

**REPORT**

**ON THE OPERATIONS OF THE  
ISSUER'S GROUP**

**For the First Half of 2017**

Łomża, 30 August 2017

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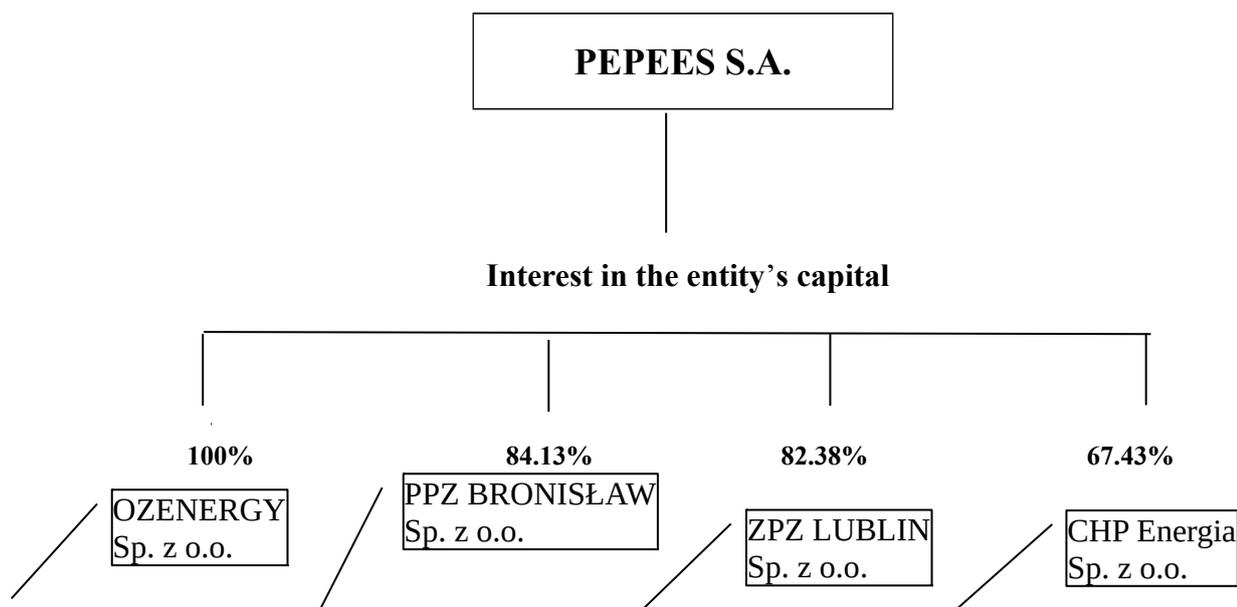
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## 1. I. Information about PEPEES Group

PEPEES Group is a modern and ever-growing corporate group specialising in the processing of potatoes to produce, among other things, potato starch, crystalline and anhydrous glucose, maltodextrin, glucose syrups, potato grits and flakes or potato protein for feed-producing purposes.

Przedsiębiorstwo Przemysłu Spożywczego PEPEES S.A. (hereinafter referred to as 'PEPEES S.A.' or 'the Company') is a parent company for Zakłady Przemysłu Ziemniaczanego 'ZPZ Lublin' sp. z o.o., Przedsiębiorstwo Przemysłu Ziemniaczanego 'Bronisław' sp. z o.o., CHP Energia sp. z o.o. and OZENERGY sp. z o.o.

The composition of the Group as at 30 June 2017 was as follows:



All subsidiaries were consolidated with the full method.

### 1. Przedsiębiorstwo Przemysłu Spożywczego 'PEPEES' Spółka Akcyjna in Łomża – the parent company

#### 1.1 General information about the Company

The Company's business name is: Przedsiębiorstwo Przemysłu Spożywczego 'PEPEES' S.A. Its registered office is in Łomża, at the address: ul. Poznańska 121.

PEPEES S.A. in Łomża is the largest starch potato processing plant in Poland and the only Polish manufacturer of crystalline glucose. Owing to the integrated management system implemented and a certified since 2007, the Group ensures high quality and full health safety of products. The Company's products are widely used in the food, pharmaceutical, feed, chemical, textile and paper industries.

According to the Company's Articles of Association, the Company's objects are as follows:

- processing of potatoes;
- manufacture of starches and starch products;
- services related to the processing and preserving of fruit and vegetables;

- manufacture of fruit and vegetable juice.

During the reporting period, the Company carried out activities related to the manufacture of starches and starch products, and the processing of potatoes.

The Company's share capital as at 30 June 2017 and as at the date of this report was PLN 5,700 thousand and was divided into 95,000 thousand ordinary bearer shares with the nominal value PLN 0.06 each.

