Transcript of Q2 2016 results conference of mBank

[edited version]

Wojciech Chmielewski, Director of Investor Relations and Group Strategy: Good afternoon. Welcome to this presentation of mBank Group's results after Q2 2016. We have the CEO, Cezary Stypułkowski, for the first time Christoph Heins, the new CFO of mBank Group, as well as Marcin Mazurek of our economists' section. First Mr. Stypułkowski.

Cezary Stypułkowski, Chief Executive Officer: Good afternoon. Before I begin let me introduce Christoph Heins who has joined our team as of July the 1st. Couple of warm words, because you will be meeting him on a regular basis. His predecessor Jörg Hessenmüller is now back in Frankfurt as Head Strategy of Commerzbank. Christoph is a career banker with Commerzbank for many years. In his "previous life" he was financial director of Commerzbank's investment banking. Prior to that, 2008-2012, he was with Commerzbank in New York. He is now with us after these career opportunities in Frankfurt and New York - he is earning his mark in Warsaw. And as you can judge by Mr. Hessenmüller's career, it's a good place here in Warsaw. So I hope you welcome him warmly and he will be a prime contact to many of you.

Now let's move on with the quarterly presentation. Let me start by saying that the results were good. They had to be good - we had a one-off, the Visa transaction. More on that later, but it was a sale of a stake in Visa with a significant gain following our strong transactionality. Different to other banks, we do not have an acquirer function, but this was a very good additional gain supporting net profit – PLN 388.5 M of net profit. As for the balance sheet numbers, all went well in corporate as well as retail banking. The growth of mortgages was somehow lower. As we explained in many occasions we are looking for better margins and we also establishing a closer relationship between the issuance of covered bonds and our expansion in mortgage lending. Retail loans were growing fast, especially our consumer finance, as it's often referred to. The NII was very good, 13% up year on year – something we are happy with. The net fee & commission income was not as strong – we incurred additional expenditures, because our income actually grew by a couple percent, whereas our costs were higher on commissions. Positive development for mBank and the market - the growing affluence of households. We have reasons to believe that - based on balances growing fast on current accounts - we are an attractive transactional bank attracting increasing numbers of customers - more than 100 000 customers acquired in the last quarter in the Czech Republic and Slovakia and also as part of our franchise with Orange. We saw some increase in corporate numbers – we have more than 20k corporate clients now. As deposits are growing faster than loans, the bank seems to be now permanently below 100% of our loan to deposit ratio. You may recall this was one of the biggest challenges in the previous strategic perspective of the bank.

Importantly, last quarter was important because the bank approved its new strategy up till 2020. The goals of our previous strategy – One Bank for our customer and employee – those were performed fully. We opened up a new perspective. These new documents were approved by the Management Board and the Supervisory Board and agreed with our partners in Frankfurt. The strategy has its main slogan, which is "To help. Not to annoy. To delight… Anywhere." And it has a touch of ease I should say, which is because we are a relatively young bank which reaches out to young people and people in the middle years. But it's also an expression of a new context that we work in, in which such slogans sound better than traditional conservative banking mottos. So, to help, not to annoy and to delight, plus, anywhere. Of course each of these terms has its message. What's important, however, is that this strategy relies on three concepts or trends which are materializing and crystalizing in the banking sector. As I've mention on many occasions, we have been evolving from what I was taught in school, which was really the main trend for people working in the banking industry – product is king, product driven institutions, that's what we used to say. But then we started to evolve gradually, and then the process has accelerated. Now we are customer centric, which is one of the trends happening now – in regulation, in maturity, in litigation, and so on. We have to address it, and I have reasons to believe that the bank anticipated the trend earlier than other institutions – but that's my subjective judgement. However, this is something we will organize ourselves around. The second trend is mobile banking. Mobile phone, we all know, it's the fastest selling device in the history of the world. Here, I believe we have a structural advantage starting with our name – mBank, the icon of mobility. We can build a better narration around it than colleagues from BZ WBK, BNP Paribas BGZ. We are positioned well, as a reference point, a benchmark in mobile banking. Whatever you say, at the end of a day, you must always work to earn a good reputation with people like yourselves - people who think about which stocks to buy, and of course stockholders want to earn fair earnings. So, this is another part of our thinking even if the situation in Poland is becoming less easy in this regard. So, client centricity - to simplify, because it's not the time to describe all of our strategy. But what's it about is that we look at the life cycle of clients from two perspectives. One is life events, the other is way we will cluster behaviours of clients – behaviours, not just income levels. The instruments, the toolkit that we have at hand, our knowledge of the clients allows us to do that. But the opposite trend is regulation, including data protection, and so we have to find a golden mean. And to speak on the side, the new regulation is on the border of the absurd. I was recently buying insurance. I called a call center of ours – and when you do it online you just tick things off and you move on - but the guy I talked to at the call center had to speak so much about things I was not interested in and I had to confirm – "Yes, I understand". It hurt my head. So, this is an area of conflict, and it's not going to be easy for the banking industry to come to a balance between what we can offer to clients and what comes from regulation, rather than from real threats to clients. So the lawyers have their day. As a lawyer by education I know what they are doing. But it's still our intention to make things easy to reach, convenient, fast, efficient. We are changing a lot now in our communications with clients, including contracts, wording, etc. I'm not going to bore you with that, but this is where we are going.

