

ZESPÓŁ ELEKTROWNI PAŃNÓW – ADAMÓW – KONIN SA CAPITAL GROUP

MANAGEMENT BOARD'S REPORT FROM THE OPERATION OF THE CAPITAL GROUP IN THE 1ST HALF OF 2019

*(This is a translation of the document issued originally in Polish language.
The Polish original should be referred to in matters of interpretation.)*

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1. SELECTED FINANCIAL DATA

<i>Selected consolidated financial data</i>	<i>Zloty thousand</i>	<i>Zloty thousand</i>	<i>Euro thousand</i>	<i>Euro thousand</i>
	<i>6 months 2019 period from 01.01.2019 to 30.06.2019</i>	<i>6 months 2018 period from 01.01.2018 to 30.06.2018</i>	<i>6 months 2019 period from 01.01.2019 to 30.06.2019</i>	<i>6 months 2018 period from 01.01.2018 to 30.06.2018</i>
Sales revenue	1 406 030	982 840	327 899	231 829
Operating profit/loss	66 344	(24 637)	15 472	(5 811)
Profit/loss before tax	61 372	(44 595)	14 313	(10 519)
Net profit/loss for the period	36 696	(52 012)	8 558	(12 268)
Net profit attributable to equity holders of the parent	37 911	(51 257)	8 841	(12 090)
Total comprehensive income	36 454	(51 167)	8 501	(12 069)
Net cash flow from operating activities	(11 646)	93 617	(2 716)	22 082
Net cash flow from investing activities	18 194	(49 532)	4 243	(11 683)
Net cash flow from financing activities	(179 383)	(126 654)	(41 834)	(29 875)
Net increase / (decrease) in cash and cash equivalents	(172 835)	(82 569)	(40 307)	(19 476)
Net profit per share (in zloty/euro per share)	0,75	(1,01)	0,17	(0,24)
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547
	<i>As of 30.06.2019</i>	<i>As of 31.12.2018</i>	<i>As of 30.06.2019</i>	<i>As of 31.12.2018</i>
Total assets	3 496 920	3 871 297	822 418	900 302
Fixed assets	2 890 285	2 968 043	679 747	690 243
Current assets	606 635	902 244	142 671	209 824
Total equity	1 661 845	1 687 147	390 838	392 360
Share capital	101 647	101 647	23 906	23 639
Share capital attributable to equity holders of the parent	1 659 772	1 683 859	390 351	391 595
Total liabilities	1 835 075	2 184 150	431 579	507 942
Long-term liabilities	981 162	974 139	230 753	226 544
Short-term liabilities	853 913	1 210 011	200 826	281 398
Book value per share (in zloty/euro per share)	32,70	33,20	7,69	7,72
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547

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Selected financial data of ZE PAK SA	Zloty thousand	Zloty thousand	Euro thousand	Euro thousand
	6 months 2019 period from 01.01.2019 to 30.06.2019	6 months 2018 period from 01.01.2018 to 30.06.2018	6 months 2019 period from 01.01.2019 to 30.06.2019	6 months 2018 period from 01.01.2018 to 30.06.2018
Sales revenues	694 488	499 987	161 961	117 935
Operating profit/loss	32 792	(36 749)	7 647	(8 668)
Profit/loss before tax	29 273	88 478	6 827	20 870
Net profit/loss for the period	23 958	93 570	5 587	22 071
Net cash flow from operating activities	(84 547)	42 546	(19 717)	10 036
Net cash flow from investing activities	19 422	(13 680)	4 529	(3 227)
Net cash flow from financing activities	(78 098)	(80 110)	(18 213)	(18 896)
Net increase / (decrease) in cash and cash equivalents	(143 223)	(51 244)	(33 401)	(12 087)
Net profit per share (in zloty/euro per share)	0,47	1,84	0,11	0,43
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547
	<i>As of</i> 30.06.2019	<i>As of</i> 31.12.2018	<i>As of</i> 30.06.2019	<i>As of</i> 31.12.2018
Total assets	1 927 733	2 151 997	453 371	500 464
Fixed assets	1 685 404	1 745 389	396 379	405 904
Current assets	242 329	406 608	56 992	94 560
Total equity	1 362 345	1 338 387	320 401	311 253
Share capital	101 647	101 647	23 906	23 639
Total liabilities	565 388	813 610	132 970	189 212
Long-term liabilities	2 433	61 392	572	14 277
Short-term liabilities	220 545	245 412	51 869	57 073
Book value per share (in zloty/euro per share)	26,81	26,33	6,31	6,12
Weighted average number of shares	50 823 547	50 823 547	50 823 547	50 823 547

Above financial data were converted into EUR according to the following exchange rates:

particular items of statement of comprehensive income (Profit & loss account) and statement of cash flows (Cash flow) – according to the exchange rate constituting an arithmetic average of average exchange rates set out by the National Bank of Poland at the end of every month of the reporting period starting from 1 January 2019 to 28 June 2019, which is 4,2880 EUR/PLN and from 1 January 2018 to 29 June 2018, which is 4,2395 EUR/PLN;

particular items of the Statement of financial position (Balance sheet) according to average EUR/PLN exchange rate published by the National Bank of Poland as of 28 June 2019, which is 4,2520 EUR/PLN and as of 31 December 2018, which is 4,3000 EUR/PLN.

2. DESCRIPTION OF THE GROUP

2.1. Basic information

As of 30 June 2019, ZE PAK Capital Group (hereinafter referred to as the “Group”, “Capital Group” the “ZE PAK SA Group”) is composed of a dominant entity Zespół Elektrowni Państw – Adamów – Konin SA (hereinafter referred to as “ZE PAK SA” or “Company”) and nine subsidiaries i.e. Elektrownia Państw II sp. z o.o., PAK – Volt SA, PAK Kopalnia Węgla Brunatnego Adamów SA (hereinafter referred to as the “PAK KWB Adamów SA”), PAK Kopalnia Węgla Brunatnego Konin SA (hereinafter referred to as the “PAK KWB Konin SA”), Przedsiębiorstwo Remontowe PAK SERWIS sp. z o.o. (hereinafter referred to as the “PAK SERWIS sp. z o.o.”), PAK Górnictwo sp. z o.o., PAK Infrastruktura sp. z o.o., PAK Adamów sp. z o.o., Aquakon sp. z o.o. in liquidation. All the above-mentioned companies are consolidated.

The companies of the biggest importance for the Group due to their scale of activity are: ZE PAK SA, dealing with production of electricity and heat, Elektrownia Państw II sp. z o.o., dealing with production of electricity, and PAK KWB Adamów SA and PAK KWB Konin SA, dealing with lignite mining. In addition to companies from the aforementioned main areas of activity, the Group also includes other companies that deal, among others, with the execution of construction and assembly works, maintenance works, service, production and trade activities aimed at satisfying the needs and comprehensive industry service.

The production facilities of the Group include three lignite-fired power plants located in the central part of Poland in Wielkopolskie voivodship. These are: Państw II – equipped with a supercritical power unit, Państw I and Konin – equipped additionally with power unit with a boiler dedicated to biomass firing. Total installed gross power output of the production facilities as at the date of this report is 1896 MW.

The Group’s mining assets are concentrated in two companies: PAK KWB Konin, which currently operates on Józwin, Tomisławice and Drzewce open casts, and PAK KWB Adamów operating on Adamów open cast.

Majority of the Group’s sales revenue is derived from sale of electricity. This is supplemented by revenues from sale of heat, contracts for construction repair services and certificates of Energy origin. An additional source of sales revenues, depending on the level of production costs, energy prices on the market and production volume, are revenues from the termination of long-term contracts (Power Purchase Agreements) for the sale of electricity, generated by Elektrownia Państw II sp. z o.o. The Group, having lignite mines in its structure, provides power plants with an access to uninterrupted lignite supplies for own production installations located in the immediate vicinity of the mines. The vertically integrated Group enables optimization of coal inventories and supplies by coordinating coal mining with the demand for this fuel. The demand for biomass is covered on the basis of contracts concluded with suppliers.

The structure of ZE PAK SA Group as at June, 30 2019 is presented at Picture 1.

Apart from the Capital Group, ZE PAK SA owns shares in Zakłady Pomiarowo-Badawcze Energetyki Energopomiar sp. z o.o. with headquarters in Gliwice and providing measurement, research and consultancy services regarding, among others power engineering. The Company holds one share in the aforementioned company with the value of PLN 151 201.01, which constitutes 2.81% of the total capital.

The main shareholder makes the Group affiliated with other entities, in which Zygmunt Solorz holds substantial direct or indirect share.

2.2. Structure

Picture 1: Structure of the Group as of 30 June 2019

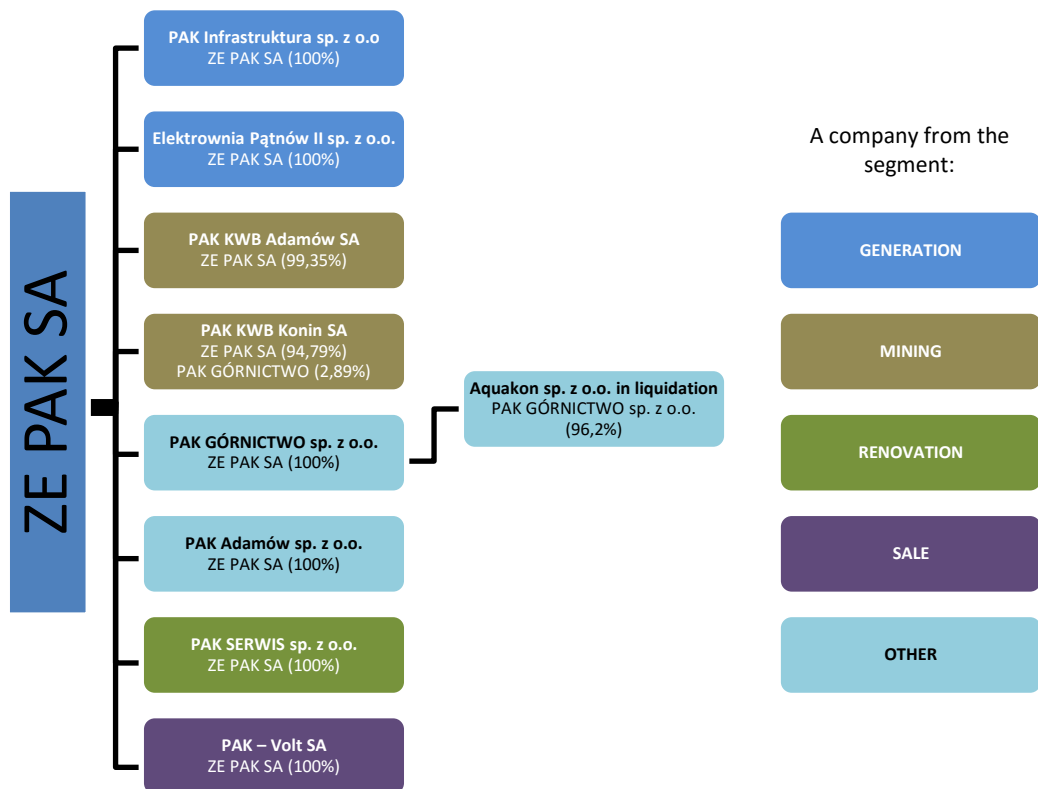


Table 1: Description of the Group's companies (excluding ZE PAK SA)

