Fair value** |
| European Investment Bank | 62 | 52 |
| Poland | 0 | 1 |
| Slovakia | 596 | 1,991 |
| **Total** | **658** | **2,044** |

Of the debt securities issued by State institutions in the Czech Republic, CZK 7,807 million (2015: CZK 3,106 million) consist of securities eligible for refinancing with the CNB.

## 18 Available-for-sale financial assets

*Available-for-sale financial assets comprise the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **(CZKm)** | **Fair value** | **Cost*** | **Fair value** | **Cost*** |
| **Shares and participation certificates** | **182** | **177** | **675** | **1** |
| Fixed income debt securities | 17,568 | 15,437 | 17,931 | 15,763 |
| Variable yield debt securities | 13,661 | 13,224 | 14,094 | 13,563 |
| **Total debt securities** | **31,229** | **28,661** | **32,025** | **29,326** |
| **Total available-for-sale financial assets** | **31,411** | **28,838** | **32,700** | **29,327** |

* Acquisition cost for shares and participation certificates; amortised acquisition cost excluding coupon for debt securities.

As of 31 December 2016, the *'Available-for-sale financial assets'* portfolio includes securities at fair value of CZK 31,229 million (2015: CZK 32,025 million) that are publicly traded on stock exchanges and securities at fair value of CZK 182 million (2015: CZK 675 million) that are not publicly traded.

As of 31 December 2016, the *'Available-for-sale financial assets'* portfolio includes bonds at fair value of CZK 1,348 million (2015: CZK 0 million) that are used as collateral for intraday facilities in central banks.

In 2016, the Bank sold a stake in Visa Europe Limited, the net gain from the sale for the Bank amounted to CZK 959 million (refer to Note 7).

*Shares and participation certificates available-for-sale at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Shares and participation certificates** | | |
| – Other currencies | 182 | 675 |
| **Total shares and participation certificates available-for-sale** | **182** | **675** |

*Shares and participation certificates available-for-sale at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Shares and participation certificates available-for-sale issued by:** | | |
| – Other foreign entities | 182 | 675 |
| **Total shares and participation certificates available-for-sale** | **182** | **675** |

*Debt securities available-for-sale at fair value comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Fixed income debt securities** | | |
| – Czech crowns | 12,663 | 13,078 |
| – Other currencies | 4,905 | 4,853 |
| **Total fixed income debt securities** | **17,568** | **17,931** |
| **Variable yield debt securities** | | |
| – Czech crowns | 10,951 | 11,375 |
| – Other currencies | 2,710 | 2,719 |
| **Total variable yield debt securities** | **13,661** | **14,094** |
| **Total debt securities available-for-sale** | **31,229** | **32,025** |

*Debt securities available-for-sale at fair value, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Debt securities available-for-sale issued by:** | | |
| – State institutions in the Czech Republic | 15,243 | 14,278 |
| – Foreign state institutions | 4,905 | 4,853 |
| – Financial institutions in the Czech Republic | 10,259 | 12,062 |
| – Foreign financial institutions | 822 | 832 |
| **Total debt securities available-for-sale** | **31,229** | **32,025** |

*Debt securities available-for-sale issued by Foreign state institutions comprise the following:*

| (CZKm) | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **Country of issuer** | **Fair value** | **Cost*** | **Fair value** | **Cost*** |
| Poland | 788 | 676 | 786 | 676 |
| Slovakia | 4,117 | 3,326 | 4,067 | 3,338 |
| **Total** | **4,905** | **4,002** | **4,853** | **4,014** |

* Acquisition cost for shares and participation certificates; amortised acquisition cost excluding coupon for debt securities.

Of the debt securities issued by State institutions in the Czech Republic, CZK 15,243 million (2015: CZK 14,277 million) consist of securities eligible for refinancing with the CNB.

**Reclassification of certain debt securities held in the portfolio of Available-for-sale financial assets**

During the first quarter of 2014, the Bank reviewed the accounting recognition of certain debt securities issued by State institutions held in the portfolio of ***'Available-for-sale financial assets'*** (hereafter only "AFS") on the basis of the Bank's changing its intention for their classification. The Bank concluded that all regulatory and accounting requirements, as well as internal limits, were satisfied for recognition of the debt securities in the nominal value of CZK 50,260 million in the portfolio of ***'Held-to-maturity investments'*** (hereafter only "HTM") and decided to reclassify the respective securities from AFS to HTM. The securities were reclassified at fair value. The corresponding unrealised gains and losses in equity of CZK 4,474 million as of the reclassification date are retained in Other Comprehensive Income. Such amounts are amortised over the remaining life of the security (refer to Note 40).

## 19 Assets held for sale

As of 31 December 2016, the Bank reported assets held for sale at a carrying amount of CZK 344 million (2015: CZK 360 million) comprising buildings and land owned by the Bank which the management of the Bank decided to sell as a component of a plan to optimise the distribution network. Depreciation of these assets has been discontinued since their classification as assets held for sale. As of 31 December 2016, the Bank recognised allowances against assets held for sale of CZK 402 million (2015: CZK 418 million).

As of 31 December 2016, ***'Assets held for sale'*** also includes investments in subsidiaries and associates classified as assets held for sale at a carrying amount of CZK 243 million (2015: CZK 0 million), refer to Note 24.

## 20 Amounts due from banks

*Balances due from banks comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Current accounts with other banks (refer to Note 35) | 788 | 445 |
| Debt securities | 5,060 | 5,157 |
| Loans and advances to banks | 12,348 | 11,472 |
| Advances due from central banks (reverse repo transactions) | 6,000 | 9,900 |
| Term placements with other banks | 33,807 | 27,633 |
| **Total amounts due from banks, gross** | **58,003** | **54,607** |
| Portfolio allowances for loans to banks (refer to Note 12) | (20) | (18) |
| Specific allowances for loans to banks (refer to Note 12) | 0 | 0 |
| **Total allowances for loans to banks** | **(20)** | **(18)** |
| **Total amounts due from banks, net** | **57,983** | **54,589** |

*Advances due from the CNB and other banks under reverse repurchase transactions are collateralised by treasury bills issued by the CNB and other debt securities, the fair values of which are as follow:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Treasury bills | 5,904 | 9,726 |
| Debt securities issued by state institutions | 167 | 426 |
| Shares | 0 | 607 |
| Investment certificates | 0 | 83 |
| **Total** | **6,071** | **10,842** |

### Securities acquired as loans and receivables

As of 31 December 2016, the Bank maintains in its portfolio bonds at an amortised cost of CZK 5,060 million (2015: CZK 5,157 million) and a nominal value of CZK 4,939 million (2015: CZK 4,939 million), of which bonds with a nominal value of CZK 2,099 million (2015: CZK 2,099 million) and EUR 79 million (2015: EUR 79 million) are issued by Financial institutions in the Czech Republic and CZK 705 million (2015: CZK 705 million) by Foreign financial institutions.

## 21 Loans and advances to customers

*Loans and advances to customers comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Loans to customers | 534,800 | 492,132 |
| Bills of exchange | 243 | 302 |
| Forfaits | 816 | 271 |
| **Total loans and advances to customers excluding debt securities and other amounts due to customers, gross** | **535,859** | **492,705** |
| Debt securities | 3,193 | 3,654 |
| Other amounts due from customers | 71 | 4 |
| **Total loans and advances to customers, gross** | **539,123** | **496,363** |
| Portfolio allowances for loans to customers (refer to Note 12) | | |
| – Individuals | (427) | (390) |
| – Corporates* | (717) | (690) |
| Specific allowances for loans to customers (refer to Note 12) | | |
| – Individuals | (3,932) | (4,481) |
| – Corporates* | (6,904) | (6,327) |
| **Total allowances for loans to customers** | **(11,980)** | **(11,888)** |
| Specific allowances for other amounts due from customers (refer to Note 12) | 0 | (1) |
| **Total allowances for loans and other amounts due from customers** | **(11,980)** | **(11,889)** |
| **Total loans and advances to customers, net** | **527,143** | **484,474** |

* This item also includes allowances for loans granted to individual entrepreneurs.

As of 31 December 2016, loans and advances to customers include accrued interest of CZK 845 million (2015: CZK 895 million), of which CZK 293 million (2015: CZK 340 million) relates to interest from overdue receivables.

As of 31 December 2016, loans provided to customers under reverse repurchase transactions in the amount of CZK 6 million (2015: CZK 819 million) are collateralised by securities with a fair value of CZK 4 million (2015: CZK 1,177 million).

*As of 31 December 2016, the loan portfolio of the Bank (excluding Debt securities and Other amounts due from customers) is comprised of the following, as broken down by classification:*

| (CZKm) | Gross receivable | Collateral applied | Net exposure | Allowances | Carrying value |
|---|---|---|---|---|---|
| Standard | 512,268 | 238,498 | 273,770 | (674)* | 511,594 |
| Watch | 6,472 | 2,685 | 3,787 | (470)* | 6,002 |
| Substandard | 4,571 | 2,586 | 1,985 | (1,937) | 2,634 |
| Doubtful | 1,924 | 929 | 995 | (663) | 1,261 |
| Loss | 10,624 | 1,158 | 9,466 | (8,236) | 2,388 |
| **Total** | **535,859** | **245,856** | **290,003** | **(11,980)** | **523,879** |

* This item includes portfolio allowances (due to losses incurred but not reported).

*As of 31 December 2015, the loan portfolio of the Bank (excluding Debt securities and Other amounts due from customers) was comprised of the following, as broken down by classification:*

| (CZKm) | Gross receivable | Collateral applied | Net exposure | Allowances | Carrying value |
|---|---|---|---|---|---|
| Standard | 467,837 | 217,774 | 250,063 | (592)* | 467,245 |
| Watch | 7,258 | 3,067 | 4,191 | (488)* | 6,770 |
| Substandard | 5,853 | 3,075 | 2,778 | (2,290) | 3,563 |
| Doubtful | 1,838 | 1,221 | 617 | (533) | 1,305 |
| Loss | 9,919 | 672 | 9,247 | (7,985) | 1,934 |
| **Total** | **492,705** | **225,809** | **266,896** | **(11,888)** | **480,817** |

* This item includes portfolio allowances (due to losses incurred but not reported).

*Set out below is a breakdown of loans by sector (excluding Debt securities and Other amounts due from customers):*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Food industry and agriculture | 14,381 | 14,447 |
| Mining and extraction | 4,298 | 5,697 |
| Chemical and pharmaceutical industry | 5,658 | 5,199 |
| Metallurgy | 8,204 | 8,635 |
| Automotive industry | 10,839 | 9,681 |
| Manufacturing of other machinery | 8,434 | 7,958 |
| Manufacturing of electrical and electronic equipment | 3,737 | 3,131 |
| Other processing industry | 9,240 | 6,171 |
| Power plants, gas plants and waterworks | 19,294 | 16,815 |
| Construction industry | 8,619 | 8,972 |
| Retail | 15,006 | 13,504 |
| Wholesale | 25,117 | 25,102 |
| Accommodation and catering | 1,431 | 1,347 |
| Transportation, telecommunication and warehouses | 10,861 | 12,544 |
| Banking and insurance industry | 57,939 | 47,492 |
| Real estate | 50,974 | 42,940 |
| Public administration | 24,627 | 28,926 |
| Other industries | 26,196 | 27,538 |
| Individuals | 231,004 | 206,606 |
| **Total loans to customers** | **535,859** | **492,705** |

The majority of loans - more than 90% (2015: more than 90%) - were provided to entities on the territory of the Czech Republic.

*Set out below is an analysis of the types of collateral held in support of loans and advances to customers as stated in the Statement of Financial Position:*

| (CZKm) | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| | Total client loan collateral* | Discounted client loan collateral value** | Applied client loan collateral value*** | Total client loan collateral* | Discounted client loan collateral value** | Applied client loan collateral value*** |
| Guarantees of state and governmental institutions | 3,097 | 2,328 | 2,325 | 2,613 | 2,262 | 2,254 |
| Bank guarantee | 14,599 | 13,992 | 13,836 | 14,367 | 13,712 | 13,340 |
| Guaranteed deposits | 2,763 | 2,681 | 2,018 | 3,383 | 3,275 | 2,172 |
| Pledge of real estate | 396,823 | 267,540 | 197,487 | 355,575 | 237,601 | 175,515 |
| Pledge of movable assets | 13,053 | 2,082 | 1,279 | 12,971 | 1,263 | 1,214 |
| Guarantee by legal entity | 30,114 | 19,895 | 13,808 | 32,665 | 20,907 | 14,256 |
| Guarantee by individual (natural person) | 1,177 | 111 | 104 | 1,200 | 138 | 122 |
| Pledge of receivables | 32,829 | 4,636 | 3,073 | 46,440 | 3,784 | 3,157 |
| Insurance of credit risk | 11,628 | 11,054 | 11,045 | 13,955 | 13,258 | 13,128 |
| Other | 2,379 | 1,744 | 881 | 1,589 | 892 | 651 |
| **Nominal value of collateral** | **508,462** | **326,063** | **245,856** | **484,758** | **297,092** | **225,809** |

* The nominal value of the collateral is determined based on internal rules of the Bank (e.g. internal property valuation, the current value of collateral, the market value of securities, etc.).
** The nominal value of the collateral is reduced by a coefficient taking into account the time value of money, the cost of selling the collateral, the risk of declining market prices, the risk of insolvency, etc.
*** The applied collateral value is the discounted collateral value reduced to the actual balance of the collateralised exposure.

Pledges on industrial real estate represent 11% of total pledges on real estate (2015: 11%).

### Debt securities designated as loans and receivables

As of 31 December 2016, the Bank holds in its portfolio bonds at an amortised cost of CZK 2,759 million (2015: CZK 2,749 million) and a nominal value of CZK 2,697 million (2015: CZK 2,687 million), of which bonds with a nominal value of CZK 450 million (2015: CZK 450 million) are issued by State institutions in the Czech Republic, CZK 1,744 million (2015: CZK 1,790 million) by Other entities in the Czech Republic and EUR 16 million (2015: EUR 17 million) and CZK 68 million (2015: CZK 0 million) by Other foreign entities. Additionally, the Bank holds in this portfolio bills of exchange at an amortised cost of CZK 388 million (2015: CZK 878 million) and a nominal value of CZK 389 million (2015: CZK 880 million), of which bills of exchange in the nominal value of CZK 210 million (2015: CZK 80 million) are issued by State institutions in the Czech Republic and CZK 179 million (2015: CZK 800 million) by Other entities in the Czech Republic. The portfolio is hedged using fair value hedge derivatives with a positive fair value of CZK 46 million (2015: CZK 27 million).

### Forborne loans and advances to customers

*Forborne loans and advances to customers as of 31 December 2016:*

| (CZKm) | Neither past due nor impaired | Past due, not impaired | Impaired | Total forborne | Allowances | Collateral applied |
|---|---|---|---|---|---|---|
| Individuals | 776 | 110 | 1,051 | 1,937 | 479 | 1,344 |
| Corporates* | 373 | 0 | 2,483 | 2,856 | 1,374 | 1,148 |
| **Total** | **1,149** | **110** | **3,534** | **4,793** | **1,853** | **2,492** |

* This item also includes loans granted to individual entrepreneurs.

*Forborne loans and advances to customers as of 31 December 2015:*

| (CZKm) | Neither past due nor impaired | Past due, not impaired | Impaired | Total forborne | Allowances | Collateral applied |
|---|---|---|---|---|---|---|
| Individuals | 616 | 52 | 1,028 | 1,696 | 438 | 1,149 |
| Corporates* | 197 | 0 | 2,115 | 2,312 | 1,345 | 666 |
| **Total** | **813** | **52** | **3,143** | **4,008** | **1,783** | **1,815** |

* This item also includes loans granted to individual entrepreneurs.

*The carrying value of forborne assets in comparison with the Bank's loan portfolio (excluding Debt securities and Other amounts due from customers):*

| | | | 31 Dec 2016 | | | 31 Dec 2015 |
|---|---|---|---|---|---|---|
| (CZKm) | Gross receivable | Forborne assets | Share in gross receivable | Gross receivable | Forborne assets | Share in gross receivable |
| Individuals | 231,004 | 1,937 | 0.84% | 206,606 | 1,696 | 0.82% |
| Corporates* | 304,855 | 2,856 | 0.94% | 286,099 | 2,312 | 0.81% |
| **Total** | **535,859** | **4,793** | **0.89%** | **492,705** | **4,008** | **0.81%** |

* This item also includes loans granted to individual entrepreneurs.

*Portfolio and specific allowances for forborne assets:*

| | | | 31 Dec 2016 | | | 31 Dec 2015 |
|---|---|---|---|---|---|---|
| (CZKm) | Portfolio allowances | Specific allowances | Total | Portfolio allowances | Specific allowances | Total |
| Individuals | 10 | 469 | 479 | 8 | 430 | 438 |
| Corporates* | 36 | 1,338 | 1,374 | 8 | 1,337 | 1,345 |
| **Total** | **46** | **1,807** | **1,853** | **16** | **1,767** | **1,783** |

* This item also includes allowances for loans granted to individual entrepreneurs.

## 22 Held-to-maturity investments

*Held-to-maturity investments comprise the following:*

| | | 31 Dec 2016 | | 31 Dec 2015 |
|---|---|---|---|---|
| (CZKm) | Carrying value | Cost* | Carrying value | Cost* |
| Fixed income debt securities | 62,425 | 61,189 | 61,003 | 59,751 |
| **Total held-to-maturity investments** | **62,425** | **61,189** | **61,003** | **59,751** |

* Amortised acquisition cost excluding coupon.

As of 31 December 2016, the ***'Held-to-maturity investments'*** portfolio includes bonds of CZK 62,425 million (2015: CZK 60,789 million) that are publicly traded on stock exchanges and bonds of CZK 0 million (2015: CZK 214 million) that are not publicly traded.

As of 31 December 2016, the ***'Held-to-maturity investments'*** portfolio includes bonds of CZK 107 million (2015: CZK 0 million) that are used as collateral for derivative deals with a central counterparty. The central counterparty is LCH.Clearnet SA. Bank uses Société Générale Newedge UK Limited as related broker.

*Fixed income debt securities held-to-maturity comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Fixed income debt securities** | | |
| – Czech crowns | 48,356 | 47,185 |
| – Foreign currencies | 14,069 | 13,818 |
| **Total fixed income debt securities** | **62,425** | **61,003** |

*Fixed income debt securities held-to-maturity, allocated by issuer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| **Fixed income debt securities issued by:** | | |
| – State institutions in the Czech Republic | 51,258 | 50,144 |
| – Foreign state institutions | 11,167 | 10,859 |
| **Total fixed income debt securities** | **62,425** | **61,003** |

*Debt securities held-to-maturity issued by Foreign state institutions comprise the following:*

| (CZKm) | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **Country of Issuer** | **Fair value** | **Cost*** | **Fair value** | **Cost*** |
| Poland | 7,938 | 7,818 | 6,023 | 5,778 |
| Slovakia | 2,822 | 3,096 | 5,146 | 4,812 |
| **Total** | **10,760** | **10,914** | **11,169** | **10,590** |

* Amortised acquisition cost excluding coupon.

## 23 Prepayments, accrued income and other assets

*Prepayments, accrued income and other assets comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Prepayments and accrued income | 509 | 464 |
| Settlement balances | 223 | 342 |
| Receivables from securities trading | 78 | 337 |
| Other assets | 2,202 | 1,661 |
| **Total prepayments, accrued income and other assets** | **3,012** | **2,804** |

*'Other assets'* include allowances for operating receivables for other debtors in the amount of CZK 222 million (2015: CZK 236 million), and in particular also advances provided and receivables for other debtors.

## 24 Investments in subsidiaries and associates

*Investments in subsidiaries and associates comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Investments in subsidiary undertakings | 20,455 | 21,340 |
| Investments in associated undertakings | 837 | 837 |
| **Total investments in subsidiaries and associates** | **21,292** | **22,177** |

### Subsidiary undertakings

*The following companies are subsidiary undertakings of the Bank as of 31 December 2016:*

| Company name | Direct holding % | Group holding % | Principal activity | Registered office | Cost of investment (CZKm) | Allowances (CZKm) | Carrying value (CZKm) |
|---|---|---|---|---|---|---|---|
| Bastion European Investments S.A. | 99.98 | 99.98 | Financial services | Brussels | 3,123 | 0 | 3,123 |
| ESSOX s.r.o. | 50.93 | 50.93 | Consumer loans, leasing | České Budějovice | 1,165 | 0 | 1,165 |
| Factoring KB, a.s. | 100 | 100 | Factoring | Prague | 1,190 | 0 | 1,190 |
| KB Penzijní společnost, a.s. | 100 | 100 | Financial services | Prague | 550 | 0 | 550 |
| KB Real Estate, s.r.o. | 100 | 100 | Support services | Prague | 511 | 0 | 511 |
| Modrá pyramida stavební spořitelna, a.s. | 100 | 100 | Construction savings scheme | Prague | 4,873 | 0 | 4,873 |
| Protos, uzavřený investiční fond, a.s. | 83.65 | 100 | Financial services | Prague | 6,329 | 0 | 6,329 |
| SG Equipment Finance Czech Republic s.r.o. | 50.1 | 50.1 | Industry financing | Prague | 1,850 | 0 | 1,850 |
| VN 42, s.r.o. | 100 | 100 | Support services | Prague | 864 | 0 | 864 |
| **Total** | | | | | **20,455** | **0** | **20,455** |

## Associated undertakings

*The following companies are associated undertakings of the Bank as of 31 December 2016:*

| Company name | Direct holding % | Group holding % | Principal activity | Registered office | Cost of investment (CZKm) | Allowances (CZKm) | Carrying value (CZKm) |
|---|---|---|---|---|---|---|---|
| CBCB – Czech Banking Credit Bureau, a.s. | 20 | 20 | Collection of data for the evaluation of credit risk | Prague | 0* | 0 | 0 |
| Komerční pojišťovna, a.s. | 49 | 49 | Insurance activities | Prague | 837 | 0 | 837 |
| **Total** | | | | | **837** | **0** | **837** |

* The cost of investment for CBCB – Czech Banking Credit Bureau, a.s. is CZK 240 thousand.

## Investments in subsidiaries and associates classified as assets held for sale

*The following investments in subsidiaries and associates of the Bank classified as assets held for sale as of 31 December 2016:*

| Company name | Direct holding % | Group holding % | Principal activity | Registered office | Cost of investment (CZKm) | Allowances (CZKm) | Carrying value (CZKm) |
|---|---|---|---|---|---|---|---|
| Cataps, s.r.o. | 20 | 20 | Financial services | Prague | 8 | 0 | 8 |
| NP 33, s.r.o. | 100 | 100 | Support services | Prague | 235 | 0 | 235 |
| **Total** | | | | | **243** | **0** | **243** |

*Set out below is an overview of year-on-year movements in investments, by issuer:*

| (CZKm) | Investment at cost as of 1 Jan 2016 | Additions | Decreases | Reclassification | Investment at cost as of 31 Dec 2016 |
|---|---|---|---|---|---|
| Bastion European Investments S.A.[2)] | 3,223 | 0 | (100) | 0 | 3,123 |
| Cataps, s.r.o.[1)] | 4 | 65 | (61) | (8) | 0 |
| ESSOX s.r.o. | 1,165 | 0 | 0 | 0 | 1,165 |
| Factoring KB, a.s. | 1,190 | 0 | 0 | 0 | 1,190 |
| KB Penzijní společnost, a.s. | 550 | 0 | 0 | 0 | 550 |
| KB Real Estate, s.r.o. | 511 | 0 | 0 | 0 | 511 |
| Modrá pyramida stavební spořitelna, a.s. | 4,873 | 0 | 0 | 0 | 4,873 |
| NP 33, s.r.o.[3)] | 405 | 0 | 0 | (405) | 0 |
| Protos, uzavřený investiční fond, a.s.[5)] | 6,705 | 0 | (376) | 0 | 6,329 |
| SG Equipment Finance Czech Republic s.r.o. | 1,850 | 0 | 0 | 0 | 1,850 |
| VN 42, s.r.o. | 864 | 0 | 0 | 0 | 864 |
| **Total subsidiaries** | **21,340** | **65** | **(537)** | **(413)** | **20,455** |
| CBCB – Czech Banking Credit Bureau, a.s. | 0* | 0 | 0 | 0 | 0* |
| Komerční pojišťovna, a.s. | 837 | 0 | 0 | 0 | 837 |
| **Total associates** | **837** | **0** | **0** | **0** | **837** |
| Cataps, s.r.o.[1)] | 0 | 0 | 0 | 8 | 8 |
| NP 33, s.r.o.[3)] a [4)] | 0 | 0 | (170) | 405 | 235 |
| **Total as assets held for sale** | **0** | **0** | **(170)** | **413** | **243** |

* The cost of investment for CBCB – Czech Banking Credit Bureau, a.s. is CZK 240 thousand.

**Changes in equity investments in subsidiaries and associates in 2016**

1) In March 2016, the Bank concluded an agreement on the sale of its interest in Cataps, s.r.o. with Worldline SA/NV based upon which the Bank transferred its merchant acquiring into Cataps, s.r.o. and subsequently sold its 80% stake in Cataps, s.r.o. Both steps were performed in September 2016. The selling price for the 80% stake in Cataps, s.r.o. was CZK 727 million. The remaining 20% stake in Cataps, s.r.o., valued at CZK 8 million, was reclassified as *'Assets held for sale'* due to the expected sale of this company.
2) In May 2016, the equity in Bastion European Investments S.A. was decreased by EUR 3.5 million (equivalent to CZK 100 million). The decrease was initiated solely by the Bank as the majority shareholder of Bastion European Investments S.A.
3) In June 2016, the Bank's investment into subsidiary NP 33, s.r.o., valued at CZK 405 million, was reclassified as *'Assets held for sale'* due to expected sale of this company.
4) In November 2016, the Bank decided to decrease share capital and to dissolve the reserve and statutory funds of NP 33, s.r.o., that amount totalling to CZK 170 million. The process of decreasing the share capital was finalised in December 2016.
5) In December 2016, the Bank decreased the capital of its subsidiary Protos, uzavřený investiční fond, a.s. through decreasing the reserve fund by CZK 450 million. The share of the Bank in this decrease was CZK 376 million which reflects the Bank's 83.65% ownership share. The remaining ownership share is held by Factoring KB, a.s. which is fully owned by the Bank.

## 25 Intangible assets

*The movements in intangible assets were as follow:*

| (CZKm) | Internally generated assets* | Software | Other intangible assets | Acquisition of assets | Total |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| As of 1 January 2015 | 10,159 | 1,666 | 42 | 690 | 12,557 |
| Additions | 673 | 200 | 0 | 1,164 | 2,037 |
| Disposals/transfers | (20) | (105) | (25) | (872) | (1,022) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| As of 31 December 2015 | 10,812 | 1,761 | 17 | 982 | 13,572 |
| Additions | 902 | 75 | 0 | 1,005 | 1,982 |
| Disposals/transfers | 0 | (4) | (3) | (975) | (982) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **11,714** | **1,832** | **14** | **1,012** | **14,572** |
| **Accumulated amortisation and allowances** | | | | | |
| As of 1 January 2015 | (7,745) | (1,434) | (41) | 0 | (9,220) |
| Additions | (947) | (108) | 0 | 0 | (1,055) |
| Disposals | 19 | 87 | 24 | 0 | 130 |
| Impairment charge | 0 | 0 | 0 | 0 | 0 |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| As of 31 December 2015 | (8,673) | (1,455) | (17) | 0 | (10,145) |
| Additions | (901) | (100) | 0 | 0 | (1,001) |
| Disposals | 0 | 4 | 3 | 0 | 7 |
| Impairment charge | 0 | (3) | 0 | (2) | (5) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **(9,574)** | **(1,554)** | **(14)** | **(2)** | **(11,144)** |
| **Net book value** | | | | | |
| As of 31 December 2015 | 2,139 | 306 | 0 | 982 | 3,427 |
| **As of 31 December 2016** | **2,140** | **278** | **0** | **1,010** | **3,428** |

* Internally generated assets comprise mainly software.

During the year ended 31 December 2016, the Bank expended CZK 185 million (2015: CZK 144 million) on research and development (when conditions for capitalisation were not met) through a charge to *'Operating expenses'*. As of 31 December 2016, the Bank recognised allowances against intangible assets of CZK 5 million (2015: CZK 0 million). These allowances primarily included allowances charged in respect of software.

## 26 Tangible assets

*The movements in tangible assets were as follow:*

| (CZKm) | Land | Buildings | Machinery, furniture and fixtures and other | Acquisition of assets | Total |
|---|---|---|---|---|---|
| **Cost** | | | | | |
| As of 1 January 2015 | 141 | 8,465 | 4,641 | 266 | 13,513 |
| Reallocation from/to assets held for sale | (30) | (1,587) | 0 | 0 | (1,617) |
| Additions | 0 | 211 | 258 | 631 | 1,100 |
| Disposals/transfers | 0 | (108) | (565) | (469) | (1,142) |
| Foreign exchange rate difference | 0 | 0 | 1 | 0 | 1 |
| As of 31 December 2015 | 111 | 6,981 | 4,335 | 428 | 11,855 |
| Reallocation from/to assets held for sale | 0 | 54 | 0 | 0 | 54 |
| Additions | 0 | 105 | 303 | 834 | 1,242 |
| Disposals/transfers | 0 | (10) | (212) | (525) | (747) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **111** | **7,130** | **4,426** | **737** | **12,404** |
| **Accumulated depreciation and allowances** | | | | | |
| As of 1 January 2015 | 0 | (4,554) | (3,812) | 0 | (8,366) |
| Reallocation of accumulated depreciation of assets held for sale | 0 | 839 | 0 | 0 | 839 |
| Additions | 0 | (257) | (261) | 0 | (518) |
| Disposals | 0 | 88 | 550 | 0 | 638 |
| Impairment charge | 0 | 0 | (5) | 0 | (5) |
| Foreign exchange rate difference | 0 | 0 | 1 | 0 | 1 |
| As of 31 December 2015 | 0 | (3,884) | (3,527) | 0 | (7,411) |
| Reallocation of accumulated depreciation of assets held for sale | 0 | 32 | 0 | 0 | 32 |
| Additions | 0 | (289) | (253) | 0 | (542) |
| Disposals | 0 | 1 | 218 | 0 | 219 |
| Impairment charge | 0 | 9 | (47) | 0 | (38) |
| Foreign exchange rate difference | 0 | 0 | 0 | 0 | 0 |
| **As of 31 December 2016** | **0** | **(4,131)** | **(3,609)** | **0** | **(7,740)** |
| **Net book value** | | | | | |
| As of 31 December 2015 | 111 | 3,097 | 808 | 428 | 4,444 |
| **As of 31 December 2016** | **111** | **2,999** | **817** | **737** | **4,664** |

As of 31 December 2016, the Bank recognised allowances against tangible assets of CZK 45 million (2015: CZK 7 million). These allowances primarily included allowances charged in respect of computer equipment.

## 27 Financial liabilities at fair value through profit or loss

As of 31 December 2016 and 2015, the *'Financial liabilities at fair value through profit or loss'* portfolio includes only liabilities arising from short sales of securities and negative fair values of financial derivative instruments held for trading. Upon initial recognition, the Bank has not designated any financial liabilities as *'Financial liabilities at fair value through profit or loss'*.

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Sold securities | 160 | 305 |
| Derivative financial instruments | 18,780 | 19,880 |
| **Total financial liabilities at fair value through profit or loss** | **18,940** | **20,185** |

For detailed information on financial derivative instruments included in the portfolio for trading, refer to Note 41(C).

## 28 Amounts due to banks

*Amounts due to banks comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Current accounts (refer to Note 35) | 3,168 | 2,741 |
| Amounts due to banks | 40,114 | 43,338 |
| **Total amounts due to banks** | **43,282** | **46,079** |

*The fair values of securities and treasury bills used as collateral for repurchase loans are as follow:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Carrying value | Fair value | Carrying value | Fair value |
| Financial assets at fair value through profit or loss | 403 | 403 | 0 | 0 |
| Available-for-sale financial assets | 758 | 758 | 0 | 0 |
| Held-to-maturity investments | 4,889 | 4,862 | 0 | 0 |
| Securities received as collateral | 0 | 0 | 117 | 117 |
| **Total** | **6,049** | **6,023** | **117** | **117** |

## 29 Amounts due to customers

*Amounts due to customers, by type of deposit, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Current accounts | 497,588 | 450,664 |
| Savings accounts | 97,381 | 95,989 |
| Term deposits | 32,766 | 31,040 |
| Amounts received from customers | 5,198 | 9,699 |
| Other payables to customers | 5,477 | 5,667 |
| **Total amounts due to customers** | **638,410** | **593,059** |

The fair value of securities and treasury bills used as collateral for repurchase loans received from customers was CZK 5,217 million (2015: CZK 9,709 million), comprising securities received as collateral.

*Amounts due to customers, by type of customer, comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Private companies | 220,252 | 225,461 |
| Other financial institutions, non-banking entities | 24,669 | 34,199 |
| Insurance companies | 6,085 | 3,167 |
| Public administration | 577 | 2,141 |
| Individuals | 224,428 | 190,680 |
| Individuals – entrepreneurs | 30,496 | 29,433 |
| Government agencies | 77,309 | 70,581 |
| Other | 16,048 | 14,643 |
| Non-residents | 38,546 | 22,754 |
| **Total amounts due to customers** | **638,410** | **593,059** |

## 30 Securities issued

*Securities issued comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Mortgage bonds | 43,362 | 43,717 |
| Depository bills of exchange | 2,393 | 10,581 |
| **Total securities issued** | **45,755** | **54,298** |

The Bank issues mortgage bonds to fund its mortgage activities.