And then, I've mentioned the smartphone revolution. There are lots of arguments I could use – who uses what kind of phone, how much time people spend on the smartphone compared to watching TV, etc. But we all know that in the next five years this revolution will continue – we are on the eve of it. Yesterday, one of the competitors asked me a question – we talked about Blik, the payment standard… Person from the bank with a name that is difficult to pronounce, or it doesn't explain a lot, has just came. Welcome. A colleague is from BZ WBK. Anyway, what I was saying. I was talking to a competitor, it was about Blik, and he tells me that there are so few transactions [on Blik]. I say, yes, few – we do about 30-40 thousand closed Blik transaction every month. Then I say – you know, in 1992 we had no card business. Today we have billions of transactions with cards. So you have to be open to what's coming, not what's in the past. So, we are positively convinced that clients will switch to mobile devices. Even if we compare ourselves to different banks in Poland and internationally, the number of mobile interaction that we have with our clients isn't comparable to even the market leaders. We have the scale, a number of clients who have accounts with us and a lot of transactionality. So we are absolutely positive that this is the way the market is going. We invested in it at the right time, we have a good product, and we have clients who are mobile twisted. So, in the coming years we will see a lot of business in this channel, and hence the investments we've made. Well, I think this explains a lot. We are talking about efficiency but we must remember that we work under specific circumstances. If you compared the current situation with 2012, when we adopted the previous strategy – WIBOR rate was 4.8% on average, so you could squeeze in a lot of margin in it. The interchange fee was 1.6%, now the average is 0.2%-0.3%. The contribution to the BFG was less than a tenth of a percent of RWA, now it's 2.5x as much. The banking tax – nobody knew what the banking tax was in Poland, only in those countries were banks posted losses and had to be recapitalized by governments. So, we have a good starting point when it comes to efficiency. We have been disciplined around our C/I for years. We continue with that. It's an important criterion for us. As time goes by I tend to digress more and more, so let me digress. I don't if I told you – I remember how very impacted I was by an analytical research report in 1994 - it was April 1994. There was a bank back then that ended up with Commerzbank – Kleinwort Benson. An analyst wrote an interesting story about the C/I tratio – it was a global paper. And I remember which banks were the most effective banks internationally back then. A bank that had C/I of 40% is called Banco Popolare, and it still operates in Spain. It was the benchmark for banking industry. I was so inspired that I made some important mistakes later on – for example I computed C/I for the branches of Bank Handlowy, which was the big, big mistake. But we started with that culture and I'm glad to say that mBank has that culture as well. However, we are not dogmatic about costs, we are strongly driven by any potential growth in our income. We are a little disappointed because if you applied the 2012's rates to our business as it is today, we would be much, much ahead of where we are now. Of course, the business looks different in retail, which has a potential for success also with regards to effectiveness. And we have this very mature corporate business, which is one among many, it doesn't differentiate itself that much. So we have to be really attentive here, especially under the regulatory pressure, which also impacts the way we define our targets – more on those later. We are an effective bank, which is not to say we don't have to look at costs. We do that, but we do it, I think, reasonably apart from one thing that needs to be approached in the long term - we have been investing heavily so we will be hit by depreciation charges sooner or later.

