annual review

2014

ČESKOMORAVSKÁ ZÁRUČNÍ A ROZVOJOVÁ BANKA, a.s.

In the Czech Republic, we represent a promotional bank aimed at contributing to the efficient development of national infrastructure and economic sectors that have been approved for public support according to the economic policies of the Czech Republic government and its regions.

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Chairman's introduction

Dear clients, business partners and shareholder representatives,

In 2014, Českomoravská záruční a rozvojová banka, a. s. (CMZRB) took further steps necessary for enabling the Bank to expand its operations in administering financial instruments, in particular loans and guarantees. The process of the Bank's transformation advanced in the past year to the next phase, through which some of its own treasury shares purchased from private shareholders were transferred to the Czech Republic by means of paying a non-cash dividend. At the same time, conditions were created for transferring the Bank's remaining own treasury shares to the Czech Republic during 2015. That will enable finalising the process initiated in 2012 of transforming CMZRB's shareholder structure and carrying out tasks ensuing for the Bank under the government's programme declaration.

Support for small enterprises through providing preferential guarantees continued successfully. Financing of these guarantees was carried out to a considerable degree from the Bank's own resources. This active approach, which was supported by the Bank's shareholder (the Czech Republic), enabled to diminish a shortfall in the guarantee offer affected especially by an overall time shift in launching support programmes financed from structural funds for the 2014–2020 programming period.

The past year was characterised by modest economic recovery together with growing activity in the small and medium-sized enterprise sector. This development together with inclusion of the Bank's own resources was reflected in a 23% increase in the amount of guarantees provided and a 26% gain in their number compared to values achieved in the previous year.

CMZRB also expanded its co-operation with Czech Export Bank the objective of which is to facilitate export financing for small and medium-sized enterprises. Existing co-operation in support of pro-export payment guarantees was broadened to include support focused on pre-export and direct export loans.

The Bank continued its cautious financial management and reliably maintained key indicators at levels confirming the Bank's stability and trustworthiness. Despite reduced income resulting from continuing changes in the price structure of current banking products and persistent low interest rates, the profit level enabled the Bank to ensure payment of cash and non-cash dividends in the planned amounts.

CMZRB also actively co-operated last year with international organisations and partner institutions, both within the European Union and outside of Europe. During the year, the Bank organised a meeting of the Permanent Working Group of the Network of European Financial Institutions for Small and Medium Sized Enterprises (NEFI). It also hosted the General Assembly of the European Association of Long-Terms Investors (ELTI) which, among other matters, emphasised the need to strengthen efforts in joint engagement of private and public resources for financing investments into infrastructure, energy savings, and innovations in Europe. The European Commission's intention to create a European Fund for Strategic Investments and support new projects in infrastructure, energy, innovation and development of small and medium-sized enterprises provides new space for public and private financial institutions across Europe to deepen their collaboration.

Crucial tasks directly related to fulfilling business objectives for the coming years which the Bank systematically pursued during 2014 include preparations for a new national guarantee programme for 2015–2023 as well as co-operation in preparing setting and implementation of the new Operational Programme Enterprise and Innovation for Competitiveness. Financial instruments should play an important role in this operational programme as well as certain others. To administer them successfully under the new legislative conditions created by increased administrative requirements and more complicated procedures will be the main challenge for all of the Bank's employees in 2015 and for the years to come. Possible expansion of CMZRB's operations in administering financial instruments supported by structural funds emphasises the importance and challenges in pursuing the Bank's long-term development.

I would therefore like to offer my sincere thanks to all of the Bank's employees and shareholder representatives for their work efforts and active contributions which have enabled us to evaluate 2014 as an overall success. I believe that 2015 will bring new opportunities and challenges, the mastery of which, as in previous years, will require that the Bank's management and its employees obtain the necessary support from the shareholder for the broadest possible extent of the Bank's operations in using financial instruments within the Czech Republic, and in particular those financed from structural funds. We will endeavour to achieve effective and accommodating support for the domestic entrepreneurial sector as well as for clients in all other areas of the Bank's operations.

Ladislav Macka
Chairman of the Board of Directors

Company profile

The Government of the Czech Republic adopted a resolution on 23 October 1991 for the founding of a specialised banking institution to support small and medium-sized enterprises. This institution was entered into the Commercial Register in January 1992 under the name Českomoravská záruční a rozvojová banka, a. s., (hereinafter referred to as “CMZRB” or the “Bank”).

The Bank’s initial scope of business was focused solely on implementing government programmes for the support of small and medium-sized enterprises. In subsequent years, that activity was extended to include providing support in the area of housing and financing infrastructure development projects. CMZRB has a full banking licence, a foreign exchange licence, and a securities broker’s licence issued under the relevant laws.

At present, CMZRB’s main mission is to facilitate primarily small and medium-sized enterprises’ access to financing through specialised banking products and, in accordance with the economic policy aims of the Government and regions of the Czech Republic, to assist in developing other selected areas of the economy that require public support.

Throughout its entire time in operation, the Bank has co-operated closely with ministries, state funds, regions, banks, economic chambers and other representatives of business. The specific character of CMZRB’s activities, the development of modern banking and communication technologies, and its traditionally good co-operation with partners enable the Bank to provide its clients with high-quality banking services all across the Czech Republic while having positive effects on those clients’ development. Clients may use the services of the Bank’s branches in Prague and in the regional centres of Brno, Hradec Králové, Ostrava and Pilsen. The Bank operates a regional office in České Budějovice for even better contact with its clients.

BANK’S OFFICES

Branch
Regional office

CMZRB offers its clients bank guarantees, preferential loans, financial subsidies and related banking services. It manages an extensive portfolio of guarantees and grants provided for apartment block repair. Financing projects to improve the technical condition of infrastructure and the development of municipalities also constitute part of the Bank’s activities. CMZRB also uses resources from international financial institutions for these purposes.

The two most important client groups are small and medium-sized enterprises and the owners of apartment blocks, in particular housing co-operatives and apartment-owners associations. Other users of the Bank’s services include municipalities, regional authorities, ministries and state funds.

Selected economic indicators

	Unit	2010	2011	2012	2013	2014
Total assets	CZK mil.	58,147	58,700	111,706	98,042	127,337
Liabilities	CZK mil.	52,455	52,965	106,748	93,591	122,642
Shareholders' equity	CZK mil.	5,692	5,735	4,958	4,451	4,695
Share capital	CZK mil.	2,132	2,132	2,132	2,132	2,132
Profit after tax	CZK mil.	854	849	812	348	262
Guarantee portfolio	CZK mil.	23,649	21,398	19,039	18,129	17,900
Capital ratio	%	16.4	17.2	14.4	16.0	17.1
Average number of employees		219	217	217	216	211
Number of branches		5	5	5	5	5

The Bank's shareholder controlling 85.81% of the shares and all voting rights is the Czech Republic, represented by the Ministry of Industry and Trade, Ministry of Regional Development, and Ministry of Finance. CMZRB holds in treasury the remaining 14.19% of its own shares. No voting rights are attached to these shares.

CMZRB conducts no research and development activities.

The Bank's activities have no negative environmental impact.

It systematically develops its employees' knowledge and skills, applies proven rules for motivating and rewarding employees, and carries out a social program.

CMZRB has no foreign branches or subsidiaries.

Governing bodies

Board of Directors

Chairman	Ladislav Macka
Vice-Chairman	Pavel Weiss
Members	Jiří Jirásek
	Lubomír Rajdl
	Jan Ulip

Supervisory Board

Chairman	Robert Szurman
Vice-Chairman	Jan Gregor, as from 24 June 2014
Members	Ladislav Koděra
	Marie Kotrlá
	Zdeněk Mareš
	Tomáš Novotný, as from 24 June 2014
	Martin Pros, as from 24 June 2014
	Jana Šindelářová

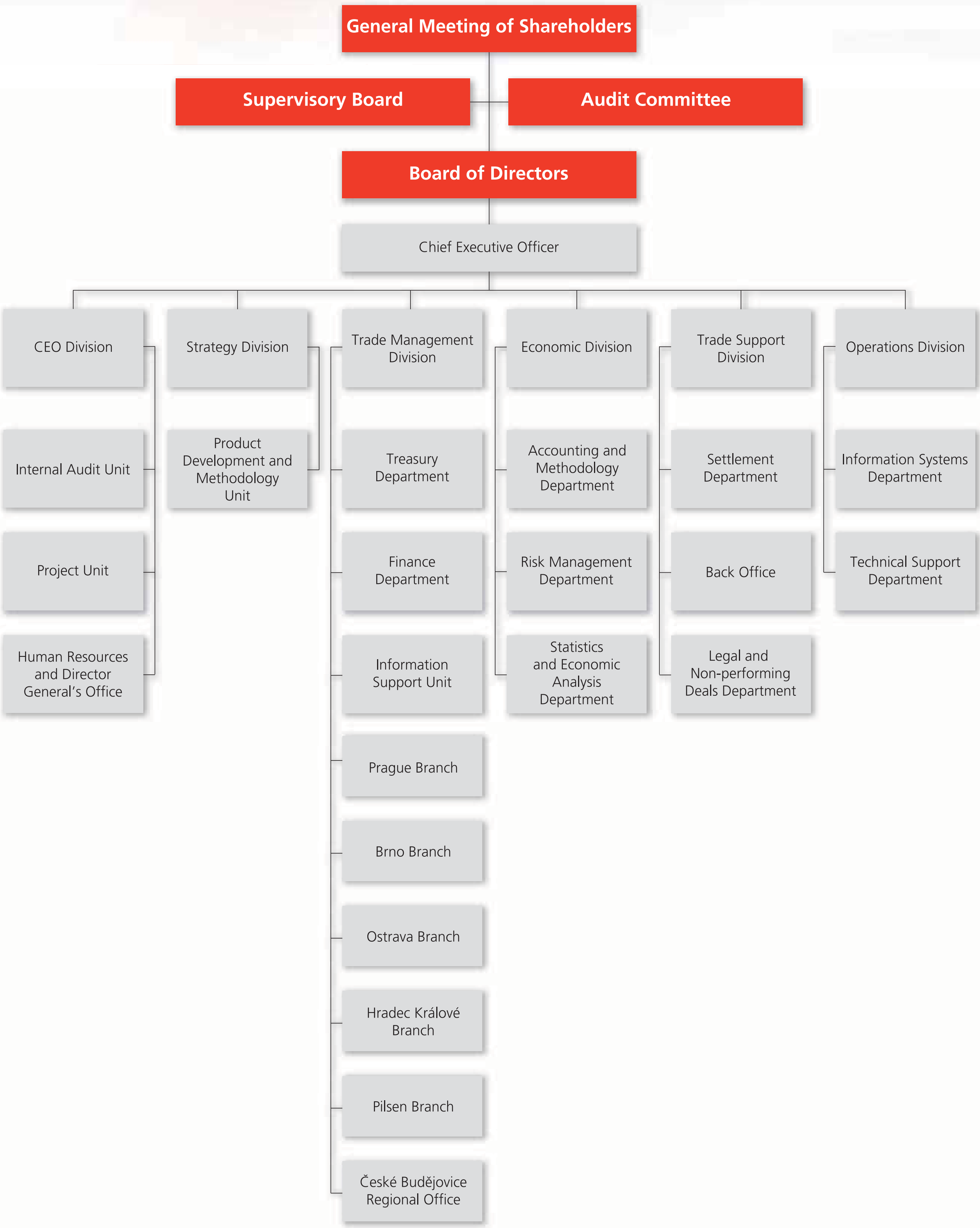
During 2014, Vladimír Bártl (as of 22 April 2014), Josef Doruška (as of 27 April 2014), Josef Hájek (as of 27 April 2014), and Daniel Braun (as of 9 December 2014) ended their membership in the Supervisory Board.

Audit Committee

Chairman	Milan Novák
Vice-Chairman	Josef Doruška, as from 28 April 2014
Members	Robert Szurman

During 2014, Růžena Kabilková (as of 27 April 2014) and Josef Hájek (as of 27 April 2014) ended their membership in the Audit Committee.

Organisation chart



Information for readers

The data disclosed up to page 31 of this Annual Review have been derived from the financial statements of Českomoravská záruční a rozvojová banka, a. s., as at 31 December 2014 and for the year then ended prepared in accordance with Czech accounting legislation (“Statutory financial statements“). The full version of the Statutory financial statements is included in the Annual Report of Českomoravská záruční a rozvojová banka, a. s., which is published on www.cmzrb.cz in the original Czech language.

The financial statements of Českomoravská záruční a rozvojová banka, a. s., in this Annual Review are prepared in accordance with International Financial Reporting Standards as adopted by the European Union.

Českomoravská záruční a rozvojová banka, a. s., declares that as of the date of processing the annual review no negative changes in the financial situation or any other changes had occurred that would influence the accurate and correct assessment as to the financial position of Českomoravská záruční a rozvojová banka, a. s.

annual review

Report of the Board of Directors on the Bank's business activities and financial situation for 2014

Economic environment and its impact on the Bank's performance

In contrast to the previous year, 2014 was marked by economic growth. Several factors contributed to improvement in the Czech Republic's overall economic situation. These included in particular favourable economic development in the euro zone, improving consumer confidence and business investment activities, and a turning point in the state's budget policy. An important factor, albeit one which individual enterprises perceived variously, was the influence of the Czech National Bank's foreign exchange intervention, which was initiated in November 2013 with the objective of avoiding threatened deflation. The Czech National Bank proceeded to this step after exhausting another instrument of monetary policy in the form of decreasing the key interest rate.

At the end of 2014, the fundamental two-week repo interest rate stood at 0.05%. Returns on financial market investments steadily diminished through the past year. This trend was apparent in both money market investments and bonds. Through revaluations of the financial investment portfolio, this trend positively affected the Bank's financial result for 2014 as well as its shareholder's equity.

The year 2014 was marked by a revival of enterprises' interest in new loans, although these were mainly for working capital. Caution regarding investments into new business capacities persisted, however, as could be seen in the structure of guarantees provided to small enterprises. Interest rates for all types of loans, including to businesses and municipalities, remained at historically low levels. Due to limited space for covering credit risk, banks increased their attention on correctly selecting clients, projects to be financed and corresponding loan security. These conditions manifested in demand for guarantees, although at the same time they created a more challenging environment for placing preferential loans, particularly when grants were simultaneously available for the same activities.

Developments in the Czech economy were not the only factors shaping the environment for the Bank's activities. The year 2014 was important, too, for a number of changes in the legal framework for CMZRB's operations and configuring the environment for its work until 2020. The Bank began already during 2014 in responding to some of these changes. Some legal regulations which became effective last year will begin significantly to influence the Bank's activities only in the coming years. This concerns mainly new EU Council and European Commission regulations for European Structural and Investment Funds, which, together with the new regulations on de minimis aid and on block exemptions for providing support to commercial projects, comprise the basic framework for conducting the Bank's main activities in the coming years. A delay in issuing these regulations, however, resulted in an overall substantial hold-up in preparing operational programmes in the Czech Republic as well as in carrying out necessary ex ante analysis for configuring financial instruments. CMZRB therefore had to respond to these circumstances by postponing until 2015 some already initiated preparations for the administration of financial instruments. The new framework national programme approved by the government in December 2014 and effective until the end of 2023 will undoubtedly contribute to partially bridging an impending gap in the offer of guarantees for small and medium-sized enterprises. This framework will devote special attention to supporting the investment projects of social entrepreneurs.

The emphasis given to broader use of financial instruments creates opportunity to expand the Bank's activities and take advantage of the effects of concentrating the administration of financial instruments. Such administration will nevertheless occur in an environment shaped by growing administrative requirements and complications as well as decreased remuneration levels. It is therefore important to complete the discussion about organising the implementation structure for financial instrument administering initiated by state authorities as soon as possible and with unambiguous conclusions. Finding a suitable method for communicating changes in rules on providing support to entrepreneurs and banks will be one of the important tools for responding to the more complicated conditions for obtaining such support.

Based on requirements from the State Housing Development Fund, last year also saw the preparation of changes in procedures and principles for payment within the long stabilised area of grant disbursement. Considering the large number of administered contracts, the transfer to the new regime and its stabilisation will be a challenging task for 2015.

Legislative requirements also resulted in greater activities than in previous years for the Bank in terms of corporate governance, as well as in conducting banking transactions. Incorporating changes ensuing from amendments to the Act on Banks and the corresponding Czech National Bank decree required adjustment to a number of CMZRB's internal guidelines. Significant attention was also devoted to measures for preventing legal entities' criminal liability and preparing and implementing a compliance programme.

Development and guarantee institutions within European associations of which CMZRB is a member displayed greater interest in exchanging experience and information and co-ordinating common positions. This affected the Bank's activities in this area. One of the key topics was improving and expanding co-operation between the European Investment Bank and national development institutions. The European Commission's massive plan to boost investments into infrastructure, energy, innovation and development of SMEs provides new possibilities for public and private financial institutions across Europe to deepen their co-operation.

Project for transforming the Bank

The government's programme declaration from April 2014 contained another impulse for continuing the Bank's transformation project which had been initiated in 2012. In this document, the government declared its intention to support the development of SMEs and in this context stated that it "shall do so by means of the development and capital strengthening of Českomoravská záruční a rozvojová banka, which, as a bank 100% owned by the state, meets the preconditions for financing primarily SMEs and their development".

In June 2014, the final phase of the Bank's ownership transformation was initiated. Based on a resolution of the General Meeting, the Bank paid cash and non-cash dividends to all shareholders, and the proportion of own shares held in treasury by the Bank thereby decreased to 14.19%. CMZRB's results for 2014 provide the opportunity for own treasury shares held by the Bank to be completely eliminated in 2015.

At a General Meeting in June 2014, the Bank's shareholder approved the new wording of the Bank's Articles of Association. Members of the Bank's supervisory board were replaced, with three new members being elected and two members re-elected. The composition of the audit committee also changed, with the number of members decreasing from four to three.

In addition to the aforementioned statutory and organisational changes, the authorised ministries representing the Bank's shareholder conducted preparation of conceptual materials for CMZRB's broader involvement in financial instruments administration. The Bank actively participated in their preparation as well as in preparing the new national guarantee programme for 2015-2023. In many ways, these materials' contents support the implementation of CMZRB's transformation project. It is very positive that the intention to define the long term space for CMZRB's further operations in the national economy has clear support from representatives of its shareholder. The final effect of CMZRB's transformation project will be decided by measures subject to government approval, which should occur during 2015.

Preparation of changes in the external environment for the Bank's broader participation in financial instrument administration was slower than originally anticipated at the time the CMZRB transformation project was initiated. Nevertheless, the results achieved last year further reinforce the foundation for the next steps which will follow in 2015. The objectives of these steps will be to prepare products meeting the requirements of programme originators as well as technical and personnel framework for their provision while complying with the conclusions from analyses defining the space for deploying financial instruments.

Economic results

Basic economic characteristics of the Bank for 2010–2014

	Unit	2010	2011	2012	2013	2014
Total balance sheet	CZK mil.	58,147	58,700	111,706	98,042	127,337
Assets:						
Deposits and loans at banks	CZK mil.	13,040	16,932	70,045	63,884	91,060
Securities accepted by the Czech National Bank for refinancing	CZK mil.	16,584	14,384	18,545	7,783	9,946
Debt securities	CZK mil.	7,235	8,443	5,513	11,272	13,929
Payments from guarantees and other classified receivables	CZK mil.	3,874	4,324	4,479	3,556	3,082
Liabilities and equity:						
Shareholders' equity	CZK mil.	5,692	5,735	4,958	4,451	4,695
Liabilities	CZK mil.	52,455	52,965	106,748	93,591	122,642
of which: reserves	CZK mil.	2,277	2,219	2,342	2,495	2,909
funds to cover credit risks	CZK mil.	3,295	2,998	2,680	2,557	2,341
Off-balance sheet:						
Guarantees granted	CZK mil.	23,649	21,398	19,039	18,129	17,900
Total revenues	CZK mil.	4,924	4,537	4,410	3,505	2,969
of which: from securities and interbank operations	CZK mil.	828	795	725	516	426
from operations with clients	CZK mil.	1,197	1,099	976	686	568
Total expenses	CZK mil.	4,070	3,688	3,599	3,157	2,707
of which: net impairment allowances and provisions	CZK mil.	404	184	225	442	382
Profit after tax*)	CZK mil.	854	849	812	348	262
Capital ratio for total capital	%	16.4	17.2	14.4	16.0	17.1

Business activity increased during 2014 in comparison with the previous year. Newly signed guarantee and loan transactions totalled CZK 8 billion (CZK 6.8 billion in 2013). The growth was made possible in particular by use of the Bank's own resources for financing the costs of preferential guarantees in programmes supporting small and medium-sized enterprises. Even this effort by the Bank to maintain continuity in the provision of guarantees was not able to compensate wholly the suspension of guarantee financing and loan programmes from EU funds, and the total value of the guarantee and loan transaction portfolios thus decreased by 5.4% to CZK 22 billion.

Savings in net provision creation and lower income taxes failed to fully offset a decline in income from business activity (–CZK 116 million) which was due to the diminished portfolios and changes in the Bank's pricing policy (since the second half of 2012, the prices of newly provided loans and guarantees have not included profit) and in income from financial investments (–CZK 105 million) during this time of historically low interest rates. The profit achieved after tax of CZK 262 million is CZK 86 million lower than in 2013. There was a year-on-year increase in shareholder's equity from CZK 4.5 billion to CZK 4.7 billion arising especially from increase in revaluation differences. The capital ratio stood at 17.14% as of 31 December 2014, which is 1.14 percentage points higher than at the close of the previous year.

