

## **Commentary to Quarterly Report SAB - Q I/04 for the first quarter of 2004**

### **Summary of financial results**

In Q1 2004, Bank Handlowy w Warszawie SA ("the Bank") reported net profit of PLN 77.5 million, which is an increase of PLN 67.1 million (i.e. 645.1%) in comparison with Q1 2003. Gross profit for Q1 2004 amounted to PLN 102.6 million, which is an increase of PLN 62.1 million (i.e. 152.9%) in comparison with Q1 2003.

Revenue, consisting of profit on banking activity and other operating income, increased by PLN 44.5 million (i.e. 9.4%) over the first quarter of 2003, while expenses, consisting of other operating expenses, general expenses and depreciation and amortisation, increased by PLN 101.0 million (i.e. 31.8%) over the first quarter of 2003.

Net movement in provisions and revaluation decreased by PLN 118.6 million (i.e. 102.5%) over the first quarter of 2003.

### **Financial accounting principles**

#### *General information*

The report for the first quarter of 2004 has been prepared on the following basis:

- Regulation of the Council of Ministers dated 16 October 2001 concerning current and periodic information reported by issuers of securities (Journal of Laws No. 139, item 1569, as amended),
- Regulation of the Council of Ministers dated 16 October 2001 concerning specific requirements that should be met in offering prospectuses and short form offering prospectuses (Journal of Laws No 139, item 1568, as amended),

and in accordance with the regulations specified in:

- the Accountancy Act of 29 September 1994 (Official Journal of 2002, Number 76, item 694, as amended),
- Regulation of the Ministry of Finance dated 10 December 2001 concerning specific accounting principles for banks (Journal of Laws No. 149, item 1673, as amended),
- Regulation of the Ministry of Finance dated 12 December 2001 concerning specific accounting principles for recognition, valuation, scope of disclosure, and presentation of financial instruments (Journal of Laws No. 149, item 1674),
- Regulation of the Ministry of Finance dated 10 December 2003 concerning principles for creating provisions for risks related to operations of banks (Journal of Laws No. 218, item 2147, as amended).

The principles adopted in the report for the first quarter of 2004 are consistent with the accounting principles adopted and described in the annual report for 2003, except for changes in the rules for creating specific provisions for credit risk and the rules of recognising interest on receivables due to the bank classified as watch, which were introduced in accordance with the amendment to the regulations concerning the accounting principles for banks, effective 1 January 2004.

These changes resulted in the reclassification of time limits for individual risk categories, so that the periods after which loans are classified as non-performing are prolonged. In addition, interest income and discount on receivables classified as watch are recognised in the profit and loss account on an accrual basis. Prior to 1 January 2004, this interest constituted classified income until its receipt.

The financial data as of 31 March 2004 has been prepared using valuation principles for assets and liabilities and recognition of net financial profit or loss, taking into account adjustments for provisions, deferred income tax assets and asset revaluation write-downs, in accordance with the regulations in force.

#### *Method of preparing financial information*

The data presented for reporting periods prior to the first quarter of 2004 has not been adjusted and is consistent with the data published in previous periodic reports.

### **Selected financial data**

Selected financial data presented at the beginning of the quarterly report is expressed in zlotys ("PLN") and in euros ("EUR"). The principles of translation from zlotys into euros are as follows:

1. balance sheet assets and liabilities are translated into euros on the basis of the average exchange rate in force as of the balance sheet date, announced by the National Bank of Poland, which as of 31 March 2004 was PLN 4.7455 and as of 31 March 2003 was PLN 4.4052;
2. profit and loss account items are translated into euros on the basis of the arithmetic mean of the average exchange rates announced by the National Bank of Poland, in force as of the last day of each complete month covered by the quarterly report, which for the first quarter of 2004 was PLN 4.7938, and for the first quarter of 2003 was PLN 4.2474;
3. earnings per one ordinary share and diluted earnings per one ordinary share are translated into euros on the basis of the arithmetic mean of the average exchange rates announced by the National Bank of Poland, in force as of the last day of each complete month over the 12 month period ended 31 March 2004 and 31 March 2003, which were PLN 4.5840 and PLN 4.0284, respectively.