Now, this strategy translates into three pillars – and, as it also happens, the letter "m" also has three bars or legs. So, apart from the slogan – let me go back to it, because it organizes our thinking – "to help, not to annoy, to delight, anywhere". We want to focus on clients by working on empathy for client. The word empathy is not very popular in Polish, and that's good for us, because we will be learning how to interpret term empathy. It's about making clients happy and making banking friendly by anticipating clients' needs in the short and in the long term. That's our first pillar. Second, how do we move banking to mobile platforms and how do we make ourselves into a reference point for mobile banking. I think to some degree we are on trajectory, but we are not yet there. But in terms of what we deliver, and how we are perceived, we are better positioned than some of our serious competitors like ING, which has a very similar culture of thinking. But I don't think that every employee of Bank Śląski knows what ING stands for. And then, we have efficiency. It's really simple. We have an assumption that is a big challenge for the management of the bank, because the assumption is that we don't have too much redundancy among our people. We have structural mismatches, but it's now that we have too many employees. Given our growth in income, this is not an issue, really, in retail. The growth in costs over the past two years, especially in terms of FTEs, was mainly because we decided to expand in the Czech Republic and Slovakia. So we reactivated our growth in those markets. So, much of the growth in FTEs, apart incremental growth of FTEs due to growing clients base that increased employment in call centers and infrastructure support, is mainly driven by expansion in the Czech Republic and Slovakia. In corporate banking, our FTEs are stable. Possibly we could be more effective there, but it's not that we are on the brink of announcing mass redundancies, as many of our competitors are doing. Some banks added new branches on the way, then they closed them – we are not doing that. We think our branch network is just right for us. What's also important when you look at efficiency it is something I mentioned before – the close link we make between the expansion of mortgages and our issuance of covered bonds, where we are the leader. We rightly anticipated the destiny of the Polish banking sector when it comes to the mortgage. And the key is, of course, to simplify processes and to digitalize. We are well advanced. We made a lot of progress in terms of how to please the client, and our clients like it. But internally, we have some processes that we will be wanting to simplify in the next months. But we are making progress in this respect – we are not using cards when we enter the building, we just use the smartphone – it's the same with garage; we apply for holiday leave on the smartphone, not on paper in the bank; if you order things for the bank, you do it from the phone. So, this cuts our costs in the long term. But that's a challenge.

Now, you will ask me to show you the figures. A disappointment here, because we've decided that in this new strategy we will move away from defining hard numbers of ROE or ROA and C/I ratio, and so on. So, the rationalizing of this approach comes from the fact the regulatory world and the environment around us is topsy-turvy. In practice it means it's hard to commit to numbers because the situation changes from one day to the next. Even three days ago I read a statement that said that the interchange fee on debit cards should go to zero. Can I manage it in the short term – no, probably not. It would be irresponsible. Our assumption is to look at specific categories, which are important to investors and analysts, and it is our ambitions to be a Top 3 bank. This makes life difficult for you, because you will have to think about how those measures will look in the sector in Poland and then you will have to evaluate our relative position. But that's the choice we have made. Importantly, our supervisory board approved this approach, and so did our main shareholder.

Importantly, our capital position – well, I've been here 6 years, I'm accountable for certain things but I feel I desire the credit for some as well. When I joined mBank I came from an institution whose CEO still uses the term "fortress balance sheet" and mBank, when I joined it, had a Tier 1 ratio of 6%, I think, in 2010. So, a lot has changed since then at mBank. We were able to absorb the regulatory interventions with a 4% additional buffer imposed on the bank in one year without having to raise any capital on the market - that was thanks to a historically different approach. Of course it costs us money – it costs you have this capital buffer to withstand the "benevolence" of the regulator. It deserves respect. Our assumption is we want to be 1.5 percentage point above the requirements - we believe this buffer will serve us well in case of changing regulations. But, to say frankly, today the capital position of the bank is much stronger. We are penalized for the Swiss franc portfolio, so this gives us some space when this portfolio is being repaid. The loan to deposit ratio, which is a very general number, of course, but we came down from 135% to 95%.

Now, briefly about the results from me, and then Christoph will give you the details. A few points I need to stress. The NII, which is much better than it was last year and a slightly better than last quarter. The net fee & commission income went down – it's because we have higher commission costs in Q2, significantly higher than in the previous quarters. Costs remained at the acceptable level, with a slight increase – you will hear more from Christoph – driven mainly by depreciation. Other important messages. We are slightly improving our NIM, which went down somewhat quarter on quarter, but the positive trend continues. C/I ratio, as we said, we want to remain under 50%. Of course, the banking tax impacted the numbers, but we will try to get there. In the meantime our C/I ratio will be reported in two ways – reported figures and net of the banking tax.

And the balance sheet. As you can see, all those arrows are in green and there's nothing there to cause concern – quite the opposite. You may be interested to know that in Q2 our cost of risk was slightly higher, but this was due to lower costs in the previous quarter - I think there were two major provisions that were released and improved the cost of risk. We are around 50 points. As I often say here - in a regular situation it's 70 points, when it's very good it's 50, when it's bad it's a 100, and if it's more than a 100 it's very, very bad.