Entity	Registered office	Scope of operations	Group's share in the capital in %	
			30.06.2019	31.12.2018
„Elektrownia Pątnów II” sp. z o.o.	62-510 Konin ul. Kazimierska 45	Electric Energy production and distribution	100,00%*	100,00%*
PAK Kopalnia Węgla Brunatnego Konin SA	62-540 Kleczew ul. 600-lecia 9	Lignite extraction	97,68%*	97,68%*
PAK Kopalnia Węgla Brunatnego Adamów SA	62-700 Turek Warenka 23	Lignite extraction	99,35%	99,35%
Przedsiębiorstwo Remontowe „PAK SERWIS” sp. z o.o.	62-510 Konin ul. Przemysłowa 158	Construction and repair services	100,00%	100,00%
„PAK GÓRNICTWO” sp. z o.o.	62-510 Konin ul. Kazimierska 45	Rail transport services, vulcanization services (conveyor belts), electrical services, drilling, mining, mechanical and reclamation services, repair and assembly services of equipment,	100,00%	100,00%
PAK – Volt SA	00-834 Warszawa ul. Pańska 77/79	Trade of electricity	100,00%	100,00%
„PAK Infrastruktura” sp. z o.o.	62-510 Konin ul. Kazimierska 45	General construction of engineering objects, not classified elsewhere	100,00%	100,00%
PAK Adamów sp. z o.o.	62-510 Konin ul. Kazimierska 45	Buying and selling real estate	100,00%	100,00%
„Aquakon” sp. z o.o. in liquidation	62-610 Sompolno Police	In liquidation	96,2%*	96,2%*

* Entities with partial or total indirect share via other companies from ZE PAK Group

2.3. Composition of the Management Board

2019 financial year began in the following composition:

- 1) Adam Kłapszta – President of the Board,
- 2) Aneta Lato-Żuchowska – Vice-President of the Board,
- 3) Zygmunt Artwik – Vice-President of the Board,
- 4) Elżbieta Niebisz – Vice-President of the Board,
- 5) Marcin Ginel – Vice-President of the Board.

On January 10th, 2019 Mr. Adam Kłapszta resigned from the membership in the Management Board and performing the position of the President of the Management Board. Ms. Elżbieta Niebisz also ceased to be a Member of the Management Board of the Company, who also resigned from the position of Vice President of the Management Board on January 10th 2019. In this situation, at the meeting held on January 10th, 2019, until the election of the new President of the Company's Management Board, the Supervisory Board entrusted the management of the Company as acting President of the Management Board to Mr. Marcin Ginel - Vice-President of the Management Board. During the same meeting, i.e. January 10, 2019, the Supervisory Board of the Company appointed Mr. Paweł Markowski as the Vice-President of the Management Board.

On April 12th, 2019 Mr. Marcin Ginel resigned from the membership in the Management Board and performing the position of the Vice President acting President of the Management Board. The same day the resignation from membership in the Management Board and the function of the Vice President was also submitted by Ms. Aneta Lato-Żuchowska. At the meeting held on April 12, 2019, the Supervisory Board of the Company, acting pursuant to art. 383 § 1 of the Code of Commercial Companies delegated a member of the Company's Supervisory Board – Mr. Henryk Sobierajski, for a period of three months to temporarily perform the duties of a Member of the Management Board, entrusting him with the duties of the President of the Management Board.

On May 10, 2019, the Company's Supervisory Board appointed Mr. Paweł Lisowski as the Vice President of the Management Board.

At the meeting on July 2, 2019, the Company's Supervisory Board, acting pursuant to art. 383 § 1 of the Code of Commercial Companies delegated a member of the Company's Supervisory Board - Mr. Henryk Sobierajski for a period of up to 3 months, to temporarily perform the duties of a Member of the Company's Management Board, entrusting him with the duties of the President of the Management Board. Also on July 2, 2019, the Company's Supervisory Board appointed Mr. Maciej Nietopiel to the Company's Management Board, entrusting him with the function of the Vice-President of the Management Board.

As of the date of publication of this report, the composition of the Company's Management Board is as follows:

- 1) Henryk Sobierajski – Member of the Supervisory Board of ZE PAK SA delegated to temporarily perform the duties of the President of the Management Board,
- 2) Zygmunt Artwik – Vice-President of the Board,
- 3) Paweł Markowski – Vice-President of the Board,
- 4) Paweł Lisowski – Vice-President of the Board,
- 5) Maciej Nietopiel – Vice-President of the Board.

2.4. Description of the changes in the Group's structure

In the first half of 2019 there were no significant changes in the structure of the Group.

3. SIGNIFICANT EVENTS AFFECTING THE GROUP'S ACTIVITY

3.1. Significant achievements and failures during the period covered by the report

Short description of the achieved financial results

In the first half of 2019, total sales revenues amounted to PLN 1 406 030 thousand and, compared to the first half of 2018, they increased by PLN 423 190 thousand, i.e. by 43.06%.

In the analysed half-year, compared to the same period last year, the Group increased its electricity sales from 4.27 TWh to 4,64 TWh, i.e. by 8.66%. The increase in sales was the result of a 54.57% increase in sales of energy from trading, sales of energy from own production dropped by 0.38 TWh, i.e. by 13.10%. The level of production was largely determined by the relationship between the price of energy on the spot market and the price of CO2 emission allowances. The net production volumes of individual Group power plants are presented in Figure 4. At the same time, in the first half of 2019, to PLN 269,15 / MWh, i.e. by 37.41%, the average obtained electricity sales price increased. The cumulative impact of both of the above-mentioned factors caused that revenues from the sale of electricity (less excise duty) amounted to PLN 1 231 699 thousand and compared to the first half of 2018 increased by PLN 398 596 thousand, i.e. by 47.84%.

In the first half of 2019, revenues in the amount of PLN 16 963 thousand were recognized as revenue from the price difference, constituting the difference between the revenues for electricity trading for the period from January 1, 2019 to June 30, 2019 realized by PAK - Volt SA for final recipients referred to in art. 5 paragraph 1 of the Act of 28 December 2018 amending the Act on excise tax and certain other acts, determined on the basis of a volume-weighted average price of electricity on the wholesale market plus other unit costs, and the amount of revenues resulting from the application of electricity prices applicable on 30 June 2018 year. For payment of the above mentioned amount of the price difference PAK - Volt SA will submit an application to Zarządca Rozliczeń SA.

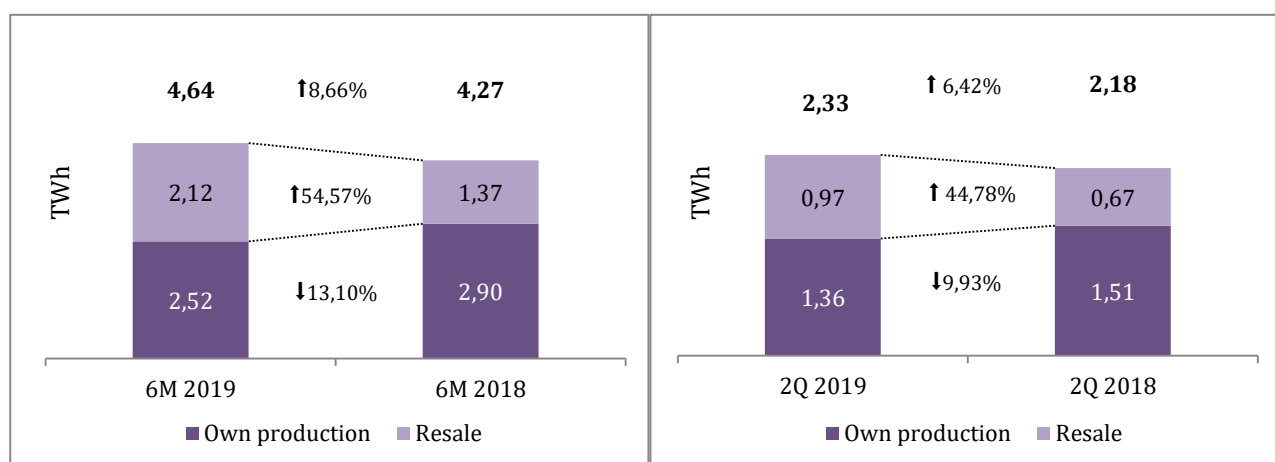
In the first half of 2019, compared to the first half of 2018, revenues from the sale of property rights from certificates of origin for energy increased by PLN 16,626 thousand, i.e. nearly three times. Such high growth dynamics is the effect of the low base from the previous year, when the Company adapted the biomass unit at the Konin power plant to the needs of heat production. However, in the first half of 2019, the biomass block produced energy continuously and the Company generated revenues from green and red certificates.

Revenues from the termination of PPAs (long-term contract for the sale of power and electricity) in the first half of 2019 amounted to PLN 61 125 thousand (including advance payment of PLN 48 371 thousand and correction of PLN 12 754 thousand), while in the first half of 2018 they amounted to 72 502 thousand PLN (including advance payment of PLN 47 443 thousand and adjustment of PLN 25 059 thousand). In both periods, the advances were at a comparable level, but there was a difference in the amount of adjustments - the adjustment for the first half of 2019 is much lower compared to the comparable period of 2018. The main reason for the lower adjustment was the achievement by Elektrownia Pańków II sp.z o.o. higher revenues, for which a constant high price of energy sales in the first half of 2019 was obtained compared to the comparable period of 2018.

Revenues from construction services contracts in the first half of 2019 compared to revenues obtained in the same period of the previous year decreased by PLN 3 862 thousand, i.e. by 10.91%. The decrease in revenues in the analysed period was associated with the implementation of less cost-intensive project phases for external customers by a company from the renovation segment PAK Serwis sp.z o.o.

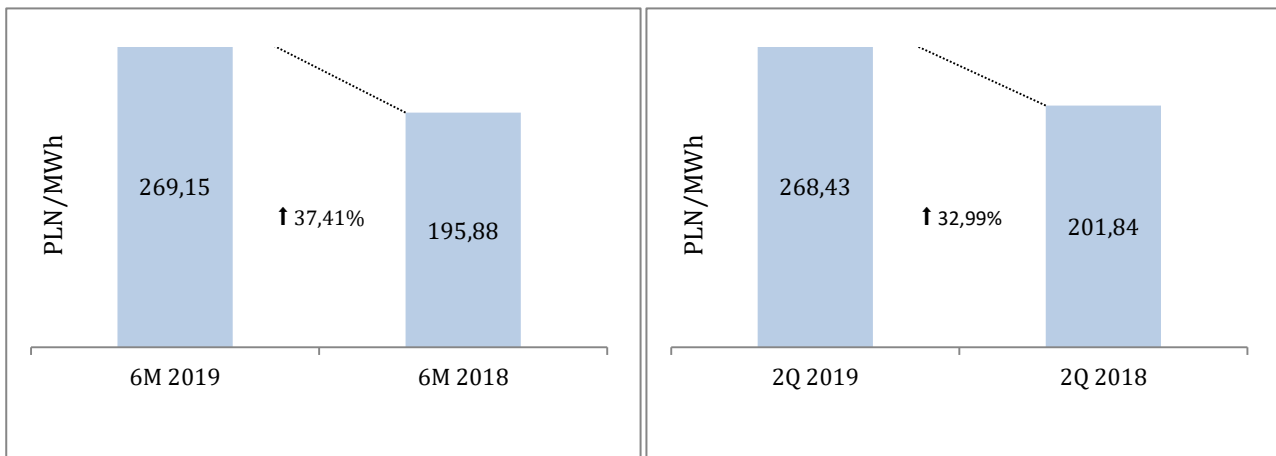
Revenues from the sale of heat in the first half of 2019 were higher than those obtained in the first half of 2018 by PLN 6 216 thousand, i.e. 33.02%. The increase in revenues from the sale of heat resulted from the higher sale price compared to the same period of the previous year.

