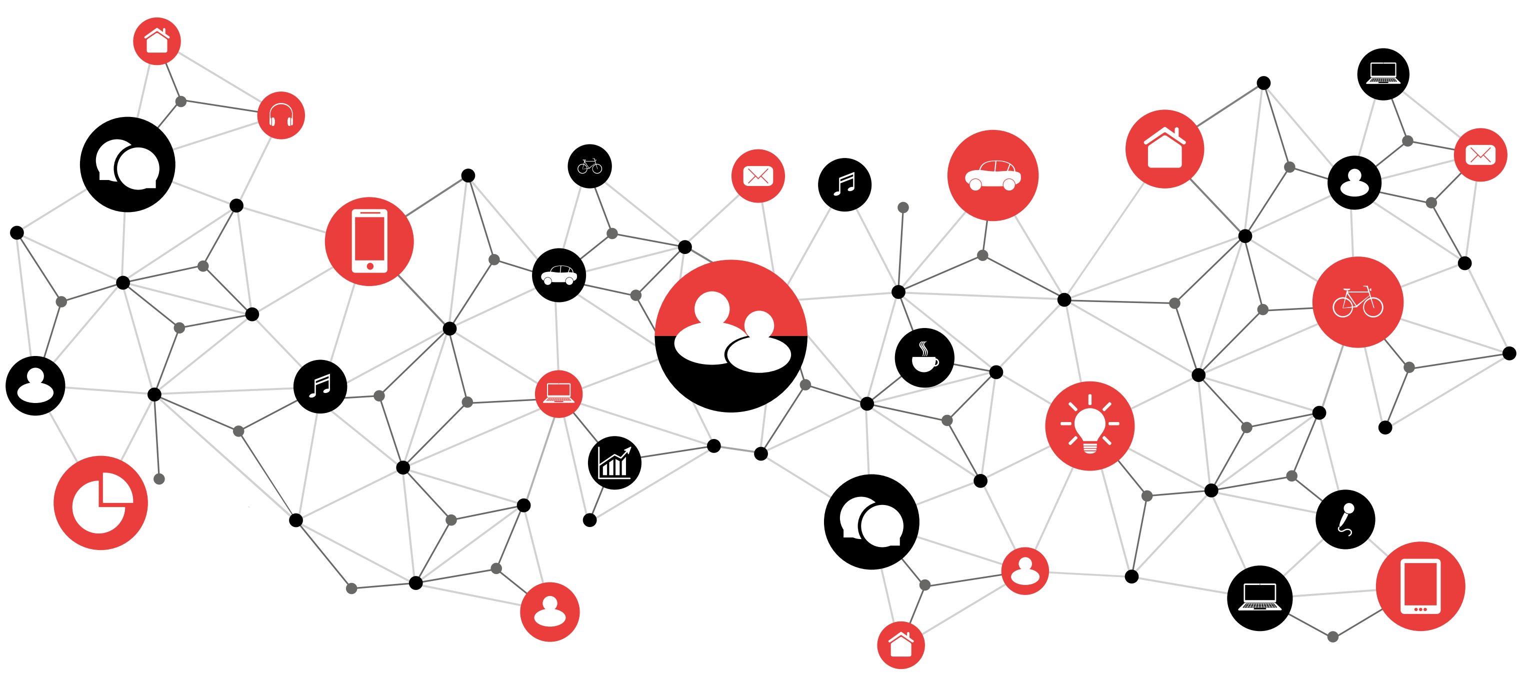
HALF-YEARLY REPORT 2018

Komerční banka, a.s.



NA PARTNERSTVÍ ZÁLEŽÍ

KB

Contents

Further information

Detailed financial and operational information about Komerční banka Group is available in other publications on KB's website for 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.

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Profile of KB

Komerční banka, a.s. (hereinafter also "KB" or the "Bank") is the parent company of KB Group (hereinafter also the "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.

Vision and mission

A real bank for real situations
We stand by ambitious and discerning individuals and their families, small businesses, and corporations, supporting them throughout their lifetime journeys and diverse business ventures to succeed in the dynamic world. We provide first-class advisory, tailor-made solutions, and industry leading innovations through our passionate people and convenient digital channels.

To create value for clients, shareholders, and employees and to serve society
We are a lifetime partner with a human touch for our customers – discerning individuals, small businesses, and corporations. We provide them with straightforward service, tailor-made solutions, and first-class advice.

We engage with our shareholders and deliver long-term, sustainable profitability.

We provide to our employees a sense of purpose and room for growth. We trust our people and nurture accountability and co-operation by putting culture and conduct at the very heart of our business practices.

We act responsibly towards our society.

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 accepted and 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 applies and develops 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.

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 that 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 towards effectively reducing its environmental impact.

Highlights from 2018's first half

January

From 1 January 2018, PSA Finance Czech Republic became a part of ESSOX. The merger created further space for improving services to clients in the area of automotive financing and for boosting operational efficiency.

Komerční banka extended the co-operation agreements for 2018 with the Agrarian Chamber of the Czech Republic and with the Federation of Food and Drink Industries of the Czech Republic. These steps confirmed once again the good relations between Komerční banka and both Chambers, whose membership includes a number of KB's clients.

February

KB significantly improved access to bank branch services for hearing-impaired clients. More than 60 branches are now equipped with the eScribe on-line service that transcribes the discussion between a client and bank advisor into a written form. The service is provided by Transkript online, a social enterprise employing blind speedwriters.

March

KB launched a new version of **www.kb.cz**. Its website now offers improved clarity, simplicity, and transparency. Separate sites were created for major groups of clients (individuals, entrepreneurs, and businesses), reflecting their differing requirements. Obtaining a banking product or service has been made much easier on the new www.kb.cz. The web even provides tips and advice for typical life situations.

As its first bit of leveraging on Open Banking opportunities created by Europe's Second Payment Services Directive (PSD2), KB equipped its internet banking application for small businesses with a Fakturoid tool for issuing, administering, and following up invoices and similar payments.

April

At the General Meeting on 25 April, Komerční banka's shareholders approved the reported financial results, distribution of profit, and paying out of the 2017 dividend of CZK 47 per share. Shareholders were informed about Komerční banka's strategic directions to be pursued in in the months ahead.

KB extended its partnership agreement with the Association of Private Farming of the Czech Republic. Under this partnership, the Bank supported, for example, an event opening private farms across the Czech Republic to the public.

May

The number of clients logging into the KB Mobilní banka application surpassed 500,000. Recently, KB enhanced its mobile banking application with several features that were heartily welcomed by clients, such as Face ID and Touch ID authorisation, the Trusteer Mobile security solution from IBM, and integration with Apple Watch and Android Wear devices.

SGEF allocated CZK 2.5 billion under a programme entitled "Climate Action" that uses a guarantee from the European Investment Bank to provide advantageous financing for projects reducing undesirable environmental footprints. SGEF and KB have traditionally been partners of European financial institutions.

June

In co-operation with Société Générale bank, KB introduced a multi-bank internet banking application known as Sogecash Web, as well as its mobile version Sogecash Web Mobile. Upon a single login, clients are able to administer their accounts in several SG Group banks across multiple countries. With the possibility to extend the Sogecash® SWIFTNet and Sogecash® SFTP tools, KB is now able to meet the complex cash management needs of multinational companies.

Following on to a successful offer of payment cards featuring superheroes, KB brought out a new and limited WANTED range of cards depicting such diabolical comic book characters as Harley Quinn, the Joker and Catwoman.

Events after the end of the half-year

With effect from 1 August 2018, the Supervisory Board of Komerční banka elected Mr David Formánek and Mr Miroslav Hiršl as members of the Board of Directors. These appointments followed the resignation of Mr Jan Pokorný from the Board of Directors as of 30 June 2018 due to a family situation and termination of Mr Peter Palečka's membership on the Board of Directors of as of 31 July 2018. Mr Palečka will continue to work in an advisory role for Komerční banka until the end of 2018.

Macroeconomic development[1]

After closing out last year on a very strong note, the economy slowed moderately in the first half of 2018. It nevertheless maintained a very robust year-on-year growth rate. Further slowing will continue throughout this year. Following 2017's expansion of 4.5%, Komerční banka estimates that the Czech economy will grow by 3.0% this year.

Economic activity continues to be driven mainly by domestic demand, while the contribution of the foreign trade balance has fallen into negative values. In addition to the partial slowdown in external demand, strong import growth also contributed to this development. This reflects the powerful dynamics of both demand-intensive investment and private consumption.

Domestic demand is significantly supported by both investment and household consumption. Private consumption has maintained its forceful dynamics, reaching 4.3% in the first quarter of this year. Only slight slowing is expected through the remainder of the year, and so consumption will increase by an average of 4.0% for 2018 as a whole. High consumer confidence reflects the strong wage growth and record-low unemployment rates. In mid-year, the jobless rate fell below 3% and is the lowest anywhere in the EU. The number of job vacancies exceeded the number of candidates for the first time in history. The shortage in labour is reflected in brisk wage growth. Remuneration continued to grow strongly last year, and that rise exceeded 8% in the first quarter. Wage growth will remain in this range through the rest of the year and will reach 8.0% on average for 2018.

Investment activity continues to grow robustly. The most significant contribution is coming from private business investments. Businesses are thus aiming to expand their production capacities in response to the continued strong demand despite the tight labour market and significantly rising wage costs. This is reflected in strengthened investment into machinery and equipment. The government sector has also begun to contribute to the growth in investment, thanks to gradual recovery in infrastructure outlays supported by EU funds in the current programme period. Investments into housing and other buildings and construction also increased. The main contributors were households along with the public sector and businesses.

Strong investment spending has also boosted the construction sector, where output rose at average rates exceeding 10% during the first five months of 2018. A revival was visible also in the civil engineering area, where average growth has been 7% so far this year. This confirms the strengthening of the public sector's investment activity, although the sector also was helped by favourable temperatures in January. Demand for real estate continues to exceed the supply, and especially for residential real estate in large cities. This is leading to a further rise in housing prices, which reached 12.2% in the second quarter.

Solid domestic demand is reflected in growing prices generally. After a weaker beginning of the year, when inflation was slightly below the 2% inflation target, inflation moved well above the target – reaching 2.6% in the middle of the year. This was due to the depreciating Czech crown along with rising prices for oil and food. All major components of consumer prices now manifest a pro-inflationary character. Both core inflation and food prices grew during May and June, and fuel prices also rose significantly. Regulated prices accelerated during June in connection with rising electricity prices. Komerční banka nevertheless expects inflation to ease towards the 2% mark through the rest of the year.

The vigorous growth in inflation and the real economy allowed the CNB to continue in normalising monetary policy. After the February rate hike, the CNB's Board seemed to be ready to restrain itself from further tightening of policy until the end of the year. The depreciating Czech crown and accelerating inflation, however, spurred the CNB to raise rates for the second time in this year already at the end of June. The crown has scarcely responded to that move, confirming that it is currently more sensitive to global sentiment than to domestic development. This fact will allow the CNB to continue in raising rates towards neutral levels at the expected pace of 25 basis points per quarter. The crown should return to an appreciation trajectory and lower volatility, but this is subject to at least partial calming of global political uncertainties. Due to the persistent strong position of foreign investors, the Czech crown is still vulnerable to external shocks.

1 The sources of primary data in this section are the Czech Statistical Office and the Czech National Bank. The data have been obtained from Bloomberg Terminal. Forecasts are by Komerční banka's Economic and Strategic Research.

KB Change strategic update

In order to address the key challenges existing in the Czech banking market, including the ongoing erosion of product margins due to competition and regulation, clients' swiftly escalating preference for digital banking channels, and rapid development of banking technologies, Komerční banka has decided to update its strategic direction. The changes and steps are formulated in the transformational programme KB Change. Its ultimate vision is to be a lifetime partner with a human touch for active individual, small business, and corporate customers, to provide employees a sense of purpose and room for growth, and to deliver long-term sustainable profitability to shareholders while acting responsibly towards society.

The updated strategy focuses on reinforcing or achieving market-leading customer satisfaction status in the target client segments throughout each client's entire lifespan. KB will differentiate itself in the market by best-in-class advisory, a relevant and comprehensive product offer leveraging the global scale of the Komerční banka and Société Générale groups, and its ability to provide better service in a simple and efficient way with tailored financial solutions.

In the years 2018–2020, KB will simplify, digitalise, and accelerate key customer processes and journeys in the retail and corporate segments. The simple basic services will increasingly be provided through digital and self-service tools. The Bank will be proactively seeking options for improving the experience and value it delivers to customers, including through partnerships with external providers of services that may enrich KB's offer.

Leadership, accountability, and information flow will be enhanced by organisational delayering and by optimising the management span of control. Activities leading to change or improvement in the Bank's functions, which represent approximately 30% of headquarters activities, will be organised in agile cross-functional teams built around specific client needs or journeys and utilising advanced data analytical capacities. Especially to further strengthen its concentration on client satisfaction, KB will also upgrade the employee motivational schemes. The operating model for the retail network will adapt to the pace of change in consumption of banking services, the network management structure will be simplified, the number of branches will be reduced by 10–15%, and the Bank will increase the share of branches wherein cash services are provided through deposit-taking ATMs. The capacity to share specialised expertise by remote means will be enhanced.

The KB Change goals include raising the client satisfaction levels as measured by Net Promoter Score among discerning individual clients, small and medium-sized enterprises, and large corporations. The improvements in culture, organisation, and motivation should measurably increase the employees' engagement. Moreover, the plan is designed to generate recurring financial benefits in terms of faster growth in revenues and gross operating income, mainly driven by stronger growth in lending and assets under management; savings in operating expenditures from improved overall efficiency; and, in a later stage, savings in needed capital expenditures due to improved processes and allocation efficiency. Implementation of the plan will bring a net positive financial contribution starting from 2019.