*Mortgage bonds according to their remaining time to maturity break out as follows:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| In less than one year | 129 | 0 |
| In one to five years | 4,829 | 5,121 |
| In five to ten years | 7,775 | 6,095 |
| In ten to twenty years | 2,541 | 4,176 |
| More than twenty years | 28,088 | 28,325 |
| **Total mortgage bonds** | **43,362** | **43,717** |

*The securities issued detailed above include the following mortgage bonds issued by the Bank:*

| Name | Interest rate | Currency | Issue date | Maturity date | 31 Dec 2016 CZKm | 31 Dec 2015 CZKm |
|---|---|---|---|---|---|---|
| HZL Komerční banky, a.s., CZ0002001142 | 5.0% | CZK | 16 Aug 2007 | 16 Aug 2019 | 3,084 | 3,101 |
| HZL Komerční banky, a.s., CZ0002001324, CZ0002001332 | 5.06% for the first twelve annual interest periods, afterwards the relevant reference rate* less 0.20% | CZK | 16 Nov 2007 | 16 Nov 2037 | 2,440 | 2,447 |
| HZL Komerční banky, a.s., CZ0002001340, CZ0002001357 | 5.02% for the first eleven annual interest periods, afterwards the relevant reference rate* less 0.20% | CZK | 16 Nov 2007 | 16 Nov 2037 | 1,756 | 1,778 |
| HZL Komerční banky, a.s., CZ0002001365, CZ0002001373 | 4.23% for the first 3M interest period, afterwards the relevant reference rate* less 0.20% | CZK | 16 Nov 2007 | 16 Nov 2037 | 1,882 | 1,862 |
| HZL Komerční banky, a.s., CZ0002001431, CZ0002001449, CZ0002001456 | 4.14% for the first 3M interest period, afterwards the relevant reference rate* less 0.20% | CZK | 30 Nov 2007 | 30 Nov 2037 | 3,382 | 3,347 |
| HZL Komerční banky, a.s., CZ0002001506, CZ0002001514, CZ0002001522, CZ0002001530, CZ0002001548 | 4.29% for the first 3M interest period, afterwards the relevant reference rate* less 0.20% | CZK | 7 Dec 2007 | 7 Dec 2037 | 5,018 | 5,001 |
| HZL Komerční banky, a.s., CZ0002001555, CZ0002001563, CZ0002001571, CZ0002001589 | 4.33% for the first 3M interest period, afterwards the relevant reference rate* less 0.20% | CZK | 12 Dec 2007 | 12 Dec 2037 | 5,023 | 5,053 |
| HZL Komerční banky, a.s., CZ0002001753 | Rate of the interest rate swap sale in CZK for 10 years plus 150 bps | CZK | 21 Dec 2007 | 21 Dec 2037 | 8,587 | 8,837 |
| HZL Komerční banky, a.s., CZ0002001761 | 4.09% | CZK | 19 Dec 2007 | 19 Dec 2017 | 129 | 259 |
| HZL Komerční banky, a.s., CZ0002002801 | 2.55% | CZK | 21 Dec 2012 | 21 Dec 2022 | 3,021 | 3,023 |
| HZL Komerční banky, a.s., CZ0002003064 | 6M PRIBOR plus 50 bps | CZK | 14 Mar 2013 | 14 Mar 2018 | 1,745 | 1,761 |
| HZL Komerční banky, a.s., CZ0002003346 | 3.50% | CZK | 31 Jan 2014 | 31 Jan 2026 | 873 | 877 |
| HZL Komerční banky, a.s., CZ0002003353 | 3.50% | CZK | 31 Jan 2014 | 31 Jan 2025 | 1,255 | 1,266 |
| HZL Komerční banky, a.s., CZ0002003361 | 3.00% | CZK | 30 Jan 2014 | 30 Jan 2024 | 951 | 954 |
| HZL Komerční banky, a.s., CZ0002003379 | 3.00% | CZK | 30 Jan 2014 | 30 Apr 2022 | 846 | 852 |
| HZL Komerční banky, a.s., CZ0002003742 | 2.00% | CZK | 18 Nov 2014 | 18 Nov 2026 | 829 | 817 |
| HZL Komerční banky, a.s., CZ0002003759 | 2.10% | CZK | 24 Nov 2014 | 24 Nov 2027 | 838 | 822 |
| HZL Komerční banky, a.s., CZ0002003767 | 2.20% | CZK | 20 Nov 2014 | 20 Nov 2028 | 849 | 829 |
| HZL Komerční banky, a.s., CZ0002003775 | 2.30% | CZK | 27 Nov 2014 | 27 Nov 2029 | 854 | 831 |
| **Total mortgage bonds** | | | | | **43,362** | **43,717** |

* The reference rate can be of the following type: 3M PRIBOR to 12M PRIBOR, the swap sale for 2 to 30 years.
Six-month PRIBOR as of 31 December 2016 was 35 bps (2015: 37 bps).
The value of the interest rate swap CZK sale average for five years as of 31 December 2016 was 52 bps (2015: 67 bps).
The value of the interest rate swap CZK sale average for ten years as of 31 December 2016 was 88 bps (2015: 103 bps).

## 31 Accruals and other liabilities

*Accruals and other liabilities comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Accruals and deferred income | 211 | 133 |
| Settlement balances and outstanding items | 0 | 0 |
| Payables from securities trading and issues of securities | 3,305 | 2,790 |
| Payables from payment transactions | 6,590 | 6,863 |
| Other liabilities | 4,043 | 3,778 |
| **Total accruals and other liabilities** | **14,149** | **13,564** |

Deferred fees from banking guarantees are reported in 'Accruals and deferred income' in the amount of CZK 22 million (2015: CZK 19 million).

*'Other liabilities'* mainly include liabilities arising from the supplies of goods and services and employee arrangements (including estimated balances).

## 32 Provisions

*Provisions comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Provisions for contracted commitments (refer to Notes 12 and 36) | 460 | 366 |
| Provisions for other credit commitments (refer to Note 12) | 1,241 | 783 |
| **Total provisions** | **1,701** | **1,149** |

The provisions for other credit commitments are held to cover credit risks associated with credit commitments issued. The provisions for contracted commitments principally comprise the provisions for ongoing contracted contingent commitments, legal disputes, self-insurance and the retirement benefits plan.

*Set out below is an analysis of the provisions for other credit commitments:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Provision for off-balance sheet commitments | 1,206 | 728 |
| Provision for undrawn loan facilities | 35 | 55 |
| **Total** (refer to Note 12) | **1,241** | **783** |

*Movements in the provisions for contracted commitments were as follow:*

| (CZKm) | Retirement benefits plan | Other provisions for contracted commitments | Total |
|---|---|---|---|
| Balance as of 1 January 2015 | 176 | 457 | 633 |
| Charge | 12 | 89 | 101 |
| Release | 0 | (334) | (334) |
| Use | (11) | (48) | (59) |
| Accrual | 3 | 0 | 3 |
| Remeasurement | 20 | 0 | 20 |
| Foreign exchange difference | 0 | 2 | 2 |
| **Balance as of 31 December 2015** | **200** | **166** | **366** |
| Charge | 12 | 34 | 46 |
| Release | 0 | (53) | (53) |
| Use | (9) | (10) | (19) |
| Accrual | 4 | 0 | 4 |
| Remeasurement | 115 | 0 | 115 |
| Foreign exchange difference | 0 | 1 | 1 |
| **Balance as of 31 December 2016** | **322** | **138** | **460** |

## 33 Deferred tax

Deferred tax is calculated from temporary differences between the tax bases and carrying values using tax rates effective in the periods in which the temporary tax difference is expected to be realised.

*Net deferred tax assets are as follow:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Banking provisions and allowances | 0 | 0 |
| Allowances for assets | 0 | 0 |
| Non-banking provisions and allowances | 30 | 31 |
| Difference between accounting and tax net book value of assets | 1 | 1 |
| Remeasurement of retirement benefits plan – equity impact (refer to Note 38) | 0 | 0 |
| Revaluation of hedging derivatives – equity impact (refer to Note 39) | 0 | 1 |
| Revaluation of available-for-sale financial assets – equity impact (refer to Note 40) | 0 | 0 |
| Other temporary differences | 0 | 0 |
| **Net deferred tax assets** | **31** | **33** |

*Net deferred tax liabilities are as follow:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Banking provisions and allowances | 284 | 184 |
| Allowances for assets | 77 | 81 |
| Non-banking provisions and allowances | 16 | 18 |
| Difference between accounting and tax net book value of assets | (323) | (332) |
| Remeasurement of retirement benefits plan – equity impact (refer to Note 38) | 31 | 9 |
| Revaluation of hedging derivatives – equity impact (refer to Note 39) | (2,667) | (2,972) |
| Revaluation of available-for-sale financial assets – equity impact (refer to Note 40) | (639) | (956) |
| Other temporary differences | 156 | 82 |
| **Net deferred tax liabilities** | **(3,065)** | **(3,886)** |

Since 2007, the Bank has not reported any deferred tax arising from the revaluation of a foreign net investment.

*Movements in the net deferred tax assets/(liabilities) were as follow:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| **Balance as of the beginning of the period** | **(3,853)** | **(4,491)** |
| Movement in the net deferred tax – profit and loss impact (refer to Note 14) | 176 | (112) |
| Movement in the net deferred tax – equity impact (refer to Notes 38, 39 and 40) | 643 | 750 |
| **Balance as of the end of the period** | **(3,034)** | **(3,853)** |

## 34 Share capital

The Bank's share capital, entered in the Register of Companies on 11 February 2000, amounts to CZK 19,004,926,000. Based on a decision of the Annual General Meeting held on 22 April 2016, the Bank split its shares in the rate of 5:1, which means that the number of the shares increased by splitting the existing shares into 190,049,260 ordinary bearer shares issued as uncertificated securities with a nominal value of CZK 100 each (ISIN: CZ0008019106). The number of shares authorised is the same as the number of shares issued. The share capital is fully paid up.

The Bank's shares are publicly traded on stock markets in the Czech Republic managed by the market organisers Burza cenných papírů Praha, a.s. (the Prague Stock Exchange) and RM-SYSTÉM, česká burza cenných papírů a.s. (the Czech Stock Exchange). Their transferability is not restricted.

Rights are attached to the ordinary shares in accordance with Act No. 90/2012 Coll., on Business Corporations and Co-operatives. No special rights are attached to the shares. Shareholders' voting rights are governed by the nominal value of their shares. The voting rights can only be eliminated on statutory grounds. The Bank cannot exercise voting rights attached to its own shares.

Shareholders are entitled to share in the Bank's profit (dividend) approved for distribution by the Annual General Meeting based on the Bank's financial results and in accordance with the conditions stipulated by generally binding legal regulations.

The right to payment of the dividend is time-barred from four years after its declared payment date. Pursuant to a resolution of the Annual General Meeting held in 2009, the Board of Directors will not plead the statute of limitations in order to bar by lapse of time the payment of dividends for the duration of 10 years from the date of dividend payment. After the lapse of 10 years from the date of dividend payment, the Board of Directors is obliged to plead the statute of limitations and to transfer the unpaid dividends to the retained earnings account.

In the event of a shareholder's death, his or her legal heir shall be entitled to exercise all rights attached to the shares. Upon the Bank's liquidation and dissolution, the means of liquidation are governed by the relevant generally binding legal regulations. The proposal for the distribution of the liquidation balance among shareholders is approved by the Annual General Meeting in proportion to the nominal values of the shares held by the Bank's shareholders.

*Set out below is a summary of the entities that hold more than 1% of the Bank's issued share capital as of 31 December 2016:*

| Name of the entity | Ownership percentage |
|---|---|
| SOCIETE GENERALE S.A. | 60.35% |
| NORTRUST NOMINEES LIMITED | 4.20% |
| CHASE NOMINEES LIMITED | 3.59% |
| BROWN BROTHERS HARRIMAN | 2.70% |
| STATE STREET BANK AND TRUST COMPANY | 2.44% |
| CLEARSTREAM BANKING, S.A. | 2.23% |
| GIC PRIVATE LIMITED | 2.06% |
| J.P. MORGAN BANK | 1.09% |
| AGF INVESTMENTS INC. | 1.00% |

Société Générale S.A., being the only entity with a qualified holding in the Bank, and moreover as the parent company, is a French company limited by shares incorporated by a Deed approved through the issuance of a Decree on 4 May 1864 and is licensed as a bank. Under the legislative and regulatory provisions relating to financial institutions, notably the articles of the Monetary and Financial Code, the Company is subject to commercial laws, in particular Articles 210-1 et seq. of the French Commercial Code, as well as its Articles of Association.

As of 31 December 2016, the Bank held 1,193,360 of its own share in treasury at a cost of CZK 726 million (2015: 238,672 treasury shares which equals the number of 238,672 shares before shares split at a cost of CZK 726 million).

**Capital management**

The Basel III rules, known in EU regulation as CRR/CRD IV, effective from 2014, did not change the process for managing the Bank's regulatory capital adequacy management, but they were taken into consideration when setting the parameters of that process as concerns in particular application of the combined capital buffer and additional Pillar 2 buffer on top of the minimum required capital ratio of 8.0%. The regulatory methodology was stabilised in 2016 (in particular the stacking order of capital buffers), and consequently an additional Pillar 2 buffer of 1.5% over the minimum required capital ratio of 8.0% is applied to the Bank. That means the total SREP (supervisory review and evaluation process) capital requirement (TSCR) is 9.5%. The combined capital buffer of 5.0% is applied on top of the TSCR capital ratio, resulting in the required overall capital ratio of 14.5% for the year 2016 (an increased by 0.1% in comparison with the previous year). The combined capital buffer consists of the capital conservation buffer of 2.5% and the systemic risk buffer of 2.5%. A countercyclical buffer was effectively not applied. Inasmuch as its capital ratio stands well above the minimum required level, the Bank meets the required level of the overall capital ratio with an adequate reserve.

The Bank manages its capital adequacy to ensure its sufficient level in an environment of changing regulatory requirements while allowing organic business growth and for potentially adverse macroeconomic development. Under the Basel III capital adequacy regulation, just as under the previous Basel II regulation, in addition to the usual reporting of the capital ratio (Pillar 1), the Bank must meet the requirements for evaluating required economic capital, stress testing and capital planning (Pillar 2). To determine the required economic capital, the Bank has selected methods close to the regulatory procedures applied for Pillar 1. Consequently, the necessary levels of economic and regulatory capital are very similar.

The Bank regularly simulates future developments under Pillar 2 based on the assumption of possible adverse external macroeconomic conditions that may either directly affect the Bank's profit or have implications resulting in deterioration in the Bank's transactions' risk profile.

The Bank compiles hypothetical macroeconomic scenarios on the basis of which it estimates medium-term impacts on earnings and on transactions' risk profiles. On this basis, the Bank acquires views as to the changing volume of the risk-weighted assets (i.e. capital requirements), financial results, and, while also taking into account the outlook for dividend payments, the level of the Bank's capital adequacy ratio.

The results of such stress testing are among those factors considered in determining the Bank's dividend policy, which is the primary tool for capital adequacy management in such situation that the Bank's capital is entirely classified as Common Equity Tier 1 capital.

The Bank's capital principally consists of the following balances: share capital, reserve funds and retained earnings.

The Bank did not purchase its own shares into treasury during 2016, and as of 31 December 2016 the Bank holds in total 1,193,360 treasury shares at a total cost of CZK 726 million which equals the number of 238,672 treasury shares before shares split. These had been purchased in previous years (2015: 238,672 treasury shares at a total cost of CZK 726 million). The purchase of treasury shares had been approved by the Bank's General Meeting especially for the purpose of managing the Bank's capital adequacy.

With regard to the fact that the capital requirements of the Basel III regulation (particularly the capital buffers, typically the countercyclical buffer) can vary over time and a part of the implementation of regulatory rules and the regulation itself are still being developed, the Bank continuously monitors and evaluates the forthcoming changes in regulatory requirements affecting the capital and capital adequacy and it analyses their potential impact within the capital planning process.

The CNB, as the local regulatory authority, oversees the Bank's compliance with the capital adequacy on both separate and consolidated bases. During the past year, the Bank complied with all regulatory requirements. Moreover, the Bank regularly prepares the regulatory report on Pillar 2 (i.e. internal capital adequacy assessment process) and submits it to the CNB.

## 35 Composition of cash and cash equivalents as reported in the Statement of Cash Flows

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 | Change in the year |
|---|---|---|---|
| Cash and current balances with central banks (refer to Note 16) | 103,993 | 116,257 | (12,264) |
| Amounts due from banks – current accounts with other banks (refer to Note 20) | 788 | 445 | 343 |
| Amounts due to central banks | (1) | (1) | 0 |
| Amounts due to banks – current accounts (refer to Note 28) | (3,168) | (2,741) | (427) |
| **Cash and cash equivalents at the end of the year** | **101,612** | **113,960** | **(12,348)** |

## 36 Commitments and contingent liabilities

### Legal disputes

The Bank conducted a review of legal proceedings outstanding against it as of 31 December 2016. Pursuant to the review of significant litigation matters in terms of the risk of losses and litigated amounts, the Bank has recorded a provision of CZK 17 million (2015: CZK 40 million) for these legal disputes (refer to Note 32). The Bank has also recorded a provision of CZK 42 million (2015: CZK 46 million) for costs associated with a potential payment of appurtenances on the pursued claims.

As of 31 December 2016, the Bank conducted a review of legal proceedings it had filed against other entities. The Bank has been notified that certain parties against which it is taking legal action may file counterclaims against it. The Bank will contest any such claims and, taking into consideration the opinion of its internal and external legal counsel, believes that any asserted claims made will not materially affect its financial position. No provision has been made in respect of these matters.

### Commitments arising from the issuance of guarantees

Commitments from guarantees represent irrevocable assurances that the Bank will make payments in the event that a customer cannot meet its obligations to the third parties. These assurances carry the same credit risk as do loans, and therefore the Bank makes provisions for these instruments (according to a customer's creditworthiness) on the same basis as is applicable to loans.

### Capital commitments

As of 31 December 2016, the Bank had capital commitments of CZK 367 million (2015: CZK 458 million) in respect of current capital investment projects.

### Commitments arising from the issuance of letters of credit

Documentary letters of credit are written, irrevocable commitments by the Bank on behalf of a customer (mandatory) authorising a third party (beneficiary) to draw drafts on the Bank up to a stipulated amount under specific terms and conditions. The Bank records provisions for these instruments (according to a customer's creditworthiness) on the same basis as is applicable to loans.

### Commitments to extend credit, undrawn loan commitments and overdrafts and approved overdraft loans

Principal off-balance sheet exposures include undrawn limits under framework agreements to provide financial services, approved overdraft loans, undrawn loan commitments, issued commitments to extend credit and unutilised facilities. The primary purpose of commitments to extend credit and framework agreements is to ensure that funds are available to a customer as required. Commitments to extend credit represent unused portions of authorisations to extend credit in the forms of loans or guarantees. In accordance with the IFRS definition of a conditioned commitment the Bank distinguishes between irrevocable and revocable commitments to extend credit and framework agreements. The irrevocability of commitments, framework agreements of undrawn loan commitments, unutilised overdrafts and approved overdraft loans results from contractual terms and conditions of the credit agreements (i.e. their use is not contingent upon customers' maintaining other specific credit standards). For irrevocable commitments or framework agreements, undrawn loan commitments, unutilised overdrafts and approved overdraft loans, the Bank recognises a provision when required (according to a customer's credit worthiness) in accordance with the same algorithm as for loans.

*Financial commitments and contingencies comprise the following:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Non-payment guarantees including commitments to issued non-payment guarantees | 36,248 | 35,358 |
| Payment guarantees including commitments to issued payment guarantees | 15,058 | 13,036 |
| Committed facilities and unutilised overdrafts | 6,333 | 10,967 |
| Undrawn credit commitments | 57,757 | 45,878 |
| Unutilised overdrafts and approved overdraft loans | 15,674 | 13,309 |
| Unutilised limits under framework agreements to provide financial services | 9,445 | 10,820 |
| Open customer/import letters of credit uncovered | 755 | 566 |
| Standby letters of credit uncovered | 1,091 | 1,336 |
| Confirmed supplier/export letters of credit | 22 | 52 |
| **Total commitments and contingencies** | **142,383** | **131,322** |

The risk associated with off-balance sheet credit commitments and contingent liabilities is assessed on the same basis as is that of loans to customers, taking into account the financial position and activities of the entity to which the Bank issued the guarantee and the collateral obtained. As of 31 December 2016, the Bank recorded provisions for these risks in the amount of CZK 1,241 million (2015: CZK 783 million). Refer to Note 32.

*Set out below is a breakdown of financial commitments and contingencies by sector:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Food industry and agriculture | 10,318 | 8,207 |
| Mining and extraction | 665 | 387 |
| Chemical and pharmaceutical industry | 3,601 | 3,406 |
| Metallurgy | 4,488 | 5,130 |
| Automotive industry | 1,501 | 1,318 |
| Manufacturing of other machinery | 7,723 | 7,253 |
| Manufacturing of electrical and electronic equipment | 2,441 | 1,894 |
| Other processing industry | 1,932 | 1,540 |
| Power plants, gas plants and waterworks | 4,674 | 7,225 |
| Construction industry | 31,968 | 32,839 |
| Retail | 3,710 | 2,880 |
| Wholesale | 7,858 | 7,821 |
| Accommodation and catering | 400 | 417 |
| Transportation, telecommunication and warehouses | 9,134 | 9,359 |
| Banking and insurance industry | 8,164 | 4,443 |
| Real estate | 3,201 | 2,876 |
| Public administration | 4,201 | 3,143 |
| Other industries | 13,047 | 12,459 |
| Individuals | 23,357 | 18,725 |
| **Total commitments and contingencies** | **142,383** | **131,322** |

The majority of commitments and contingencies originate on the territory of the Czech Republic.

*Set out below is an analysis of the types of collateral held in support of financial commitments and contingencies:*

| (CZKm) | 31 Dec 2016 Total commitments and contingencies collateral* | 31 Dec 2016 Discounted commitments and contingencies collateral value** | 31 Dec 2016 Applied commitments and contingencies collateral value*** | 31 Dec 2015 Total commitments and contingencies collateral* | 31 Dec 2015 Discounted commitments and contingencies collateral value** | 31 Dec 2015 Applied commitments and contingencies collateral value*** |
|---|---|---|---|---|---|---|
| Guarantees of state and governmental institutions | 658 | 523 | 523 | 0 | 0 | 0 |
| Bank guarantee | 1,585 | 1,515 | 1,475 | 975 | 918 | 873 |
| Guaranteed deposits | 2,187 | 2,174 | 2,072 | 2,133 | 2,103 | 1,975 |
| Pledge of real estate | 11,629 | 7,231 | 5,990 | 9,981 | 6,105 | 4,995 |
| Pledge of movable assets | 84 | 8 | 8 | 226 | 22 | 22 |
| Guarantee by legal entity | 6,540 | 1,988 | 1,821 | 7,452 | 5,247 | 5,034 |
| Guarantee by individual (natural person) | 50 | 10 | 10 | 65 | 6 | 6 |
| Pledge of receivables | 1,939 | 0 | 0 | 3,317 | 0 | 0 |
| Insurance of credit risk | 1,554 | 1,476 | 1,476 | 2,085 | 1,925 | 1,925 |
| Other | 21 | 0 | 0 | 22 | 0 | 0 |
| **Total nominal value of collateral** | **26,247** | **14,925** | **13,375** | **26,256** | **16,326** | **14,830** |

* The nominal value of the collateral is determined based on internal rules of the Bank (e.g. internal property valuation, the current value of collateral, the market value of securities, etc.).
** The nominal value of the collateral is reduced by a coefficient taking into account the time value of money, the cost of selling the collateral, the risk of declining market prices, the risk of insolvency, etc.
*** The applied collateral value is the discounted collateral value reduced to the actual balance of the collateralised exposure.

In accordance with Act No. 427/2011, on Supplementary pension saving, and in accordance with the statutes of the Transformovaný fond KB Penzijní společnost, a.s. (hereafter only the “Fund”) created after 1 January 2013, the KB Penzijní společnost, a.s. guarantees at least a zero return for clients on an annual basis and must ensure that the value of assets in the Fund is always equal to or greater than the value of liabilities. Otherwise, KB Penzijní společnost, a.s. is required to contribute to the Fund assets necessary to adjust the difference at latest within 30 days after the end of the quarter in which such fact was identified. These transferred assets constitute a special capital fund of the Fund and are primarily used to cover losses of the current year or accumulated losses from prior periods.

In accordance with the Fund’s conservative strategy and based on sensitivity analysis, the usage of the guarantee is not probable in the near future as of the financial statements date.

## 37 Related parties

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the other party on making financial or operational decisions. As of 31 December 2016, the Bank was controlled by Société Générale S.A., which owns 60.35% of its issued share capital.

A number of banking transactions are entered into with related parties in the normal course of business. These specifically include loans, deposits, transactions with derivative financial instruments and other types of transactions. These transactions are carried out on an arm’s length basis.

## Amounts due to and from the Group subsidiaries

*The following table summarises loans issued to the Group subsidiaries and their deposits with the Bank:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Bastion European Investments S.A. | 3,058 | 3,157 |
| ESSOX s.r.o. | 7,493 | 5,379 |
| Factoring KB, a.s. | 5,915 | 5,109 |
| KB Real Estate, s.r.o. | 483 | 513 |
| Modrá pyramida stavební spořitelna, a.s. | 12,900 | 11,500 |
| SG Equipment Finance Czech Republic s.r.o. | 12,873 | 13,916 |
| **Total loans** | **42,722** | **39,574** |
| Bastion European Investments S.A. | 0 | 91 |
| Cataps, s.r.o. | 0 | 4 |
| ESSOX s.r.o. | 937 | 807 |
| Factoring KB, a.s. | 1 | 1 |
| KB Penzijní společnost, a.s. | 470 | 624 |
| KB Real Estate, s.r.o. | 53 | 54 |
| Modrá pyramida stavební spořitelna, a.s. | 2 | 0 |
| NP 33, s.r.o. | 17 | 132 |
| Protos, uzavřený investiční fond, a.s. | 79 | 475 |
| SG Equipment Finance Czech Republic s.r.o. | 2,187 | 3,795 |
| VN 42, s.r.o. | 419 | 299 |
| **Total deposits** | **4,165** | **6,282** |

*The following table summarises the fair value of financial derivatives to which the Bank is a party and in relation to the Group subsidiaries:*

| (CZKm) | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Modrá pyramida stavební spořitelna, a.s. | 55 | 38 |
| Protos, uzavřený investiční fond, a.s. | 2 | 18 |
| SG Equipment Finance Czech Republic s.r.o. | 1 | 1 |
| **Total positive fair value of financial derivatives** | **58** | **57** |
| Modrá pyramida stavební spořitelna, a.s. | 711 | 635 |
| Protos, uzavřený investiční fond, a.s. | 5 | 0 |
| **Total negative fair value of financial derivatives** | **716** | **635** |

Modrá pyramida stavební spořitelna, a.s. owns mortgage bonds in a nominal value of CZK 30,600 million (2015: CZK 30,600 million) issued by the Bank. ESSOX s.r.o. owns mortgage bonds issued by the Bank in the nominal value of CZK 629 million (2015: CZK 757 million). KB Penzijní společnost, a.s. owns mortgage bonds issued by the Bank in the nominal value of CZK 417 million (2015: CZK 417 million).

As of 31 December 2016 and 2015, other amounts due to and from the Group subsidiaries were not significant.

*Interest income from loans granted to the Group subsidiaries:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Bastion European Investments S.A. | 120 | 125 |
| ESSOX s.r.o. | 50 | 69 |
| Factoring KB, a.s. | 19 | 18 |
| KB Real Estate, s.r.o. | 16 | 17 |
| Modrá pyramida stavební spořitelna, a.s. | 2 | 0 |
| SG Equipment Finance Czech Republic s.r.o. | 142 | 197 |
| **Total interest from loans granted by the Bank** | **349** | **426** |

In addition to interest on loans to the Bank's Group subsidiaries, other income in the year ended 31 December 2016 amounted to CZK 356 million (2015: CZK 187 million) and total expenses amounted to CZK 1,747 million (2015: CZK 1,467 million).

As of 31 December 2016, the Bank reported guarantees granted and undrawn credit commitments to the Group subsidiaries totalling CZK 405 million (2015: CZK 335 million).

### Amounts due to and from the Société Générale Group entities

*Principal balances due from the Société Générale Group entities include the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **(CZKm)** | **Total** | **Of which derivatives** | **Total** | **Of which derivatives** |
| ALD Automotive s.r.o. (Czech Republic) | 5,146 | 0 | 3,820 | 0 |
| ALD Automotive s.r.o. (Slovak Republic) | 370 | 0 | 648 | 0 |
| BRD – GROUPE Société Générale | 30 | 0 | 0 | 0 |
| Komerční pojišťovna, a.s. | 1,587 | 1,521 | 1,986 | 1,911 |
| PJSC Rosbank | 146 | 0 | 67 | 0 |
| SG Expressbank | 15 | 0 | 10 | 0 |
| SG New York | 498 | 0 | 0 | 0 |
| SG Marocaine de Banques | 4 | 0 | 0 | 0 |
| SG Zurich | 176 | 0 | 0 | 0 |
| Société Générale Algerie | 0 | 0 | 2 | 0 |
| Société Générale China | 3 | 0 | 19 | 0 |
| Société Générale International | 473 | 0 | 3 | 0 |
| Société Générale Paris | 8,392 | 4,311 | 7,997 | 4,230 |
| Société Générale oddzial w Polsce | 2 | 0 | 1 | 0 |
| Société Générale – Splitska Banka | 11 | 0 | 5 | 0 |
| **Total** | **16,853** | **5,832** | **14,558** | **6,141** |

*Principal balances owed to the Société Générale Group entities include the following:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| **(CZKm)** | **Total** | **Of which derivatives** | **Total** | **Of which derivatives** |
| ALD Automotive s.r.o. (Czech Republic) | 368 | 0 | 186 | 0 |
| BRD – GROUPE Société Générale | 8 | 0 | 3 | 1 |
| Crédit du Nord | 7 | 0 | 0 | 0 |
| Inter Europe Conseil | 0 | 0 | 2 | 0 |
| Komerční pojišťovna, a.s. | 2,532 | 46 | 2,106 | 47 |
| PEMA Praha, spol. s r.o. | 101 | 0 | 13 | 0 |
| SG Amsterdam | 47 | 0 | 46 | 0 |
| SG Banques au Liban | 1 | 0 | 14 | 0 |
| SG Bruxelles | 50 | 0 | 0 | 0 |
| SG ISSUER | 1 | 0 | 0 | 0 |
| SG Frankfurt | 8 | 0 | 1 | 0 |
| SG London | 13 | 0 | 11 | 0 |
| SG New York | 1 | 0 | 2 | 0 |
| SG Private Banking (Suisse) | 184 | 0 | 280 | 0 |
| SG Zurich | 0 | 0 | 1 | 0 |
| SGSS Nantes | 3 | 0 | 0 | 0 |
| Société Générale Bank & Trust | 63 | 0 | 19 | 0 |
| Société Générale Paris | 22,938 | 7,025 | 25,586 | 6,925 |
| Société Générale oddzial w Polsce | 1 | 0 | 3 | 0 |
| SOGEPROM Česká republika, s.r.o. | 5 | 0 | 6 | 0 |
| Société Générale – Splitska Banka | 1 | 0 | 1 | 0 |
| **Total** | **26,332** | **7,071** | **28,280** | **6,973** |

Amounts due to and from the Société Générale Group entities principally comprise balances of current and overdraft accounts, nostro and loro accounts, issued loans, interbank market loans and placements, deposited margins in favour of the counterparty and fair values of derivatives.

As of 31 December 2016, the Bank also carried off-balance sheet exposures to the Société Générale Group entities, of which off-balance sheet nominal assets and liabilities amounted to CZK 371,922 million (2015: CZK 280,152 million) and CZK 341,528 million (2015: CZK 268,917 million), respectively. These amounts principally relate to currency spots and forwards, interest rate forwards and swaps, options, commodity derivatives, emission allowances and guarantees for credit exposures.

As of 31 December 2016 and 2015, the Bank also carried other amounts due to and from the Société Générale Group entities which are not significant.

During the year ended 31 December 2016, the Bank had total income of CZK 22,334 million (2015: CZK 21,935 million) and total expenses of CZK 19,185 million (2015: CZK 19,940 million) in relation to the Société Générale Group entities. That income includes income from interbank deposits, fees from transactions with securities, profit from financial operations and interest income on hedging derivatives. Expenses comprise those of interbank deposits, a loss from financial operations, interest expense on hedging derivatives and expenses related to the provision of management, consultancy and software services.

### Remuneration and amounts due from members of the Board of Directors and Supervisory Board

*Remuneration paid to the members of the Board of Directors and Supervisory Board during the years was as follows:*

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Remuneration to the Board of Directors members* | 58 | 61 |
| Remuneration to the Supervisory Board members** | 6 | 5 |
| **Total** | **64** | **66** |

* Remuneration to the Board of Directors members includes wages paid during the year ended 31 December 2016 to the current and former directors under mandate and management contracts and other compensation and benefits granted in 2016. It also includes a part of bonuses awarded in 2016. The remuneration includes as well benefits arising to the Bank's employees under a collective bargaining agreement.

** Remuneration to the Supervisory Board members includes amounts paid during the year ended 31 December 2016 to the current and former members of the Supervisory Board. Amounts for the Supervisory Board members elected by employees additionally include income paid to them under their employment arrangement with the Bank. The remuneration also includes benefits arising to the Bank's employees under a collective bargaining agreement.

| | 31 Dec 2016 | 31 Dec 2015 |
|---|---|---|
| Number of the Board of Directors members at the end of the period | 5 | 6 |
| Number of the Supervisory Board members at the end of the period | 9 | 9 |

In respect of loans and guarantees as of 31 December 2016, the Bank recorded receivables from loans granted to members of the Board of Directors and Supervisory Board totalling CZK 15 million (2015: CZK 21 million). During 2016, draw-downs of CZK 1 million (2015: CZK 10 million) were made under the loans granted. Loan repayments during 2016 amounted to CZK 1 million (2015: CZK 11 million). The increase of loans in 2016 is affected by new members already having loans in the amount of CZK 6 million. The amount of loans of resigning members amounted to CZK 12 million as of 31 December 2015.

## 38 Movements in the remeasurement of retirement benefits plan in the equity

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Remeasurement of retirement benefits plan as of 1 January | (47) | (27) |
| Deferred tax asset/(liability) as of 1 January | 9 | 5 |
| **Balance as of 1 January** | **(38)** | **(22)** |
| **Movements during the year** | | |
| Gains/(losses) from remeasurement of retirement benefits plan | (115) | (20) |
| Deferred tax | 22 | 4 |
| | **(93)** | **(16)** |
| Remeasurement of retirement benefits plan as of 31 December | (162) | (47) |
| Deferred tax asset/(liability) as of 31 December (refer to Note 33) | 31 | 9 |
| **Balance as of 31 December** | **(131)** | **(38)** |

## 39 Movements in the revaluation of hedging instruments in the equity

In accordance with IAS 39, certain derivatives were designated as hedges. The changes in fair values of cash flow hedges are recorded in a separate line of equity in the hedging reserve.