Now the bank's picture, as measured by our relative market position. Importantly, over two years we have improved our position by 1 percentage point in retail banking, which is a good step, an important achievement. It's happening mainly due to current accounts and transactional accounts. We are growing steadily as a lending bank, where our position was the weakest, up by almost 1% - that's one of the fastest growing lines. Our mortgage loans, the growth rate here is less strong, but that's a conscious choice we've made. Our market share in the segment is 7 or 8% at this point in time, and it's also marked by our exposure to Swiss franc loans. As for the other numbers, I don't want to bore you with that. Over to Christoph.

Christoph Heins, Vice-President of the Management Board, Chief Financial Officer: Yes, thank you very much and also good afternoon from my side. Let's please turn to slide 18, where you can see some more details on the development of the balance sheet, especially in the second quarter. As you may see, the lending growth remains subdued, explained by the fact that our margins in segments such as mortgage loans and large corporate loans are higher than those of our competitors. However, in Q2 the Group's loan portfolio increased by 3.6% quarter over quarter and by 4.5% year over year. Loans to retail clients grew by PLN 1.8 bn or 3.8% quarter over quarter. Excluding the FX effect, retail loans grew by 1.5% quarter on quarter. Our consumer financing reached record-high sales with 1.7 bn in Q2. When we compare this to previous quarters, where we had run rate of 1.2 bn, and I think last quarter we saw 1.3 bn, that's extremely positive from our perspective. Sales of new mortgage loans in Q2 were somewhat higher than in Q1, however, well below those levels we saw in 2015. Our Swiss franc portfolio declined by another 84 M in the last quarter due to continued repayments. Loans to corporate clients in Q2 went up by PLN 1.1 bn or 3.4% quarter on quarter, mainly driven by an increase of loans to the SMEs, basically.

Let's now turn to the next slide. On the deposit side – we had a solid growth of deposits, both in the retail and in the corporate segment. Amounts due to customers increased by more than 5% quarter on quarter and by almost 17% year on year. Retail deposits went up by 1.6 bn or 3.4%, supported by a rising customer base, persisting risk aversion of customers to alternative investments and by offering convenient features, which, basically, already shows a little bit of what the CEO just mentioned with respect to the future strategy and the features that we are offering to our clients. When we look at the biggest increase here that we saw we recorded in funds on current accounts and saving accounts, which obviously helps on our funding costs, also going forward. After a seasonal outflow, I would say, on the corporate deposits side, corporate deposits increased by PLN 2.5 bn or 7.7% quarter on quarter. The increase was driven mainly by balances on current accounts, which went up by PLN 1.3 bn. As a result of this development, the loan to deposit ratio stood at 94.7% compared to 96.1% in March, and 105.7% last year in June.

Let’s please move on to slide number 20 on the income side. Revenues of mBank Group were very strong in Q2, boosted by the one-off, i.e. the Visa transaction. We booked 251.7 M, which obviously helped on that front. Even without that one-off though, we were pretty close to 1 bn on the top line revenues that is a certain threshold for us and a certain ambition. The core revenues, when we include the interest income and the fee income together, amounted to PLN 894.1m, which is pretty much in line with a previous quarters. Stable development on that front. The interest income was relatively stable – we saw higher income on loans. Interest income was relatively stable. We saw higher income on loans fueled by increased volumes, and increased income on cash and short-term placements, which more than compensated lower income on the interest income interest rates derivatives and weaker income on investment securities. Interest expense decreased. That decrease was driven mainly by lower cost of customer deposits driven by repricing effort on the deposits both on the retail side as well as the corporate side. NIM remained pretty stable, a little bit down QoQ. Excluding the run-down of the CHF mortgage portfolio stood at 2.6%. The net fee & commission income, as it was already mentioned, decreased slightly by 2.0 M or 1% quarter on quarter. We saw an increase in fee and commission income – however, the expenses were even higher in that quarter. Let me explain this a little bit. We saw positive results on our cooperation with AXA Group, i.e. we sold more insurance products and some other third party products, so that we had to pay more agency fees on that front. Fees related to payment card transactions – that was the only component that really dropped, all the other fee components went up. So, this is more of a timing topic, I would expect a rebound on the fee & commission income in the coming quarters. Because usually, when you book certain expenses, revenue streams are coming in later on to some extent. You can see the details of that composition on slide 39 in the pack.