Key ambitions of the KB Change Plan

Ambition category	Target population	Metric	Score
Client satisfaction	Defined individual clients SMEs Large corporations	Net Promoter Score	Number one among key peers in each target segment
Employee engagement	KB Group employees	Blended index	≥ 80%
Working in agile teams	KB headquarters	% of HQ employees	30%
Revenues	KB Group	Net banking income (excl. one-off items)	≥ CZK 33 billion
Operational efficiency	KB Group	OPEX / NBI (excl. one-off items)	≤ 45%
Profitability	KB Group	Return on shareholders' equity (excl. one-off items)	≥12%

In support of achieving the plan's goals, KB will enhance its investments in 2018 and 2019, particularly with a focus on improving its capacity to provide and sell services through digital channels.

Komerční banka has assessed the scope of activities and investments to be undertaken within the KB Change Plan, as well as expenditures directly generated from these steps. In accordance with International Financial Reporting Standards (mainly IAS 13), KB created in June 2018 a restructuring reserve covering the expected expenditures arising directly from restructuring within the KB Change programme. The total restructuring reserve amounts to CZK 295 million, of which CZK 223 million in expected costs for severance payments linked to optimising the retail network and headquarters were recognised in personnel expenses. The Bank also booked a charge of CZK 71 million in general administrative expenses related mainly to the expected costs of reducing branch facilities. The costs of development activities will be recognised on an ongoing basis.

Business performance of KB Group

Developments in the client portfolio and distribution networks

At the end of June 2018, KB Group was serving 2,393,000 clients on a consolidated basis (+0.6% year on year). Standalone KB recorded 1,666,000 clients (+0.7% year on year), of which 1,408,000 were individuals. The remaining 258,000 customers were comprised of entrepreneurs, businesses and corporations (including municipalities and associations). Modrá pyramida was attending to 487,000 customers, and the number of pension insurance participants at KB Penzijní společnost reached 532,000. Services of ESSOX Group (including the PSA Finance franchise) were being used by 214,000 active clients.

Komerční banka's clients had at their disposal 378 banking branches (including one branch for corporate clients in Slovakia), 761 ATMs (of which 274 were deposit-taking 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 1,437,000 by the end of June 2018 and corresponds to 86.3% of all clients. Mobile banking was itself being used by 514,000 of KB's clients. Customers held 1,564,000 active payment cards, of which 179,000 were credit cards. The number of active credit cards issued by ESSOX came to 106,000. Modrá pyramida's customers had at their disposal 213 points of sale and approximately 800 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.

Loans to customers

Total gross volume of lending to clients rose by 4.2% year on year to CZK 624.8 billion[1].

In lending to individuals, the overall volume of housing loans[2] grew by 5.9% from the year earlier. Within this total, the portfolio of mortgages to individuals expanded by 3.9% to CZK 221.7 billion. Modrá pyramida accelerated growth of its portfolio to reach 16.0% year on year (CZK 47.1 billion). The volume of KB Group's consumer lending (provided by the Bank and ESSOX Group in the Czech Republic and Slovakia) was up by 5.8%, at CZK 39.0 billion.

The total volume of loans to businesses provided by KB Group rose by 3.4% year on year to CZK 318.3 billion. This growth rate was influenced by greater issuance of bonds by corporations and intense competition in the market characterised by abundant liquidity. Lending to small businesses grew by 6.4% to CZK 35.3 billion. The overall CZK volume of credit granted by KB to medium-sized and large corporate clients in the Czech Republic and Slovakia (inclusive of factor finance outstanding at Factoring KB and car dealers' financing from PSA Finance) increased by 2.9% year on year to CZK 256.2 billion. At CZK 26.7 billion, the total credit and leasing amounts outstanding at SGEF were up by 4.6% year over year.

Amounts due to customers and assets under management

The volume of standard client deposits within KB Group rose by 4.6% year on year to CZK 806.6 billion[3].

Deposits at Komerční banka from individual clients grew by a swift 9.7% from the year earlier to CZK 265.5 billion. The deposit book at Modrá pyramida contracted by 2.1% to CZK 61.3 billion due to maturing of older contracts. Total deposits from businesses and other corporations climbed by 2.9% to CZK 465.8 billion.

Client assets managed by KB Penzijní společnost were higher by 8.3%, at CZK 55.5 billion. Technical reserves in life insurance at Komerční pojišťovna, totalling CZK 47.3 billion, were at the same level as a year earlier. The volumes in mutual funds held by KB Group clients grew by 7.4% to CZK 63.1 billion.

The Group's liquidity as measured by the ratio of net loans[4] to deposits (excluding repo operations with clients but including debt securities held by KB and issued by the Bank's clients) was at 75.5%.

1 Excluding volatile reverse repo operations with clients but including debt securities issued by KB's corporate clients. If reverse repo operations are included, gross lending increased by 3.3% to CZK 635.2 billion.

2 Housing loans: mortgages to individuals provided by KB + loans to clients provided by Modrá pyramida.

3 Excluding volatile repo operations with clients. The total volume of 'Amounts due to customers' climbed by 6.4% to CZK 832.0 billion.

4 Gross volume of loans reduced by the volume of provisions.

Financial performance of KB Group according to IFRS

Income statement

As part of updating its reporting methodology, and mainly in the context of implementing the new IFRS 9 reporting standard, Komerční banka reclassified with effect from 1 January 2018 certain items of the Income Statement and the Statement of Financial Position. For improved information value, the comparative comments below are based on a pro-forma retrospective restatement of the respective accounting lines of the Income Statement from 2017.

Komerční banka's revenues (net operating income) for the first six months of 2018 decreased by 1.5% year on year to CZK 15,397 million. Within this total, net interest income improved and net fees and commissions declined slightly. Net profit from financial operations dropped visibly and as expected, due to a high base in the first half of 2017, when the CNB's discontinuation of its currency commitment had boosted clients' activity in hedging financial risks.

Net interest and similar income[1] was up by 3.7% to CZK 10,793 million. The result was underpinned by higher market interest rates that support yields from reinvestment of deposits and capital. On the other hand, intense competition on the banking market pushed down spreads on loans. The net interest margin, computed as the ratio of net interest income to interest-earning assets reported on the balance sheet, reached 2.2% in the first half 2018[2].

Net fee and commission income[1] moved lower by 1.5% to CZK 3,077 million. The overall number of transactions executed by clients rose, most notably in card payments. Transaction fees were diminished, however, due to inclusion of more transactions in account packages in 2017. This was partly offset by higher income from account maintenance, as more clients opted for superior accounts with wider range of included services. Fees from cross-selling were up slightly, supported mainly by volume growth in mutual funds. Income from loan services declined, influenced by shrinking fees from housing loans in KB and Modrá pyramida and lower fees from certain loans to business clients. Fees from specialised financial services were down, mainly because the comparison base had been elevated in the first half of 2017 by several large deals.

Net profit on financial operations decreased by 29.4% to CZK 1,407 million. A lower level had been expected, because the 2017 result had been boosted by clients' exceptionally strong currency hedging activity before and shortly after the CNB eliminated its floor under the CZK exchange rate on 6 April 2017. In the first half of 2018, clients' demand for hedging of currency risks was solid, especially when movement in the Czech crown's exchange rate took a rather unexpected direction. On the other hand, some clients did not perceive the market interest rates as particularly attractive for entering into new positions for hedging interest rate risks. Fees and commissions from FX transactions were higher year on year, on a slight increase in the volume of these transactions.

Dividend and other income rose by 15.5% to CZK 120 million. This line primarily comprises revenues from property rental and ancillary services.

Recurring operating expenses were up by a modest 1.7% to CZK 7,493 million. Recurring personnel expenses were higher by 4.0% to CZK 3,775, reflecting mainly an increase in average remuneration as the number of employees was almost stable (+0.3%) at 8,481[3]. General administrative expenses (excluding the regulatory funds) were lower by 3.8%, at CZK 2,002 million. The cost of Resolution and similar funds declined by 2.5% to CZK 833 million. This amount comprises the full-year cost of contributions to the Deposit Insurance Fund and Resolution Fund. Recurring depreciation and amortisation grew by 9.4% to CZK 883 million, driven mainly by new and upgraded software and IT equipment.

In accordance with International Financial Reporting Standards (mainly IAS 13), KB created a restructuring reserve in June 2018 covering the expected expenditures arising directly from restructuring within the KB Change programme. The total restructuring reserve amounts to CZK 295 million, of which CZK 223 million in expected costs of severance payments linked to optimising the retail network and headquarters were recognised in personnel expenses. The Bank also booked a charge of CZK 71 million in general administrative expenses related mainly to the expected cost of reducing branch facilities.

Also in 2018's second quarter, KB released CZK 193 million over-accrued in the previous years in general administrative expenses for various services from entities of Société Générale Group. Including this one-off positive impact (i.e. reduction) on operating expenditures and also including the prior year's one-off impairment of a head office building of CZK 242 million, reported operating expenses were lower by a slight -0.3%, at CZK 7,595 million.

Profit before allowances for loan losses, provisions for other risk, profit on subsidiaries, and income tax (operating profit) for the first

1 As from 1 January 2018, Komerční banka reclassified fees for early repayment of loans, which compensate the Bank for a loss from necessary adjustments of the hedging position, from 'Net fee and commission income' to 'Net interest income'. Year-on-year commentaries are in comparison with the restated base.

2 Net interest margin stood at 2.3% in the middle of 2017, but the ratios are not fully comparable because of impacts from application of the new IFRS 9 standard on certain balance sheet values.

3 Recalculated to a full-time equivalent number.

half of 2018 was down by 2.7% to CZK 7,802 million. Recurring operating profit, excluding one-off impairment of a building booked in first quarter 2017, as well as one-off creation of the restructuring reserve and one-off release of the over-accrued amounts for corporate services in second quarter 2018, was down by 4.3% to CZK 7,904 million.

Cost of risk, calculated in accordance with the methodology established by the new accounting standard IFRS 9, reached a negative CZK 401 million, inasmuch as the Group was able to release loan loss provisions on certain exposures due to a positive performance from recovery activities. The economic environment in the Czech Republic and Europe was supportive throughout the first half of 2018 and the default rates remained low. Cost of risk in relative terms[1] as measured over the average volume of the lending portfolio in the first half of 2018 reached -13 basis points.

Income from shares in associated undertakings (i.e. Komerční pojišťovna) increased by 4.6% to CZK 113 million. Profit attributable to exclusion of companies from consolidation reached CZK 82 million (CZK 0 in the first half of 2017). That was related to finalising the sale price for KB's stake in Cataps in connection with the sale of an additional 19% in Cataps in February 2018.

Net profit from other assets reached CZK 17 million for the first half, generated from sales of buildings in the held-for-sale portfolio. This had been CZK 1,109 million in the same period of last year, when it had included also a gain from the sale of a headquarters building.

Income tax was higher by 4.8%, at CZK 1,515 million. If the tax effect of the one-off items were to be excluded, income taxes would be up by 0.6%.

KB Group's consolidated net profit for the first half of 2018, at CZK 6,902 million, was lower by 12.4% in comparison with the prior year's first six months. Of this amount, CZK 149 million was profit attributable to the Non-controlling owners of minority stakes in KB's subsidiaries (–19.0% versus the year earlier).

Reported net profit attributable to the Group's equity holders totalled CZK 6,753 million, which is 12.3% less than in the first half of 2017. Recurring attributable net profit (i.e. excluding one-off effects from revaluation and sale of headquarters buildings in 2017 and from finalisation of the sale price for Cataps, creation of the restructuring reserve, and release of over-accrual for corporate services in 2018) was almost stable, dipping by 0.7% year on year to CZK 6,754 million (as one-off items from the first half 2018 generally offset one another).

Other comprehensive income, which derives mainly from revaluations and remeasurements of some hedging, foreign exchange, and securities positions, reached CZK -457 million. The Group's comprehensive income for the first half of 2018 amounted to CZK 6,445 million, of which CZK 150 million was attributable to owners of non-controlling stakes.

1 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.

Statement of financial position

Unless indicated otherwise, the following text provides a comparison of the balance sheet values as of 30 June 2018 with the values from the statement of financial position as of 1 January 2018 after first-time application of IFRS 9. Since 2018, the IFRS 9 reporting standard has introduced a new approach to the classification and measurement of financial assets, a new credit risk impairment methodology, and new hedge accounting rules. Financial assets must be classified based on the entity's business model for managing the financial assets and on the financial assets' contractual cash flow characteristics. According to the determined business model, financial assets are measured at amortised cost, at fair value through profit or loss, or at fair value through other comprehensive income. Due to this change in accounting methodology, comparison with the audited statement of financial position as of 31 December 2017 would be less meaningful.

Assets

As of 30 June 2018, KB Group's total assets had risen by 11.1% year to date to CZK 1,112.7 billion.

Cash and current balances with central banks were down by 34.7%, at CZK 21.3 billion. A large component of this item is comprised of liquidity reserves at central banks.

Financial assets at fair value through profit or loss (trading securities and derivatives and financial assets whose cash flows do not comprise solely payments of principal and interest) increased by 46.1% to CZK 31.5 billion.

The fair value of hedging financial derivatives declined by 22.0% to CZK 10.5 billion.

Year to date, there was a 5.4% rise in financial assets at fair value through other comprehensive income amounting to CZK 25.3 billion. This consisted mainly of public debt securities.