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Cash flow hedge fair value as of 1 January | 15,807 | 19,742 |
| Deferred tax asset/(liability) as of 1 January | (2,971) | (3,733) |
| **Balance as of 1 January** | **12,836** | **16,009** |
| **Movements during the year** | | |
| Gains/(losses) from changes in fair value | 2,405 | 191 |
| Deferred tax | (456) | (36) |
| | **1,949** | **155** |
| Transferred to interest income/expense | (4,008) | (4,195) |
| Deferred tax | 761 | 797 |
| | **(3,247)** | **(3,398)** |
| Transferred to net profit/loss on financial operations | 1 | 0 |
| Deferred tax | 0 | 0 |
| | **1** | **0** |
| Transferred to personnel expenses | 5 | (8) |
| Deferred tax | (1) | 1 |
| | **4** | **(7)** |
| Change in the hedge of foreign currency risk of foreign net investment | (4) | 77 |
| | **(4)** | **77** |
| Cash flow hedge fair value as of 31 December | 14,206 | 15,807 |
| Deferred tax asset/(liability) as of 31 December (refer to Note 33) | (2,667) | (2,971) |
| **Balance as of 31 December** | **11,539** | **12,836** |

## 40 Movements in the revaluation of available-for-sale financial assets in the equity

| (CZKm) | 2016 | 2015 |
|---|---|---|
| Reserve from fair value revaluation as of 1 January | 5,032 | 4,948 |
| Deferred tax asset/(liability) as of 1 January | (956) | (940) |
| **Balance as of 1 January** | **4,076** | **4,008** |
| **Movements during the year** | | |
| Gains/(losses) from changes in fair value | (20) | 896 |
| Deferred tax | 4 | (170) |
| | **(16)** | **726** |
| (Gains)/losses from reclassified financial assets (refer to Note 18) | (691) | (812) |
| Deferred tax | 131 | 154 |
| | **(560)** | **(658)** |
| (Gains)/losses from sale | (960) | 0 |
| Deferred tax | 182 | 0 |
| | **(778)** | **0** |
| Reserve from fair value revaluation as of 31 December | 3,361 | 5,032 |
| Deferred tax asset/(liability) as of 31 December (refer to Note 33) | (639) | (956) |
| **Balance as of 31 December** | **2,722** | **4,076** |

# 41 Risk management and financial instruments

## (A) Credit risk

### Assessment of borrower's credit rating

The assessment of credit risk is based on quantitative and qualitative criteria, which leads to a rating assignment. The Bank uses several types of ratings, depending on the type and profile of the counterparty and the types of transactions. As a result, specific ratings are assigned to both the Bank's clients and to specific client transactions. The same process of rating assignment is applied in relevant cases to respective guarantors and sub-debtors, which enables better assessment of the quality of accepted guarantees and collaterals.

In 2016, the Bank focused on updating selected credit risk models in order to optimally reflect the current macroeconomic situation and goals set by the Bank as well as on increasing effectiveness in monitoring the risk profiles of individual client portfolios and the quality of tools and models for credit risk management.

As in previous years, the results of regular stress testing played an important role, allowing more precise estimates of the expected intensity of credit risk for the ensuing periods and thus optimisation of the Bank's credit risk management tools and more accurate estimation of expected future losses.

### *(a) Business clients and municipalities*

For entrepreneurs, corporate clients and municipalities, the Bank uses the obligor rating (expressed on the 22 grade Société Générale rating master scale) with the aim to evaluate the counterparty's Probability of Default (PD) and the Loss Given Default (LGD) rating to assess the quality of available guarantees and collaterals and to evaluate the potential loss from counterparty transactions. These models are also used for regular updates of Expected Loss (EL) and Unexpected Loss (UL) for all client exposures reported in accordance with the Basel III requirements.

For large and medium-sized clients, the obligor rating is the combination of the financial rating based primarily on the data in the financial statements and an economic rating obtained through the evaluation of non-financial information relating to a particular client.

In the entrepreneurs and small companies segment, the obligor rating is the combination of financial, non financial and personal data, data on client behaviour within the Bank and information from external credit bureaus. When clients are funded via simple products, the setting of the rating is alternatively limited to the evaluation of data on clients' behaviour within the Bank (behavioural rating).

In the municipalities segment, the obligor rating is the combination of the financial rating based on the data in the financial statements and of an economic rating acquired through the assessment of non-financial information relating to a specific municipality.

The Bank is also using dedicated rating model for housing co-operatives and association of owners. A special model for real estate developers and investors is currently in the validation phase.

### *(b) Ratings for banks and sovereigns*

For banks, other financial institutions (namely insurance companies, brokers and funds) and for sovereigns (central banks and central governments), the Bank uses the economic rating models developed by Société Générale.

### *(c) Ratings for individual clients*

The Bank uses two types of ratings with the aim to evaluate the default risk for individuals: (1) the application rating, which results from an evaluation of clients' personal data, data on the behaviour within the Bank, and data available from external credit bureaus; and (2) a behavioural rating which is based on evaluation of information on the clients' behaviour within the Bank. The application rating is primarily used for active applications of clients for funding, while the behavioural rating (which includes the calculation of indicative limits for simple products with low exposure) is used for active offers of funding by the Bank. The behavioural rating of clients is concurrently used as an input for regular updates of the probability of default of all client exposures reported in accordance with the Basel III requirements.

### (d) *Internal register of negative information*

The Bank maintains an internal register of negative information. The register integrates the maximum quantity of available internal and external negative information on subjects related to the credit process. It includes algorithms for evaluating the negative information and contributes substantially to protecting the Bank from risky entities.

### (e) *Credit bureaus*

The evaluation of data from credit bureaus is one of the principal factors impacting the assessment of applications for client funding, and especially so in the retail client segments (individuals and small businesses).

### (f) *Credit fraud prevention*

The Bank uses an automated system for the detection of credit frauds and also for co ordinated reactions to credit fraud attacks. The system is fully integrated with the Bank's main applications. The system was updated in 2016 to reflect current market trends mainly in financing of the Individuals segment. Further upgrade of processes and controls preventing credit frauds in the small business segment will be performed in 2017.

## Credit concentration risk

The Bank's credit concentration risk is actively managed as a part of overall credit risk management utilising standard tools: credit risk assessment, setting of internal limits, use of risk mitigation techniques, regular reporting, producing of sector analyses and stress testing. The Bank maintains its objective not to take on any excessive credit concentration risk. Credit concentration risk management procedures cover individual counterparties as well as economically connected groups, countries, selected industry sectors and collateral providers. The system of internal limits is established so that the Bank complies with the regulatory limits set by legislation in respect of concentration risk. Refer to Notes 21 and 36 for quantitative information about credit concentration risk.

*The Bank's maximum credit exposure as of 31 December 2016:*

| | Total exposure | | | Collateral applied | | |
|---|---|---|---|---|---|---|
| (CZKm) | Statement of financial position | Off-balance sheet* | Total credit exposure | Statement of financial position | Off-balance sheet* | Total collateral |
| **Current balances with central banks** | **94,997** | **x** | **94,997** | **0** | **x** | **0** |
| **Financial assets at fair value through profit or loss** | **30,482** | **x** | **30,482** | **0** | **x** | **0** |
| **Positive fair value of hedging financial derivatives** | **21,614** | **x** | **21,614** | **0** | **x** | **0** |
| **Available-for-sale financial assets** | **31,411** | **x** | **31,411** | **0** | **x** | **0** |
| **Amounts due from banks** | **58,003** | **1,141** | **59,144** | **10,901** | **54** | **10,955** |
| **Loans and advances to customers** | **539,123** | **141,242** | **680,365** | **245,856** | **13,321** | **259,177** |
| – Individuals | 231,004 | 23,357 | 254,361 | 176,587 | 3,968 | 180,555 |
| of which: mortgage loans | 207,823 | 16,150 | 223,973 | 172,421 | 3,965 | 176,386 |
| consumer loans | 19,773 | 94 | 19,867 | 4,166 | 4 | 4,170 |
| – Corporates** | 304,855 | 117,885 | 422,740 | 69,269 | 9,353 | 78,622 |
| of which: top corporate clients | 165,673 | 75,191 | 240,864 | 36,036 | 4,309 | 40,345 |
| – Debt securities | 3,193 | x | 3,193 | 0 | x | 0 |
| – Other amounts due from customers | 71 | x | 71 | 0 | x | 0 |
| **Held-to-maturity investments** | **62,425** | **x** | **62,425** | **0** | **x** | **0** |
| **Total** | **838,055** | **142,383** | **980,438** | **256,757** | **13,375** | **270,132** |

* Undrawn amounts, commitments, guarantees, etc.
** This item also includes loans provided to individual entrepreneurs.

The maximum credit exposure is presented on a gross basis (i.e. without the impact of allowances).

*The Bank's maximum credit exposure as of 31 December 2015:*

| | | | Total exposure | | | Collateral applied |
|---|---|---|---|---|---|---|
| **(CZKm)** | **Statement of financial position** | **Off-balance sheet*** | **Total credit exposure** | **Statement of financial position** | **Off-balance sheet*** | **Total collateral** |
| **Current balances with central banks** | **104,900** | **x** | **104,900** | **0** | **x** | **0** |
| **Financial assets at fair value through profit or loss** | **29,889** | **x** | **29,889** | **0** | **x** | **0** |
| **Positive fair value of hedging financial derivatives** | **23,066** | **x** | **23,066** | **0** | **x** | **0** |
| **Available-for-sale financial assets** | **32,700** | **x** | **32,700** | **0** | **x** | **0** |
| **Amounts due from banks** | **54,607** | **1,575** | **56,182** | **14,573** | **269** | **14,842** |
| **Loans and advances to customers** | **496,363** | **129,747** | **626,110** | **225,809** | **14,561** | **240,370** |
| – Individuals | 206,606 | 18,725 | 225,331 | 157,078 | 3,150 | 160,228 |
| of which: mortgage loans | 185,151 | 11,673 | 196,824 | 153,097 | 3,094 | 156,191 |
| consumer loans | 17,842 | 145 | 17,987 | 3,900 | 17 | 3,917 |
| – Corporates** | 286,099 | 111,022 | 397,121 | 68,731 | 11,411 | 80,142 |
| of which: top corporate clients | 148,318 | 71,278 | 219,596 | 34,682 | 7,385 | 42,067 |
| – Debt securities | 3,654 | x | 3,654 | 0 | x | 0 |
| – Other amounts due from customers | 4 | x | 4 | 0 | x | 0 |
| **Held-to-maturity investments** | **61,003** | **x** | **61,003** | **0** | **x** | **0** |
| **Total** | **802,528** | **131,322** | **933,850** | **240,382** | **14,830** | **255,212** |

* Undrawn amounts, commitments, guarantees, etc.
** This item also includes loans provided to individual entrepreneurs.

The maximum credit exposure is presented on a gross basis (i.e. without the impact of allowances).

## Classification of receivables

The Bank classifies its receivables arising from financial activities into five categories in accordance with CNB Regulation No. 163/2014. The Standard and Watch categories represent non-default while Substandard, Doubtful and Loss represent default. The classification reflects both quantitative criteria (payment discipline, financial data) and qualitative criteria (e.g. in-depth client knowledge). The classification of individuals reflects also the default sharing principle for co-debtors and guarantors of defaulted receivables in accordance with the Basel III principles.

The structure of the credit portfolio according to the classification is regularly reported to the CNB and to investors.

When forbearance measures are granted, the forborne exposures receive default status (i.e. are classified as Substandard, Doubtful or Loss according to the CNB classification). The forbearance classification discontinues after fulfilment of the pre-defined conditions:

I. In the first place after 12 months reclassification to the performing forborne exposures (i.e. those classified as Standard or Watch) is possible based on an analysis of the debtor's financial condition;
II. Followed by a minimum 2-year probation period.

In addition, proper payments must be made throughout the probation period (i.e. the material days past due, with materiality being set identically as for defaulted receivables) must not exceed 30 days. Otherwise, the exposure is downgraded back into default status.

## Characteristics of receivables that are not classified

Pursuant to the regulation issued by the CNB, the Bank does not classify other amounts due from customers. These amounts consist of non-credit receivables that principally originated from the payment system, fraudulent withdrawals, bank cheques, receivables associated with purchases of securities (on behalf of clients) that have not been settled, and receivables that arise from business arrangements that do not represent financial activities, specifically receivables arising from outstanding rental payments on non-residential premises, sale of real estate and prepayments made.

## Allowances for receivables

Depending on the client segment, materiality, risk profile and specificity of the receivables, allowances are calculated either: (i) taking into account the present value of expected future cash flows while considering all available information, including the estimated value of collateral foreclosure and the expected duration of the recovery process; or (ii) according to models using historical delinquency statistics regularly updated based on the latest loss observations and new risk drivers reflecting the phase of the business cycle; or (iii) using models based on probabilities of default and loss given default until the impairment event occurs and an individual or model allowances for impaired loans are recognised.

*The following table shows the split of customer loans (Substandard, Doubtful and Loss) based on the type of assessment:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Individually | Statistical model | Individually | Statistical model |
| Individuals | 0 | 6,362 | 2 | 7,551 |
| Corporates* | 8,177 | 2,580 | 8,312 | 1,745 |
| **Total** | **8,177** | **8,942** | **8,314** | **9,296** |

* This item also includes loans granted to individual entrepreneurs.

*As of 31 December 2016, the Bank reported the following loans not past due and past due loans not impaired:*

| | Loans | Past due loans, not impaired | | | | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | not past due | 1 to 29 days | 30 to 59 days | 60 to 89 days | 90 days to 1 year | Over 1 year | Total | Total |
| **Banks** | | | | | | | | |
| – Standard | 56,051 | 179 | 0 | 0 | 0 | 0 | 179 | 56,230 |
| – Watch | 1,773 | 0 | 0 | 0 | 0 | 0 | 0 | 1,773 |
| **Total** | **57,824** | **179** | **0** | **0** | **0** | **0** | **179** | **58,003** |
| **Customers** | | | | | | | | |
| – Standard | 509,632 | 2,622 | 13 | 1 | 0 | 0 | 2,636 | 512,268 |
| – Watch | 5,882 | 241 | 272 | 77 | 0 | 0 | 590 | 6,472 |
| **Total** | **515,514** | **2,863** | **285** | **78** | **0** | **0** | **3,226** | **518,740** |

*As of 31 December 2015, the Bank reported the following loans not past due and past due loans not impaired:*

| | Loans | Past due loans, not impaired | | | | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | not past due | 1 to 29 days | 30 to 59 days | 60 to 89 days | 90 days to 1 year | Over 1 year | Total | Total |
| **Banks** | | | | | | | | |
| – Standard | 52,319 | 0 | 0 | 0 | 0 | 0 | 0 | 52,319 |
| – Watch | 2,288 | 0 | 0 | 0 | 0 | 0 | 0 | 2,288 |
| **Total** | **54,607** | **0** | **0** | **0** | **0** | **0** | **0** | **54,607** |
| **Customers** | | | | | | | | |
| – Standard | 464,984 | 2,472 | 379 | 2 | 0 | 0 | 2,853 | 467,837 |
| – Watch | 6,005 | 212 | 945 | 95 | 1 | 0 | 1,253 | 7,258 |
| **Total** | **470,989** | **2,684** | **1,324** | **97** | **1** | **0** | **4,106** | **475,095** |

The amount of the collateral applied in respect of past due loans not impaired was CZK 1,704 million (2015: CZK 2,244 million).

## Loan collateral

The Bank uses collateral as one of its techniques for mitigating credit risk. The risk management related to collateralisation is performed by departments within the Risk Management Arm independently of the Bank's business lines.

The Bank has fully implemented in its internal system the rules for assessing collateral's eligibility according to CNB Regulation No. 163/2014. In compliance with the CNB validation, the Bank uses the Advanced Internal Ratings-Based (A-IRB) approach. For clients of the Slovak branch, the Bank uses the Standardised (STD) approach for assessing collateral eligibility.

The recognised value of collateral is set based on the Bank's internal rules for collateral valuation and discounting. The methods used in defining values and discounts take into account all relevant risks, the expected cost of collateral sale, length of sale, the historical experience of the Bank, as well as collateral eligibility according to the CNB regulation, bankruptcy/insolvency rules and other regulations. Specifically, for all real estate collateral, which is the most common type of collateral, the Bank uses independent valuations performed or supervised by a dedicated specialised department. Collateral values reflected in the calculation of capital requirements and other processes (regulatory exposure management, granting process, creation of provisions and reserves) involve the fulfilment of collateral eligibility according to CNB Regulation No. 163/2014.

The Bank (except for the Slovak branch) uses the on-line connection to the Real Estate Register for reviewing and acquiring data on pledged real estates in granting mortgages or other loans secured by real estates and for regular monitoring of selected events that may put the Bank's pledge right to real estate at risk.

## Real estate collateral valuation

Activities related to the valuation of real estates obtained as collaterals for corporate and retail loans are independent from the Bank's business processes. The valuation process is managed and controlled by a specialised internal department which co-operates with various external valuation experts.

In 2016, together with the principal activity involving real estate valuation, the Bank focused mainly upon ongoing monitoring of the real estate market with the aim to promptly identify any adverse development and to take appropriate measures as required. The Bank monitors both the residential and commercial real estate markets. An integral component of that monitoring is the revaluation of selected real estate depending on the Basel III requirements. As a result of the statistical monitoring of market prices for residential real estates, adjustment is performed regularly.

## Recovery of receivables from borrowers

The Bank continuously responded to the changing legal environment and its impact on the collection of receivables. Given the size of the portfolio in recovery, the Bank is continuously improving the efficiency and process of recovery. These efforts also involve intensified and enhanced use of external recovery capacities. During 2016, the Bank continued in regular sales of uncollateralised retail receivables to selected qualified investors so that the maximum achievable recovery rate is obtained.

The Bank paid increased attention to the application of the Insolvency Act and its impact on the process of collecting receivables from retail and corporate clients. The Bank plays an active role in the insolvency process, from the position of secured creditor, creditors' committee member or representative of creditors, whether in bankruptcy proceedings or in reorganisations, which are used by the Bank depending on the debtor's circumstances and the attitudes of other creditors.

## Credit risk hedging instruments

The Bank has not entered into any credit derivative transactions to hedge or reallocate its credit exposures.

## Credit risk of financial derivatives

The daily calculation of counterparty risk associated with financial derivatives is based on the Credit Value at Risk (CVaR) indicator. This indicator projects the potential adverse development of the market value of a derivative and the potential loss that the Bank may incur if the counterparty fails to fulfil its obligations. The maximum potential exposure is calculated at the 99% probability level and depends on the current market value and type of derivative product, the remaining time until maturity of the derivative transaction, as well as the nominal value and volatility of the underlying assets.

As of 31 December 2016, the Bank was exposed to a credit exposure of CZK 23,021 million (2015: CZK 30,945 million) on financial derivative instruments (expressed in CVaR). This amount represents the gross replacement cost at market rates as of 31 December 2016 for all outstanding agreements. The netting agreement and parameters of collateral agreement are taken into account where applicable.

The Bank puts limits on exposures to counterparties from financial derivatives in order to avoid excessive credit exposures to each client which could arise from movements in market prices. On a daily basis, the Bank monitors compliance with limits. If these are exceeded, an appropriate alert is triggered and action is taken when relevant. In the event that the limit breach is triggered by the deliberate action of a dealer ("active limit breach"), such behaviour is penalised. The Board of Directors is informed about active limit breaches on a regular basis.

## (B) Market risk

**Segmentation of the Bank's financial operations**
For market risk management purposes, the Bank's activities are internally separated into two books: the Market Book and the Structural Book. The Market Book consists of transactions initiated by the investment banking activities and the treasury desk (interbank and individually priced deposits/loans, repos/reverse repos, securities classified as held for trading, derivatives originated by investment banking). The Structural Book consists principally of business transactions (lending, accepting deposits, amounts due to and from customers), hedging transactions within the Structural Book, and other transactions not included in the Market Book.

**Products generating market risk**
Products that are traded by the Bank and generate market risks include interbank loans and deposits, currency transactions (spots, swaps, forwards), interest rate instruments (interest rate swaps, cross currency swaps, forward rate agreements, interest rate futures and futures on debt securities), government and corporate bonds, bills of exchange programmes and cash and carry exposure in emission allowances.

More complex derivatives (options, commodity derivatives, structured derivatives) which are being sold to clients are immediately offset on the market by doing "back-to-back" trades in the interbank market, mostly with Société Générale. This ensures that the Bank is not exposed to market risks associated with these derivatives (e.g. volatility risk, correlation risk, etc.).

**Market risk in the Market Book**
The Bank has developed a complex system of market risk limits with the objective of limiting potential losses due to movements in market prices by limiting the size of the risk exposure.

Since 2016, in addition to measuring and limiting the market risk at the level of Market Book as whole, the Bank measures and limits the market risks for the trading activities and the treasury activities separately.

The Bank monitors compliance with all limits on a daily basis, and if these are exceeded the Bank takes corrective action to reduce the risk exposure. The Board of Directors is informed on a quarterly basis about developments in the exposure to market risk.

In order to measure market risks inherent in the activities of the Market Book, the Bank uses the one-day historical 99% Value-at-Risk (hereafter only „VaR") concept. VaR is calculated using full revaluation of the position by means of historical market price scenarios. This method reflects correlations between various financial markets and underlying instruments on a non-parametric basis, inasmuch as it uses scenarios simulating one-day variations of relevant market parameters over a period of time limited to the past 260 business days. The resulting 99% VaR indicator captures the loss that would be incurred after eliminating the 1% of the most unfavourable occurrences. This estimate is calculated as the average of the second and the third largest potential losses out of the 260 considered scenarios.

The VaR for a one-day horizon with a confidence level of 99% was CZK -16 million as of 31 December 2016 (2015: CZK -16 million). The average VaR was CZK -16 million in 2016 (2015: CZK -17 million).

The accuracy of the VaR model is validated through a back-testing calculation, whereby actual trading results and hypothetical results (i.e. results excluding deals closed during the day) are compared with the VaR results. Actual results should not exceed VaR more frequently than on 1% of the days within a given period.

In addition, the Bank performs stress tests on a daily basis which capture losses potentially generated by larger shocks. These stress events have a lower probability of occurrence than do VaR scenarios, and they measure potential losses relevant to the risk exposure in the Market Book. Several types of stress tests for foreign exchange, interest rate and $CO_2$ allowance cash and carry exposures are used. These are developed either based on actual crisis situations in the past (such as the Greek crisis in 2010) or from a hypothetical crisis that could negatively influence the performance of the Market Book.

Additional specific metrics such as sensitivities to market parameters or size of exposure are used to obtain a detailed picture of risks and strategies.

The Bank complies with the Société Générale Group's VaR and stress tests methodology and uses Group's software for market risk management.

**Market risk in the Structural Book**

The Bank manages foreign exchange risk so as to minimise risk exposures. In order to achieve this, the foreign exchange position of the Structural Book is measured on a daily basis and subsequently hedged under established rules. For the purpose of hedging foreign exchange positions within the Structural Book, the Bank uses standard currency instruments in the interbank market, such as currency spots and forwards.

Interest rate risk within the Structural Book is monitored and measured using a static gap analysis, sensitivity of interest income to a parallel shift of the yield curve, and Earnings at Risk (hereafter only „EaR") for net interest income. The EaR indicator shows the maximum departure of the planned net interest income level from the initial value that is attributable to the movements in interest rates over a one-year time horizon and at the 99% confidence level.

The indicators are monitored separately for CZK, USD, EUR, and the sum of other foreign currencies.

The indicator of the Bank's sensitivity to a change in market interest rates is measured upon the assumption of an instantaneous, one-off and adverse parallel shift of the market yield curve by 1% p.a. It is determined as the present value of the costs of closing out the Bank's open interest rate position after the adverse change of interest rates occurred. As of 31 December 2016, the CZK interest rate risk sensitivity was CZK -533 million (2015: CZK -507 million), the EUR sensitivity was CZK 71 million (2015: CZK -20 million), the USD sensitivity was CZK 8 million (2015: CZK 15 million), and for other currencies it was CZK -1 million (2015: CZK -70 million) for the hypothetical assumption of a 1% change in market interest rates. The Bank is limited by this indicator, and the level of the limit is determined to be approximately 2% of capital.

In order to hedge against interest rate risk within the Structural Book, the Bank uses both standard derivative instruments available in the interbank market (such as forward rate agreements and interest rate swaps) and appropriate investments into securities or a favourable selection of interest rate parameters for other assets and liabilities.

## (C) Financial derivatives

The Bank operates a system of market risk and counterparty limits which are designed to restrict disproportionate exposures due to movements in market prices and counterparty concentrations. The Bank also monitors adherence to all limits on a daily basis and follows up on any breaches of these limits and takes corrective action to reduce the risk exposure.

The following tables set out nominal and fair values of financial derivative instruments categorised as held for trading and hedging.

*Financial derivative instruments designated as held for trading are as follow:*

| | 31 Dec 2016 Nominal value | | 31 Dec 2015 Nominal value | | 31 Dec 2016 Fair value | | 31 Dec 2015 Fair value | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | Assets | Liabilities | Assets | Liabilities | Positive | Negative | Positive | Negative |
| **Interest rate instruments** | | | | | | | | |
| Interest rate swaps | 686,106 | 686,106 | 618,325 | 618,325 | 9,720 | 10,107 | 9,357 | 10,108 |
| Interest rate forwards and futures* | 2,986 | 2,986 | 23,107 | 23,107 | 1 | 0 | 2 | 2 |
| Interest rate options | 39,957 | 39,957 | 7,532 | 7,532 | 58 | 58 | 33 | 33 |
| **Total interest rate instruments** | **729,049** | **729,049** | **648,964** | **648,964** | **9,779** | **10,165** | **9,392** | **10,143** |
| **Foreign currency instruments** | | | | | | | | |
| Currency swaps | 203,110 | 203,209 | 166,808 | 166,682 | 1,966 | 2,017 | 1,058 | 966 |
| Cross currency swaps | 138,556 | 138,558 | 128,763 | 128,847 | 4,445 | 3,993 | 5,715 | 5,402 |
| Currency forwards | 52,210 | 51,868 | 29,918 | 29,792 | 377 | 295 | 295 | 229 |
| Purchased options | 66,709 | 66,895 | 58,646 | 59,099 | 1,276 | 0 | 984 | 0 |
| Sold options | 66,895 | 66,709 | 59,098 | 58,646 | 0 | 1,276 | 0 | 983 |
| **Total currency instruments** | **527,480** | **527,239** | **443,233** | **443,066** | **8,064** | **7,581** | **8,052** | **7,580** |
| **Other instruments** | | | | | | | | |
| Forwards on emission allowances | 4,194 | 4,052 | 4,570 | 4,978 | 400 | 260 | 68 | 472 |
| Commodity forwards | 4,162 | 4,162 | 2,590 | 2,590 | 148 | 145 | 68 | 66 |
| Commodity swaps | 9,079 | 9,079 | 13,912 | 13,912 | 622 | 605 | 1,588 | 1,570 |
| Purchased commodity options | 424 | 424 | 356 | 356 | 24 | 0 | 49 | 0 |
| Sold commodity options | 424 | 351 | 356 | 356 | 0 | 24 | 0 | 49 |
| **Total other instruments** | **18,283** | **18,068** | **21,784** | **22,192** | **1,194** | **1,034** | **1,773** | **2,157** |
| **Total** | **1,274,812** | **1,274,356** | **1,113,981** | **1,114,222** | **19,037** | **18,780** | **19,217** | **19,880** |

* Fair values include only forwards. Regarding futures, the Bank places funds on a margin account which is used on a daily basis to settle fair value changes. Receivables arising from these margin accounts are reported within other assets.

*Financial derivative instruments designated as held for trading are shown below at nominal values by remaining contractual maturity as of 31 December 2016:*

| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| **Interest rate instruments** | | | | |
| Interest rate swaps | 98,065 | 385,099 | 202,942 | 686,106 |
| Interest rate forwards and futures* | 2,986 | 0 | 0 | 2,986 |
| Interest rate options | 946 | 37,082 | 1,929 | 39,957 |
| **Total interest rate instruments** | **101,997** | **422,181** | **204,871** | **729,049** |
| **Foreign currency instruments** | | | | |
| Currency swaps | 200,604 | 2,506 | 0 | 203,110 |
| Cross currency swaps | 18,271 | 68,486 | 51,799 | 138,556 |
| Currency forwards | 40,275 | 11,935 | 0 | 52,210 |
| Purchased options | 38,442 | 28,267 | 0 | 66,709 |
| Sold options | 38,538 | 28,357 | 0 | 66,895 |
| **Total currency instruments** | **336,130** | **139,551** | **51,799** | **527,480** |
| **Other instruments** | | | | |
| Forwards on emission allowances | 2,281 | 1,913 | 0 | 4,194 |
| Commodity forwards | 4,162 | 0 | 0 | 4,162 |
| Commodity swaps | 7,059 | 2,020 | 0 | 9,079 |
| Purchased commodity options | 402 | 22 | 0 | 424 |
| Sold commodity options | 402 | 22 | 0 | 424 |
| **Total other instruments** | **14,306** | **3,977** | **0** | **18,283** |
| **Total** | **452,433** | **565,709** | **256,670** | **1,274,812** |

* The remaining contractual maturity of forward rate agreements (FRA) and futures covers the period to the fixing date when off-balance sheet exposures are reversed.

*Financial derivative instruments designated as held for trading are shown below at nominal values by remaining contractual maturity as of 31 December 2015:*

| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| **Interest rate instruments** | | | | |
| Interest rate swaps | 118,130 | 318,340 | 181,855 | 618,325 |
| Interest rate forwards and futures* | 23,107 | 0 | 0 | 23,107 |
| Interest rate options | 88 | 6,436 | 1,008 | 7,532 |
| **Total interest rate instruments** | **141,325** | **324,776** | **182,863** | **648,964** |
| **Foreign currency instruments** | | | | |
| Currency swaps | 165,242 | 1,566 | 0 | 166,808 |
| Cross currency swaps | 17,825 | 51,888 | 59,050 | 128,763 |
| Currency forwards | 26,143 | 3,775 | 0 | 29,918 |
| Purchased options | 31,865 | 26,781 | 0 | 58,646 |
| Sold options | 32,366 | 26,732 | 0 | 59,098 |
| **Total currency instruments** | **273,441** | **110,742** | **59,050** | **443,233** |
| **Other instruments** | | | | |
| Forwards on emission allowances | 1,610 | 2,960 | 0 | 4,570 |
| Commodity forwards | 2,590 | 0 | 0 | 2,590 |
| Commodity swaps | 12,090 | 1,822 | 0 | 13,912 |
| Purchased commodity options | 145 | 211 | 0 | 356 |
| Sold commodity options | 145 | 211 | 0 | 356 |
| **Total other instruments** | **16,580** | **5,204** | **0** | **21,784** |
| **Total** | **431,346** | **440,722** | **241,913** | **1,113,981** |

* The remaining contractual maturity of forward rate agreements (FRA) and futures covers the period to the fixing date when off-balance sheet exposures are reversed.

*Financial derivative instruments designated as hedging are as follows:*

| | 31 Dec 2016 Nominal value | | 31 Dec 2015 Nominal value | | 31 Dec 2016 Fair value | | 31 Dec 2015 Fair value | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | Assets | Liabilities | Assets | Liabilities | Positive | Negative | Positive | Negative |
| Interest rate swaps for cash flow hedging | 619,884 | 619,885 | 582,625 | 582,625 | 21,099 | 6,031 | 22,671 | 5,957 |
| Interest rate swaps for fair value hedging | 24,116 | 24,116 | 17,685 | 17,685 | 166 | 2,395 | 106 | 2,094 |
| Cross currency swaps for cash flows hedging | 41,099 | 42,110 | 37,826 | 39,864 | 348 | 946 | 280 | 1,951 |
| Forwards on stocks for cash flow hedging | 49 | 49 | 49 | 49 | 1 | 1 | 9 | 0 |
| **Total** | **685,148** | **686,160** | **638,185** | **640,223** | **21,614** | **9,373** | **23,066** | **10,002** |

*Remaining contractual maturities of derivatives designated as hedging are shown below as of 31 December 2016:*

| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| Interest rate swaps for cash flow hedging | 104,258 | 297,424 | 218,202 | 619,884 |
| Interest rate swaps for fair value hedging | 0 | 6,289 | 17,827 | 24,116 |
| Cross currency swaps for cash flow hedging | 8,235 | 31,631 | 1,233 | 41,099 |
| Forwards on stocks for cash flow hedging | 19 | 30 | 0 | 49 |
| **Total** | **112,512** | **335,374** | **237,262** | **685,148** |

*Remaining contractual maturities of derivatives designated as hedging are shown below as of 31 December 2015:*

| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Total |
|---|---|---|---|---|
| Interest rate swaps for cash flow hedging | 103,896 | 271,687 | 207,042 | 582,625 |
| Interest rate swaps for fair value hedging | 0 | 300 | 17,385 | 17,685 |
| Cross currency swaps for cash flow hedging | 13,276 | 23,317 | 1,233 | 37,826 |
| Forwards on stocks for cash flow hedging | 21 | 28 | 0 | 49 |
| **Total** | **117,193** | **295,332** | **225,660** | **638,185** |

*Shown below are the undiscounted cash flows from derivatives designated for cash flow hedging according to the periods within which they are expected to affect profit or loss:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| (CZKm) | Up to 1 year | 1 to 5 years | Over 5 years | Up to 1 year | 1 to 5 years | Over 5 years |
| Floating cash flows from cash flow hedging derivatives | (284) | (1,440) | (1,221) | (210) | (1,225) | (1,227) |

The Bank treats as hedges only those contracts for which it is able to demonstrate that all criteria set out in IAS 39 for recognising the transactions as hedges have been met.

*During 2016, the Bank recorded the following hedges:*

1. Interest rate risk hedging:
   a. The fair values of long-term loans provided and of investments into long-term government securities classified into the ***'Available-for-sale financial assets'*** portfolio and investments into long-term securities classified into the ***'Loans and advances to customers'*** portfolio are hedged by interest rate swaps and cross currency swaps, respectively;
   b. The fair values of issued long-term mortgage bonds classified into the ***'Securities issued'*** portfolio are hedged by interest rate swaps;
   c. The fair values of fixed rate deposits or repos are hedged by interest rate swaps;
   d. Future cash flows from a portfolio of current assets traded on the interbank market and from loans to clients with variable interest rates are hedged by a portfolio of interest rate swaps or cross currency swaps (cash flows will materialise on an ongoing basis and will also affect the Bank's Statement of Income on an ongoing basis);
   e. Future cash flows from a portfolio of short-term liabilities traded on the interbank market and short term liabilities to clients are hedged by a portfolio of interest rate swaps (cash flows will materialise on an ongoing basis and will also affect the Bank's Statement of Income on an ongoing basis).

2. Foreign exchange risk hedging:
   a. In selected material cases, the Bank hedges the future cash flows of firm commitments arising from the Bank's contractual obligations (e.g. contractual payments to third parties in a foreign currency) or receivables of the Bank (e.g. dividends). The hedging instrument consists of foreign currency assets (e.g. securities, short-term loans on the interbank market) or foreign currency liabilities (e.g. short-term client liabilities), respectively;
   b. Visa shares transactions – hedging of future cash flows from selling of the Visa Europe stake for cash payment, hedging instruments were foreign currency liabilities (short-term client liabilities), the hedge relationship ended correctly in 2016. Hedging the fair value of newly issued Visa Inc. preferred shares, hedging instruments are foreign currency liabilities (short-term client liabilities).

3. Share price risk hedging:
   a. A portion of the bonus of selected Bank employees is paid in cash equivalents of the Société Générale S.A. share price. The risk of change in the Société Générale S.A. share price is hedged at the Société Générale level. Hedging instruments are forwards on stocks. The hedge relationship ended correctly in 2016;
   b. A portion of the bonus of selected Bank employees is paid in cash equivalents of the Komerční banka, a.s. share price. The Bank hedges the risk of change in the Komerční banka, a.s. share price. Hedging instruments are forwards on stocks.