Chart 1: Electricity sale



Source: Internal data

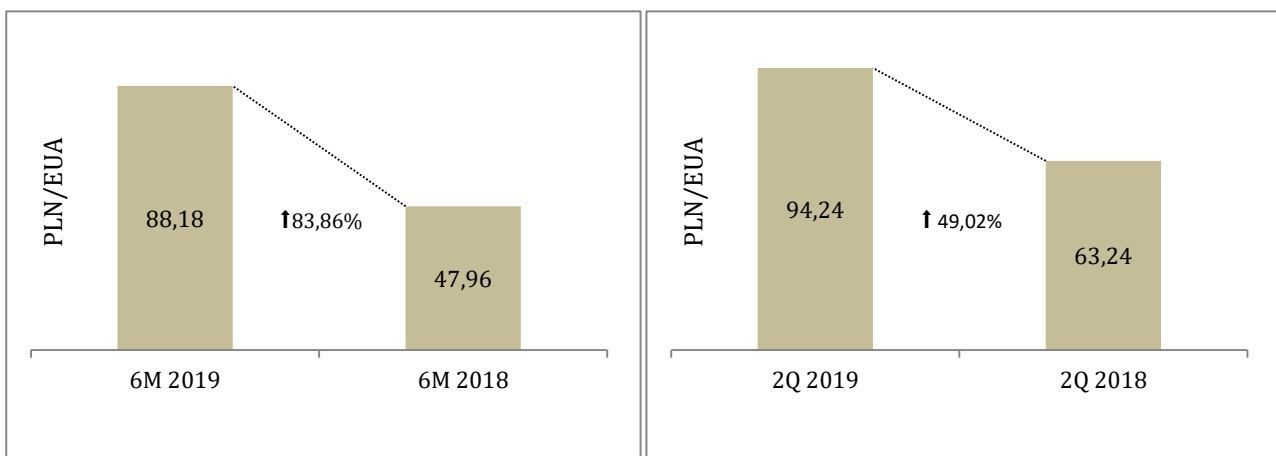
Chart 2: Average electricity prices*



* Average price, calculated as electricity sales revenues (own production, from resale and system service) divided by sales volume.

Source: Internal data

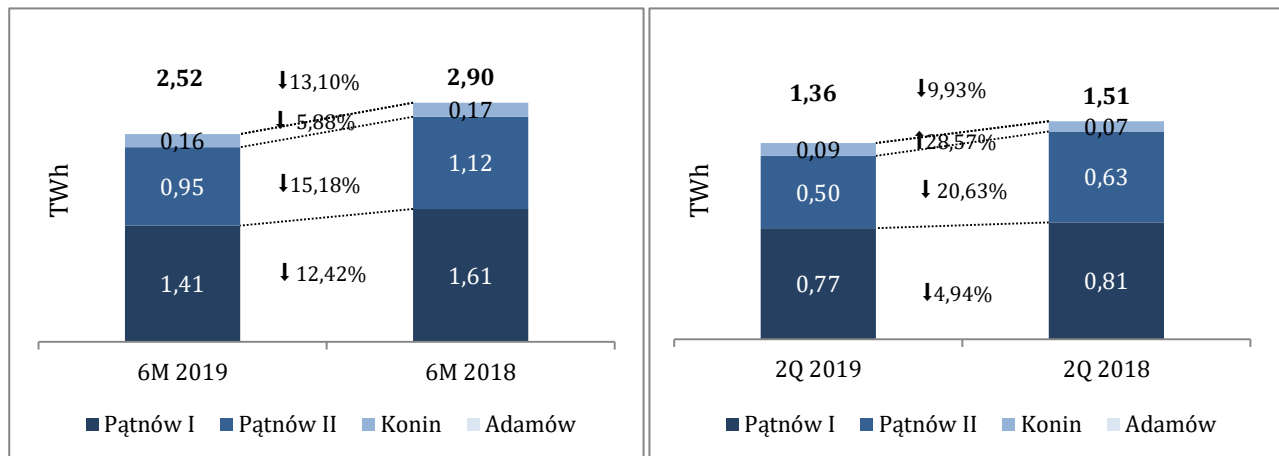
Chart 3: Average prices of CO₂ emission allowances purchase*(EUA)



* Average price calculated as the costs of purchasing emission allowances incurred to cover emissions for a given period divided by the volume of CO₂ emissions..

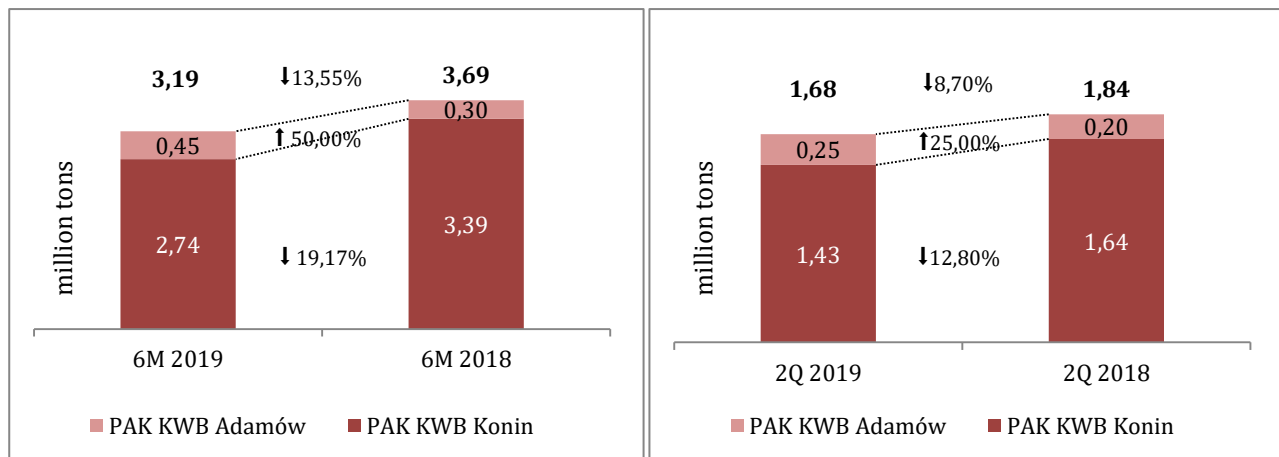
Source: Internal data

Chart 4: Net electricity production



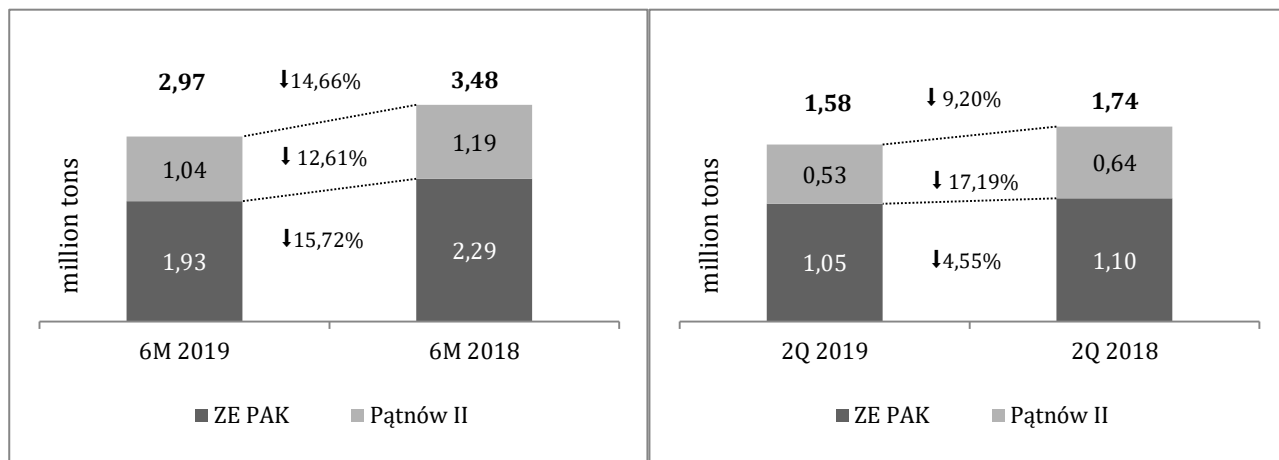
Source: Internal data

Chart 5: Lignite consumption



Source: Internal data

Chart 6: CO₂ emission



Source: Internal data

Table 2: List of consolidated sale revenues

	PLN thousand 6 months period ended 30 June 2019	PLN thousand 6 months period ended 30 June 2018	PLN thousand change	%
				dynamics
Revenues from the sales of electricity (reduced by excise duty)	711 131	570 406	140 725	24,67
Revenues from sales of traded electricity	520 568	262 697	257 871	98,16
Revenues from the price difference amount	16 963	-	16 963	-
Property rights on energy certificates of origin	25 820	9 194	16 626	180,84
Revenues from contracts for construction services	31 538	35 400	(3 862)	(10,91)
Compensation for termination of long-term contracts	61 125	72 502	(11 377)	(15,69)
Revenues from sales of heat	25 043	18 827	6 216	33,02
Other sales revenues	13 842	13 814	28	0,20
Total sales revenues	1 406 030	982 840	423 190	43,06

Table 3: Selected items of the consolidated income statement

	PLN thousand 6 months period ended 30 June 2019	PLN thousand 6 months period ended 30 June 2018	PLN thousand change	%
				dynamics
Sales revenues	1 406 030	982 840	423 190	43,06
Prime cost	(1 288 495)	(941 939)	346 556	36,79
Gross sales profit (loss)	117 535	40 901	76 634	187,36
Other operating revenues	13 078	4 166	8 912	213,92
Cost of sales	(2 683)	(2 042)	641	31,39
General and administrative expenses	(55 253)	(64 792)	(9 539)	(14,72)
Other operating costs	(6 333)	(2 870)	3 463	120,66
Profit (loss) from operating activities	66 344	(24 637)	90 981	-
Financial revenues	8 058	5 530	2 528	45,71
Financial costs	(13 030)	(25 488)	(12 458)	(48,88)
Gross profit (loss)	61 372	(44 595)	105 967	-
Income tax (tax load)	(24 676)	(7 417)	17 259	232,70
Net profit (loss)	36 696	(52 012)	88 708	-
Net other comprehensive income	(242)	845	(1 087)	-
Comprehensive income	36 454	(51 167)	87 621	-
EBITDA*	163 132	71 496	91 636	128,17

* The Company defines and calculates EBITDA as the profit/(loss) on operating activities (calculated as the net profit/(loss) for the accounting year corrected by the (i) income tax (tax load), (ii) financial revenues, as well as (iii) financial costs) corrected by the depreciation (shown in the income statement), as well as impairment write-downs against tangible assets, intangible assets, and mining assets.