Financial assets at amortised cost increased by 13.0% to reach CZK 1,001.7 billion. The biggest portion of this, (net) loans and advances to customers, went up by 4.9% to CZK 622.8 billion. A 97.3% share in the gross amount of client loans was classified in Stage 1 or Stage 2, while 2.7% of the loans were classified in Stage 3 (non-performing loans). Loans and advances to banks rose by 36.7% and reached CZK 304.5 billion. The majority of this item consists in reverse repos with the central bank. Debt securities went up slightly as well, growing by 5.8% to reach CZK 74.4 billion at the end of the first half.

Revaluation differences on portfolio hedge items were CZK –0.4 billion. Current and deferred tax assets stood at CZK 0.2 billion. Other assets and accrued accounts, which include receivables from security trading and settlement balances, declined overall by 9.7% to reach CZK 5.3 billion. Assets held for sale diminished by 66.4% to CZK 0.1 billion.

Investments in subsidiaries and associates decreased by 12.9%, reaching CZK 1.0 billion.

The net book value of tangible assets rose by 2.1% to CZK 7.6 billion, and intangible assets grew by 3.8% to reach CZK 4.9 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 12.6% higher in comparison to the beginning of 2018 and stood at CZK 1,017.6 billion.

Financial liabilities at amortised costs went up by 12.8% to CZK 959.6 billion. The largest proportion of this total, amounts due to customers, was larger by 9.2% and reached CZK 832.0 billion. This total included CZK 25.3 billion of liabilities from repo operations with clients and CZK 7.9 billion of other payables to customers. Amounts due to banks increased in 2018's first half by 43.2% to CZK 120.3 billion.

The volume outstanding of securities issued grew by 51.9% to CZK 7.3 billion.

Revaluation differences on portfolios hedge items expanded to CZK −4.7 billion. Current and deferred tax liabilities decreased by 15.3% to CZK 0.9 billion. Other liabilities and accruals, which include payables from securities trading and settlement balances, climbed by 14.0% to CZK 21.5 billion.

Provisions increased by 6.7% to CZK 2.1 billion. The provisions for other credit commitments are held to cover credit risks associated with credit commitments issued. The provisions for contracted commitments principally comprise those for ongoing contracted contingent commitments, legal disputes, self insurance, and the retirement benefits plan.

Subordinated debt, at CZK 2.6 billion, was up by 1.9% year to date. As that debt is issued in euro, the change reflects the weakening of the Czech crown over the same period.

Equity
Equity decreased year to date by 3.1% to CZK 95.1 billion inasmuch as the CZK 8.9 billion in the yearly dividend paid out during the second quarter exceeded the profit accrued during the first six months of the current year. Of this total dividend payout, the value going to non-controlling interests reached CZK 3.2 billion. As of 30 June 2018, KB held in treasury 1,193,360 of its own shares constituting 0.63% of the registered capital.

Regulatory capital and capital requirements

Total regulatory capital for the capital adequacy calculation came to CZK 80.9 billion as of 30 June 2018, up 9.0% year on year. Capital adequacy stood at 18.1%. The Core Tier 1 capital amounted to CZK 78.3 billion (+5.5% year on year), and the Core Tier 1 ratio was at 17.5%. The Tier 2 capital amounted to CZK 2.6 billion, or 0.6% of risk-weighted assets.

KB's overall capital requirement as of 30 June 2018 was 15.5% relative to the consolidated volume of risk-weighted assets. As from 1 July 2018, KB's overall capital requirements climbed to approximately 16.0%, the required minimum Core Tier 1 capital level to 12.125%, and the minimum Tier 1 capital ratio to 14.0%. This follows the increase by 50 basis points to 1.00% in the countercyclical capital buffer for Czech exposures with effect from 1 July 2018.

The CNB announced a further rise in this buffer with effect from 1 January 2019 by 25 basis points (to 1.25%) and by an additional 25 basis points (to 1.5%) from 1 July 2019.

As measured by the Liquidity Coverage Ratio, KB's liquidity throughout the first half of 2018 safely met requirements established by the applicable regulations.

Definitions of the performance indicators mentioned herein:

Net interest margin (NIM): 'Net interest income' divided by average interest-earning assets (IEA) year to date (IEA comprise 'Cash and current balances with central banks' [Current balances with central banks only], 'Loans and advances to banks', 'Loans and advances to customers', 'Financial assets at fair value through profit or loss' [debt securities only], 'Financial assets at fair value through profit or loss – non SPPI' [debt securities only], 'Financial assets at fair value through other comprehensive income' [debt securities only], 'Debt securities');

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: 'Total loans and advances to customers, gross' minus 'Other amounts due from customers plus debt securities issued by KB's clients and held by the Bank;

Net loans to deposits: ('Net loans and advances to customers' including debt securities held by KB issued by the Bank's clients less 'reverse repo operations with clients') divided by the quantity (total 'Amounts due to customers' less 'repo operations with clients').

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

(source: Profit and Loss Statement)	1H 2018
Net interest income and similar income, year to date	10,793
Of which:	
Loans and advances at amortised cost	9,112
Debt securities at amortised cost	966
Debt securities, other	208
Financial liabilities at amortised cost	(971)
Hedging financial derivatives - income	4,798
Hedging financial derivatives - expense	(3,321)

(source: Balance Sheet)	30 Jun 2018	1 Jan 2018
Cash and current balances with central banks/ Current balances with central banks	13,324	22,593
Loans and advances to banks	304,488	222,821
Loans and advances to customers	622,803	593,639
Financial assets at fair value through profit of loss/ Debt securities	5,897	1,633
Financial assets at fair value through profit of loss - non SPPI/ Debt securities	2,652	2,694
Financial asset at fair value through other comprehensive income (FV OCI)/ Debt securities	25,030	23,798
Debt securities	74,433	70,340
Interest-bearing assets (end of period)	1,048,627	937,518
Average interest-bearing assets, year to date	993,072	

NIM year to date, annualised	2.17%	

Expected development and main risks to that development in the second half of 2018

In its baseline macroeconomic scenario, Komerční banka expects the Czech economy will grow its output by approximately 3.0%, mainly driven by rising household consumption and fixed investments but with somewhat diminishing contribution of net exports (as imports should expand faster than exports).

In the second half, the situation on the labour market will still be favourable from a workers' perspective, but employers will experience increasing difficulties to find sufficient staff to pursue expansion plans and the mounting wage bill will eat into profit margins.

In combination with year-on-year higher prices of some important inputs, such as crude oil, the higher labour costs will feed inflation. Although the reported year-on-year growth rate should decelerate slightly compared to the high June figure (due to a higher base from 2017), the CNB will probably continue in gradually raising its monetary policy rates.

Competition on the banking market will remain vigorous, marked by excessive Czech crown liquidity in the market, attempts by some players to acquire or regain market shares in certain important product categories, and rapid adoption of technological innovations by clients as well as financial institutions.

Regulation will pose further impediments for the banking business, as the countercyclical capital buffer will be increased by an additional 50 basis points from July (plus a further 25 basis points from January 2019 and again from July 2019) and there will be new limits on the debt-to-income and debt service-to-income ratios of mortgage borrowers. The latter measure may cause some front-loading of mortgage sales before it becomes effective in October.

In such context, KB management expects the annual growth rate of the loan portfolio in 2018 will remain in the mid- to low-single digits, although it will be somewhat faster than the 2% pace achieved in 2017. This growth will be driven mainly by retail lending. Competition on the mortgage market may intensify especially before the CNB's new regulations begin from October to reduce access to housing credit for a part of the population. Given the favourable labour market situation and high levels of household confidence, unsecured lending to consumers could see an accelerating trend in 2018's remaining months. Business lending may not grow much, given the increasing bond issuance and intense competition, as well as still-abundant liquidity at many companies. Total deposits will probably grow faster than loans, and particularly in the retail and SME segments. In the situation of rising interest rates, clients may increasingly prefer to place their cash reserves into saving and term accounts instead of current accounts. The volume of assets under management in mutual funds, life insurance, and pension funds should continue to expand.

KB Group's total net operating income for 2018 should end at a similar level as in 2017. Growth in net interest income will be driven by increasing volumes of loans and deposits, as well as rising interest rates. The upside will be limited, however, by competitive pressure on lending spreads. Income from fees and commissions will diminish marginally, despite overall growth in the numbers and activity of clients, mainly due to residual effects from previous repricing of certain services. Net profit from financial operations will decrease significantly on a year-on-year basis, because the previous year's gains generated by significant customers' hedging activity around the time of the currency floor's release had been extraordinary.

Recurring operating expenditures are targeted to grow at below the rate of inflation. Personnel expenses will be the main contributor to that growth but depreciation and amortisation charges also will rise, reflecting investments into new software applications, equipment, and facilities. Administrative expenses will thus need to be managed very vigorously.

The situation of a net release of provisions for credit losses is exceptional. The pace of future normalisation of risk costs will depend mainly on how macroeconomic conditions develop in the Czech Republic, and to some extent in Slovakia, or, possibly, on individual circumstances of clients with larger exposures. The expected continuation of a supportive economic trend is consistent with cost of risk for 2018 that is significantly below a normalised rate of 30 to 40 basis points.

Among the key risks to the expectations described above (albeit with a low probability of their occurring during 2018) are the following: an abrupt worsening of the macroeconomic environment, caused, for example, by imposition of major obstacles to international trade; a solitary impairment of a large credit exposure; or a significant worsening of the competitive situation on the Czech banking market leading to material erosion of profit spreads on key products.

The management expects that KB's operations will generate sufficient profit in 2018 to cover the Group's capital needs ensuing from its growing volume of assets as well as to pay 65% of consolidated net profit attributable to shareholders in dividends.

Developments in KB's corporate governance

The General Meeting held on 25 April 2018 approved the Board of Directors' report on the Bank's business activity and state of its assets for the year 2017 as presented. Moreover, the General Meeting approved the annual financial statements and the consolidated financial statements for 2017, as well as the distribution of the net profit from 2017. The latter included a dividend pay-out of CZK 8.9 billion, which amounts to CZK 47 per share. The record day was 18 April 2018 and the dividend payment day was 28 May 2018.

The General Meeting also elected Mr Petr Dvořák as a member of the Audit Committee with effect from 26 April 2018. The General Meeting decided upon amendments to the Bank's Articles of Association in order to ensure their compliance with the currently valid law. Furthermore, the General Meeting decided once again about the conditions for acquiring the Bank's shares into treasury and appointed the company Deloitte Audit as the external auditor of Komerční banka for the year 2018.

With effect from 30 June 2018, Mr Jan Pokorný has decided due to personal reasons to resign his membership on the Board of Directors of Komerční banka and the position of Senior Executive Director for Large Corporate Clients, Structured Financing, Investment Banking, and KB's Branch in Slovakia.

Effective from 31 July 2018, Mr Peter Palečka has terminated his membership on the Board of Directors of Komerční banka and the position of Senior Executive Director, Corporate Secretary. Mr Palečka will remain at KB until the end of 2018 as an advisor to the CEO.

On the proposal of the Nominations Committee and with the consent of the Czech National Bank, Komerční banka's Supervisory Board elected Mr David Formánek and Mr Miroslav Hiršl as members of the Board of Directors with effect from 1 August 2018.

Changes in Group structure

With effect from 1 January 2018, the company PSA FINANCE ČESKÁ REPUBLIKA s.r.o. was merged with its sole owner, ESSOX s.r.o. That entity will continue to operate under the name ESSOX s.r.o. As of 1 January 2018, the company PSA FINANCE SLOVAKIA, s.r.o. changed its name to ESSOX FINANCE, s.r.o., with registered address at Karadžičova 16, 821 08 Bratislava, Slovak Republic. ESSOX FINANCE, s.r.o. is fully owned by ESSOX s.r.o. ESSOX s.r.o. is owned by Komerční banka (with a 50.93% stake) and SG Consumer Finance (with the remaining 49.07%).

On 27 February 2018, KB announced the sale of its 19% stake in the company Cataps, s.r.o., with registered office at Lazarská 11/6, 120 00 Prague 2, registration No. 036 33 144 (Cataps) to Worldline SA/NV, with registered office at Haachtsesteenweg 1442, 1130 Brussels, Belgium (Worldline). Upon concluding this transaction, KB's remaining stake is 1% of Cataps.

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 in making financial or operational decisions. As of 30 June 2018, the Group was controlled by Société Générale, which owns 60.35% of the Bank's 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 were carried out on an arm's length basis.

Amounts due to and from the Group companies

As of 30 June 2018, the Group had deposits of CZK 2,516 million due to the associate, Komerční pojišťovna, a.s. Interest paid from deposits amounted to CZK 10 million. The positive fair value of financial derivatives in relation to the associate, Komerční pojišťovna, a.s. amounted to CZK 973 million and the negative fair value to CZK 252 million. Interest expense from financial derivatives amounted to CZK 242 million and interest income from financial derivatives to CZK 366 million. The book value of mortgage bonds issued by the Bank was CZK 815 million and interest expense from mortgage bonds amounted to CZK 10 million. Fee expense totalled CZK 42 million, fee income CZK 193 million, and insurance expense CZK 8 million.