### **Brief description of the Bank's activities in the first quarter of 2004**

#### 1. Corporate and Investment Bank

- *Global Transaction Services*

In January 2004, the Bank signed an agreement to install UniKasa Payment Service Network terminals at gas distribution stations and gas works of Karpacka Spółka Gazownictwa Sp. z o.o., enabling individual customers to pay their invoices through UniKasa at over 300 network outlets.

In March 2004, the Bank signed an agreement with the Euronet network, enabling UniKasa terminals to be fitted with the option of sale of pre-paid cards for all cellular phone networks. This service will facilitate customer access to pre-paid phone cards. In the future, the Bank plans to expand the range of network functions by the sale of additional services.

- *Treasury products*

In the first quarter of 2004 the Bank concluded two innovative transactions. Specifically the structured private placement of PLN 750 million Treasury Bonds for the Ministry of Finance and a commodity price hedge for 583,000 tonnes of coal.

- *Corporate finance*

In January 2004, the Bank participated in the short-term debt securities issuance programme of Europejski Fundusz Leasingowy S.A., with the indebtedness limit of PLN 600 million. The Bank acted as co-arranger and dealer of the programme. As at 31 March 2004, the Bank had a leading share of 23.5% in the market for short-term debt securities issuance.

In March 2004, the Bank participated in the arrangement of a syndicated loan of PLN 88 million for Elektrociepłownia Wybrzeże S.A.

- *Branch network reorganisation*

In Q1 2004, the Bank continued the reorganisation of its branch network, which commenced in the previous year. On 22 March 2004, another Corporate and Investment Bank branch was combined with a branch of the Consumer Bank. In March 2004, the network reorganisation programme was extended to identify Corporate and Investment Bank branches where excess space could be reduced.

- *Employment restructuring*

The Management Board of the Bank decided that the Bank would terminate contracts of employment of up to 630 employees between 1 April and 31 December 2004. The reductions will be made in the Corporate and Investment Banking Sector and in the Management and Support Sector. The staff reductions aim at adjusting the employment status and structures to the changes in strategies and methods of operations at the Bank, following reorganisation in given areas and introduction of new technological and organisational solutions. In consequence the quality and efficiency of customer service is expected to improve. On 23 March 2004, the Bank entered into an agreement with trade unions, which specifies the procedure for dealing with employees made redundant in the above-mentioned period, and in particular the amounts of severance payments for those employees.

## 2. Consumer Bank

- *Credit cards*

The portfolio of credit cards serviced increased by 11.7% in comparison with the end of March 2003, reflecting the sale of the co-branded Motokarta Kredytowa Citibank-BP card issued in cooperation with BP Polska Sp. z o.o. Up to the end of March 2004, 34,000 Motokarta Kredytowa Citibank-BP cards have been issued.

On 18 February 2004, Citibank Credit Card holders were granted the ability to make automated payments via direct debit order from an account operated in another bank.

- *Loans and advances*

In the first quarter of 2004 there was significant growth in the sale of loans and advances. The number of advances granted, excluding CitiFinancial, increased by as much as 182.9% over the first quarter of 2003.

- *Direct debit*

The over-the-phone direct debit service continued to develop. Over the period from the launch of the service on 1 November 2003 up to the end of March 2004, individual customers of the Bank made 5,600 direct debit orders on the phone.

- *Mortgage loan offering*

In March 2004, the Bank, in cooperation with GE Bank Mieszkaniowy SA, provided a new mortgage loan offering. In selected multi-functional branches and CitiGold branches across Poland customers gained access to basic information about the offering and terms of credit and were able to make an appointment with a representative of GE Bank Mieszkaniowy SA. The mortgage loan is intended for the purchase of an apartment or a home in the primary or secondary market, and also for construction or enlargement of a house, on attractive economic terms. Loans are available in four currencies – zlotys, euros, swiss francs and US dollars, and have a variable interest rate.