The cost of sales in the first half of 2019 amounted to PLN 1 288 495 thousand and increased by PLN 346 556 thousand, i.e. by 36.79% compared to the cost incurred in the first half of 2018. Higher CO2 emission costs contributed the most to the increase in own costs. The increase in issue costs by PLN 95 386 thousand resulted from the increase in the price of acquired emission allowances. The unit price of allowances acquired in the first half of 2019 was PLN 88.18 / EUA, which means an increase of 83.86% compared to the same period of 2018. Higher material costs result from higher biomass costs. In the first half of 2018, the situation regarding biomass costs was different because in the first quarter the reconstruction of the biomass block at the Konin power plant for heat production was being completed, hence the biomass costs incurred in the first quarter of last year were mostly qualified in investment outlays. The increase in material consumption costs would have been higher were it not for the reduction of electricity consumption costs in mines in the amount of PLN 13,841 thousand as a result of applying energy prices in force on June 30, 2018. The higher volume of purchased electricity intended for trading, as well as its higher price, contributed to the increase in

the value of goods and materials sold. Higher taxes and fees mean higher fees in the mines for the use of land excluded from forestry and agricultural production. In turn, the lower cost of sales was mainly affected by lower employee benefits costs associated with a decrease in average employment. Lower costs of external services relate to the largest extent to the services of subcontractors ordered by a company from the renovation segment PAK Serwis sp.z o.o. in connection with ongoing orders.

Table 4: Consolidated costs by type

	<i>PLN thousand</i> <i>6 months period</i> <i>ended</i> <i>30 June 2019</i>	<i>PLN thousand</i> <i>6 months period</i> <i>ended</i> <i>30 June 2018</i>	<i>PLN thousand</i> <i>change</i>	<i>%</i> <i>dynamics</i>
Depreciation	97 072	96 135	937	(0,97)
Impairment write-downs on fixed assets	(284)	(2)	(282)	14 100,00
Impairment write-downs on inventory	1 168	111	1 057	952,25
Consumption of materials	152 281	139 154	13 127	9,43
Outsourcing	43 146	45 863	(2 717)	(5,92)
Taxes and fees excluding excise tax	85 093	76 365	8 728	11,43
Costs of CO ₂ emissions	261 555	166 169	95 386	57,40
Costs of employee benefits	215 282	225 202	(9 920)	(4,40)
Other costs by type	14 273	20 170	(5 897)	(29,24)
Value of sold goods and materials and sold traded electricity	489 055	253 318	235 737	93,06
Total costs by type	1 358 641	1 022 485	336 156	32,88

Other operating revenues in the first half of 2019 amounted to PLN 13 078 thousand and were PLN 8 912 thousand higher than those generated in the same period last year. Higher revenues were made up of released provisions for certificates of origin, compensation received from contractors and realized gains on the sale of CO₂ emission allowances and non-financial fixed assets.

Selling expenses in the first half of 2019 amounted to PLN 2 683 thousand and were PLN 641 thousand higher than those obtained in the same period last year.

General and administrative expenses in the first half of 2019 amounted to PLN 55 253 thousand and were lower than those incurred in the same half of last year by PLN 9 539 thousand, i.e. 14.72%. Lower employee costs mainly contributed to the decline.

Other operating expenses in the reporting half-year amounted to PLN 6 333 thousand and increased compared to the first half of the previous year by PLN 3 463 thousand. The increase in other operating costs is associated with the need to pay fines to contractors in connection with the construction and assembly work carried out.

In the first half of 2019, ZE PAK SA Group obtained operating profit of PLN 66 344 thousand. In the same period last year, a loss of PLN 24 637 thousand was recorded.

In the first half of 2019, the results achieved were negatively affected by a negative financial result of PLN 4 972 thousand. The impact of financial activities in the same period last year reduced the result by PLN 19 958 thousand. The difference in the result on financial activities in both compared periods results from both higher financial revenues and lower financial costs. The increase in financial revenues in the first half of 2019 was due to the situation on the energy market, which allowed for the recognition of the effect of reversal of provisions for contracts for energy supply contracts at PAK - Volt SA. On the other hand, lower financial costs resulted primarily from a better exchange rate situation (in the first half of 2019 there was a slight decrease in the EUR / PLN exchange rate, while in the corresponding period of last year there was a significant weakening of zloty against euro) and lower interest on financial liabilities.

Gross profit in the first half of 2019 amounted to PLN 61 372 thousand, compared to the gross loss recorded in the first half of 2018.

Net profit in the first half of 2019 amounted to PLN 36 696 thousand, compared to the net loss for the first half of 2018 at PLN 52 012 thousand.

The description of factors and events, especially unusual events substantially affecting the assets, liabilities, capital, net financial result or cash flow

In the first half of 2019, no unusual events were noted that had a significant impact on assets, liabilities, equity, net financial result or cash flows.

Implementation of investment projects

In the period from January 1 to June 30, 2019, the Group's capital expenditure was PLN 16 902 thousand.

At present, ZE PAK SA Group does not implement large investment projects. Investment activity in the generation segment focuses on the implementation of the necessary tasks to ensure the maintenance of current efficiency and a more effective use of owned generation assets.

As part of new ventures, in the first stage of the procedure, great emphasis was placed on the preparation of two investment tasks:

1. Adaptation of the K7 coal boiler at Konin power plant for the exclusive combustion of biomass together with the necessary technical infrastructure.
2. Construction of a solar farm with the capacity of 70 MWp on reclaimed land in the area of Brudzew commune.

The planned adaptation of the K7 boiler for the exclusive combustion of biomass will include the following main systems: the boiler, biomass feeding system, electrostatic precipitator, ash removal and generator. After the reconstruction, the system will produce electricity for the needs of the National Power System and will be a reserve in the event of a breakdown or renovation of the existing biomass unit producing heat for the city of Konin. After K7 boiler has been adapted for biomass combustion, the coal installations at Konin power plant will be completely decommissioned.

As part of the work on the project of adapting the K7 boiler for the exclusive combustion of biomass, in November 2018 an application was submitted for funding the project from the National Fund for Environmental Protection and Water Management and the concept of modernization was developed along with the necessary technical infrastructure. On July 17, 2019, the final environmental decision was obtained. At the end of July this year, tender procedures were gradually started for the selection of contractors for individual sub-tasks related to the adaptation of the K7 boiler for the exclusive combustion of biomass.

The planned solar farm will be located in the post-mining areas of PAK KWB Adamów located in Brudzew commune. Power output from the solar farm will be implemented through the existing Main Power Point, which will be rebuilt.

As part of the work on the solar farm construction project, in November 2018 an application was submitted for funding the project from the National Fund for Environmental Protection and Water Management and a concept for the construction of a solar farm with a capacity of about 70 MWp was developed. On July 17, 2019, the final environmental decision was obtained, and on August 7, 2019, an application was submitted to Brudzew Commune Office for determining the building conditions for the construction of a solar farm.

In the mining segment, the mines belonging to the Capital Group carried out investment tasks on active opencasts aimed at maintaining production capacity.

3.2. Other significant events of the reporting period, events after the balance sheet date and other information which are relevant for the assessment of the human resources, property, financial situation and ability of the Company and the Group to fulfil its obligations

Non-revolving loan agreement for financing the activities of PAK KWB Konin SA

Due to the repayment date on July 26, 2019 of overdraft in the amount of PLN 66 700 thousand granted to PAK KWB Konin SA by Alior Bank SA on November 20, 2013, PAK KWB Konin SA signed an agreement on July 25, 2019 of non-revolving loan in the amount of PLN 66 700 thousand with Alior Bank SA for the repayment of the previous loan and further financing of the company's current operations. Non-revolving loan bears interest according to WIBOR 3M rate increased by the bank's margin. The loan will be repaid in monthly instalments, the final repayment date is December 15, 2021.

Tender Offer for the sale of shares of ZE PAK SA

On 30 July 2019 Argumenol Investment Company Limited announced a Tender Offer for the sale of ZE PAK SA shares. The subject of the tender offer is 34 823241 ordinary bearer shares of the Company with a nominal value of PLN 2.00 each.

The shares, being the subject of the tender offer jointly represent approx. 68.52% of the share capital of the Company and entitle to 34 823 241 votes at the General Meeting of the Company, which corresponds to approx. 68.52% of votes at the General Meeting of the Company.

The Offeror has not specified the minimum number of shares covered by subscriptions, after reaching which the Offeror will be required to purchase these shares. The shares covered by the Tender Offer will be purchased at the price of PLN 7.47 for each of the shares.

Enrolment has started on August 20 and end on September 19, 2019. The expected date of the share purchase transaction is September 24, and the transaction will be settled on September 27.

On August 7, 2019, the Management Board of ZE PAK SA, in current report No. 24/2019, presented its position regarding the announced tender offer for the sale of shares. For the purpose of preparing this position, the Management Board has analysed the tender offer document, market prices of the Company's shares for the 6 and 3 months preceding the announcement of the Tender Offer, publicly available information on current valuations of the Company and other industry companies and publicly available financial and operational information about the Company and its Capital Group, including in particular the data contained in the consolidated and separate financial statements.

When preparing this position, the Management Board of the Company was also guided by its knowledge of the industry, the development prospects and major challenges currently facing companies operating in the lignite electricity generation sector.

The Management Board of the Company expressed the view that, in principle, increasing the involvement of a strategic investor in the Company's shareholding can positively affect its interest by willingness to contribute to its development. The Management Board of the Company was not able to precisely define the strategic plans of the offeror. The tender offeror does not include information on the impact of the tender offer on the employment status of the Company, therefore, the Company's Management Board was not able to assess the impact of the tender offer on employment.

Regarding the price per share of the Company proposed in the tender offer, the Management Board stated that in its opinion the price proposed in the tender offer falls within the estimated range of the fair value of the Company's shares.

Conclusion of an agreement for the supply of heat to the city of Konin

On September 6, 2019 the Company signed an agreement with Miejskie Przedsiębiorstwo Energetyki Ciepłej - Konin Sp. z o.o. ("MPEC"), the subject of which is the sale of heat to the City of Konin with the commencement of deliveries from July 1, 2022. The agreement has been concluded for a definite period and is valid until June 30, 2032.

Heat, which is the subject of sale to MPEC Konin, is currently, based on an existing contract, generated by ZE PAK SA in a dedicated biomass combustion installation that is a cogeneration unit, which currently has the status of an installation generating heat from renewable energy sources. The heat sale prices used by ZE PAK SA result from the tariff in force for a given year, which is subject to approval by the President of the Energy Regulatory Office.

The agreement is a continuation of existing cooperation in the field of heat supply for the city of Konin.

4. INFORMATION ON SIGNIFICANT PROCEEDINGS PENDING BEFORE A COURT, A BODY COMPETENT FOR ARBITRATION PROCEEDINGS OR A PUBLIC ADMINISTRATION BODY RELATED TO ZE PAK SA OR SUBSIDIARIES CONSOLIDATED UNDER THE GROUP

Zespół Elektrowni Państw - Adamów - Konin SA and the companies consolidated within the Group were not a party in proceedings pending before court, competent arbitration authority or public administration authority in the first half of 2019, whose single or total value would exceed 10% of ZE PAK SA's equity with the exception of those described below.

Proceedings on the refund of excise duty overpayment

In light of the regulations mandatory within the European Union, especially regulations of Article 21 paragraph 5 of the Energy Directive, in relation to Article 6 paragraph 1 of the Horizontal Directive, after 1 January 2006, the object of excise tax is sale of energy at the last stage of trade, i.e. sale by the distributor to the final recipient (consumer).

Taxation with this tax does not cover an earlier stage of trade, e.g. between the producer of electricity and its distributor. In this case, the tax obligation arises at the time of supply of electricity to the consumer.

As at 1 March 2009, the Act of 6 December 2008 on excise duty entered into force, according to which the sale of electricity to an entity which is not its final customer is not subject to excise duty.