Credit risk constituted the most significant type of risk impacting the Bank, and 85% of capital dedicated to risk coverage related to this type of risk. As of the end of 2014, all expected credit risk losses were fully covered by impairment allowances and provisions in an amount corresponding to Czech and international standards, and the total balance of impairment allowances and provisions for credit risk was CZK 4.8 billion (i.e. 22% of the value of the guarantee and loan portfolio). Credit risks for certain types of guarantee products were covered by credit risk funds provided by the programme originators in a total value of CZK 2.3 billion. As of the end of the year, moreover, the Bank had at its disposal reserve funds in shareholder's equity of CZK 1.15 billion.

* While using the Bank's own resources for financing preferential guarantees in programmes supporting small and medium-sized enterprises in the amount of CZK 208 million in 2012, CZK 743 million in 2013 and CZK 566 million in 2014.

The overall balance sheet at the end of 2014 was 30% larger than in the previous year and netted to CZK 127 billion. This growth was related especially to higher short-term liabilities (+CZK 30.4 billion), and in particular those due to state institutions. On the assets side, there was in particular an increase in amounts due from banks (+CZK 27.2 billion) and in values of bonds (+CZK 4.8 billion). The balance sheet total does not include bank guarantees issued primarily for loans to small and medium-sized enterprises and which comprise a significant part of the Bank's business activities and credit exposure. Their value was CZK 17.9 billion as of the end of 2014.

On the assets side, the Bank had at its disposal a portfolio of financial investments amounting to CZK 115 billion (90.3% of net assets) and placed as bank deposits, predominantly in the forms of reverse repo operations (71.5% of net assets), as well as state bonds and bonds of selected banks and companies (18.8% of net assets). Loans provided to state institutions constituted an important net asset item (6% of net assets), as did loans to other clients (3.1% of net assets) reported in the item loans and advances to customers. Non-earning assets comprised 0.4% of the total balance sheet.

The funding sources on the liabilities and equity side were provided primarily by amounts due to customers (81.6% of liabilities and equity) and banks (11.2% of liabilities and equity), shareholder's equity (3.7% of liabilities and equity), provisions (2.3% of liabilities and equity), and temporary and other liabilities.

From a perspective of profit development, 2014 saw a decline from the level previously achieved. This development had been planned, however, as non-profit products have been provided since 2012. After correcting for costs covered from the Bank's own resources used for programmes supporting small and medium-sized enterprises ensuring continuity in the provision of preferential guarantees (CZK 566 million), CMZRB would continue to display very good economic efficiency. The comparable profit figure would thus be CZK 828 million (CZK 1,091 million in 2013), which would represent a comparable return on shareholder's equity of 21.5% and profit per employee of CZK 3.92 million after administrative costs per employee of CZK 1.46 million.

Calculation of capital ratio and other additional indicators

Indikator	Unit	2010	2011	2012	2013	2014
Tier 1 (T1) capital	CZK '000	**4,666,426**	**4,821,166**	**3,775,768**	**3,876,104**	**3,867,425**
Common equity tier 1 (CET1) capital	CZK '000	**4,666,426**	**4,821,166**	**3,775,768**	**3,876,104**	**3,867,425**
Instruments eligible for CET1 capital	CZK '000	**2,131,550**	**2,131,550**	**237,810**	**237,810**	**1,355,628**
Paid-in CET1 instruments	CZK '000	2,131,550	2,131,550	2,131,550	2,131,550	2,131,550
Acquired own CET1 instruments	CZK '000	**0**	**0**	**-1,893,740**	**-1,893,740**	**-775,922**
Own CET1 instruments acquired directly	CZK '000	0	0	-1,893,740	-1,893,740	-775,922
Retained earnings/accumulated losses	CZK '000	**1,406,286**	**1,570,430**	**2,414,171**	**2,519,209**	**1,413,018**
Retained earnings/accumulated losses from previous years	CZK '000	1,406,286	1,570,430	2,414,171	2,519,209	1,413,018
Accumulated other comprehensive income	CZK '000	0	0	0	0	514,099
Other reserve funds	CZK '000	1,150,000	1,150,000	1,150,000	1,150,000	1,150,000
Adjustments to CET1 capital from use of prudential filters	CZK '000	0	0	0	0	-18,546
Value adjustments pursuant to prudential revaluation requirements	CZK '000	0	0	0	0	-18,546
Other intangible assets	CZK '000	**-21,410**	**-30,814**	**-26,213**	**-30,915**	**-32,675**
Other intangible assets – gross value	CZK '000	-21,410	-30,814	-26,213	-30,915	-32,675
Other transitional adjustments to CET1 capital	CZK '000	0	0	0	0	-514,099
Tier 2 (T2) capital	CZK '000	0	0	0	0	0
Capital	CZK '000	**4,666,426**	**4,821,166**	**3,775,768**	**3,876,104**	**3,867,425**
Total risk exposure	CZK '000	**28,411,843**	**28,081,701**	**26,221,834**	**24,183,705**	**22,563,626**
Total risk-weighted exposure relating to credit risk pursuant to the Standardised Approach	CZK '000	**23,393,030**	**22,976,463**	**20,432,320**	**20,526,097**	**18,765,897**
Exposures to central governments and banks	CZK '000	0	60,041	182,699	89,147	31,084

Indikator	Unit	2010	2011	2012	2013	2014
Exposures to regional governments and local bodies	CZK ‘000	516,771	780,542	349,186	355,538	205,584
Exposures to institutions	CZK ‘000	1,901,311	2,137,722	1,282,623	1,059,241	1,114,966
Exposures to enterprises	CZK ‘000	18,764,045	17,820,212	16,442,222	16,912,362	14,904,965
Exposures to retail	CZK ‘000	538,087	538,652	520,986	692,337	1,428,522
Exposures secured by property	CZK ‘000	32,141	91,361	95,616	89,595	156,394
Exposures in default	CZK ‘000	1,004,164	845,239	871,180	565,639	493,518
Exposures in covered bonds	CZK ‘000	507,758	382,885	578,004	671,612	144,034
Exposures to institutions and enterprises with short-term credit evaluation	CZK ‘000	50,919	133,916	41,343	26,379	77,467
Equities	CZK ‘000	0	0	0	0	1,347
Other exposures	CZK ‘000	77,834	185,893	68,461	64,247	208,016
Risk exposure relating to position, foreign exchange and commodity risks pursuant to the Standardised Approach	CZK ‘000	**2,126,725**	**2,167,525**	**2,804,401**	**622,385**	**592,813**
Tradable debt instruments	CZK ‘000	2,804,401	622,385	592,813		
Currency transactions	CZK ‘000	93,900	0	0	0	0
Total risk exposure relating to operational risk	CZK ‘000	**2,892,088**	**2,937,713**	**2,985,113**	**3,035,223**	**2,909,928**
Operational risk – basic indicator approach	CZK ‘000	2,892,088	2,937,713	2,985,113	3,035,223	2,909,928
Total risk exposure relating to revaluation adjustments to credit risk	CZK ‘000	**0**	**0**	**0**	**0**	**294,988**
Standardised Approach	CZK ‘000	0	0	0	0	294,988
Capital ratio for Tier 1 equity capital	%	16.4	17.2	14.4	16.0	17.1
Capital ratio for Tier 1 capital	%	16.4	17.2	14.4	16.0	17.1
Capital ratio for total capital	%	16.4	17.2	14.4	16.0	17.1
Return on average assets (ROAA)[1]	%	1.34	1.43	1.19	0.41	0.35
Return on average equity (ROAE)[1]	%	18.39	17.67	18.57	9.02	6.81
Assets per employee1	CZK ‘000	265,510	266,816	514,772	445,646	595,033
Administrative costs per employee[1]	CZK ‘000	1,385	1,397	1,399	1,356	1,455
Net profit per employee[1]	CZK ‘000	3,899	3,860	3,740	1,583	1,226

Reconciliation of regulatory and accounting capital

The following tables summarise the composition of regulatory and accounting capital as well as individual indicators as of 31 December 2014 and 31 December 2013, thus providing complete reconciliation of individual regulatory capital items with the institution’s capital and the balance sheet.

[1] Calculations were made pursuant to Decree No. 163/2014 Coll., on performing the activities of banks, credit unions and investment firms.

As of 31 December 2014	Regulatory capital CZK mil.	Shareholder's equity CZK mil.
Paid-in share capital entered in the Commercial Register	2,132	2,132
(–) Capital investments into own instruments	-776	-776
Retained earnings from previous periods	1,413	1,413
Profit for the period	0	262
Accumulated other comprehensive income	514	514
Other reserve funds	1,150	1,150
(–) Value adjustments pursuant to prudential revaluation requirements (additional value adjustments)	-19	-
(–) Intangible assets other than goodwill	-33	-
(–) Adjustments relating to unrealised gains and losses	**-514**	-
Total capital eligible for inclusion into Tier 1	**3,867**	
Total shareholder's equity		**4,695**
Total Tier 2 capital	0	
Capital relevant for calculating large exposure limits, qualified participation limits and capital ratio	**3,867**	

As of 31 December 2013	Regulatory capital CZK mil.	Shareholder's equity CZK mil.
Paid-in share capital entered in the Commercial Register	2,132	2,132
(–) Capital investments into own instruments	-1,894	-1,894
Retained earnings from previous periods	2,519	2,519
Profit for the period	0	348
Accumulated other comprehensive income	-	196
Other reserve funds	1,150	1,150
(–) Value adjustments pursuant to prudential revaluation requirements (additional value adjustments)	-	-
(–) Intangible assets other than goodwill	-31	-
(–) Adjustments relating to unrealised gains and losses	-	-
Total capital eligible for inclusion into Tier 1	**3,876**	
Total shareholder's equity		**4,451**
Total Tier 2 capital	0	
Capital relevant for calculating large exposure limits, qualified participation limits and capital ratio	**3,876**	

Business activities

1/ Product overview

During 2014, the Bank provided the following products:

a) Guarantees

- Guarantees for bank loans provided by a simplified procedure and with a limited guaranteed amount for a portfolio of guaranteed loans (hereinafter just "portfolio guarantees") provided under the GUARANTEE programme (guarantees for loans to small enterprises) for loans up to CZK 5 million and as much as 70% of the loan principal,
- guarantees for tender bids for small and medium-sized enterprises in amounts of CZK 100,000 to CZK 5 million, and
- preferential guarantees for bank loans under the INOSTART programme for entrepreneurs implementing projects anywhere in the Czech Republic for loans up to CZK 15 million and as much as 60% of the loan principal.

b) Loans

- Loans for small enterprises in South Bohemia Region in amounts up to CZK 1 million, with a fixed interest rate of 4% p.a. and maturity up to 5 years under the Programme of Preferential Regional Loans for Small Enterprises and Municipalities in the South Bohemia Region;
- loans for municipalities in South Bohemia Region in amounts up to CZK 2 million with a fixed interest rate that is continuously updated for new loans according to the development of market interest rates and maturity up to 10 years under the Programme of Preferential Regional Loans for Small Enterprises and Municipalities in South Bohemia Region;
- loans for small enterprises, including start-up enterprises, within the Moravian–Silesian Region to implement projects increasing employment in amounts up to CZK 10 million, with interest rates of 1 – 5% p.a., maturity up to 7 years and the possibility of subsidies under the REVIT programme;
- long-term loans for municipalities or associations of municipalities (with the exception of Prague) under the MUFIS 2 investment financing programme to maintain and develop municipal infrastructure in amounts up to CZK 40 million, with a fixed or variable interest rate determined individually according to current market conditions, maturity up to 10 years and a grace period up to 2 years; and
- long-term loans funded by the Regional Development Fund for municipalities or associations of municipalities (with the exception of Prague) to co-finance projects for improving local infrastructure for business and non-business purposes in amounts up to CZK 30 million, with a preferential fixed or variable interest rate determined individually according to current market conditions, maturity up to 10 years and a grace period up to 3 years.

In 2014, the Bank also conducted commercial representation activities for Czech Export Bank for two types of products which can be used by entrepreneurs with turnover for the most recently completed accounting period not exceeding the equivalent of EUR 50 million and at least a two-year history. These consisted of:

- guarantees for loans not exceeding 80% of the receivables provided to subcontractors of domestic exporters, usually in amounts up to CZK 30 million with a guarantee term up to 2 years;
- loans for financing production for export in amounts up to 85% of the export contract's value with a variable interest rate and maturity up to 2 years; and
- direct export supplier loans with maturity up to 2 years with a variable interest rate in amounts up to 100% of the export contract's value.

Both types of loans may be provided in the currency of the export contract (usually CZK, EUR or USD).

2/ Support to small and medium-sized enterprises

a) Overall results

CMZRB provided support to small and medium-sized enterprises (hereinafter just SMEs) especially on the basis of agreements concluded with the Ministry of Industry and Trade.

Guarantees for investment loans and loans for the purchase of inventory were provided only in the programme financed by national resources. The outcome from implementing this programme, which was designated only for small enterprises, confirms the continuing strong interest among enterprises, and especially in the area of obtaining loans to finance inventory.

Provision of guarantees for loans to start-up enterprises for innovative projects within the INOSTART programme continued in 2014. The INOSTART programme was expanded during the year across the entire Czech Republic. Loans supported by guarantees from CMZRB were provided by Česká spořitelna, a.s.

The Bank also supported small entrepreneurs with preferential loans through two programmes. The first was the REVIT programme focused on revival and developing entrepreneurial activities within the Moravian-Silesian Region. Applications for support from this programme ceased to be accepted at the end of 2014. The second loan programme was implemented in co-operation with the South Bohemia Region to support business projects being implemented within this region.

In 2014, SMEs submitted a total of 2,423 applications for support in the form of loan guarantees and applications for loans (see Table 3). In total, 1,988 of these applications were approved and 32 applications were rejected because they either did not meet programme criteria or represented risks too great for the project to receive financing. A total of 178 applicants withdrew their applications during processing. The remaining 225 applications were not resolved in 2014 and will carry over into 2015.

Applications for support and their settlement — Table 3

Indicator		**2010**	**2011**	**2012**	**2013**	**2014**
Total applications submitted	Number	2,288	487	1,095	1,903	2,423
Approved	Number	1,318	241	793	1,563	1,988
Rejected or withdrawn	Number	855	109	125	229	210
Carried into following year	Number	115	137	177	111	225

Most of the loans and guarantees provided were directed to small enterprises with up to 49 employees (see Table 4).

Supported projects divided according to sizes of enterprises — Table 4

	Guarantees (excluding bids to public tenders)				Loans			
	Number		Amount		Number		Amount	
Number of employees		**(%)**	**CZK mil.**	**(%)**		**(%)**	**CZK mil.**	**(%)**
0 to 9	1,078	55.2	1,874.2	46.7	26	72.2	54.7	63.3
10 to 49	873	44.7	2,124.0	53.0	8	22.2	14.6	17.0
50 to 249	1	0.1	12.0	0.3	2	5.6	17.0	19.7
Total	**1,952**	**100.0**	**4,010.2**	**100.0**	**36**	**100.0**	**86.3**	**100.0**

b) Guarantees

The Bank provided 1,952 loan guarantees in a total amount of CZK 4,010 million based on guarantee contracts concluded in 2014. The guarantees supported loans of CZK 5,711 million (see Table 5).

Guarantees issued (excluding bids to public tenders) and loans guaranteed Table 5

Indicator		2010	2011	2012	2013	2014
Guarantees issued	Number	1,224	111	697	1,546	1,952
Amount of guarantees issued	CZK mil.	6,593	472	1,534	3,251	4,010
Amount of loans guaranteed	CZK mil.	10,070	630	2,215	4,616	5,711
Average guarantee coverage	%	65	75	69	70	70

In the national guarantee programme, small enterprises acquired guarantees in the amount of CZK 3,967 million. These guarantees were used as security for 1,939 loans in amounts totalling CZK 5,639 million. Of these, 10 guarantees in a sum of CZK 102 million were provided in 2014 to enterprises affected by floods in June 2013. Start-up enterprises were provided with 13 guarantees amounting to CZK 43 million within the INOSTART programme.

The largest proportions of guarantees were used to support projects in the Moravian–Silesian Region and in Prague (see Table 6).

Regional structure of guarantees provided
(in % of contracted value of guarantees issued) Table 6

Region		2010	2011	2012	2013	2014
Praha (Capital City of Prague)	%	5.6	4.3	8.1	11.2	14.2
Středočeský (Central Bohemia Region)	%	8.2	13.0	4.8	8.2	10.6
Jihočeský (South Bohemian Region)	%	4.9	2.6	7.5	5.5	5.9
Plzeňský (Pilsen Region)	%	7.0	6.3	4.3	4.6	4.7
Karlovarský (Karlovy Vary Region)	%	1.4	1.2	2.2	1.5	1.1
Ústecký (Ústí Region)	%	2.1	1.9	3.0	3.7	2.8
Liberecký (Liberec Region)	%	9.7	11.3	5.1	3.9	3.3
Královéhradecký (Hradec Králové Region)	%	10.0	1.2	5.1	4.6	4.6
Pardubický (Pardubice Region)	%	3.8	13.7	5.2	4.7	4.1
Vysočina (Vysočina Region)	%	4.7	1.5	5.4	3.1	3.1
Jihomoravský (South Moravian Region)	%	15.2	4.6	8.4	14.0	13.1
Olomoucký (Olomouc Region)	%	8.3	19.9	15.4	6.8	8.0
Zlínský (Zlín Region)	%	7.1	1.3	4.5	6.0	4.7
Moravskoslezský (Moravian-Silesian Region)	%	12.0	17.1	20.8	22.2	19.8
Total	%	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Based on a commitment to extend the liability period, the Bank prolonged this period through amendments to guarantee contracts for 1,321 guarantees summing to CZK 3,616 million. This enabled entrepreneurs to draw additional credit to finance working capital needs.

In addition to guarantees for bank loans, 421 guarantees were provided for bids to public tenders totalling CZK 210 million.

The breakdown of guarantees for 2014 according to the main groups of economic activities to which project support was directed was fundamentally influenced by the conditions that had been established for programme support. The largest number of guarantees was provided to projects in wholesale and retail, followed by manufacturing (see Table 7).

Sector structure of guarantees provided in 2013
(in % of contracted values of newly issued guarantees) Table 7

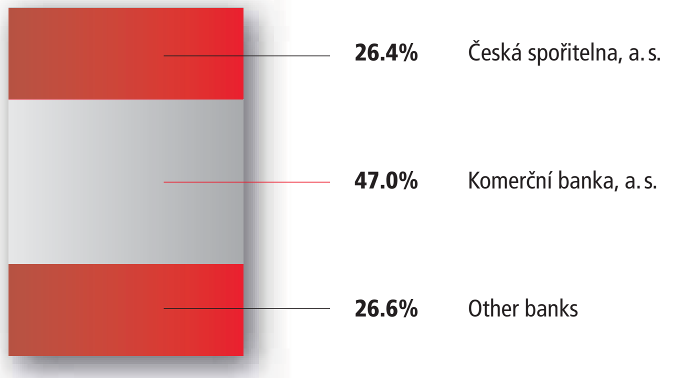
Sector		
Manufacturing (CZ NACE 10-33)	%	26.5
Electricity, gas, steam and air conditioning supply (CZ NACE 35)	%	0.5
Construction (CZ NACE 41-43)	%	12.2
Wholesale and retail trade; repair and maintenance of motor vehicles and motorcycles (CZ NACE 45-47)	%	52.2
Accommodation and food service activities (CZ NACE 55-56)	%	1.8
Other service activities (CZ NACE 05-09, 36-39, 49-53, 58-75, 77-82, 84-88, 90-99)	%	6.8
Total	%	**100.0**

During 2014, the majority of guaranteed transactions were concluded with Komerční banka, a.s., and Česká spořitelna, a.s., (see Graph 1).

Among other banks, Raiffeisenbank, a.s., (8.4%) and UniCredit Bank Czech Republic, a.s., (8.3%) had the greatest participation in guarantee transactions followed by GE Money Bank, a.s. (4.6%) and Československá obchodní banka, a.s. (3.7%).

Graph 1

Percentage breakdown of guarantee transactions by lending banks (2014)



On the basis of a Contract for Commercial Representation concluded with Czech Export Bank, in 2014 Czech Export Bank provided two pro-export payment guarantees amounting to CZK 24 million.

c) Loans

In 2014, the Bank provided a total of 36 loans for small enterprises amounting to CZK 86 million (see Table 8).

These consisted of:

- preferential loans for small enterprises within the REVIT programme, with 22 loans provided and amounting to CZK 73 million for projects in the Moravian-Silesian Region; and
- reduced-interest loans under the South Bohemia Regional Programme, with 14 loans provided amounting to CZK 13 million.

Preferential loans provided Table 8

Indicator		2010	2011	2012	2013	2014
Loans provided	Number	94	136	96	17	36
Amount of loans provided	CZK mil.	629	1,090	782	101	86
Average loan amount	CZK mil.	6.7	8.0	8.1	6.0	2.3

The largest proportion of supported loans was in manufacturing (see Table 9).