Amounts due to and from Société Générale Group entities

Principal balances due from Société Générale Group entities consist of the following:

(CZKm)	30 June 2018		1 Jan 2018	
	Total	Of which derivatives	Total	Of which derivatives
ALD Automotive s.r.o. (Czech Republic)	6,628	0	6,185	0
ALD Automotive s.r.o. (Slovak Republic)	103	0	160	0
BRD – GROUPE Société Générale SA	62	0	22	0
PJSC Rosbank	331	0	205	0
SG Bruxelles	143	0	26	0
SG Expressbank	50	0	56	0
SG New York	1	0	0	0
SG Paris	13,024	5,872	8,771	4,633
SG S.A. oddzial w Polsce	4	0	1	0
SG Zurich	135	0	175	0
SGA Société Générale Acceptance	2,652	0	2,708	0
Société Générale China Limited	32	0	1	0
Société Générale International Limited	3,235	0	2,572	0
SKB Banka D.D. Ljubljana	1	0	1	0
SG Banka Srbija	0	0	1	0
Total	**26,401**	**5,872**	**20,884**	**4,633**

Principal balances owed to Société Générale Group entities consist of the following:

(CZKm)	30 June 2018		1 Jan 2018	
	Total	Of which derivatives	Total	Of which derivatives
ALD Automotive s.r.o. (Czech Republic)	367	0	368	0
ALD Automotive s.r.o. (Slovak Republic)	4	0	27	0
BRD – GROUPE Société Générale SA	76	0	79	0
Crédit du Nord	27	0	12	0
PEMA Praha, spol. s r.o.	59	0	70	0
PJSC Rosbank	0	0	1	0
SG Amsterdam	29	0	23	0
SG Banques au Liban	1	0	2	0
SG ISSUER	1	0	1	0
SG Frankfurt	72	0	41	0
SG London	190	0	78	0
SG New York	12	0	16	0
SG Milan	4	0	0	0
SG Paris	68,323	8,697	38,863	6,988
SG Private Banking /Suisse/ S.A.	149	0	67	0
SG S.A. oddzial w Polsce	3	0	98	0
SG Zurich	8	0	1	0
SGSS Nantes	0	0	11	0
Société Générale Bank & Trust	83	0	123	0
SKB Banka D.D. Ljubljana	1	0	0	0
SG Express Bank	9	0	2	0
SG Option Europe	1	0	1	0
SOGEPROM Česká republika s.r.o.	5	0	5	0
Total	**69,424**	**8,697**	**39,889**	**6,988**

Amounts due to and from Société Générale Group entities principally comprise balances of current and overdraft accounts, nostro and loro accounts, subordinated debt, issued loans, interbank market loans and placements, deposited margins in favour of a counterparty and fair values of derivatives.

As of 30 June 2018, the Group also carried off-balance sheet exposures to the Société Générale Group, of which off-balance sheet nominal assets and liabilities, respectively, amounted to CZK 520,171 million and CZK 495,879 million. 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 30 June 2018 the Group also carried other amounts due to and from Société Générale Group entities which are immaterial.

During the period ended 30 June 2018, the Group realised total income of CZK 17,277 million and total expenses of CZK 17,448 million in relation to Société Générale Group entities. That included income from interbank deposits, fees from securities transactions, profit from financial operations and interest income on hedging derivatives. Expenses comprised those of interbank deposits and subordinated debt, a loss from financial operations, interest expense on hedging derivatives, and expenses related to the provision of management, consultancy and software services.

Amounts due from the Persons managing key function and Supervisory Boards

In respect of loans and guarantees as of 30 June 2018, the Group recorded receivables from loans granted to the members of the Board of Directors and Supervisory Board totalling CZK 12 million (CZK 12 million as of 1 January 2018). During the first half of 2018, no drawings were made under the loans granted. During the first half of 2018, loan repayments amounted to CZK 1 million.

Report on Financial Results as of 30 June 2018 according to IFRS

Contents

Consolidated Income Statement and Statement of Comprehensive Income

for the period ended 30 June 2018

Consolidated Income Statement			Restated
(CZKm)	Note	30 Jun 2018	30 Jun 2017
Interest income and similar income		15,085	13,134
Interest expense and similar expense		(4,292)	(2,724)
Net interest income and similar income		**10,793**	10,410
Net fee and commission income		3,077	3,125
Net profit on financial operations		1,407	1,992
Dividend income		3	3
Other income		117	100
Net operating income		**15,397**	15,630
Personnel expenses		(3,998)	(3,630)
General administrative expenses		(2,714)	(2,935)
Depreciation, amortisation and impairment of operating assets		(883)	(1,049)
Total operating expenses		**(7,595)**	(7,614)
Operating profit		**7,802**	8,016
Cost of risk		**401**	94
Income from share of associated undertakings		113	108
Net profit/(loss) on subsidiaries and associates		82	0
Gain on a bargain purchase		2	0
Net profits on other assets		17	1,109
Profit before income taxes		**8,417**	9,327
Income taxes		(1,515)	(1,446)
Net profit for the period		**6,902**	7,881
Profit attributable to the Non-controlling owners		149	184
Profit attributable to Group's equity holders		6,753	7,697
Earnings per share/diluted earnings per share (in CZK)		**35.76**	40.76

Consolidated Statement of Comprehensive Income		
(CZKm)	30 Jun 2018	30 Jun 2017
Net profit for the period	**6,902**	7,881
Items that will not be reclassified to Income Statement		
Remeasurement of retirement benefits plan, net of tax	0	0
Revaluation of equity securities, net of tax	40	33
Items that may be reclassified subsequently to Income Statement		
Cash flows hedging		
- Net fair value gain/(loss), net of tax	(143)	(3,657)
- Transfer to net profit/(loss), net of tax	(39)	(1,511)
Hedge of a foreign net investment	(50)	85
Foreign exchange gain/(loss) on translation of a foreign net investment	53	(103)
Revaluation of debt securities, net of tax	(269)	(688)
Revaluation of debt securities (associated undertakings), net of tax	(49)	(72)
Other income from associated undertakings	0	0
Other comprehensive income for the period, net of tax	**(457)**	(5,913)
Comprehensive income for the period, net of tax	**6,445**	1,968
Comprehensive income attributable to Non-controlling owners	150	186
Comprehensive income attributable to Group's equity holders	6,295	1,782

The accompanying Notes are an integral part of this Consolidated Income Statement and Statement of Comprehensive Income.

Consolidated Statement of Financial Position

As of 30 June 2018

(CZKm)	Note	30 Jun 2018	1 Jan 2018
Assets			
Cash and current balances with central banks		21,318	32,663
Financial assets at fair value through profit or loss - trading		28,800	18,841
Financial assets at fair value through profit or loss - non-SPPI	4	2,652	2,694
Positive fair value of hedging financial derivatives		10,459	13,408
Financial assets at fair value through other comprehensive income	5	25,332	24,039
Financial assets at amortised cost	6	1,001,724	886,800
Revaluation differences on portfolios hedge items		(360)	(251)
Current tax assets		146	42
Deferred tax assets		70	254
Prepayments, accrued income and other assets		5,257	5,822
Investments in associates and unconsolidated subsidiaries		1,049	1,181
Intangible fixed assets		4,861	4,684
Tangible fixed assets		7,563	7,404
Goodwill		3,752	3,752
Assets held for sale		107	319
Total assets		**1,112,710**	1,001,652
Liabilities			
Amounts due to central banks		1	1
Financial liabilities at fair value through profit or loss		24,408	19,304
Negative fair value of hedging financial derivatives		11,199	10,329
Financial liabilities at amortised cost	8	959,647	850,925
Revaluation differences on portfolios hedge items		(4,721)	(1,468)
Current tax liabilities		36	263
Deferred tax liabilities		821	749
Accruals and other liabilities		21,519	18,869
Provisions	9	2,089	1,958
Subordinated debt		2,608	2,560
Total liabilities		**1,017,607**	903,490
Shareholders' equity			
Share capital		19,005	19,005
Share premium and reserves		72,879	75,445
Minority equity		3,219	3,712
Total shareholders' equity		**95,103**	98,162
Total liabilities and shareholders' equity		**1,112,710**	1,001,652

The accompanying Notes are an integral part of this Consolidated Statement of Financial Position.

Consolidated Statement of Changes in Shareholders' Equity

for the period ended 30 June 2018

(CZKm)	Share capital	Own shares	Capital funds and retained earnings*	Share-based payment	Revaluation of equity securities	Remeasurement of retirement benefits plan	Cash flow hedging	Hedge of a foreign net investment	Revaluation of debt securities	Total	Non-controlling interest	Total, including non-controlling interest
Balance as of 31 December 2017	**19,005**	**(577)**	**75,352**	**443**	**77**	**(154)**	**119**	**(7)**	**2,291**	**96,549**	**3,797**	**100,346**
Changes in accounting policies	0	0	(672)	0	0	0	0	0	(1,427)	(2,099)	(85)	(2,184)
Balance as of 1 January 2018	19,005	(577)	74,680	443	77	(154)	119	(7)	864	94,450	3,712	98,162
Treasury shares, other	0	0	55	16	0	0	0	0	0	71	1	72
Payment of dividends	0	0	(8,932)	0	0	0	0	0	0	(8,932)	(644)	(9,576)
Transactions with owners	**0**	**0**	**(8,877)**	**16**	**0**	**0**	**0**	**0**	**0**	**(8,861)**	**(643)**	**(9,504)**
Profit for the period	0	0	6,753	0	0	0	0	0	0	6,753	149	6,902
Other comprehensive income for the period, net of tax	0	0	(49)**	0	40	0	(182)	2	(269)	(458)	1	(457)
Comprehensive income for the period	**0**	**0**	**6,704**	**0**	**40**	**0**	**(182)**	**2**	**(269)**	**6,295**	**150**	**6,445**
Balance as of 30 June 2018	**19,005**	**(577)**	**72,507**	**459**	**117**	**(154)**	**(63)**	**(5)**	**595**	**91,884**	**3,219**	**95,103**

*Capital and reserve funds and retained earnings as of 30 Jun 2018 consist of other funds created from profit in the amount of CZK 4,671 million (1 Jan 2018: CZK 4,671 million), net profit from the period in the amount of CZK 6,753 million (1 Jan 2018: CZK 14,930 million) and retained earnings in the amount of CZK 61,083 million (1 Jan 2018: CZK 55,079 million).

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

(CZKm)	Share capital	Share premium and own shares	Capital and reserve funds and retained earnings*	Share-based payment	Revaluation of equity securities	Remeasurement of retirement benefits plan	Cash flow hedging	Hedge of a foreign net investment	Revaluation of debt securities	Total	Non-controlling interest	Total, including non-controlling interest
Balance as of 31 December 2016	**19,005**	**(577)**	**68,063**	**406**	**6**	**(131)**	**11,379**	**1**	**3,418**	**101,570**	**3,831**	**105,401**
Treasury shares, other	0	0	43	15	0	0	0	0	0	63	1	64
Payment of dividends	0	0	(7,602)	0	0	0	0	0	0	(7,602)	(375)	(7,977)
Transactions with owners	**0**	**0**	**(7,554)**	**15**	**0**	**0**	**0**	**0**	**0**	**(7,539)**	**(374)**	**(7,913)**
Profit for the period	0	0	7,697	0	0	0	0	0	0	7,697	184	7,881
Other comprehensive income for the period, net of tax	0	0	(72)**	0	33	0	(5,168)	(15)	(688)	(5,910)	(3)	(5,913)
Comprehensive income for the period	**0**	**0**	**7,625**	**0**	**33**	**0**	**(5,168)**	**(15)**	**(688)**	**1,787**	**181**	**1,968**
Balance as of 30 June 2017	**19,005**	**(577)**	**68,134**	**421**	**39**	**(131)**	**6,211**	**(14)**	**2,730**	**95,818**	**3,638**	**99,456**

*Capital and reserve funds and retained earnings as of 30 Jun 2017 consist of other funds created from profit in the amount of CZK 4,671 million (31 Dec 2016: CZK 4,670 million), net profit from the period in the amount of CZK 7,697 million (31 Dec 2016: CZK 13,688 million) and retained earnings in the amount of CZK 55,766 million (31 Dec 2016: CZK 49,705 million).

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

The accompanying Notes are an integral part of this Consolidated Statement of Changes in Shareholders' Equity.

Consolidated Cash Flow Statement

for the period ended 30 June 2018

(CZKm)	30 Jun 2018	30 Jun 2017
Profit before taxes	**8,417**	9,327
CASH FLOWS FROM OPERATING ACTIVITIES		
Non-cash and other adjustments:		
Creation and release of allowances and provisions	(477)	(234)
Amortisation expense on tangible and intangible fixed assets	883	1,049
Gains/(losses) from the sale of assets	(17)	1
Revaluation of derivatives	823	(1,924)
Accrued interest, amortisation of discount and premium	(779)	(456)
Profit or (Loss) from subsidiaries and associates	(200)	(111)
Other changes	364	779
Operating profit before change in operating assets and liabilities	**9,014**	8,431
Changes in assets and liabilities from operating activities after non-cash adjustments:		
Amounts due from banks (received/paid)	(81,334)	(9,660)
Loans and advances to customers	(28,138)	(22,038)
Debt securities at amortised cost	(2,984)	4,920
Financial assets at fair value through other comprehensive income	(1,012)	628
Financial assets at fair value through profit and loss - non-SPPI	(5,259)	4,165
Other assets	429	(1,022)
Amounts due to banks (received/paid)	38,326	32,860
Amounts due to customers	69,486	81,219
Financial liabilities at fair value through profit and loss	147	83
Other liabilities	2,067	8,784
Net cash flows from operating assets and liabilities	**(8,272)**	99,939
Net cash flows from operating activities before taxes	742	108,370
Income tax paid	(1,478)	(1,675)
Net cash flows from operating activities	**(736)**	106,695
CASH FLOWS FROM INVESTMENT ACTIVITIES		
Dividends received	219	207
Purchase of tangible and intangible assets	(1,156)	(1,039)
Sale of tangible and intangible assets	17	57
Purchase of investments in subsidiaries and associates	0	0
Sale of investments in subsidiaries and associates	221	1,486
Net cash flows from investment activities	**(699)**	711

(CZKm)	30 Jun 2018	30 Jun 2017
CASH FLOWS FROM FINANCING ACTIVITIES		
Dividends paid	(8,876)	(7,495)
Dividends paid to non-controlling interest	(644)	(375)
Purchase of own shares	0	0
Securities issued	2,189	1,933
Securities redeemed*	0	(836)
Subordinated debts	52	0
Increase in minority equity	0	0
Net cash flows from financing activities	**(7,279)**	(6,773)
Net increase/(decrease) in cash and cash equivalents	**(8,714)**	100,633
Cash and cash equivalents at the beginning of the year	24,308	110,064
Net increase/(decrease) in cash and cash equivalents	(8,714)	100,633
Foreign exchange differences on cash and cash equivalents at the beginning of the year	111	(139)
Cash and cash equivalents at the end of the year	**15,705**	210,558
Interest received	**13,555**	12,207
Interest paid	**(3,541)**	(2,350)

*The amount also includes coupon payments received and paid.