Due to the above fact, pursuant to Article 75 § 1, in relation to Article 75 § 2 of the Act of 29 August 1997 – Tax Ordinance, ZE PAK SA submitted applications for stating overpayment of the excise tax for 2006, 2007, 2008, as well as January and February 2009 for the total amount of PLN 626 million, with the justification that pursuant to the regulations of the EU law and the judicial decisions of the Provincial Administrative Courts, the activities executed by ZE PAK SA are not subject to the excise tax. Particular applications were recognised at the following levels: the Customs Office in Kalisz, the Customs Chamber in Poznań, and, currently, the Provincial Administrative Court in Poznań („PAC”), as well as the Supreme Administrative Court. Due to the position of judicature presented in the course of court proceedings, the amount of overpayment, the repayment of which the Company submits, has been reduced to the amount of damages caused by economic analyses, i.e. currently up to the amount of approximately PLN 108 million.

Moreover, in association with the rulings of the Administrative Courts regarding other power companies, in the subject of overpaid excise duty and the resolution I GPS 1/11 of the National Administrative Court („NSA”) of 22 June 2011 (where the NSA ruled that transferring the tax load in price, excludes the possibility to return the overpayment), notwithstanding the ongoing administrative proceedings, on 10 February 2012, the Company initiated a civil-law proceedings, filing an application to summon the State Treasury to a conciliation hearing regarding the amount of PLN 626 406 thousand, to the District Court Warszawa Śródmieście. A conciliatory settlement was not reached since during the hearing of 16 April 2012, the representatives of the Treasury did not agree to settle.

Simultaneously, the Company, waiting for the results of the tax proceedings regarding the previously submitted application for overpayment, submitted in writing, on 14 September 2012, in the Customs Chamber in Poznań, additional explanations in the form of results of a detailed economic analysis, the purpose of which was to demonstrate whether the Company suffered loss related to the payment of excise tax to which it was not obliged. The Company's opinion is that the submitted document also applies to other overpayment applications from the entire period embraced by the proceedings, i.e. between January 2006 and February 2009. Ultimately, all applications were included in the cause lists of the Provincial Administrative Court (WSA) and the Supreme Administrative Court (NSA). As of the date of development of this statement, the status of the proceeding is as follows:

- Twenty two cases for the period of January 2006 – November 2007 (excluding November 2006) were conducted again from the start by the Head of the Customs Office, after the cases returned from the Supreme Administrative Court. The Company submitted monthly economic analyses of suffering the prejudice. After the negative decisions of the Head of the Customs Office and then of the Head of Customs Chamber, complaints were submitted to the Provincial Administrative Court in Poznań, Hearings before the Provincial Administrative Court in Poznań took place on 4 and 18 November 2015. In all cases, negative judgements for the Company were issued. In February 2016, the Company submitted cassation appeals to the Supreme Administrative Court. Currently, the Company is expecting the determination of hearing dates before the Supreme Administrative Court, The Supreme Administrative Court dismissed the Company's cassation appeals in the abovementioned 22 cases at the hearings held on April 10 and 11, 2018.
- 14 proceedings for the period of December 2007 – February 2009 (excluding July 2008) on 26 January 2017, hearings took place before the Provincial Administrative Court in Poznań. In all the cases, the Company's appeals against the Customs Chamber in Poznań were dismissed. The Company submitted applications for a written justification of the judgement, which were obtained on 7 March 2017, to the Provincial Administrative Court. After analysing the justifications for the judgments on April 6, 2017, the Company submitted 14 cassation appeals to the Supreme Administrative Court. Currently, the Company is awaiting the appointment of court hearings before the Supreme Administrative Court.
- the proceeding for November 2006 was concluded with a negative judgement of the Supreme Administrative Court of 8 December 2011.
- the proceeding for July 2008 reached the recognition of our cassation appeal by the Supreme Administrative Court. On the hearing on 29 April 2015, the Supreme Administrative Court dismissed the Company's cassation appeal and pointed out that it fully agrees with the Provincial Administrative Court in Poznań in the judgement, against which the cassation appeal was submitted.

Notwithstanding the foregoing proceedings, ZE PAK SA lodged a complaint against the actions of the Polish authorities to the European Commission („EC”), pursuant to art. 258 of the Treaty on the Functioning of the European Union. The opinion issued by the EC may oblige the Polish tax authorities to pass a ruling beneficial to ZE PAK SA.

On 21 March 2017, ZE PAK SA received a “pre-closure letter” from the EC, which initially denied the relevance of ZE PAK SA’s position, however, at the same time giving the right to a second comment on the subject, which ZE PAK SA exercised. On 9 June 2017, a letter summarising the reasoning of ZE PAK SA, in terms of the overpaid excise tax. As a result of the consideration of the arguments raised in the said letter, the EC took the position in which it stated that the arguments invoked by ZE PAK SA did not contain grounds for the Commission to take any action, therefore the procedure regarding the complaint of ZE PAK SA against the activities of Polish authorities would be closed.

In case of the Elektrownia Pańków II sp. z o.o., the proceedings for all periods (one case) were included in the cause lists of the Provincial Administrative Court after a negative decision of the Head of Customs Chamber. The aforementioned company does not have access to comparative analyses of suffering the prejudice. On 4 November 2015, a hearing in the Provincial Administrative Court in Poznań took place. On November 18, 2015, a negative judgment was announced, from which the company on February 8, 2016 filed a cassation complaint to the Supreme Administrative Court. The Supreme Administrative Court dismissed the Company's cassation complaint at the hearing held on April 11, 2018.

Proceedings on an environmental decision issued to PAK KWB Konin SA concerning lignite deposit in Tomisławice

PAK KWB Konin SA is a party in the administrative proceedings related to the environmental decision regarding the lignite deposit in Tomisławice. On 7 August 2007, the Head of Wierzbinek Commune issued an environmental decision regarding the lignite open cast. On 5 December 2008, this decision was contested by nine physical persons supported by the Greenpeace organisation due to alleged major infringement of the regulations of the law. On 25 March 2009, the Self-government Appeal Court dismissed the application to reverse the environmental decision. The plaintiffs applied for the judicial review. On 4 May 2009, after the judicial review, the Self-government Appeal Court sustained its previous decision. The plaintiffs again appealed against the environmental decision. On 5 May 2010, the Provincial Administrative Court in Poznań ruled that the environmental decision, pursuant to which the license for the extraction of lignite at the Tomisławice deposit was granted, infringes the regulations of the law in a major manner. PAK KWBK SA and the Self-government Appeal Court submitted an appeal against this judgement. On 21 March 2012, the Supreme Administrative Court overturned the contested decision of the Provincial Administrative Court in Poznań and referred the matter for reconsideration. On 6 November 2012, the Provincial Administrative Court in Poznań announced the decision repealing the decision of the Self-government Appeal Court of 25 March 2009 refusing to declare the invalidity of the environmental decision issued on 7 August 2007 by the Head of Wierzbinek Commune, related to the extraction of lignite from the Tomisławice open pit by PAK KWBK SA. On 7 January 2013, PAK KWBK Konin SA submitted a cassation appeal from the described decision.

After the review on the hearing on 7 October 2014, the Supreme Administrative Court dismissed the cassation appeal of PAK Kopalnia Węgla Brunatnego Konin SA from the judgement of the Provincial Administrative Court in Poznań of 6 November 2012 repealing the decision of the Self-government Appeal Court in Konin of 25 March 2009 refusing the annulment of the environmental decision issued on 7 August 2007 by the Head of Wierzbinek Commune related to the extraction of lignite from Tomisławice open pit.

Dismissal of the cassation appeal of PAK Kopalnia Węgla Brunatnego Konin SA means that the judgement of the Provincial Administrative Court in Poznań of 6 November 2012 became legally binding and the case regarding the statement of invalidity of the environmental decision will be examined again by the Self-government Appeal Court. On 18th January 2019 the Local Government Appeal Court in Konin issued a decision refusing to annul the environmental decision issued on August 7, 2007 by the Head of Wierzbinek Commune related to the exploitation of Tomisławice lignite open pit.

The decision of the Local Government Appeal Court in Konin, means that the environmental decision issued by the Head of Wierzbinek Commune is still in legal circulation. The decision is not final. The opposite party has submitted an application for reconsideration of the case by the Local Government Appeal Court in Konin.

Proceedings on an environmental decision on lignite deposit in Ościsłowo

On 13 March 2017, PAK KWB Konin SA received the decision of the Regional Director for Environmental Protection in Poznań (“RDOŚ in Poznań”) of 10 March 2017, refusing the establishment of the environmental conditions for the investment titled: “Extraction of lignite and associated minerals from the Ościsłowo Open Pit.” The decision of RDOŚ in Poznań is not final. PAK KWB Konin SA appealed accordingly to the General Directorate for Environmental Protection in Warsaw. The appeal included a request to revoke the appealed ruling in its entirety and determine the environmental conditions for the execution of the above-mentioned project. On 30 November 2017, General Director of Environmental Protection in Warsaw has decided to repeal a decision in its entirety (contested by PAK KWB Konin SA - a subsidiary of the Company) of the Regional Director for Environmental Protection in Poznań (“RDOŚ in Poznań”).

dated March 10, 2017, refusing to specify environmental conditions for the project entitled: " Extraction of lignite and associated minerals from Ościsłowo Open Pit" and forward the case for reconsideration by RDOŚ in Poznań.

PAK KWB Konin SA, by letter of December 18, 2017 filed an objection against the abovementioned decision of GDOŚ in Warsaw to the Provincial Administrative Court in Warsaw (WSA). In the opinion of PAK KWB Konin S.A. there were grounds for issuing a reformatory decision by GDOŚ in Warsaw, i.e. amending the contested decision of RDOŚ in Poznań and substantive decision in this matter, not referring the matter for reconsideration. The other party also opposed the WSA. Both objections were dismissed by the WSA. The verdict was passed on March 1, 2018. On April 12, 2018, PAK KWB Konin SA filed a cassation complaint with the Supreme Administrative Court in Warsaw against the verdict of the WSA in Warsaw of 1 March 2018. This complaint was upheld and the case was re-examined by the Provincial Administrative Court in Warsaw, which in its judgment of 18 October 2018 overruled the decision of GDOŚ, which will again have to hear the appeals lodged in the present case.

Currently, the case is being reconsidered by GDOŚ in Warsaw, which in a letter of 6 March 2019 called on PAK KWB Konin SA to submit explanations and supplement the evidence within two months of receiving the request. By letter of April 12, 2019, PAK KWB Konin SA applied for extension of the deadline to September 30, 2019. In connection with the above, the General Director for Environmental Protection set a new deadline for settling the matter on September 30, 2019.

The proceedings for issuing the environmental decision were initiated on 16 September 2015.

5. INFORMATION REGARDING THE SHAREHOLDING STRUCTURE

Share capital of ZE PAK is represented by 50.823.547 shares. Shares are ordinary. Each share gives right to one vote at General Meeting of Shareholders.