Sector structure of loans provided
(in % of contracted value of newly issued loans) Table 9

Sector		
Manufacturing (CZ NACE 10-33)	%	54.4
Construction (CZ NACE 41-43)	%	11.8
Wholesale and retail trade; repair and maintenance of motor vehicles and motorcycles (CZ NACE 45-47)	%	15.1
Accommodation and food service activities (CZ NACE 55-56)	%	1.2
Other service activities (CZ NACE 05-09, 36-39, 49-53, 58-75, 77-82, 84-88, 90-99)	%	17.5
Total	%	**100.0**

In relation to its commercial representation activities for Czech Export Bank's pro-export loans, the first application for a pro-export loan amounting to CZK 25 million was submitted for evaluation in December 2014.

3/ Support for reconstructing apartment houses

In 2014, the Bank administered a total of 9,354 Contracts on Providing Grants to Cover Loan Interest (of the original 10,122 contracts concluded). On the basis of these, it paid out more than CZK 876 million. From the start of the programme in support of apartment house reconstruction until the end of 2014, grant recipients were collectively paid a total of CZK 7,067 million, which comprises 51.7% of the total volume of concluded Contracts on Providing Grants to Cover Loan Interest (CZK 13,664 million).

The Bank also administered a portfolio of bank loan guarantees during 2014 which enabled owners or co-owners of apartment houses to obtain loans for their repair. As of the end of 2014, this portfolio was composed of 1,587 bank loan guarantees (of which 112 were portfolio guarantees), and the unpaid principal of the guaranteed loans amounted to CZK 5,023 million.

4/ Financing municipal infrastructure

a) Loans under the MUFIS 2 programme

The MUFIS 2 programme had been announced in October 2009, and loans provided are designated for the purchase or refurbishment of municipal properties, and especially technical infrastructure, school and pre-school facilities, as well as cultural and sport facilities. The programme also encompasses projects directed to saving energy. Loans are provided from the Common Loan Fund created from the resources of the Bank and MUFIS, a.s.

In 2014, the Bank provided 2 new loans totalling CZK 28 million. Since the programme's announcement, 11 loans summing to almost CZK 74 million have been provided.

b) Loans from the Regional Development Fund

Loans from the Regional Development Fund are designated for projects focusing on transportation and technical infrastructure, construction of commercial real estate, as well as sport, cultural and educational facilities. Issuance of these loans is dependent on the generation of sufficient funds from loan repayments in previous years. In 2014, the Bank provided 2 loans totalling CZK 11 million. Since announcing the programme with new conditions in 2008, 36 loans have been issued amounting to CZK 332 million.

5/ Trading on financial markets

During 2014, the Bank concluded transactions on the money and capital markets in order to manage its liquidity, administer its portfolio of money and capital market instruments, manage interest-rate and currency risks, and refinance the lending programme for supporting SMEs. In administering its portfolio of money and capital market instruments, the Bank continued its conservative investment strategy. CMZRB was oriented exclusively to purchasing government bonds, treasury bills and bonds of a selected group of issuers with the highest credit ratings.

6/ Other lending activities

As a financial manager for infrastructure programmes, the Bank secured financing for these programmes totalling CZK 1.3 billion during 2014. This amount included resources obtained from the European Investment Bank, the state budget and the State Fund for Transport Infrastructure.

A large part of those resources (CZK 750 million) was used for water management projects. It consisted of CZK 162 million for anti-flood programmes and CZK 588 million for construction and renovation projects relating to water supply and sewage infrastructure.

As a financial manager, the Bank disbursed CZK 550 million for financing transportation projects. All of these related to Czech Motorways Project B, which takes in construction of the Lovosice – Ústí nad Labem section of the D8 motorway and the Osičky – Hradec Králové section of the D11 motorway.

In 2014, the Bank continued administering interest subsidy payments related to commercial loans for participants in the Project for Construction and Renovation of Water Supply and Sewage Infrastructure, paying out almost CZK 30 million to 102 recipients.

External communications

An added value from the Bank s operations can be reached only if its activities react to requests and suggestions from the external environment. During 2014, the Bank concentrated its attention and communication activities to several crucial topics. As a result of the Bank's focus on the domestic market, most of these transpired at the national level. Nevertheless, it is also necessary to mention the Bank's increased activity in international co-operation and contacts with development and guarantee institutions in the EU as well as in other countries.

Two top-priority and very closely connected topics related to continuing the transformation process of the Bank, which had been initiated in 2012 by purchasing shares from banks that were its private shareholders. The next step was transfer of the own treasury shares thereby acquired to the ownership of the Czech Republic, and external circumstances made of these preparations an arduous task. This was completed in the new legal environment ensuing after the new Civil Code came into effect. The solution based on paying a non-cash dividend, the first phase of which took place in mid-2014, resulted from relatively lengthy negotiations among the shareholder's representatives within which the Bank's management participated. The negotiations had the objective of ensuring a legally secure and economically feasible method for this operation.

Increased emphasis on broader use of financial instruments to support projects in various areas of the economy in a natural manner introduced an additional matter which directly affected the Bank's activities and its operational direction for the years to come. This concerned finding the most appropriate institutional solution for the administration of financial instruments in the Czech Republic. CMZRB contributed to this discussion by submitting its suggestions to those ministries representing the Czech Republic as shareholder. As of the end of the year, discussions on this topic had not yet concluded.

Important impetus for CMZRB to address several ministries was the final phase in preparation of new operational programmes for the current structural fund programming period as well as a number of national documents to establish procedures for their implementation. As the most important manager of such financial instruments in the Czech Republic during the 2007-2013 programming period, the Bank drew upon its experience thus acquired to submit suggestions and recommendations to the respective ministries. Some were submitted directly and others via a Czech Banking Association working group. The Bank's recommendations and comments concerned establishing conditions for financial instrument operations and in the case of the Operational Programme Enterprise and Innovation for Competitiveness (OP EIC) also this programme's content and later individual executive support programmes.

In the second half of 2014, negotiations were underway (and included the preparation of contractual documentation and other materials) focused upon the sole objective of preparing a new long-term national guarantee programme under the authority of the Ministry of Industry and Trade. Approval of the GUARANTEE 2015–2023 programme created the long-term framework for execution of a national programme which will be the main guarantee offer for SMEs in 2015. In subsequent years, this programme will complement OP EIC guarantee programmes in business sectors not supported by this operational programme. Implementing the new guarantee programme requires concluding agreements between CMZRB and those banks which will utilise these guarantees. Their preparation and negotiations brought new ideas for improving co-operation and achieving greater efficiency on both sides.

Resolving communication with clients and banks in connection with changes in disbursement principles for apartment block repair grants initiated by the State Housing Development Fund was a very demanding task last year which required very intensive preparations from the Bank and State Housing Development Fund. This task will continue in the years to come.

The year 2014 also brought further deepening of co-operation with Czech Export Bank. The range of products regarding which the Bank provides for the introductory phase of communications with applicants on the basis of a contract for commercial representation expanded to included pre-export and direct export loans.

Co-operation with trade associations, commercial banks and other entities was also ongoing in various forms, thereby broadening the interested parties' awareness as to various types of support. Through this channel, too, knowledge was acquired as to the current needs and problems of the individual target groups of applicants and recipients of support. The Bank used the knowledge so obtained in order to improve the services it provides and passed this information on to those partners responsible for establishing the conditions of the provided support. Last year was also significant from the perspective of international co-operation ensuing from CMZRB's membership in three associations joining partner financial institutions and guarantee and development banks, predominantly from EU countries. These were the Network of European Financial Institutions for SMEs (NEFI), European Association of Guarantee Institutions (AECM), and European Association of Long-Term Investors (ELTI). CMZRB organised a workshop and meeting of the Permanent Working Group of NEFI with the objective of analysing impact of latest EU regulations concerning state aid on programmes designated for the SME sector. This included sharing experiences in applying various models for administering state aid.

In November 2014, CMZRB hosted the second General Assembly of the ELTI, which as of the date of the meeting brought together 22 institutions focused on long-term financing and with a total balance sheet of EUR 2.3 trillion. ELTI called for strengthening the use of public funds to support economic growth and expanded its membership to include two new institutions.

CMZRB's direct contacts with the European Investment Bank and the Council of Europe Development Bank also continued. Moreover, non-European institutions showed interest in the method of setting and implementing guarantee programmes in the Czech Republic. In the second half of the year, meetings took place in Prague with representatives of Japanese guarantee institutions, managers from Korea Credit Guarantee Fund, and officials from the Bulgarian National Guarantee Fund.

Goals for further development

The possibilities for implementing the Bank's development goals were significantly impacted during 2014 by an overall slowing of preparations for the current structural funds period, by delay in key decisions on the extent of financial instruments and the areas within which they may be used under operational programmes, as well as in reaching an institutional solution for their administration. The direction and objective of the strategic goals did not change, however. While developing in accordance with the project for CMZRB's transformation, these goals remain to develop the Bank's activities in administering financial instruments using structural funds beyond providing support to SMEs and establishing itself as the most important loan and guarantee fund manager providing services to managing authorities responsible for operational programmes.

CMZRB's activity will continue to be performed in a way that will consistently allow the state to use the Bank's services as an in-house provider. The process of transferring own treasury shares to the Czech Republic in the form of non-cash dividends will be completed in 2015.

The main economic principles according to which the Bank is managed will continue to maintain its ability over the long term to operate in the black while achieving a rational level of profit that prevents the real value of its share capital from being eroded. At the same time, however, the Bank will take advantage of possibilities in implementing the transformation project and developing its operations to develop and diversify activities supporting the government's intentions to revive investments.

A key challenge will be to prepare and manage the Bank's operations not only as an administrator of financial instruments created directly by the governing bodies of operational programmes but also, as so required, to administer the fund of funds and its products.

In 2015, the Bank will focus especially on:

- utilization of resources revolving from financial instruments and obtained through additional measures approved by the Bank's shareholder to finance the first call of the national GUARANTEE 2015-2023 programme for SMEs;
- conducting activities of the guarantee fund for the INOSTART programme, as well as loan programmes for municipalities;
- ensuring smooth disbursement of grants for apartment block repair pursuant to up-dated rules;
- co-operation with the Ministry of Industry and Trade in preparing the first calls under new support programmes financed by structural funds using financial instruments and their implementation structures;
- collaborating with other managing authorities of operational programmes in preparing for use of financial instruments in their operational programmes financed from structural funds; and
- preparing product changes in accordance with the conditions of structural funds legislation in terms of organisation, methodology, staffing and IT support.

Report of the Supervisory Board of Českomoravské záruční a rozvojové banky, a.s.

During 2014, the Supervisory Board regularly carried out its duties as defined by law and the Articles of Association of Českomoravská záruční a rozvojová banka, a. s. In its capacity as the Bank's oversight body, the Supervisory Board monitored the work of the Board of Directors in discharging its duties, conducting the Bank's business activities and financial management, and executing its strategic policy. The Supervisory Board was regularly informed about the Bank's activities, its financial situation and other essential matters.

Having examined the financial statements for the year ended 31 December 2014, and on the basis of the external auditor's report, the Supervisory Board states that the accounting records and books were kept in a transparent manner and in compliance with the generally binding accounting regulations for banks as well as with the Articles of Association of the Bank. The accounting records and books reflect the Bank's actual financial situation in all important respects.

KPMG Česká republika Audit, s.r.o., performed an audit of the financial statements and confirmed that the financial statements provide a true and fair view of the financial position of Českomoravská záruční a rozvojová banka, a. s., as of 31 December 2014 and of its operations for that year in accordance with Czech accounting standards. The Supervisory Board acknowledged the Auditor's report by consent.

The Supervisory Board reviewed without comment the Report of the Board of Directors on the Bank's Business Activities and Financial Situation for 2014. It likewise examined the Report of the Board of Directors on Relations between Related Entities for 2014.

Based upon the facts stated above and pursuant to the Articles of Association of Českomoravská záruční a rozvojová banka, a. s., the Supervisory Board recommends that the General Meeting approve the following as presented by the Bank's Board of Directors: Report of the Board of Directors on the Bank's Business Activities and Financial Situation for 2014, Report of the Board of Directors on Relations between Related Entities for 2014, and the financial statements of Českomoravská záruční a rozvojová banka, a. s. for 2014.

The Supervisory Board also reviewed the following proposals presented by the Bank's Board of Directors: the profit distribution for 2014, the proposal for transferring the Bank's treasury shares to the shareholder (the Czech Republic), the increase in the Bank's participation in co-financing support, the change of the Articles of Association of Českomoravská záruční a rozvojová banka, a. s., the Bank's long-term strategy for 2015-2023, appointment of the members of the Bank's bodies (Supervisory Board and the Audit Committee), remuneration of the members of the Bank's bodies for 2014 (Supervisory Board and the Audit Committee), and the policies for remunerating members of the Bank's bodies (Supervisory Board and the Audit Committee) in the following period.

Prague, 10 March 2015

On behalf of the Audit Committee of Českomoravská záruční a rozvojová banka, a. s.:

Robert Szurman
Supervisory Board Chairman

Report of the Audit Committee of Českomoravské záruční a rozvojové banky, a. s.

The Audit Committee was established by a resolution of the General Meeting of Českomoravská záruční a rozvojová banka, a. s., on 27 April 2010.

During 2014, the Audit Committee fulfilled its obligations and carried out its duties as defined by Act No. 93/2009 Coll., on Auditors, and in accordance with the Articles of Association of Českomoravská záruční a rozvojová banka, a. s. (hereinafter referred to as the "Bank").

Within its competence, the Audit Committee oversaw in 2014 the procedure of compiling the Bank's financial statements for 2013 and the process of their mandatory audit as executed by the auditor KPMG Česká republika Audit, s.r.o. It also appraised the independence of the audit firm KPMG Česká republika Audit, s.r.o. and the character of additional services provided by the external auditor, concluding that on the basis of the presented documents the external auditor may be regarded as independent. Last year's co-operation with the external auditor proceeded without issue.

The Audit Committee also reviewed the Report on the Information Systems Audit, which was conducted by the audit firm Deloitte Advisory s.r.o.

At its regular meetings, the Audit Committee also discussed evaluations as to the effectiveness and efficiency of the Bank's management and control systems, the risk management system and the activities of the Bank's Internal Audit Unit. The Audit Committee states that the systems established within the Bank are functional and efficient and that the measures adopted in relation to the audit findings were satisfactorily followed.

On the basis of a resolution of the Bank's General Meeting in April 2014, the number of members of the Audit Committee was decreased to a total of 3 members. In October 2014, the Bank's Supervisory Board decided to broaden the Audit Committee's authority to include the function of the Risk Committee. Said changes were then included into the wording of the Statutes and the Audit Committee's rules of procedure and the Audit Committee began exercising the function of the Risk Committee.

Prague, 10 March 2015

On behalf of the Audit Committee of Českomoravská záruční a rozvojová banka, a. s.:

Milan Novák
Audit Committee Chairman

annual review

Independent auditor's report to shareholders of Českomoravská záruční a rozvojová banka, a.s.

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Independent Auditor's Report to the Shareholders of Českomoravská záruční a rozvojová banka, a.s.

We have audited the accompanying financial statements of Českomoravská záruční a rozvojová banka, a.s., which comprise the statement of financial position as of 31 December 2014 and the statement of comprehensive income, the statement of changes in equity and the cash flow statement for the year then ended, and the notes to these financial statements including a summary of significant accounting policies and other explanatory notes. Information about Českomoravská záruční a rozvojová banka, a.s. is set out in Note 1 to these financial statements.

Statutory Body's Responsibility for the Financial Statements

The statutory body of Českomoravská záruční a rozvojová banka, a.s. is responsible for the preparation of financial statements that give a true and fair view in accordance with International Financial Reporting Standards as adopted by the European Union and for such internal controls as the statutory body determines are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with the Act on Auditors and International Standards on Auditing and the relevant guidance of the Chamber of Auditors of the Czech Republic. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal controls relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal controls. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements give a true and fair view of the financial position of Českomoravská záruční a rozvojová banka, a.s. as of 31 December 2014, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union.

Prague
26 March 2015

KPMG Česká republika Audit

KPMG Česká republika Audit, s.r.o.
Registration number 71

Pavel Závitkovský
Partner
Registration number 69

annual review

2014

Financial statements for the year ended 31 December 2014 prepared in accordance with IFRS as adopted by the EU

Income statement

	Note	Year ended 31 December 2014 CZKm	Year ended 31 December 2013 CZKm
Interest and similar income		994	1,202
Interest and similar expenses		(483)	(590)
Net interest income	**3.1**	**511**	**612**
Fee and commission income		456	527
Fee and commission expenses		(4)	(4)
Net fee and commission income	**3.2**	**452**	**523**
Gains from financial operations	3.3	102	232
Losses on financial operations	3.3	(72)	(151)
Administrative expenses	3.4	(338)	(329)
Increase in loan impairment and write-offs	3.5	32	(289)
(Increase)/decrease in provisions for guarantees and other provisions	3.6	(341)	(82)
Other operating income		(1)	(1)
Operating profit		**345**	**515**
Share of earnings in associates accounted for using the equity method	3.15	-	1
Profit before income tax		**345**	**516**
Income tax expense	3.7	(89)	(173)
Profit for the year		**256**	**343**

Statement of comprehensive income

	Note	Year ended 31 December 2014 CZKm	Year ended 31 December 2013 CZKm
Profit for the year		**256**	**343**
Other comprehensive income			
Valuation gains/(losses) on available-for-sale financial assets	341	(105)	
Net gains/(losses) on available-for-sale financial assets transferred to income statement on disposal	3.3	52	(79)
Deferred income tax relating to components of the comprehensive income	3.7	(75)	35
Other comprehensive income for the year, net of tax		318	(149)
Total comprehensive income		**574**	**194**

Statement of financial position

	Note	31 December 2014 CZKm	31 December 2013 CZKm
Assets			
Cash and balances with central banks	3.8	91,234	64,152
Loans and advances to banks	3.9	180	140
Financial assets held for trading			
- Debt securities	3.10	415	271
- Derivatives	4.2.2	169	176
Debt securities designated at fair value	3.10	1,091	1,527
Loans and advances to customers	3.11	11,590	14,231
Financial assets available for sale	3.12	16,610	12,237
of which: assets pledged as collateral		8,550	5,650
Financial assets held to maturity	3.13	5,760	5,020
of which: assets pledged as collateral		1,546	1,110
Current income tax assets	3.7	49	42
Investment in associate	3.15	106	105
Intangible assets		33	31
Property, plant and equipment	3.16	135	138
Other assets	3.14	71	77
Total assets		**127,443**	**98,147**
Liabilities			
Deposits from banks	3.17	14,315	15,898
Deposits from customers	3.18	103,952	73,516
Financial liabilities held for trading - derivatives	4.2	221	205
Hedging derivatives	4.2.2	41	54
Current income tax liabilities	3.7	-	-
Deferred tax liabilities	3.7	33	15
Provisions	3.6	2,909	2,495
Other liabilities	3.19	1,179	1,415
Total liabilities		**122,650**	**93,598**
Shareholders' equity			
Share capital	3.20	2,132	2,132
Statutory and other reserves		1,150	1,150
Own treasury shares		(776)	(1,894)
Revaluation reserve for AFS securities	514	196	
Retained earnings		1,773	2,965
Total shareholders' equity		**4,793**	**4,549**
Total liabilities and shareholders' equity		**127,443**	**98,147**

The accompanying notes are an integral part of these financial statements.

These financial statements were prepared by the Bank and approved by the Board of Directors of the Bank on 26 March 2015.