4. Hedging of an investment in foreign subsidiaries:
   a. The foreign exchange risk associated with investments in subsidiaries is hedged by selected foreign currency liabilities (e.g. short-term client liabilities).

The Bank does not report any instance of hedge accounting being applied to a highly probable forecasted transaction that is no longer anticipated to be effected.

Further information on hedges is provided in Notes 3, 5 and 7 to these Financial Statements.

### (D) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The length of time for which the rate of interest is fixed on a financial instrument therefore indicates to what extent that instrument is exposed to interest rate risk. Market developments have led to a situation where interest rates are negative in certain currencies. This fact does not change the essence of interest rate risk measurement and management because the principle of recognising changes in interest rates over time remains unchanged just as the concept of hedging against interest rate risk by matching volumes with changing values within the given period remains valid. Due to legal and technical limitations, methods to prevent negative rates from being applied at the client's level can be applied with the objective of maintaining accordance between a transaction's contractual and economic natures. With respect to ongoing market practice, client deposits are seeing the introduction of deposit fees, which constitute a specific response to the existence of negative market interest rates and which also comply with the requirements given by limitations ensuing from the existing legal framework.

The Bank uses internal models for managing interest rate risk. The objective of these models is to describe the expected economic behaviour of the Bank's clients when market interest rates fluctuate. It is the policy of the Bank's management to manage the exposure to fluctuations in net interest income arising from changes in interest rates through a gap analysis of assets and liabilities in individual groups. Further information about interest rate risk management is provided in Section (B) of this Note.

The table below provides information on the extent of the Bank's interest rate exposure based either on the contractual maturity date of its financial instruments or, in the case of instruments that reprice to a market rate of interest before maturity, the next repricing date. Those assets and liabilities that do not have a contractual maturity or a repricing date were grouped into the *'Undefined'* category. The table includes an analysis of other assets and liabilities not within the scope of financial instruments as defined in IAS 32.

| (CZKm) | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Undefined | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and current balances with central banks | 103,993 | 0 | 0 | 0 | 0 | **103,993** |
| Financial assets at fair value through profit or loss | 11,445 | 0 | 0 | 0 | 19,037 | **30,482** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 21,614 | **21,614** |
| Available-for-sale financial assets | 304 | 9,472 | 3,626 | 18,009 | 0 | **31,411** |
| Assets held for sale | 0 | 0 | 0 | 0 | 587 | **587** |
| Amounts due from banks | 49,426 | 4,751 | 2,069 | 1,737 | 0 | **57,983** |
| Loans and advances to customers | 232,583 | 67,673 | 191,376 | 35,511 | 0 | **527,143** |
| Held-to-maturity investments | 0 | 3,564 | 28,367 | 30,494 | 0 | **62,425** |
| Current tax assets | 0 | 0 | 0 | 0 | 0 | **0** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 31 | **31** |
| Prepayments, accrued income and other assets | 0 | 0 | 0 | 0 | 3,012 | **3,012** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 21,292 | **21,292** |
| Intangible assets | 0 | 0 | 0 | 0 | 3,428 | **3,428** |
| Tangible assets | 0 | 0 | 0 | 0 | 4,664 | **4,664** |
| **Total assets** | **397,751** | **85,460** | **225,438** | **85,751** | **73,665** | **868,065** |
| **Liabilities** | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities through profit or loss | 160 | 0 | 0 | 0 | 18,780 | **18,940** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 9,373 | **9,373** |
| Amounts due to banks | 35,104 | 8,178 | 0 | 0 | 0 | **43,282** |
| Amounts due to customers | 24,000 | 13,646 | 288 | 0 | 600,476* | **638,410** |
| Securities issued | 1,968 | 9,367 | 17,640 | 16,780 | 0 | **45,755** |
| Current tax liabilities | 0 | 0 | 0 | 0 | 357 | **357** |
| Deferred tax liabilities | 0 | 0 | 0 | 0 | 3,065 | **3,065** |
| Accruals and other liabilities | 0 | 0 | 0 | 0 | 14,149 | **14,149** |
| Provisions | 0 | 0 | 0 | 0 | 1,701 | **1,701** |
| **Total liabilities** | **61,233** | **31,191** | **17,928** | **16,780** | **647,901** | **775,033** |
| **Statement of Financial Position interest rate gap as of 31 December 2016** | **336,518** | **54,269** | **207,510** | **68,971** | **(574,236)** | **93,032** |
| Nominal value of derivatives** | 575,690 | 271,474 | 380,241 | 325,299 | 0 | **1,552,704** |
| **Total off-balance sheet assets** | **575,690** | **271,474** | **380,241** | **325,299** | **0** | **1,552,704** |
| Nominal value of derivatives** | 692,176 | 264,161 | 407,575 | 189,806 | 0 | **1,553,718** |
| Undrawn portion of loans*** | (8,624) | (8,483) | 9,291 | 7,816 | 0 | **0** |
| Undrawn portion of revolving loans*** | (578) | 578 | 0 | 0 | 0 | **0** |
| **Total off-balance sheet liabilities** | **682,974** | **256,256** | **416,866** | **197,622** | **0** | **1,553,718** |
| **Net off-balance sheet interest rate gap as of 31 December 2016** | **(107,284)** | **15,218** | **(36,625)** | **127,677** | **0** | **(1,014)** |
| **Cumulative interest rate gap as of 31 December 2016** | **229,234** | **298,721** | **469,606** | **666,254** | **92,018** | **x** |

* This item principally includes client deposits where the Bank has the option to reset interest rates and hence they are not sensitive to interest rate changes.
** Assets and liabilities arising from derivatives include interest rate swaps, interest rate forwards and futures, interest rate options and cross currency swaps.
*** Undrawn loans and revolving loans are reported on a net basis, that is, the Bank reports both the expected drawings and repayments within one line. This line does not reflect commitments to extend loans with a fixed repayment schedule or commitments to provide a revolving loan inasmuch as the interest rate has not been determined for such commitments.

| (CZKm) | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Undefined | Total |
|---|---|---|---|---|---|---|
| **Assets** | | | | | | |
| Cash and current balances with central banks | 116,257 | 0 | 0 | 0 | 0 | **116,257** |
| Financial assets at fair value through profit or loss | 7,186 | 3,487 | 0 | 0 | 19,216 | **29,889** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 23,066 | **23,066** |
| Available-for-sale financial assets | 3,378 | 8,234 | 9,026 | 12,062 | 0 | **32,700** |
| Assets held for sale | 0 | 0 | 0 | 0 | 360 | **360** |
| Amounts due from banks | 46,015 | 2,025 | 4,217 | 2,332 | 0 | **54,589** |
| Loans and advances to customers | 209,678 | 69,282 | 182,999 | 22,515 | 0 | **484,474** |
| Held-to-maturity investments | 2,961 | 0 | 19,566 | 38,476 | 0 | **61,003** |
| Current tax assets | 0 | 0 | 0 | 0 | 303 | **303** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 33 | **33** |
| Prepayments, accrued income and other assets | 0 | 0 | 0 | 0 | 2,804 | **2,804** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 22,177 | **22,177** |
| Intangible assets | 0 | 0 | 0 | 0 | 3,427 | **3,427** |
| Tangible assets | 0 | 0 | 0 | 0 | 4,444 | **4,444** |
| **Total assets** | **385,475** | **83,028** | **215,808** | **75,385** | **75,830** | **835,526** |
| **Liabilities** | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities through profit or loss | 305 | 0 | 0 | 0 | 19,880 | **20,185** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 10,002 | **10,002** |
| Amounts due to banks | 40,019 | 6,060 | 0 | 0 | 0 | **46,079** |
| Amounts due to customers | 30,029 | 9,535 | 1,106 | 0 | 552,389* | **593,059** |
| Securities issued | 6,695 | 4,015 | 23,243 | 20,345 | 0 | **54,298** |
| Current tax liabilities | 0 | 0 | 0 | 0 | 0 | **0** |
| Deferred tax liabilities | 0 | 0 | 0 | 0 | 3,886 | **3,886** |
| Accruals and other liabilities | 0 | 0 | 0 | 0 | 13,564 | **13,564** |
| Provisions | 0 | 0 | 0 | 0 | 1,149 | **1,149** |
| **Total liabilities** | **77,049** | **19,610** | **24,349** | **20,345** | **600,870** | **742,223** |
| **Statement of Financial Position interest rate gap as of 31 December 2015** | **308,426** | **63,418** | **191,459** | **55,040** | **(525,040)** | **93,303** |
| Nominal value of derivatives** | 512,361 | 291,707 | 304,795 | 307,000 | 0 | **1,415,863** |
| **Total off-balance sheet assets** | **512,361** | **291,707** | **304,795** | **307,000** | **0** | **1,415,863** |
| Nominal value of derivatives** | 611,989 | 268,676 | 345,984 | 191,336 | 0 | **1,417,985** |
| Undrawn portion of loans*** | (5,622) | (5,281) | 7,774 | 3,129 | 0 | **0** |
| Undrawn portion of revolving loans*** | 0 | 0 | 0 | 0 | 0 | **0** |
| **Total off-balance sheet liabilities** | **606,367** | **263,395** | **353,758** | **194,465** | **0** | **1,417,985** |
| **Net off-balance sheet interest rate gap as of 31 December 2015** | **(94,006)** | **28,312** | **(48,963)** | **112,535** | **0** | **(2,122)** |
| **Cumulative interest rate gap as of 31 December 2015** | **214,420** | **306,150** | **448,646** | **616,221** | **91,181** | **x** |

* This item principally includes client deposits where the Bank has the option to reset interest rates and hence they are not sensitive to interest rate changes.
** Assets and liabilities arising from derivatives include interest rate swaps, interest rate forwards and futures, interest rate options and cross currency swaps.
*** Undrawn loans and revolving loans are reported on a net basis, that is, the Bank reports both the expected drawings and repayments within one line. This line does not reflect commitments to extend loans with a fixed repayment schedule or commitments to provide a revolving loan inasmuch as the interest rate has not been determined for such commitments.

*Average interest rates as of 31 December 2016 and 2015 were as follows:*

| | 31 Dec 2016 | | | 31 Dec 2015 | | |
|---|---|---|---|---|---|---|
| | CZK | USD | EUR | CZK | USD | EUR |
| **Assets** | | | | | | |
| Cash and current balances with central banks | 0.05% | x | x | 0.04% | x | x |
| Treasury bills | 0.00% | x | x | 0.01% | x | x |
| Amounts due from banks | 0.08% | 1.27% | 0.14% | 0.06% | 0.92% | 0.39% |
| Loans and advances to customers | 2.30% | 2.80% | 1.66% | 2.53% | 2.39% | 1.87% |
| Interest-earning securities | 1.63% | 0.00% | 1.34% | 1.39% | 0.00% | 1.48% |
| **Total assets** | **1.33%** | **1.36%** | **1.14%** | **1.55%** | **1.40%** | **1.37%** |
| **Total interest-earning assets** | **1.76%** | **1.85%** | **1.18%** | **1.80%** | **1.70%** | **1.40%** |
| **Liabilities** | | | | | | |
| Amounts due to central banks and banks | 0.07% | 0.73% | 0.40% | 0.04% | 0.86% | 0.43% |
| Amounts due to customers | 0.02% | 0.03% | 0.02% | 0.04% | 0.02% | 0.05% |
| Debt securities | 3.06% | 0.97% | 0.16% | 3.72% | 1.27% | 0.42% |
| **Total liabilities** | **0.16%** | **0.08%** | **0.16%** | **0.25%** | **0.15%** | **0.17%** |
| **Total interest-bearing liabilities** | **0.17%** | **0.09%** | **0.17%** | **0.26%** | **0.16%** | **0.19%** |
| **Off-balance sheet assets** | | | | | | |
| Nominal value of derivatives (interest rate swaps, options, etc.) | 0.95% | 2.64% | 0.71% | 1.09% | 2.62% | 1.03% |
| Undrawn portion of loans | 1.55% | 0.00% | 1.75% | 1.90% | 2.25% | 1.48% |
| Undrawn portion of revolving loans | 4.90% | 1.29% | 0.29% | 5.62% | x | 0.29% |
| **Total off-balance sheet assets** | **1.18%** | **2.62%** | **0.71%** | **1.32%** | **2.60%** | **1.02%** |
| **Off-balance sheet liabilities** | | | | | | |
| Nominal value of derivatives (interest rate swaps, options, etc.) | 0.71% | 2.32% | 0.63% | 0.79% | 2.23% | 1.04% |
| Undrawn portion of loans | 1.55% | 0.00% | 1.75% | 1.90% | 2.25% | 1.48% |
| Undrawn portion of revolving loans | 4.90% | 1.29% | 0.29% | 5.62% | x | 0.29% |
| **Total off-balance sheet liabilities** | **0.96%** | **2.31%** | **0.63%** | **1.04%** | **2.21%** | **1.03%** |

Note: he above table sets out the average interest rates for December 2016 and 2015 calculated as a weighted average for each asset and liability category.

The 2W repo rate announced by the CNB remained at the level of 0.05% throughout 2016. Czech crown money market rates (PRIBOR) decreased by as much as 0.03% (1–12M). Interest rates in the derivatives market decreased by 0.10–0.17% (2–10Y).

Euro money market rates decreased during 2016 by as much as 0.14% (3–6M) and 0.19% (1Y). Derivative market rates decreased by as much as 0.12% (2Y) and 0.29% (10Y).

Dollar money market rates increased during 2016 by as much as 0.52% (12M), and derivative market rates increased by as much as 0.22% (10Y) and 0.33% (2Y).

*Following is a breakdown of financial assets and liabilities by their exposure to interest rate fluctuations:*

| | 31 Dec 2016 | | | | 31 Dec 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | Fixed interest rate | Floating interest rate | No interest | Total | Fixed interest rate | Floating interest rate | No interest | Total |
| **Assets** | | | | | | | | |
| Cash and current balances with central banks | 0 | 93,292 | 10,701 | **103,993** | 13,800 | 89,122 | 13,335 | **116,257** |
| Financial assets at fair value through profit or loss | 7,466 | 2,140 | 20,876 | **30,482** | 6,846 | 1,026 | 22,017 | **29,889** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 21,614 | **21,614** | 0 | 0 | 23,066 | **23,066** |
| Available-for-sale financial assets | 17,568 | 13,661 | 182 | **31,411** | 17,931 | 14,094 | 675 | **32,700** |
| Amounts due from banks | 8,299 | 49,550 | 134 | **57,983** | 6,644 | 47,904 | 41 | **54,589** |
| Loans and advances to customers | 316,162 | 206,221 | 4,760 | **527,143** | 294,570 | 185,472 | 4,432 | **484,474** |
| Held-to-maturity investments | 62,425 | 0 | 0 | **62,425** | 61,003 | 0 | 0 | **61,003** |
| **Liabilities** | | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | **1** | 1 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 0 | 0 | 18,940 | **18,940** | 0 | 0 | 20,185 | **20,185** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 9,373 | **9,373** | 0 | 0 | 10,002 | **10,002** |
| Amounts due to banks | 16,055 | 26,292 | 935 | **43,282** | 7,522 | 38,371 | 186 | **46,079** |
| Amounts due to customers | 105 | 631,768* | 6,537 | **638,410** | 202 | 585,664* | 7,193 | **593,059** |
| Securities issued | 15,922 | 29,833 | 0 | **45,755** | 13,631 | 40,649 | 18 | **54,298** |

Note: Individual assets and liabilities are split into the categories of 'Fixed interest rate', 'Floating interest rate', and 'No interest' according to contractual parameters defining the interest rate structure. For this purpose, a fixed interest rate is defined as a rate with a repricing period exceeding one year. Products having no parameters defining their interest rate structure are included in the 'No interest' category.

* This item principally includes client deposits where the Bank has the option to reset interest rates and hence they are not sensitive to interest rate changes.

## (E) Liquidity risk

Liquidity risk is a measure of the extent to which the Bank may be required to raise funds to meet its commitments associated with financial instruments.

Liquidity risk management is based upon the liquidity risk management system approved by the Bank's Board of Directors. Liquidity is monitored on a bank-wide level, with the Market Book also having a standalone limit. The Bank has established its liquidity risk management rules such that it maintains its liquidity profile in normal conditions (basic liquidity scenario) and in crisis conditions (crisis liquidity scenario). As such, the Bank has defined a set of indicators for which binding limits are established.

The Bank is exposed to daily calls on its available cash resources from derivatives, overnight deposits, current accounts, maturing deposits, loan draw-downs and guarantees. The Bank's experiences show that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty. The Bank sets limits on the minimum proportion of maturing funds available to meet such calls and on the minimum level of interbank and other borrowing facilities (mainly reverse repo transactions with CNB) that should be in place to cover withdrawals at unexpected levels of demand.

The liquidity risk of the Bank is managed as stipulated above (and in particular not on the basis of undiscounted cash flows).

The table below provides a breakdown of assets, liabilities and equity into relevant maturity groupings based on the remaining period from the financial statements date to the contractual maturity date. The table includes an analysis of other assets and liabilities not within the scope of financial instruments as defined in IAS 32.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and current balances with central banks | 9,255 | 0 | 0 | 0 | 0 | 94,738 | **103,993** |
| Financial assets at fair value through profit or loss | 700 | 594 | 1,395 | 4,623 | 2,293 | 20,877 | **30,482** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 21,614 | **21,614** |
| Available-for-sale financial assets | 0 | 20 | 4,575 | 3,546 | 20,696 | 2,574 | **31,411** |
| Assets held for sale | 0 | 0 | 587 | 0 | 0 | 0 | **587** |
| Amounts due from banks | 19,759 | 22,211 | 3,150 | 6,824 | 59 | 5,980 | **57,983** |
| Loans and advances to customers | 4,929 | 59,123 | 50,606 | 159,923 | 238,011 | 14,551 | **527,143** |
| Held-to-maturity investments | 0 | 353 | 4,231 | 27,843 | 29,998 | 0 | **62,425** |
| Current tax assets | 0 | 0 | 0 | 0 | 0 | 0 | **0** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 0 | 31 | **31** |
| Prepayments, accrued income and other assets | 120 | 2 | 0 | 0 | 0 | 2,890 | **3,012** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 0 | 21,292 | **21,292** |
| Intangible assets | 0 | 0 | 0 | 0 | 0 | 3,428 | **3,428** |
| Tangible assets | 0 | 0 | 0 | 0 | 0 | 4,664 | **4,664** |
| **Total assets** | **34,763** | **82,303** | **64,544** | **202,759** | **291,057** | **192,639** | **868,065** |
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 160 | 0 | 0 | 0 | 0 | 18,780 | **18,940** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 9,373 | **9,373** |
| Amounts due to banks | 12,721 | 5,890 | 2,164 | 12,980 | 9,527 | 0 | **43,282** |
| Amounts due to customers | 609,341 | 13,522 | 14,054 | 1,493 | 0 | 0 | **638,410** |
| Securities issued | 279 | 1,706 | 952 | 4,769 | 37,917 | 132 | **45,755** |
| Current tax liabilities | 0 | 357 | 0 | 0 | 0 | 0 | **357** |
| Deferred tax liabilities | 0 | 0 | 0 | 0 | 0 | 3,065 | **3,065** |
| Accruals and other liabilities | 13,735 | 12 | 0 | 0 | 0 | 402 | **14,149** |
| Provisions | 11 | 171 | 762 | 269 | 4 | 484 | **1,701** |
| Equity | 0 | 0 | 0 | 0 | 0 | 93,032 | **93,032** |
| **Total liabilities** | **636,248** | **21,658** | **17,932** | **19,511** | **47,448** | **125,268** | **868,065** |
| **Statement of Financial Position liquidity gap as of 31 Dec 2016** | **(601,485)** | **60,645** | **46,612** | **183,248** | **243,609** | **67,371** | **0** |
| Off-balance sheet assets* | 50,043 | 178,351 | 131,053 | 171,181 | 53,033 | 0 | **583,661** |
| Off-balance sheet liabilities* | 53,277 | 199,484 | 186,686 | 216,614 | 57,647 | 13,555 | **727,263** |
| **Net off-balance sheet liquidity gap as of 31 Dec 2016** | **(3,234)** | **(21,133)** | **(55,633)** | **(45,433)** | **(4,614)** | **(13,555)** | **(143,602)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from FX spot, fixed term and option contracts and payables under guarantees, letters of credit and committed facilities.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Assets** | | | | | | | |
| Cash and current balances with central banks | 26,189 | 0 | 0 | 0 | 0 | 90,068 | **116,257** |
| Financial assets at fair value through profit or loss | 0 | 1,570 | 2,377 | 2,730 | 1,195 | 22,017 | **29,889** |
| Positive fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 23,066 | **23,066** |
| Available-for-sale financial assets | 0 | 1,516 | 326 | 7,503 | 20,208 | 3,147 | **32,700** |
| Assets held for sale | 0 | 0 | 360 | 0 | 0 | 0 | **360** |
| Amounts due from banks | 14,143 | 23,689 | 2,077 | 7,404 | 832 | 6,444 | **54,589** |
| Loans and advances to customers | 4,367 | 51,461 | 56,993 | 143,082 | 213,189 | 15,382 | **484,474** |
| Held-to-maturity investments | 0 | 3,078 | 1,040 | 19,083 | 37,802 | 0 | **61,003** |
| Current tax assets | 0 | 28 | 275 | 0 | 0 | 0 | **303** |
| Deferred tax assets | 0 | 0 | 0 | 0 | 0 | 33 | **33** |
| Prepayments, accrued income and other assets | 389 | 1 | 0 | 0 | 0 | 2,414 | **2,804** |
| Investments in subsidiaries and associates | 0 | 0 | 0 | 0 | 0 | 22,177 | **22,177** |
| Intangible assets | 0 | 0 | 0 | 0 | 0 | 3,427 | **3,427** |
| Tangible assets | 0 | 0 | 0 | 0 | 0 | 4,444 | **4,444** |
| **Total assets** | **45,088** | **81,343** | **63,448** | **179,802** | **273,226** | **192,619** | **835,526** |
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 305 | 0 | 0 | 0 | 0 | 19,880 | **20,185** |
| Negative fair values of hedging financial derivatives | 0 | 0 | 0 | 0 | 0 | 10,002 | **10,002** |
| Amounts due to banks | 23,127 | 4,086 | 5,189 | 6,630 | 7,047 | 0 | **46,079** |
| Amounts due to customers | 568,847 | 12,868 | 9,583 | 1,761 | 0 | 0 | **593,059** |
| Securities issued | 8 | 6,376 | 4,612 | 5,060 | 38,200 | 42 | **54,298** |
| Current tax liabilities | 0 | 0 | 0 | 0 | 0 | 0 | **0** |
| Deferred tax liabilities | 0 | 0 | 0 | 0 | 0 | 3,886 | **3,886** |
| Accruals and other liabilities | 12,942 | 229 | 0 | 0 | 0 | 393 | **13,564** |
| Provisions | 8 | 110 | 269 | 355 | 1 | 406 | **1,149** |
| Equity | 0 | 0 | 0 | 0 | 0 | 93,303 | **93,303** |
| **Total liabilities** | **605,238** | **23,669** | **19,653** | **13,806** | **45,248** | **127,912** | **835,526** |
| **Statement of Financial Position liquidity gap as of 31 Dec 2015** | **(560,150)** | **57,674** | **43,795** | **165,996** | **227,978** | **64,707** | **0** |
| Off-balance sheet assets* | 49,522 | 151,449 | 88,241 | 134,060 | 60,284 | 0 | **483,556** |
| Off-balance sheet liabilities* | 53,529 | 174,050 | 139,279 | 172,258 | 64,505 | 13,132 | **616,753** |
| **Net off-balance sheet liquidity gap as of 31 Dec 2015** | **(4,007)** | **(22,601)** | **(51,038)** | **(38,198)** | **(4,221)** | **(13,132)** | **(133,197)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from FX spot, fixed term and option contracts and payables under guarantees, letters of credit and committed facilities.

The table below contains the remaining contractual maturities of non-derivative financial liabilities and contingent liabilities of the Bank based on the undiscounted cash flows as of 31 December 2016.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss (except derivatives) | 160 | 0 | 0 | 0 | 0 | 0 | **160** |
| Amounts due to banks | 12,721 | 5,890 | 2,166 | 13,027 | 9,862 | 0 | **43,666** |
| Amounts due to customers | 609,345 | 13,532 | 14,107 | 1,516 | 0 | 0 | **638,500** |
| Securities issued | 295 | 1,857 | 2,279 | 7,889 | 39,020 | 132 | **51,472** |
| Current tax liabilities | 0 | 357 | 0 | 0 | 0 | 0 | **357** |
| Deferred tax liabilities | 0 | 0 | 0 | 0 | 0 | 3,065 | **3,065** |
| Accruals and other liabilities | 13,735 | 12 | 0 | 0 | 0 | 402 | **14,149** |
| Provisions | 11 | 171 | 762 | 269 | 4 | 484 | **1,701** |
| **Total non-derivative financial liabilities** | **636,268** | **21,819** | **19,314** | **22,701** | **48,886** | **4,083** | **753,071** |
| Other loans commitment granted | 1,641 | 13,976 | 35,850 | 24,770 | 1,342 | 13,477 | **91,056** |
| Guarantee commitments granted | 1,135 | 7,185 | 19,509 | 20,120 | 3,300 | 78 | **51,327** |
| **Total contingent liabilities** | **2,776** | **21,161** | **55,359** | **44,890** | **4,642** | **13,555** | **142,383** |

The table below contains the remaining contractual maturities of non-derivative financial liabilities and contingent liabilities of the Bank based on the undiscounted cash flows as of 31 December 2015.

| (CZKm) | On demand up to 7 days | Up to 3 months | 3 months to 1 year | 1 year to 5 years | Over 5 years | Maturity undefined | Total |
|---|---|---|---|---|---|---|---|
| **Liabilities** | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss (except derivatives) | 305 | 0 | 0 | 0 | 0 | 0 | **305** |
| Amounts due to banks | 23,175 | 4,088 | 5,201 | 6,692 | 7,057 | 0 | **46,213** |
| Amounts due to customers | 568,927 | 13,034 | 9,656 | 2,110 | 0 | 0 | **593,727** |
| Securities issued | 350 | 6,547 | 5,376 | 8,978 | 39,786 | 42 | **61,079** |
| Current tax liabilities | 0 | 0 | 0 | 0 | 0 | 0 | **0** |
| Deferred tax liabilities | 0 | 0 | 0 | 0 | 0 | 3,886 | **3,886** |
| Accruals and other liabilities | 12,942 | 229 | 0 | 0 | 0 | 393 | **13,564** |
| Provisions | 8 | 110 | 269 | 355 | 1 | 406 | **1,149** |
| **Total non-derivative financial liabilities** | **605,708** | **24,008** | **20,502** | **18,135** | **46,844** | **4,727** | **719,924** |
| Other loans commitment granted | 2,486 | 14,817 | 32,125 | 18,729 | 1,649 | 13,071 | **82,877** |
| Guarantee commitments granted | 1,556 | 7,866 | 17,753 | 18,573 | 2,636 | 61 | **48,445** |
| **Total contingent liabilities** | **4,042** | **22,683** | **49,878** | **37,302** | **4,285** | **13,132** | **131,322** |

## (F) Foreign exchange position

The table below provides an analysis of the Bank's main currency exposures. The remaining currencies are shown within *'Other currencies'*. The Bank manages its foreign exchange position on a daily basis. For this purpose, the Bank has a set of internal limits.

| (CZKm) | CZK | EUR | USD | Other currencies | Total |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash and current balances with central banks | 102,103 | 1,250 | 325 | 315 | **103,993** |
| Financial assets at fair value through profit or loss | 24,657 | 5,505 | 314 | 6 | **30,482** |
| Positive fair values of hedging financial derivatives | 19,030 | 2,333 | 251 | 0 | **21,614** |
| Available-for-sale financial assets | 23,614 | 7,620 | 177 | 0 | **31,411** |
| Assets held for sale | 587 | 0 | 0 | 0 | **587** |
| Amounts due from banks | 24,957 | 22,585 | 9,988 | 453 | **57,983** |
| Loans and advances to customers | 420,020 | 100,319 | 5,974 | 830 | **527,143** |
| Held-to-maturity investments | 48,356 | 14,069 | 0 | 0 | **62,425** |
| Current tax assets | 0 | 0 | 0 | 0 | **0** |
| Deferred tax assets | 0 | 31 | 0 | 0 | **31** |
| Prepayments, accrued income and other assets | 2,532 | 405 | 74 | 1 | **3,012** |
| Investments in subsidiaries and associates | 18,169 | 3,123 | 0 | 0 | **21,292** |
| Intangible assets | 3,425 | 3 | 0 | 0 | **3,428** |
| Tangible assets | 4,662 | 2 | 0 | 0 | **4,664** |
| **Total assets** | **692,112** | **157,245** | **17,103** | **1,605** | **868,065** |
| **Liabilities** | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 15,715 | 2,961 | 258 | 6 | **18,940** |
| Negative fair values of hedging financial derivatives | 7,072 | 2,219 | 82 | 0 | **9,373** |
| Amounts due to banks | 4,003 | 38,151 | 1,072 | 56 | **43,282** |
| Amounts due to customers | 549,835 | 73,744 | 12,228 | 2,603 | **638,410** |
| Securities issued | 45,482 | 19 | 38 | 216 | **45,755** |
| Current tax liabilities | 353 | 4 | 0 | 0 | **357** |
| Deferred tax liabilities | 3,065 | 0 | 0 | 0 | **3,065** |
| Accruals and other liabilities | 11,594 | 1,927 | 492 | 136 | **14,149** |
| Provisions | 1,271 | 327 | 59 | 44 | **1,701** |
| Equity | 92,704 | 328 | 0 | 0 | **93,032** |
| **Total liabilities** | **731,095** | **119,680** | **14,229** | **3,061** | **868,065** |
| **Net FX position as of 31 December 2016** | **(38,983)** | **37,565** | **2,874** | **(1,456)** | **0** |
| Off-balance sheet assets* | 1,306,650 | 504,567 | 147,940 | 16,001 | **1,975,158** |
| Off-balance sheet liabilities* | 1,271,354 | 539,060 | 150,152 | 14,682 | **1,975,248** |
| **Net off-balance sheet FX position as of 31 December 2016** | **35,296** | **(34,493)** | **(2,212)** | **1,319** | **(90)** |
| **Total net FX position as of 31 December 2016** | **(3,687)** | **3,072** | **662** | **(137)** | **(90)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from spot transactions and nominal value of all derivative deals.

| (CZKm) | CZK | EUR | USD | Other currencies | Total |
|---|---|---|---|---|---|
| **Assets** | | | | | |
| Cash and current balances with central banks | 114,002 | 1,764 | 237 | 254 | **116,257** |
| Financial assets at fair value through profit or loss | 21,169 | 8,237 | 482 | 1 | **29,889** |
| Positive fair values of hedging financial derivatives | 20,614 | 2,081 | 371 | 0 | **23,066** |
| Available-for-sale financial assets | 24,452 | 8,246 | 2 | 0 | **32,700** |
| Assets held for sale | 360 | 0 | 0 | 0 | **360** |
| Amounts due from banks | 28,183 | 21,369 | 4,885 | 152 | **54,589** |
| Loans and advances to customers | 392,888 | 84,054 | 6,774 | 758 | **484,474** |
| Held-to-maturity investments | 47,185 | 13,818 | 0 | 0 | **61,003** |
| Current tax assets | 275 | 28 | 0 | 0 | **303** |
| Deferred tax assets | 0 | 33 | 0 | 0 | **33** |
| Prepayments, accrued income and other assets | 2,237 | 224 | 328 | 15 | **2,804** |
| Investments in subsidiaries and associates | 18,954 | 3,223 | 0 | 0 | **22,177** |
| Intangible assets | 3,427 | 0 | 0 | 0 | **3,427** |
| Tangible assets | 4,440 | 4 | 0 | 0 | **4,444** |
| **Total assets** | **678,186** | **143,081** | **13,079** | **1,180** | **835,526** |
| **Liabilities** | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 0 | **1** |
| Financial liabilities at fair value through profit or loss | 16,343 | 3,399 | 443 | 0 | **20,185** |
| Negative fair values of hedging financial derivatives | 7,947 | 2,044 | 11 | 0 | **10,002** |
| Amounts due to banks | 14,708 | 29,634 | 1,704 | 33 | **46,079** |
| Amounts due to customers | 511,558 | 67,823 | 11,414 | 2,264 | **593,059** |
| Securities issued | 52,734 | 990 | 313 | 261 | **54,298** |
| Current tax liabilities | 0 | 0 | 0 | 0 | **0** |
| Deferred tax liabilities | 3,886 | 0 | 0 | 0 | **3,886** |
| Accruals and other liabilities | 11,212 | 1,937 | 308 | 107 | **13,564** |
| Provisions | 713 | 391 | 33 | 12 | **1,149** |
| Equity | 92,841 | 462 | 0 | 0 | **93,303** |
| **Total liabilities** | **711,943** | **106,680** | **14,226** | **2,677** | **835,526** |
| **Net FX position as of 31 December 2015** | **(33,757)** | **36,401** | **(1,147)** | **(1,497)** | **0** |
| Off-balance sheet assets* | 1,240,816 | 376,874 | 120,140 | 17,797 | **1,755,627** |
| Off-balance sheet liabilities* | 1,213,012 | 410,133 | 118,403 | 16,353 | **1,757,901** |
| **Net off-balance sheet FX position as of 31 December 2015** | **27,804** | **(33,259)** | **1,737** | **1,444** | **(2,274)** |
| **Total net FX position as of 31 December 2015** | **(5,953)** | **3,142** | **590** | **(53)** | **(2,274)** |

* Off-balance sheet assets and liabilities include amounts receivable and payable arising from spot transactions and nominal value of all derivative deals.

## (G) Operational risk

Since 2008, the Bank has used the Advanced Measurement Approach (AMA) for operational risk management. In addition to standard operational risk instruments used within the AMA approach, such as operational losses collection, Risk Control Self-Assessment (RCSA), Key Risk Indicators (KRI) or Scenario Analysis (SA), the Bank developed and deployed also a permanent supervision system consisting of a set of operational everyday controls and a set of formalised periodic controls. The Bank is continuously developing all the aforementioned operational risk instruments and supporting continuous development of an operational risk culture throughout all organisational units.

The information collected by the Operational Risks Department is regularly analysed and provided to the Bank's management. Based on this information, the management may decide on further strategic steps within the framework of operational risk management. The evaluation of operational risks is also an integral component of the process for new product development and validation.

## (H) Legal risk

The Bank regularly monitors and evaluates legal disputes filed against it. In order to cover all contingent liabilities arising from legal disputes, the Bank establishes a provision equal to the claimed amount in respect of all litigation where it is named as a defendant and where the likelihood of payment has been estimated to exceed 50%. The Bank also manages its legal risk through the assessment of legal risks involved in the contracts to which the Bank is a party.