On the dividend income, 2.6 M in Q2. That includes dividends from minority stakes that we hold, similar to other banks in Poland. On the net trading income, that went down this quarter by PLN 24.6 M or 29%. Where that does it come from? We had a lower FX result than in the previous quarters and, other than in previous quarters, we had a negative amount due to losses on interest rate derivatives. When we recall the events pre-referendum in the UK – the so-called BREXIT – and also after that markets were extremely volatile. While we are not exposed to the British pound, we are obviously exposed to Swiss francs and euro denominated assets and liabilities, we saw massive movements both on the spread side as well as on the FX side. So, those two components basically led to that fact. I also want to highlight here that we saw already in July, to some extent, a rebound in the market, but that’s a different quarter obviously. Gains less losses from investment securities - PLN 248 M, that’s the category where we booked VISA transaction, as I already mentioned - PLN 251.7 M. I think everybody is aware of those two components – the cash up front, the deferred cash as well as the preferred stocks, for which we took a prudent valuation approach. Other operating income stood at PLN 2 M in Q2, much lower than in Q1. That is really a result of a very positive results in Q1 – we had two main elements in Q1. First, we saw strong activity on mLocum - that’s why we had a very positive results on that side. Second, we recognized the sale of non-performing loans retail portfolio in Q1.

On slide 21 you can see the details of the development of our costs. As already mentioned costs increased by roughly PLN 10 M, i.e. 2.1% quarter on quarter. Excluding a one-off on the amortization of an IT system, costs were stable. Overhead costs remained flattish. Personnel costs increased only marginally - by PLN 1 M or 0.5%. Material costs, excluding the BFG contribution, declined by approximately PLN 2 M. The BFG contribution remained stable quarter on quarter at PLN 37 M. The amortization charge – I already mentioned this – this is an IT system that was used by the former Multibank and due to the merger we obviously don’t need that system anymore. That’s why we decided to write-off that balance on that front. On year over year comparison, the Group’s quarterly operating costs increased by PLN 6.3 M or 1.3%, driven by higher amortization and the BFG contribution. Personnel costs remained flat year over year despite higher employment – we had 84 FTEs more year over year, whilst the material costs basically declined by 7% your on year. Finally, the C/I ratio of the Group amounted to 40.8%, which obviously included the large one-off from the VISA transaction. Without that one-off, the C/I ratio would be at 51.6%, which is slightly above our aspiration level – however, still a very good result.

On slide 22, let me draw your attention to the loan loss provisions and the risk costs. Net impairment of loans and advances normalized after an exceptionally low LLPs in Q1, particularly on the corporate side. Despite the quarterly increase, the average quarterly LLPs in H1/2016 were lower than the average quarterly provisions recognized in H1/2015 and in full year 2015. Please look at page 36 for more details on that front. As I already said on the corporate side - the normalization on the LLPs side. That means that the cost of risk for the corporate portfolio in Q2 increased from 5 to 50 bps, which is a very normal level, and you can see this already on the slide here, when you compare this with previous quarters. The LLPs for retail loans increased by PLN 10.9 M or nearly 17% quarter on quarter, and that's really driven by increase in loan volume. I think it's worth mentioning that over several quarters we have been recording record NML sales, which by definition attract a higher cost of risk. We are very happy with the quality of the loans, the new loans and the loan portfolio all overall, but obviously must accept a slightly higher LLP run-rate on that front. Finally, the cost of risk for the Group in Q2 stood at 59 bps, while YtD cost of risk amounted to 47 bps, which again confirms a very good quality of our loan portfolio.

Moving on to the next slide. The impaired loans of the Group increased by 3.9% in the last quarter – with that we are pretty much unchanged compared to the level recorded a year ago. In retail banking impaired loans went up by 2.4% quarter on quarter, while in corporate business by 5.9%. The growth of impaired loans was accompanied by an increase of the entire gross loan portfolio. Therefore, the impaired loans ratio for the Group at the end of June remained unchanged at 5.8%. The impaired loan ratios on the retail side declined slightly to 5.6% as a result of the increased volume of the retail loans. Our Swiss franc mortgage loans continue to perform well despite the ongoing discussions on the FX mortgage loans restructuring plans. As I already mentioned, we had a further decline of 84 M in our Swiss franc portfolio due to regular repayments. The coverage ratio for the Group at the end of June stood at 58.5% and was pretty unchanged compared to March. Including the IBNR the provisions reached 63.7%.