5.1. Shareholders holding, either directly or indirectly through subsidiaries, at least 5% of the total number of votes

Table 4: List of shareholders holding, either directly or indirectly through subsidiaries, at least 5% of the total number of votes at the Company's General Meeting as of the date of submission of this report. The list made according to the information available to the Company on the basis of the submission of notifications on the acquisition / disposal of shares

<i>Shareholder</i>	<i>pcs</i> <i>Number of shares and</i> <i>corresponding number of</i> <i>votes at the General</i> <i>Meeting</i>	<i>%</i> <i>Share [%] in the</i> <i>total number of</i> <i>shares/votes</i>
Zygmunt Solorz (indirectly) through:	26 200 867	51,55
– <i>Elektrim SA</i>	<i>196 560</i>	<i>0,39</i>
– <i>Embud 2 sp. z o.o. S.K.A.</i>	<i>592 533</i>	<i>1,16</i>
– <i>Trigon XIX Fundusz Inwestycyjny Zamknięty</i>	<i>10 004 001</i>	<i>19,68</i>
– <i>Argumenol Investment Company Limited</i>	<i>15 407 773</i>	<i>30,32</i>
Nationale – Nederlanden OFE	4 503 242	8,86
OFE PZU „Złota Jesień”	4 635 719	9,12

The list of shareholders holding, directly or indirectly through subsidiaries, at least 5% of the total number of votes at the date of this quarterly report does not differ from the analogous list as of the date of publication of the latest periodic report.

On July 30, 2019, Argumenol Investment Company Limited announced a tender offer to sell the Company's shares. More information on the tender offer is provided in section 3.2 of this report.

5.2. List of the shareholding structure of the management and supervising personnel

Below there is the status of the Company's shares held by managing and supervising persons as at the date of submitting this half-year report and as at the day of submitting the previous periodic report (to the best of the Company's knowledge, based on notifications of purchase / sale of shares).

Table 5: Status of the Company's shares held by managing persons

Name	ZE PAK SA shares as at the day of submitting this report	ZE PAK SA shares as at the day of submitting the previous report
Henryk Sobierajski	0	0
Paweł Markowski	0	0
Zygmunt Artwik	0	0
Paweł Lisowski	0	1 430
Maciej Nietopiel	0	0

Table 6: Status of the Company's shares held by supervising persons

Name	ZE PAK SA shares as at the day of submitting this report	ZE PAK SA shares as at the day of submitting the previous report
Wojciech Piskorz	0	0
Wiesław Walendziak	0	0
Tomasz Szeląg	0	0
Henryk Sobierajski	0	0
Leszek Wysłocki	0	0
Sławomir Sykucki	0	0
Sławomir Zakrzewski	0	0
Piotr Stępnia	0	0
Grzegorz Krystek	0	0

6. OPINION OF THE MANAGEMENT BOARD ON THE POSSIBILITY OF EXECUTION OF FINANCIAL FORECASTS PUBLISHED EARLIER

Zespół Elektrowni Pątnów – Adamów – Konin SA has not published any financial forecasts.

7. INFORMATION REGARDING THE PAID OR DECLARED DIVIDENDS

The company did not pay or declare dividend payment in the first half of 2019.

8. INFORMATION ON THE CONCLUSION BY ZE PAK SA OR ENTITIES CONSOLIDATED UNDER THE GROUP OF SIGNIFICANT TRANSACTIONS WITH ENTITIES AFFILIATED PURSUANT TO CONDITIONS OTHER THAN MARKET CONDITIONS

Zespół Elektrowni Pątnów – Adamów – Konin SA and companies consolidated under the Group have not concluded transactions with entities affiliated pursuant to conditions other than market conditions in the first half of 2019.

9. INFORMATION ON GRANTING BY ZE PAK SA OR ENTITIES CONSOLIDATED UNDER THE GROUP OF SIGNIFICANT GUARANTEES, SURETIES, CREDITS OR LOANS

Zespół Elektrownia Pątnów - Adamów - Konin SA and subsidiaries consolidated within the Group did not grant guarantees, sureties or loans of significant value in the first half of 2019.

10. INFORMATION CONCERNING THE ISSUE, REDEMPTION, AND REPAYMENT OF NON-EQUITY AND CAPITAL SECURITIES

In the first half of 2019, the companies of ZE PAK SA Capital Group did not issue or buy out non-equity and equity securities.

11. FACTORS WHICH, IN THE MANAGEMENT BOARD'S OPINION, WILL AFFECT THE COMPANY'S RESULTS IN THE PERSPECTIVE OF AT LEAST ONE QUARTER

The process of forecasting future results of the ZE PAK Capital Group must include a wide range of factors occurring actually, potentially or theoretically, existent in the branch and markets in which the Company conducts its operations. These include both internal factors as well as factors with their source in the environment. In the view of the Board, they can be divided into factors which constantly influence the Group's functioning as well as those which appear incidentally in the period which is embraced by a given periodical report.

The most important factors which constantly affect the Company's results include the following:

- macro-economic trends in the Polish economy and the demand for electricity;
- regulatory environment;
- electricity prices;
- prices and supply of certificates of origin;
- fuel costs, coal extraction costs;
- CO₂ allowances costs;
- compensation for the stranded costs related to the termination of Elektrownia Państw II's LTC contract;
- seasonality and meteorological conditions;
- investment expenses, in particular those privileged to obtain CO₂ emission allowances free of charge;
- EUR/PLN exchange rate and interest rates level.

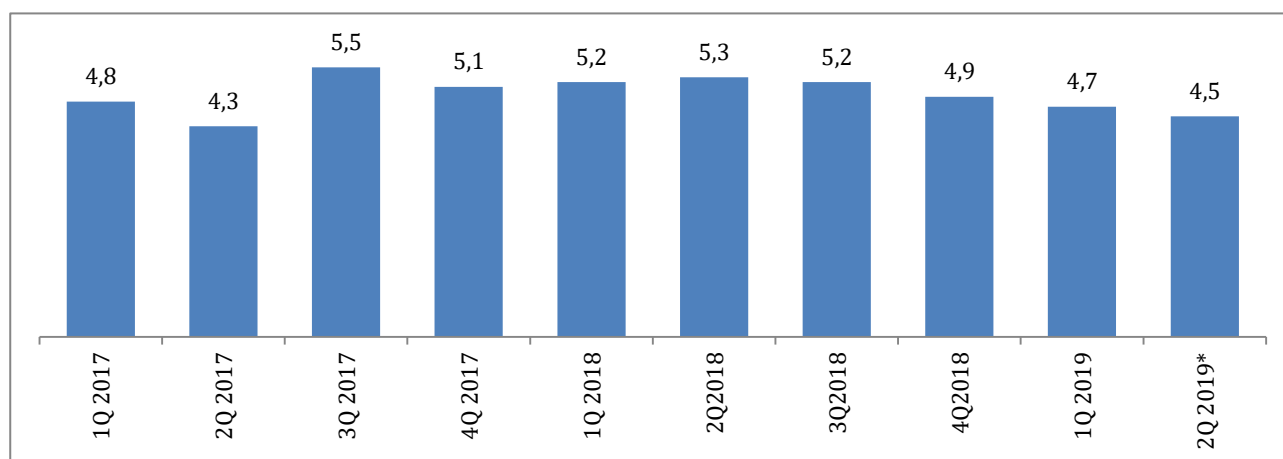
Furthermore, an important factor that could have a significant impact on the Company's financial results in the further quarters includes the value impairment test result. In accordance with IAS 36, the value impairment test of assets is carried out after the occurrence of certain conditions. The last such a test was carried out on 30 June 2019, and its result justified the write-down for asset components. It should be noted that the valuation model of the Company's assets shows sensitivity to a range of parameters, among others, the ones described in this section. Therefore, in the face of deterioration of the operational perspectives, both the market ones and those having its origin in the legal conditions, the assumptions for the valuation model of the Company's assets can change, and consequently the value impairment test result may cause the necessity of verifying the value of the write-downs against the asset components in the future. Another analysis of the reasons justifying the potential necessity to conduct the value impairment test of the Company's asset components will be executed at the end of the next reporting period.

11.1. Macro-economic trends in the Polish economy and the demand for electricity

When conducting activities within the territory of Poland and obtaining most revenues from the sale of electricity, it is necessary to take into consideration the macro-economic trends in the Polish economy. A very significant factor is the increase in the real GDP and industrial production in Poland, the development of the service sector as well as the increase in individual consumption. All of the aforementioned factors significantly affect the demand for electricity and its consumption.

Preliminary estimate of the Central Statistical Office for the growth of gross domestic product ("GDP") of Poland in the second quarter of 2019 was calculated at 4.5%, in the first quarter the growth dynamics was 4.7%. Compared to the value of dynamics recorded last year, they are slightly lower, but still compared to many of Poland's major European trade partners are still relatively high.

Chart 7: GDP dynamics (%) in relation to the analogous quarter of the previous year (yearly average fixed prices)

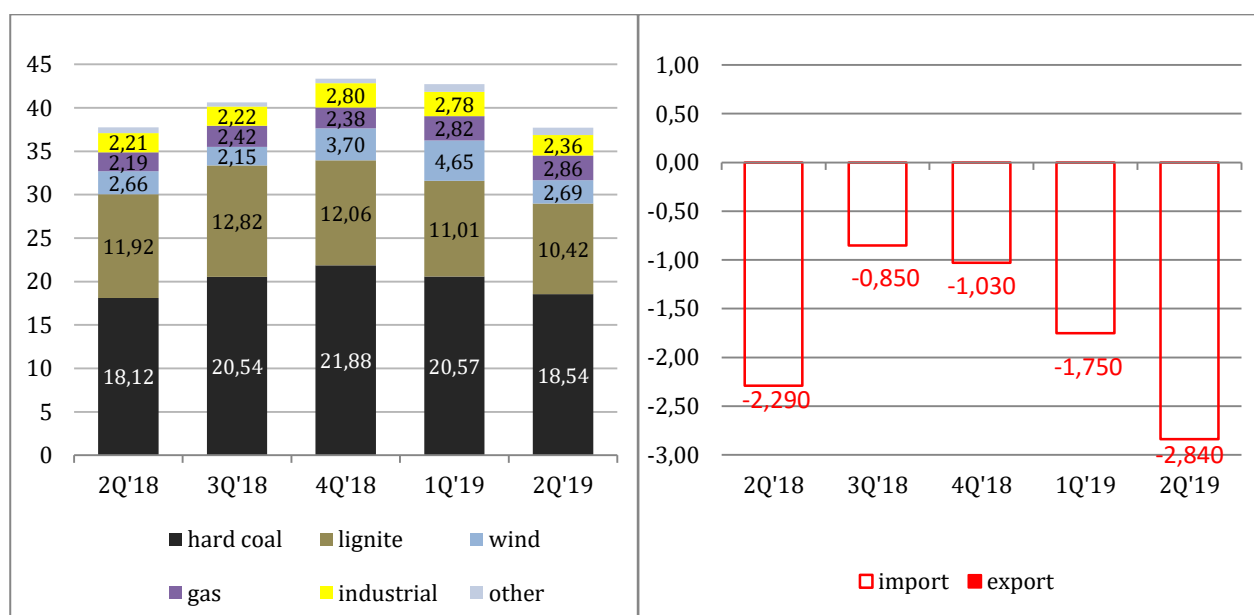


* The so-called preliminary estimate of gross domestic product in the second quarter of 2018, seasonally unadjusted, at constant average annual prices of the previous year.

Source: Own elaboration based on CSO Data

Consumption remained the main growth factor in the first half of 2019, mainly due to: low unemployment, fast wage growth and social transfer programs. GDP growth was also supported by investment growth. It is characteristic that despite the economic stagnation in the main trade partners (in the largest EU economies), the dynamics of economic growth in Poland is still relatively high.