As at the date of the publication of this interim report, i.e. 31 August 2017, the shareholding structure of the Company was as follows:

SHAREHOLDERS	Number of shares	Interest in share capital %	Number of votes	Share in the total number of votes at GMS %
Mr Maksymilian Maciej Skotnicki*	20,395,465	21.47	20,395,465	21.47
Mr Michał Skotnicki*	10,700,011	11.26	10,700,011	11.26
Mr Newth Jonathan Reginald	7,995,200	8.42	7,995,200	8.42
Mr Krzysztof Borkowski - indirectly	7,923,409	8.34	7,923,409	8.34
Richie Holding Ltd	6,133,100	6.45	6,133,100	6.45
Others**	41,852,815	44.06	41,852,815	44.06
Total	95,000,000	100.00	95,000,000	100.00

\* Mr Maksymilian Maciej Skotnicki and Mr Michał Skotnicki are persons referred to in Article 87 Clause 4 item 1 of the Act on Public Offering [...] and, thus, together they hold the total of 31,095,476 shares/votes representing 32.732% of the share capital/of the total number of votes in the Company.

\*\* Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych (previously a significant shareholder of the Company) has been included in 'Others', because, in accordance with the notice received by the Company, on 30 June 2017, it sold the total of 700,000 shares and currently it does not exceed the threshold of 5% of the share capital/total number of votes.

None of the other shareholders have reported the holding of at least 5% of the share capital, and, in consequence, from the date of publishing the previous quarterly report, i.e. 15 May 2017, no other changes in the shareholding of the Company have had place apart from the aforementioned changes.

## 1.2 The Company's authorities

### *Board of Directors*

From 1 January 2017 until 30 June 2017, the composition of the Board of Directors of PEPEES S.A. was as follows:

Mr Wojciech Faszczewski – President  
Mr Tomasz Rogala – Member

Members of the Board of Directors are appointed and dismissed by the Supervisory Board. The Board of Directors have all management powers in the Company, except for the powers reserved for the Supervisory Board or the General Meeting of Shareholders. The decision on the issue or redemption of shares is made by the General Meeting of Shareholders by way of a resolution.

### ***Supervisory Board***

In the period from 1 January 2017 to 30 June 2017, the composition of the Supervisory Board of PEPEES S.A. was as follows:

1. Mr Maciej Kaliński – Chairman
2. Mr Piotr Marian Taracha – Vice-Chairman
3. Mr Krzysztof Stankowski – Secretary
4. Mr Robert Malinowski – Member
5. Ms Agata Czerniakowska – Member

### **2. Zakłady Przemysłu Ziemniaczanego 'LUBLIN' Spółka z ograniczoną odpowiedzialnością in Lublin – a subsidiary**

### **General information about the Company**

The Company's core objects are the production and sale of starch syrup and dried potatoes.

The Company's share capital as at 30 June 2017 amounted to PLN 2,761,200, and its shareholders were as follows:

- PEPEES S.A. - 22,748 shares with the value of PLN 2,274,800, i.e. 82.38%
- The Company's employees - 3,244 shares with the value of PLN 324,400, i.e. 11.75%
- Farmers - 1,620 shares with the value of PLN 162,000, i.e. 5.87%

### **2.2 The Company's authorities**

#### ***Board of Directors***

From 1 January 2017 until 30 June 2017, the composition of the Board of Directors was as follows:

- Mr Piotr Kaniowski – President of the Board of Directors  
Ms Małgorzata Dudzic – Member/Chief Financial Officer

#### ***Supervisory Board***

In 2017, the Company's activities were supervised by the Supervisory Board composed of:

- Mr Wojciech Faszczewski – Chairman
- Mr Piotr Taracha – Vice-Chairman
- Mr Piotr Łojko – Secretary
- Mr Mariusz Świetlicki – Member

– Ms Agata Czerniakowska – Member

### **3. OZEnergy Spółka z ograniczoną odpowiedzialnością in Łomża – a subsidiary**

#### **3.1 General information about the Company**

The Company's objects, according to its Articles of Association, are as follows: electric power generation and supply; sewerage and waste management; remediation activities; growing of crops; production, trade, rendering of services, including export and import. As at the balance sheet date and as at the date of this report, the company has not started operations yet.

The Company's share capital as at 30 June 2017 amounted to PLN 95,000 and was divided into 1,900 equal and indivisible shares, each with the value of PLN 50.

The composition of the Board of Directors as at 30 June 2017:

Mr Roman Minierski – President

### **4. Przedsiębiorstwo Przemysłu Ziemniaczanego BRONISŁAW Spółka z ograniczoną odpowiedzialnością in Bronisław – a subsidiary**

#### **4.1 General information about the Company**

The Company's objects are as follows:

- manufacture of starches and starch products;
- sales of potato-based products in Poland and abroad;
- agricultural services.