## (I) Estimated fair value of assets and liabilities of the Bank

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction in the principal (or most advantageous) market at the measurement date under current market conditions (i.e. an exit price). Where available, fair value estimates are made based on quoted market prices. However, no readily available market prices exist for a significant portion of the Bank's financial instruments. In circumstances where quoted market prices are not readily available, the fair value is estimated, as appropriate, using discounted cash flow models or other generally acceptable pricing models. Changes in underlying assumptions, including discount rates and estimated future cash flows, significantly affect these estimates.

In estimating the fair value of the Bank's financial instruments, the following methods and assumptions were used.

*(a) Cash and current balances with central banks*
The reported values of cash and current balances with the central bank are generally deemed to approximate their fair value.

*(b) Amounts due from banks*
The estimated fair value of amounts due from banks that mature in 180 days or less approximates their carrying amounts. The fair value of other amounts due from banks is estimated based upon discounted cash flow analysis using interest rates currently offered for investments with similar terms (market rates adjusted to reflect credit risk). The fair value of non-performing amounts due from banks is estimated using a discounted cash flow analysis. The fair value of a loss loan is equal to the appraised value of the underlying collateral.

*(c) Loans and advances to customers*
The fair value of variable yield loans that regularly reprice and which have no significant change in credit risk generally approximates their carrying value. The fair value of loans at fixed interest rates is estimated using discounted cash flow analysis based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality. The fair value of non-performing loans is estimated using a discounted cash flow analysis, including the potential realisation of the underlying collateral.

### (d) *Held-to-maturity investments*

The fair value of the held-to-maturity portfolio is based upon quoted market prices. Where no market prices are available, the fair value is estimated based on discounted cash flow models using the interest rate currently offered as of the financial statements date.

### (e) *Amounts due to central banks, banks and customers*

The fair value of deposits repayable on demand represents the carrying value of amounts repayable on demand as of the financial statements date. The carrying value of term deposits at variable interest rates approximates their fair values as of the financial statements date. The fair value of deposits at fixed interest rates is estimated by discounting their future cash flows using market interest rates. Amounts due to banks and customers at fixed interest rates represent only a fraction of the total carrying value and hence the fair value of total amounts due to banks and customers approximates the carrying values as of the financial statements date.

### (f) *Securities issued*

The fair value of debt securities issued by the Bank is based upon quoted market prices. Where no market prices are available, the fair value is estimated using a discounted cash flow analysis.

*The following table summarises the carrying values and fair values of those financial assets and liabilities not presented on the Bank's Statement of Financial Position at their fair values:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Carrying value | Fair value | Carrying value | Fair value |
| **Financial assets** | | | | |
| Cash and current balances with central banks | 103,993 | 103,993 | 116,257 | 116,257 |
| Amounts due from banks | 57,983 | 58,412 | 54,589 | 54,927 |
| Loans and advances to customers | 527,143 | 541,630 | 484,474 | 500,479 |
| Held-to-maturity investments | 62,425 | 66,244 | 61,003 | 65,839 |
| **Financial liabilities** | | | | |
| Amounts due to central banks | 1 | 1 | 1 | 1 |
| Amounts due to banks | 43,282 | 43,283 | 46,079 | 46,071 |
| Amounts due to customers | 638,410 | 636,619 | 593,059 | 591,711 |
| Securities issued | 45,755 | 46,473 | 54,298 | 54,876 |

*The following table presents the hierarchy of fair values for those financial assets and liabilities not presented on the Bank's Statement of Financial Position at their fair values:*

| | 31 Dec 2016 | | | | 31 Dec 2015 | | | |
|---|---|---|---|---|---|---|---|---|
| (CZKm) | Fair value | Level 1 | Level 2 | Level 3 | Fair value | Level 1 | Level 2 | Level 3 |
| **Financial assets** | | | | | | | | |
| Cash and current balances with central banks | 103,993 | 8,996 | 0 | 94,997 | 116,257 | 11,357 | 0 | 104,900 |
| Amounts due from banks | 58,412 | 0 | 0 | 58,412 | 54,927 | 0 | 0 | 54,927 |
| Loans and advances to customers | 541,630 | 0 | 0 | 541,630 | 500,479 | 0 | 0 | 500,479 |
| Held-to-maturity investments | 66,244 | 66,244 | 0 | 0 | 65,839 | 65,839 | 0 | 0 |
| **Financial liabilities** | | | | | | | | |
| Amounts due to central banks | 1 | 0 | 0 | 1 | 1 | 0 | 0 | 1 |
| Amounts due to banks | 43,283 | 0 | 0 | 43,283 | 46,071 | 0 | 0 | 46,071 |
| Amounts due to customers | 636,619 | 0 | 0 | 636,619 | 591,711 | 0 | 0 | 591,711 |
| Securities issued | 46,473 | 0 | 0 | 46,473 | 54,876 | 0 | 0 | 54,876 |

## (J) Allocation of fair values of financial instruments at fair value to the hierarchy of fair values

*Financial assets and financial liabilities at fair value by fair value hierarchy (refer to Note 3.5.4):*

| (CZKm) | 31 Dec 2016 | Level 1 | Level 2 | Level 3 | 31 Dec 2015 | Level 1 | Level 2 | Level 3 |
|---|---|---|---|---|---|---|---|---|
| **Financial assets** | | | | | | | | |
| Financial assets at fair value through profit or loss | | | | | | | | |
| – Emission allowances | 1,839 | 1,839 | 0 | 0 | 2,800 | 2,800 | 0 | 0 |
| – Debt securities | 9,606 | 8,501 | 1,105 | 0 | 7,872 | 5,184 | 2,688 | 0 |
| – Derivatives | 19,037 | 401 | 18,636 | 0 | 19,217 | 68 | 19,149 | 0 |
| **Financial assets at fair value through profit or loss** | **30,482** | **10,741** | **19,741** | **0** | **29,889** | **8,052** | **21,837** | **0** |
| **Positive fair value of hedging financial derivatives** | **21,614** | **0** | **21,614** | **0** | **23,066** | **0** | **23,066** | **0** |
| Available-for-sale financial assets | | | | | | | | |
| – Shares and participation certificates | 182 | 0 | 0 | 182 | 675 | 0 | 0 | 675 |
| – Debt securities | 31,229 | 20,148 | 11,081 | 0 | 32,025 | 19,130 | 12,895 | 0 |
| **Available-for-sale financial assets** | **31,411** | **20,148** | **11,081** | **182** | **32,700** | **19,130** | **12,895** | **675** |
| **Financial assets at fair value** | **83,507** | **30,889** | **52,436** | **182** | **85,655** | **27,182** | **57,798** | **675** |
| **Financial liabilities** | | | | | | | | |
| Financial liabilities at fair value through profit or loss | | | | | | | | |
| – Sold securities | 160 | 160 | 0 | 0 | 305 | 305 | 0 | 0 |
| – Derivatives | 18,780 | 261 | 18,519 | 0 | 19,880 | 472 | 19,408 | 0 |
| **Financial liabilities at fair value through profit or loss** | **18,940** | **421** | **18,519** | **0** | **20,185** | **777** | **19,408** | **0** |
| **Negative fair value of hedging financial derivatives** | **9,373** | **0** | **9,373** | **0** | **10,002** | **0** | **10,002** | **0** |
| **Financial liabilities at fair value** | **28,313** | **421** | **27,892** | **0** | **30,187** | **777** | **29,410** | **0** |

*Financial assets at fair value – Level 3:*

| | 2016 | | 2015 | |
|---|---|---|---|---|
| (CZKm) | Available-for-sale financial assets | Total | Available-for-sale financial assets | Total |
| **Balance as of 1 January** | **675** | **675** | **2** | **2** |
| Comprehensive income/(loss) | | | | |
| – In the Statement of Income | 0 | 0 | 0 | 0 |
| – In Other Comprehensive Income | 303 | 303 | 674 | 674 |
| Purchases | 164 | 164 | 0 | 0 |
| Sales | (960) | (960) | (1) | (1) |
| Settlement | 0 | 0 | 0 | 0 |
| Transfer from Level 1 | 0 | 0 | 0 | 0 |
| **Balance as of 31 December** | **182** | **182** | **675** | **675** |

*Shares and participation certificates*

When using an alternative method of valuation based on the price/book value ratio, the fair value is not significantly different from the fair value determined on the basis of the present value of future cash flows which was used for the original valuation.

## 42 Offsetting financial assets and financial liabilities

*The table below provides information about rights of offset and related arrangements for financial instruments as of 31 December 2016:*

| | Assets/liabilities set off according to IAS 32 | | | Amounts which have not been set off | | |
|---|---|---|---|---|---|---|
| (CZKm) | Gross amount of financial assets/ liabilities* | Gross amount of financial assets/ liabilities set off by financial liabilities/ assets | Net amount of financial assets/ liabilities | Financial instruments recognised in Statement of Financial Position | Cash collateral related to financial instruments | Net amount |
| Positive fair value of derivatives | 40,651 | 0 | 40,651 | 22,776 | 9,817 | 8,058 |
| Negative fair value of derivatives | 28,153 | 0 | 28,153 | 22,776 | 4,234 | 1,143 |

* This item includes also counterparties with only positive or negative fair value of derivatives.

*The table below provides information about rights of offset and related arrangements for financial instruments as of 31 December 2015:*

| | Assets/liabilities set off according to IAS 32 | | | Amounts which have not been set off | | |
|---|---|---|---|---|---|---|
| (CZKm) | Gross amount of financial assets/ liabilities* | Gross amount of financial assets/ liabilities set off by financial liabilities/ assets | Net amount of financial assets/ liabilities | Financial instruments recognised in Statement of Financial Position | Cash collateral related to financial instruments | Net amount |
| Positive fair value of derivatives | 42,283 | 0 | 42,283 | 25,584 | 10,667 | 6,032 |
| Negative fair value of derivatives | 29,882 | 0 | 29,882 | 25,584 | 4,179 | 119 |

* This item includes also counterparties with only positive or negative fair value of derivatives.

## 43 Assets in custody and assets under management

*The table below provides information about assets in custody and assets under management:*

| | 31 Dec 2016 | | 31 Dec 2015 | |
|---|---|---|---|---|
| (CZKm) | Cash | Securities | Cash | Securities |
| Assets in custody | 3,305 | 573,252 | 2,789 | 528,359 |
| Assets under management | 0 | 2,137 | 0 | 1,760 |

Assets in custody include securities in the amount of CZK 44,821 million (2015: CZK 48,926 million) of Group subsidiaries.

## 44 Post balance sheet events

**Headquarters building**

In March 2017, in line with its long-term strategy of optimising the headquarters buildings, the Group sold one of its headquarters buildings. As of the end of 2016, the building had been classified as held for sale. The result of the transaction will be presented in the line ***'Depreciation, amortisation, impairment and disposal of assets'*** of the Consolidated Statement of Income.

# Securities issued by Komerční banka

## Shares

The registered capital of Komerční banka of CZK 19,004,926,000 is divided into 190,049,260 registered common shares.

| | 2016[1] | 2015 | 2014 | 2013 | 2012 |
|---|---|---|---|---|---|
| Number of shares issued[2] | 190,049,260 | 38,009,852 | 38,009,852 | 38,009,852 | 38,009,852 |
| Number of outstanding shares | 188,855,900 | 37,771,180 | 37,771,180 | 37,771,180 | 37,771,180 |
| Market capitalisation (CZK billion) | 168.2 | 188.1 | 180.2 | 168.0 | 152.4 |
| Earnings per share (CZK)[3] | 72.5 | 337.8 | 343.0 | 331.7 | 369.4 |
| Dividend per share for the year (CZK)[4] | 40.0[5] | 310.0 | 310.0 | 230.0 | 230.0 |
| Dividend payout ratio (%)[6] | 55.5 | 92.4 | 91.0 | 69.8 | 62.6 |
| Book value per share (CZK)[7] | 537.8 | 2,711.4 | 2,816.0 | 2,479.6 | 2,588.5 |
| Share price (CZK) | | | | | |
| closing price at year-end | 885 | 4,950 | 4,740 | 4,421 | 4,010 |
| maximum | 1,091 | 5,667 | 5,179 | 4,810 | 4,214 |
| minimum | 818 | 4,590 | 4,230 | 3,400 | 3,089 |

1) Values in 2016 reflect the effect of 1-to-5 split of KB shares implemented in April 2016.
2) Nominal value of each share is CZK 100. Before the split of KB shares, the nominal value was CZK 500.
3) Earnings attributable to shareholders per average number of shares outstanding (IFRS consolidated)
4) Dividend per share before tax. The statutory tax rate applicable in the Czech Republic is 15% or, in certain cases 35%. Dividend is paid in the following year.
5) Proposal for the Annual General Meeting on 25 April 2017
6) Total dividend paid / Consolidated net profit attributable to shareholders (IFRS consolidated)
7) Shareholders' equity excluding minority equity (IFRS consolidated) divided by average number of shares outstanding

### Rights vested in the shares

Rights are attached to the common shares in accordance with Act No. 90/2012 Coll., on Business Corporations, and with the Bank's Articles of Association as approved by the General Meeting. No special rights are attached to the shares. Shareholders' voting rights are governed by the nominal value of their shares. Each CZK 100 of nominal share value is equivalent to one vote.

The shareholder shall be entitled to a proportion of the Bank's profit approved for distribution to the Shareholders by the General Meeting (a dividend) taking into account the Bank's financial results and terms and conditions specified by the generally binding legal regulations and the payment of which was decided upon by the Board of Directors based on the fulfilment of the terms and conditions specified by the generally binding legal regulations.

In accordance with the Articles of Association, the right to a share in profit shall accrue to any shareholder registered as owning shares in the statutory records of the securities' issuer 7 calendar days prior to the date of the General Meeting which approved the share of the profit to be distributed among shareholders. The share in profit shall become payable upon expiration of 30 days following the date of the General Meeting at which the resolution on the dividend payment was adopted.

The right to claim a payment of the dividend shall lapse 3 years from the day when the shareholder learnt of the due date for the payment of the share in profit or when he could or should have learnt this, however, no later than within 10 years of the due date. Pursuant to a resolution of the Annual General Meeting held in 2009, the Board of Directors will not plead the statute of limitations in order to bar by lapse of time the payment of dividends for the duration of 10 years from the date of dividend payment. After the lapse of 10 years from the date of dividend payment, the Board of Directors is obliged to plead the statute of limitations and to transfer the unpaid dividends to the retained earnings account.

Upon the Bank's liquidation and dissolution, the means of liquidation is governed by the relevant generally binding legal regulations. Distribution of the remaining balance on liquidation among shareholders is approved by the Annual General Meeting in proportion to the nominal values of the shares held by the Bank's shareholders.

## Stock split

The General Meeting held on 22 April 2016 approved splitting the issued shares of Komerční banka at a rate of 1 to 5 by providing each shareholder with five new shares, each with a nominal value of CZK 100, in exchange for each of the original shares with a nominal value of CZK 500. The split took legal effect on 25 April 2016 with its entry into the Register of Companies. The Central Securities Depository changed the respective entry as of 11 May 2016. The split shares began trading on the Prague Stock Exchange on 12 May 2016.

## Stock exchange listing

As of 31 December 2016, Komerční banka's shares were listed under ISIN CZ0008019106 on the Prime Market of the Prague Stock Exchange (PSE) and were traded at RM-SYSTEM Czech Stock Exchange. The average daily trading volume of KB shares on the PSE of CZK 198.7 million (EUR 7.4 million) was the second highest[1] among shares traded on the exchange and represented a daily capital rotation of 0.12%.

## Global depositary receipts

Global depositary receipts (GDRs) representing shares of Komerční banka in the ratio 3:1, registered under ISIN US5004594090 and US5004591021, were issued in 1995 and 1996 and traded on the London Stock Exchange until 30 March 2016. The programme of Komerční banka's GDRs and the respective depositary agreement with The Bank of New York Mellon was terminated on 3 June 2016. KB's Board of Directors had approved termination of the programme in January 2016. Improvements in the Czech Republic's institutional framework and integration into the European Union's regulatory environment have eliminated the need to provide this additional layer of assurance to investors through listing on a developed stock market.

## Stock market performance

From a global perspective, equity markets delivered in 2016 solid growth. The MSCI ACWI index of 46 developed and emerging markets increased by 5.6% in USD terms (11.7% in CZK). However, that growth mostly bypassed Europe and Japan. The US stock market's S&P 500 index gained 9.5% in USD (15.9% in CZK terms), but the MSCI EU index covering 17 markets of the European Union, including the Czech Republic, lost 2.8% for the year (the same in EUR and CZK terms). The average performance of European banks was even weaker, as the STOXX Europe 600 Banks index decreased by 7.2%.

The year 2016 did not start well for global equities, as investors were wary of recession in the United States, oil prices were declining to very low levels, again raising risks of deflation in Europe, and capital flight from China had also raised economic fears. The athmosphere relaxed a bit from mid February and the markets set out on a quite steady growth trend through the rest of the year, which was interrupted only very briefly in June by the outcome of the referendum in the United Kingdom to exit the European Union. At the end of the year, US stocks and also other markets were boosted by expectations of investors that the administrative of the incoming US President Donald Trump would generate a fiscal stimulus accelerating economic growth. Meanwhile, presumptions of forthcoming deregulation and increasing in inflation and interest rates underpinned banks globally.

## KB share price development

The KB shares closed out trading for 2016 at CZK 885, which was 10.6% below the closing price of a year earlier[2]. As of 31 December 2016, Komerční banka's market capitalisation stood at CZK 168.2 billion (EUR 6.2 billion), ranking it third among titles listed on the PSE.

In the first quarter, KB's share price performed well thanks to resilience of financial results and growing business volumes reported by the Bank for 2015. The closing share price reached its high for 2016 on 21 March at CZK 1,091. From this peak, the KB share price was trending slightly downwards, reflecting the concerns of investors due to still declining market interest rates and uncertainty as to the future capital requirements to be announced by the central bank. The share price reacted strongly to the announcement on 3 August

1 Source: Prague Stock Exchange
2 Adjusted for the 1:5 split of KB shares effective on the Prague Stock Exchange from 12 May 2016.

with the results for the second quarter that the Bank had put under review its dividend policy due to the new information on further important increase in the capital requirements. By 29 August, the share price touched its lowest for 2016 at CZK 818. After summer holidays, the KB share price recovered somewhat, influenced by positive commercial and financial results of the Bank and search by foreign investors for financial assets denominated in Czech crowns before the CNB would remove the currency floor vis-a-vis the euro. The increase in interest rates that followed the election of Mr Trump as President of the USA probably also had some positive impact on the share price.

The gross dividend of CZK 62 per share[1] paid out in 2016 represented 92.4% of KB Group's attributable net profit for 2015. The corresponding gross dividend yield based on 2015's closing share price was 6.3%. Komerční banka's dividend policy aims to ensure appropriate remuneration of shareholders for their investment while also maintaining solid and safe capital adequacy with a view to potential growth opportunities and currently applicable as well as anticipated regulatory requirements.

## Total return for shareholders

The total return from holding KB shares in 2016 was a negative 4.9%, comprising a 10.6% decrease in the share price and the contribution from reinvesting the net dividend on the payment day.

## Dialogue with shareholders and the capital market

Apart from the 60.4% of KB's share capital held by Société Générale, an international financial services group headquartered in Paris, France, the Bank's free float is held by a diverse base of shareholders, ranging from large international asset managers to private individuals. From the total of more than 46,000 shareholders as of 31 December 2016, individuals resident in the Czech Republic numbered almost 41,000.

The vast majority of freely traded shares are held by institutional investors located in such main global financial centres as New York, Boston and London.

KB works to build long-term relationships with its shareholders through regular and open communication with all capital market participants. During 2016, Komerční banka management participated in almost 100 investor presentations and meetings involving around 150 institutions in Prague, London, New York, Boston and Frankfurt.

More than 20 companies regularly publish their investment research reports on Komerční banka.

## Acquisition of treasury shares in 2016

Komerční banka held 1,193,360 of its own shares as of 31 December 2016. These securities had been purchased on a European regulated market during 2006 and 2011 in accordance with decisions by the Bank's general meetings of 28 April 2005, 26 April 2006 and 21 April 2011 allowing KB to acquire its own shares into treasury.

During 2016, Komerční banka did not acquire its own shares into the banking book, nor did it dispose of its own shares from this portfolio. In 2016, Komerční banka intermediated transactions in KB shares for its clients through its own account, in the volume of 206 shares before the share split and 8,577 shares after the share split.

Based upon the consent of the General Meetings convened on 23 April 2015 and on 22 April 2016, Komerční banka was authorised to acquire its ordinary shares as treasury stock under the following conditions:

- The maximum amount of shares that can be held by the Bank at any specific moment shall be 3,800,985 ordinary shares (or 19,004,925 ordinary shares following the split realised in 2016) representing the total nominal value of CZK 1,900,492,500.
- The share purchase value must be at least CZK 1 per share and at most CZK 7,000 per share.
- The time for which it is possible for the Bank to acquire the shares is 18 months.
- Shares may not be acquired by the Bank should such acquisition breach the conditions stipulated in S. 301 (b) and (c) and S. 302 of Act No. 90/2012 Coll., the Corporations and Co-operatives Act or, as the case may be, any other applicable legal rules of the Czech Republic or the European Union.

# Bonds

*List of bonds issued by Komerční banka (as of 31 December 2016)*

| No. | Bond | ISIN | Issue date | Maturity date | Volume in CZK | Number of pieces | Interest rate | Payout of interest |
|---|---|---|---|---|---|---|---|---|
| 1. | HZL 2007/2019 | CZ0002001142 [2] | 16 August 2007 | 16 August 2019 | 3,000,000,000 | 30 | 5.00% p.a. | yearly |
| 2. | HZL 2007/2037 | CZ0002001324 [2] | 16 November 2007 | 16 November 2037 | 1,200,000,000 | 12 | Note A | stated |
| 3. | HZL 2007/2037 | CZ0002001332 [2] | 16 November 2007 | 16 November 2037 | 1,200,000,000 | 12 | Note A | stated |
| 4. | HZL 2007/2037 | CZ0002001340 [2] | 16 November 2007 | 16 November 2037 | 1,200,000,000 | 12 | Note B | stated |
| 5. | HZL 2007/2037 | CZ0002001357 [2] | 16 November 2007 | 16 November 2037 | 500,000,000 | 5 | Note B | stated |
| 6. | HZL 2007/2037 | CZ0002001365 [2] | 16 November 2007 | 16 November 2037 | 1,000,000,000 | 10 | RS minus 0.20% p.a. | stated |
| 7. | HZL 2007/2037 | CZ0002001373 [2] | 16 November 2007 | 16 November 2037 | 1,000,000,000 | 10 | RS minus 0.20% p.a. | stated |
| 8. | HZL 2007/2037 | CZ0002001381 [2] | 16 November 2007 | 16 November 2037 | 500,000,000 | 5 | RS minus 0.20% p.a. | stated |
| 9. | HZL 2007/2037 | CZ0002001399 [2] | 16 November 2007 | 16 November 2037 | 500,000,000 | 5 | RS minus 0.20% p.a. | stated |
| 10. | HZL 2007/2037 | CZ0002001431 [2] | 30 November 2007 | 30 November 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 11. | HZL 2007/2037 | CZ0002001449 [2] | 30 November 2007 | 30 November 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 12. | HZL 2007/2037 | CZ0002001456 [2] | 30 November 2007 | 30 November 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 13. | HZL 2007/2037 | CZ0002001464 [2] | 30 November 2007 | 30 November 2037 | 500,000,000 | 5 | RS minus 0.20% p.a. | stated |
| 14. | HZL 2007/2037 | CZ0002001472 [2] | 30 November 2007 | 30 November 2037 | 500,000,000 | 5 | RS minus 0.20% p.a. | stated |
| 15. | HZL 2007/2037 | CZ0002001480 [2] | 30 November 2007 | 30 November 2037 | 500,000,000 | 5 | RS minus 0.20% p.a. | stated |
| 16. | HZL 2007/2037 | CZ0002001498 [2] | 7 December 2007 | 7 December 2037 | 500,000,000 | 5 | RS minus 0.20% p.a. | stated |
| 17. | HZL 2007/2037 | CZ0002001506 [2] | 7 December 2007 | 7 December 2037 | 700,000,000 | 7 | RS minus 0.20% p.a. | stated |
| 18. | HZL 2007/2037 | CZ0002001514 [2] | 7 December 2007 | 7 December 2037 | 1,000,000,000 | 10 | RS minus 0.20% p.a. | stated |
| 19. | HZL 2007/2037 | CZ0002001522 [2] | 7 December 2007 | 7 December 2037 | 1,000,000,000 | 10 | RS minus 0.20% p.a. | stated |
| 20. | HZL 2007/2037 | CZ0002001530 [2] | 7 December 2007 | 7 December 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 21. | HZL 2007/2037 | CZ0002001548 [2] | 7 December 2007 | 7 December 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 22. | HZL 2007/2037 | CZ0002001555 [2] | 12 December 2007 | 12 December 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 23. | HZL 2007/2037 | CZ0002001563 [2] | 12 December 2007 | 12 December 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 24. | HZL 2007/2037 | CZ0002001571 [2] | 12 December 2007 | 12 December 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 25. | HZL 2007/2037 | CZ0002001589 [2] | 12 December 2007 | 12 December 2037 | 1,200,000,000 | 12 | RS minus 0.20% p.a. | stated |
| 26. | 2007/2017 | CZ0003701427 [1] | 18 December 2007 | 1 December 2017 | 76,700,000 | 767 | 4.216% p.a. | yearly |
| 27. | HZL 2007/2017 | CZ0002001761 [1] | 19 December 2007 | 19 December 2017 | 128,620,000 | 12,862 | 4.09% p.a. | yearly |
| 28. | HZL 2007/2037 | CZ0002001753 [1] | 21 December 2007 | 21 December 2037 | 8,330,000,000 | 833 | RS plus 1.5% p.a. | yearly |
| 29. | HZL 2007/2037 | CZ0002001746 [1] | 28 December 2007 | 28 December 2037 | 1,240,000,000 | 124 | RS plus 1.5% p.a. | yearly |
| 30. | HZL 2012/2022 | CZ0002002801 [1] | 21 December 2012 | 21 December 2022 | 3,000,000,000 | 300,000 | 2.55% p.a. | yearly |
| 31. | 2012/2017 | CZ0003703597 [1] | 21 December 2012 | 21 December 2017 | 3,000,000,000 | 3,000,000,000 | 3.50% p.a. | yearly |
| 32. | 2012/2018 | CZ0003703605 [1] | 21 December 2012 | 21 December 2018 | 5,000,000,000 | 5,000,000,000 | Note C | yearly |
| 33. | 2012/2019 | CZ0003703613 [1] | 21 December 2012 | 21 December 2019 | 5,000,000,000 | 5,000,000,000 | Note D | yearly |
| 34. | HZL 2013/2018 | CZ0002003064 [1] | 14 March 2013 | 14 March 2018 | 1,747,000,000 | 174,700 | 6M PRIBOR plus 0.50% p.a. | semiannually |
| 35. | HZL 2014/2022 | CZ0002003379 [1] | 30 January 2014 | 30 April 2022 | 800,000,000 | 80,000 | 3.00% p.a. | yearly |
| 36. | HZL 2014/2024 | CZ0002003361 [1] | 30 January 2014 | 30 January 2024 | 900,000,000 | 90,000 | 3.00% p.a. | yearly |
| 37. | HZL 2014/2025 | CZ0002003353 [1] | 31 January 2014 | 31 January 2025 | 1,117,000,000 | 111,700 | 3.50% p.a. | yearly |
| 38. | HZL 2014/2026 | CZ0002003346 [1] | 31 January 2014 | 31 January 2026 | 800,000,000 | 80,000 | 3.50% p.a. | yearly |
| 39. | HZL 2014/2026 | CZ0002003742 [2] | 18 November 2014 | 18 November 2026 | 750,000,000 | 75,000 | 2.00% p.a. | yearly |
| 40. | HZL 2014/2028 | CZ0002003767 [2] | 20 November 2014 | 20 November 2028 | 750,000,000 | 75,000 | 2.20% p.a. | yearly |
| 41. | HZL 2014/2027 | CZ0002003759 [2] | 24 November 2014 | 24 November 2027 | 750,000,000 | 75,000 | 2.10% p.a. | yearly |
| 42. | HZL 2014/2029 | CZ0002003775 [2] | 27 November 2014 | 27 November 2029 | 750,000,000 | 75,000 | 2.30% p.a. | yearly |

Notes: Certain bonds are held by Komerční banka or other companies within the KB Group.
HZL = mortgage bond, RS = reference rate
1) dematerialised bonds
2) bonds in paper form

Note A: 5.06% p.a. for the first twelve annual periods, afterwards the relevant RS minus 0.20% p.a.

Note B: 5.02% p.a. for the first eleven annual periods, afterwards the relevant RS minus 0.20% p.a.

Note C: 1.50% p.a. for the first year period
2.50% p.a. for the second year period
4.00% p.a. for the third year period
4.50% p.a. for the fourth year period
5.00% p.a. for the fifth year period
5.50% p.a. for the sixth year period

Note D: 1.50% p.a. for the first year period
2.00% p.a. for the second year period
2.50% p.a. for the third year period
5.00% p.a. for the fourth year period
5.50% p.a. for the fifth year period
6.00% p.a. for the sixth year period
6.50% p.a. for the seventh year period

All bonds (with the exception of HZL ISIN CZ0002003742, HZL ISIN CZ0002003767, HZL ISIN CZ0002003759 and HZL ISIN CZ0002003775 that are order bonds) are made out to the bearer. All bonds are denominated in CZK.

All bonds were issued under the second KB Debt Issuance Programme approved by the Czech National Bank on 4 June 2007. This 30-Year Debt Issuance Programme enables the Bank to issue bonds in a maximum amount of CZK 150 billion outstanding.

Heretofore unredeemed bonds were issued in the relevant years in accordance with the Bonds Act, the Securities Act and the Act on Capital Market Undertakings, as amended. The bonds' prospectuses, the base prospectuses of the bond programmes or issuance terms and conditions and supplements to the bond programmes were approved, if required by law, by the Czech National Bank.

**Public tradability and transferability**
HZL ISIN CZ0002002801 and CZ0002003064 were admitted for trading on the Regulated Market of the Prague Stock Exchange. The transferability of the bonds is not limited.

**Rights vested in the bonds**
Rights and obligations pertaining to the bonds are governed and interpreted in accordance with the legal regulations of the Czech Republic. They are explicitly expressed in the issuance terms and conditions for each issue. Bonds bear interest from the date of issue, and coupon payments are made quarterly, semiannually, yearly or at stated intervals. The bonds' returns are paid by the issuer – Komerční banka.

The bonds will be redeemed by Komerční banka in the whole amount of the nominal value (with the exception of HZL ISIN CZ0002001142, HZL ISIN CZ0002001761 and bond ISIN CZ0003701427) on the maturity day. HZL ISIN CZ0002001142, HZL ISIN CZ0002001761 and bond ISIN CZ0003701427 are amortised bonds.

# Information on remuneration to auditors for services provided in 2016

*Remuneration to the auditors of KB and KB Group for services performed during 2016:*

| Type of service – CZK thousand, excl. VAT | KB | KB Group |
|---|---|---|
| Statutory audit | 16,076 | 24,275 |
| Audit related services | 0 | 0 |
| Legal and tax related services | 154 | 154 |
| Other verification services | 622 | 4,350 |
| Non-audit services | 5 | 5 |
| **Total** | **16,857** | **28,784** |

# Report on Relations among Related Entities for the year ended 31 December 2016

(hereinafter the **"Report on Relations"**)

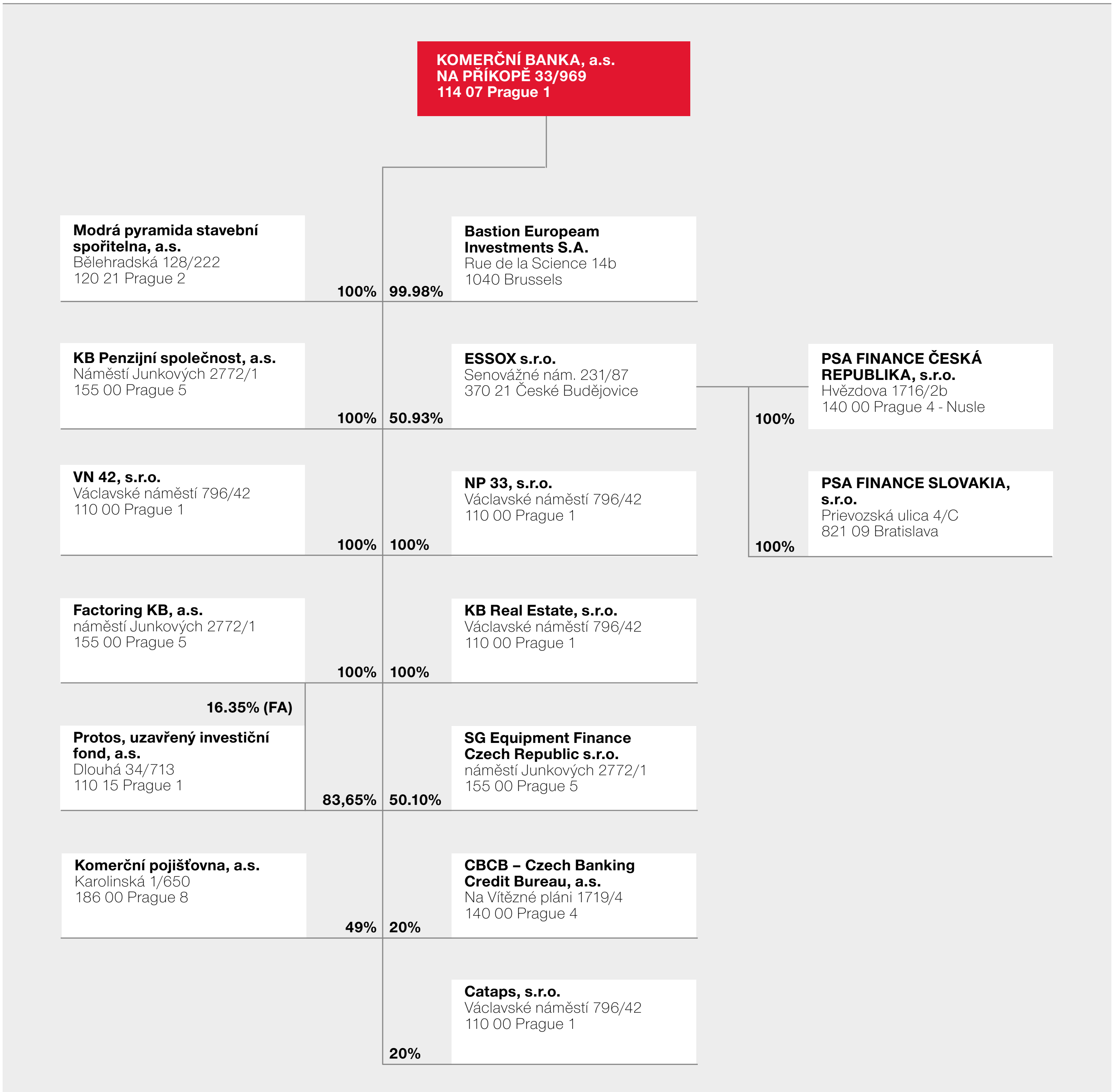
Komerční banka, a.s., with its registered office in Prague 1, Na Příkopě 33/969, 114 07, Corporate ID: 45317054, incorporated in the Register of Companies maintained by the Municipal Court in Prague, Section B, File 1360, (hereinafter **"KB"** or **"Komerční banka"**), is part of a business group (holding company) in which there exist the following relations between KB and its controlling entity and further between KB and other entities controlled by the same controlling entities (hereinafter the **"related entities"**).