Ing. Ladislav Macka
Chairman of the Board

Ing. Jan Ulip
Member of the Board

Statement of changes in equity

	Share capital	Statutory and other reserves	Own treasury shares	Revaluation reserve for AFS securities	Retained earnings	Total
	CZKm	CZKm	CZKm	CZKm	CZKm	CZKm
Balance at 1 January 2013	**2,132**	**1,150**	**(1,894)**	**345**	**3,322**	**5,055**
Profit for the period	-	-	-	-	343	343
Net fair value gains on AFS securities	-	-	-	(105)	-	(105)
Net gains on AFS securities transferred to income statement	-	-	-	(79)	-	(79)
Deferred income tax relating to components of other comprehensive income	-	-	-	35	-	35
Total comprehensive income	-	-	-	(149)	343	194
Dividends relating to 2012	-	-	-	-	(700)	(700)
Balance at 31 December 2013	**2,132**	**1,150**	**1,894)**	**196**	**2,965**	**4,549**
Profit for the period	-	-	-	-	256	256
Net fair value losses on AFS securities	-	-	-	341	-	341
Net gains on AFS securities transferred to income statement	-	-	-	52	-	52
Deferred income tax relating to components of other comprehensive income	-	-	-	(75)	-	(75)
Total comprehensive income	-	-	-	318	256	574
Dividends relating to 2013	-	-	737	-	(1,067)	(330)
Other changes			381	-	(381)	-
Balance at 31 December 2014	**2,132**	**1,150**	**(776)**	**514**	**1,773**	**4,793**

Statement of cash flows

	Note	2014 CZKm	2013 CZKm
Profit before income tax		345	516
Adjustments for non-cash transactions			
Loans impairment and write-offs and provisions for guarantees		309	371
Depreciation and amortisation		24	24
Share of profit of associates		-	(1)
Change in fair values and foreign exchange differences		(34)	(44)
Other non-cash items		35	5
Net interest income		(511)	(612)
Fee and commission income		(456)	(527)
		(288)	(268)
(Increase)/decrease in operating assets			
Loans and advances to banks		(21)	70
Loans and advances to customers		2,911	2,345
Other assets		317	1,515
Increase/(decrease) in operating liabilities			
Deposits from banks		(1,570)	561
Deposits from customers		30,434	(13,407)
Other liabilities		95	(67)
Interest received		987	1,265
Interest paid		(422)	(565)
Fee and commission received		243	246
Net cash flow from operating activities before income tax and payments under guarantee calls		32,686	(8,305)
Payments made under guarantee calls		(236)	(169)
Income taxes paid		(195)	(214)
Net cash flow from operating activities		**32,255**	**(8,688)**
Cash flows from investing activities			
Purchases of securities		(8,607)	(8,066)
Sales of securities and proceeds from matured securities		3,841	11,330
Purchase of tangible and intangible assets		(58)	(31)
Net cash flow from investing activities		**(4,824)**	**3,233**
Cash flows from financing activities			
Dividends paid		(330)	(700)
Net cash flow from financing activities		**(330)**	**(700)**
Net increase/ (decrease) in cash and cash equivalents		**27,101**	**(6,155)**
Cash and cash equivalents at the beginning of the year	**3.21**	**64,160**	**70,315**
Cash and cash equivalents at the end of the year	**3.21**	**91,261**	**64,160**

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Notes to the financial statements

Notes to the financial statements

1/ General information

Českomoravská záruční a rozvojová banka, akciová společnost (henceforth the "Bank" or "ČMZRB") was formed as a joint stock company pursuant to the Czech Commercial Code and was incorporated in 1992. The Bank's registered office is located at Jeruzalémská 964/4, Prague 1, Czech Republic. The Bank has five branches in the Czech Republic (in Brno, Hradec Králové, Ostrava, Plzeň and Prague) and one regional office in České Budějovice.

The Bank's activities are focused on supporting small and medium-sized businesses in the Czech Republic by providing preferential loans (Note 2 d), preferential guarantees (Note 2 j) and issuing infrastructure loans to municipalities and their legal associations, as well as water sector entities with municipal equity participations (Note 2 b). The Bank's loan portfolio includes also loans to the Ministry of Finance provided in connection with infrastructure programs (Note 3.11). The Bank also acts as an agent disbursing Czech government agency's funds as subsidy of interest costs to the block of flats' owners that meet specified criteria (Note 2 f). The purpose-bound funds are made available to Bank by the Czech state and international financial institutions. In some cases the Bank participates on program funding.

These financial statements include the Bank and its associated undertaking MUFIS a.s. (see Note 3.15) (together the "Group").

Using the Bank's own resources to finance support for SMEs in 2014

Taking into consideration the multi-annual halt of financing programs supporting small and medium entrepreneurship ("SME") from the resources of the Operating program Entrepreneurship and innovation, the Bank used, with the consent of the shareholders, its own resources in order to finance the guarantees for this sector as a part of the national guarantee program. In 2014 the total amount of CZK 566 million was used for this purpose (in 2013 the total of CZK 743 million was used with the impact to profit), by which the reported profit for 2014 is lower. This measure enabled to maintain the continuity of support of SME in 2014.

2/ Summary of significant accounting policies

(a) Basis of preparation

The financial statements are prepared in accordance with International Financial Reporting Standards as adopted by the European Union ('IFRS'). The financial statements comprise the income statement and statement of comprehensive income presented as two separate statements, the statement of financial position, the statement of changes in equity, the statement of cash flows and the notes.

The financial statements have been prepared under the historical cost convention, except for available-for-sale financial assets, financial assets held at fair value through profit or loss and all derivative contracts that have been measured at fair value.

The accompanying financial statements are based on the accounting records, together with appropriate adjustments and reclassifications necessary for fair presentation in accordance with IFRS.

The financial statements are presented in CZK, which is the Bank's functional and presentation currency. The figures shown in the financial statements are stated in CZK million.

Cash and cash equivalents in the statement of cash flows include highly liquid investments. Note 3.21 shows in which item of the statement of financial position cash and cash equivalents are included.

Notes to the financial statements

The cash flows from operating activities are determined by using the indirect method. Profit before tax in the statement of cash flows is therefore adjusted by non-cash items, such as measurement gains or losses, changes in provisions, as well as changes from receivables and liabilities. In addition, all income and expenses from cash transactions that are attributable to investing or financing activities are eliminated. Interest received or paid is classified as operating cash flows.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires management to exercise its judgment in the process of applying the Bank's accounting policies. Changes in assumptions may have a significant impact on the financial statements in the period the assumptions changed. Management believes that the underlying assumptions are appropriate and that the Bank's financial statements therefore present the financial position and results fairly. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed in Note 2 p.

New Standards, Amendments and Interpretations adopted since 1 January 2014

The following revised standards effective from 1 January 2014 are mandatory and relevant for the Company and have been applied by the Company since 1 January 2014.

IAS 27 (2011) Separate Financial Statements carries forward the existing accounting and disclosure requirements of IAS 27 (2008) for separate financial statements, with some minor clarifications. As well, the existing requirements of IAS 28 (2008) and IAS 31 for separate financial statements have been incorporated into IAS 27 (2011). The Standard no longer addresses the principle of control and requirements relating to the preparation of consolidated financial statements, which have been incorporated into IFRS 10 Consolidated Financial Statements.

IAS 28 (2011) Investments in Associates and Joint Ventures. This amended standard supersedes IAS 28 Investments in Associates (2008). IAS 28 (2011) makes the following amendments:

- FRS 5 applies to an investment, or a portion of an investment, in an associate or a joint venture that meets the criteria to be classified as held for sale; and
- on cessation of significant influence or joint control, even if an investment in an associate becomes an investment in a joint venture or vice versa, the entity does not remeasure the retained interest.

Amendments to IAS 32 Offsetting Financial Assets and Financial Liabilities. The amendments do not introduce new rules for offsetting financial assets and liabilities; rather they clarify the offsetting criteria to address inconsistencies in their application.

IFRS 10 Consolidated Financial Statements and IAS 27 (2011) Separate Financial Statements. IFRS 10 provides a single model to be applied in the control analysis for all investees, including entities that currently are SPEs in the scope of SIC-12. IFRS 10 introduces new requirements to assess control that are different from the existing requirements in IAS 27 (2008). Under the new single control model, an investor controls an investee when it is exposed or has rights to variable returns from its involvements with the investee, it has the ability to affect those returns through its power over that investee and there is a link between power and returns. The new Standard also includes the disclosure requirements and the requirements relating to the preparation of consolidated financial statements. These requirements are carried forward from IAS 27 (2008).

IFRS 11 Joint Arrangements supersedes and replaces IAS 31, Interest in Joint Ventures. IFRS 11 does not introduce substantive changes to the overall definition of an arrangement subject to joint control, although the definition of control, and therefore indirectly of joint control, has changed due to IFRS 10. Under the new Standard, joint arrangements are divided into two types, each having its own accounting model.

IFRS 12 Disclosure of Interests in Other Entities requires additional disclosures relating to significant judgments and assumptions made in determining the nature of interests in an entity or arrangement, interests in subsidiaries,

Notes to the financial statements

joint arrangements and associates and unconsolidated structured entities.

Amendments to IFRS 10, IFRS 12 and IAS 27 – Investment Entities. The Amendments provide an exception to the consolidation requirements in IFRS 10 and requires qualifying investment entities to measure their investments in controlled entities – as well as investments in associates and joint ventures – at fair value through profit or loss, rather than consolidating them.

The consolidation exemption is mandatory (i.e. not optional), with the only exception being that subsidiaries that are considered as an extension of the investment entity's investing activities, must still be consolidated.

An entity qualifies as an investment entity if it meets all of the essential elements of the definition of an investment entity. According to these essential elements an investment entity:

- obtains funds from investors to provide those investors with investment management services;
- commits to its investors that its business purpose is to invest for returns solely from appreciation and/or investment income; and
- measures and evaluates the performance of substantially all of its investments on a fair value basis.

The amendments also set out disclosure requirements for investment entities.

Amendments to IAS 36 – Recoverable Amount Disclosures for Non-Financial Assets. The Amendments clarify that recoverable amount should be disclosed only for individual assets (including goodwill) or cash-generated units for which an impairment loss was recognized or reversed during the period.

The Amendments also require the following additional disclosures when an impairment for individual assets (including goodwill) or cash-generated units has been recognized or reversed in the period and recoverable amount is based on fair value less costs to disposal:

- the level of IFRS 13 'Fair value hierarchy' within which the fair value measurement of the asset or cash-generating unit is categorized;
- for fair value measurements categorized within Level 2 and Level 3 of the fair value hierarchy, a description of the valuation techniques used and any changes in that valuation technique together with the reason for making it;
- for fair value measurements categorized within Level 2 and Level 3, each key assumption (i.e. assumptions to which recoverable amount is most sensitive) used in determining fair value less costs of disposal. If fair value less costs of disposal is measured using a present value technique, discount rate(s) used both in current and previous measurement should be disclosed.

Amendments to IAS 39 – Novation of Derivatives and Continuation of Hedge Accounting. The Amendments allows hedge accounting to continue in a situation where a derivative, which has been designated as a hedging instrument, is novated to effect clearing with a central counterparty as a result of laws and regulations, when the following criteria are met:

- The novation is made as a consequence of laws or regulations
- A clearing counterparty becomes a new counterparty to each of the original counterparties of the derivative instrument
- Changes to the terms of the derivative are limited to those necessary to replace the counterparty.

AS Standards, interpretations and amendments to published standards that are not yet effective and are relevant for the Company's financial statements

A number of new Standards, amendments to Standards and Interpretations are not yet effective as at 31 December 2014, and have not been applied in preparing these financial statements. Of these pronouncements, potentially

Notes to the financial statements

the following will have an impact on the Company's operations. The Company plans to adopt this pronouncement when it becomes effective. The Company is in the process of analyzing the likely impact on its financial statements.

Amendments to IAS 19 – Defined Benefit Plans: Employee Contributions (effective for annual periods beginning on or after 1 February 2015). Amendments to IAS 19 – Defined Benefit Plans: Employee Contributions Amendments to IAS 19 – Defined Benefit Plans: Employee ContributionsAmendments to IAS 19 – Defined Benefit Plans: Employee Contributions The amendments are relevant only to defined benefit plans that involve contributions from employees or third parties meeting certain criteria. Namely that they are:

- set out in the formal terms of the plan;
- linked to service; and
- independent of the number of years of service.

When these criteria are met, a company is permitted (but not required) to recognize them as a reduction of the service cost in the period in which the related service is rendered.

The entity does not expect the Amendment to have any material impact on the financial statements since it does have any defined benefit plans that involve contributions from employees or third parties.

IFRIC 21 Levies (effective for annual periods beginning on or after 17 June 2014). The Interpretation provides guidance as to the identification of the obligating event giving rise to a liability, and to the timing of recognizing a liability to pay a levy imposed by government.

In accordance with the Interpretation, the obligating event is the activity that triggers the payment of that levy, as identified in the relevant legislation and as a consequence, the liability for paying the levy is recognized when this event occurs.

The liability to pay a levy is recognized progressively if the obligating event occurs over a period of time.

If the obligating event is the reaching of a minimum activity threshold, the corresponding liability is recognized when that minimum activity threshold is reached.

The Interpretation sets out that an entity cannot have a constructive obligation to pay a levy that will be triggered by operating in a future period as a result of the entity being economically compelled to continue to operate in that future period.

It is expected that the Interpretation, when initially applied, will not have a material impact on the financial statements, since it does not results in a change in the entity's accounting policy regarding levies imposed by governments.

Annual Improvements to IFRSs 2010-2012 and 2011-2013 Cycles were issued by the IASB in December 2013 and introduce eleven amendments to nine standards and consequential amendments to other standards and interpretations that result in accounting changes for presentation, recognition or measurement purposes. The Annual Improvements to IFRSs 2010-2012 cycle of amendments are applicable to annual periods beginning on or after 1 February 2015, with earlier adoption permitted. The Annual Improvements to IFRSs 2011-2013 cycle of amendments are applicable to annual periods beginning on or after 1 January 2015, with earlier adoption permitted.

(b) Treatment of associated undertakings

Investments in associated undertakings are accounted for using the equity method of accounting and are initially recognized at cost. These are undertakings in which the Bank has between 20 percent and 50 percent of the voting

Notes to the financial statements

rights, and over which the Bank exercises significant influence. Significant influence is the power to participate in the financial and operating policy decisions of the investee but is not control or joint control over those policies. Equity accounting involves recognizing the Bank's share of the associate's profit or loss for the period in the profit or loss. The Bank's interest in the associate is carried in the statement of financial position at an amount that reflects its share of net assets of the associate.

For summarized financial information on the associate MUFIS a.s. accounted for using the equity method, see Note 3.15.

(c) Foreign Currencies

Foreign currency transactions that are transactions denominated, or that require settlement, in a foreign currency are translated into the functional currency using the exchange rates prevailing at the dates of the transactions (Czech National Bank official rate).

Monetary items denominated in foreign currency are translated with the closing rate as at the reporting date. Non-monetary items measured at historical cost denominated in a foreign currency are translated with the exchange rate as at the date of initial recognition; non-monetary items in a foreign currency that are measured at fair value are translated using the exchange rates at the date when the fair value was determined.

Foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at year-end exchange rates of monetary assets and liabilities are recognized in the income statement.

All foreign exchange gains and losses recognized in the income statement are presented net in the income statement within 'Income from financial operations' or 'Expense on financial operations'.

In the case of changes in the fair value of monetary assets denominated in foreign currency classified as available for sale, a distinction is made between translation differences resulting from changes in amortized cost of the security and other changes in the carrying amount of the security. Translation differences related to changes in the amortized cost are recognized in profit or loss, and other changes in the carrying amount, except impairment, are recognized in other comprehensive income.

(d) Financial assets and liabilities

In accordance with IAS 39, all financial assets and liabilities – which include derivative financial instruments – have to be recognized in the statement of financial position and measured in accordance with their assigned category.

Financial assets

The Bank allocates financial assets to the following IAS 39 categories: financial assets at fair value through profit or loss; loans and receivables; held-to-maturity investments; and available-for-sale financial assets. Management determines the classification of its financial instruments at initial recognition.

(a) Financial assets at fair value through profit or loss

This category comprises two sub-categories: financial assets classified as held for trading, and financial assets designated by the Bank at fair value through profit or loss upon initial recognition.

Notes to the financial statements

A financial asset is classified as held for trading if it is acquired or incurred principally for the purpose of selling or repurchasing it in the near term or if it is part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit-taking. Derivatives are also categorized as held for trading unless they are designated and effective as hedging instruments. Bank's financial assets held for trading consist of debt instruments. These financial assets are recognized in the statement of financial position as 'Financial assets held for trading'.

Financial instruments included in this category are recognized initially at fair value; transaction costs are taken directly to the income statement. Gains and losses arising from changes in fair value are included directly in the income statement and are reported as 'Income from financial operations' or 'Expense on financial operations'. Interest income on financial assets held for trading are included in 'Interest and similar income'. The instruments are derecognized when the rights to receive cash flows have expired or the Bank has transferred substantially all the risks and rewards of ownership and the transfer qualifies for derecognizing.

The Bank designates certain financial assets upon initial recognition at fair value through profit or loss (fair value option). This designation cannot subsequently be changed. According to IAS 39, the fair value option is only applied when the following conditions are met:

- the application of the fair value option reduces or eliminates an accounting mismatch that would otherwise arise or
- the financial assets are part of a portfolio of financial instruments which is risk managed and reported to senior management on a fair value basis, or
- the financial assets consists of debt host and an embedded derivative that must otherwise be separated.

To reduce accounting mismatch, the fair value option is applied to certain debt securities that are hedged with cross-currency interest rate swaps but for which the hedge accounting conditions of IAS 39 are not fulfilled. The aim is to recognize the changes in the fair value of the securities together with change in the fair value of the derivatives in the income statement.

Debt securities for which the fair value option is applied are recognized in the statement of financial position as 'Financial assets designated at fair value'. Fair value changes relating to financial assets designated at fair value through profit or loss are recognized in 'Gains and (losses) on securities – changes in fair value of the securities designated at fair value through profit or loss'.

(b) Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Bank includes in this category principally Loans originated by the Bank by providing money directly to a borrower.

Loans and receivables are initially recognized at fair value – which is the cash consideration to originate the loan including any transaction costs – and measured subsequently at amortized cost using the effective interest rate method. Loans and receivables are reported in the statement of financial position as loans and advances to banks or customers or as investment securities available for sale or held to maturity.

Interest on loans is included in the income statement and is reported as 'Interest and similar income'.

Preferential loans provided by the Bank

The Czech government and the Bank created various schemes to provide zero interest, low interest rate and subordinated loans to Czech enterprises that meet specified conditions (economic sectors supported by the Czech

Notes to the financial statements

government or the European Union). The Bank participates partially on the funding of these loans, however, recognizes the full amount due from final recipient on its statement of financial position in Loans and advances to customers. To compensate to the Bank for the below-market interest rate, the Bank receives from the funding partner the fees for managing the scheme, credit risk fee and the market interest rate agreed on a yearly basis for the Bank's share on funding. Overall amount of these fees is recognized as interest and similar income.

Based on the arrangements, the Bank is effectively able to transfer part of credit risk on these loans to the government (subject to certain limits). Such arrangements represent in substance a guarantee issued by the government. Once the loans are written-off due to credit quality deterioration in accordance with the Bank's rules, the funds deposited by the government for the provision of these loans (included in Amounts due to state institutions - see Note 3.18) are settled against these amounts. The financial guarantee received is not separately recognized as a receivable and is being effectively part of the funds provided by the government.

Following collection of the receivable or its settlement against the program funding when deemed uncollectible, the receivable is derecognized, the loss exceeding the contractually agreed portion of credit risk, if any, covered by the government in respect of loans with the program would be settled by the Bank.

(c) Held-to-maturity financial assets

Held-to-maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Bank's management has the positive intention and ability to hold to maturity, other than those that the Bank designates as available for sale and those that meet the definition of loans and receivables.

These financial assets are initially recognized at fair value including directly attributable and incremental transaction costs and measured subsequently at amortized cost, using the effective interest method.

Interest on held-to-maturity investments is included in the income statement and reported as 'Interest and similar income'. In the case of an impairment, the impairment loss is reported as a deduction from the carrying value of the investment and recognized in the income statement as 'Net gains/(losses) on financial operations'. No provisions on held-to-maturity investments had to be recognized either in 2014 or 2013.

(d) Available-for-sale financial assets

Available-for-sale investments are financial assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or that are not classified as loans and receivables, held-to-maturity investments or financial assets at fair value through profit or loss.

Available-for-sale financial assets are initially recognized at fair value plus transaction costs and measured subsequently at fair value with gains and losses being recognized in the statement of comprehensive income, except for impairment losses, until the financial asset is derecognized. If an available-for-sale financial asset is determined to be impaired, the cumulative gain or loss previously recognized in the statement of comprehensive income is recognized in the income statement.

However, interest calculated using the effective interest method, and foreign currency gains and losses on Bank's bonds classified as available for sale are recognized in the income statement.

(e) Recognition

The Bank uses settlement date accounting for regular way contracts when recording financial asset transactions. 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 recognized on the day of receipt of a financial instrument (sending of cash) and derecognized on the day of its provision (collection of cash). In case of a portfolio of financial assets measured at fair value, changes in the fair value of the financial assets are recognized from the purchase trade date to the sale trade date. Accrued interest on debt financial assets is recognized from the purchase settlement date to the sale settlement date.

All loans and receivables are recognized when funds are provided to customers. Loans and receivables are derecognized when fully repaid by the borrower or written-off.

The Bank settles and derecognizes financial liabilities at the date on which all related risks and costs attributable to the specific liability are transferred or settled.

Financial assets that are transferred to a third party but do not qualify for derecognition are presented in the statement of financial position as 'Assets pledged as collateral', if the transferee has the right to sell or repledge them.

Financial liabilities

The Bank's holding in financial liabilities is comprised by financial liabilities at fair value through profit or loss (financial liabilities held for trading, i.e. financial derivatives and short sales), financial liabilities at amortised cost and hedging derivatives.

(a) Financial liabilities at fair value through profit or loss

In the Bank's case, this category comprises only financial derivatives held for trading and short sales. The Bank recognizes its financial derivatives in the category held for trading unless they are designated and effective as hedging instruments. These instruments are recognized in the statement of financial position as 'Financial liabilities held for trading'.

Gains and losses arising from changes in fair value of financial liabilities classified as held for trading are included in the income statement and are reported as 'Net gains/(losses) on financial operations'.

(b) Other liabilities measured at amortised cost

Financial liabilities that are not classified as at fair value through profit or loss fall into this category and are measured at amortized cost. Financial liabilities measured at amortized cost are principally deposits and loans from banks or customers.

Determination of fair value

The best evidence of fair value are quoted prices in an active market. If the market for a financial instrument is not active, the entity establishes the fair value by using a valuation technique.

The objective of using a valuation technique is to establish what the transaction price would have been on the measurement date in an arm's length exchange motivated by normal business considerations.