The accompanying Notes are an integral part of this Consolidated Cash Flow Statement.

Notes to the Consolidated Financial Statements
Period ended 30 June 2018

1. Events for the period ended 30 June 2018

Dividends declared in respect of the year ended 31 December 2017
In accordance with the resolution of the Bank's General Meeting of Shareholders held on 25 April 2018, the Bank paid out CZK 8,932 million (CZK 47 per share before tax) in dividends and the remaining balance of the net profit was allocated to retained earnings. Moreover, the Group decided to pay out CZK 189 million in dividends to non-controlling owners of ESSOX s.r.o. and CZK 455 million to non-controlling owners of SG Equipment Finance Czech Republic.

Changes in equity investments in subsidiaries and associates in 2018
As of the effective date 1 January 2018, ESSOX s.r.o. and PSA FINANCE CZECH REPUBLIC, s.r.o. were merged into ESSOX s.r.o. ESSOX s.r.o. is a subsidiary of the Bank and PSA FINANCE CZECH REPUBLIC, s.r.o. had been a subsidiary of ESSOX s.r.o.

As of 1 January 2018, PSA FINANCE SLOVAKIA, s.r.o. changed its business name to ESSOX FINANCE, s.r.o. ESSOX FINANCE, s.r.o. is a subsidiary of ESSOX s.r.o.

Starting from the accounting period beginning on 1 January 2018, Modrá pyramida stavební spořitelna, a.s. changed its accounting and reporting policies from Czech GAAP (Act No. 563/1991 Coll., on Accounting; Decree of the Ministry of Finance of the Czech Republic No. 501/2002 Coll., implementing certain provisions of Act No. 563/1991 for banks and financial institutions; and relevant accounting standards prepared and promulgated by the Ministry of Finance of the Czech Republic) to International Financial Reporting Standards as adopted by the European Union.

In February 2018, the Bank exercised its right to sell 19% of the shares in Cataps, s.r.o. to Worldline SA/NV. As of the end of 2017 the shares had been classified as 'Assets held for sale'. The result of the transaction is recognised and presented in the 'Income from share of associated undertakings'. Upon conclusion of the transaction, the Bank holds a remaining interest of 1% in Cataps, s.r.o. The Bank and Worldline will continue to work closely together within the KB SmartPay alliance.

With effect from 1 June 2018, the company STD2 (KB's wholly owned subsidiary) changed its legal form from that of a public-limited company to that of a limited-liability company.

The Consolidated Financial Statements presented for the period ended 30 June 2018 are based on the current best estimates. The management of the Group believes they 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.

Seasonality and unusual items
The Group's principal activities are not significantly influenced by seasonality, and in the first half of 2018 no unusual transaction occurred.

2. Principal accounting policies

These Consolidated Financial Statements were neither audited nor reviewed by an auditor. The presented information is consistent with IAS 34 Interim Financial Reporting requirements.

With a transition date of 1 January 2018, the Group has newly applied IFRS 9 Financial Instruments and related relevant amendments of IFRS 7 Financial instruments: Disclosures.

The replacement of the previous standard IAS 39 by the new standard IFRS 9 has resulted in significant changes in accounting policies for financial instruments (classification and measurement, impairment of financial assets). Given the extent of the changes, a complete set of principal accounting policies is included in this publication.

As permitted by the transitional provisions of IFRS 9, the Group elected not to restate comparative information. Therefore the comparative information for 2017 is reported under IAS 39 and is not comparable to the information presented for 2018. Differences arising from the adoption of IFRS 9 have been recognised directly in the opening balance of equity as of 1 January 2018 and are disclosed in Note 2.4. The Group has also elected, as a policy choice permitted under IFRS 9, to continue to apply hedge accounting in accordance with IAS 39.

2.1. Underlying assumptions of the Consolidated Financial Statements

2.1.1. 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).

2.1.2. 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.

2.2. Basis of preparation

2.2.1. 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.

2.2.2. Historical cost

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

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’.

2.2.3. 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, financial assets at fair value through other comprehensive income or hedging derivatives;
- The business model evaluation for managing financial assets;
- The value of intangible assets, except goodwill;
- The amount of impairment of assets;
- Provisions recognised under liabilities;
- The initial value of goodwill for each business combination;
- 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; and
- Assessment of the substance of participation interests in Group entities.

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.

2.2.4. 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 control, the Group considers all relevant facts and circumstances while taking into account in particular voting rights, potential voting rights and contractual arrangements. This assessment may require the use 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 months of given transactions. 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 in the net assets of the investee.

2.3. Principal accounting policies

2.3.1. Transactions in foreign currencies

2.3.1.1. 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 and a subsidiary, ESSOX FINANCE, s.r.o., in the Slovak Republic and a subsidiary, Bastion European Investments S.A., in Belgium. These all have the euro as their functional currency and are considered as foreign operations from a financial reporting point of view.

2.3.1.2. 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 (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 on 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 on 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'.

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, however, related foreign exchange rate differences are recognised in the same way. These non-monetary items include equity instruments, for which the Group has decided at initial recognition to use the irrevocable election to measure these at fair value and with changes recognised in Other Comprehensive Income without subsequent recycling into profit or loss on realisation. Also recognised in Other Comprehensive Income are foreign exchange rate differences related to the fair value revaluation of debt instruments held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets (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 positions 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 recognised in 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 within 'Equity' in the line 'Hedge of a foreign net investment'.

2.3.2. Recognition of income and expenses

2.3.2.1. 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 rate hedging derivatives, are recognised on an accrual basis within 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 2.3.5.7 Effective interest rate method). For credit-impaired financial assets, interest income is calculated by applying the effective interest rate to the amortised cost of the asset, i.e. an amount adjusted for expected credit losses over the life of the asset. Interest income and expense related to interest rate hedging derivatives are recognised in the aforementioned lines 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'.

2.3.2.2. Net fee and commission income

The recognition of income from fees and commissions depends on the purpose for which any given 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'.

2.3.2.3. 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 financial assets held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets.

Also recognised in this line are interest income and expense related to interest-bearing instruments classified as financial assets or financial liabilities at fair value through profit or loss.

2.3.2.4. Dividend 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'.

2.3.3. 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.

2.3.4. 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.

2.3.5. Financial instruments

2.3.5.1. 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. Gains and losses from the changes in fair value are recognised depending on the type of financial instrument and taking into account the classification based on both the business model and contractual cash flow characteristics (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).

2.3.5.2. 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, within 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 of revenues recognised in the Statement of Income in accordance with IFRS 15 (within the Statement of Financial Position in the line ‘Accruals and other liabilities’), or the impairment for expected credit losses from 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 within 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 within the Statement of Income in the line ‘Cost of risk’.

2.3.5.3. “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. The Group trades financial instruments only for the prices quoted in active markets. 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).

2.3.5.4. Financial assets classification and subsequent measurement

The classification of the Group‘s financial instruments is determined at the date of a given instrument’s initial recognition and is unchanged throughout the period of holding that financial instrument, with rare exceptions occuring for situations mentioned in 2.3.5.5 Reclassification of financial assets and liabilities.

Depending on the nature of the financial instrument and evaluation of both the business model for managing the financial asset and the its contractual cash flow characteristics, a financial instrument held by the Group is measured subsequent to initial recognition at:

I. Amortised costs;
II. Fair value through other comprehensive income; or
III. Fair value through profit or loss.

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”).

The selection of valuation method differs for loans and debt instruments, equity instruments and derivatives.

2.3.5.4.1. Loans and debt instruments

Loans and debt instruments are non-derivative financial assets with legally enforceable fixed or determinable payments and fixed maturities.

Classification and subsequent measurement of loans and debt instruments are determined based on the evaluation of:

- The Group’s business model for managing the financial assets; and
- A financial asset’s contractual cash flow characteristics (applying the solely payment of principal and interest SPPI test).

Description of business models

The business model is determined on a level at which the financial assets are jointly managed to achieve a particular business objective. The business model does not depend on management’s intentions for an individual instrument, but it reflects the way a portfolio of financial assets is managed in order to generate cash flows under standard economic conditions. The Group classifies financial assets into the following business models:

(i) “Hold to collect contractual cash flows”;
(ii) “Hold to collect contractual cash flows and sell”; or
(iii) “Held for trading”.

(i) “Hold to collect contractual cash flows” business model

Loans and debt instruments that the Group classifies in the business model “Hold to collect contractual cash flows” are held in order to collect contractual cash flows over the life of the instrument. The Group expects and has the intention and ability to hold these loans and debt instruments until maturity. In determining whether cash flows are going to be realised by collecting the financial assets’ contractual cash flows, the Group considers frequency, value and timing of sales in prior periods, the reasons for those sales and expectations about future sales activity for a given portfolio.

The Group admits the following sales that are consistent with the business model “Hold to collect contractual cash flows”:

- sales due to an increase in the assets’ credit risk irrespective of their frequency and value;
- sales made to manage credit risk concentration if those sales are infrequent (even if significant in value) or insignificant in value (even if frequent);
- sales made close to the maturity of the assets when the proceeds from the sales approximate the collection of the remaining contractual cash flows;
- sales made based on requirements imposed by third parties, such as regulatory bodies.

The Group classifies into the business model “Hold to collect contractual cash flows”: (i) all loans and receivables; and (ii) all debt instruments that are not part of liquidity buffer and are not determined for trading; and (iii) from 1 January 2018 onwards all new investments into CZK-denominated bonds constituting part of liquidity buffer with maturity up to 12 years.

(ii) “Hold to collect contractual cash flows and sell” business model

Loans and debt instruments that the Group classifies in the business model “Hold to collect contractual cash flows and sell” are held in order to achieve collecting contractual cash flows and selling financial assets. In this type of business model, both collecting contractual cash flows and selling financial assets are integral to achieving the objective of the business model. The objective of this business model is to manage the Group’s everyday liquidity needs. The Group expects that in case of a structural deficit of assets and liabilities, sales of these loans and debt instruments will be realised to cover the lack of liquid assets.

As compared to the business model whose objective is to hold financial assets to collect contractual cash flows, the Group expects greater frequency and value of sales. Selling financial assets is not an incidental activity, but an integral part of achieving the business model’s objective. There is no threshold for the frequency or value of sales that must occur in this business model, however, as both collecting contractual cash flows and selling financial assets are integral to achieving its objective.

The Group classifies into the business model “Hold to collect contractual cash flows and sell”: (i) all EUR-denominated government bonds (or quasi-government bonds) part of liquidity buffer; and (ii) from 1 January 2018 onwards all new investments into CZK-denominated government bonds part of liquidity buffer and, in accordance with the Group’s internal rules, with maturity either longer than 12 years or longer than 10 years.

(iii) “Held for trading” business model

Loans and debt instruments that the Group classifies in the business model “Held for trading” are held with the objective of realising cash flows through the sale of the assets. The Group makes decisions based on the assets’ fair values and manages the assets to realise those fair values.

The Group classifies into the business model “Held for trading” all other loans and debt instruments that are not part of the business model “Hold to collect contractual cash flows” or “Hold to collect contractual cash flows and sell”.

Contractual cash flows characteristics test

Based on an assessment of the contractual cash flow characteristics, the Group ascertains whether the contractual cash flows on loans and debt instruments are solely payments of principal and interest on the principal amount outstanding. Principal is the fair value of the financial asset at initial recognition. Interest consists in particular of consideration for the time value of money and credit risk; or it also can include consideration for liquidity risk, administrative costs or profit margin that is consistent with the basic lending arrangement.

Measurement at amortised costs
After initial recognition, loans and debt instruments are subsequently measured at amortised costs if both of the following conditions are met: the financial asset is held within the business model "Hold to collect contractual cash flows" and the contractual cash flows correspond to the characteristics of payments of principal and interest on the principal amount outstanding.

Amortised costs constitute the amounts at which the financial instruments are measured at initial recognition minus the principal repayments and using the effective interest method plus or minus fees that are an integral part of the financial asset and amortisation of premium or discount (i.e. any difference between the initial amount and the maturity amount) and further reduced by any loss allowance for expected credit losses. The interest income is recognised in the line 'Interest income and similar income' within the Statement of Income. The impairment loss is recognised within the Statement of Income in the line *'Cost of risk'*.

Measurement at fair value through other comprehensive income
After initial recognition, loans and debt instruments are subsequently measured at fair value and with changes being recognised in other comprehensive income if both of the following conditions are met: the financial asset is held within the business model "Hold to collect contractual cash flows and sell" and the contractual cash flows correspond to the characteristics of payments of principal and interest on the principal amount outstanding.