This Report on Relations was compiled in accordance with Section 82 et seq. of Act No. 90/2012 Coll., on Business Corporations and Co-operatives (the Business Corporations Act) for the year ended 31 December 2016, that is, from 1 January 2016 to 31 December 2016 (hereinafter the **"reporting period"**).

## I. Introduction

**Structure of relations among entities within the business group:**

In the period from 1 January 2016 to 31 December 2016, KB was a member of the Société Générale S.A. Group, with its registered office at 29, BLD Haussmann, 75009 Paris, France, registration number in the French Register of Companies: R.C.S. Paris B552120222 (1955 B 12022) (hereinafter **"SG"** or **"SG Paris"**). The structure of relations within KB Group is shown below and the structure of relations within the whole of SG Group is shown in the annex:




Note: Percentage of share capital and participation in voting rights may differ.

*During the 2016 reporting period, KB had business relationships with the following related entities:*

| Company | Registered office | SG's share in voting rights |
|---|---|---|
| ALD (SIA) | K. Ulmana gatve 119, Riga, LV-2167, Latvia | 75 |
| ALD (UAB) | Ukmerges 283, Vilnius, LT -06313, Lithuania | 75 |
| ALD Automotive Hungary | 1133 Budapest, Váci út 76, Hungary | 100 |
| ALD Automotive Polska sp. z.o.o. | Ostrobramska 101A, 04-041 Warsaw, Poland | 100 |
| ALD Automotive s.r.o. | U Stavoservisu 527/1, Prague 10, 100 40, Czech Republic | 100 |
| ALD Automotive Slovakia s.r.o., | Panónska cesta 47, Bratislava 851 01, Slovakia | 100 |
| ALD EESTI AS | Akadeemia tee15A, 12618 Tallinn, Estonia | 75.01 |
| Banca Romana Pentrui Devzoltare (B.R.D.) | Boulevard Ion Mihalache No. 1-7, sector I, Bucharest, Romania | 100 |
| Bastion European Investments S.A. | Rue de la Science 14b,1040 Brussels, Belgium | 100 |
| Cataps, s.r.o. | Václavské náměstí 796/42, 110 00, Prague 1, Nové Město, Czech Republic | 100* |
| Crédit du Nord | 28 Place Rihour 59800 Lille, France | 100 |
| ESSOX s.r.o. | Senovážné náměstí 231/7, České Budějovice, 370 21, Czech Republic | 100 |
| European Fund Services, SA | 17 rue Antoine Jans L-1820 Luxembourg, Luxembourg | 100 |
| Factoring KB a.s. | náměstí Junkových 2772/1, Prague 5 – Stodůlky, 155 00, Czech Republic | 100 |
| Inter Europe Conseil | 29, Boulevard Haussmann,75009, Paris, France | 100 |
| KB Penzijní společnost, a.s. | náměstí Junkových 2772/1, Prague 5 – Stodůlky, 155 00, Czech Republic | 100 |
| KB Real Estate, s.r.o. | Václavské náměstí 796/42, 110 00, Prague 1, Nové Město, Czech Republic | 100 |
| Komerční pojišťovna, a.s. | Karolinská 1, č.p. 650, Prague 8, 186 00, Czech Republic | 100 |
| Lyxor International Asset Management (LIAM) | Tour Société Générale, 17 Cours Valmy, 92800 Puteaux, France | 100 |
| MOBIASBANCA GOUPE SG | 81a, Stefan cel Mare si Sfant ave, Chisinau, Moldavia | 87,9 |
| Modrá pyramida stavební spořitelna, a.s. | Bělehradská 128, č.p. 222, Prague 2, 120 21, Czech Republic | 100 |
| Newedge Group (Frankfurt branch) | Neue Mainzer Strasse 52, 60311 Frankfurt am Main, Federal Republic of Germany | 100 |
| NP 33, s.r.o. | Václavské náměstí 796/42, 110 00, Prague 1, Nové Město, Czech Republic | 100 |
| OHRIDSKA BANKA AD SKOPJE | ul. Orce Nikolov br. 54, Skopje, 1000 Macedonia | 71,33 |
| PEMA Polska sp. z. o. o. (Gefa Bank ) | Ul. Krzysztofa Kolumba 3, 62-052 Komorniki,,woj. Wielkopolskie, Poland | 100 |
| PEMA Praha, spol. s r.o. | Ul. Dopraváků 723, 184 00 Prague 8, Czech Republic | 100 |
| PEMA Slovakia, spol. s r. o. (Gefa Bank ) | Pri Prachárni 20, 04001 Košice, Slovakia | 100 |
| Protos, uzavřený investiční fond, a.s. | Dlouhá 34, č.p. 713, Prague 1, 110 15, Czech Republic | 100 |
| Rosbank | 11 Masha Poryvaeva Street, 107 078 Moskva, Russian Federation | 99,95 |
| SG Albania | Blv. Deshmoret e Kombit Twin Towers, Kulla II, Kati Perdhe, Tirane, 1000, Albania | 88,64 |
| SG Algerie | Résidence EL KERMA, 16 105 Gué de Konstantine, Algeria | 100 |
| SG Asset Management Alternative Investments (SGAM AI) | 170 place Henri Renault, 92400 Courbevoie, France | 100 |
| SG Bank & Trust (SGBT) (SG Equipment) | 11-13 Avenue Emile Reuter L-2420 Luxembourg, Luxembourg | 100 |
| SG De Bank Au Liban | Masraf Street, Beirut, Lebanon | 16.8 |
| SG Equipment Finance Czech Republic s.r.o. | náměstí Junkových 2772/1, Prague 5 – Stodůlky, 155 00, Czech Republic | 100 |
| SG Equipment Finance Hungary Plc. | 1062 Budapest, Vaci út 1-3, Hungary | 100 |
| SG Equipment Leasing Hungary Ltd | 1062 Budapest, Vaci út 1-3, Hungary | 100 |
| SG Equipment Leasing Polska | Marszalkowska 111 St., 00-102 Warsaw, Poland | 100 |
| SG Express Bank | Vladislav Varnenchik Blvd. 92, 9000 Varna, Bulgaria | 99,74 |
| SG Hambros | 8 St James's Square, London, Great Britain | 100 |
| SG China Ltd. | Taikang International Tower, Wudinghou Street, Xicheng District, 100140 Peking, China | 100 |
| SG Issuer S.A. (SGBT) | 15 Boulvard du Prince Henri Luxembourg, 1724, Luxembourg | 100 |
| SG Maroccaine de Banques | 55, boulevard Abdelmoumen, Casablanca, Morocco | 100 |
| SG Montenegro | Bulevar Revolucije br. 17, Podgorica 81000, Montenegro | 90,56 |
| SG Option Europe | 17 Cours Valmy, La Defense Cedex, Paris, France | 100 |
| SG Paris | 29, Boulevard Haussmann, Paris, France | |

| Company | Registered office | SG's share in voting rights |
|---|---|---|
| SG Private Banking (Suisse) SA | Rue de la Corraterie 6, Case Postale 5022, CH-1211 Geneva 11, Switzerland | 100 |
| SG Private Banking Belgique | Rue des Colonies, 11,1000 Brussels, Belgium | 100 |
| SG Private wealth management SA (SGBT) | 11-13 Avenue Emile Reuter L-2420 Luxembourg, Luxembourg | 100 |
| SG Securities (London) Ltd. | Exchange House – 12 Primrose Street, London EC2A 2EG, Great Britain | 100 |
| SG Securities Services | Via Benigno Crespi 19, 20159 Milano, Italy | 100 |
| SG Splitska Banka | Rudjera Boskovica 16, 21000 Split, Croatia | 100 |
| SG Srbija | 50 Bulevar Zorana Dindica, Belgrade, Serbia | 100 |
| SG Sucursal en Espana | Genova 26, Madrid, Spain | 100 |
| SG Vehicle Finance Hungary Plc. (SG Equipment) | 1062 Budapest, Vaci út 1-3, Hungary | 100 |
| SGA Société Générale Acceptance N.V. (SG Americas) | Pietermaai 15, Willemstad, Netherlands Antilles | 100 |
| SKB Banka | Ajdovscina 4, 1513 Ljubljana, Slovenia | 99,73 |
| Société Générale Newedge UK Limited | 10 Bishops Square, London, E1 6EG, Great Britain | 100 |
| Sogecap | 50 avenue du Général de Gaulle, 92093 Paris, La Défense CEDEX, France | 100 |
| Sogeprom Česká republika s.r.o. | Legerova 802/64, Prague 2 – Vinohrady, 120 00, Czech Republic | 100 |
| VN 42, s.r.o. | Václavské náměstí 796/42, 110 00, Prague 1, Nové Město, Czech Republic | 100 |

* Since 1 October 2016, Komerční banka has 20% ownership and 40% of the voting rights. The company is therefore no longer part of the KB Group.

### Role of the Company within the Group:

Komerční banka is the parent company of KB Group and is part of the international financial group of Société Générale (hereinafter "SG Group"). As a part of SG Group, Komerční banka provides universal banking services on the territory of the Czech Republic and is a universal bank offering a wide range of services in the area of retail, corporate and investment banking. KB Group companies offer additional specialised services, including pension savings and building society schemes, leasing, factoring, consumer lending and insurance. As a part of KB Group, the Bank provides certain subsidiaries with trademark licences. Komerční banka provides certain IT services, other services and advisory in the area of human resources, and advisory in the areas of compliance, operational risks and insurance within SG Group. KB Internal Audit carries out audit missions within SG Group according to the approved audit plan.
The products of KB's subsidiaries are sold using Komerční banka's sales network. KB provides banking services in Slovakia through its branch there. Komerční banka offers some of its products using, inter alia, the network of Modrá pyramida stavební spořitelna, a.s.

As a part of its management and control system KB receives data on the whole control and management system and also provides these data, including data on KB, to the company SG (the data include, inter alia, budgets, business plans, business continuity and crisis management plans, and anti-money laundering measures).

KB participates in the creation of group policies on the territory of the Czech Republic.

### Manner and means of control

Société Générale, as the majority shareholder, exerts its influence on KB's activity through the General Meeting. During the reporting period, it had four representatives on the Bank's nine-member Supervisory Board and one representative on the three-member Audit Committee. Three Société Générale employees were, during the reporting period, seconded to the Board of Directors of Komerční banka as Société Générale's members; at the end of the reporting period, however, there was only one seconded member of the Board of Directors. Furthermore, based on a contract entered into by and between SG and KB, SG seconds its employees to certain positions. At this time, there are nine such employees within KB.

In accordance with Section 79 of the Business Corporations Act, SG is a controlling entity in respect to KB. Control is formally exercised by implementing SG's methodologies in KB's internal regulations, in particular in the area of risk management and capital adequacy. Furthermore, there is informal control in the form of consultancy on individual areas of KB's activity.

KB acts as controlling entity in relation to its subsidiaries. Control is formally exercised by implementing KB's methodologies in the subsidiaries' internal regulations, and informal control takes the form of consultancy on individual activity areas.

## II. Relations within the Group

### A. Important actions adopted in the reporting period at the initiative or in the interest of the controlling entity or entities controlled by the controlling entity in respect of assets exceeding 10% of the controlled entity's equity

No such actions were adopted.

### B. Overview of mutual contracts between the controlled entity and the controlling entity or among controlled entities

**Banking transactions**

During the reporting period, Komerční banka had the relationships stated below with companies controlled by SG Group and which are subject to banking secrecy in the areas stated below. Relations with KB's subsidiaries are presented in the financial statements as of 31 December 2016.

*Deposit arrangements*
In the deposit segment, KB had entered into arrangements with 30 branches and subsidiaries of SG Group as of the end of the reporting period. As of 31 December 2016, KB maintained a total of 64 accounts, of which 30 were loro accounts for branches and subsidiaries of SG Group, 30 were current accounts and 4 were overdraft accounts opened for non-banking entities of SG Group. The average monthly overdraft balance (borrowing) on loro accounts was CZK 60.95 million; the average monthly credit balance (deposit) was CZK 10,810.54 million. During the reporting period, the average monthly credit balance on current and overdraft accounts was CZK 211.91 million; the average monthly overdraft balance on these accounts was CZK 82.09 million. During the reporting period, KB's interest income on overdraft accounts and overdrafts on current accounts was CZK 0.52 million; income from the fees associated with the maintenance of accounts and related transactions amounted to CZK 5.06 million.

KB's cross-border payment transactions were partly conducted through nostro accounts maintained with SG Paris, B.R.D, SG New York, SG Warszawa, SG Express Bank, Rosbank, SG Splitska Banka and SG China. During the reporting period, KB's average monthly deposit on nostro accounts with SG was CZK 629.26 million; the average monthly overdraft balance on nostro accounts was CZK 343.08 million. Interest income on nostro accounts for the reporting period was CZK 0.128 million; interest expenses amounted to CZK 0.001 million. KB's expenses arising from the fees for the maintenance of, and transactions on, nostro accounts for the reporting period were CZK 0.7 million; income fees (i.e. provided discounts from credit operations on nostro accounts) amounted to CZK 18.6 million. KB's income arising from the fees from loro accounts for the reporting period was CZK 2.527 million. Interest expenses paid by KB on loro accounts amounted to CZK 20.1 thousand and interest income totalled CZK 0.474 million in the reporting period.

Six subsidiaries of SG Group held term deposits (including depository bills) with KB during the reporting period. The average monthly balance of these deposits was CZK 6,471.62 million in the reporting period. The aggregate amount of interest expenses from term deposits (including depository bills) was CZK 2.16 million for the reporting period.

Nostro, loro, current, term and overdraft accounts of related entities were maintained under standard terms and conditions.

*Loan arrangements*
In the loan segment, KB provided loans during 2016 to two SG Group subsidiaries. These totalled 204 loans in the aggregate amount of CZK 5,408.5 million. The average monthly balance of the loans during the reporting period was CZK 4,788.9 million. The aggregate amount of interest income was CZK 33.396 million.

As of the end of the reporting period, KB had provided six entities of SG Group with bank guarantees (payment, non-payment) or credit lines in the amount of CZK 892.3 million.

As of the end of the reporting period, KB had received guarantees from four SG Group entities as collateral for loans provided to clients in the aggregate amount of CZK 6,755.8 million. The aggregate amount of fees for guarantees received in the reporting period amounted to CZK 9.23 million.

*Investment banking arrangements*
In the investment banking segment, KB carried out transactions with 14 branches and subsidiaries from within SG Group. The total number of transactions was 38,943 (1,952 on-balance sheet transactions and 36,991 off-balance sheet transactions) in the aggregate nominal amount of CZK 1,894,421 million. The income from the investment banking transactions amounted to CZK 21,358.5 million and the costs totalled CZK 18,697.2 million.

The aggregate nominal amount of on-balance sheet transactions was CZK 771,787.8 million and consisted of the following:

- Depository transactions – a total of 1,589 transactions in the aggregate amount of CZK 724,045.7 million; and
- Securities held for trading – a total of 363 transactions in the aggregate amount of CZK 47,742.1 million.

The aggregate nominal amount of off-balance sheet transactions was CZK 1,122,633 million and consisted of the following:

- Foreign currency transactions (spots, forwards, swaps) totalling 22,487 transactions in the aggregate nominal amount of CZK 597,156.6 million;
- Interest rate derivative transactions (interest rate swaps and futures) totalling 744 transactions in the aggregate nominal amount of CZK 337,806 million;
- Option transactions with currency instruments totalling 9,871 transactions in the aggregate nominal amount of CZK 158,010.8 million;
- Commodity transactions were carried out only with SG Paris; KB executed 3,675 transactions in the aggregate amount of CZK 26,575.9 million; and
- Emission allowance transactions – KB executed a total of 214 transactions in the aggregate amount of CZK 3,083.5 million with SG Paris during the reporting period.

All of the banking products were provided under standard terms and conditions, in accordance with KB's price list, and while taking into consideration the creditworthiness of individual clients under conditions customary in business or interbank transactions. None of these transactions were carried out at the instruction of the controlling entity. KB incurred no damage as a result of banking transactions entered into during the reporting period.

## Other mutual contracts

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Lease of non-residential premises – Ostrava | ALD Automotive s.r.o. | 31 Oct 2003 |
| Lease of non-residential premises – České Budějovice | ALD Automotive s.r.o. | 1 Dec 2003 |
| Lease of non-residential premises – Pilsen | ALD Automotive s.r.o. | 17 Feb 2004 |
| Mutual co-operation agreement + 1 amendment dated 1 Jul 2010 (banking services) | ALD Automotive s.r.o. | 1 Aug 2007 |
| Lease of non-residential premises – Brno | ALD Automotive s.r.o. | 31 Dec 2009 |
| Co-operation agreement – Jobs | ALD Automotive s.r.o. | 9 Jun 2010 |
| Framework service agreement (IT area) | ALD Automotive s.r.o. | 31 Aug 2010 |
| Accession to the rules of co-operation between KB and group members in the area of sourcing and procurement | ALD Automotive s.r.o. | 16 Aug 2011 |
| Separate agreement no. 1 – VoIP | ALD Automotive s.r.o. | 6 Oct 2011 |
| Separate agreement no. 2 – Provision of technical infrastructure services, connectivity services | ALD Automotive s.r.o. | 1 Nov 2012 |
| Network package | ALD Automotive s.r.o. | 1 Nov 2012 |
| Co-operation agreement + amendment dated 7 Dec 2015 | ALD Automotive s.r.o. | 29 Mar 2013 |
| Lease of non-residential premises – Hradec Králové + amendment dated 13 Feb 2015 | ALD Automotive s.r.o | 31 Mar 2013 |
| Agreement – Outsourcing of HR services + Amendment no. 1 | ALD Automotive s.r.o. | 1 Apr 2013<br>1 Apr 2016 |
| Framework agreement for full-service leasing and finance leasing with subsequent purchase + Amendment no. 1 | ALD Automotive s.r.o. | 22 May 2013<br>31 May 2016 |
| Agreement for co-operation in performance of the contract for employee group risk insurance | ALD Automotive s.r.o. | 29 Oct 2013 |
| Service contract – Lease of a mailing machine, provision of postal services | ALD Automotive s.r.o. | 17 Jul 2014 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Agreement for co-operation in performance of the group insurance agreement for work-related accident and occupational disease insurance for Members of Board of Directors and administrators of the financial group of Komerční banka and Société Générale | ALD Automotive s.r.o. | 29 Dec 2014 |
| Framework agreement to lease means of transport | ALD Automotive s.r.o. | 7 Jan 2015 |
| Lease of non-residential premises – Pilsen | ALD Automotive s.r.o. | 30 Sep 2015 |
| Non-disclosure agreement | ALD Automotive s.r.o. | 9 Jul 2010 |
| Non-disclosure agreement | ALD Automotive Slovakia s.r.o. | 19 Oct 2015 |
| Service contract – Outsourcing (HR services) | ALD Automotive Slovakia s.r.o | 1 Jan 2016 |
| Framework agreement – Full-service leasing, financial leasing | ALD Automotive Slovakia s.r.o | 8 Jun 2016 |
| Custodian services agreement + 1 amendment | B.R.D. | 20 Oct 2011 |
| Service level agreement | B.R.D. | 20 Oct 2011 |
| Additional payment contract | Cataps, s.r.o. | 29 Aug 2016 |
| Partnership agreement – Execution of contracts | Cataps, s.r.o. | 13 Aug 2016 |
| Loan agreement | Cataps, s.r.o. | 12 Aug 2016 |
| Interim servicing agreement | Cataps, s.r.o. | 13 Aug 2016 |
| Co-operation contract (VAT) | Cataps, s.r.o. | 29 Sep 2016 |
| Framework agreement for the rental of employee-driven vehicles | Cataps, s.r.o. | 31 Aug 2016 |
| Interim servicing agreement | Cataps, s.r.o., Worldline SA/NV | 29 Sep 2016 |
| Marketing alliance agreement | Cataps, s.r.o., Worldline SA/NV, Worldline SA | 10 Mar 2016 |
| Shareholders agreement | Cataps, s.r.o., Worldline SA/NV | 10 Mar 2016 |
| Agreement to provide a non-monetary additional payment outside the registered capital + completion certificates + expert's assessment | Cataps, s.r.o. | 29 Aug 2016 |
| Service contract (client) | ESSOX s.r.o. | 21 Sep 2005 |
| Mutual co-operation agreement + 1 amendment | ESSOX s.r.o. | 1 Aug 2007 |
| Co-operation agreement | ESSOX s.r.o. | 17 Sep 2008 |
| Co-branded cards distribution agreement + 1 amendment | ESSOX s.r.o. | 16 Jan 2009 |
| Co-operation agreement + 1 amendment | ESSOX s.r.o. | 20 Oct 2009 |
| Confidentiality agreement | ESSOX s.r.o. | 9 Jul 2010 |
| Individual pricing agreement + 1 amendment | ESSOX s.r.o. | 27 Apr 2009 |
| Agreement on the organisation of periodic control + 1 amendment (client) | ESSOX s.r.o. | 28 Feb 2011 |
| Personal data processing framework agreement (administrator) | ESSOX s.r.o. | 12 Apr 2011 |
| Framework service agreement (recipient) | ESSOX s.r.o. | 26 Apr 2011 |
| Separate agreement no. 1 – Provision of services for access to KB's external entity | ESSOX s.r.o. | 30 Jun 2011 |
| Service contract – C4M access + 1 amendment | ESSOX s.r.o. | 29 Jul 2011 |
| Contract for exchange of negative client information within KB/SG Financial Group in the Czech Republic | ESSOX s.r.o. | 19 Aug 2011 |
| Confidentiality agreement | ESSOX, s.r.o. | 10 May 2010 |
| Lease of non-residential premises and payment of relating services + 1 amendment | ESSOX, s.r.o. | 8 Mar 2006 |
| Agreement for the provision of a PROFIBANKA chip card reader | ESSOX, s.r.o. | 26 Jun 2007 |
| Service contract – Outsourcing + 5 amendments (provider) | ESSOX, s.r.o. | 15 Dec 2009 |
| Service contract – Outsourcing (HR services) | ESSOX s.r.o. | 21 Dec 2011 |
| Co-operation agreement + 1 amendment | ESSOX s.r.o. | 1 Aug 2012 |
| Distribution agreement for product "Corporate Car Loans" + 1 amendment | ESSOX s.r.o. | 1 Aug 2012 |
| Individual pricing agreement + 1 amendment | ESSOX s.r.o. | 27 Aug 2012 |
| Agreement for co-operation in performance of the contract for employee group risk insurance No. 3280000000 in the wording of amendment no. 1 of 29 Jun 2012 | ESSOX s.r.o. | 22 Aug 2012 |
| Co-branded cards co-operation agreement | ESSOX s.r.o. | 28 Dec 2012 |
| Framework agreement for the provision of financial services + 3 amendments | ESSOX s.r.o. | 31 Jul 2014 |
| Service level agreement | ESSOX s.r.o. | 25 Nov 2014 |
| Separate agreement No. 2 – Provision of technical infrastructure services, service hosting | ESSOX s.r.o. | 29 Aug 2014 |
| Agreement for framework insurance contract no. 7720802024 | ESSOX, s.r.o. | 10 Feb 2014 |
| Agreement to enter into a lease of non-residential premises and payment of relating services | ESSOX, s.r.o. | 27 Mar 2015 |