Valuation techniques include using recent arm's length market transactions between knowledgeable, willing parties, if available, reference to the current fair value of another instrument that is substantially the same and discounted cash flow analysis.

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The chosen valuation technique makes maximum use of market inputs and relies as little as possible on entity-specific inputs. It incorporates all factors that market participants would consider in setting a price and is consistent with accepted economic methodologies for pricing financial instruments. Periodically, an entity calibrates the valuation technique and tests it for validity using prices from any observable current market transactions in the same instrument (i.e., without modification or repackaging) or based on any available observable market data.

For more complex instruments, the Bank uses developed valuation models, which are usually based on valuation methods and techniques generally recognized as standard within the industry. Valuation models are used primarily to value derivatives transacted in the over-the-counter market. All the inputs to these models are market observable. The fair value of over-the-counter (OTC) derivatives is determined using valuation methods that are commonly accepted in the financial markets, such as present value techniques and option pricing models. The fair value of foreign exchange forwards is generally based on current forward exchange rates.

For the categorization of the financial instruments carried at fair value see Note 5.

Derecognition

Financial assets are derecognized when the contractual rights to receive the cash flows from these assets have ceased to exist or the assets have been transferred and substantially all the risks and rewards of ownership of the assets are also transferred (that is, if substantially all the risks and rewards have not been transferred, the Bank tests control to ensure that continuing involvement on the basis of any retained powers of control does not prevent derecognition). Financial liabilities are derecognized when they have been redeemed or otherwise extinguished.

Collateral (bonds) furnished by the Bank under standard repurchase agreements and securities lending and borrowing transactions are not derecognized because the Bank retains substantially all the risks and rewards on the basis of the predetermined repurchase price, and the criteria for derecognition are therefore not met.

Reclassification of the financial assets

The Bank may choose to reclassify financial assets that would meet the definition of loans and receivables out of the held-for-trading or available-for-sale categories if the Bank has the intention and ability to hold these financial assets for the foreseeable future or until maturity at the date of reclassification. The Bank has not performed any of the reclassification or any type of other reclassifications between categories of the financial assets in 2014 or 2013.

(e) Offsetting financial instruments

Financial assets and liabilities are offset and the net amount reported in the statement of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

(f) Interest and fee income and expenses

Interest income and expense are recognized in the profit and loss account for all interest bearing instruments on an accruals basis using the effective interest rate. Loan origination fees are included in the effective interest rate and are therefore reported in ‘Interest income’. Other fees and commissions are recognized in the period to which they relate on an accruals basis. Interest income includes interest income for all fixed income instruments.

Notes to the financial statements

As part of its activities, the Bank acts as an agent disbursing government's funds as subsidy of interest costs of the loans provided by the Czech state agency to the debtors that meet specified criteria. Therefore, the grant is not recognized on the statement of financial position of the Bank. The Bank's services are: (i) it is a payment agent and (ii) the Bank processes paperwork, e.g. subsidy agreements on behalf of the government. The Bank obtains remuneration for the services provided of the agreed percentage of funds disbursed. This remuneration from the government partner is recognized as earned as it is calculated on annual basis based on the agreed contract with the provider of the assistance.

(g) Impairment of financial assets

(a) Assets carried at amortised cost

The Bank assesses at each reporting date whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The Bank regularly assesses its loan portfolio for impairment. As part of this analysis, the Bank splits all loans into two categories: non-performing loans, i.e., a larger than insignificant part of the principal and interest is past due for more than 90 days, and performing loans. If there is any objective evidence that a loan may be impaired (deterioration of a debtor's financial health, payment default, etc), the amortized cost of the loan is reduced through a provision to its estimated recoverable value. The recognition, use and release of provisions are accounted for on a monthly basis always by reference to the loan balances at the month-end. The provision is reduced if objective reasons for loan impairment cease to exist. In such cases, the original amount is reversed and a required provision is released. Provisions are used when loans are sold or written off. Provisions are released to income when the reasons for maintaining the provision cease to exist (for example, when the loan is repaid).

The Bank makes an estimate of realized losses on an individual basis for individually significant loans and on a portfolio basis for individually insignificant loans by reference to historical experience.

Management of the Bank uses estimates based on historical experience of losses on loans that have similar risk characteristics (that is, on the basis of the Bank's grading process that considers asset type, industry, geographical location, collateral type, past-due status and other relevant factors). Those characteristics are relevant to the estimation of future cash flows for groups of such assets by being indicative of the debtors' ability to pay all amounts due according to the contractual terms of the assets being evaluated. The methods and assumptions adopted in estimating amounts and the timing of future cash flows are regularly reviewed to reduce differences between the estimated and actual data.

The Bank writes off loss loans when it can be reasonably anticipated that clients will be unable to fulfil their obligations to the Bank in respect of these loans. Subsequent recoveries are credited to the income statement in the line 'Decrease/ increase in loan impairment and write-offs'.

For further information on credit risk refer to Note 4.1.

(b) Available for sale financial assets

The Bank performs regular assessments to determine whether available for sale financial assets suffered impairment. When a decline in the fair value of an available-for-sale financial asset has been recognized in other comprehensive income and there is objective evidence that the asset is impaired, the carrying amount of the impaired security is decreased directly and at the same time the cumulative loss that had been recognized

Notes to the financial statements

in other comprehensive income is reclassified from equity to profit or loss line 'Net gains/ (losses) on financial operations' as a reclassification adjustment even though the financial asset has not been derecognized. The amount of this loss reflects the difference between the cost (less the repayments of principal and amortization, if any) and the current fair value, reflecting previous impairment losses recognized in expenses.

(h) Sale and repurchase agreements

Securities sold subject to repurchase agreements ('repos') are reclassified in the financial statements as pledged assets when the transferee has the right by contract or custom to sell or repledge the collateral; the counterparty liability is included in Due to banks or Due to customers, as appropriate.

Securities purchased under agreements to resell ('reverse repos') are recorded as loans and advances to other banks or customers, as appropriate. The difference between sale and repurchase price is treated as interest and accrued over the life of the agreements using the effective interest method.

(i) Derivative financial instruments and hedging

In the normal course of business, the Bank enters into contracts for derivative financial instruments which represent a financial instrument that requires none or a very low initial investment. The derivative financial instruments used include interest rate and currency forwards and swaps. These financial instruments are held by the Bank in order to hedge interest rate risk and currency exposures associated with its transactions.

Derivative financial instruments are initially recognized at fair value and are subsequently remeasured to their fair value. Fair values are obtained from the discounted cash flow models. All derivatives are carried as assets when fair value is positive and as liabilities when fair value is negative.

On the date a derivative contract is entered into, the Bank designates certain derivatives as an accounting hedge of the fair value of a recognized asset or liability (fair value hedge). Hedge accounting is used for derivatives and the hedged items designated in this way provided that certain criteria are met.

The Bank's criteria for a derivative instrument to be accounted for as an accounting hedge include:

(a) They meet the Bank's risk management strategy,
(b) At the inception of the hedge, the hedging relationship is formally documented, the documentation identifies the hedged item and the hedging instrument, defines the risk that is being hedged and the approach to establishing and documenting whether the hedge is effective, and
(c) The hedge is effective, that is, if, at inception and throughout the period, changes in the fair value of the hedged item are almost fully offset by changes in the fair value of the hedging instrument and the results are within a range of 80 percent to 125 percent.

Changes in the fair value of derivatives that are designated and qualify as fair value hedges and that prove to be highly effective in relation to the hedged risk are recorded in profit or loss along with the corresponding change in fair value of the hedged asset or liability that is attributable to the specific hedged risk. The ineffective element of the hedge is charged directly to profit or loss in line 'Income from financial operations' or 'Expense on financial operations'.

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognized immediately in the income statement under 'Income from financial operations' or 'Expense on financial operations'.

Notes to the financial statements

Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the income statement under 'Income from financial operations' or 'Expense on financial operations'.

(j) Provisions and financial guarantees obligations

Provisions for legal claims are recognized when the Bank has a present legal obligation as a result of past events, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate of the amount of the obligation can be made.

Provisions are measured at the present value of the expenditures expected to be required to settle the obligation using a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the obligation. The increase in the provision due to passage of time is recognized as interest expense.

Financial guarantee contracts

Financial guarantee contracts are contracts that require the issuer to make specified payments to reimburse the holder for a loss it incurs because a specified debtor fails to make payments when due, in accordance with the terms of a debt instrument.

Bank provides two main types of financial guarantees:

- the financial guarantees to the small and medium enterprises in various preferential guarantee programs in cooperation with the Czech state, and
- the financial guarantees in PANEL program launched by the State Fund of Housing Development ("SFRB") in support of reconstruction and refurbishment of specific block of flats with the aim to improve their quality and lifetime.

Under the agreements concluded between the Bank and the Czech state or the Bank and SFRB, the Bank issues preferential financial guarantees for loans provided by third party banks. The difference between the full market price of the guarantee and the fee paid by client is funded by the Czech state (intermediating in some cases the programs of the European Union) or by SFRB. The Bank immediately deducts such support funded by the Czech state whole in advance from the customer's bank account as its fee for the issued financial guarantee and these fees received are recognized in the income statement over the life of the guarantee. The terms and conditions of the financial guarantee contracts with related parties are described in Note 3.24.

In addition, the government refunds to the Bank losses on financial guarantees issued under the schemes up to the amount agreed in the contract between the Bank and the Czech state. For these purposes the amounts are deposited within special bank account for each guarantee provided and recognized as Amounts due to state institutions (see Note 3.18).

Financial guarantees are initially recognized in the financial statements at fair value on the date the guarantee was given. The fair value of a financial guarantee at the time of signature is zero because all guarantees are agreed on arm's length terms and the value of the premium agreed corresponds to the value of the guarantee obligation. No receivable for future premiums is recognized. Subsequent to initial recognition, the Bank's liabilities under such guarantees are measured at the higher of the initial amount, less amortization of fees recognized in accordance with IAS 18, and the best estimate of the amount required to settle the guarantee (i.e. the amount determined in accordance with IAS 37 Provisions, Contingent liabilities and Contingent assets). Provisions for guarantees are made for estimated losses above the amounts deposited by the Czech state. These estimates are determined based on experience of similar transactions and history of past losses, supplemented by the judgment of the Bank's management. Risk category method applied by the Bank is considering the likelihood that

Notes to the financial statements

an outflow will be required in settlement by considering the class of obligations (i.e. those arising from a certain type of the financial guarantees) as a whole. A provision is therefore recognized even if the likelihood of an outflow with respect to any specific item included in the same class of obligations may be small.

(k) Property, plant and equipment and intangible assets

Tangible and intangible assets are stated at historical cost less the accumulated depreciation and accumulated impairment losses. Fixed assets are depreciated through the accumulated depreciation charge. Depreciation is calculated on a straight line basis in order to write off the cost of each asset to their residual value over its estimated useful economic life. Assets in the course of construction are not depreciated.

The estimated useful economic lives are set out below:

Machinery and equipment, computers, vehicles, software	4 years
Fixtures, fittings and equipment	10 years
Buildings and structures	30 years

The Bank periodically tests its assets for impairment. Where the carrying amount of an asset is greater than its estimated recoverable amount, it is written down to its recoverable amount. Where assets are identified as being surplus to the Bank's requirements, management of the Bank determines a provision for asset impairment. In respect of the assets owned by the Bank, the provision is assessed by reference to a fair value based on third party valuation reports adjusted downwards for an estimate of associated sale costs.

Repairs and renewals are charged directly to the income statement when the expenditure is incurred.

(l) Employee benefits

The Bank governs through internal guidelines provision of employee benefits. Some benefits are provided regularly to all employees (e.g. additional pension insurance); others are provided in relation to the actual need of an employee (e.g. loans).

Contributions are made to the government's retirement benefit scheme at the statutory rates in force during the year based on gross salary payments. The cost of social security payments is charged to the income statement in the same period as the related salary cost.

(m) Current and deferred income tax

Tax is calculated in accordance with the provisions of the relevant legislation of the Czech Republic based on the profit determined in accordance with the Czech Accounting Standards.

Deferred tax is provided using the statement of financial position liability method for temporary differences arising between the tax bases of assets and liabilities and their carrying values for financial reporting purposes. Deferred income tax is determined using tax rates effective in the periods in which the temporary tax difference is expected to be realized. The principal temporary differences arise from specific allowances for loan losses and provisions for the guarantees and unrealized gains and losses from available for sale financial assets. Deferred tax assets in respect of tax losses carried forward and other temporary differences are recognized to the extent that it is probable that future taxable profit will be available against which the tax assets can be utilized.

Notes to the financial statements

Current and deferred tax are recognized as an expense or income in the income statement, except for the deferred tax effects related to fair value re-measurement of available-for-sale investments. As the fair value re-measurement is recognized in other comprehensive income, deferred tax is also recognized in the other comprehensive income and subsequently reclassified to the income statement together with the gain or loss on derecognition.

(n) Share capital

Shares are classified as equity when there is no contractual obligation to transfer cash or other financial assets. Own shares held by the Bank are recognized as a deduction in equity until they are cancelled or resold. When such shares are subsequently sold, reissued or otherwise disposed of, any consideration received is included in equity.

Dividends on ordinary shares are recognized in equity in the period in which they are approved by the Bank's general meeting of shareholders. Dividends for the year that are proposed or declared after the Statement of financial position date are disclosed in the subsequent events note.

(o) Subsequent Events

The effects of events which occurred between the statement of financial position date and the date when the financial statements were authorized for issue are reflected in the financial statements in the event that these events provide further evidence of conditions which existed at the Statement of financial position date.

Where significant events occur subsequent to the statement of financial position date prior to authorizing the financial statements for issue which are indicative of conditions which arose subsequent to the Statement of financial position date, the effects of these events are disclosed but do not result in adjustments in the financial statements.

(p) Key Bank's management judgments and estimates

The presentation of financial statements in conformity with IFRS requires management of the Bank to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities as of the reporting date and the reported amounts of revenues and expenses during the reporting period. These estimates, which specifically relate to the impairment of financial assets and provisions arising from the provided financial guarantees, are based on the information available as of the date of preparation of the financial statements and actual results could differ from those estimates.

Impairment losses on loans to customers and provisions for financial guarantees

Management uses estimates based on historical loss experience for assets and financial guarantees with credit risk characteristics similar to those in the portfolio when scheduling its future cash flows. The methodology and assumptions used for estimating both the amount and timing of future cash flows are reviewed regularly to reduce any differences between loss estimates and actual loss experience. Should the estimated percentages of the impairment provisions divert from the current management estimate by +/-1%, the impairment loss is to be estimated CZK 58 million higher/lower.

Notes to the financial statements

3/ Additional information to statement of financial position and income statement items

3.1. Interest income

CZKm	2014	2013
Interest income on loans and advances to banks	14	15
Interest income on loans and advances to customers	269	355
Interest on loans granted to the government institutions	299	331
Interest on debt securities	412	501
- held for trading	3	4
- designated at fair value through profit or loss	46	61
- available for sale	202	259
- held to maturity	161	177
Interest income	**994**	**1,202**
Interest on amounts due to banks	(296)	(338)
Interest on deposits due to customers	(17)	(22)
Interest on deposits from government institutions	(97)	(159)
Interest from unwinding discounts on provisions (Note 3.6)	(73)	(71)
Interest expenses	**(483)**	**(590)**
Net interest income	**511**	**612**

Interest income includes CZK 238 million (2013: CZK 287 million) of interest income on impaired financial assets.

3.2. Fee and commission income

CZKm	2014	2013
Fees from financial guarantees	386	453
Credit related fees and commissions	35	37
Fees and commissions from payment transactions	35	37
Fee and commission income	**456**	**527**
Fee and commission expense from trading activities	(4)	(4)
Fee and commission expense	**(4)**	**(4)**
Net fee and commission income	**452**	**523**

3.3. Gains and losses from financial operations

CZKm	2014	2013
Gains and (losses) on securities	80	55
- available for sale	52	79
- amounts reclassified from other comprehensive income on disposal	52	79
- changes in fair value of securities held for trading	31	7
- changes in fair value of securities designated at fair value through profit or loss	(3)	(33)
- gain from revaluation of short sales	-	2
Net gains/ (losses) on derivatives held for trading	(72)	108
Net gains/ (losses) on hedging derivatives	5	33
Exchange differences (including exchange differences on available for sale and held to maturity debt securities)	17	(115)
Total income and expenses on financial operations	**30**	**81**

Net gains/ (losses) on hedging derivatives are due to high hedge accounting effectiveness almost fully compensated in the income statement in lines “Exchange differences“ in case of the foreign currency risk hedging

Notes to the financial statements

and in “Interest income“ and “Interest expense“ in case of interest rate risk hedging. The overall accounting hedge ineffectiveness amounts to CZK 1 million in 2014 (2013: CZK 1 million).

3.4. Administrative expenses

CZKm	2014	2013
Wages, salaries and bonuses	(174)	(169)
Social security costs	(51)	(49)
of which: state pension scheme contributions	(34)	(34)
Total personnel expenses	**(225)**	**(218)**
General administrative expenses	(113)	(111)
Total administrative expenses	**(338)**	**(329)**

Wages, salaries and key management compensations:

CZKm	2014	2013
Wages and salaries of the Bank’s employees	(110)	(110)
Key management personnel compensation	(47)	(43)
- wages and salaries of the Bank’s management	(27)	(37)
- compensations to Board of Directors members	(18)	(4)
- compensations to Supervisory Board members	(1)	(1)
- compensation to Audit Committee members	(1)	(1)
Other employees' expenses	(10)	(9)
Social fund expenditures	(7)	(7)
Total wages, salaries and bonuses	**(174)**	**(169)**

Staff Analysis

	2014	2013
Number of members of the Board of Directors	5	5
Number of members of the Supervisory Board	9	9
Number of members of the Audit Committee	3	4
Average number of the Bank’s management	17	22
Average number of Bank’s employees (excl. above listed)	194	194

Other administrative expenses comprise:

CZKm	2014	2013
General administrative expenses	(71)	(69)
Rental charges	(12)	(11)
Audit, legal, tax and other professional services	(6)	(7)
Depreciation and amortization	(24)	(24)
Total other administrative expenses	**(113)**	**(111)**

Notes to the financial statements

3.5. Increase in loan impairment and write-offs

Overall charge for the loan impairment can be analyzed as follows:

31 December 2014

CZKm	Loans to private legal entities and individuals	Loans to municipalities	Total
Additions/Disposals to loan impairment allowances	(6)	39	33
Receivables written-off during the year not fully provided for	-	-	-
Additions to allowances to other assets	(1)	-	(1)
Total increase in loan impairment allowances and write-offs	**(7)**	**39**	**32**

31 December 2013

CZKm	Loans to private legal entities and individuals	Loans to municipalities	Total
Additions/Disposals to loan impairment allowances	(341)	66	(275)
Receivables written-off during the year not fully provided for	(14)	-	(14)
Total increase in loan impairment allowances and write-offs	**(355)**	**66**	**(289)**

Reconciliation of the allowance account for impairment:

Year ended 31 December 2014

CZKm	Loans to private legal entities and individuals	Loans to municipalities	Total
Balance at 1 January 2014	**1,811**	**146**	**1,957**
Additions/Disposals to impairment allowances	6	(39)	(33)
Use of the allowances for write-offs	(46)	-	(46)
Balance at 31 December 2014	**1,771**	**107**	**1,878**

Year ended 31 December 2013

CZKm	Loans to private legal entities and individuals	Loans to municipalities	Total
Balance at 1 January 2013	**1,570**	**212**	**1,782**
Additions/Disposals to impairment allowances	341	(66)	275
Use of the allowances for write-offs	(100)	-	(100)
Balance at 31 December 2013	**1,811**	**146**	**1,957**

3.6. Provisions for guarantees and other provisions

The balance of provisions for guarantees and other provisions comprises:

CZKm	31 December 2014	31 December 2013
Provisions for guarantees (Note 3.22)	2,457	2,302
Provisions for loan commitments (Note 3.22)	27	56
Other provisions	425	137
Total provisions	**2,909**	**2,495**

Reconciliation of the provisions for guarantees and other provisions:

CZKm	2014	2013
Balance at 1 January	2,495	2,342
Increase/(decrease) in provisions for guarantees and loan commitments	341	82
Interest expense from unwinding discounts (Note 3.1)	73	71
Balance at 31 December	**2,909**	**2,495**

Notes to the financial statements

3.7. Income taxes

CZKm	2014	2013
Profit before income tax	345	516
Theoretical tax calculated at a statutory income tax rate 2014: 19% (2013: 19%)	66	98
Non-taxable income from securities –permanent difference	(5)	(6)
Effect of non-recognized contingent deferred tax asset	24	76
Other permanent items	2	3
Income tax expense as reported in income statement	89	173
- current	146	172
- deferred	(57)	1
Income tax paid during the year	195	214
Current income tax assets at 31 December	49	42
Current income tax liabilities at 31 December	-	-
Effective tax rate	**26%**	**34%**

Deferred taxation

The recognized deferred tax can be analysed as follows:

CZKm	31 December 2014	31 December 2013
Other provisions	88	31
Deferred tax recognized in other comprehensive income for revaluation of available for sale securities	(121)	(46)
Total deferred tax	**(33)**	**(15)**

CZKm	31 December 2014	31 December 2013
Deferred tax reported in the statement of financial position		
- to be recovered after more than 12 months	81	26
- to be recovered within 12 months	7	5
Deferred tax recognized in other comprehensive income for revaluation of available for sale securities		
- to be recovered within 12 months	(121)	(46)
Total deferred tax	**(33)**	**(15)**

Potential deferred tax asset of CZK 269 million as at 31 December 2014 (2013: CZK 245 million) arising from differences between accounting and tax values of impairment allowances and provisions has not been recognized as it is not probable that this difference will become tax deductible in the foreseeable future.