The Company's share capital as at 30 June 2017 amounted to PLN 800.000 and was divided into 1,600 equal and indivisible shares, each with the nominal value of PLN 500. PEPEES is the major shareholder; it holds 84.125% of the share capital. Other shareholders are natural persons.

#### **4.2 The Company's authorities**

##### ***Board of Directors***

The composition of the Board of Directors from 1 January 2017 to 30 June 2017:

- Mr Wojciech Faszczewski – President
- Mr Roman Minierski – Vice-President

##### ***Supervisory Board***

From 1 January 2017 to 30 June 2017, the Company's activities were supervised by the Supervisory Board composed of:

- Mr Piotr Taracha – Chairman
- Mr Piotr Łuniewski – Member
- Mr Grzegorz Dobrowolski – Member
- Mr Stanisław Bukowski – Member

## **5. CHP Energia Sp. z o.o. - a subsidiary**

### **5.1 General information about the Company**

The Company's objects are as follows:

- power generation
- electricity transmission and distribution

The company's share capital as at 31 December 2016 amounted to PLN 5,298,000 and was divided into 10,596 equal and indivisible shares, each with the nominal value of PLN 500.

PEPEES is the major shareholder; it holds 67.43% of the share capital. Other shareholders are natural persons.

### **5.2 The Company's authorities**

#### ***Board of Directors***

The composition of the Board of Directors from 1 January 2017 to 30 June 2017:

- Mr Andrzej Wyszyński – President
- Mr Mirosław Siemieniako – Vice-President

#### ***Supervisory Board***

The composition of the Supervisory Board from 1 January 2017 to 30 June 2017:

- Mr Wojciech Faszczewski – Chairman
- Mr Tomasz Rogala – Member
- Mr Wojciech Zagdański – Member

## **6. Changes in the organisation of PEPEES Group**

On 27.04.2017, the Company entered into a conditional sales agreement with a natural person, who is a shareholder of the Company, under which the Company acquired a 34.9167% stake ('Stake') in Gospodarstwo Rolne Ponary sp. z o.o. ('Ponary').

As a result of the shares subscription, Ponary has become an associate.

At the same time, the Company entered into agreements to secure its right to acquire all other shares in Ponary. The Company intends to exercise this right and acquire the remaining shares of Ponary gradually when it has free funds available. The acquisition of the remaining shares of Ponary will each time depend on the failure of the Polish Agricultural Property Agency to exercise its right of pre-emption.

Apart from the aforementioned changes, there were no other changes in PEPEES Group in the reporting period.

## 2. II. Factors and events affecting the Group's operations

### 1. The market

Production, trade and rendering of services related mainly to the processing of potatoes and power generation were the main revenue-generating activities of PEPEES S.A. Group in the reporting period. In PEPEES S.A. Group, the parent company conducts manufacturing and trading activities related to products and goods from the starch industry.

Until the time of taking control of the subsidiary CHP Energia sp. z o.o. (i.e. until 24 October 2016), the Group had been operating in a single, main reporting segment covering the processing of potatoes to obtain starch, dried potato-based products and starch hydrolysates. Hence, from that time, both at the level of the Group and of the parent company, a single segment has been identified in the daily records and internal reports, i.e. 'processing of potatoes'.

At the same time, due to the taking control of CHP Energia, starting from the consolidated financial statements for 2016, another 'power generation' segment was separated which comprises the activities of the aforementioned subsidiary.

Within the segment: 'the processing of potatoes', the Company produces:

- potato starch;
- a few varieties of glucose;
- a wide range of starch syrups;
- potato grits;
- potato flakes.

The Group processes both starch potatoes and food potatoes. Potatoes are the primary source of starch, not only in Poland, but throughout Europe. Starch potatoes are potatoes containing at least 13% of starch. One can obtain starch from such potatoes, for food-related and technical purposes, by its mechanical separation from other potato components, washing out, purifying, drying and screening.

Europe is the largest manufacturer of potato starch in the world. In the EU, in recent years, the output amounted to ca. 1.85 million tonnes p.a.; 92% of that quantity was produced by EU-15 states and almost 8% by new Member States. Poland's share in the potato starch production in the EU amounts to ca. 6%.

Food potatoes are processed in the subsidiary ZPZ Lublin sp. z o.o., mainly to obtain potato grits and potato flakes, and partially in PPZ Bronisław sp. z o.o., to obtain potato flakes.

CHP Energia sp. z o.o. is an enterprise which, in its strategy, provides for the running of a biogas plant and of the integrated plant producing solid fuel from biomass, and power generation in green co-generation. The generated excess heat is used to dry the biomass used as a fertiliser in agriculture. In addition, the Company carries out trading activities related to the purchase and bailing of pulp. The establishment of agricultural biogas plants is part of the implementation of commitments towards the European Union. New legal regulations already implemented and the support system will accelerate the development of this sector in Poland.