With that, let's please move on to the funding structure of the bank, which was pretty much unchanged compared to the previous quarter. The main funding source for mBank comes from deposits side and again we continue to see steady growth on that front. Amounts due to banks - the second largest funding source – roughly 10% of total funding. Our indebtedness towards Commerzbank, which amounts to CHF 2.3 bn, will be reduced until December to CHF 1.5 bn. So we have a clear plan on the repayment schedule on that front. In June the bank – and that's public knowledge – obtained additional funding from Industrial and Commercial Bank of China. That was a euro denominated loan. mBank Hipoteczny – mBH - continues to provide for stable funding via issuance of covered bonds. In Q2, mBH issued two sets totaling PLN 150 M. They were the first issues of PLN covered bonds with a fixed rate coupon. And I think at this point it's also worth mentioning that the rating was upgraded by Fitch for the mortgage covered bonds by 2 notches - from BBB+ to A. Our EMTN Programme was updated in Q1, however, whether or not we will be able to issue anything in the second half of this year highly depends on the further development of the discussions around the FX mortgage conversion plans. All in all, we have a comfortable funding plan, which also allows for future growth.

Coming next to the capital ratios and other regulatory ratios. At the end of June, the total capital ratio of the Group stood at 18.3% and the Common Equity Tier 1 Ratio amounted to 15.6%. Thus we are much above the minimum regulatory requirements for TCR and CET1, which since the beginning of 2016, after the inclusion of the additional capital buffers resulting from the FX mortgage loans and the capital conservation buffer stood at 16.97% and 13.04%, respectively. Obviously stand-alone mBank has much, much higher capital ratio accordingly. The difference when you look at the small drop on the capital ratios quarter on quarter. Let me highlight. On the CET1 ratio we saw two events. The one is basically, we booked bonds as available for sale and you have certain events there when that's book in other comprehensive income. A drop in valuation, which again also came during the market volatility and the BREXIT front caused a small reduction of the CET1 capital ratio. And the other component is related to the VISA transaction – the income from the sale of the VISA shares will be reflected in CET1 capital after we get the approval from KNF so we can also recognize the profit from Q2. So that's a little bit of washed – so you first reduce it on the capital side and then you gain the capital back via the approval for recognizing the profit, basically. A detailed decomposition of the factors responsible for the capital ratios you can also see in the appendix. And last but not least the liquidity ratios after H1 are well ahead of full Basel III phase-in requirements, as you may see on the right hand side at that chart. With that I'm handing over to me colleague on the macroeconomic side. Thank you.

Marcin Mazurek, Senior Analyst: Thank you very much and good afternoon. The first half of the year was all about low investor activity. In Q1 there was a deep drop in investments. According to early statistics, Q2 was not much better, so it could still continue the down trend. We compare investor activity with construction business here because investment is dropping mainly due to drop in public investments. As for private investments, small companies are much better according to NBP surveys. In the first half of the year not only investor activity was low, our exports were going down as well even though the zloty has depreciation. In our view this means that demand for Polish goods is still falling. Demand from our main trade partners in the euro zone, including the UK, is low. As a consequence, the structure of GDP in 2016 will be mainly driven by consumption. Consumption is driven by the very good labour market, growing employment, and growing wages, as well as government program of special allowances for families with kids – "500+". In our opinion GDP this year will grow 3.3 or 3.4%, which will be less than last year. In this environment there is currently no inflation. Importantly, core inflation remains very low. The growth of inflation expected in the coming months will not be driven by prices getting higher – rather, it's due to the comparable base of last year. So, inflation year on year will be higher because it was so very low last year. Next slide please.

As for credit aggregates, we see solid growth in corporate deposits, mainly due to costs discipline and the weak zloty. Corporate loans are growing less fast. At least for the time being this coincides with a drop in investments and also the introduction of the banking tax. This overlap in time does not imply any correlation, however. As for consumers, deposits are growing very fast due to the good labour market and the "500+" program. Consumer finance, consumer loans are growing high. Mortgages – less fast because of stricter lending requirements that may push out some consumers from the market or discourage them from borrowing. Polish bonds have a higher premium now - it had dropped recently, but it still remains massive. So, the spread to the German bonds remains very high. But although the spread has remained at 300 points, changes in yields reflect the situation in the global economy. We believe that the rates in the global economy will remain low or get lower. Hence the chances are that the yield on Polish bonds will go down both in terms of the spread to the German bonds and the risk premium on the Polish bonds. So, in summary, the yields will be rather low. As for the zloty, the currency remains weak compared to other currencies in the region. We are expecting it to appreciate very, very modestly. We believe that the exchange rate to the euro may go down to 4.25 later this year. But there are still risks looming over the Polish economy, including the discussions of the conversion of FX loans that have been mentioned before. So the zloty remains rather weak under pressure. Thank you.