Chart 8: Structure of electricity generation and the balance of the electricity exchange with foreign countries (gross amounts) – TWh



Source: Own elaboration based on PSE data

Data on the functioning of the National Power System and the Balancing Market, presented by Polskie Sieci Elektroenergetyczne SA, show that gross domestic electricity consumption in the first half of 2019 amounted to 85.03 TWh¹ and, compared to the first half of the previous year, it fell symbolically by 0.1%. In the first half of 2019, gross electricity production amounted to 80.44 TWh, which means a decrease by 1.0% compared to the same period of the

¹ Table 3. Structure of electricity production in domestic power plants, the volume of electricity exchange with foreign countries and national energy consumption - monthly values and from the beginning of the year - gross value.

previous year. Coal-fired power plants had the largest share in the production structure, production from hard coal amounted to 39.11 TWh. 21.43 TWh was produced from lignite. Wind farms produced 7.34 TWh. The foreign exchange balance in the first half of 2019 amounted to 4.59 TWh on the import side.

11.2. Regulatory environment

Entities operating on the electricity market are subject to strict regulations, such as the Energy Law, the Act on Renewable Energy Sources ("RES"), provisions on the public sale of part of the energy produced, as well as support for specific energy production technologies, as well as regulations and directives of European Commission and international conventions concerning, inter alia, environmental protection and climate change (including CO₂ emissions). Account should also be taken of tax law provisions and interpretations and recommendations issued by the Energy Regulatory Office. Any changes in the described areas may be of great importance for the Group's operations. Any changes in the described areas may be of key importance for the Group's operations. Regulatory risk is one of the most important electricity generators in the industry.

On June 5, 2019, the European Parliament and the Council of the European Union adopted a regulation on the internal market in electricity (No. 2019/943), which will apply from January 1, 2020. The provisions of this regulation introduce rules regarding the design of capacity mechanisms. Article 22 (4) includes provisions stating that new installations where emissions exceed 550 grams CO₂ per kilowatt hour (kWh) from fossil fuels will not be able to benefit from state support within the capacity market after July 1, 2025. On the other hand, existing power plants emitting more than 550 grams of CO₂ per kWh and more than 350 kg of CO₂ per year on average for each installed kW of power will be able to participate in these mechanisms until July 1, 2025. Capacity contracts, which will be signed within the capacity market by the end of 2019, will be removed from the regulatory restrictions.

On August 2, 2019, the ordinance of the Minister of Energy on the parameters of the main auction for the year of delivery 2024 and the parameters of additional auctions for the year of delivery 2021 (item 1457), specifying the conditions of participation in the main auction for 2024 and additional auctions for 2021, was published. This regulation lowered the investment expenditure threshold required to conclude a multi-year contract and maximum prices for existing, new and modernized entities.

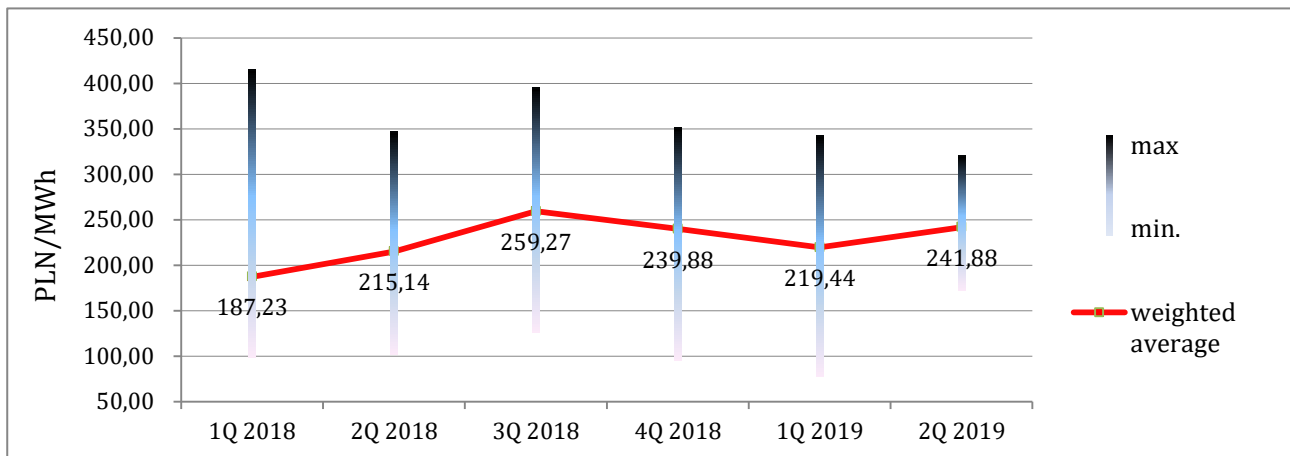
On August 14, 2019, in the Journal of Laws under item 1524 an act was amended to amend the act on renewable energy sources and certain other acts, which contained the amount of energy and value intended for sale at auction this year. The amended act also extended the periods required for generation for the first time after the auction of solar energy from 18 to 24 months, and from wind from 24 to 33 months.

11.3. Electricity prices

The Group generates the vast majority of revenues from generation and sale of electricity, therefore the risk of changes in the price for which it sells electricity is of key importance for the level of revenues generated by the Group.

On the day-ahead market of Towarowa Giełda Energii SA, the first half of 2019 was characterized by a decrease in the weighted average energy price compared to the preceding two quarters. There are several factors worth mentioning that had an impact on electricity prices in the first half of 2019. In the analysed period, domestic electricity consumption was lower by 1.39% compared to the same period last year. A very important factor that clearly influenced the prices was the very high windiness and the associated high generation of wind turbines. Generation from wind sources in the first half of 2019 was higher by over 25.52% compared to the first half of 2018, with a slight change in installed capacity. A factor that could also have an impact on price formation, and whose importance is difficult to determine, was the confusion surrounding the introduction of "freezing" energy prices for final customers and the lack of implementing acts on this topic. The very fast pace of legislative changes and uncertainty as to the interpretation of the regulations could have influenced the expectations and purchasing strategies of market participants. However, it should be remembered that CO₂ prices are still high, the Weighted Average Price (IRDN) in the first quarter of 2019 was PLN 219.44 / MWh, i.e. by PLN 32.21, i.e. 17.20% compared to the first quarter 2018 year. The weighted average price (IRDN) in the second quarter of 2019 was also higher at PLN 241.88 / MWh, i.e. by PLN 26.74, i.e. 12.43% higher than in the second quarter of the previous year.

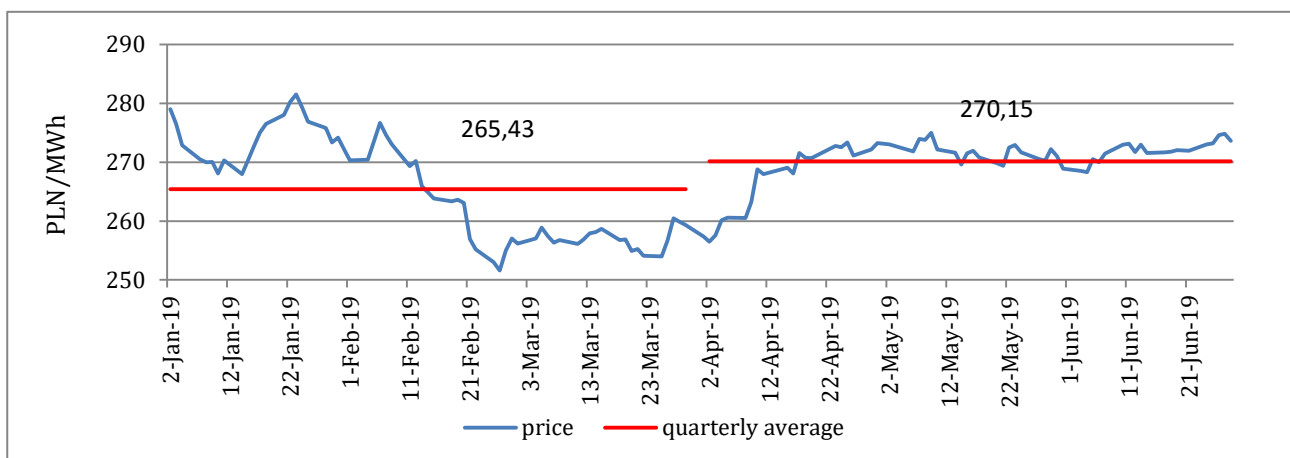
Chart 9: Energy prices (IRDN - Instruments of the Day Ahead Market)



Source: Own elaboration based on TGE data

On the electricity forward market of the Polish Power Exchange, the reference forward contract BASE_Y-20 in January and February 2019 was characterized by a mild downward trend to stabilize in March at slightly below 258 PLN / MWh. The situation on the futures market obviously depended to a large extent on current quotations, but the factors shaping prices on the futures market are still the same and can be associated with high levels of steam coal prices for domestic customers and high prices of CO2 emission allowances. The arithmetic average of the daily clearing rates for the BASE_Y-20 contract in the first half of 2019 was at the level of PLN 267.75 / MWh, while in the first quarter of 2019 it was at the level of PLN 265.43 / MWh, while in the second quarter it increased up to PLN 270.15 / MWh.

Chart 10: The price of the futures contract for the supply of electricity (band) for 2020

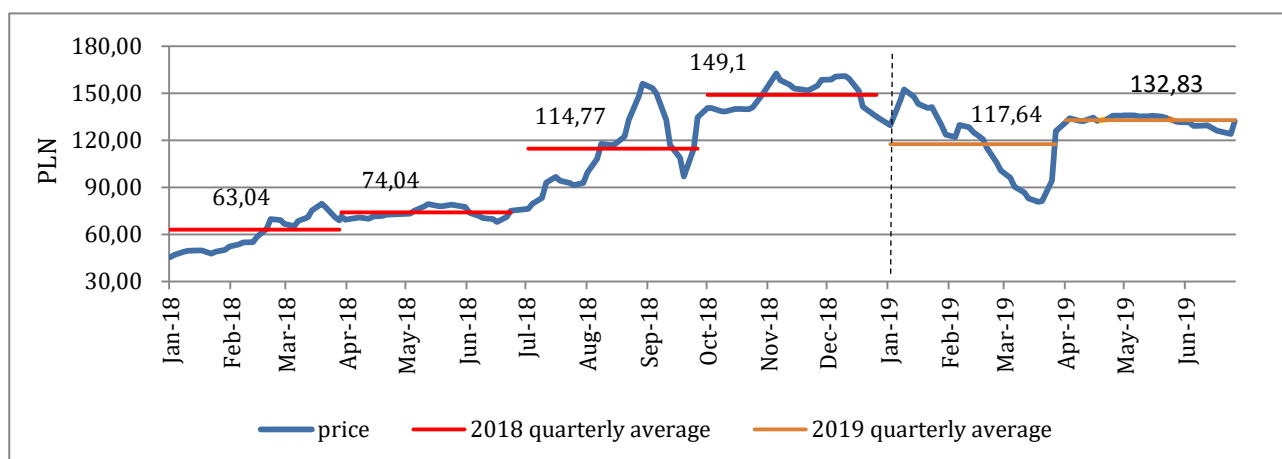


Source: Own elaboration based on TGE data

11.4. Prices supply of certificates of origin

Due to the fact that one of the power units at ZE PAK SA is dedicated to combusting biomass and in addition, the Group utilizes high-efficiency co-generation in order to generate heat, a producer is entitled to green and red certificates, provided certain regulatory requirements are met. The number of obtained certificates of origin depends on the level of generation from a given sources and is usually higher than the number, which the Company is obliged to present for redemption, which in the case of a surplus allows to sell specific volumes to other market participants. However, biomass unit generation largely depends on the green certificates market price levels. During periods, when the total generated biomass energy and green certificate prices do not ensure reaching the assumed financial effect, the generation may be decreased or halted, which also automatically decreases the amount of generated green certificates. Due to the fact that the level of income generated from the sale of certificates of origin is lower than the level of revenues generated from the sale of electricity, the risk of price changes for certificates of origin also has a smaller impact on results than, for example, the risk of changes in energy prices.