Unrealised gains or losses from fair value changes as well as gains or losses from changes in fair value resulting from changes in foreign exchange rates are recognised within Other Comprehensive Income in the line 'Revaluation of debt securities, net of tax'.

When holding the financial asset, loss allowances are recognised. Unlike financial assets measured at amortised costs however, the loss allowances are not presented separately in the Statement of Financial Position and do not reduce the carrying amount of the financial asset. The loss allowances are recognised directly in Other Comprehensive Income and within the Statement of Income in the line 'Cost of risk'.

Gains or losses from changes in foreign exchange rates on loans and debt instruments are recognised within the Statement of Income in the line 'Net profit/(loss) on financial operations', except that exchange rate gains or losses related to fair value revaluation are recognised within Other Comprehensive Income. Accrued interest income is recognised within the Statement of Income in the line 'Interest income and similar income'.

When a financial asset is derecognised, the cumulative gain or loss previously recognised in Other Comprehensive Income is recognised within the Statement of Income in the line 'Net profit/(loss) on financial operations'.

Measurement at fair value through profit or loss
After initial recognition, loans and debt instruments are subsequently measured at fair value and with changes being recognised in profit or loss if the financial asset is classified in the business model "Held for trading" or if the contractual cash flows do not correspond to the characteristics of payments of principal and interest on the principal amount outstanding.

The category fair value through profit or loss is a residual category. The Group classifies loans and debt instruments into this category if they do not meet the criteria for measurement at amortised cost or at fair value through other comprehensive income.

Unrealised gains and losses as well as realised gains or losses arising from revaluation of those financial assets, interests and foreign exchange rate differences are recognised within the Statement of Income in the line 'Net profit/(loss) on financial operations'. Considering the fact that the changes of fair value are recognised directly in profit or loss, these financial assets are not subject to impairment testing and the impairment losses are not recognised.

2.3.5.4.2. Equity instruments
Equity instruments are non-derivative financial assets entitling their owners to participate in the exercise of ownership rights without a defined maturity and without legally enforceable fixed or determinable payments.

Equity instruments are measured at fair value and with changes being recognised in profit or loss, except that there exists an option at initial recognition to measure the equity instrument at fair value and with changes being recognised in other comprehensive income without subsequent recycling into profit or loss on disposal. This election is irrevocable and is made on an instrument-by-instrument basis. For this reason, equity instruments are not subject to impairment testing and the impairment losses are not recognised.

The Group may exercise this option only for instruments that are not held for trading. When exercising the option, the disposal will not result in realisation and recognition of the disposal's result in the Statement of Income; instead, it will remain in the Other Comprehensive Income of the Group and, after approval by the General Meeting, will eventually be transferred to retained earnings. Dividend income arising from equity instruments is recognised when the right to receive dividends is established and it is presented within the Statement of Income in the line 'Dividend income'.

The Group applies the option (measurement of equity instruments at fair value through other comprehensive income) for investments in which it holds equity interests of less than 20%. This approach is based on the Group's intention to continue holding these investments over the long-term or the existence of a long-term restriction against selling these investments.

2.3.5.4.3. 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, price of a financial instrument, price of a commodity, 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 respond similarly 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 for hedging.

Derivatives held for trading 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.

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. As permitted by IFRS 9, the Group applies hedge accounting methods in accordance with IAS 39. 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 within the Statement of Income in the 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 within 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 foreign currency risk of financial assets (loans and debt instruments with fixed interest rates) and interest rate risk of deposits, repos, mortgage bonds issued, as well as selected portfolios of building savings. The effectiveness of a hedge is regularly tested through prospective and retrospective tests on a quarterly basis.

If a 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.

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' within 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 the cash flows of 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 subsidiaries Bastion European Investments S.A. and ESSOX FINANCE, s.r.o. 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.

2.3.5.4.4. Financial liabilities

The Group classifies financial liabilities into the categories 'Financial liabilities at amortised costs' *or 'Financial liabilities at fair value through profit or loss'*, depending on the methods for managing the performance of the financial liability.

When the performance of the financial liability is managed based on trading that mostly reflects active and frequent purchases and sales, (i.e. financial instruments held for trading that are mostly used to generate profit from short-term fluctuations in price or margin), the Group classifies these financial liabilities after initial recognition as subsequently measured at fair value through profit or loss. Such financial liabilities include only liabilities from disposed securities and trading derivatives with a negative value. They are recognised within the Statement of Financial Position in the line 'Financial liabilities at fair value through profit or loss'.

Unrealised as well as realised gains or losses arising from revaluation of those financial liabilities, interests and foreign exchange rate differences are recognised within the Statement of Income in the line 'Net profit/(loss) on financial operations'.

After their initial recognition, all other financial liabilities are subsequently measured at amortised cost using the effective interest rate method. The Group classifies non-derivative financial liabilities with fixed or determinable payments as subsequently measured at amortised costs. These financial liabilities 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'. Interest expense is recognised within 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 within the Statement of Income in the line 'Net interest income' as an adjustment to the interest paid from its own bonds.

2.3.5.4.5. 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.

Derivatives embedded in financial assets, loans and debt instruments within the scope of IFRS 9, are not separated from the host contract. Instead, the whole hybrid instrument is measured at amortised cost if it is held within the business model "Hold to collect contractual cash flows" and the contractual cash flows are solely payments of principal and interest on the principal amount outstanding. The entire hybrid instrument is measured at fair value with changes of fair vale recognised in other comprehensive income if it is held within the business model "Hold to collect contractual cash flows and sell" and the contractual cash flows are solely payments of principal and interest on the principal amount outstanding. In all other cases, the hybrid instrument is measured at fair value and with changes of fair value recognised in profit or loss.

The embedded derivative is separated and accounted for as a derivative if, and only if, all of the following conditions are met:

- The host contract is not an asset within the scope of IFRS 9;
- 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.

If the embedded derivative cannot be measured separately, the entire hybrid contract is designated as at fair value through profit or loss.

2.3.5.5. Reclassification of financial assets and liabilities

Reclassification of loans and debt instruments shall occur when, and only when, the objectives of the business models change for an entire category of financial instruments that are jointly managed with the objectives "Hold to collect contractual cash flows", "Hold to collect contractual cash flows and sell" and "Held for trading".

Reclassification is not possible:

- If the Group exercises the option to designate a financial asset at initial recognition as an instrument measured at fair value through profit or loss (“Fair value option”);
- For equity instruments (measured at fair value through profit or loss or through other comprehensive income); or
- For financial liabilities.

If the Group reclassifies loans and debt instruments, the change in classification is applied prospectively from the first day of the next reporting period following the change in business model.

Measurement of reclassified financial assets at the reclassification date and subsequently:

- When reclassifying a financial asset out of the fair value through profit or loss measurement category and into the fair value through other comprehensive income measurement category, the financial asset continues to be measured at fair value and at the reclassification date, new effective interest rate is determined. Subsequent changes in fair value are recognised in other comprehensive income. For the purpose of calculating expected credit losses from the reclassification date, the date of reclassification is treated as the date of initial recognition of the asset;
- When reclassifying a financial asset out of the fair value through profit or loss measurement category and into the amortised cost measurement category, its fair value at the reclassification date becomes its new gross carrying amount and a new effective interest rate is determined. For the purpose of calculating expected credit losses from the reclassification date, the date of reclassification is treated as the date of initial recognition of the asset;
- When reclassifying a financial asset out of the fair value through other comprehensive income measurement category and into the fair value through profit or loss measurement category, the financial asset continues to be measured at fair value. The cumulative gain or loss previously recognised in other comprehensive income is reclassified from equity to profit or loss as a reclassification adjustment at the reclassification date;
- When reclassifying a financial asset out of the fair value through other comprehensive income measurement category and into the amortised cost measurement category, the financial asset is reclassified at its fair value at the reclassification date. The cumulative gain or loss previously recognised in other comprehensive income is removed from equity and adjusted against the fair value of the financial asset at the reclassification date. As a result, the financial asset is measured at the reclassification date as if it had always been measured at amortised cost. The effective interest rate and the measurement of expected credit losses are not adjusted as a result of the reclassification;
- When reclassifying a financial asset out of the amortised cost measurement category and into the fair value through profit or loss measurement category, its fair value is measured at the reclassification date. Any gain or loss arising from a difference between the previous amortised cost of the financial asset and its fair value is recognised in profit or loss;
- When reclassifying a financial asset out of the amortised cost measurement category and into the fair value through other comprehensive income measurement category, its fair value is measured at the reclassification date. Any gain or loss arising from a difference between the previous amortised cost of the financial asset and its fair value is recognised in other comprehensive income. The effective interest rate and the measurement of expected credit losses are not adjusted as a result of the reclassification.

The Group did not reclassify any loans and debt instruments.

2.3.5.6. 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, price 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 or 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 using a so-called credit valuation adjustment (CVA) or for the Group's own default risk using a debit valuation adjustment (DVA), 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 ask 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.

2.3.5.7. Effective interest rate method

The effective interest rate is that 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.

2.3.5.8. 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 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.

2.3.5.9. Impairment of financial assets

The impairment of financial assets is based on the expected credit loss model.

All of the following assets are subject to the Group's impairment requirements:

- Financial assets measured at amortised cost;
- Debt instruments assets measured at fair value through other comprehensive income mentioned in 2.3.5.4.1 Loans and debt securities held in the business model "Hold to collect contractual cash flows and sell";
- Loan commitments if a present commitment to provide credit exists (except for loan commitments measured at fair value through profit or loss);
- Financial guarantee contracts (to which IFRS 9 applies except for those measured at fair value through profit or loss);
- Finance lease receivables in the scope of IAS 17 Leases.

The Group does not assesses impairment on non-client financial assets with an insignificant credit risk, such as, in particular, CNB receivables from obligatory minimum reserves, nostro accounts, contract assets within the scope of IFRS 15 Revenue from contracts with customers (i.e. rights to consideration after the transfer of goods or services), intragroup receivables, and others.

For determination of the impairment, the financial assets are classified into three categories depending on the extent of credit deterioration since initial recognition:

- Stage 1 – financial assets are initially recognised in Stage 1. Subsequently, this stage remains unchanged for financial assets for which the credit risk has not increased significantly since initial recognition or that have low credit risk at the reporting date;
- Stage 2 – financial assets with a significant increase in credit risk since initial recognition but that do not have objective evidence of impairment;
- Stage 3 – financial assets that have objective evidence of impairment at the reporting date.

The transition between risk stages is assessed on an individual basis by evaluating risk characteristics specific for a given asset. For that purpose, the Group uses, in particular, the relative criteria for increased probability of default, supplemented by such absolute criteria, as days past due and the client's rating.

Significant increase in credit risk
The Group assesses at each reporting date whether credit risk has increased significantly. This assessment is based on the increase in probability of default since initial recognition. The Group uses, in particular, relative criteria supplemented by absolute criteria, considering also the delay of contractual payments by more than 30 days past due.

Credit-impaired financial assets
The Group recognises financial assets as credit-impaired when one or more events have occurred that have a detrimental impact on the estimated future cash flows. Evidence of credit-impairment may include observable data about the following events:

- Significant financial difficulty of the issuer or borrower;
- A breach of contract, such as a default or a past-due event;
- Concession granted by the lender, for reasons of the borrower's financial difficulty, that the lender would not otherwise consider;
- Increased probability that the borrower will enter bankruptcy;
- The disappearance of an active market for that financial asset because of financial difficulties; or
- The purchase or origination of a financial asset at a deep discount that reflects the credit losses incurred.

Measurement of expected credit losses
Except for purchased or originated credit-impaired financial assets, the Group recognises expected credit losses (hereafter only "expected losses") to the extent of:

- 12-month expected losses (expected losses that result from default events on a financial instrument that are possible within 12 months after the reporting date – Stage 1); or
- lifetime expected losses (expected losses that result from all possible default events over the expected life of a financial instrument – Stages 2 and 3).

The Group recognises loss allowance in amounts equal to lifetime expected credit losses for credit exposures where there have been significant increases in credit risk since initial recognition.

If in subsequent reporting periods the credit quality of the financial instrument improves such that there is no longer a significant increase in credit risk since initial recognition, then the Group reverts to recognising a loss allowance based on 12-month expected losses. This does not apply to purchased or originated credit-impaired financial assets.

Basis for estimating expected losses
Expected losses are measured in a way that reflects an unbiased and probability-weighted amount that is determined by evaluating a range of possible outcomes and takes into account the time value of money. The Group considers reasonable and supportable information about past events, current conditions, and forecasts of future economic conditions. When measuring the expected losses and taking into account the time value of money, the expected cash flows are discounted to the reporting date using the original effective interest rate determined at initial recognition (or an approximation thereof).

The Group assesses expected losses for default events of significant exposures based on expected cash flows from the client's economic activity or realisation of collateral.

For estimating expected losses for purchased or originated credit-impaired financial assets, the Group applies the credit-adjusted effective interest rate. Unlike the effective interest rate (calculated using the estimated future cash flows while not taking into account expected losses), the credit-adjusted effective interest rate incorporates the impact of expected losses of the financial asset.

Purchased or originated credit-impaired financial assets
Purchased or originated credit-impaired financial assets are accounted differently as the assets are already impaired at initial recognition. For these assets, lifetime expected losses are incorporated into the expected cash flows used to calculate the credit-adjusted effective interest rate at initial recognition. Subsequently, any changes in expected losses are recognised as loss allowance and as gain or loss in the Statement of Income.