### 2. Basic products, trade goods and services sold by the Group

Within the segment: 'the processing of potatoes', the Company produces:

- potato starch, used for many applications in the food, pharmaceutical, paper, textile and chemical industries;
- a few varieties of glucose used by the food industry, confectionery industry and pharmaceutical industry;

- maltodextrin, which is an essential ingredient of powdered products (ice cream, sauces, soups, fruit extracts, flavoured sprinkles) and vitamin and mineral preparations and supplements for children and athletes;
- a wide range of starch syrups used in confectionery and baking industries;
- potato grits used by the food industry;
- potato flakes used in the food industry.

In the 'power generation' segment, the Company produces:

- electricity from agricultural biogas;
- heat for its own needs used e.g. to dry animal feeds.

### 3. Sales volume and structure

Table 1 presents the structure of sales revenue in the period from 1 January 2017 to 30 June 2017 as compared to the corresponding period in 2016.

**Table 1: Net sales revenue structure in the first half of 2017 and the first half of 2016**

(amounts in PLN 000s)

Range of products	First half of 2017	Structure in 2017	First half of 2016	Structure 2016	Growth rate
potato-based products	91,625	78.98%	69,205	80.01%	132.40%
heat	352	0.30%	1,757	2.03%	20.03%
electricity	4,884	4.21%	0	0.00%	-
animal feeds	366	0.32%	0	0.00%	-
<b>other sales, including:</b>	18,784	16.19%	15,533	17.96%	120.93%
a) services	589	0.51%	355	0.41%	165.92%
b) trade goods and materials	18,195	15.68%	15,178	17.55%	119.88%
<b>Total net sales revenue</b>	<b>116,011</b>	<b>100.00%</b>	<b>86,495</b>	<b>100.00%</b>	<b>134.12%</b>

### 4. Polish and foreign markets for the Group's products

**Table 2: Sales revenue by markets**

(amounts in PLN 000s)

Net sales revenue	First half of 2017	First half of 2016
<b>Poland, including:</b>	<b>79,632</b>	<b>62,137</b>
- products	64,018	47,593
- trade goods	15,025	14,189
- services	589	355
<b>EU countries - intra-Community supplies, including:</b>	<b>5,339</b>	<b>5,671</b>
- products	4,944	5,571
- trade goods	395	100
<b>Other countries – export, including:</b>	<b>31,040</b>	<b>18,687</b>
- products	28,266	17,798
- trade goods	2,774	889
<b>Total</b>	<b>116,011</b>	<b>86,495</b>

#### 4.1 Sales in Poland by industries and geographical regions

The products from the potato industry were sold in 2017 throughout Poland, and the biggest sales were recorded in the following provinces: wielkopolskie, lubelskie, podlaskie, mazowieckie, małopolskie, dolnośląskie and śląskie.

The Group distributed its products both through the network of wholesalers and trading companies making deliveries to the food industry; and it supplied its products directly to production plants, mainly from the food, confectionery, meat and pharmaceutical industries, for which starch products are the raw material for further processing or a component in the manufacturing process.

In the period, the largest share in the sales on the Polish market was recorded for potato starch, which accounts for 40.4% (in terms of value) of all products manufactured by the Group, and the next product is maltodextrin (9.2%) and glucose (ca. 6.2%).