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| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Group insurance agreement for work-related accident and occupational disease insurance for Members of Board of Directors and administrators of the financial group of Komerční banka and Société Générale N°334000000 | ESSOX s.r.o. | 14 Jul 2016 |
| Contract – Soft collection service 0000021702/0000 | ESSOX s.r.o. | 29 Apr 2015 |
| Sublease no. 22231 + 2 amendments | ESSOX, s.r.o. | 11 Feb 2016 |
| Contract for the payment of insurance premium and of insurance broker's commission | ESSOX, s.r.o. | 23 Aug 2016 |
| Service level agreement | European Fund Services, SA | 12 Nov 2008 |
| IT – Partial agreement no. 1, connectivity services, | | |
| provision of technical infrastructure solution services | Factoring KB a.s. | 1 Dec 2012 |
| Individual pricing agreement + 2 amendments | Factoring KB a.s. | 31 Jul 2012 |
| Framework agreement for the rental of employee-driven motor vehicles | Factoring KB a.s. | 22 Sep 2014 |
| Service contract for the provision of postal services duplicate documentation shredding | Factoring KB a.s. | 31 Oct 2013 |
| Service contract – BI services | Factoring KB a.s. | 27 Dec 2012 |
| Framework agreement for the provision of technical infrastructure solution services | Factoring KB a.s. | 8 Sep 2010 |
| Database usage license agreement | Factoring KB a.s. | 1 Apr 2011 |
| IT – Partial agreement no. 2, physical hosting of equipment, provision of technical infrastructure solution services + 1 amendment | Factoring KB a.s. | 1 Dec 2012 |
| IT – Partial agreement no. 3, IT infrastructure hosting, provision of technical infrastructure solution services | Factoring KB a.s. | 1 Dec 2012 |
| IT – Partial agreement no. 4, VoIP, provision of technical infrastructure solution services | Factoring KB a.s. | 31 Dec 2012 |
| IT – Partial agreement no. 5, email, provision of technical infrastructure solution services | Factoring KB a.s. | 25 May 2015 |
| IT – Partial agreement no. 6, fileshare, provision of technical infrastructure solution services | Factoring KB a.s. | 29 Feb 2016 |
| IT – Partial agreement no. 7, end user workplace (EUV), provision of technical infrastructure solution services | Factoring KB a.s. | 18 Jan 2016 |
| IT – Partial agreement no. 8, service desk (SD), provision of technical infrastructure solution services | Factoring KB a.s. | 18 Jan 2016 |
| IT – Partial agreement no. 9, identity and access, provision of technical infrastructure solution services | Factoring KB a.s. | 18 Jan 2016 |
| IT – Partial agreement no. 10, platform hosting, provision of technical infrastructure solution services | Factoring KB a.s. | 18 Jan 2016 |
| IT – Partial agreement no. 11, DR (disaster recovery), provision of technical infrastructure solution services | Factoring KB a.s. | 18 Jan 2016 |
| Service contract – information security services | Factoring KB a.s. | 27 Oct 2015 |
| Co-operation agreement no. 0000020447/0000 + 1 amendment (Framework agreement) | Factoring KB a.s. | 31 Dec 2012 |
| Service level agreement – Co-operation in the area of reporting and accounting | Factoring KB a.s. | 26 Nov 2014 |
| Lease of non-residential premises, movable assets and payment of relating services (3) + 1 amendment | Factoring KB a.s. | 8 Jun 2006<br>18 Jun 2008<br>19 Dec 2011<br>30 Sep 2015 |
| Lease of non-residential premises, movable assets and payment of relating services + 1 amendment | Factoring KB a.s. | 30 Aug 2012<br>30 Dec 2014 |
| Sublease agreements for parking places (3) | Factoring KB a.s. | 28 Aug 2012<br>1 Jan 2013<br>23 Mar 2015 |
| License agreement - LOGO + 1 amendment | Factoring KB a.s. | 20 Dec 2004<br>29 Jan 2015 |
| Contract for the payment of insurance premium and of insurance broker's commission | Factoring KB a.s. | 17 Jun 2016 |
| Agreement for co-operation in performance of contract for employee group risk insurance no. 3280000000, in the wording of Amendment no. 1 | Factoring KB a.s. | 24 Aug 2012 |
| Agreement for co-operation in performance of group insurance agreement of work-related accident and occupational disease insurance for Members of Board of Directors and administrators of the financial group of Komerční banka and Société Générale No. 334000000 | Factoring KB a.s. | 26 Sep 2016 |
| Mutual co-operation agreement + 1 amendment – Provision of banking services to employees | Factoring KB a.s. | 1 Aug 2007<br>1 Jul 2010 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Agreement – Outsourcing of HR services (excluding payroll) KB Agr. No. 20596/0000 + Amendment (2) | Factoring KB a.s. | 1 Jan 2013<br>1 Oct 2013<br>31 Mar 2016 |
| Service contract – Outsourcing (HR services) + 1 amendment | Factoring KB a.s. | 4 Jan 2010<br>1 Apr 2016 |
| Co-operation agreement – jobs (vacancies staffing) | Factoring KB a.s. | 28 Apr 2010 |
| Distribution agreement + 1 amendment | Factoring KB a.s. | 1 Dec 2008<br>10 Jan 2013 |
| Framework agreement – personal data processing | Factoring KB a.s. | 1 Dec 2008 |
| Confidentiality agreement | Factoring KB a.s. | 9 Aug 2010 |
| Rules for co-operation between KB and members of the Group in the field of sourcing and purchasing | Factoring KB a.s. | 4 Oct 2010 |
| Agreement on the organisation of periodic control (internal audit services) + 1 amendment | Factoring KB a.s. | 5 May 2011 |
| Service contract – access to C4M – amendment (1) | Factoring KB a.s. | 24 May 2011<br>29 May 2012 |
| Service contract – Safety at work, environment protection, fire protection | Factoring KB a.s. | 30 Jan 2015 |
| License agreement + amendment no. 1 | KB Penzijní společnost, a.s. | 20 Dec 2004<br>18 Dec 2014 |
| Framework agreement for personal data processing | KB Penzijní společnost, a.s. | 11 Aug 2006 |
| Service contract (sharing data from subsidiaries) + Amendment nos. 1 and 2 | KB Penzijní společnost, a.s. | 24 Nov 2006<br>28 Aug 2009<br>6 May 2010 |
| Mutual co-operation agreement + Amendment no. 1 | KB Penzijní společnost, a.s. | 1 Aug 2007<br>1 Jul 2010 |
| Agreement for co-operation within the Group under Section 5a of Act No. 235/2004 Coll., the VAT Act + Amendments nos. 1 and 2 | KB Penzijní společnost, a.s. | 19 Nov 2008<br>22 Oct 2009<br>6 Aug 2014 |
| Agreement on KB Call Centre services + Amendment no. 1 | KB Penzijní společnost, a.s. | 31 Dec 2009<br>31 Dec 2013 |
| Service contract – Outsourcing (HR services) + Amendment no. 1 | KB Penzijní společnost, a.s. | 4 Jan 2010<br>6 Dec 2016 |
| Service contract – Outsourcing + Amendment no. 1 | KB Penzijní společnost, a.s. | 9 Jan 2010<br>11 Sep 2013 |
| Co-operation agreement – Jobs | KB Penzijní společnost, a.s. | 28 Apr 2010 |
| Confidentiality agreement | KB Penzijní společnost, a.s. | 9 Jul 2010 |
| Rules for co-operation between KB and members of the Group in the field of sourcing and purchasing | KB Penzijní společnost, a.s. | 13 Sep 2010 |
| IT service framework agreement + Amendment no. 1 | KB Penzijní společnost, a.s. | 2 Nov 2010<br>31 Dec 2014 |
| Notification service contract (Contract no. 1 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 10 Jun 2011 |
| Contract for the provision of technical infrastructure services – Connectivity services (Contract no. 2 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 20 Dec 2012 |
| Contract for the provision of technical infrastructure services – Physical hosting of equipment (Contract no. 3 relating to Framework Agreement) + Amendment no. 1 | KB Penzijní společnost, a.s. | 20 Dec 2012<br>20 Jul 2016 |
| Contract for the provision of technical infrastructure services – IT infrastructure hosting – VMWare (Contract no. 4 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 20 Dec 2012 |
| Contract for the provision of technical infrastructure services – Voice over IP (Contract no. 5 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 31 Dec 2012 |
| Contract for the provision of technical infrastructure services –Fileshare service (Contract no. 6 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 8 Aug 2013 |
| Contract for the provision of technical infrastructure services –Smartphone service (Contract no. 7 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 8 Aug 2013 |
| Contract for the provision of technical infrastructure services –EUW service (Contract no. 8 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 8 Aug 2013 |
| Contract for the provision of technical infrastructure services – service desk (Contract no. 9 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 8 Aug 2013 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Contract for the provision of technical infrastructure services –Email service (Contract no. 10 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 8 Aug 2013 |
| Contract for the provision of technical infrastructure services – Platform hosting (Contract no. 11 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 17 Jun 2014 |
| Contract for the provision of technical infrastructure services – identity and access (Contract no. 13 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 31 Jan 2014 |
| Contract for the provision of technical infrastructure services –HW rental (Contract no. 15 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 20 Jul 2016 |
| Contract for the provision of technical infrastructure services – KBPS application development (Contract no. 16 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 4 Mar 2015 |
| Contract for the provision of technical infrastructure services – Application Support (Contract no. 17 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 4 Mar 2015 |
| Contract for the provision of technical infrastructure services – Notification service (Contract no. 18 relating to Framework Agreement) | KB Penzijní společnost, a.s. | 3 Oct 2016 |
| Agreement on the organisation of periodic control + Amendment no. 1 | KB Penzijní společnost, a.s. | 21 Jan 2011<br>30 Dec 2011 |
| Compliance service agreement | KB Penzijní společnost, a.s. | 1 Dec 2011 |
| Co-operation agreement + Amendment no. 1 | KB Penzijní společnost, a.s. | 10 Aug 2012<br>30 Mar 2015 |
| Sublease agreement (offices) + Amendment no. 1 | KB Penzijní společnost, a.s. | 10 Aug 2012<br>26 Jun 2014 |
| Sublease agreements for parking + Amendment nos. 1 and 2 | KB Penzijní společnost, a.s. | 10 Aug 2012<br>30 May 2014<br>8 Jan 2016 |
| Agreement for co-operation in performance of contract for employee group risk insurance | KB Penzijní společnost, a.s. | 22 Aug 2012 |
| Agreement – Outsourcing of services (documentation processing) | KB Penzijní společnost, a.s. | 25 Sep 2012 |
| Distribution agreement for products “Pension Saving Plan – Pillar II” and “Supplementary Pension Saving Plan with a State Contribution – Pillar III” + Amendments nos. 1 and 2 | KB Penzijní společnost, a.s. | 21 Dec 2012<br>4 Sep 2013<br>20 Jan 2016 |
| Agreement – Outsourcing of HR services (excluding payroll) + Amendment no. 1 | KB Penzijní společnost, a.s. | 1 Jan 2013<br>31 Mar 2016 |
| Agreement – Outsourcing of services: operational risks + Amendment no. 1 | KB Penzijní společnost, a.s. | 25 Mar 2013<br>27 Mar 2015 |
| Service agreement + Amendment no. 1 | KB Penzijní společnost, a.s. | 21 May 2013<br>2 Jun 2014 |
| Confidentiality agreement | KB Penzijní společnost, a.s. | 12 Aug 2013 |
| Contract for issue of payment place mandate | KB Penzijní společnost, a.s. | 1 Oct 2013 |
| Contract for personal data processing (in connection with contract for issue of payment place mandate) | KB Penzijní společnost, a.s. | 1 Oct 2013 |
| Service contract – Outsourcing – BI services | KB Penzijní společnost, a.s. | 1 Nov 2013 |
| Agreement to enter into framework insurance agreement | KB Penzijní společnost, a.s. | 11 Feb 2014 |
| Framework agreement for the rental of employee-driven motor vehicles | KB Penzijní společnost, a.s. | 22 Sep 2014 |
| 2 x Backup site provision agreement | KB Penzijní společnost, a.s. | 10 Nov 2014 |
| Service level agreement | KB Penzijní společnost, a.s. | 24 Nov 2014 |
| Contract of mandate – Supplier contract administration + Amendment no. 1 | KB Penzijní společnost, a.s. | 31 Dec 2014<br>6 Apr 2016 |
| Agreement of work-related accident and occupational disease insurance for Members of Board of Directors and administrators of the financial group of Komerční banka and Société Générale N°333000000 | KB Penzijní společnost, a.s. | 23 Mar 2015 |
| Parking place sublease agreement | KB Penzijní společnost, a.s. | 31 Mar 2015 |
| Service agreement – OHS, environmental protection and fire protection | KB Penzijní společnost, a.s. | 28 May 2015 |
| Purchase agreement | KB Penzijní společnost, a.s. | 7 Mar 2016 |
| Contract for the payment of insurance premium and of insurance broker’s commission | KB Penzijní společnost, a.s. | 17 Jun 2016 |
| Agreement for co-operation in performance of group insurance agreement for work-related accident and occupational disease insurance for Members of Board of Directors and administrators of the financial group of Komerční banka and Société Générale N°334000000 | KB Penzijní společnost, a.s. | 12 Sep 2016 |
| Service contract – information security services | KB Penzijní společnost, a.s. | 16 Sep 2016 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Real estate lease agreement + 6 amendments | KB Real Estate, s.r.o. | 4 Jun 2012<br>26 Sep 2012<br>4 Sep 2013<br>14 Dec 2013<br>31 Dec 2014<br>31 Dec 2015,<br>31 Dec 2016 |
| Service contract – Outsourcing (accounting services) | KB Real Estate, s.r.o. | 1 Apr 2015 |
| Service contract – Outsourcing (support services) | KB Real Estate, s.r.o. | 3 Nov 2015 |
| Contract for the payment of insurance premium and of insurance broker's commission | KB Real Estate, s.r.o. | 8 Jun 2016 |
| Co-operation agreement | Komerční pojišťovna, a.s. | 27 Dec 2000 |
| Contract for individual group risk insurance, including 8 amendments | Komerční pojišťovna, a.s. | 9 Jan 2003 |
| Framework agreement – Spektrum insurance programme in the wording of Amendments nos. 1, 2, 3 and 4 | Komerční pojišťovna, a.s. | 28 Jan 2003 |
| Lease of non-residential premises, movable assets and payment of relating services – Jihlava, including 8 amendments | Komerční pojišťovna, a.s. | 31 Jan 2003 |
| PATRON collective insurance contract in the wording of Amendment no. 1 | Komerční pojišťovna, a.s. | 25 Aug 2003 |
| Contract for collective insurance of credit cards of Komerční banka, a.s., including 2 amendments | Komerční pojišťovna, a.s. | 1 Nov 2004 |
| License agreement + 1 Amendment | Komerční pojišťovna, a.s. | 20 Dec 2004 |
| Lease of non-residential premises, movable property and payment of relating services – Brno | Komerční pojišťovna, a.s. | 31 May 2005 |
| Co-operation agreement | Komerční pojišťovna, a.s. | 22 Sep 2005 |
| Framework agreement for personal data processing | Komerční pojišťovna, a.s. | 24 Mar 2006 |
| Contract for the intermediation of "VITAL AND VITAL PLUS PROGRAM", including 2 amendments | Komerční pojišťovna, a.s. | 25 Apr 2006 |
| Contract for the intermediation of "VITAL GRANT", including 2 amendments | Komerční pojišťovna, a.s. | 25 Apr 2006 |
| Contract for the intermediation of "VITAL", including 5 amendments | Komerční pojišťovna, a.s. | 25 Apr 2006 |
| Contract for the intermediation of MERLIN and PROFI MERLIN, including 2 amendments | Komerční pojišťovna, a.s. | 25 Apr 2006 |
| Contract for the intermediation of PATRON and PROFI PATRON | Komerční pojišťovna, a.s. | 25 Apr 2006 |
| Contract for the intermediation of RISK LIFE FOR MORTGAGE LOANS, including amendments nos. 1, 2, 3, and 4 | Komerční pojišťovna, a.s. | 25 Apr 2006 |
| Payment co-operation agreement | Komerční pojišťovna, a.s. | 29 May 2006 |
| Contract for the intermediation of TRAVEL INSURANCE, including amendments nos. 1, 2 and 3 | Komerční pojišťovna, a.s. | 14 Jun 2006 |
| Contract for the intermediation of sale of VITAL INVEST, including 30 amendments | Komerční pojišťovna, a.s. | 4 Oct 2006 |
| TVIS/STVIS and spot transactions contract | Komerční pojišťovna, a.s. | 7 Dec 2006 |
| Contract for intermediation of the sale of VITAL PREMIUM, including 8 amendments | Komerční pojišťovna, a.s. | 18 Dec 2006 |
| Contract for acceptance of payment cards – internet, including Amendment no. 1 | Komerční pojišťovna, a.s. | 29 Mar 2007 |
| Agreement to send electronic notifications of clearing | Komerční pojišťovna, a.s. | 5 Jun 2007 |
| Framework distribution contract, including Amendment no. 1 | Komerční pojišťovna, a.s. | 22 Jun 2007 |
| Lease of non-residential premises, movable assets and payment of relating services – Ostrava, including 2 amendments | Komerční pojišťovna, a.s. | 29 Jun 2007 |
| Contract for the collective insurance of consumer loans, including 6 amendments | Komerční pojišťovna, a.s. | 1 Aug 2007 |
| Mutual co-operation agreement, including Amendment no. 1 | Komerční pojišťovna, a.s. | 1 Aug 2007 |
| Contract for collective insurance of credit cards of Komerční banka, a.s., including 3 amendments | Komerční pojišťovna, a.s. | 1 Nov 2007 |
| Fees clearing agreement | Komerční pojišťovna, a.s. | 1 Oct 2008 |
| Contract of co-operation in the group VAT registration, including 2 amendments | Komerční pojišťovna, a.s. | 21 Nov 2008 |
| Contract for collective insurance of payment cards, including 9 amendments | Komerční pojišťovna, a.s. | 26 Jan 2009 |
| Contract for the intermediation of VITAL PLUS, including amendments nos. 1, 2, 3 and 4 | Komerční pojišťovna, a.s. | 14 Apr 2009 |
| Contract for collective insurance of corporate lending, including 2 amendments | Komerční pojišťovna, a.s. | 5 May 2009 |
| Contract for collective insurance of MERLIN and PROFI MERLIN, including 8 amendments | Komerční pojišťovna, a.s. | 5 Oct 2009 |
| VITAL INVEST FORTE custody agreement | Komerční pojišťovna, a.s. | 6 Oct 2009 |
| Contract for collective insurance of goods purchasing relating to credit cards, including 1 amendment | Komerční pojišťovna, a.s. | 29 Oct 2009 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Agreement to co-operate in portfolio valuation | Komerční pojišťovna, a.s. | 9 Dec 2009 |
| Contract for acceptance of electronic payments made through Moje platba | Komerční pojišťovna, a.s. | 14 Dec 2009 |
| Call centre service contract | Komerční pojišťovna, a.s. | 31 Dec 2009 |
| Service contract – Outsourcing (HR services), including 1 amendment | Komerční pojišťovna, a.s. | 21 Apr 2010 |
| Confidentiality agreement | Komerční pojišťovna, a.s. | 9 Jul 2010 |
| IT service framework agreement, including separate agreements 1–6 and including 1 amendment no. 3 to separate agreement no. 6 | Komerční pojišťovna, a.s. | 14 Sep 2010 |
| Accession to the rules of co-operation between KB and Group members in the area of sourcing and acquisitions | Komerční pojišťovna, a.s. | 15 Oct 2010 |
| Contract for collective insurance of the “A KARTA” and “LADY” credit cards, including 1 amendment | Komerční pojišťovna, a.s. | 1 Apr 2011 |
| Lease of non-residential premises, movable assets and payment of relating services – Hradec Králové | Komerční pojišťovna, a.s. | 29 Aug 2011 |
| Commitment letter – Optimo 6Y EMTN in CZK | Komerční pojišťovna, a.s., SG | 20 Sep 2011 |
| Contract for collective insurance of “Moje pojištění plateb”, including 1 amendment | Komerční pojišťovna, a.s. | 7 Dec 2011 |
| Contract for collective insurance of “Profi pojištění plateb”, including 2 amendments | Komerční pojišťovna, a.s. | 7 Dec 2011 |
| Separate agreement nos. 1–4 relating to framework IT services agreement, including amendments | Komerční pojišťovna, a.s. | 22 Feb 2012 |
| Agreement for co-operation in performance of the contract for employee group risk insurance | Komerční pojišťovna, a.s. | 29 Feb 2012 |
| Contract for employee group risk insurance, including 6 amendments | Komerční pojišťovna, a.s. | 29 Feb 2012 |
| Commitment letter (Optimo Komodity II) dated 24 Apr 2012 | Komerční pojišťovna, a.s., SG | 24 Apr 2012 |
| Individual pricing agreement, including 1 amendment | Komerční pojišťovna, a.s. | 30 Aug 2012 |
| Separate agreement no. 5 – provision of notification services, including 1 amendment | Komerční pojišťovna, a.s. | 7 Sep 2012 |
| Contract for the intermediation of Vital Premium in EUR, including 2 amendments | Komerční pojišťovna, a.s. | 23 Nov 2012 |
| Product development co-operation agreement, including 2 amendment | Komerční pojišťovna, a.s. | 21 Dec 2012 |
| Pension insurance distribution contract | Komerční pojišťovna, a.s. | 2 Jan 2013 |
| Framework agreement to indemnify clients | Komerční pojišťovna, a.s. | 21 Jan 2013 |
| Contract for collective insurance of corporate cards and golden corporate cards | Komerční pojišťovna, a.s. | 21 Jan 2013 |
| Contract for the provision of BI consulting, including 2 amendments | Komerční pojišťovna, a.s. | 26 Jun 2013 |
| Contract for optional collective insurance of consumer loans | Komerční pojišťovna, a.s. | 28 Aug 2013 |
| Contract for intermediation of the “MOJE JISTOTA” risk life insurance, including 1 amendment | Komerční pojišťovna, a.s. | 27 Sep 2013 |
| Minutes of the agreement not to provide a discount on administrative costs on survival of Vital Plus contracts | Komerční pojišťovna, a.s. | 7 Apr 2014 |
| Separate agreement No. 6 – Provision of WEBEX technical infrastructure services | Komerční pojišťovna, a.s. | 1 Aug 2014 |
| Service level agreement – Co-operation in the area of accounting and reporting | Komerční pojišťovna, a.s. | 1 Jan 2015 |
| Agreement for co-operation in performance of the group insurance agreement for work-related accident and occupational disease insurance for Members of Board of Directors and administrators of the financial group of KB/SG no. 333000000 | Komerční pojišťovna, a s. | 25 Mar 2015 |
| Agreement on cancellation of obligations under the group Insurance agreement on work-related accident and occupational disease insurance for Members of the Board of Directors, administrators of the financial group of Komerční banka and Société Générale | Komerční pojišťovna, a s. | 13 Jul 2016 |
| Distribution agreement for product VITAL PREMIUM IN USD | Komerční pojišťovna, a s. | 31 Mar 2015 |
| Commitment letter – Accumulator note in CZK | Komerční pojišťovna, a.s., SG | 25 Apr 2015 |
| Agreement to provide a 20% discount on travel insurance for selected clients of Komerční banka | Komerční pojišťovna, a.s. | 1 Oct 2015 |
| Service contract – Outsourcing – BI services | Komerční pojišťovna, a.s. | 10 Dec 2015 |
| Service contract – Outsourcing – BI services (SOL2) | Komerční pojišťovna, a.s. | 10 Dec 2015 |
| Minutes of the agreement to cut the basis for the calculation of the commission for the sale of travel insurance | Komerční pojišťovna, a.s. | 28 Jan 2016 |
| Separate distribution agreement for product “MojePojištění majetku” | Komerční pojišťovna, a.s. | 25 Apr 2016 |
| Agreement on termination of separate distribution agreement for product Risk Life Insurance Pojištění Penze | Komerční pojišťovna, a.s. | 30 Apr 2016 |
| Minutes of the agreement to cut the basis for the calculation of the commission for the sale of travel insurance | Komerční pojišťovna, a.s. | 15 Jun 2016 |
| Contract for the payment of insurance premium and of insurance broker’s commission | Komerční pojišťovna, a.s. | 30 Jun 2016 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Group insurance agreement on work-related accident and occupational disease insurance for Members of the Board of Directors and administrators of the financial group of Komerční banka and Société Générale no. 334000000 | Komerční pojišťovna, a.s. | 13 Jul 2016<br>1 Sep 2016 |
| Agreement for co-operation in performance of group insurance agreement on work-related accident and occupational disease insurance for Members of the Board of Directors and administrators of the financial group of Komerční banka and Société Générale no. 334000000 | Komerční pojišťovna, a.s. | 4 Aug 2016 |
| Commitment letter for Certus, Certus 2 – Vital Invest product sales agreement | Komerční pojišťovna, a.s., SG | 11 Feb 2013 |
| Commitment letter for Certus 3 | Komerční pojišťovna, a.s., SG | 29 Jun 2015 |
| Commitment letter for Certus 4 | Komerční pojišťovna, a.s., SG | 26 Oct 2015 |
| Commitment letter for Certus 5 | Komerční pojišťovna, a.s., SG | 1 Feb 2016 |
| Commitment letter for Certus 6 | Komerční pojišťovna, a.s., SG | 18 Apr 2016 |
| Commitment letter for Certus 7 | Komerční pojišťovna, a.s., SG | 17 Oct 2016 |
| Distribution agreement, including amendments nos. 1 and 2 | LIAM | 15 Feb 2008 |
| Contact bank agreement, including amendments nos. 1 and 2 | LIAM | 25 Feb 2008 |
| Outsourcing agreement – Treasury (provision of services) | Modrá pyramida stavební spořitelna, a.s. | 7 Feb 2008 |
| Universal contract to hand over cash in packaging | Modrá pyramida stavební spořitelna, a.s. | 15 May 2011 |
| ATM placement contract no. 2004/2011/9526(ATM services at Kounicova 29, Brno) | Modrá pyramida stavební spořitelna, a.s. | 3 Oct 2011 |
| ATM placement contract no. 20076/0000 (ATM services at Jindřišská ul. 17, č.p. 889, Prague 1) | Modrá pyramida stavební spořitelna, a.s. | 27 Feb 2012 |
| ATM placement contract no. 20162/0000 (ATM services at Bělehradská 128, č.p. 222, Prague 2) | Modrá pyramida stavební spořitelna, a.s. | 02 Apr 2012 |
| Group co-operation agreement under Sec. 5a of VAT Act No. 235/2004 Coll., as amended, including amendments nos. 1 and 2 (co-operation and payment for representation) | Modrá pyramida stavební spořitelna, a.s. | 27 Nov 2008, Amendment no. 1 of 22 Oct 2009, Amendment No. 2 of 22 Aug 2014 |
| Service level agreement (co-operation in the area of accounting and reporting, accounting and supplementary information for the needs of KB Group consolidated accounts) | Modrá pyramida stavební spořitelna, a.s. | 10 Dec 2014 in effect since 1 Jan 2015 |
| Contract for the use of KB's sales network (including amendments nos. 1, 2, 3 and 4) (intermediation of deals – building saving contracts) | Modrá pyramida stavební spořitelna, a.s. | 1 Mar 2005, Amendment no. 1 of 12 Jun 2009, Amendment no. 2 of 30 Sep 2010, Amendment no. 3 of 1 Oct 2011, Amendment no. 4 of 30 Apr 2014, Amendment no. 5 of 30 Jan 2015 |
| Confidentiality agreement – Quadrilateral agreement | Modrá pyramida stavební spořitelna, a.s. BHW Holding AG and Česká pojišťovna, a.s. | 11 Aug 2006 |
| Co-operation agreement – Client scoring | Modrá pyramida stavební spořitelna, a.s. | 31 Aug 2007 |
| Framework agreement from personal data processing (KB as administrator, MPSS as processor) since 30 May 2009 (personal data processing) | Modrá pyramida stavební spořitelna, a.s. | 30 May 2009 |
| Framework agreement from personal data processing (MPSS as administrator, KB as processor) since 30 May 2009, including Amendment no. 1 of 12 Sep 2011 (personal data processing) | Modrá pyramida stavební spořitelna, a.s. | 30 May 2009, Amendment no. 1 of 12 Sep 2011 |
| Agreement on KB call centre services of 1 Jan 2010, including cost re-invoicing from KB to MPSS in 2015<br>KB call centre services MPSS, including marketing cost re-invoicing from KB to MPSS in 2016 | Modrá pyramida stavební spořitelna, a.s. | 1 Jan 2010, Amendment no. 1 of 1 Sep 2016 |
| Separate distribution agreement (Perfektní půjčka) of 1 Apr 2011, including amendments nos.1, 2 and 3 (loan brokerage) | Modrá pyramida stavební spořitelna, a.s. | 1 Apr 2011, Amendment no. 1 of 31 Jan 2013, Amendment No. 2 of 21 Jan 2014, Amendment No. 3 of 29 May 2014 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Separate distribution agreement (MůjÚčet, G2.2) of 1 Apr 2011, including amendments nos. 1, 2, 3, 4 and 5 (service procurement under the contract) | Modrá pyramida stavební spořitelna, a.s. | 1 Apr 2011, Amendment no. 1 of 20 Apr 2012, Amendment no. 2 of 31 Jan 2013, Amendment no. 3 of 29 May 2014, Amendment no. 4 of 29 May 2014, Amendment no. 5 of 21 Oct 2014, Amendment no. 6 of 10 Nov 2015, Amendment no. 7 of 30 Nov 2015, Amendment no. 8 of 15 Aug 2016 |
| Separate distribution agreement (A karta, Lady karta, Kreditní karta VISA Elektron) of 1 Apr 2011, including amendments nos.1, 2 and 3 (service procurement under the contract) | Modrá pyramida stavební spořitelna, a.s. | 1 Apr 2011, Amendment no. 1 of 31 Jan 2013, Amendment no. 2 of 21 Jan 2014, Amendment no. 3 of 29 May 2014a Amendment no. 4 of 10 Nov 2015 |
| Separate distribution agreement (mortgage and pre-mortgage loans since 9 Sep 2011, including amendments nos. 1 and 2 (loan procurement under the contract) | Modrá pyramida stavební spořitelna, a.s. | 9 Sep 2011, Amendment no. 1 of 19 Dec 2011, Amendment no. 2 of 31 Jan 2013, Amendment no. 3 of 10 Nov 2015 Amendment no. 4 of 1 Jan 2016 |
| Agreement for co-operation in the performance of contract for employee group risk insurance no. 3280000000 in the wording of Amendment no. 1 of 29 Jun 2012.HR-Accession to the insurance contract made between Komerční pojišťovna, a.s. (insurer) and Modrá pyramida stavební spořitelna, a.s. (policy holder). The insurance also applies to MPSS employees with effect since 1 Feb 2012. The insured risk concerns employee's death. | Modrá pyramida stavební spořitelna, a.s., Komerční pojišťovna a.s. | 10 Sep 2012 |
| Framework agreement for the provision of better conditions to KB and AG Group employees – MPSS building savings plan holders | Modrá pyramida stavební spořitelna, a.s. | 1 Nov 2013 |
| Co-operation agreement, including Amendment no. 1, including the marketing cost re-invoicing in 2016 from MPSS to KB and from KB to MPSS | Modrá pyramida stavební spořitelna, a.s. | 31 Jan 2013, Amendment no. 1 of 16 May 2015 |
| Distribution agreement for products "Úvěry pro bytová družstva a společenství vlastníků bytových jednotek," including Amendment no. 1 (procurement of loans to housing co-operatives and apartment owners associations) | Modrá pyramida stavební spořitelna, a.s. | 1 Nov 2013, Amendment no. 1 of 10 Nov 2015 |
| Distribution agreement concerning the consumer loan product | Modrá pyramida stavební spořitelna, a.s. | 18 Dec 2014 |
| Framework contract for employee temporary assignment, including Amendment no. 1; reimbursement of costs incurred in connection with employee temporary assignment | Modrá pyramida stavební spořitelna, a.s. | 1 Dec 2006, Amendment No. 1 31 Jul 2007 |
| Mutual co-operation agreement of 31 Aug 2007 including Amendment no. 1 (MPSS employee benefits in KB) | Modrá pyramida stavební spořitelna, a.s. | 1 Aug 2007, Amendment No. 1 of 1 Jul 2010 |
| Lease agreement – Parking places in a CMP garage, including Amendment no. 1 | Modrá pyramida stavební spořitelna, a.s. | 31 Jan 2007, Amendment no. 1 of 30 Apr 2013 |
| Confidentiality agreement relating to "HP OV SD license agreement" | Modrá pyramida stavební spořitelna, a.s. | 9 Feb 2009 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Agreement to reimburse costs of licence use (replacing the 2007 oral agreement to reimburse costs of licence use), including Amendment no. 1 (payment of the price of the service and provision of co-operation) | Modrá pyramida stavební spořitelna, a.s. | 28 May 2009, Amendment no. 1 of 11 Feb 2010, validity extended orally also in 2016 (in 2017 there will be a new contract) |
| Lease of non-residential premises and payment of relating services (Uherský Brod) | Modrá pyramida stavební spořitelna, a.s. | 20 Nov 2008 |
| Confidentiality agreement relating to “Service agreement – Outsourcing (HR services)” | Modrá pyramida stavební spořitelna, a.s. | 27 Apr 2010 |
| Service agreement – Outsourcing (HR services), including Amendment no. 1 | Modrá pyramida stavební spořitelna, a.s. | 30 Nov 2010, Amendment no. 1 of 20 Dec 2013 |
| Confidentiality agreement relating to “Contract of co-operation in sourcing and procurement” – HR services | Modrá pyramida stavební spořitelna, a.s. | 9 Jul 2010 |
| Accession to the rules of co-operation between KB and FG members FS in the area of sourcing and procurement of 16 Sep 2010 | Modrá pyramida stavební spořitelna, a.s. | 16 Sep 2010 |
| Agreement on the organisation of periodic control of 17 Dec 2010, including Amendment no. 1 | Modrá pyramida stavební spořitelna, a.s. and Société Générale S.A. | 17 Dec 2010, Amendment of 17 Oct 2012 |
| Framework service agreement of 24 Jan 2011, including Amendment no. 1 | Modrá pyramida stavební spořitelna, a.s. | 24 Jan 2011, Amendment no. 1 of 11 Oct 2011 |
| Service agreement – Outsourcing – Data warehouse of 30 Jun 2011, including amendments nos.1, 2, 3, 4 and 5 | Modrá pyramida stavební spořitelna, a.s. | 30 Jun 2011, Amendment no. 1 of 15 Oct 2011, Amendment no. 2 of 13 May 2013, Amendment no. 3 of 31 Dec 2013, Amendment no. 4 of 3 Nov 2014, Amendment no. 5 of 22 Jan 2016 |
| Separate agreement no. 2 of 31 Oct 2011, including Amendment no. 1 under IT service framework agreement of 24 Jan 2011 | Modrá pyramida stavební spořitelna, a.s. | 31 Oct 2011, Amendment no. 1 of 22 Dec 2016 |
| Separate agreement no. 3 of 31 Oct 2011 under IT service framework agreement of 24 Jan 2011 | Modrá pyramida stavební spořitelna, a.s. | 31 Oct 2011 |
| Separate agreement no. 4 of 31 Oct 2011 under IT service framework agreement of 24 Jan 2011, including Amendment no. 1 of 5 Oct 2012 | Modrá pyramida stavební spořitelna, a.s. | 31 Oct 2011, Amendment no. 1 of 5 Oct 2012 |
| Separate agreement no. 1 of 31 Nov 2011 under IT service framework agreement of 24 Jan 2011, including Amendment no. 1 of 5 Oct 2012 and Amendment No. 2 of 1 Jan 2014 | Modrá pyramida stavební spořitelna, a.s. | 31 Nov 2011, Amendment no. 1 of 5 Oct 2012 Amendment no. 2 of 01 Jan 2014 |
| Separate agreement No. 5 of 2011 relating to the IT service framework agreement (notification services – SMS gateway) | Modrá pyramida stavební spořitelna, a.s. | 29 Jun 2012 |
| Service agreement – Outsourcing. Assessment of risks relating to MPSS real estate in KB’s system | Modrá pyramida stavební spořitelna, a.s. | 20 Dec 2011 |
| Agreement on KB-MPSS risk management co-operation and relating SLA (8) | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on scoring calculator for MPSS | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on pre-Scoring of clients and negative information delivery | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on scoring model for HC and AO(BD/SVJ scoring model) | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on delivery of inputs for real estate revaluation | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on Exchange of Fraud Lists | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on co-operation on IRBA implementation in MPSS | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| SLA – Agreement on data administration and delivery for claim reporting | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| SLA – Agreement on risk services remuneration(price for risk management co-operation services) | Modrá pyramida stavební spořitelna, a.s. | 31 Mar 2014 |
| Agreement to enter into a lease of non-residential premises and payment of relating services (back-up worksite at Prague 5 –Stodůlky) | Modrá pyramida stavební spořitelna, a.s. | 1 Sep 2014 |
| Lease of non-residential premises and payment of relating services (back-up worksite at Prague 5 –Stodůlky) | Modrá pyramida stavební spořitelna, a.s. | 1 Sep 2014 |
| Lease of non-residential premises and payment of relating services (Antala Staška 2059, Prague 4) | Modrá pyramida stavební spořitelna, a.s. | 1 Dec 2014 |
| Lease of non-residential premises and payment of relating services (Kyjov) | Modrá pyramida stavební spořitelna, a.s. | 27 Jul 2015 |
| Agreement – Services PD/LGD models for RWA calculation | | |
| (models for MPSS loan providing) | Modrá pyramida stavební spořitelna, a.s. | 18 Dec 2014 |
| Insurance contract no. 7720935797 – Property risk insurance from 1 Jan 2016 to 31 Dec 2017 | Modrá pyramida stavební spořitelna, a.s. | 2016 |
| Agreement to perform under of group insurance agreement of works-related accident and occupational disease insurance for Members of Board of Directors of the financial group of Komerční banka/Société Générale N 333000000 from 1 Jul 2015 to 30 Jun 2016 | Modrá pyramida stavební spořitelna, a.s. | 2016 |
| Agreement to perform under of group insurance agreement of works-related accident and occupational disease insurance for Members of Board of Directors of the financial group of Komerční banka/Société Générale N 334000000 from 1 Jul 2016 to 30 Jun 2017 | Modrá pyramida stavební spořitelna, a.s. | 2016, 2017 |
| Agreement – Outsourcing of HR services (excluding Payroll) | Modrá pyramida stavební spořitelna, a.s. | 29 Jan 2016 |
| Contract for negative information exchange within KB/SG FG in the Czech Republic | Modrá pyramida stavební spořitelna, a.s. | 19 Feb 2016 |
| Contract for the personal data protection and provision (debt collection) | Modrá pyramida stavební spořitelna, a.s. | 29 Feb 2016 |
| Memorandum of understanding – Co-operation within KB FG in claim mass assignment | Modrá pyramida stavební spořitelna, a.s. | 3 Mar 2016 |
| Contract for the payment of insurance premium and of insurance broker's commission | Modrá pyramida stavební spořitelna, a.s. | 30 Jun 2016 |
| Assignment and confirmation of user rights expiration (ORACLE) | Modrá pyramida stavební spořitelna, a.s. | 31 Oct 2016 |
| Memorandum of understanding ORACLE license transfer | Modrá pyramida stavební spořitelna, a.s. | 31 Oct 2016 |
| Agreement for cost re-invoicing from KB to MPSS | Modrá pyramida stavební spořitelna, a.s. | 2016 |
| Lease of non-residential premises and payment of relating services + 4 amendments | NP 33, s.r.o. | 18 Nov 2013<br>30 Dec 2014<br>19 Feb 2015<br>31 Dec 2015<br>20 Dec 2016 |
| Service contract – Outsourcing (support services) | NP 33, s.r.o. | 18 Nov 2013 |
| Service contract – Outsourcing (accounting services) | NP 33, s.r.o. | 3 Nov 2014 |
| VAT Group co-operation agreement | NP 33, s.r.o. | 8 Jun 2014 |
| Contract for the payment of insurance premium and of insurance broker's commission | NP 33, s.r.o. | 8 Jun 2016 |
| Service level agreement | Protos, uzavřený investiční fond, a.s. | 8 Dec 2014 |
| Administration order | Protos, uzavřený investiční fond, a.s. | 9 Dec 2015 |
| Global terms of business | SG, Newedge Group (Frankfurt branch) – originally | 31 Dec 2010 |
| Transfer of futures accounts | SG, Newedge Group (Frankfurt branch) – originally | 26 Jun 2009 |
| Novation agreement | SG, Newedge UK Financial Limited – originally | 7 Oct 2011 |
| Newedge EMIR reporting services agreement | SG, Newedge UK Financial Limited – originally | 3 Feb 2014 |
| Agreement + Application for client + Representation letter | SG, Newedge – originally ;<br>Eurex Clearing AG (Frankfurt) | 26 Jun 2014 |
| Clearing Agreement (Appendix 4 - FOA Clearing Module) | SG, Newedge UK Financial Limited – originally | 23 Apr 2015 |
| EORS acceptance letter | SG, Newedge – originally | 2 Apr 2015 |
| Lease of non-residential premises and payment of relating services + 1 amendment – Ostrava | SG Equipment Finance Czech Republic s.r.o. | 1 Dec 2014 |
| Lease of non-residential premises, movable assets and payment of relating services + 2 amendments – Prague | SG Equipment Finance Czech Republic s.r.o. | 21 Oct 2013 |
| Lease of non-residential premises and payment of relating services – Pilsen | SG Equipment Finance Czech Republic s.r.o. | 30 Sep 2015 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Lease of non-residential premises, movable assets and payment of relating services – Ústí nad Labem | SG Equipment Finance Czech Republic s.r.o. | 28 Jan 2016 |
| Lease of non-residential premises and payment of relating services – České Budějovice | SG Equipment Finance Czech Republic s.r.o. | 27 May 2011 |
| Sublease agreements for parking places – Prague | SG Equipment Finance Czech Republic s.r.o. | 30 Oct 2013 |
| Lease of non-residential premises and payment of relating services + 2 amendments – Bratislava | SG Equipment Finance Czech Republic s.r.o. | 30 Oct 2012 |
| Framework agreement for the rental of employee-driven motor vehicles | SG Equipment Finance Czech Republic s.r.o. | 21 Oct 2014 |
| Individual pricing agreement | SG Equipment Finance Czech Republic s.r.o. | 15 Dec 2006 |
| Individual pricing agreement | SG Equipment Finance Czech Republic s.r.o. | 27 Jun 2014 |
| Framework agreement to provide financial services (7181080BE0000) + 11 amendments | SG Equipment Finance Czech Republic s.r.o. | 20 Dec 2010 |
| Framework service agreement | SG Equipment Finance Czech Republic s.r.o. | 14 Dec 2010 |
| Framework agreement to provide financial services (RAS) reg. No. 9900022630000 + 4 amendments | SG Equipment Finance Czech Republic s.r.o. | 29 Sep 2014 |
| Framework agreement to provide financial services (11/12/BA) + 1 amendment | SG Equipment Finance Czech Republic s.r.o. | 6 Aug 2012 |
| Separate agreement No. 1 – Provision of technical infrastructure services, connectivity services | SG Equipment Finance Czech Republic s.r.o. | 1 Jun 2012 |
| Separate agreement No. 2 – Provision of technical infrastructure services, physical hosting of equipment | SG Equipment Finance Czech Republic s.r.o. | 1 Jun 2012 |
| Separate agreement No. 3 – Provision of technical infrastructure services, IT infrastructure hosting (VMWare) | SG Equipment Finance Czech Republic s.r.o. | 1 Jun 2012 |
| Co-operation agreement – Jobs | SG Equipment Finance Czech Republic s.r.o. | 14 Apr 2010 |
| Service contract – Access to C4M | SG Equipment Finance Czech Republic s.r.o. | 12 Oct 2011 |
| Agreement on reimbursement of cost | SG Equipment Finance Czech Republic s.r.o. | 13 Dec 2013 |
| Service level agreement | SG Equipment Finance Czech Republic s.r.o. | 1 Sep 2014 |
| Service agreement | SG Equipment Finance Czech Republic s.r.o. | 30 Oct 2013 |
| Service agreement – Outsourcing (HR services) | SG Equipment Finance Czech Republic s.r.o. | 15 Jun 2011 |
| Agreement on the Organisation of Periodic Control + 1 amendment | SG Equipment Finance Czech Republic s.r.o. + Société Générale | 26 Jan 2011 |
| Mutual co-operation agreement | SG Equipment Finance Czech Republic s.r.o. | 1 Aug 2007 |
| Agreement on KB Call Centre services | SG Equipment Finance Czech Republic s.r.o. | 31 Dec 2009 |
| Personal data processing framework agreement between KB and SGEF | SG Equipment Finance Czech Republic s.r.o. | 1 Dec 2010 |
| Co-operation agreement | SG Equipment Finance Czech Republic s.r.o. | 30 Jun 2010 |
| Rules of co-operation between KB and Group members in the area of sourcing and acquisitions | SG Equipment Finance Czech Republic s.r.o. | 20 Sep 2010 |
| Agreement for co-operation in performance of the contract for employee group risk insurance | SG Equipment Finance Czech Republic s.r.o. | 20 Aug 2012 |
| Confidentiality agreement | SG Equipment Finance Czech Republic s.r.o. | 1 Dec 2010 |
| Confidentiality agreement | SG Equipment Finance Czech Republic s.r.o. | 9 Jul 2010 |
| Agreement on framework insurance contract no. 7720802024 + 1 amendment | SG Equipment Finance Czech Republic s.r.o. | 10 Feb 2014 |
| Contact bank agreement | SG Private Wealth Management S.A. | 29 Apr 2016 |
| Distribution agreement | SG Private Wealth Management S.A. | 30 Apr 2016 |
| Terms for Business for Treasury Equities, Derivatives and Fixed Income Products | SG London | 4 Oct 2007 |
| Appointment of process agent for Komerční banka, a.s | SG London | 6 May 2011 |
| Appointment of process agent for Komerční banka, a.s | SG London | 14 Sep 2011 |
| Appointment of process agent for Komerční banka, a.s. | SG London | 23 Jan 2013 |
| Appointment of process agent for Komerční banka a.s., including an amendment | SG New York | 12 Jan 2004 |
| USD clearing services agreement for Komerční banka | SG New York | 7 Aug 2015 |
| 6x Sending reports to SG Economic, Equity and Strategy Research | SG Paris | 2002 |
| Analytical coverage of the Czech Republic for the needs of SG Research | SG Paris | 2002 |
| Exchange of opinions on the macroeconomic situation | SG Paris | 2002 |
| Exchange of opinions on economic development with SG analysts | SG Paris | 2002 |
| Exchange of opinions on financial markets development | SG Paris | 2002 |
| Revisions of written texts | SG Paris | 2012 |
| Inserting KB's analytical reports, economic and strategic analyses in SG's database of analyses | SG Paris | 2002 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| ISDA master agreement (intermediation of transactions with all types of derivatives on the interbank market) | SG Paris | 23 Nov 1998 |
| Global master agreement (framework agreement to close repo and buy-sell-back deals) | SG Paris | 4 Nov 2003 |
| Contract on the provisions of services relating to securities (custody contract) | SG Paris | 19 Jul 2004 |
| General terms and conditions for use of e-confirmation | SG Paris | 10 Feb 2005 |
| Sub-custodian service agreement | SG Paris | 16 Sep 2005 |
| Sub-custodian service agreement | SG Paris | 12 Dec 2005 |
| Agreement relating to the intermediation in the sale of market products linked to investment banking activity in the Czech Republic | SG Paris | 22 Dec 2006 |
| Agreement relating to the use of the Glass Custody Tool | SG Paris | 8 Mar 2007 |
| Custodian services agreement | SG Paris | 8 Mar 2007 |
| ISDA master agreement (emission allowances) | SG Paris | 23 Nov 2007 |
| Co-operation agreement (framework conditions of co-operation in the area of internal audit) | SG Paris | 31 Mar 2008 |
| Service level agreement on credit RWA calculation + Amendment no. 1 | SG Paris | 20 Jul 2008<br>18 Dec 2013 |
| Credit support annex (financial collateral transactions) | SG Paris | 27 Oct 2009 |
| Custody contract | SG Paris | 19 Feb 2010 |
| Intra-group corporate services fees agreement | SG Paris | 11 Jun 2010 |
| Intra-group IT services fees agreement | SG Paris | 11 Jun 2010 |
| Bilateral agreement on rate reset and payment notices produced by the ISDA Operations Committee | SG Paris | 6 Oct 2010 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, PEMA Polska | 15 Feb 2011 |
| Contract concerning T3C competence centres, including 1 amendment | SG Paris | 22 Feb 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, ALD Automotive Hungary | 28 Feb 2011 |
| Custody contract | SG Securities Services | 8 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, PEMA Prague | 11 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, PEMA Slovakia | 11 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, ALD Automotive Polska | 28 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, SG Equipment Leasing Hungary | 29 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, SG Vehicle Finance Hungary Plc. | 29 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, SGEF Hungary Plc. | 29 Mar 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, ALD Automotive s.r.o. | 19 Apr 2011 |
| Agreement on the organisation of periodic control, including 1 amendment. | SG Paris, ALD Automotive UAB | 17 May 2011 |
| Agreement on the organisation of periodic control, including 1 amendment. | SG Paris, ALD Automotive SIA | 23 May 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, ALD EESTI AS | 7 Jun 2011 |
| Agreement on the organisation of periodic control, including 1 amendment | SG Paris, SG Equipment Leasing Polska | 13 Sep 2011 |
| Agreement on the organisation of periodic control | SG Paris, SG Warszawa | 30 Dec 2011 |
| Amendment to Service level agreement (backup procedure conditions) | SG Paris | 13 Mar 2013 |
| Agreement on the organisation of periodic control | SG Paris, Komerční pojišťovna, a.s. | 24 Jun 2013 |
| Amendment for incoming or outgoing XML SEPA credit transfer and SEPA direct debit messages – Euro account maintenance & clearing service agreement | SG Paris | 30 Dec 2013 |
| IT services agreement | SG Paris | 1 Jan 2014 |
| Amendment for incoming or outgoing XML SCT (SEPA credit transfer) and SDD (SEPA direct debit) messages | SG Paris | 13 Jan 2014 |
| Service level agreement (SGCIB Global Applications) | SG Paris | 7 Aug 2014 |
| Client service agreement – Regulatory capital calculation and allocation of operational risk | SG Paris | 26 Sep 2014 |
| Consent form (derivatives trade reporting) | SG Paris | 30 Sep 2015 |
| Agreement relating to the use of SGSS Gallery for custody reports | SG Paris | 21 Oct 2015 |
| International Sogexpress agreement | SG Paris | 24 Jun 2016 |
| Service level agreement | SG Paris | 27 Oct 2016 |
| Custody account agreement | SG Warszawa | 13 Nov 2009 |
| Service level agreement (custody services) | SG Warszawa | 13 Nov 2009 |
| Brokerage conformity agreement (distribution agreement) | SGAM AI | 10 Jul 2004 |