## 3. Awards and honours

- The prestigious financial monthly, Global Finance, recognised the Bank as the best bank in Poland in the foreign exchange market (“Best Foreign Exchange Bank 2004”).
- The President of the Warsaw Stock Exchange honoured Dom Maklerski Banku Handlowego S.A. with an award for the largest share of stock exchange turnover and for the largest share of market maker activity.
- The Editing Board of the Polish edition of the Newsweek weekly awarded the Bank the title of the best employer of 2003 in the financial institutions category.
- The Bank was recognised as the best bank in Poland in the ranking list of “Best Emerging Market Banks 2004” published by the Global Finance magazine.
- The “Twój Styl” magazine granted to the bank the special award “Alicja 2003” as a member of the Coalition for Direct Debit.

- Analysts of the Bank were ranked number one for their forecasts of macroeconomic indices published in Gazeta Bankowa in 2003.
- MasterCard International awarded the Bank the silver “Rock Award 2003” in the category of highest achievements in credit card development.

#### **Description of factors and events that had an effect on the financial results for Q1 2004**

In Q1 2004, the Bank reported net profit of PLN 77,548,000, which is an increase of PLN 67,141,000 (i.e. 645.1%) in comparison with Q1 2003. Gross profit for Q1 2004 amounted to PLN 102,637,000, which is an increase of PLN 62,059,000 (i.e. 152.9%) in comparison with Q1 2003.

Profit on banking activity in Q1 2004 was higher than in the corresponding period of the previous year by PLN 39,790,000 (i.e. 8.6%), reflecting the following:

- increase in net interest income of PLN 7,552,000 (i.e. 4.1%), caused mainly by lower interest expenses incurred by the Bank;
- increase in commissions of PLN 25,845,000 (i.e. 21.4%), which mainly resulted from the increase in commission income on insurance products and in fees for the issue and use of charge cards and credit cards;
- decline in net profit on financial operations of PLN 8,103,000 (i.e. 21.5%), due to a lower profit from the sale and valuation of debt securities;
- increase in the result on foreign exchange operations by PLN 14,519,000 (i.e. 12.4%), correlated mainly with the result on foreign exchange operations on financial instruments;

In Q1 2004, operating expenses increased by PLN 100,187,000 (i.e. 39.2%) in comparison with Q1 2003, mainly reflecting additional costs of creating a severance provision for employee reductions within the framework of the employment restructuring plan and additional accruals for management options. There were also additional accruals for services relating to IT systems and advisory support provided by companies within the strategic shareholder group.

Net movement in provisions and revaluation decreased by PLN 118,567,000 million (i.e. 102.5%) from the prior year, reflecting a relative stabilisation in the quality of the Bank's loan portfolio, the high coverage of credit exposures with provisions established in the past, and the prolongation of time limits for individual risk categories following the introduction of new principles for creating specific risk provisions.

The improvement in the macroeconomic situation continued in 2004 contributing to the relative stabilisation of the quality of the credit portfolio. The share of non-performing loans in the gross credit portfolio increased slightly from 30.8% at the end of December 2003 to 30.9% at the end of March 2004, while at the same time the nominal value of these receivables decreased.

#### **Important events after the balance sheet date not included in the Financial Statements**

After 31 March 2004, no events that could have a significant impact on the results of the Bank have occurred without being included in this report.

## **Comparison of results to the forecast for 2004**

The Bank has not publicly announced its results forecast for 2004.

## **Information about the Shareholders**

As of the report submittal date, the only shareholder of the Bank which held directly or indirectly, through subsidiaries, at least 5% of votes at the General Meeting of Shareholders of Bank Handlowy w Warszawie SA was Citibank Overseas Investment Corporation (COIC), a subsidiary of Citibank N.A., that held 89.33% of the votes at the General Meeting of Shareholders of Bank Handlowy w Warszawie SA. The number of shares held by COIC amounted to 116,717,574, which represented 89.33% of the authorised share capital of the Bank. The number of votes associated with the shares held by COIC was 116,717,574, which represented 89.33% of the total number of votes at the General Meeting of Shareholders of the Bank.