CZKm	2014	2013
Deferred tax balance at 1 January	(15)	(49)
Movement through income statement	57	(1)
Movement in deferred tax recognized in other comprehensive income for revaluation of available for sale securities	(75)	35
Deferred tax balance at 31 December	**(33)**	**(15)**

The deferred tax is calculated at the statutory income tax rate of 19% (31 December 2013: 19%), which is a statutory income tax rate enacted for the period, when the Bank anticipates realising the temporary differences.

Notes to the financial statements

3.8. Cash and balances with central banks

CZKm	31 December 2014	31 December 2013
Obligatory minimum reserves	347	400
Cash in hand	7	8
Amounts due under reverse repo transactions	90,880	63,744
Total cash in hand and balances with central banks	**91,234**	**64,152**

Obligatory minimum reserves represent mandatory deposits with the Czech National Bank.

3.9. Loans and advances to banks

CZKm	31 December 2014	31 December 2013
Current accounts with other banks	27	8
Included in cash and cash equivalents (Note 3.21.)	27	8
Other amounts due from banks	153	132
Total loans and advances to banks	**180**	**140**

All the amounts due from banks are unimpaired exposures before due date and no provisions are recognized. As the majority of the balances are collateralized exposures with local Czech banks under reverse repo transactions, the credit quality of the balances is not further analyzed in these financial statements.

3.10. Securities at fair value through profit or loss

CZKm	31 December 2014	31 December 2013
Government bonds – domestic	415	271
Government bonds – foreign	-	-
Securities held for trading	415	271
Government bonds – domestic	359	469
Government bonds – foreign	349	557
Bonds issued by Czech financial institutions	266	380
Bonds issued by other Czech entities	117	121
Securities designated at fair value through profit or loss	1,091	1,527
Total securities at fair value through profit or loss	**1,506**	**1,798**

3.11. Loans and advances to customers

CZKm	31 December 2014	31 December 2013
Loans to private legal entities and individuals	5,040	6,036
Loans to the Ministry of Finance of the Czech Republic and other government entities	7,693	9,311
Loans to municipalities	735	841
Gross amounts due from customers	**13,468**	**16,188**
Provisions for loans to customers (Note 3.5)	(1,878)	(1,957)
Net amounts due from customers	**11,590**	**14,231**

Loans to the Ministry of Finance represent principally the loans provided in connection with infrastructure programs which were transferred to the Bank from Konsolidační banka Praha in 2000. These programs are principally targeted at funding the construction of the highway network, repairs of international roads, removal of flood damage and water sector investments. The funding of these programs was provided by the European Investment Bank (Note 3.17) and is denominated also in EUR.

Notes to the financial statements

Set out below is the currency structure of the outstanding infrastructure loan principal amounts on the side of assets and liabilities (Note 3.17):

	31 December 2014		31 December 2013	
	Assets	Liabilities	Assets	Liabilities
	CZKm	CZKm	CZKm	CZKm
CZK – principal	3,344	3,344	4,114	4,114
CZK – accrued interest	1	1	1	1
EUR – principal	4,292	4,292	5,128	5,128
EUR – accrued interest	56	56	68	68
Total	**7,693**	**7,693**	**9,311**	**9,311**

The disclosures per classes of the loans and advances to customers are made in the credit risk section in Note 4.1 and reconciliation of changes in the allowance account during the period for each class of the loans and advances to customers is disclosed in Note 3.5..

3.12. Financial assets available for sale

Available for sale ("AFS") securities comprise debt securities as follows:

CZKm	31 December 2014	31 December 2013
Fixed income debt securities	6,663	4,447
Variable yield debt securities	9,947	7,790
Total debt securities available for sale	**16,610**	**12,237**

All AFS securities as at 31 December 2014 and 2013 were publicly traded on stock exchanges. They are denominated in various currencies and the currency risk is hedged (see Note 4.3).

AFS securities of CZK 8,550 million (2013: CZK 5,650 million) were pledged as collateral to third parties in sale and repurchase agreements to provide security over the money borrowed. These assets have been reclassified as pledged assets on the face of the statement of financial position as the borrower possessing the collateral has the right to re-pledge it or sell, however also has an obligation to return it.

AFS securities have been issued by the following issuers:

CZKm	31 December 2014	31 December 2013
- Czech state institutions	13,508	9,252
- Czech local government institutions	526	478
- Czech financial institutions	1,501	2,132
- Other Czech entities	183	58
- Foreign state institutions	67	68
- Foreign financial institutions	807	249
- Other foreign entities	18	-
Total debt securities available for sale	**16,610**	**12,237**

3.13. Financial assets held to maturity

Held to maturity ("HTM") securities have been issued by the following issuers:

CZKm	31 December 2014	31 December 2013
Czech state institutions	5,760	5,020
Total debt securities held to maturity	**5,760**	**5,020**

Notes to the financial statements

HTM securities are denominated in various currencies (see also Note 4.3). HTM securities comprise only securities generating fixed income.

HTM securities of CZK 1,546 million (2013: CZK 1,110 million) were pledged as collateral to third parties in sale and repurchase agreements to provide security over the money borrowed. These assets have been reclassified as pledged assets on the face of the statement of financial position as the borrower possessing the collateral has the right to re-pledge it or sell, however also has an obligation to return it.

3.14. Other assets

CZKm	31 December 2014	31 December 2013
Financial assets		
Accrued income	45	54
Non-financial assets		
Prepaid expenses	11	9
Other	23	21
Total other assets, gross	79	84
Impairment provisions (Note 3.5)	(8)	(7)
Total other assets, net	**71**	**77**

3.15. Investments in associate

The financial statements include an at equity measured investment in associate, MUFIS a.s., with its registered office address at Jeruzalémská 4, Prague 1 (‘MUFIS’), key details of which are set out below.

The Bank formed MUFIS, with share capital of CZK 1 million in 1994. In 1995, the Bank disposed of 51 percent of the issued share capital, and holds a 49 percent investment in MUFIS at 31 December 2014 and 2013. In 2014, the share capital was increased to CZK 2 million.

Shareholders’ structure	31 December 2014	31 December 2013
ČMZRB	49%	49%
Ministry of Finance	49%	49%
Association of Czech Municipalities	2%	2%

The Bank signed on 27 August 2009 with MUFIS an agreement on cooperation within the area of financing infrastructure projects for municipalities in the Czech Republic. MUFIS is currently involved in providing loans to municipalities and clusters of municipalities through the Joint credit fund created along with ČMZRB.

Summary financial information in CZKm	Equity	The Bank’s share on equity	Total assets	Profit after tax	The Bank’s share on profit
At 31 December 2014 and for the year then ended	216	106	216	0,5	0,2
At 31 December 2013 and for the year then ended	215	105	216	2,9	1,4

Notes to the financial statements

3.16. Property, plant and equipmen

CZKm	Land	Buildings	Equipment and fittings	Total
At 1 January 2013				
Acquisition cost	10	304	138	452
Accumulated depreciation	-	(173)	(132)	(305)
Net book value	**10**	**131**	**6**	**147**
Year ended 31 December 2013				
Opening net book value	10	131	6	147
Additions	-	-	4	4
Disposals	-	-	-	-
Depreciation charge	-	(10)	(3)	(13)
Closing net book value	**10**	**121**	**7**	**138**
At 31 December 2013				
Acquisition cost	10	304	123	437
Accumulated depreciation	-	(183)	(116)	299
Net book value	**10**	**121**	**7**	**138**
Year ended 31 December 2014				
Opening net book value	10	121	7	138
Additions	-	4	19	23
Disposals	-	-	(13)	(13)
Depreciation charge	-	(9)	(4)	(13)
Closing net book value	**10**	**116**	**9**	**135**
At 31 December 2014				
Acquisition cost	10	308	126	444
Accumulated depreciation	-	(192)	(117)	(309)
Net book value	**10**	**116**	**9**	**135**

3.17. Deposits from bank

CZKm	31 December 2014	31 December 2013
Due to other banks	13,715	13,863
Received term deposits from other banks	600	2,035
Amounts due to banks	**14,315**	**15,898**

Amounts due to other banks include principally the payables to the development banks (European Investment Bank, Kreditanstalt für Wiederaufbau, Nordic Investment Bank and Council of Europe Bank) of CZK 9,850 million at 31 December 2014 (31 December 2013: CZK 11,826 million), majority of which represents a funding for infrastructure loans described in Note 3.11.

Notes to the financial statements

3.18. Deposits from customers

Amounts due to customers, by type of deposit, comprise:

CZKm	31 December 2014	31 December 2013
Current accounts	4,932	5,371
Term deposits	25,047	8,784
Repo operations with the Ministry of Finance	71,296	56,582
Guarantee deposits	714	559
Other payables to clients	1,963	2,220
Total	**103,952**	**73,516**

Amounts due to customers, by type of customer, comprise:

CZKm	31 December 2014	31 December 2013
Amounts due to state institutions	99,280	69,990
Amounts due to municipalities	60	62
Amounts due to other customers	4,612	3,464
Total amounts due to customers	**103,952**	**73,516**

The 'Amounts due to state institutions' line includes, inter alia, payables comprising funding and funds to cover risks attached to the guarantee support programs provided by the Bank (Note 2 d and 2 j):

CZKm	31 December 2014	31 December 2013
Funding from the providers of the individual support programs not yet returned	2,597	2,720
Funds deposited by the program partners to cover risks attached to providing the financial guarantees	2,341	2,557

3.19. Other liabilities

CZKm	31 December 2014	31 December 2013
Payable to employees	33	45
Deferred income	886	1,100
- financial guarantees premium deferred income	861	1,071
- other deferred income	25	29
Accrued expenses (financial liability)	36	28
Amount payable to Ministry for Regional Development in respect to intermediation of the support program (financial liability)	201	210
Other	23	32
Total accruals and other liabilities	**1,179**	**1,415**

3.20. Equity and profit allocation

Share capital

	31 December 2014	31 December 2013
8,900 shares with a nominal value of CZK 239,500	2,132	2,132

The shares are registered and issued in book-entry form. All issued shares are fully paid.

Shares owned by the Czech Republic are recorded by Central Securities Depository Prague on asset accounts of Ministry of Industry and Trade, Ministry of Regional Development and Ministry of Finance.

Notes to the financial statements

The Bank's Shareholders as of 31 December 2014 and 2013 can by analyzed as follows:

	2014	2013
Shareholder	%	%
Czech Republic	85.809	72.330
Českomoravská záruční a rozvojová banka, a.s. *)	14.191	27.670
Total	**100.000**	**100.000**

*) According to paragraph 309 clause 1 of the Business Corporations Act („Zákon o obchodních korporacích“) the Bank does not have any voting rights related to its own treasury shares.

Evidence of the Czech state's shares by Central Securities Depository Prague on Ministries' asset accounts

	2014	2013
	%	%
Ministry of Industry and Trade	28.764	24.250
Ministry of Regional Development	28.764	24.250
Ministry of Finance	28.281	23.830
Total	**85.809**	**72.330**

Own treasury shares

Acquired own shares are recognized at cost and presented in a separate line within equity. Own treasury shares were acquired for market price of CZK 1,893,740,000, which was determined by sworn expert.

There was a change in the market value of Bank's shares in connection with the payment of a non-financial dividend in the form of own treasury shares. New market value in the amount of CZK 1,513,139,000 was determined by expert opinion. The movement of this valuation is presented under "Other changes" in the Statement of changes in equity.

Dividends

The General Meeting of the Bank decided to distribute dividend in the amount of CZK 456 million (of which CZK 341 million was distributed from the 2013's net profit and CZK 115 million from retained earnings), of which CZK 126 million was assigned to Bank s own treasury shares. According to paragraph 309 clause 2 of the Business Corporations Act („Zákon o obchodních korporacích“) the right to dividend associated with own treasury shares expires with its due date. In accordance with this Act, the Bank transferred unpaid dividend to retained earnings.

The General Meeting also decided to pay a non-financial dividend in the form of own treasury shares. In 2014, the Bank paid out 1,200 own treasury shares in total value of CZK 737 million.

Profit Allocation

The statutory net profit of the Bank as recognized in accordance with Czech accounting standards for the year ended 31 December 2014 is proposed to be allocated and net profit for 2013 of the Bank was allocated as follows:

CZKm	**2014**	**2013**
Allocated to retained earnings	-	-
Dividend *)	276	456
Change in retained earnings *)	(20)	(113)
Net profit per statutory financial statements	**256**	**343**

Notes to the financial statements

*) from the planned amount of dividend for 2014 the amount of CZK 39 million (in 2013: CZK 126 million) relates to shares held by the Bank. The right to dividend payment expires according to § 309 paragraph 2 of the Corporations Law („Zákon o obchodních korporacích“) on their due date. The actual impact on retained earnings is thus CZK 19 million (in 2013: CZK 12 million).

Following the decision of the general meeting of the Bank, dividends payable to the Ministry of Industry and Trade, Ministry for Regional Development and Ministry of Finance from the 2013's net profit in the total amount of CZK 330 million were paid on 15 July 2014 (Ministry of Finance) and 18 July 2014 (Ministry of Industry and Trade and Ministry for Regional Development) with amount CZK 51,282 per one share. The amount of dividends attributable to own treasury shares held by the Bank were transferred to retained earnings on 15 July 2014.

Revaluation reserve

The revaluation reserve shows the effects from the fair value measurement of available for sale securities after deduction of deferred taxes. No gains or losses other than foreign exchange are recognized in the income statement until the asset has been disposed or impaired.

Retained earnings and statutory and other reserves

Retained earnings consist of undistributed profits from previous years. Statutory reserve consists of CZK 800 million provided by the Czech State, which has to be set aside in accordance with national law and internally allocated revenue reserve of CZK 350 million.

3.21. Cash and cash equivalents

CZKm	31 December 2014	31 December 2013
Cash and balances with central banks (Note 3.8.)	91,234	64,152
Loans and advances to banks (Note 3.9.)	27	8
Total	**91,261**	**64,160**

Cash and cash equivalents comprise balances with less than three months' original maturity, including cash in hand, deposits held at call with banks and other short-term highly liquid investments.

3.22. Financial guarantees and loan commitments

Commitments to extend loans and financial guarantees for loans to third parties expose the Bank to credit risk and loss in the event that the client fails to comply with contractual conditions.

CZKm	31 December 2014	31 December 2013
Total issued financial guarantees	17,900	18,129
Loan commitments issued to clients	1,428	1,219
Total financial guarantees and loan commitments	**19,328**	**19,348**

In conducting repo and reverse repo transactions, the Bank uses government bonds. Receivables from reverse repo transactions are included in amounts due from banks (Note 3.9). Payables from repo transactions are included in amounts due to customers (Note 3.18). The securities received under reverse repo transactions are not recognized on statement of financial position, but the Bank has the right to re-pledge it or sell, however it also has an obligation to return it. Fair value of the securities held under reverse repo transactions was CZK 69,580 million at 31 December 2014 (2013: CZK 53,429 million).

3.23. Legal contingencies

On 21 February 2002, the Bank was named as a defendant in a legal dispute initiated by AO Invest, spol. s r.o., in respect of compensation of a damage of CZK 238 million. The plaintiff alleges that the claimed damage was incurred with regard to the mediated purchase of 1,050 bonds of ZPS, a.s. The legal dispute was halted due to AO Invest, spol. s r.o., being declared bankrupt. The legal dispute is currently being conducted against the bankruptcy trustee of AO Invest. During 2008, the litigated amount decreased to CZK 137 million as a result of the plaintiff withdrawing the claim for compensation of CZK 100 million. At the end of 2008, the bankruptcy trustee sold the receivable, which is subject to the legal dispute, to MISORA HOLDINGS Limited, incorporated in British Virgin Islands. No decision has yet been taken regarding the involvement of this entity in the legal dispute. The legal dispute has not yet been completed and it is highly difficult to predict the development for the Bank, nor can the reliable estimate of the potential outflow of economic benefits be made.

3.24. Related party disclosures

Related parties of the Bank comprise:

1/ the Czech state. Dividends allocations are described in Note 3.20 and income taxes in Note 3.7.
2/ the associated undertaking MUFIS;
3/ key management personnel (being defined as Board of Directors, Supervisory Board, Audit Committee and Bank's senior management) – for the detail of the expenses see Note 3.4; and
4/ entities controlled by the same controlling entity, i.e. by the Czech state.

The balances from related-party transactions with the Czech state and entities controlled by the same controlling entity (in the table below - "Other related parties") at the period-end date, related expense and income for the year (except for the income taxes and dividends) and off-balance sheet exposures are as follows:

Notes to the financial statements

CZKm	31 December 2014	31 December 2013
Assets	**28,873**	**25,473**
Czech state	27,734	24,322
Associates	-	-
Key management	1	1
Other related parties	1,138	1,150
Liabilities	**99,495**	**70,154**
Czech state	98,872	69,580
Associates	203	154
Key management	12	10
Other related parties	408	410
Revenues	**758**	**962**
Czech state	639	816
Associates	-	-
Key management	-	-
Other related parties	119	146
Expenses	**68**	**122**
Czech state	21	12
Associates	1	1
Key management	46	43
Other related parties	-	66
Collaterals provided under repo transactions and other off-balance sheet assets in the normal course of business	71,275	56,575
Czech state	71,275	56,575
Other related parties	-	-
Collaterals received under reverse repo transactions and other off-balance sheet liabilities in the normal course of business	**1,700**	**1,731**
Czech state	717	748
Other related parties	983	983

In the opinion of management all transactions entered into with related parties were made in the ordinary course of business on substantially the same terms and conditions, including interest rates, as those prevailing at the same time for comparable transactions with other customers, and did not involve more than normal credit risk or present other unfavorable features. These include current accounts, loans, deposits and securities issued by these entities and provided collaterals and loan commitments.

In PANEL guarantee program the Bank receives from Státní fond rozvoje bydlení (“SFRB”) a fee of 1.3% p.a. of the guaranteed balance amount which is included in Fee and commission income of CZK 64 million (2013: 77 million).

Revenues from the Czech state include also interest income (see Note 3.1) from the infrastructure loans taken over from the Ministry of Finance. For details of the transaction see Note 3.11.

Terms and conditions of the related party transactions - average effective interest rates

The table below provides average interest rates of significant items of related parties assets and liabilities as of 31 December 2014 and 2013.

	31 December 2014	31 December 2013
Assets		
Amounts due from banks	0.00%	0.04%
Loans to customers	3.19%	3.09%
Available for sale securities	1.83%	1,96%
Securities at fair value through profit or loss	4.12%	4,10%
Securities held to maturity	3.85%	4,10%
Liabilities		
Amounts due to banks	0.00%	0.00%
Amounts due to customers	0.09%	0.83%
Repo operations with the Ministry of Finance	0.04%	0.04%

4/ Risk management and financial instruments

4.1. Credit risk

4.1.1. Risk management method

Credit rating of amounts due from customers and banks

The credit rating of the enterprises that are small and medium-sized businesses, municipalities, water management enterprises, housing associations and associations of owners of housing units, and non-profit organizations is undertaken in accordance with the Bank's internal regulations and involves assessing the borrower's credit worthiness on the basis of an analysis of economic and other aspects. The assessment of other than economic aspects involves analyzing external and internal factors that impact the client's activities and operations. The economic assessment focuses on undertaking a financial analysis of economic indicators and additional information. Credit worthiness is evaluated in relation to each transaction that carries an element of credit risk; credit risk exposure and the ratings are periodically assessed over the whole life of the loan transaction. Credit risk is expressed by assigning the borrower the relevant risk category. Credit risk exposure involved in a specific transaction is controlled by establishing contractual conditions and obtaining collateral in support of the transaction.

The monitoring of rating and credit risk involves assessing the following criteria (at minimum):

- Current financial and economic situation of the clients;
- Compliance with contractual terms, specifically reviews of the repayments of loan principal and interest amounts, payment of the fee for the provision of a guarantee, contractual penalties and charges, provision of information to the Bank, and balances on the client's bank accounts;
- Restructuring;
- External factors, primarily economic, political and legal;
- Loan analysts quarterly monitor the development of selected data and information for the monitoring of all clients as part of a client's financial analysis;
- Staff of the Risky Transactions Department monitor the records of clients in bankruptcy, settlement and liquidation on an ongoing basis, with regular weekly checks;
- Staff of business units monitor, on a monthly basis, the summary of clients for which the central loan register indicates that they have past due receivables.

Measuring credit risk of the portfolio

The Bank uses the following techniques to measure risks inherent in the loan and guarantee portfolio:

Notes to the financial statements

The method of quantified losses on the portfolio of loans and guarantees exposures compares the total quantified losses of doubtful and loss receivables with the redemption of these exposures. The quantification of losses also reflects the current balances of substandard exposures adjusted by an empirical and well-established coefficient which represents an estimate of the default rate of exposures in this category.