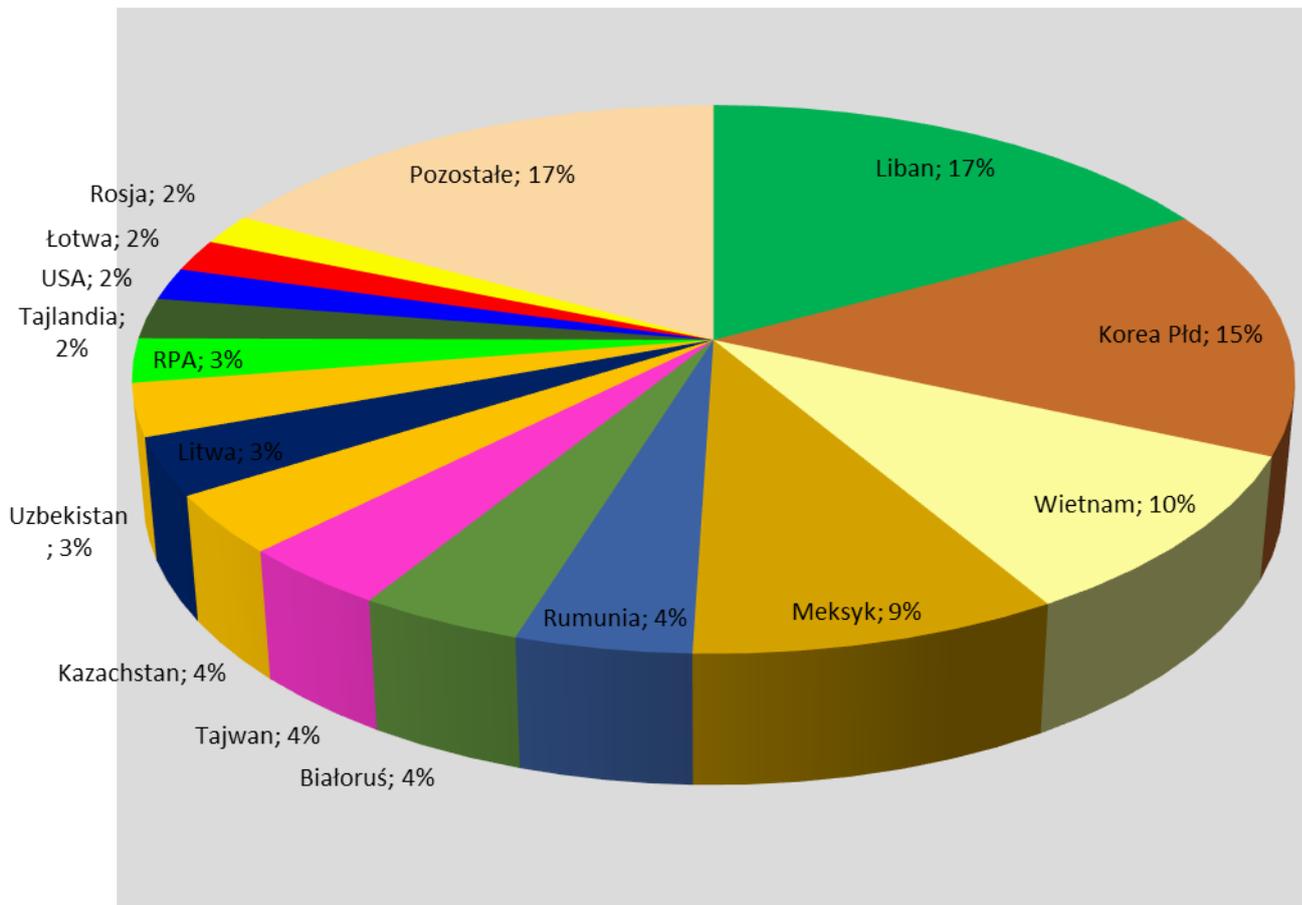
#### **4.2 *Export and intra-Community sales***

In the first half of 2017, exports and intra-Community sales amounted to 31.4% of total sales. In the corresponding period of the previous year, this share was at the level of 28.2%.

This year, the Group sold its products to 16 countries in the European Union and to 20 countries from the rest of the world.

The main markets are in Asia, the Middle East, Central America and the countries of the former Soviet Union, i.e. Belarus, Kazakhstan, Uzbekistan, Russia, Latvia and Lithuania. In the first half of 2017, the largest quantities of products were sold to Lebanon.

### Sktruktura sprzedaży międzynarodowej w 1 połowie 2017 r. /w ujęciu wartościowym/.



#### 5. The sources of supplies of production materials, trade goods and services

Food potatoes and potatoes for industrial use are the main production material in PEPEES S.A. Group; they are purchased in the autumn on the basis of procurement contracts concluded in the spring. Since the beginning of the 1990's, a downward trend in potato production in Poland has been observed. At the end of the 1990's, their share in the crop structure exceeded 10% and now it is only 3%. Ca. 400,000 ha are used in Poland to grow potatoes; however, the cultivation area for starch potatoes is less than 25,000 ha, i.e. only 6% of the total potato cultivation area.

The main raw material for power generation in CHP Energia is biomass produced primarily from plant waste bought from farmers and from PEPEES—waste from the production of starch (potato pulp).

In addition, the following raw materials are purchased for the production process: paper packaging, enzymes, starch, glucose syrup, industrial gases, electrical materials, fine coal, metal parts, bags, sulphur dioxide, shrink film, hydrochloric acid, labels, cardboard boxes, diatomaceous earth, glues and adhesives, varnishes, thinners, enamels, steel strip, pesticides, etc.

The basic raw material, i.e. potatoes for industrial use, is purchased from individual farmers who are not affiliated with any organisations important for the Company's business. In 2017, materials, trade goods and services were purchased mainly from Polish companies or agencies of foreign companies. The dependence on a single supplier exists in the case of enzymes and filtering materials, as their suppliers are the only representatives in Poland of foreign companies producing the raw materials needed by the Group.

There is no single supplier whose share in the Group's revenue is at least 10%.

## **6. Agreements material for the Group's business**

### **6.1 Business agreements**

In 2017, the companies of PEPEES S.A. Group did not conclude agreements of substantial value.