The ownership structure has not changed in relation to the major shareholders since the last quarterly report submittal.

## **Changes in ownership of the Issuer's shares by managing and supervising persons**

As far as the Bank is aware, as of the quarterly report submittal date, managing and supervising persons held 752 shares of Bank Handlowy w Warszawie SA. These shares are held exclusively by supervising persons. The number of Bank shares held by managing and supervising persons has not changed since the last quarterly report submittal.

## **Information on pending proceedings**

In Q1 2004, no proceedings relating to the liabilities or receivables of the Bank, the value of which would constitute at least 10% of the Bank's equity, were pending before any court, administrative authority or a body competent for arbitration.

In Q1 2004, the total value of all pending legal actions related to receivables of the Bank exceeded 10% of the Bank's equity and amounted to PLN 897,869,000, and is explained as follows:

The substantial majority of amounts for legal actions related to receivables of the Bank have arisen from the high number of arrangement and bankruptcy proceedings in which Bank Handlowy w Warszawie SA. participates as a creditor, as well as proceedings for appending the enforcement clause to bank enforcement titles, especially in the Consumer Banking Sector. The aforementioned proceedings result from the deteriorated financial standing of the Bank's counterparties, especially borrowers. Moreover, it should be pointed out that the litigations described above, especially the arrangement proceedings and bankruptcy proceedings, are characterised by excessive duration and lengthy judicial procedures. As a result of the aforementioned procedural lengthiness there are few arrangement proceedings and bankruptcy proceedings that end in valid court adjudication within a period shorter than two years, and many of them take four or even more years to be concluded. The Bank's report covers some proceedings, which commenced several years earlier.

In the Bank's opinion, the aforementioned total value of all pending legal actions will gradually decrease, in line with the procedural progress and bankruptcy proceedings, which also applies to proceedings for appending an enforcement clause to bank enforcement titles. This occurred in the first quarter of 2004, and the amount of the Bank's receivables covered by litigations was reduced.

Under the legal regulations in force, the Bank is obliged to create provisions for non-performing receivables already at the stage when the risk level related to the economic performance of a given receivable increases (in the case of bank loans, relevant regulations make the creation of provisions

dependent on the timeliness of loan instalment repayments), and therefore in practice as of the date of commencement of arrangement or bankruptcy proceedings the provision for the given receivable has already been created for the relevant amount.

Simultaneously, as a rule, when bankruptcy proceedings or proceedings for appending an enforcement clause to bank enforcement title come to an end, the Bank recovers at least part of the payment due and is then able to dissolve the created provisions in whole or in part. The same happens in the case of concluded arrangement proceedings, where after the debt has been reduced, the debtor pays the remaining part of its liabilities towards the Bank.

A description of the most important pending legal actions in relation to the Bank's receivables are provided below:

<b>Parties to the proceedings</b>	<b>Litigation value</b>	<b>Proceedings initiation date</b>	<b>Description of the case</b>
Creditor: Bank Handlowy w Warszawie SA	PLN 50,874,000 (loan-related receivable)	22 June 2001 – declaration of bankruptcy.	Within the bankruptcy proceedings the official receiver is disposing of assets. The Bank is awaiting the distribution of funds from the bankruptcy estate.
Creditor: Bank Handlowy w Warszawie SA.	PLN 112,984,000 (loan-related receivable)	8 August 1996 – declaration of bankruptcy.	Within the bankruptcy proceedings the official receiver is disposing of assets. The Bank is awaiting the distribution of funds from the bankruptcy estate.
Creditor: Bank Handlowy w Warszawie SA	PLN 16,500,000	Suit for payment under loan liability.	Case pending. The defendant has raised objections to the issued order for payment.
Plaintiff: Bank Handlowy w Warszawie SA	PLN 33,976,000	Suit for payment under loan liability.	Case pending. The defendant has raised objections to the issued order for payment.
Creditor: Bank Handlowy w Warszawie SA	PLN 30,953,000 (loan-related receivable)	On 3 March 2004, the court declared the debtor bankrupt.	Case pending. The Bank reported a receivable on 8 April 2004.
Creditor: Bank Handlowy w Warszawie SA	PLN 37,134,000 (loan-related receivable)	On 30 June 2003 the court declared the debtor bankrupt.	Case pending.