The weighted risk exposure method compares the weighted risk exposure with the original contractual amount of the loans (the balance of the actual loan draw-down) and guarantees. The weighted risk exposure consists of the sum of recorded provisions, the sum of receivables written-off, the sum of outstanding principal, the sum of outstanding interest and the sum of outstanding contractual penalties on client accounts, segmented by individual years of the portfolio's duration.

The risk category method compares quantified losses with the original contractual value of the loans or guarantees.

The incurred loss method is derived from calculated probabilities of individually unidentified default on individual internal risk categories described below and loss given default for specified type of exposures (loans, loans granted within the water infrastructure support program and guarantees).

Risk categories

The Bank has risk (internal rating) categories 4 to 10, which are linked to the Czech National Bank's risk categories: standard loans 4, 5 and 6, watch 7, substandard 8, doubtful 9 and loss 10. In 2012 the Bank established internal rating category X9. Clients, which the Bank considers doubtful and which are overdue only 180 days or less, are classified into this category.

Credit enhancement

In the course of its lending and guarantees business, the Bank accepts movable and immovable assets pledged as collateral. This fact is also considered in calculation of the impairment provisions. The Bank also uses various forms of guarantee statements to collateralize its loan receivables.

Movable and immovable asset collateral is recorded in operating records and is valued on the basis of an appraisal prepared by a licensed appraiser (nominal value of collateral). The Bank centrally revalues real estate collateral to market values every two years on the basis of pricing maps prepared by an external agency. Collaterals provided by individuals and legal entities and bills of exchange are recorded in operating records and are valued at estimated values provided by the Bank's internal regulation.

The recoverable value of collateral takes into account both the cost of recovering collateral and the time value of money.

If the borrower's receivable is past due by more than 360 days, the Bank does not attribute any value to the collateral, since the historical evidence proves negligible workouts from such collaterals.

Recovery of Amounts due from borrowers

The Bank recovers due receivables arising from bank guarantees and loans through its internal debt work-out system by using all statutory recovery instruments available according to generally applicable legal regulations. With a view to expediting the recovery process, the Bank has employed an arbitration clause in respect of loan contracts and enforceable notarial and distrainer deeds.

Notes to the financial statements

Economic sector risk concentrations

The Bank principally monitors risk concentrations in the area of loans issued to small and medium-sized businesses and receivables arising primarily from water management loans. These risks are periodically monitored and reassessed at least on an annual basis. Credit risk limits are approved by the Board of Directors. This concentration translates into the definition of the classes of the loans to customers.

Geographical concentrations

Although the Bank performs its key activities in the Czech Republic, some investments in securities are done also outside of the Czech Republic. For the geographical concentrations see Note 4.1 B.

Risk concentrations

Significant risk concentration is defined by the Bank as a situation, where excessive concentration of exposures against mutually related entities or groups, certain industries, business activities or geographical areas would have significant impact on Bank's performance and stability in the case of negative development.

The Bank primarily monitors risk concentrations in the area of preferential guarantees issued for loans to small and medium-sized businesses and for loans issued on housing units' repairs, preferential loans issued by the Bank to small and medium-sized businesses and loans to entrepreneurs and municipalities for water management projects. Majority of these loans and guarantees is provided in cooperation with the government and given the fact that the state participates on risk in some types of loans and guarantees the Bank's risk is effectively shared and thus limited. The Bank manages its risk concentrations in relation to credit exposure using system of limits for credit risk management. To identify concentration of credit risk the Bank mainly uses methods and procedures that are based on data analysis, which are stored in internal business and accounting systems of the Bank. The Bank does not use any hedging derivatives to eliminate these risks. The risks are periodically monitored.

Credit risk of other financial assets

Generally, in accordance with its internal regulations, the Bank defines eligible financial instruments for its investments. These principally involve deposits, bonds (mortgage bonds, CZK bonds, EUR bonds, and other foreign currency bonds) and derivatives (FX FWD, FX SWAP, CCS, IRS).

Credit assessment of counterparties and issuers involves analyzing the borrower's solvency on the basis of credit ratings published by internationally recognized rating agencies and evaluating economic and other aspects. The solvency of counterparties and issuers is periodically assessed over the whole life of the commercial loan transaction.

Notes to the financial statements

4.1.2. Credit risk – quantitative disclosures

aa) Quality of amounts due from customers

Information about the credit quality of financial assets that are neither past due nor impaired

31 December 2014

	Risk category							
CZKm Classes of financial assets	**4, 5**	**6**	**7**	**8**	**9**	**10**	**Not specified**	**Total**
Loans to private legal entities and individuals	120	546	122	19	-	-	26	833
Loans to Czech government entities	7,693	-	-	-	-	-	-	7,693
Loans to municipalities	-	218	-	-	-	-	-	218
Total	**7,813**	**764**	**122**	**19**	**-**	**-**	**26**	**8,744**

31 December 2013

	Risk category							
CZKm Classes of financial assets	**4, 5**	**6**	**7**	**8**	**9**	**10**	**Not specified**	**Total**
Loans to private legal entities and individuals	123	1,143	169	24	-	-	27	1,486
Loans to Czech government entities	9,311	-	-	-	-	-	-	9,311
Loans to municipalities	-	180	-	-	-	-	-	180
Total	**9,434**	**1,323**	**169**	**24**	**-**	**-**	**27**	**10,977**

Analysis of financial assets that are individually determined to be impaired

31 December 2014

	Risk category					
CZKm Classes of financial assets	**7**	**8**	**9**	**10**	**Not specified**	**Total**
Loans to private legal entities and individuals	1,598	457	504	1,041	606	4,206
Loans to municipalities	461	43	14	-	-	518
Total	**2,059**	**500**	**518**	**1,041**	**606**	**4,724**

31 December 2013

	Risk category					
CZKm Classes of financial assets	**7**	**8**	**9**	**10**	**Not specified**	**Total**
Loans to private legal entities and individuals	1,843	583	576	984	564	4,550
Loans to municipalities	565	62	34	-	-	661
Total	**2,408**	**645**	**610**	**984**	**564**	**5,211**

Notes to the financial statements

Analysis by regulatory rating

The loans to clients comprise the following, broken down by regulatory classification:

CZKm	Internal rating	31 December 2014	31 December 2013
Standard	4 – 6	8,555	10,737
Watched	7	2,228	2,621
Substandard	8	520	672
Doubtful	9	517	610
Loss	10	1,648	1,548
Total		**13,468**	**16,188**
Impairment provision for loans to customers (Note 3.5)		(1,878)	(1,957)
Net amounts due from customers		**11,590**	**14,231**

Analysis of provisions by risk category

CZKm		31 December 2014		31 December 2013	
Risk category		Type of provision		Type of provision	
		Individual	Portfolio	Individual	Portfolio
4 – 6	Standard	-	46	-	62
7	Watched	260	31	314	42
8	Sub-standard	154	-	187	-
9	Doubtful	272	-	371	-
10	Loss	1,115	-	981	-
Total		**1,801**	**77**	**1,853**	**104**
Total provisions			**1,878**		**1,957**

Analysis by collateral

The loan portfolio comprises the following, broken down by type of collateral:

CZKm	31 December 2014	31 December 2013
Bank guarantees and collateral by reliable guarantors	739	715
Cash collateral	16	18
Real estate collateral	1,963	2,185
Other loan collateral	48	58
Uncollateralized	10,702	13,212
Total	**13,468**	**16,188**
Impairment provision for loans to customers (Note 3.5)	(1,878)	(1,957)
Net amounts due from customers	**11,590**	**14,231**

Renegotiated loans to customers

CZKm	31 December 2014	31 December 2013
Loans to private legal entities and individuals	396	429

Notes to the financial statements

Aging analysis of loans past due which are not classified as individually impaired

31 December 2014

CZKm	Past due 30 days	Past due 30 – 90 days	Past due 90 – 180 days
Loans to private legal entities and individuals	-	-	-
Total	**-**	**-**	**-**

31 December 2013

CZKm	Past due 30 days	Past due 30 – 90 days	Past due 90 – 180 days
Loans to private legal entities and individuals	-	-	1
Total	**-**	**-**	**1**

31 December 2014

CZKm	Bank guarantee and collateral by reliable guarantors	Collateral by pledged real estate	Uncollateralised
Loans to private legal entities and individuals	-	-	-
Total	**-**	**-**	**-**

31 December 2013

CZKm	Bank guarantee and collateral by reliable guarantors	Collateral by pledged real estate	Uncollateralised
Loans to private legal entities and individuals	-	-	-
Total	**-**	**-**	**-**

ab) Quality of guarantees portfolio

31 December 2014 in CZKm

	Risk classification								
Programs	**5**	**6**	**7**	**8**	**X9[1)]**	**9**	**10**	**No risk category***	**Total**
Guarantees for small and medium sized enterprises provided until 2006	7	27	79	49	-	55	132	-	349
PANEL small portfolio guarantees	-	38	117	7	-	13	5	216	396
PANEL individual investment guarantees	-	942	3,045	435	-	185	5	14	4,626
Other previously provided guarantees	-	-	-	-	-	-	22	-	22
Vadium	-	-	89	-	-	-	4	-	93
Small portfolio guarantees for businessmen since 2007	-	69	267	138	1	48	5	940	1,468
Small portfolio guarantees without external risk enhancement	19	170	595	200	-	38	1	5,799	6,822
Individual investment and operating guarantees for small and medium sized enterprises since 2007	47	144	2,351	624	-	557	220	181	4,124
Total	**73**	**1,390**	**6,543**	**1,453**	**1**	**896**	**394**	**7,150**	**17,900**

* Portfolio approach

[1)] Category X9 is used by the Bank to designate guarantees where the Bank anticipates delivery of the pay-out call

Notes to the financial statements

31 December 2013 in CZKm

	Risk classification								
Programs	**5**	**6**	**7**	**8**	**X9[1]**	**9**	**10**	**No risk category***	**Total**
Guarantees for small and medium sized enterprises provided until 2006	8	49	147	100	77	25	144	-	550
PANEL small portfolio guarantees	-	60	132	12	11	-	-	238	453
PANEL individual investment guarantees	-	1,015	3,847	496	149	3	-	17	5,527
Other previously provided guarantees	-	-	-	-	-	-	22	-	22
Vadium	-	1	106	-	-	-	-	-	107
Small portfolio guarantees for businessmen since 2007	9	112	521	190	49	1	1	1,533	2,416
Small portfolio guarantees without external risk enhancement	5	119	431	145	43	-	1	3,321	4,065
Individual investment and operating guarantees for small and medium sized enterprises since 2007	51	227	2,776	741	817	-	272	105	4,989
Total	**73**	**1,583**	**7,960**	**1,684**	**1,146**	**29**	**440**	**5,214**	**18,129**

* Portfolio approach

[1] Category X9 is used by the Bank to designate guarantees where the Bank anticipates delivery of the pay-out call

ac) Quality of Securities portfolio

The securities portfolio comprises the following, broken down by rating classification and classes of financial instruments:

31 December 2014

CZKm	**AA- to AA+**	**A- to A+**	**Lower than A**	**Total**
Securities at fair value through profit or loss	415	1,091	-	1,506
Securities available for sale	9,832	6,327	451	16,610
Securities held to maturity	770	4,990	-	5,760
Total	**11,017**	**12,408**	**451**	**23,876**

31 December 2013

CZKm	**AA- to AA+**	**A- to A+**	**Lower than A**	**Total**
Securities at fair value through profit or loss	159	1,639	-	1,798
Securities available for sale	6,531	5,706	-	12,237
Securities held to maturity	-	5,020	-	5,020
Total	**6,690**	**12,365**	**-**	**19,055**

ad) Quality of derivatives portfolio

The derivatives portfolio as at 31 December 2014 and 2013 includes established banking counterparties (with external rating equivalent of AA+ to A).

Notes to the financial statements

b) Geographical concentration of assets

31 December 2014
Assets

CZKm	Czech Republic	European Union	Total
Cash and balances with central banks	91,234	-	91,234
Amounts due from banks	180	-	180
Securities at fair value through profit or loss	1,157	349	1,506
Positive fair values of financial derivative transactions	169	-	169
Loans and advances to customers	11,590	-	11,590
Securities available for sale	15,718	892	16,610
Securities held to maturity	5,760	-	5,760
Other financial assets	45	-	45
Total financial assets	**125,853**	**1,241**	**127,094**
Non-financial assets	**349**	**-**	**349**
Total	**126,202**	**1,241**	**127,443**

31 December 2013
Assets

CZKm	Czech Republic	European Union	Total
Cash and balances with central banks	64,152	-	64,152
Amounts due from banks	140	-	140
Securities at fair value through profit or loss	1,241	557	1,798
Positive fair values of financial derivative transactions	176	-	176
Loans and advances to customers	14,231	-	14,231
Securities available for sale	11,920	317	12,237
Securities held to maturity	5,020	-	5,020
Other financial assets	54	-	54
Total financial assets	**96,934**	**874**	**97,808**
Non-financial assets	**339**	**-**	**339**
Total	**97,273**	**874**	**98,147**

c) The Bank's maximum credit risk exposure

31 December 2014 in CZKm

		Total exposure		**Collateral held**
	Assets	**Financial guarantees and loan commitments**	**Total credit exposure**	
Cash and balances with central banks	91,234	-	91,234	69,580
Amounts due from banks	180	-	180	-
Securities at fair value through profit or loss	1,506	-	1,506	-
Financial derivatives	169	-	169	-
Loans to customers	11,590	-	11,590	2,765
- *Loans to private legal entities and individuals*	3,269	-	3,269	2,403
- *Loans to the Czech government entities*	7,693	-	7,693	-
- *Loans to municipalities*	628	-	628	362
Securities available for sale	16,610	-	16,610	-
Securities held to maturity	5,760	-	5,760	-
Other financial assets	45	-	45	-
Financial guarantees and loan commitments	**-**	**19,328**	**19,328**	**2,341**
Total financial assets	**127,094**	**19,328**	**146,422**	**74,686**
Non-financial assets	**349**			
Total assets	**127,443**			

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31 December 2013 in CZKm

		Total exposure		Collateral held
	Assets	**Financial guarantees and loan commitments**	**Total credit exposure**	
Cash and balances with central banks	64,152	-	64,152	53,429
Amounts due from banks	140	-	140	-
Securities at fair value through profit or loss	1,798	-	1,798	-
Financial derivatives	176	-	176	-
Loans to customers	14,231	-	14,231	2,976
- Loans to private legal entities and individuals	4,225	-	4,225	2,569
- Loans to the Czech government entities	9,311	-	9,311	-
- Loans to municipalities	695	-	695	407
Securities available for sale	12,237	-	12,237	-
Securities held to maturity	5,020	-	5,020	-
Other financial assets	54	-	54	-
Financial guarantees and loan commitments	**-**	**19,349**	**19,349**	**2,557**
Total financial assets	**97,808**	**19,349**	**117,157**	**58,962**
Non-financial assets	**339**			
Total assets	**98,147**			

The maximum credit exposure is presented at carrying values net of any recognized impairment losses. Collaterals held for due from banks represents the fair value of the securities obtained under reverse repo transactions, for loans to customers principally the collateralized mortgages (see Note 4.1.2) and in case of the financial guarantees the current level of funds deposited by the programs partners to cover risks attached to providing of the financial guarantees (see Note 3.18).

4.2. Market risk

4.2.1. Management of the market risk

Characteristics of Market Risks

The principal market risk management strategy is defined in the Bank's internal regulations and in the documents approved by the Board of Directors of the Bank, and primarily provides guidance on the following areas:

- Acceptable degree of market risks;
- Market risk management techniques;
- Set of limits used; and
- Basic requirements regarding the Bank's organizational structure in terms of market risk management, including segregation of duties and information flows.

Description of Transactions Carrying Market Risks

The Bank is exposed to market risks in acquiring, holding and selling investment instruments defined in the Investment Strategy of ČMZRB. This risk arises from open positions in interest rates and currencies, there are no exposures to risk in equities.

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Market Risk Measurement

The Bank measures interest rate risk using basic techniques (interest rate GAP analysis, duration and elasticity of interest rates) and techniques to calculate capital adequacy as set out in Regulation (EU) No 575/2013 of the European Parliament and of the Council.

In addition, the Bank has developed a series of internal limits to restrict its market risk exposure. The interest rate GAP analysis measures interest rate risk inherent in the trading and banking book on a collective basis. Interest rate risk is restricted through limits to net interest rate exposure in each time bucket. Interest rate risk inherent in all bond portfolios is restricted by having a limit in place in respect of the elasticity of the bond portfolio. The Bank undertakes stress testing on a quarterly basis in accordance with Regulation no.163/2014.

Market Risk Management

The Bank's instrument for managing market risks involves the external capital adequacy limit and internal limits for interest rate risk and elasticity of the interest rate in respect of the bond portfolio. In addition, the market risk is mitigated through the implementation of an internal capital adequacy limit.

Foreign currency risk is prevented by limits set out in Regulation (EU) No 575/2013 of the European Parliament and of the Council.

Interest rate risk limits restrict the size of interest rate GAP in each time bucket of an interest rate GAP analysis in relation to the Bank's capital and are expressed in percentage terms. The limit for elasticity of the interest rate in respect of the bond portfolio restricts the market risk associated with all bond portfolios together with derivatives hedging risk arising from the change in exchange rates when the Bank holds foreign currency bonds.

The Bank's internal capital adequacy limit sets out requirements that are more stringent than the external capital adequacy limit established by the banking regulator. The Bank uses hedging derivatives to manage market risk. The Bank has secured loans from European Investment Bank and German Kreditanstalt für Wiederaufbau as well as bonds. The risk management department of the Bank calculates accounting hedge effectiveness.

4.2.2. Derivates

Trading derivatives

	31 December 2014		31 December 2013	
CZKm	**Notional value asset**	**Notional value liability**	**Notional value asset**	**Notional value liability**
Interest rate swaps	500	500	500	500
Currency and cross - currency swaps	2,586	2,526	3,340	3,277
Total	**3,086**	**3,026**	**3,840**	**3,777**

	31 December 2014		31 December 2013	
CZKm	**Positive fair value**	**Negative fair value**	**Positive fair value**	**Negative fair value**
Interest rate swaps	-	65	-	44
Currency swaps	169	156	176	161
Total	**169**	**221**	**176**	**205**

Notes to the financial statements

Hedging derivatives

The Bank uses the fair value hedging derivatives to hedge currency risk relating to recognized hedged items, which are securities denominated in foreign currencies (see Notes 3.12 and 4.3).

	31 December 2014		31 December 2013	
CZKm	**Notional value asset**	**Notional value liability**	**Notional value asset**	**Notional value liability**
Cross currency swaps	203	211	276	295
Total	**203**	**211**	**276**	**295**

	31 December 2014		31 December 2013	
CZKm	**Positive fair value**	**Negative fair value**	**Positive fair value**	**Negative fair value**
Cross currency swaps	-	41	-	54
Total	**-**	**41**	**-**	**54**

4.3. Foreign currency risk

The Bank's financial position and cash flows are exposed to the risks of changes in exchange rates of common foreign currencies. The Bank monitors its foreign currency positions on a daily basis. In the event that the Bank breaches limits, it undertakes measures as outlined in its internal regulations relating to foreign currency exposure limits.

The table below provides summary information about the Bank's exposure to foreign currency risk. The tables set out foreign currency assets and liabilities at carrying values, analyzed by currency.

The Bank covers its open position by using financial derivatives as can be seen from the tables below and the sensitivity analysis.

31 December 2014

CZKm	CZK	EUR	USD	Total
Cash and balances with central bank	91,234	-	-	91,234
Amounts due from banks	154	26	-	180
Securities at fair value through profit or loss	774	466	266	1,506
Financial derivatives	169	-	-	169
Loans to customers, net	7,242	4,348	-	11,590
Securities available for sale	16,610	-	-	16,610
Securities held to maturity	5,760	-	-	5,760
Other financial assets	45	-	-	45
Total financial assets	**121,988**	**4,840**	**266**	**127,094**
Non-financial assets	**349**	**-**	**-**	**349**
Total assets	**122,337**	**4,840**	**266**	**127,443**
Amounts due to banks	7,750	6,565	-	14,315
Amounts due to customers	103,903	49	-	103,952
Financial derivatives	262	-	-	262
Other financial liabilities	237	-	-	237
Total financial liabilities	**112,152**	**6,614**	**-**	**118,766**
Non-financial liabilities and equity	**8,677**	**-**	**-**	**8,677**
Total liabilities and equity	**120,829**	**6,614**	**-**	**127,443**
Statement of financial position net	(1,509)	(1,775)	266	-
Off-balance sheet derivatives notional position, net	1,552	1,803	(251)	-
Net position	**43**	**28**	**15**	**-**

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31 December 2013

CZKm	CZK	EUR	USD	Total
Cash and balances with central bank	64,152	-	-	64,152
Amounts due from banks	132	8	-	140
Securities at fair value through profit or loss	626	792	380	1,798
Financial derivatives	176	-	-	176
Loans to customers, net	9,035	5,196	-	14,231
Securities available for sale	12,179	58	-	12,237
Securities held to maturity	5,020	-	-	5,020
Other financial assets	54	-	-	54
Total financial assets	**91,374**	**6,054**	**380**	**97,808**
Non-financial assets	**339**	**-**	**-**	**339**
Total assets	**91,713**	**6,054**	**380**	**98,147**
Amounts due to banks	8,128	7,770	-	15,898
Amounts due to customers	73,485	31	-	73,516
Financial derivatives	259	-	-	259
Other financial liabilities	238	-	-	238
Total financial liabilities	**82,110**	**7,801**	**-**	**89,911**
Non-financial liabilities and equity	**8,236**	**-**	**-**	**8,236**
Total liabilities and equity	**90,346**	**7,801**	**-**	**98,147**
Statement of financial position position, net	(1,367)	(1,747)	380	-
Off-balance sheet derivatives notional position, net	1,436	1,794	(358)	-
Net position	**69**	**47**	**22**	**-**

Foreign exchange rates sensitivity analysis

Set out below is a sensitivity analysis to foreign currency risk. The statement of financial position items in foreign currencies were tested in respect of the upward movement of a foreign exchange rate by 10% (a 10% appreciation of the currencies would have an equal and opposite effect). The open position in EUR and USD currencies is hedged using derivatives. The hedging instruments almost fully counter-balance the open position (see tables above) and therefore also the income statement and equity impact of the movements in foreign exchange rates is not significant as of the statement of financial position date and also during the year. The table below summarizes the sensitivities in CZK in comparison only to CZK/EUR exchange rates valid as of 31 December 2014 or 2013 as EUR was the only significant currency in which the Bank had open position as at that date (for open position amounts see above).