Notwithstanding the foregoing, the Issuer indicates the following agreements concluded in 2017:

- the agreement concerning the purchase of a 34.9167% stake in Gospodarstwo Rolne PONARY sp. z o.o. for PLN 4,259.8 thousand;
- a contract for the purchase of pesticides for potato plantations with the value of PLN 3,075 thousand;
- a contract for the production and assembly of a palletizing line with the value of PLN 1,990 thousand;
- trading agreements;
- agreements concerning the modernisation of buildings, structures, plant and machinery and repairs.

### **6.2**

### **Loan agreements**

- a) *with BOŚ S.A.:*

Annex No. 1 dated 23 May 2017 to the non-revolving loan agreement dated 18 February 2016 between PEPEES S.A. in Łomża and BOŚ S.A. The subject of the agreement is to reduce the amount of the loan from PLN 1,200 thousand to PLN 1,024 thousand, and change the repayment schedule. Other terms of the contract remain unchanged.

***b) with BGŻ BNP Paribas S.A.***

Amendment No. 4 dated 21 June 2017 to the multi-purpose credit line agreement concluded between PEPEES S.A. and its subsidiaries, i.e. Zakłady Przemysłu Ziemniaczanego Lublin sp. z o.o. and Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław sp. z o.o., and BGŻ BNP Paribas S.A. The Annex changed, in particular, the amounts of limits available for the revolving and non-revolving loan, as a result of which, at present the total credit limit granted to the Issuer and its subsidiaries amounts to PLN 37 million. The annex has amended the revolving loan limit in such a way that currently the revolving loan granted to the parent company, ZPZ Lublin sp. z o.o. and PPZ Bronisław sp. z o.o. amounts to PLN 3.75 million, PLN 1.125 million and PLN 1.125 million respectively, while the non-revolving loan granted to the parent company, ZPZ Lublin sp. z o.o. and PPZ Bronisław sp. z o.o. amounts to PLN 15 million, PLN 1.5 million and PLN 9.5 million respectively. The annex has not introduced any changes related to the overdraft facility and, in accordance with the original terms of the agreement, the overdraft facility granted to the parent company, ZPZ Lublin sp. z o.o. and PPZ Bronisław sp. z o.o. amounts to PLN 4 million, PLN 0.5 million and PLN 0.5 million respectively. In addition, the Annex has extended the scope of the purpose of the non-revolving loan in such a way that currently it includes the financing and refinancing of the purchase of potatoes and the financing of the purchase of seed potatoes for farmers.

No loan agreements of the companies from PEPEES Group were terminated in the first half of 2017.

### **6.3**

### **Leases**

- A lease concerning a passenger car with the value of PLN 121 thousand concluded on 7 March 2017 for the period of 60 months with BGŻ BNP Paribas S.A.
- A lease concerning a passenger car with the value of PLN 39 thousand concluded on 23 March 2017 for the period of 60 months with BGŻ BNP Paribas S.A.
- A lease concerning a passenger car with the value of PLN 237 thousand concluded on 24 April 2017 for the period of 36 months with Volkswagen Leasing.

### **6.4**

### **Insurance contracts**

The companies concluded the following insurance contracts:

1. fire insurance;
2. business interruption insurance;

3. burglary and robbery insurance;
4. electronic equipment insurance;
5. liability insurance, including:
  - tort liability insurance
  - contractual liability insurance
  - product liability insurance
  - directors and officers liability insurance
6. motor vehicle insurance (liability insurance, auto accident and theft insurance)

## **6.5 Agreements between shareholders**

As at the date of this report, the Company is not aware of any agreements made between its shareholders.

## **7. Organisational or equity links between the Issuer and other entities; its major investments in Poland and abroad**

As at 30 June 2017, the main investments of PEPEES S.A. comprise shares in the subsidiaries that have been consolidated and shares in the associate Gospodarstwo Rolne 'Ponary' sp. z o.o. (with the Issuer's interest at the level of 34.92% in the share capital/total number of votes) measured with the equity method, and 3,000 shares of Warszawski Rolno-Spożywczy Rynek Hurtowy S.A. with the value of PLN 2,550 thousand.

In addition, the Group holds interests in three other Polish entities (ZM Ostrołęka, Agencja Rozwoju and BPS) which ensure less than 5% of the total number of votes at the General Meeting of Shareholders, and they are not material in terms of their value and the Group's investment policy.

## **8. Related party transactions**

During the reporting period, the companies of PEPEES S.A. Group concluded transactions with related parties and all such transactions were made on an arm's length basis.

### **The Issuer's transactions with its subsidiaries:**

#### *Transactions between PEPEES S.A. in Łomża and ZPZ LUBLIN sp. z o.o. in Lublin*

Transactions between PEPEES S.A. in Łomża and its subsidiary ZPZ LUBLIN sp. z o.o. in Lublin consisted in the purchase from the subsidiary of starch and potato grits for PLN 802 thousand.