| Title of contract (or subject matter of contract – if not clear from the title) | Contracting party | Date of contract |
|---|---|---|
| Introduction broker agreement (SGAM funds purchase brokerage) | SGAM AI | 19 Feb 2007 |
| Custody agreement | SG Splitska Banka | 26 May 2010 |
| Custody agreement | SG Splitska Banka | 28 May 2012 |
| Service level agreement relating to a custody agreement | SG Splitska Banka | 27 Nov 2013 |
| Agreement on the organisation of periodic control | SG Splitska Banka | 31 Jan 2015 |
| UCITS V addendum | SG Splitska Banka | 13 Oct 2016 |
| EURO medium-term note master purchase agreement (securities trading) | SGAM Banque | 13 Jul 2007 |
| Novation agreement (revision of securities trading conditions) | SGAM Banque | 29 Mar 2010 |
| ISDA master agreement (FX transactions framework agreement) | SG Bank & Trust (SGBT) | 7 May 2010 |
| Sub-custody & brokerage service agreement | SG Bank & Trust (SGBT) | 1 Apr 2011 |
| Custody contract | SG Montenegro | 2 Dec 2014 |
| Custody contract | SKB Banka | 28 May 2015 |
| Custody agreement | SKB Banka | 14 Sep 2016 |
| Service level agreement | SKB Banka | 30 Sep 2016 |
| Lease of non-residential premises and payment of relating services + 4 amendments | VN 42, s.r.o. | 18 Nov 2013<br>14 Dec 2013<br>22 Dec 2014<br>9 and 19 Feb 2015<br>31 Dec 2015 |
| Service agreement – Outsourcing (support services) | VN 42, s.r.o. | 18 Nov 2013 |
| Service agreement – Outsourcing (accounting services) | VN 42, s.r.o. | 3 Nov 2014 |
| VAT group co-operation agreement | VN 42, s.r.o. | 15 Jul 2014 |
| Contract for the payment of insurance premium and of insurance broker’s commission | VN 42, s.r.o. | 8 Jun 2016 |

## C. Assessment of advantages and disadvantages arising from the relations within the Group and an assessment as to injury

**Advantages and disadvantages arising from the relations within the Group**

The SG Group is diversified and provides universal banking services. The entire Group takes advantage of mutual synergistic effects, including product pooling, a strong international brand and SG's know-how. KB, for example, uses SG's global network to provide Trade Finance Products while co-operating in the payments area and using SG's wide network. Thanks to the Group, it is possible for KB to use the global cash pooling network, offer transnational solutions in the cash management area and offer SG products. KB benefits from SG's global experience in the Global Finance Platform area. The advantages from the KB's integration into the SG Group contribute to the KB's positive financial results.

**Assessment of injury**

The KB's Board of Directors has reviewed all arrangements between the KB and the companies that were part of the Group during the 2016 reporting period and states that the KB incurred no injury as a result of any contracts, agreements or any other legal acts in effect or adopted by the KB or as a result of any other influence otherwise exerted by SG in the reporting period.

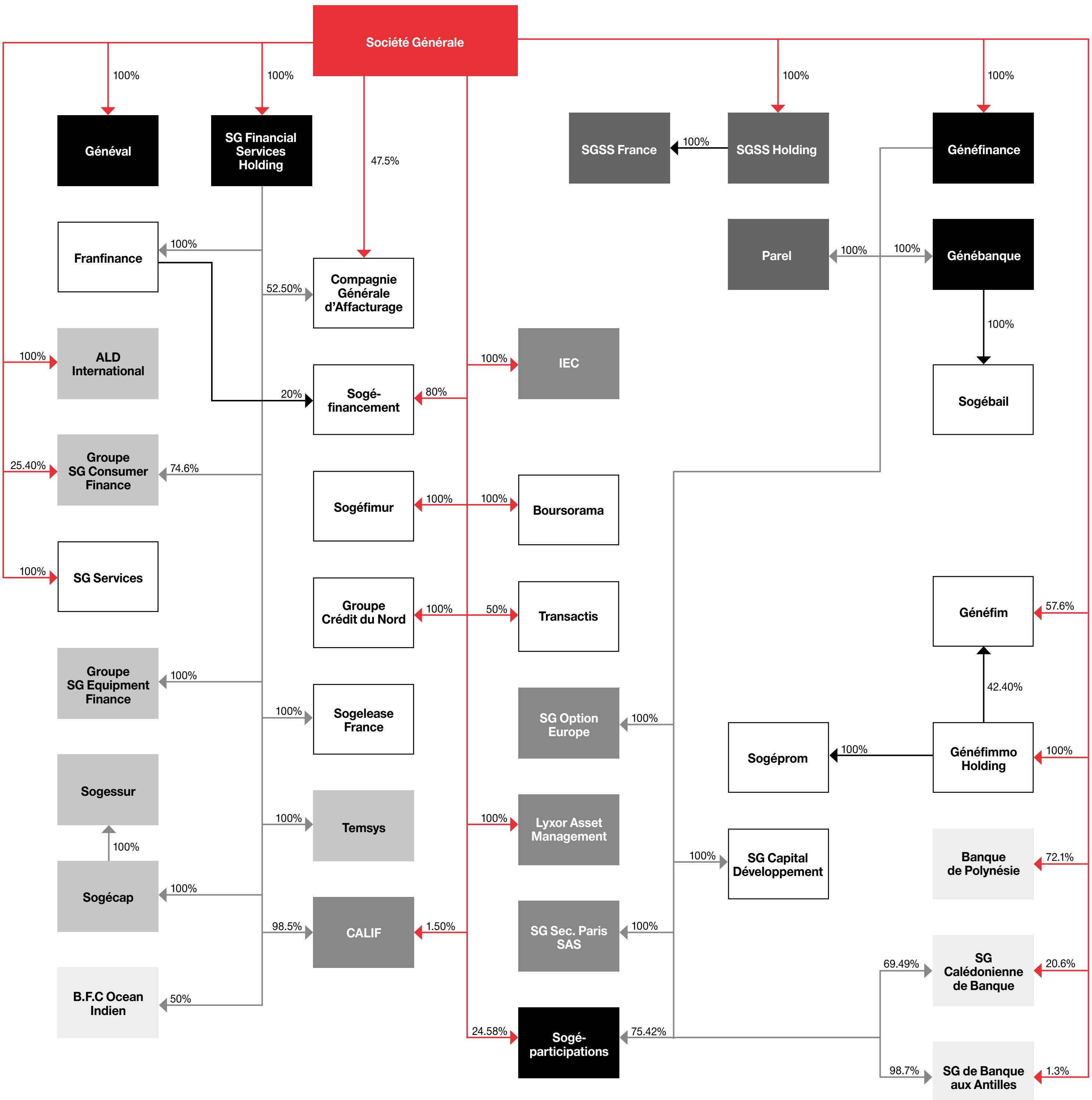
In Prague on 7 March 2017

**Albert Le Dirac'h**
Chairman of the Board of Directors
Komerční banka, a.s.

**Peter Palečka**
Member of the Board of Directors
Komerční banka, a.s.

# The structure of relationships SG Group – % of the share capital

## FRANCE



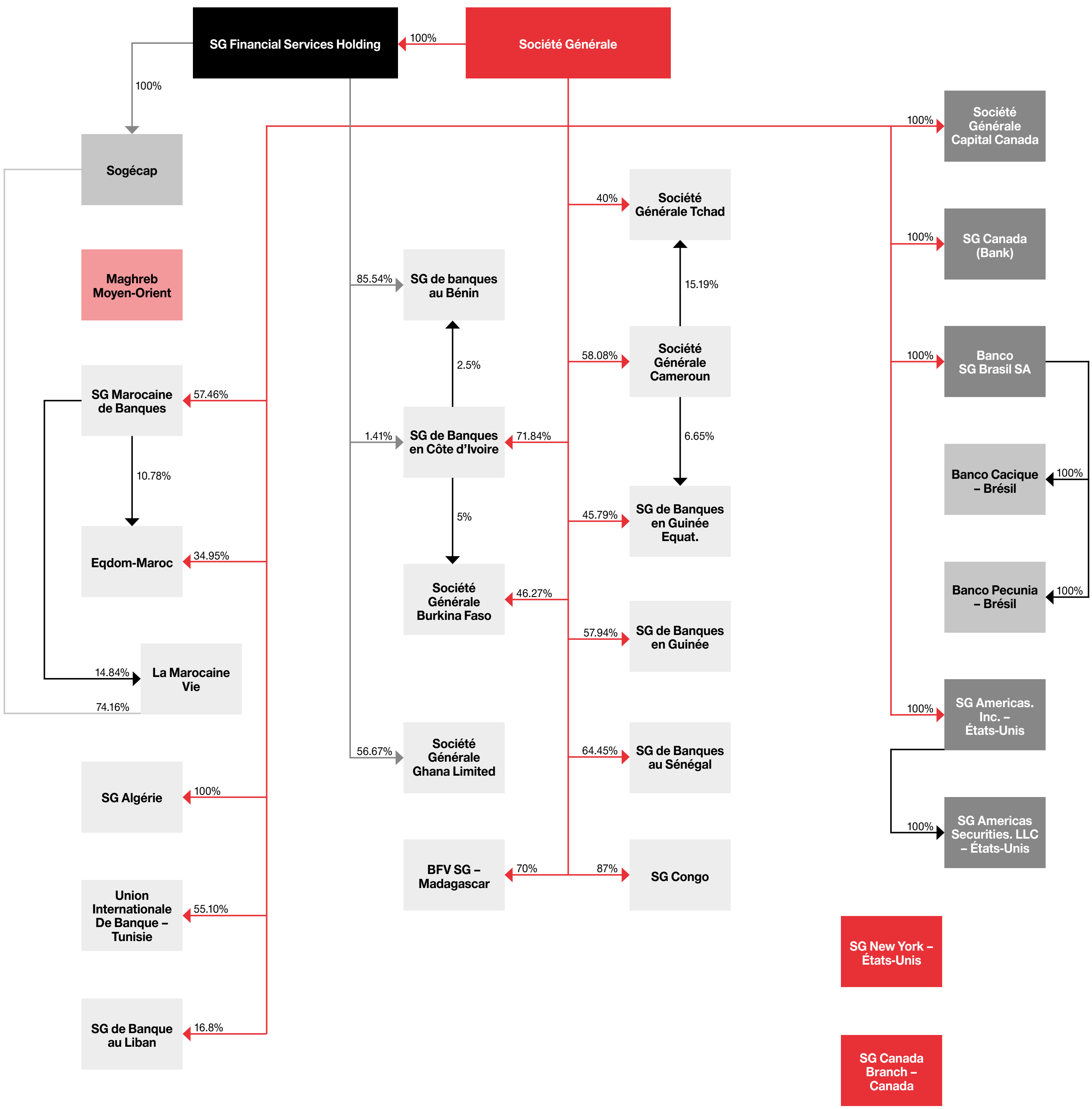

Note: Percentage of share capital and participation in voting rights may differ

CONSOLIDATED FINANCIAL STATEMENTS
SEPARATE FINANCIAL STATEMENTS
SECURITIES ISSUED BY KB
LEGAL INFORMATION
AFFIDAVITS
GLOSSARY

# EUROPE


Note: Percentage of share capital and participation in voting rights may differ.

# AFRICA AND AMERICAS




Note: Percentage of share capital and participation in voting rights may differ.

# ASIA AND AUSTRALIA


Note: Percentage of share capital and participation in voting rights may differ.

# Report of the Supervisory Board

Throughout 2016, the Supervisory Board carried out its tasks as defined by law and by the Articles of Association. It supervised the exercise of powers by the Board of Directors, checked the accounts and other financial documents of Komerční banka, a.s., ascertained the effectiveness of the management and control system and made its regular assessments.

Having checked the Bank's annual (separate) and consolidated financial statements for the period from 1 January 2015 to 31 December 2016, the Supervisory Board reports that the accounts and financial documents were maintained in a transparent manner and in accordance with generally binding regulations providing for banks book-keeping. The accounts and financial documents show all important aspects of the financial situation of Komerční banka, a.s., and the financial statements worked out on their basis present a true and fair view of the Bank's and Group's accounting and financial situation.

The Supervisory Board recommends that the general meeting approve the annual (separate) and consolidated financial statements and the distribution of profit for the year 2016 as proposed by the Board of Directors of the Bank.

The Supervisory Board checked the Report on Relations among Related Entities in 2016 drawn up under § 82 et seq. of the Corporations Act, and states on the basis of the presented documents that, during the accounting period from 1 January 2016 to 31 December 2016, Komerční banka, a.s. did not suffer any harm resulting from the contracts, agreements, other legal acts made or adopted by the Bank or from any influence otherwise exerted by Société Générale.

Prague, 16 March 2017

On behalf of the Supervisory Board of Komerční banka, a.s.:

**Jean-Luc Parer**
Chairman of the Supervisory Board

# Management affidavit

To the best of our knowledge, we believe that this annual report gives a fair and true view of the Bank's and Group's financial position, business activities and results from the year 2016, as well as of the outlook for the development of the Bank's and Group's financial situation, business activities and results.

Prague, 21 March 2017

Signed on behalf of the Board of Directors:

**Albert Le Dirac'h**
Chairman of the Board of Directors and Chief Executive Officer

**Libor Löfler**
Member of the Board of Directors and Senior Executive Director, Chief Operating Officer

# Independent Auditor's Report to the Shareholders of Komerční banka, a.s.

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Tax ID. No.: CZ49620592

# INDEPENDENT AUDITOR'S REPORT

To the Shareholders of Komerční banka a.s.

Having its registered office at: Na Příkopě 33 č.p. 969, 114 07, Prague 1

**Report on the Audit of the Consolidated and Separate Financial Statements**

Opinion

We have audited the accompanying consolidated financial statements of Komerční banka, a.s. and its subsidiaries (hereinafter also the "Group") and separate financial statements of Komerční banka, a.s. (hereinafter also the "Company") prepared on the basis of International Financial Reporting Standards ("IFRS") as adopted by the EU.

The consolidated financial statements comprise the consolidated statement of financial position as at 31 December 2016, consolidated statement of income and consolidated statement of comprehensive income, consolidated statement of changes in equity and consolidated statement of cash flows for the year then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies and other explanatory information (the "Consolidated Financial Statements").

The separate financial statements comprise the separate statement of financial position as at 31 December 2016, separate statement of income and separate statement of comprehensive income, separate statement of changes in equity and separate statement of cash flows for the year then ended, and notes to the separate financial statements, including a summary of significant accounting policies and other explanatory information (the "Separate Financial Statements").

In our opinion:

- The accompanying Consolidated Financial Statements give a true and fair view of the financial position of the Group as at 31 December 2016, and of their financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU;
- The accompanying Separate Financial Statements give a true and fair view of the financial position of the Company as at 31 December 2016, and of its financial performance and their cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the EU.

Basis for Opinion

We conducted our audit in accordance with the Act on Auditors and Auditing Standards of the Chamber of Auditors of the Czech Republic, which are International Standards on Auditing (ISAs), as amended by the related application guidelines. Our responsibilities under this law and regulation are further described in the Auditor's Responsibilities for the Audit of the Consolidated and Separate Financial Statements section of our report. We are independent of the Group and the Company in accordance with the Act on Auditors and the Code of Ethics adopted by the Chamber of Auditors of the Czech Republic and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the Consolidated and Separate Financial Statements of the current period. These matters were addressed in the context of our audit of the Consolidated and Separate Financial Statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

| Key audit matter | Related audit procedures |
|---|---|
| Allowances for the loans and advances to customers | |
| (Please refer to Notes 21 and 42A to the Consolidated Financial Statements and to Notes 21 and 41A to the Separate Financial Statements for the details)<br><br>At 31 December 2016, gross loans and advances to customers (hereinafter "loans") comprised of CZK 595,781 million and CZK 539,123 million for the Group and the Company respectively against which allowances for loans to customers (hereinafter "allowances") of CZK 15,583 million and CZK 11,980 million were recorded, respectively. The directors exercise significant judgment when determining both when and how much to record as allowances.<br><br>The Group uses one of three methods to assess the amount of allowances:<br><br>1. For larger, individually significant loans classified as default (Substandard, Doubtful and Loss loans based on the Czech National Bank's classification) the allowances are assessed on an individual basis requiring management to monitor the borrower's repayment abilities individually including the estimated value from the collateral foreclosure and expected duration of the recovery process etc.<br>2. For smaller, individually not significant impaired loans where the loans are homogeneous in nature (for example the consumer and mortgage loans to individuals and smaller corporate portfolios) the allowance is calculated by models using historical delinquency statistics.<br>3. Portfolio allowances are calculated for losses that have been incurred but have not been identified at the year-end. Portfolio allowances are held against non-impaired loans across all segments and calculated using models based on probabilities of default and loss given default as well as emergence periods between the impairment event occurring and an individual (1.) or model allowance for impaired loans (2.) being recognised.<br><br>Because of the significance of these judgements and the size of loans and advances to customers, the audit of allowances is a key audit matter. | We evaluated whether the internal impairment policies comply with the requirement of the relevant accounting standard (IAS 39).<br><br><u>Testing of internal controls</u><br><br>We tested the design and operating effectiveness of the key internal controls to determine which loans and advances to customers are impaired and allowances for those assets. Our procedures included testing:<br><br>• System-based and manual controls over the timely recognition of impaired loans and advances;<br>• Controls over the allowance calculation and allowance recording;<br>• Controls over collateral valuation estimate;<br>• The governance process of management validation of allowance calculations; and<br>• IT controls relating to access rights and change management of relevant IT applications with the assistance of our IT specialists.<br><br><u>Identification of impaired loans</u><br><br>We tested a sample of loans and advances (including loans that had not been identified by management as potentially impaired) to form our own assessment as to whether impairment events had occurred and to assess whether impairments had been identified in a timely manner.<br><br><u>Allowances for loans determined individually (1.)</u><br><br>For individually assessed loans we selected a sample of loans and, where we deemed them to be impaired, tested the estimation of the future expected cash flows from customers including from realisation of collateral held. This work involved assessing the work performed by external experts used by the Group to value the collateral or to assess the estimates of future cash flows. In some cases, we used our own industry experts, particularly in respect of commercial real estate, to assess the appropriateness of valuations and estimates used by the Group. Where we determined that a more appropriate assumption or input in provision measurement could be made, we recalculated the provision on that basis and compared the results in order to evaluate management estimate.<br><br><u>Allowances for loans determined using statistical models (2. and 3.)</u><br><br>For the allowances determined by models used by the Group, we were assessing, in cooperation with our credit risk specialists, the model methodology, the internal validation reports and results of the models back-testing for selected internal models. We assessed whether the modelling assumptions used considered all relevant risks, and whether the additional adjustments to reflect un-modelled risks |

| Key audit matter | Related audit procedures |
|---|---|
| | were reasonable in light of historical experience, economic climate, current operational processes and the circumstances of the customers as well as our own knowledge of practices used by other similar banks. On a sample basis, we evaluated the appropriateness of risk parameters used in the calculation of allowances. |
| Interest and fee income recognition | |
| (Please refer to Notes 5 and 6 to the Consolidated and Separate Financial Statements for the details)<br><br>For the year ended 31 December 2016 the interest income and similar income comprised of CZK 26,757 million and CZK 23,186 million for the Group and the Company respectively. Total fee and commission income for the same period comprised of CZK 7,914 million and CZK 6,865 million for the Group and the Company respectively. With the main source being customer loans and deposits these are the main contributors to the net operating income of the Company and the Group affecting the profitability.<br><br>While interest income is accrued over the expected life of the financial instrument, the recognition of fee income depends on the nature of the fees as follows:<br><br>• Fees that are directly attributable to the financial instrument are accrued over the expected life of such an instrument and are presented as interest income;<br>• Fees for services provided are recognised when service is provided and are presented as fee and commission income;<br>• Fees for the execution of an act are recognised when the act has been completed and are presented as fee and commission income.<br><br>Revenue recognition specifics, a high volume of individually small transactions which depends on data quality of interest and fee inputs and on IT solutions for their recording resulted in this matter being identified as a key audit matter. | We tested the design and operating effectiveness of the key internal controls and focused on:<br><br>• Assessment of interest/fees recognition during new product validation;<br>• Interest/fee inputs on customer loans and deposits, including authorisation of the changes in the interest and fee price list and authorisation of non-standard interest/fees;<br>• Recording of fee and interest income and management oversight; and<br>• IT controls relating to access rights and change management of relevant IT applications with the assistance of our IT specialists.<br><br>We performed the following procedures with regard to interest and fees revenue recognition:<br><br>• We evaluated the accounting treatment performed by the Company in respect of fees charged to clients to determine whether the methodology complies with the requirement of the relevant accounting standard (IAS 39).<br><br>We focused our testing on challenging the correct classification of:<br><br>• Fees that are identified as directly attributable to the financial instrument;<br>• Fees that are not identified as directly attributable to the financial instrument;<br>• We assessed the completeness and accuracy of data used for the calculation of interest using data analytics;<br>• We evaluated the mathematical formula used for accruing the relevant income over expected life of the loan. |

Other Information in the Annual Report

In compliance with Section 2(b) of the Act on Auditors, the other information comprises the information included in the Annual Report other than the Consolidated and Separate Financial Statements and auditor’s report thereon. The Board of Directors is responsible for the other information.

Our opinion on the Consolidated and Separate Financial Statements does not cover the other information. In connection with our audit of the Consolidated and Separate Financial Statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the Consolidated and Separate Financial Statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. In addition, we assess whether the other information has been prepared, in all material respects, in accordance with applicable law or regulation, in particular, whether the other information complies with law or regulation in terms of formal requirements and procedure for preparing the other information in the context of materiality, i.e. whether any non-compliance with these requirements could influence judgments made on the basis of the other information.

Based on the procedures performed, to the extent we are able to assess it, we report that:

- The other information describing the facts that are also presented in the Consolidated and Separate Financial Statements is, in all material respects, consistent with the Consolidated and Separate Financial Statements; and
- The other information is prepared in compliance with applicable law or regulation.

In addition, our responsibility is to report, based on the knowledge and understanding of the Group and the Company obtained in the audit, on whether the other information contains any material misstatement of fact. Based on the procedures we have performed on the other information obtained, we have not identified any material misstatement of fact.

Responsibilities of the Company's Board of Directors, Supervisory Board and Audit Committee for the Consolidated and Separate Financial Statements

The Board of Directors is responsible for the preparation and fair presentation of the Consolidated and Separate Financial Statements in accordance with International Financial Reporting Standards as adopted by the EU and for such internal control as the Board of Directors determines is necessary to enable the preparation of Consolidated and Separate Financial Statements that are free from material misstatement, whether due to fraud or error.

In preparing the Consolidated and Separate Financial Statements, the Board of Directors is responsible for assessing the Group's and the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the Board of Directors either intends to liquidate the Group or the Company or to cease operations, or has no realistic alternative but to do so.

The Supervisory Board and the Audit Committee are responsible for overseeing the Group and Company's financial reporting process.

Auditor's Responsibilities for the Audit of the Consolidated and Separate Financial Statements

Our objectives are to obtain reasonable assurance about whether the Consolidated and Separate Financial Statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these Consolidated and Separate Financial Statements.

As part of an audit in accordance with the above law or regulation, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the Consolidated and Separate Financial Statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control;
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's and the Company's internal control;
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by the Board of Directors;
- Conclude on the appropriateness of the Board of Directors' use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group's and the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the Consolidated and Separate Financial Statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Group or the Company to cease to continue as a going concern;

- Evaluate the overall presentation, structure and content of the Consolidated and Separate Financial Statements, including the disclosures, and whether the Consolidated and Separate Financial Statements represent the underlying transactions and events in a manner that achieves fair presentation;
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group and the Company to express an opinion on the Consolidated and Separate Financial Statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with the Board of Directors, the Supervisory Board and the Audit Committee regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide the Audit Committee with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with the Board of Directors, the Supervisory Board and the Audit Committee, we determine those matters that were of most significance in the audit of the Consolidated and Separate Financial Statements of the current period and are therefore the key audit matters. We describe these matters in our auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

**Report on Report on Relations among Related Entities (the "Report on Relations")**

We have reviewed the factual accuracy of the information included in the accompanying Report on Relations of Komerční banka, a.s. for the year ended 31 December 2016 which is included in this annual report on pages 259 to 282. This Report on Relations is the responsibility of the Company's Statutory Body. Our responsibility is to express our view on the Report on Relations based on our review.

We conducted our review in accordance with Auditing Standard 56 issued by the Chamber of Auditors of the Czech Republic. This standard requires that we plan and perform the review to obtain moderate assurance as to whether the Report on Relations is free of material factual misstatements. A review is limited primarily to inquiries of the Company's personnel and analytical procedures and examination, on a test basis, of the factual accuracy of information, and thus provides less assurance than an audit. We have not performed an audit of the Report on Relations and, accordingly, we do not express an audit opinion.

Nothing has come to our attention based on our review that indicates that the information contained in the Report on Relations of Komerční banka, a.s. for the year ended 31 December 2016 contains material factual misstatements.

The Company has decided not to disclose amounts under related party contracts citing business secrecy restrictions.

In Prague on 21 March 2017

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|---|---|
| Audit firm: | Statutory auditor: |
| Deloitte Audit s.r.o.<br>registration no. 079 | David Batal<br>registration no. 2147 |

# Glossary

**ATM**
An electronic telecommunications device that enables the customers of a financial institution to perform financial transactions, particularly cash withdrawal or money deposit, without the need for a human cashier or bank teller.

**Bank**
Komerční banka, a.s.

**Basel III**
The regulatory requirements in the European Union are established within the Basel III capital framework through Regulation No. 575/2013 on prudential requirements for credit institutions and investment firms (the Capital Requirements Regulation, or "CRR") and by Directive 2013/36/EU on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms (Capital Requirements Directive 4, or "CRD IV"). CRD IV was transposed into Czech law by an amendment to the Banking Act and publication of CNB Decree No. 163/2014 Coll.

**CRD IV**
Capital Requirements Directive  supervisory framework in the European Union which reflects the Basel II and Basel III rules on capital measurement and capital standards.

**CNB**
Czech National Bank

**Currency conversion rates**
Throughout this annual report, average currency exchange rates announced by the Czech National Bank are used for translation from foreign currencies of monetary values of flow variables (accruing over a period), such as revenues, costs or net profits. CNB's daily declared exchange rates are used for translation of monetary values of stock variables, such as balance sheet items. For example, CZK/EUR exchange rate of 27.025 is used for stock as of 31 December 2015 and 27.020 as of 31 December 2016. Average CZK/EUR exchange rate for the year 2015 was 27.283 and it was 27.033 for 2016.

**Cataps**
Cataps, s.r.o. For more information see chapter "Komerční banka Group ".

**Daily capital rotation of KB shares**
Average daily trading volume of KB shares on the Prague Stock Exchange divided by market capitalisation of KB at the close of the period.

**EET**
A manner of recording of sales when the data for each transaction with a merchant is sent on-line to the fiscal authority.

**EIF**
European Investment Fund

**ESSOX**
ESSOX s.r.o. For more information see chapter "Komerční banka Group".

**FinTech**
A business composed of companies that use new technology and innovation to leverage available resources in order to compete in the marketplace of traditional financial institutions and intermediaries in the delivery of financial services.

**Group**
Komerční banka Group. For more information see chapter “Komerční banka Group”.

**IBAN**
International Bank Account Number, account number format set by standard issued by the European Committee for Banking Standards and which supports automated processing of cross-border payment orders.

**IFRS**
International Financial Reporting Standards comprise a set of standards issued by the International Accounting Standards Board governing the preparation and presentation of financial statements. The aim of the standards is to achieve a high degree of comparability and transparency of accounts on a global basis.

**KB**
Komerční banka, a.s.

**KB Penzijní společnost**
KB Penzijní společnost, a.s. For more information see chapter “Komerční banka Group”.

**KB Slovakia**
Komerční banka, a.s., pobočka zahraničnej banky  (KB branch in Slovakia)

**KP**
Komerční pojišťovna, a.s.

**MEM**
Medium enterprises and municipalities

**Merchant acquirer**
An acquiring bank (also known simply as an acquirer) is a bank or financial institution that processes credit or debit card payments on behalf of a merchant. The acquirer allows merchants to accept credit card payments from the card-issuing banks within an association.

**Modrá pyramida**
Modrá pyramida stavební spořitelna, a.s. For more information see chapter “Komerční banka Group”.

**NP 33**
NP 33, s.r.o.

**OCR**
Overall Capital Requirement, the sum of the total SREP capital requirement (TSCR), requirements for capital buffers and macro-prudential requirements, when expressed as own funds requirements.

**PSA Finance Czech Republic, PSA Finance CZ**
PSA FINANCE ČESKÁ REPUBLIKA s.r.o. For more information see chapter “Komerční banka Group”.

**PSA Finace Slovakia, PSA Finance SK**
PSA FINANCE SLOVAKIA, s.r.o. For more information see chapter “Komerční banka Group”.

**SEPA**
Single Euro Payments Area

**SG**
Société Générale

**SREP**
Supervisory Review and Evaluation Process, referred to in Articles 76 to 87 and in Article 97 et seq. of Directive 2013/36/EU. The key purpose of SREP is to ensure that institutions have adequate arrangements, strategies, processes and mechanisms as well as capital and liquidity to ensure sound management and coverage of risks to which they are or might be exposed, including those revealed by stress testing and risks that the institution may pose to the financial system.

**TSCR**
Total SREP capital requirement, the sum of own funds requirements as specified in Article 92 of Regulation (EU) 575/2013 and additional own funds requirements determined in accordance with EBA guideliness for the Supervisory Review and Evaluation Process (SREP).

**SG Equipment Finance (SGEF)**
SG Equipment Finance Czech Republic s.r.o. For more information see chapter „Komerční banka Group“.

Consultancy, design and production: ENTRE s.r.o.

www.kb.cz

NA PARTNERSTVÍ ZÁLEŽÍ