Wojciech Chmielewski: Thank you very much, now it's time for your questions.

/Q&A section is not included in the webcast in the English version due to the encountered technical difficulties during the conference. Please be informed that the text below has been translated from the Polish transcript/

Dariusz Górski, DM BZ WBK: I have a question regarding the growth of non-mortgage loan volumes in the last quarter. Could I ask for more details on this? Where does it come from, and, more importantly, is it sustainable? In corporate banking you also have a significant increase in the K1 segment and I'm wondering where does it come from and whether it is sustainable.

Christoph Heins: Thank you for your question. Regarding retail banking – consumer finance. We have a stable growth especially on cash loans, but also credit cards. Of course, it was a much stronger growth than in the previous quarters, I don't know whether 1.7 bn can be repeated in the next quarter, but I'm sure that we will exceed the reported results from previous quarters, i.e. it will be more than 1.3 bn.

Cezary Stypułkowski: On the corporate credit. The more visible growth is in the K2 segment, not K1. This is low relative to the circumstances in which we operate. Generally, balance in K1 is falling, so it could be that we had 624 M in the segment, that is 3-4 loans. This is nothing spectacular, we can rather expected that K1 volumes will be flat or even falling. However, what is key for us is the K2 and the growing, to a high extend, K3 portfolio. Moreover, what we care about the most is SME in retail, which grows fast, but from low base.

Dariusz Górski: Any comment on the pipeline? Because some of your competitors, I would say, are complaining.

Cezary Stypułkowski: Yes, today we had a credit committee and I talked with my colleagues on the side. There is no inflow of new projects, this is pretty clear. There are some renewals, but the demand for corporate credit is not significant.

Dariusz Górski: Again on the corporate credit – margin on corporate loans is somewhat lower that in the previous quarter. As of now, not many banks have reported their Q2 results, but I'm wondering why there is a decrease, since the other banks, which have also shown their results on Q2, don't report a fall in margin in this category.

Cezary Stypułkowski: We have a higher growth in K1, which is always characterized by lower margins. But I don't think this is something spectacular, the uptick or downtick in the particular quarter. We don't regard this quarterly change as very important.

Dariusz Górski: You have shown a very nicely looking slide with falling share and level of CHF. And my question is whether you think, or know, that the FX buffer will be adjusted in the end of the year, simply because your CHF portfolio will be smaller?

Cezary Stypułkowski: The way in which this buffer has been levied on the banking sector may raise concerns on methodological and fairness grounds. Basically, we are reliant on the benevolence of the regulator. Logically, decreasing portfolio should at some point lead to lower requirements on capital buffer. There is no special procedure in this regard, but surely we will seek to decrease this buffer. This year, as you remember, we have successfully applied for a reduction in this buffer on the basis of methodological interpretations on the way the buffer is calculated. So, I think the KNF is generally open. However, part of the truth about this buffer is that it has been imposed due to the KNF's discontent from the fact that the banking sector was not so responsive to the proposal it has set forth in respect to the CHF mortgages – this is how I interpret it. It cannot be ruled out that the process of capital freeing up in the context of falling CHF loans volume will be slower, it won't be automatic. The regulator will probably ask for argumentation, documentation - in this context my colleagues will have a lot of work - and later on we will, in certain time perspective, receive a relief on the buffer.

Dariusz Górski: Question on the fees on cards. They have fallen significantly quarter on quarter, and this is a second quarter in a row. I'm asking for the reasons and also on your feelings regarding future performance in this category. And a second question, which the CEO has provoked, is on interchange fees from debit cards, which are still significant.

Cezary Stypułkowski: Generally, fees income had increased, we had an issue on the cost side, however.

Zdzisław Wojtera, Director of Controlling and Management Information: Interchange in the Czech Republic and Slovakia – we have a dynamically growing card transactions, so our costs are going up, but in the same time decreasing interchange means that our revenues are falling. So, our costs are growing on the increasing transaction volume.

Wojciech Chmielewski: Do we have any more questions?

Kamil Stolarski, Haitong: Question on the strategy. You have mentioned your strategic goals in a relative way. I have a more general question following your work on the strategy. Is the Polish banking sector going to recoup the costs of the banking tax? The banking tax came into force for a few months now, and looking at your yield on loans and also looking at what your competitors are reporting, recovering appears to be very, very slow than we would have assume.