In 2017, PEPEES S.A. sold to ZPZ Lublin sp. z o.o. starch for PLN 103 thousand and a service for PLN 106 thousand. The selling price is determined using the cost-plus pricing method or on the basis of price lists applicable in transactions with unrelated parties.

In addition, ZPZ Lublin sp. z o.o. paid to PEPEES S.A. interest on the cash loan granted in previous years amounting to PLN 63 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 3 million.

*Transactions between PEPEES S.A. in Łomża and PPZ Bronisław sp. z o.o. in Bronisław*

During the reporting period, PEPEES S.A. purchased from its subsidiary starch, potato flakes and services, and sold a service. The total value of purchases from PPZ Bronisław sp. z o.o. amounted to PLN 2,794 thousand, and to PLN 1 thousand in the case of sales. In addition, PPZ Bronisław sp. z o.o. paid to PEPEES S.A. interest on the cash loan granted in the previous year amounting to PLN 92 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 3,973 thousand.

*Transactions between PEPEES S.A. in Łomża and CHP Energia sp. z o.o.*

PEPEES S.A. purchased from CHP Energia sp. z o.o. beet pulp for PLN 283 thousand, bio-compost for PLN 175 thousand and a service for PLN 2 thousand; and sold to CHP Energia sp. z o.o. a service with the value of PLN 9 thousand and paid to it the compensation for the termination of the agreement on the sales of property rights amounting to PLN 20 thousand. As at the balance sheet date, there are outstanding loans amounting to PLN 2,234 thousand, the interest of PLN 69.7 thousand, and trade receivables of PLN 210 thousand.

**Transactions with shareholders, and members of the management personnel and their family members in the reporting period:**

The Company acquired from a shareholder, who is entitled to 11.26% (32.73% together with its related party) of the total number of votes at the General Meeting of Shareholders of Pepees, 11,313 shares in Gospodarstwo Rolne Ponary sp. z o.o. with the nominal value of PLN 565.65 thousand, for the price of PLN 4,259.8 thousand, entitling to 34.9167% of the votes at the General Meeting of Shareholders.

**9. Loans and borrowings**

As at 30 June 2017, PEPEES S.A. Group had borrowings, which are presented in the table below:

*(amounts in PLN 000s)*

**Table 3: Borrowings as at 30.06.2017**

<b>Loan type /Agreement/</b>	<b>Lending bank</b>	<b>Contractual loan value</b>	<b>Debt as at 30.06.2017</b>	<b>Repayment date</b>
1	2	3	4	5
Overdraft facility (Pepees)	Bank Zachodni WBK S.A.	4,000	0	31.08.2017
Revolving loan (Pepees)	Bank Zachodni WBK S.A.	10,000	1,575	31.08.2017
Working capital loan for the purchase of potatoes (Pepees)	Bank Zachodni WBK S.A.	15,000	3,750	31.08.2017
Overdraft facility (Pepees)	BGŻ BNP Paribas	4,000	0	31.08.2017
Revolving loan	BGŻ BNP Paribas	10,000	3,750	31.08.2017
Working capital loan for the purchase of potatoes (Pepees)	BGŻ BNP Paribas	15,000	5,625	31.08.2017
Subsidised investment loan	Bank Spółdzielczy S.A./Bank	3,465	0	30.06.2017

(Pepees)	Polskiej Spółdzielczości S.A.			
Subsidised investment loan (Pepees)	Bank Polskiej Spółdzielczości S.A.	1,295	332	30.11.2018
Investment loan (Pepees)	BNP Paribas	9,822	6,464	25.02.2022
Investment loan (Pepees)	Bank Ochrony Środowiska S.A.	1,200	1,024	31.12.2020
Loan (Pepees)	BNP Paribas Lease Group sp. z o.o.	533	267	13.06.2018
Overdraft facility (ZPZ Lublin)	Bank Zachodni WBK S.A.	500	0	31.08.2017
Revolving working capital loan in a credit account (ZPZ Lublin)	Bank Zachodni WBK S.A.	3,000	1,125	31.08.2017
Non-revolving working capital loan in a credit account (ZPZ Lublin)	Bank Zachodni WBK S.A.	1,500	375	31.08.2017
Overdraft facility (PPZ Bronisław)	Bank Zachodni WBK S.A.	500	0	31.08.2017
Revolving working capital loan in a credit account (PPZ Bronisław)	Bank Zachodni WBK S.A.	3,000	1,125	31.08.2017
Non-revolving working capital loan in a credit account (PPZ Bronisław)	Bank Zachodni WBK S.A.	8,000	1,914	31.08.2017
Overdraft facility (ZPZ Lublin)	BGŻ BNP Paribas	500	0	31.08.2017
Revolving working capital loan in a credit account (ZPZ Lublin)	BGŻ BNP Paribas	3,000	1,125	31.08.2017
Non-revolving working capital loan in a credit account (ZPZ Lublin)	BGŻ BNP Paribas	1,500	562	31.08.2017
Overdraft facility (PPZ Bronisław)	BGŻ BNP Paribas	500	0	31.08.2017
Revolving working capital loan in a credit account (PPZ Bronisław)	BGŻ BNP Paribas	3,000	746	31.08.2017
Non-revolving working capital loan in a credit account (PPZ Bronisław)	BGŻ BNP Paribas	8,000	3,932	31.08.2017
Working capital loan to finance current liabilities associated with business activities (CHP Energia)	Spółdzielczy Bank Rozwoju Branch in Szepietowo	3,000	2,820	31.05.2017
The overdraft facility to cover payment obligations related to the business activities (CHP Energia)	Spółdzielczy Bank Rozwoju Branch in Szepietowo	1,000	812	23.02.2017
Syndicated investment loan to implement the investment project "The Construction of a Biogas Plant in Szepietowo District" (CHP Energia)	1. Spółdzielczy Bank Rozwoju Branch in Szepietowo 2. Bank Spółdzielczy in Brańsk 3. Bank Spółdzielczy Branch in Andrzejów	12,830	12,224	31.12.2023
Working capital loan associated with business	Spółdzielczy Bank Rozwoju Branch in Szepietowo	800	720	31.12.2019