2.3.5.10. 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 debt instruments held in the business models "Hold to collect contractual cash flows and sell" or "Held for sale" that are measured and recognised as 'Financial assets at fair value through other comprehensive income' or 'Financial assets at fair value through profit or loss'. 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 ‘Loans and advances to banks’ or ‘Loans and advances to customers’.

The Group is allowed to provide securities received in reverse repo transactions as collateral or to 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’.

2.3.6. Assets held for sale

The line ‘Assets held for sale’ represents assets the carrying amounts for which the Group expects 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 ‘Net profits on other 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).

2.3.7. Income tax

2.3.7.1. 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.

2.3.7.2. 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, and financial assets measured at fair value through other comprehensive income.

2.3.8. Leasing

Leases are classified as finance leases whenever the terms of the lease transfer substantially all the risks and benefits 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 this income 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 it 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 ‘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 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.

2.3.9. 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 or amortised 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 and impairment of operating 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:

	30 Jun 2018	1 Jan 2018
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
- Other components	15	15
- 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 components 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, 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 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 and impairment of operating assets'.

Repairs and maintenance are charged directly to the Statement of Income when they occur.

2.3.10. 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 a 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 3-year 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. Occasionally, however, 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 it reviews the procedures used for their measurement and the measurement of non-controlling interest in the acquiree and the consideration transferred.

2.3.11. Provisions

The Group recognises provisions for contracted commitments (principally comprising the provisions for ongoing contracted potential commitments, legal disputes, self-insurance, and the retirement benefits plan) and for restructuring.

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 as 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.

A provision for restructuring is recognised when the Group has approved a detailed formal plan for restructuring and the restructuring has either commenced or the main features of the restructuring plan have been announced to those affected before the end of the reporting period. A restructuring provision shall include only the direct expenditures arising from the restructuring which are necessarily entailed by the restructuring and not associated with the ongoing activities of the entity.

The Group also recognises provisions for credit-related commitments into which the Group enters in the normal course of business. These credit-related commitments do not meet the criteria for recognition in the Statement of Financial Position and 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. The provisions represent impairment based on expected losses from any potential financial liabilities arising from these credit-related commitments. Provisions for credit-related commitments are created on the same basis as are loss allowances for financial assets.

2.3.12. Employee benefits

2.3.12.1. 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:

2.3.12.2. 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 that is paid in the following year, and (ii) a deferred component that 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'.

2.3.12.3. Free share plan

To enhance loyalty and motivation to contribute to 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 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 granting date, is spread over the vesting period and recorded in the lines 'Personnel expenses' and 'Share-based transactions' 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.

2.3.13. 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 treasury shares' under equity. Gains and losses on sales of treasury shares are recognised in equity and presented as well in the line 'Share premium and treasury shares'.

2.3.14. Contingent assets, contingent liabilities and off-balance sheet items

In addition to transactions giving rise to 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 constitute 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 or liability is defined as a possible asset or 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 2.3.5.4.3 Derivatives and hedge accounting.

2.3.15. 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.

2.3.16. 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.

2.4. Changes in accounting policies

As of 1 January 2018, the Group has implemented the new standard IFRS 9 Financial Instruments superseding the current standard IAS 39. The new approach to classification and measurement of financial assets and the new impairment methodology are reflected in Note 2.

As of 1 January 2018 the Group has made the following changes in reporting principles:

- Early repayment fees – newly recognised in the line 'Net interest income', previously in the line *'Net fee and commission income'*;
- Dividend income – newly recognised in a separate line part of 'Net operating income' previously part of 'Net interest and similar income';
- Provisions for other risk expenses – newly recognised in the line 'General administrative expenses'(GAE), previously in the line 'Allowances and provisions for loans, securities and other risk expenses' (CoR);
- Fees from insurance as a supplementary service where the Bank is acting as an agent – newly the net approach to reporting in the line 'Net fee and commission income' following the requirements of the new standard IFRS 15 Revenue from contracts with customers that the Group has implemented as of 1 January 2018. Previously, fee income and expenses had been reported on a gross basis.

	Reported	Restated
(CZKm)	30 Jun 2017	30 Jun 2017
Net interest income and similar income	10,313	10,410
Net fee and commission income	3,225	3,125
Net operating income	15,630	15,630
General and administrative expenses	(2,944)	(2,935)
Cost of risk	103	94

In 2018, the Group modified the method of compiling the Cash Flow Statement, it is now compiled by the indirect method. The reason for the change was to unify the approach with that of the parent company and with general practice in the market. The Group also changed the classification of cash flows from equity instruments and debt securities. These items were previously reported in cash flows from financial activities and now they are reported in cash flows from operating activities. The new classification is more in line with the nature of those assets and is consistent with the inclusion of these items in the parent's Cash Flow Statement.

The comparable period was set up in a new structure without any impact on total cash flows.

The following tables show the impact from the application of IFRS9:

Reconciliation of carrying amounts - Financial assets and liabilities

(CZKm)	IAS 39 as of 31 December 2017		Reclassification	Remeasurement		IFRS 9 as of 1 January 2018	
Financial assets	**Measurement category**	**Balance**		**ECL**	**Other**	**Measurement category**	**Balance**
Financial assets at amortised cost							
Loans and advances to banks		228,374		4			222,821
To: Financial assets at FVTPL - non SPPI			(2,708)				
To: Financial assets at FVOCI			(2,039)				
To: Debt securities at amortised costs			(810)				
Loans and advances to customers		598,102		(828)			593,639
To: Debt securities at amortised costs			(3,635)				
Debt securities at amortised costs				(11)			70,340
From: Loans and advances to banks			810				
From: Loans and advances to customers			3,635				
From: Available-for-sale financial assets			20,010		(149)		
From: Held-to-maturity financial assets			46,045				
Total	**L&R**	**826,476**	**61,308**	**(835)**	**(149)**	**AC**	**886,800**
Available-for-sale financial assets		29,712					0
To: Financial assets at FVOCI			(9,262)				
To: Debt securities at amortised costs			(20,010)		(440)		
Total	**AFS**	**29,712**	**(29,272)**		**(440)**	**N/A**	**0**
Held-to-maturity financial assets		59,915					0
To: Financial assets at FVOCI			(12,194)		(339)		
To: Debt securities at amortised costs			(46,045)		(1,337)		
Total	**HTM**	**59,915**	**(58,239)**		**(1,676)**	**N/A**	**0**
Financial assets at fair value through other comprehensive income							
From: Available-for-sale financial assets			9,262				
From: Held-to-maturity financial assets			12,194		547		
From: Loans and advances to banks			2,039		(3)		
Total	**N/A**	**0**	**23,495**		**544**	**FVOCI**	**24,039**
Financial assets at fair value through profit or loss - non SPPI							
From: Loans and advances to banks			2,708		(14)		
Total	**N/A**	**0**	**2,708**		**(14)**	**FVTPL**	**2,694**

(CZKm)	IAS 39 as of 31 December 2017		Reclassification	Remeasurement		IFRS 9 as of 1 January 2018	
Financial liabilities	**Measurement category**	**Balance**		**ECL**	**Other**	**Measurement category**	**Balance**
Provisions		1,911		47			1,958
Total	**AC**	**1,911**		**47**		**AC**	**1,958**

Reconciliation of impairment allowance

(CZKm)	as of 31 December 2017			as of 1 January 2018
Impairment allowance	Loan loss allowance under IAS 39/Provision under IAS 37	Reclassification	Remeasurement	Loan loss allowance under IFRS 9
Impairment of financial assets				
Loans and receivables (IAS 39), Held-to-maturity financial assets (IAS 39) / Financial assets at amortised costs (IFRS 9)				
Loans and advances to banks at amortised costs	(10)		4	(6)
Loans and advances to customers at amortised costs	(12,747)		(828)	(13,575)
Debt securities at amortised costs	0		(11)	(11)
Total	**(12,757)**		**(835)**	**(13,592)**
Provisions for guarantees and other credit-related commitments				
Provisions for guarantees and other credit-related commitments	1,394		47	1,441

Reconciliation of reserves and retained earnings

(CZKm)	Reserves and retained earnings
OCI / Revaluation reserve	
Closing balance under IAS 39 (31 December 2017)	2,326
Reclassification of debt securities from AFS to AC	(589)
Reversal of revaluation relates to HTM created from AFS under IAS39	(1,676)
Reclassification of debt securities from HTM to FVOCI	544
Recognition of ECL under IFRS 9, for debt financial assets at FVOCI	(4)
Deferred tax	298
Opening balance under IFRS 9 (1 January 2018)	899
Retained earnings	
Closing balance under IAS 39 (31 December 2017)	75,352
Re measurement impact of reclassifying from AC to FVTPL	(14)
Recognition of ECL under IFRS 9 including those measured at FVOCI	(882)
Deferred tax	138
Non-controlling interest	85
Opening balance under IFRS 9 (1 January 2018)	74,680
Non-controlling interest	(85)
Total change in equity due to adopting IFRS 9	**(2,184)**

Reclassifications of financial assets to amortised costs

(CZKm)	2018
From available-for-sale financial assets (IAS 39 classification)	
Fair value as of 30 June 2018	19,681
Fair value gain/(loss) that would have been recognised in OCI during the year if the financial asset had not been reclassified	(632)

3. Segment reporting

	Retail banking		Corporate banking		Investment banking		Other		Total	
(CZKm)	2018	2017	2018	2017	2018	2017	2018	2017	2018	2017
Net interest income and similar income	6,657	6,269	3,000	3,176	202	82	934	883	10,793	10,410
Net fee and commission income	2,132	2,177	929	1,024	(43)	(97)	59	21	3,077	3,125
Net profit on financial operations	512	479	721	930	103	527	71	56	1,407	1,992
Dividend income	0	0	0	0	0	0	3	3	3	3
Other income	73	41	(15)	14	150	83	(91)	(38)	117	100
Net operating income	**9,374**	8,966	**4,635**	5,144	**412**	595	**976**	925	**15,397**	15,630

Given the specifics of banking activities, the Board of Directors of the Bank (the chief operating decision maker) is provided with the 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 the liquidity component reflecting the existing opportunities to acquire and invest financial resources.

The Group's income is primarily (more than 99%) generated on the territory of the Czech Republic.

4. Financial assets at fair value through profit or loss – non-SPPI

As of 30 June 2018, 'Financial assets at fair value through profit or loss' include debt securities at fair value of CZK 2,652 million (1 January 2018: CZK 2,694 million) that are issued by foreign financial institutions.

5. Financial assets at fair value through other comprehensive income

Financial assets at fair value comprise the following:

(CZKm)	30 Jun 2018	1 Jan 2018
Shares and other participation	302	241
Debt securities	25,030	23,798
Financial assets at fair value through other comprehensive income	**25,332**	24,039

Shares and other participation at fair value through other comprehensive income, allocated by sector, comprise the following:

(CZKm)	30 Jun 2018	1 Jan 2018
Other financial institutions	301	240
Non-financial institutions	1	1
Total	**302**	241

Debt securities at fair value through other comprehensive income, allocated by sector, comprise the following:

(CZKm)	30 Jun 2018	1 Jan 2018
Government institutions	22,963	19,208
Credit institutions	2,067	4,590
Total	**25,030**	23,798

6. Financial assets at amortised cost

(CZKm)	30 Jun 2018	1 Jan 2018
Loans and advances to banks	304,488	222,821
Loans and advances to customers	622,803	593,639
Debt securities	74,433	70,340
Financial assets at amortised cost	**1,001,724**	886,800

As of 30 June 2018, the loan portfolio of the Group is comprised of the following, as broken down by classification:

(CZKm)	Gross carrying value Stage 1	Gross carrying value Stage 2	Gross carrying value Stage 3	Gross carrying value total	Allowances Stage 1	Allowances Stage 2	Allowances Stage 3	Total allowances	Carrying value
Central banks	254,037	0	0	**254,037**	0	0	0	**0**	**254,037**
Government institutions	24,288	20	476	**24,784**	(8)	(1)	(47)	**(56)**	**24,728**
Credit institutions	49,233	1,124	95	**50,452**	(1)	(1)	0	**(2)**	**50,450**
Other financial institutions	39,574	2	57	**39,633**	(55)	0	(9)	**(64)**	**39,569**
Non-financial institutions	232,407	12,052	9,056	**253,515**	(700)	(546)	(5,829)	**(7,075)**	**246,440**
Households	299,561	10,531	7,740	**317,832**	(279)	(592)	(4,894)	**(5,765)**	**312,067**
Total loans	**899,100**	**23,729**	**17,424**	**940,253**	**(1,043)**	**(1,140)**	**(10,779)**	**(12,962)**	**927,291**
Central banks	0	0	0	**0**	0	0	0	**0**	**0**
Government institutions	69,724	0	0	**69,724**	(12)	0	0	**(12)**	**69,712**
Credit institutions	1,813	0	0	**1,813**	0	0	0	**0**	**1,813**
Other financial institutions	96	0	0	**96**	0	0	0	**0**	**96**
Non-financial institutions	2,812	0	0	**2,812**	0	0	0	**0**	**2,812**
Total debt securities	**74,445**	**0**	**0**	**74,445**	**(12)**	**0**	**0**	**(12)**	**74,433**

As of 1 January 2018, the loan portfolio of the Group was comprised of the following, as broken down by classification:

(CZKm)	Gross carrying value Stage 1	Gross carrying value Stage 2	Gross carrying value Stage 3	Gross carrying value total	Allowances Stage 1	Allowances Stage 2	Allowances Stage 3	Total allowances	Carrying value
Central banks	184,521	0	0	**184,521**	0	0	0	**0**	**184,521**
Government institutions	26,107	19	508	**26,634**	(7)	(1)	(54)	**(62)**	**26,572**
Credit institutions	36,891	1,415	0	**38,306**	(3)	(3)	0	**(6)**	**38,300**
Other financial institutions	27,970	8	64	**28,042**	(62)	0	(10)	**(72)**	**27,970**
Non-financial institutions	221,623	10,966	9,854	**242,443**	(687)	(403)	(6,223)	**(7,313)**	**235,130**
Households	284,058	17,852	8,185	**310,095**	(236)	(692)	(5,200)	**(6,128)**	**303,967**
Total loans	**781,170**	**30,260**	**18,611**	**830,041**	**(995)**	**(1,099)**	**(11,487)**	**(13,581)**	**816,460**
Central banks	0	0	0	**0**	0	0	0	**0**	**0**
Government institutions	65,651	0	0	**65,651**	(11)	0	0	**(11)**	**65,640**
Credit institutions	1,839	0	0	**1,839**	0	0	0	**0**	**1,839**
Other financial institutions	70	0	0	**70**	0	0	0	**0**	**70**
Non-financial institutions	2,791	0	0	**2,791**	0	0	0	**0**	**2,791**
Total debt securities	**70,351**	**0**	**0**	**70,351**	**(11)**	**0**	**0**	**(11)**	**70,340**

Set out below is a breakdown of loans and advances to non-financial institutions by sector:

(CZKm)	30 Jun 2018	1 Jan 2018
Agriculture, forestry and fishing	11,235	11,090
Mining and quarrying	2,938	3,914
Manufacturing	64,903	61,486
Electricity, gas, steam and air conditioning supply	15,853	14,099
Water supply, sewerage, waste management and remediation activities	2,178	2,610
Construction	10,826	9,337
Wholesale and retail trade, repair of motor vehicles and motorcycles	42,579	41,236
Transportation and storage	18,723	17,595
Accommodation and food service activities	1,340	1,126
Information and communication	5,982	5,971
Real estate activities	46,253	41,907
Professional, scientific and technical activities	7,244	8,191
Administrative and support service activities	5,584	6,961
Public administration and defence, compulsory social security	541	382
Education	218	238
Human health and social work activities	1,989	1,934
Arts, entertainment and recreation	2,656	2,720
Other service activities	12,473	10,508
Total loans and advances to non-financial institutions	**253,515**	**241,305**

Debt securities, allocated by sector, comprise the following:

(CZKm)	30 Jun 2018	1 Jan 2018
Central banks	0	0
Government institutions	69,712	65,640
Credit institutions	1,813	1,839
Other financial institutions	96	70
Non-financial institutions	2,812	2,791
Total	**74,433**	**70,340**

7. Bonds issued by foreign government institutions and assimilated

As of 30 June 2018, bonds issued by foreign government institutions and assimilated designated as ‘Financial assets at fair value through other comprehensive income’ and as ‘Financial assets at amortised cost’ comprise the following:

	Carrying value at 30 Jun 2018			Carrying value at 1 Jan 2018		
(CZKm)	Debt securities at fair value	Debt securities at amortised cost	Total	Debt securities at fair value	Debt securities at amortised cost	Total
European Investment Bank	0	1,713	**1,713**	0	1,736	**1,736**
Poland	7,542	0	**7,542**	8,169	0	**8,169**
Slovakia	6,502	0	**6,502**	6,468	0	**6,468**
Romania	1,774	0	**1,774**	1,744	0	**1,744**
Azerbaijan	0	15	**15**	0	14	**14**
Total	**15,818**	**1,728**	**17,546**	**16,381**	**1,750**	**18,131**

8. Financial liabilities at amortised cost

(CZKm)	30 Jun 2018	1 Jan 2018
Amounts due to banks	120,335	84,050
Amounts due to customers	831,975	762,043
Securities issued	7,337	4,832
Financial liabilities at amortised cost	**959,647**	850,925

Securities issued comprise the following:

(CZKm)	30 Jun 2018	1 Jan 2018
Mortgage bonds	1,018	2,762
Depository bills of exchange	6,319	2,070
Total securities issued	**7,337**	4,832

The Group issues mortgage bonds to fund its mortgage activities.

Mortgage bonds according to their remaining time to maturity break out as follow:

(CZKm)	30 Jun 2018	1 Jan 2018
In less than one year	0	1,753
In one to five years	1,018	1,009
In five to ten years	0	0
In ten to twenty years	0	0
in twenty to thirty years	0	0
Total mortgage bonds	**1,018**	**2,762**

During the first half of 2018, the Group properly paid up mortgage bonds with aggregate nominal volume of CZK 1,747 million.

The securities issued detailed above include the following mortgage bonds issued by the Group:

Name	Interest rate	Currency	Issue date	Maturity date	30 Jun 2018 (CZKm)	1 Jan 2018 (CZKm)
HZL Komerční banky, a.s. CZ0002002801	2.55%	CZK	21 Dec 2012	21 Dec 2022	1,018	1,009
HZL Komerční banky, a.s. CZ0002003064	6M PRIBOR plus 50 bps	CZK	14 Mar 2013	14 Mar 2018	0	1,753
Total mortgage bonds					**1,018**	**2,762**

Note: Six-month PRIBOR was 124 bps as of 30 June 2018 (1 Jan 2018: 85 bps).

9. Provisions

Provisions comprise the following:

		Restated
(CZKm)	30 Jun 2018	1 Jan 2018
Provisions for contracted commitments	508	517
Provisions for other credit commitments	1,287	1,394
Adoption of IFRS 9	0	47
Provisions for restructuring cost	294	0
Total provisions	**2,089**	**1,958**

The provisions for other credit commitments are held to cover credit risks associated with credit commitments issued. The provisions for contracted commitments principally comprise provisions for ongoing contracted contingent commitments, legal disputes, self-insurance and the provisions for loyalty and jubilee bonuses and the retirement benefits plan.

In 2018, the Group created provisions for restructuring costs related to the “KB Change” transformation project in the detailed amount of CZK 294 million (2017: CZK 0 million) in accordance with estimated redundancy payments, consultancy costs, and other costs necessary in order to implement the detailed restructuring plan. Provisions are reported in the Income Statement lines ‘Personnel expenses’ in the amount of CZK 223 million (2017: CZK 0 million) and ‘General administrative expenses’ in the amount of CZK 71 million (2017: CZK 0 million).

Set out below is a breakdown of the provisions for other credit commitments by risk level:

(CZKm)	30 Jun 2018	1 Jan 2018
Stage 1	152	153
Stage 2	78	81
Stage 3	1,057	1,207
Total	**1,287**	**1,441**

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 at 1 January 2018	368	0	149	517
Charge	13	0	28	41
Release	(7)	0	(40)	(47)
Use	0	0	(7)	(7)
Accrual	3	0	0	3
Remeasurement	0	0	0	0
Foreign exchange difference	0	0	1	1
Balance at 30 June 2018	**377**	**0**	**131**	**508**

(CZKm)	Retirement benefits plan	Provisions for loyalty and jubilee bonuses	Other provisions for contracted commitments	Total
Balance at 1 January 2017	323	2	148	473
Charge	12	0	18	30
Release	0	0	(8)	(8)
Use	(6)	0	(26)	(32)
Accrual	2	0	0	2
Remeasurement	0	0	0	0
Foreign exchange difference	0	0	(4)	(4)
Balance at 30 June 2017	**331**	**2**	**128**	**461**

10. Commitments and contingent liabilities

Legal disputes

The Group conducted a review of legal proceedings outstanding against it as of 30 June 2018. 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 18 million for these legal disputes. The Group has also recorded a provision of CZK 4 million for costs associated with a potential payment of interest on the pursued claims.

As of 30 June 2018, the Group conducted a review of legal proceedings 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.

Financial commitments and contingencies comprise the following:

(CZKm)	30 Jun 2018	1 Jan 2018
Non-payment guarantees incl. commitments to issue non-payment guarantees	33,518	34,461
Payment guarantees including commitments to issue payment guarantees	17,510	15,974
Committed facilities and unutilised overdrafts	12,731	11,494
Undrawn credit commitments	79,105	69,484
Unutilised overdrafts and approved overdraft loans	12,891	13,673
Unutilised limits under framework agreements to provide financial services	7,809	7,787
Open customer/import letters of credit uncovered	391	898
Stand-by letters of credit uncovered	2,565	1,024
Confirmed supplier/export letters of credit	1,025	794
Total contingent revocable and irrevocable commitments	**167,545**	**155,589**

Set out below is a breakdown of financial commitments and contingencies by sector:

(CZKm)	30 Jun 2018	1 Jan 2018
Agriculture, forestry and fishing	3,246	2,915
Mining and quarrying	662	279
Manufacturing	27,579	27,579
Electricity, gas, steam and air conditioning supply	3,326	4,996
Water supply, sewerage, waste management and remediation activities	1,041	801
Construction	28,988	30,004
Wholesale and retail trade, repair of motor vehicles and motorcycles	11,655	11,323
Transportation and storage	6,161	5,016
Accommodation and food service activities	500	466
Information and communication	2,711	2,732
Financial and insurance activities	8,109	2,755
Real estate activities	6,352	5,084
Professional, scientific and technical activities	9,126	9,253
Administrative and support service activities	1,965	1,316
Public administration and defence, compulsory social security	11,159	8,247
Education	349	247
Human health and social work activities	1,459	1,260
Arts, entertainment and recreation	1,279	1,934
Other service activities	2,427	2,477
Individuals	39,451	36,905
Contingent liabilities	**167,545**	**155,589**

The majority of commitments and contingencies originate on the territory of the Czech Republic.

11. Estimated fair value of assets and liabilities of the Group

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 value:

	30 Jun 2018		1 Jan 2018	
(CZKm)	Carrying value	Fair value	Carrying value	Fair value
Financial assets				
Cash and current balances with central banks	21,318	21,318	32,663	32,663
Financial assets at amortised cost	1,001,724	1,007,060	886,800	896,233
- loans and advances to banks	304,488	304,464	222,821	223,117
- loans and advances to customers	622,803	627,132	593,639	600,051
- debt securities	74,433	75,464	70,340	73,065
Financial liabilities				
Amounts due to central banks	1	1	1	1
Financial liabilities at amortised cost	959,647	959,032	850,925	850,007
- amounts due to banks	120,335	120,283	84,050	84,028
- amounts due to customers	831,974	831,970	762,043	761,497
- securities issued	7,337	6,779	4,832	4,482
Subordinated debt	2,608	2,608	2,560	2,560

The hierarchy of fair values of those financial assets and liabilities not presented on the Group's Statement of Financial Position at their fair value:

	30 Jun 2018				1 Jan 2018			
(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	21,318	7,993	0	13,325	32,663	10,070	0	22,593
Financial assets at amortised cost	1,007,060	75,464	0	931,596	896,233	73,065	0	823,168
- amounts due from banks	304,464	0	0	304,464	223,117	0	0	223,117
- loans and advances to customers	627,132	0	0	627,132	600,051	0	0	600,051
- debt securities	75,464	71,718	3,230	516	73,065	69,344	3,190	531
Financial liabilities								
Amounts due to central banks	1	0	0	1	1	0	0	1
Financial liabilities at amortised cost	959,032	0	0	959,032	850,007	0	0	850,007
- amounts due to banks	120,283	0	0	120,283	84,028	0	0	84,028
- amounts due to customers	831,970	0	0	831,970	761,497	0	0	761,497
- securities issued	6,779	0	0	6,779	4,482	0	0	4,482
Subordinated debt	2,608	0	0	2,608	2,560	0	0	2,560

12. Transfers between levels of the fair value hierarchy

During the first half of 2018, there were no transfers between levels.

13. Events after the reporting period

No significant event occurred after the reporting period.

Ratings

Ratings of Komerční banka as of 30 June 2018*

	Short-term	Long-term
Standard & Poor's	A-1	A
Moody's	Prime-1	A2
Fitch	F1	A-

Note: *KB was assigned a credit rating by rating agencies registered under Regulation of the European Parliament and Council (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%

Shareholder structure

The share capital of Komerční banka totals CZK 19,004,926,000 and is divided into 190,049,260 ordinary 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.

As of 30 June 2018, the number of shareholders consisted of 48,205 legal entities and private individuals, of which 42,879 were private individuals from the Czech Republic. KB held in treasury 1,193,360 of its own shares, constituting 0.6% of the registered capital. Strategic shareholder Société Générale maintained a 60.4% stake, and minority shareholders held 39.0% of KB's equity.

Major shareholders of Komerční banka owning more than 1% of the share capital as of 30 June 2018 per the extract from the issuers register taken from the Central Securities Depository.

Shareholder	Proportion of share capital
Société Générale S.A.	60.35%
Chase Nominees Limited	4.30%
Nortrust Nominees Limited	3.76%
Clearstream Banking S.A.	2.41%
Brown Brothers Harriman	2.07%
State Street Bank and Trust Company	2.01%
GIC Private Limited	1.75%
J.P. Morgan Bank	1.01%
Other shareholders	22.34%

Management affidavit

To the best of our knowledge, we believe that this half-yearly report gives a fair and true view of the Bank's and Group's financial position, business activities and results from the first half of 2018, as well as of the outlook for the development of the Bank's and Group's financial situation, business activities and results.

Prague, 28 August 2018

Signed on behalf of the Board of Directors:

Jan Juchelka

Chairman of the Board of Directors
and Chief Executive Officer

Vladimír Jeřábek

Member of the Board of Directors
and Senior Executive Director