In Q1 2004, the total value of litigations with the Bank's participation, related to liabilities of the Bank, did not exceed 10% of the shareholders' equity of the Bank.

#### **Information on significant transactions with related entities**

On 26 April 2004, the Bank executed with Citibank N.A., the sole shareholder in Citibank Overseas Investment Corporation, which is a majority shareholder of the Bank, the CitiDirect service level agreement. Based on the agreement Citibank N.A. (as the service provider) agrees to provide for the benefit of the Bank (the service user) the CitiDirect internet transaction service for the use of the Bank and its customers. This agreement represents a continuation of the cooperation between the parties.

On 27 April 2004, the Bank executed a service agreement with Citibank N.A., London Branch; Citibank N.A., New York; Citibank International PLC, London Branch; Citigroup Global Markets Deutschland AG & CO, Germany; Citigroup Global Markets Limited, London; Citigroup Global Markets Asia Limited, Hong Kong; Citigroup Global Markets, INC., related entities to Citibank N.A., the sole shareholder in Citibank Overseas Investment Corporation, which is a majority shareholder of

the Bank. Based on the agreement, the above mentioned entities will provide for the benefit of the Bank as recipient of various support services related to the current activity of the Bank, including advisory services in the following functional areas: management, finance, accounting, audit and assessment of compliance, law and taxes, marketing and public matters, employees matters, administrative issues, analysis and risk assessment.

On 29 April 2004, the Bank executed with Citibank N.A., the sole shareholder in Citibank Overseas Investment Corporation, which is a majority shareholder of the Bank, the IT systems service level agreement. Based on the agreement Citibank N.A. (as the service provider) agrees to provide for the benefit of the Bank (the service user) services related to a number of systems used in the Bank's operations. This agreement represents a continuation of the cooperation between the parties.

### **Information on significant agreements on loan surety or on guarantee granting**

As at the end of Q1 2004, the total value of sureties and guarantees granted by the Bank or its subsidiaries to a single entity does not exceed 10% of the Bank's shareholders' equity.

### **Other important information**

#### *Personnel changes in the Bank's authorities in Q1 2004*

On 30 March 2004, Mr Wiesław Kalinowski submitted his written resignation from the function of the Vice-President of the Bank Management Board to the President of the Bank Supervisory Board. As of that date, his mandate as a member of the Bank Management Board expired.

#### *Other information*

On 23 March 2004, the Bank Management Board adopted a resolution on the proposed allocation of profit for 2003. The Bank Management Board proposed to allocate PLN 241,720,260.00 for dividend payment. The above proposal means that the dividend per one share is PLN 1.85. The Bank Management Board proposed 26 July 2004 as the date of determination of the right to the dividend and 1 September 2004 as the date of dividend payment. The above proposal of the Bank Management Board has been considered by the Supervisory Board, and then will be submitted to the General Meeting of Shareholders for approval.

### **Factors that will influence the future financial results achieved by the Issuer**

The most important factors that will influence the level of the Bank's results in the future include the following:

- the expected further improvement of the economic situation and of financial standing of the Bank's customers, which should be reflected in the gradual growth of demand for banking services, especially loans, and in the improvement of the loan portfolio quality;
- the direction of the interest rate policy adopted by the National Bank of Poland.

The Quarterly Report for Quarter 1 of 2004 will be made available on the official website of Bank Handlowy w Warszawie SA at [www.citibankhandlowy.pl](http://www.citibankhandlowy.pl)

Signature of the Financial Reporting and Control  
Department Director  
Date and signature

Signature of the Management Board Member  
Chief Financial Officer  
Date and signature

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