	2014 CZKm	2013 CZKm
Sensitivity to changes in EUR rates		
Expected rate fluctuation, %	10%	10%
Open position	28	47
Effect on profit and loss	3	(1)
Effect on equity	-	6

4.4. Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. The length of time for which the rate of interest is fixed on a financial instrument indicates to what extent it is exposed to interest rate risk.

The table below provides information on the extent of the Bank’s interest rate exposure based either on the contractual maturity date of its financial instruments or, in the case of instruments that reprice to a market interest

Notes to the financial statements

rate before maturity, the next repricing date. Those assets and liabilities that do not have contractual maturity or a repricing date were grouped in the 'non-specified' category.

The Bank has a significant portion of amounts due to customers which are not interest bearing instruments. These comprise part of state deposits and risk funds (see Note 3.18). These liabilities are presented as liabilities with non-specified interest rate sensitivity.

Impaired loans are carried on a non-accrual basis and presented as items with non-specified interest rate sensitivity.

31 December 2014

	Up to 3 months CZKm	3 months to 1 year CZKm	1 year to 5 years CZKm	Over 5 years CZKm	Non-specified CZKm	Total CZKm
Cash and balances with central bank	91,227	-	-	-	7	91,234
Amounts due from banks	179	-	-	-	1	180
Securities at fair value through profit or loss	4	140	757	605	-	1,506
Financial derivatives	-	-	-	-	169	169
Loans to customers, net	833	1,398	6,679	1,612	1,068	11,590
Securities available for sale	10	1,299	4,628	10,673	-	16,610
Securities held to maturity	-	2,135	1,489	2,136	-	5,760
Other financial assets	-	-	-	-	45	45
Total financial assets	**92,253**	**4,972**	**13,553**	**15,026**	**1,290**	**127,094**
Non-financial assets	**-**	**-**	**-**	**-**	**349**	**349**
Total	**92,253**	**4,972**	**13,553**	**15,026**	**1,639**	**127,443**
Amounts due to banks	5,714	1,207	5,993	1,400	1	14,315
Amounts due to customers	100,734	64	-	-	3,154	103,952
Financial derivatives -	-	-	-	262	262	
Other financial liabilities	-	-	-	-	237	237
Total financial liabilities	**106,448**	**1,271**	**5,993**	**1,400**	**3,654**	**118,766**
Non-financial liabilities and equity	**-**	**-**	**-**	**-**	**8,677**	**8,677**
Total	**106,448**	**1,271**	**5,993**	**1,400**	**12,331**	**127,443**
Net interest position	**(14,195)**	**(3,701)**	**(7,560)**	**(13,626)**	**(10,962)**	**-**

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31 December 2013

	Up to 3 months CZKm	3 months to 1 year CZKm	1 year to 5 years CZKm	Over 5 years CZKm	Non-specified CZKm	Total CZKm
Cash and balances with central bank	64,144	-	-	-	8	64,152
Amounts due from banks	139	-	-	-	1	140
Securities at fair value through profit or loss	5	495	500	798	-	1,798
Financial derivatives	-	-	-	-	176	176
Loans to customers, net	1,245	1,438	7,870	2,505	1,173	14,231
Securities available for sale	364	1,441	3,992	6,440	-	12,237
Securities held to maturity	-	-	2,644	2,376	-	5,020
Other financial assets	-	-	-	-	54	54
Total financial assets	**65,897**	**3,374**	**15,006**	**12,119**	**1,412**	**97,808**
Non-financial assets	**-**	**-**	**-**	**-**	**339**	**339**
Total	**65,897**	**3,374**	**15,006**	**12,119**	**1,751**	**98,147**
Amounts due to banks	5,384	1,210	7,042	2,247	15	15,898
Amounts due to customers	69,762	138	-	-	3,616	73,516
Financial derivatives	-	-	-	-	259	259
Other financial liabilities	-	-	-	-	238	238
Total financial liabilities	**75,146**	**1,348**	**7,042**	**2,247**	**4,128**	**89,911**
Non-financial liabilities and equity	**-**	**-**	**-**	**-**	**8,236**	**8,236**
Total	**75,146**	**1,348**	**7,042**	**2,247**	**12,364**	**98,147**
Net interest position	**(9,249)**	**2,026**	**7,964**	**9,872**	**(10,613)**	**-**

Interest rate sensitivity analysis

Statement of financial position items sensitive to interest rates were analyzed under the 2% expected parallel increase in interest rates. The Bank modelled 8 scenarios for possible movements of interest rates as the benchmark; the most probable alternative of 2% parallel shift was selected for reporting purposes. The impact on profit and loss and equity (in the case of available-for-sale securities) is outlined below.

Statement of financial position item	31 December 2014 Sensitivity/Impact	31 December 2013 Sensitivity/Impact	Comment
Assets			
Loans to customers	(178)	(220)	
Loans to banks	(10)	(18)	
Held to maturity securities	-	-	Only fixed interest rates securities in the portfolio
Available for sale securities	(108)	8	Impact on equity reserve
Available for sale securities	(77)	5	Impact on profit and loss
Financial derivatives	(186)	(243)	
Liabilities			
Due to banks	554	750	
Due to customers	2	2	
Financial derivatives	188	245	

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4.5. Liquidity risk

Liquidity risk is the risk that the Bank will lose its ability to meet its financial obligations as they fall due or that it will not be able to fund its assets. Liquidity risk may result from a temporary payment insolvency and low liquidity of the market with financial instruments, which makes it impossible to quickly close out positions thereby limiting access to funding. The basic liquidity management tool involves the record-keeping and planning of the Bank's cash flows. In support of liquidity management, the Bank uses two mechanisms - payment notices and price setting. The liquidity management strategy is established and implemented through the preparation of a 'Liquidity Scenario' and 'Emergency Plan for Events Jeopardising the Bank's Liquidity'. The Bank's liquidity position is monitored through the liquidity reserve limit in relation to the value of adjusted weighted risk exposure.

The Bank is exposed to daily calls on its available cash resources from overnight deposits, current accounts, maturing deposits, loan draw-downs, guarantees, margins and settlement of derivatives. The Bank does not maintain cash resources to meet all of these needs as experience shows that a minimum level of reinvestment of maturing funds can be predicted with a high level of certainty.

The table below analyses assets and liabilities of the Bank into relevant maturity groupings based upon the remaining maturity period as of the period-end date.

As the main depositors of the Bank are state institutions (Ministry of Finance etc.) the current accounts of the Bank are presented as being repayable on demand because these funds can be withdrawn upon demand. However these deposits represent specific financing granted, e.g. funding for state approved programs and therefore their withdrawal is not likely in large volume upon demand.

The Bank has a significant portion of amounts due to customers which are held for an undefined amount of time to finance individual support programs. These comprise part of state deposits and risk funds (see Note 3.18). These liabilities are presented as liabilities with undefined maturity.

31 December 2014

	Up to 3 months CZKm	3 months to 1 year CZKm	1 year to 5 years CZKm	Over 5 years CZKm	Maturity undefined CZKm	Total CZKm
Cash and balances with central bank	91,230	-	-	-	4	91,234
Amounts due from banks	27	-	-	-	153	180
Securities at fair value through profit or loss	4	140	757	605	-	1,506
Financial derivatives	1	-	50	103	15	169
Loans to customers, net	1,329	1,602	7,323	1,336	-	11,590
Securities available for sale	10	1,299	4,628	10,673	-	16,610
Securities held to maturity	-	2,135	1,489	2,136	-	5,760
Other financial assets	36	-	-	-	9	45
Total financial assets	**92,637**	**5,176**	**14,247**	**14,853**	**181**	**127,094**
Non-financial assets	**14**	**6**	**-**	**-**	**329**	**349**
Total	**92,651**	**5,182**	**14,247**	**14,853**	**510**	**127,443**
Amounts due to banks	5,314	1,207	6,136	1,658	-	14,315
Amounts due to customers	101,169	779	1	2,003	-	103,952
Financial derivatives	-	8	129	125	-	262
Other financial liabilities	1	-	-	-	236	237
Total financial liabilities	**106,484**	**1,994**	**6,266**	**3,786**	**236**	**118,766**
Non-financial liabilities and equity	**291**	**868**	**766**	**1,903**	**4,849**	**8,677**
Total	**106,775**	**2,862**	**7,032**	**5,689**	**5,085**	**127,443**
Net liquidity exposure	**(14,124)**	**2,320**	**7,215**	**9,164**	**(4,575)**	**-**

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31 December 2013

	Up to 3 months CZKm	3 months to 1 year CZKm	1 year to 5 years CZKm	Over 5 years CZKm	Maturity undefined CZKm	Total CZKm
Cash and balances with central bank	64,151	-	-	-	1	64,152
Amounts due from banks	8	-	-	-	132	140
Securities at fair value through profit or loss	5	495	500	798	-	1,798
Financial derivatives	110	42	-	24	-	176
Loans to customers, net	1,786	1,653	8,596	2,196	-	14,231
Securities available for sale	364	1,441	3,992	6,440	-	12,237
Securities held to maturity	-	-	2,644	2,376	-	5,020
Other financial assets	43	-	-	-	11	54
Total financial assets	**66,467**	**3,631**	**15,732**	**11,834**	**144**	**97,808**
Non-financial assets	**11**	**5**	**-**	**-**	**323**	**339**
Total	**66,478**	**3,636**	**15,732**	**11,834**	**467**	**98,147**
Amounts due to banks	4,935	1,210	7,047	2,706	-	15,898
Amounts due to customers	70,627	697	1	2,191	-	73,516
Financial derivatives	4	55	72	128	-	259
Other financial liabilities	1	-	-	-	237	238
Total financial liabilities	**75,567**	**1,962**	**7,120**	**5,025**	**237**	**89,911**
Non-financial liabilities and equity	**208**	**668**	**918**	**1,838**	**4,604**	**8,236**
Total	**75,775**	**2,630**	**8,038**	**6,863**	**4,841**	**98,147**
Net liquidity exposure	**(9,297)**	**1,006**	**7,694**	**4,971**	**(4,374)**	**-**

Contractual liquidity of the main non-derivative financial liabilities at amortized cost and derivatives – undiscounted basis

a/ Amounts due to banks and customers

31 December 2014

CZKm	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Amounts due to banks	9,781	1,411	6,726	1,645	19,563
Amounts due to customers	103,139	100	25	-	103,264

31 December 2013

CZKm	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Amounts due to banks	5,001	1,729	8,931	3,038	18,699
Amounts due to customers	72,820	139	15	544	73,518

b/ Derivatives settled on a net basis

The table below analyses the Bank's derivative financial liabilities that will be settled on a net basis into relevant maturity groupings based on the remaining period at the period-end date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted net cash flows.

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31 December 2014

CZKm	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Interest rate swaps	-	(12)	(45)	(8)	(65)

31 December 2013

CZKm	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Interest rate swaps	1	(12)	(28)	(6)	(45)

c/ Derivatives settled on a gross basis

The Bank's derivatives that will be settled on a gross basis comprise of foreign exchange derivatives: currency forward, currency swaps and cross currency interest rate swaps.

The table below analyses the Bank's derivative financial liabilities that will be settled on a gross basis into relevant maturity groupings based on the remaining period at the period-end date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

4.6. Operational risk

31 December 2014

CZKm	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Cross-currency swaps:					
Cash inflows	114	396	1,641	731	2,913
Cash outflows	104	414	1,713	722	2,953

31 December 2013

CZKm	Up to 3 months	3 months to 1 year	1 year to 5 years	Over 5 years	Total
Cross-currency swaps:					
Cash inflows	115	788	1,994	1,003	3,900
Cash outflows	106	851	2,004	973	3,934

The Bank defines operational risk as the risk of loss arising from human errors, the inappropriateness or failure of internal processes, failures of systems or the risk of loss resulting from external events.

The system of the Bank's operational risk management is built around the following four cornerstones:

- Strategy (clear vision, management attitude, culture);
- Organization (Board of Directors, Assets and Liabilities Management Committee, internal audit, operational risk management coordinator, and the Bank's departments);
- Processes (identification, evaluation, countermeasures, monitoring and reporting); and
- Infrastructure (system, source of information, data collection and communication).

Identification of Operational Risk

The Bank identifies individual operational risks in all of its departments and categorizes them according to the underlying cause (human error, internal process, information system, external factor). Responsibility for identifying operational risks primarily rests with the head of the department where the risk originates (via a self-evaluation

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form). Collection of information from individual departments and its processing is within the remit of the coordinator. The Bank identifies and records each risk to which it is exposed, even a risk that is no longer treated as a risk due to the countermeasures that are currently being implemented.

Evaluation of Operational Risk

Operational risk is evaluated in terms of the likelihood of its occurrence (graded one to five) and the significance of impact if it materializes (graded one to five). The Bank has opted for a qualitative approach to evaluating the risk which better meets its needs and better reflects the situation within the Bank. The evaluation is based on a reasonable estimate and uses scores to assess the likelihood of the occurrence and the significance of impact. Following the evaluation, individual risks are rated according to their overall significance (risk profile) into the following three levels:

- Low (ideal risk profile where the Bank only checks the effectiveness of the existing measures);
- Medium (the risk is acceptable only if the implementation of an appropriate countermeasure to mitigate the risk is too costly); and
- High (the risk is not acceptable, additional countermeasures need to be put in place and the risk mitigated).

Countermeasures

Responsibility for the implementation of an appropriate countermeasure against operational risks rests within the department where the risk originates (mitigation of the likelihood of the occurrence of operational risk or its impact on the Bank).

Monitoring and Reporting

The basic tool for monitoring is the database of incidents and a report on operational risk management within the Bank. These activities result in a risk profile of the Bank. Operational risk events include all events that have a direct impact on the Bank’s profit or loss according to the Bank’s activities during which the event occurred.

4.7. Capital management

The Bank has identified the following risks which should be covered entirely or partially by capital: market risks, interest rate risk of the banking book, credit risk and concentration risk, liquidity risk and operational risk.

The principal objectives of the Bank in managing capital risks are as follows:

- Quantification of risks in the form of economic capital which is needed to cover potential losses arising from these risks;
- Comparison of capital requirements with capital resources;
- Management of capital resources with respect to current and future risks;
- Determination of the maximum acceptable degree of risks with respect to available capital resources;
- Monitoring and management of the performance of business activities with respect to the risk or the capital requirements; and
- Strategic planning with respect to the risk, allocated capital resources and capital efficiency of individual business activities of the Bank.

The Bank has established an internal limit for capital adequacy at 12%. The Bank has implemented the standard approach for capital management which is in compliance with Basel II requirements.

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CZKm	31 December 2014	31 December 2013
Tier 1 capital		
Share capital	2,132	2,132
Less: Own treasure shares	(776)	(1,894)
Other reserves	1,150	1,150
Retained earnings (without profit for the current year, statutory non-consolidated)	1,413	2,519
Less: Values adjusting according to requirements for prudent valuation	(19)	-
Less: intangible assets	(33)	(31)
Total qualifying Tier 1 capital	**3,867**	**3,876**
Total regulatory capital	**3,867**	**3,876**
Total risk weighted exposure	**22,564**	**24,184**
Capital adequacy ratio	**17,14%**	**16,03%**

5/ Fair values of assets and liabilities and fair value hierarchy

The fair value of financial instruments is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. When available, fair value estimates are made based on quoted market prices. However, no readily available market prices exist for a significant portion of the Bank’s financial instruments. In circumstances where the quoted market prices are not readily available, the fair value is estimated using discounted cash flow models or other generally acceptable pricing models as appropriate. Changes in underlying assumptions, including discount rates and estimated future cash flows, significantly affect the estimates. Therefore, the calculated fair market estimates might not be realized in a current sale of the financial instrument. In estimating the fair value of the Bank’s financial instruments, the following methods and assumptions were used.

(a) Cash and balances with central banks

The carrying values of cash and balances within central banks are generally deemed to approximate their fair value.

(b) Securities held to maturity

Fair values of securities in the ‘Held-to-Maturity’ portfolio are taken from the active market, where these instruments are quoted.

(c) Due from banks

The fair value of amounts due from banks is estimated based upon discounted cash flow analyses using interest rates currently offered for investments with similar terms (market rates adjusted to reflect credit risk).

(d) Loans to customers

The fair value of variable yield loans that regularly reprice, with no significant change in credit risk, generally approximates their carrying value. The fair value of loans at fixed interest rates is estimated using discounted cash flow analyses, based upon interest rates currently offered for loans with similar terms to borrowers of similar credit quality.

Notes to the financial statements

(e) Loans and advances to banks

The fair value of term deposits repayable on demand approximates the carrying value of amounts repayable on demand as of the period-end date. The fair value of term deposits at variable interest rates approximates their carrying values as of the period-end date. The fair value of deposits at fixed interest rates is estimated by discounting their future cash flows using market interest rates.

The following table summarizes the carrying values and fair values of those financial assets and liabilities not presented on the statement of financial position at their fair value:

CZKm	31 December 2014 Carrying value	31 December 2014 Fair value	31 December 2013 Carrying value	31 December 2013 Fair value
Financial assets				
Cash and balances with central banks	91,234	91,232	64,152	64,152
Loan and advances to banks	180	180	140	140
Loans to customers	11,590	11,262	14,231	13,062
- *Loans to private legal entities and individuals*	3,269	3,163	4,225	3,913
- *Loans to the Czech government entities*	7,693	4,795	9,311	9,311
- *Loans to municipalities*	628	604	695	630
Securities held to maturity	5,760	6,332	5,020	5,350
Other financial assets	45	45	54	54
Financial liabilities				
Amounts due to banks	14,315	14,028	15,898	14,891
Amounts due to customers	103,952	103,923	73,516	73,454
Other financial liabilities	237	237	238	238

Fair value hierarchy

IFRS 7 specifies a hierarchy of valuation techniques based on whether the inputs to those valuation techniques are observable or unobservable. Observable inputs reflect market data obtained from independent sources; unobservable inputs reflect the Bank's market assumptions. These two types of inputs have created the following fair value hierarchy:

- Level 1 – Quoted prices (unadjusted) in active markets for identical assets or liabilities. This level includes listed debt instruments on exchanges (for example Prague Stock Exchange and other recognized stock exchanges)
- Level 2 – Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices). This level includes over-the-counter derivative contracts. The sources of input parameters like PRIBOR or other yield curves are Bloomberg and Reuters.
- Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs). This level includes financial instruments with significant unobservable components

This hierarchy requires the use of observable market data when available. The Bank considers only relevant and observable market prices in its valuations and does not have any financial assets or liabilities at fair value to be categorized in Level 3. There have not been any reclassifications between the Levels 1 and 2 during the presented periods.

Notes to the financial statements

31 December 2014	Level 1	Level 2
Financial assets at fair value through profit and loss		
Financial assets held for trading		
- Debt securities	415	-
- Derivatives	-	169
Debt securities designated at fair value	1,091	-
Available-for-sale debt securities:	16,610	-
Total assets at fair value	**18,116**	**169**
Financial liabilities at fair value through profit and loss		
- Derivatives held for trading	-	221
Hedging derivatives	-	41
Total liabilities at fair value	**-**	**262**

31 December 2013	Level 1	Level 2
Financial assets at fair value through profit and loss		
Financial assets held for trading		
- Debt securities	271	-
- Derivatives	-	176
Debt securities designated at fair value	1,527	-
Available-for-sale debt securities:	12,237	-
Total assets at fair value	**14,035**	**176**
Financial liabilities at fair value through profit and loss		
- Derivatives held for trading	-	205
Hedging derivatives	-	54
Total liabilities at fair value	**-**	**259**

6/ Subsequent events

No significant events having a material impact on the financial statements of the Bank for the year ended 31 December 2014 occurred subsequent to the period-end date.

The Board of Directors has authorized these financial statements for submission to the General Meeting of Shareholders. These financial statements have been signed, on the basis of authority delegated by the Board of Directors, by Ladislav Macka, Chairman of the Board and Jan Ulip, Member of the Board.

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