Cezary Stypułkowski: I think you shouldn't look only at one product. Of course, our ambitions, our internal assumption is that we will recoup the tax within three years, more or less. I think, the more holistic view on how the banking industry will behave is that through many years the banking sector in Poland has been driven by relatively high interest margin, in the environment of high interest rates, which has allowed the banking sector, including our bank, to offer many products for zero. This has damaged the sector. And the lowering of the interest rates, which has happen abruptly, in 24 months, more or less. Additionally the banking tax. All this changed the dynamics in the sector, and, in my opinion, the key thing now is that banks will have to look differently at how fees & commissions are shaped. If I could ask for a slide showing the regulatory environment. If you look at what was the situation back in 2012 and how the environment looks today, in every line the banking sector took some form of a hit – interchange, banking tax, interest rates and the ability to bear margin in the nominal interest rates. All this means that the model has to change. I don't know if said it here, I think I already mentioned it in the last quarter. I saw the comparison of absolute level of fees & commissions per citizen over 15 years old in the European Union – not per client, because we enter a definitional sphere, but per person over 15 years old, which is a more solid statistic. If we look at this, then in Poland it is 70-80 euro, and it's the second lowest after Romania, where it reaches 56 euro. In Czech, so in a country where we operate, it's around 150 euro, in Germany – 450 euro, in France – 700 and in Austria – 1000. So, whatever statistic we look at there is a room for growth. As the society gets wealthier and makes more transactions, and as we sophisticate our product offer, then in my opinion there is a room for growth in fees & commissions in relative terms. In my opinion, we shouldn't expect that the banking sector will recoup everything solely by asset expansion and interest margin improvement. It will also happen in the sphere of fees & commissions policies. However, this is not an announcement that mBank will start charging for an account.

Kamil Stolarski: One more question on the outlook for costs in the coming years. It appears that your costs were growing faster than on the overall market, 4 - 6%. Are the projects in Czech Republic/Slovakia going to be continued in the 2020 perspective?

Cezary Stypułkowski: Of course, we are under some pressure, as I already mentioned – amortization is hitting us, and this is one of the factors that we have to take into consideration. The result of expansion into the Czech Republic and Slovakia is not what the bank has expected. But on the other hand, with our business model, we encounter barriers in Poland, i.e. we are not a bank for everyone, we are a bank for clients with certain digital maturity, and these amount to 12-13 million in Poland. Today, we report that we have 5 million clients. By principle, these clients have had some form of a digital contact with the bank. Even if it's a dormant customer, then relationship with us, to a high extent, has started over the Internet. This would mean that penetration rate of this client segment, calculated accordingly, is above 30%, and this is in a market that is very competitive. In my opinion, structurally mBank should expand beyond borders. The problem is that there are too many factors that cause uncertainty here in Poland to take a decision for expansion. We think that the operations in the Czech Republic and Slovakia, on the one hand, is something that teaches us presence on foreign markets; this is a huge learning curve, that doesn't exist in this scale in any other bank in Poland. On the other hand, in case of Slovakia, this is an inflow of funds that would have been otherwise difficult to obtain, I'm talking about funds in euro. Maybe the market is a little bit too small, but we are experimenting and obviously it comes at a cost. Secondly, the bank invests with no simultaneous cuts in employment. So, we have two factors, which are quite important. But I would stress that we do not discipline ourselves to be in line with others banks – we have significantly different business model. Our thinking is rather to be disciplined within the C/I ratio. The factor, which I have mentioned here, on the growing amortization, will undoubtedly have an impact on our cost base in the coming years – we are building new headquarters, a number of things will happen in this regard. But we will be trying to be disciplined in the context of C/I ratio, rather than compare our costs lines with other banks.

Wojciech Chmielewski: Maybe a quick question that has arrived to us over the Internet. What are your thoughts on the idea of regulating the interchange fee to 0%?

Cezary Stypułkowski: Without enthusiasm, I would say. If I were to build on the content of this question, I would say that I have partly answered this question when I mentioned the relatively low level of fees & commissions in Poland when compared to the European market. Secondly, it's hard for me intellectually to agree with people that postulate that everything should be for free, although I'm aware that we live in the times where more things can be imagined then stems from my education or experience.

Wojciech Chmielewski: Do we have any more question?

Cezary Stypułkowski: We will also be at your disposal during lunch, which we have prepared for you.

Wojciech Chmielewski: Thank you very much and I invite for informal talks during lunch.