Chart 11: Price of RES Energy certificate of origin



Source: Own elaboration based on TGE data

In the first quarter of 2019, prices of energy certificates of origin (green certificates) were highly volatile. There are two factors for the reasons for the fluctuations. The first was a very high wind generation, wind farms are the largest source of certificate supply on the market. The second factor responsible first for the price reduction and later for their increase were works on the amendment to the RES Act, where during subsequent versions entries appeared and disappeared trying to make changes in the amount of the substitution fee, however, after abandoning these entries, the price of property rights stabilized and from April to the end of the second quarter it fluctuated around 130 zlotys. The weighted average price of green certificates in the first quarter of 2019 was at the level of 117.64 PLN / MWh, which means an increase by 54.60 PLN / MWh, i.e. by 86.61% compared to the first quarter of 2018. In the second quarter of 2019, the weighted average price of green certificates increased to PLN 132.83 / MWh, which means an increase of 58.79 PLN / MWh, i.e. by 79.40% compared to the weighted average price from the second quarter of 2018.

11.5. Extraction and supply costs of coal and other fuels

A fuel cost is the important part of the costs related to the electricity and heat generation in companies of the ZE PAK SA Group. The prices of fuel largely determine the competitiveness of particular electricity production processes. The ZE PAK SA Group's power plants produce most of their electricity from brown coal, but they also use forest and agricultural biomass. Furthermore, heavy and light heating oil is used in minimum quantities for heating purposes in the process of electricity production.

Two lignite coal mines, PAK KWB Konin SA and PAK KWB Adamów SA, which are the suppliers of lignite coal to ZE PAK SA Group's power plants causes that ZE PAK Group does not rely on external suppliers and eliminates the exposure to potential fluctuations of brown coal prices. Nevertheless, the Group is exposed to the fluctuations in prices of other fuels used (mainly biomass) and part of the costs related to the extraction of brown coal depends on the factors which remain outside the direct control of the Group.

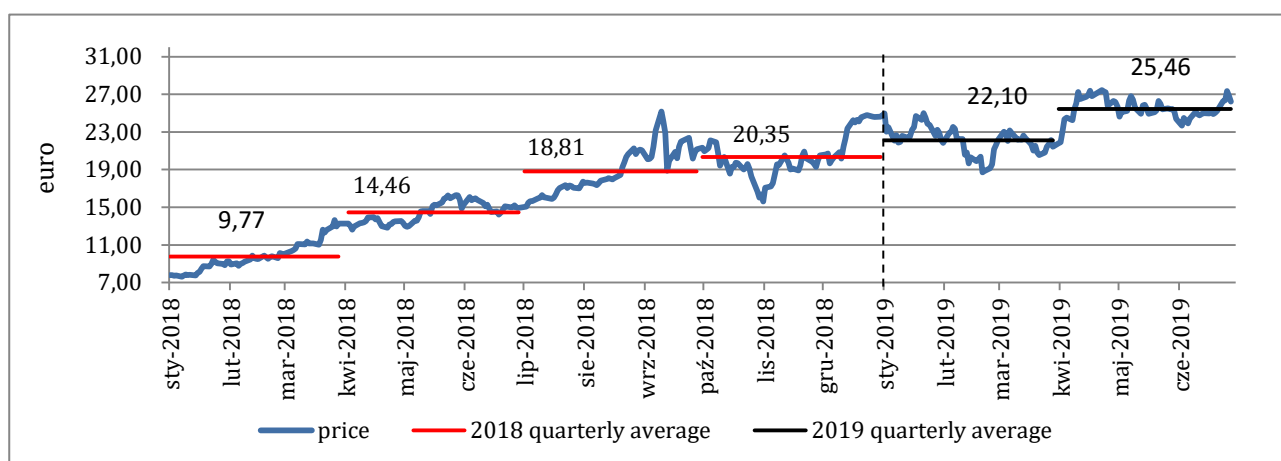
The deposits exploited by the Group's mines have specified richness. The opportunity to achieve the expected level of electricity production in the long term is partially dependent on the ability of extracting from the currently exploited deposits and launching the exploitation of new brown coal deposits, which would be economically viable. As part of activities to ensure the raw material for the Group's generation assets, PAK KWB Konin executed designing works at the perspective brown coal deposits. In order to develop the perspective deposits, it is necessary to obtain all necessary formal approvals and permits, culminated with obtaining a license to extraction. The process of obtaining approvals and permits is a multi-step and stretched in time. In view of the above, there is a risk of delays and postponements in the schedule of developing subsequent deposits which, in turn, may entail risks of interruptions of coal supplies for the Group's generating assets. The opportunity to start the extraction from the prospective coal deposits in the future may be limited by many factors beyond the control of the Group. The main risk factors include: failure to obtain the necessary licenses, adverse settlements of the local government in terms of shaping the special policy, lack of opportunity to obtain adequate financing. The risk related to the cost and quantity of fuel supplies is crucial for the overall level of costs and production volume.

11.6. CO₂ emission allowances costs

The activities in the scope of generating electricity and heat from conventional sources are associated with the need to incur the CO₂ emission costs. In view of the fact that these costs represent an important item in the structure of the costs incurred by the producers of energy from lignite, the impact of emitted quantities of CO₂ and the risk of price changes of CO₂ emission allowances (EUA) is of great importance to the activities' results.

In the first half of 2019, the CO₂ emission allowance market, like the previous two quarters, was characterized by very high price volatility. The difference between the minimum and maximum quotations was 8.75 euros, i.e. about 35% compared to the price at the end of 2018. Such high and persistent volatility may confirm the interest of speculative financial investors in this market. The fundamental factors that shaped the situation on the emission allowance market in the first half of 2019 were the uncertainty about the future of Great Britain in the EU (and thus in the EU ETS system), the emission settlement date for 2018 (30 April), prices achieved in auctions on the primary market, expectations regarding Germany's declaration regarding the resignation from the use of coal in the energy sector, weather conditions and the evolution of energy prices and the level of production from renewable sources. The arithmetic average of EUA quotations in the first half of 2019 was EUR 23.78, which means an increase of 96% compared to the first half of 2018.

Chart 12: Price of the futures contract for the supply of EUA



Source: Own elaboration based on ICE data

11.7. Compensation for the stranded costs related to the termination of the „Long-term Contract” („PPA”) Elektrownia Państw II sp. z o.o.

The long-term contract for the sale of power and electricity (PPA) was concluded between Elektrownia Państw II sp. z o.o. and Polskie Sieci Elektroenergetyczne SA. The contract was a long-term agreement in the scope of supply of electricity according to the established price formula.

Due to the early termination (on 1 April 2008) of PPA, pursuant to the Act of PPA, Elektrownia Państw II sp. z o.o. is entitled to receive sufficient compensation. The amount of compensation is estimated according to an applicable formula specified in the Act. Elektrownia Państw II sp. z o.o. is covered by the said act by the end of 2025. The mechanism determining the amount of revenues related to compensation for stranded costs largely functions on the basis of offsetting, therefore the risk related to the level of revenues from this source is to a certain extent dependent on other types of risk affecting the level of costs and revenues, e.g. energy prices or prices of allowances for emissions.

11.8. Seasonality and meteorological conditions

The demand for electricity and heat, especially among consumers, is subject to season fluctuation. So far, the practice showed that the consumption of electricity was higher in the winter (mainly due to low temperatures and shorter days) and lowered in the summer (due to the summer period, higher ambient temperatures, and a longer day). In the last couple of years, there is an increase in the demand for electricity in the summer, which is caused mostly by the rising number of used cooling devices and air conditioning.

Irrespective of the factors described above, meteorological conditions are becoming more and more important for the Group's production level. In the past, the operations of the Group were not subject to significant seasonality of demand, due to low costs, the work of blocks was carried out continuously (in the basis) for almost a whole year. Currently, taking into account the growing share of RES in the energy generation segment, including primarily wind sources, weather conditions are becoming more and more important in the estimation of the Group's production volume, with particular regard to wind conditions. Statistically, periods of the best wind conditions are the first and the fourth quarter. It should be taken into account that in periods when wind conditions are extremely good and the production of wind turbines is high, the demand for the Group's production may be subject to periodic reductions, similarly in periods of lower wind production can increase.

However, the risk related to seasonality and meteorological conditions is not crucial in the Group's operations.

11.9. Investment expenses

Activities in the coal mining and energy production sector require significant investment expenditures. The Group's generation assets require periodic renovations and ongoing modernizations, both due to the tightening of environmental protection requirements and the need to increase the efficiency of electricity production. The level of investment outlays had a material impact, and, according to expectations, it may still have a significant impact on the results of operating activities, the level of indebtedness and cash flow. Delays in implementation, changes in the investment program and exceeding the budget may have a serious impact on future capital expenditures as well as on results, financial situation and development prospects. In addition, some of the investment projects planned by the Group, reported to the National Investment Plan, involve the allocation of free units authorizing to CO₂ emissions, however, if these investments are not implemented, the ability to use the free allocation is also prevented. Also in the case of certain expenditures, the sustaining of which authorized the allocation of free emission rights, when the investment project submitted to KPI was not completed on time, the possibility of returning the received permits should be reckoned in the part in which they were previously granted.

11.10. EUR/PLN exchange rate, the level of interest rates

Despite the fact that the Group conducts its activities in Poland, where it incurs costs and gains revenues in zloty, there is a couple of significant factors which make the financial results dependent on the exchange rate of EUR/PLN and the level of WIBOR and EURIBOR interest rates. The most important factors include:

- transactions connected with EUA purchase are settled in EURO,
- The companies in the Group use debt financing based on a variable interest rate.

The Group's exposure to risk caused by changes in interest rates relates primarily to financial liabilities. The Group has financial liabilities, mainly investment and working capital loans with variable interest rates.

As early as in the first quarter of 2019, part of the debt (i.e. syndicated loan taken out by Elektrownia Pańków II sp. z o.o.) was denominated in EUR, which meant that the depreciation of PLN against EUR had a negative impact on financial results, as it increases the cost of financing in PLN related to debt in a foreign currency, while the depreciation of the value of the euro against the zloty had a positive impact on financial results, as it reduces the cost of financing in PLN related to debt in a foreign currency. However, this factor will no longer affect the financial results because the debt denominated in euro was fully repaid in April 2019.

The Group companies periodically use instruments to limit the risk arising from exchange rate fluctuations, e.g. for part of the flows related to the purchase of CO₂ emission allowances. Forwards are used to hedge the exchange rate. Management Boards monitor the financial and market situation on an ongoing basis, and if necessary, they may decide on the need to use financial instruments to hedge against currency risk. In accordance with the principles applied in ZE PAK SA Group, any transactions will be collateral and will be matched to the hedged item in terms of volume and maturity. The decision to choose a hedging instrument will also take into account: price, market liquidity, product simplicity, ease of valuation and accounting, and flexibility.

SIGNATURES:

Henryk Sobierajski
Member of the Supervisory Board
of ZE PAK SA delegated to temporarily
perform the duties of the President of the Board

Zygmunt Artwik
Vice President of the Management Board

Paweł Markowski
Vice President of the Management Board

Paweł Lisowski
Vice President of the Management Board

Maciej Nietopiel
Vice President of the Management Board