activities (CHP Energia)				
Investment loan to finance/refinance the purchase of a real property (PPZ Bronisław)	Bank Zachodni WBK S.A.	800	716	30.11.2021
Loan from a counterparty (CHP Energia)	CES	1,500	823	07.12.2017

## 10. Cash loans, guarantees and sureties granted

*Sureties granted by the parent company PEPEES S.A. as at 30 June 2017:*

The agreement of 9 June 2014 concerning the conditions of granting a security for a loan repayment concluded between PEPEES S.A. in Łomża and CHP Energia sp. z o.o. Pursuant to the agreement, PEPEES S.A. grants the security for the repayment of the investment loan taken out by CHP Energia sp. z o.o. The value of the investment loan taken by CHP Energia sp. z o.o. amounts to PLN 12,830 thousand. The security granted by PEPEES S.A. is in the form of an endorsement on bills of exchange up to the amount of PLN 12,224 thousand for the period until 25 May 2024.

*Sureties granted to the parent company PEPEES S.A. as at 30 June 2017:*

Short-term loans are secured with e.g. mortgages on the assets of the subsidiaries: ZPZ Lublin sp. z o.o. and PPZ Bronisław sp. z o.o.

In the first half of 2017, the subsidiaries neither granted nor obtained any sureties. In the first half of 2017, the companies form PEPEES S.A. Group neither granted nor obtained any sureties.

## 11. Description of the use of emission earnings

In 2017, the Company and the Group did not issue any shares and did not acquire any Treasury shares.

## 12. Explanation of differences between the financial results disclosed in the report and previously published forecasts for the year

The Company and the Group did not publish financial forecasts for 2017.

## 13. Financial resources management assessment

In the first half of 2017, the Parent Company and the Group were fully capable of meeting their obligations towards both suppliers and financial institutions. There was no risk of default. Also in the next reporting period, there should be no risk of losing financial liquidity by the Group. Any cash surpluses were placed in short-term deposits.

#### **14. Risk-related financial instruments, and the objectives and methods of financial risk management**

The information on used financial instruments and the financial risk are the same for both the Group and the Parent Company, which coordinates the process of managing the aforementioned risk at the Group level.

The main financial instruments used by the Group comprised bank loans, lease agreements, short-term deposits, and cash.

In the reporting period, the Group did not conclude transactions involving derivatives. It also did not apply hedge accounting.

Other instruments arising directly in the course of business comprised trade receivables and payables.

The main financial risks in 2017 include the risk of changes in market prices of products manufactured by the Group, and the currency risk. The Company's main objective in the area of the management of these risks is their elimination or mitigation.

The Group's business risk is closely related to changes in product prices on the Polish market and foreign exchange rates, whose fluctuations affect the revenue from export sales. Also, the purchase prices of imported materials for the production process depend on the level of currency risk.

Due to the financing of operating and investing activities with bank loans, the Group is exposed to the interest rate risk.

The liquidity risk in the Group is not deemed high. This is due to the proper implementation of the trade credit management policy. KUKI evaluates counterparties and insures receivables.

Any cash surpluses are placed in short-term deposits, which make it possible to pay obligations when due. In periods of greater demand for working capital, i.e. during the 'potato campaign', the short-term bank loan for the purchase of potatoes, whose individual tranches are closely correlated with the schedule of the purchases of the raw material for the production process, is the main financial instrument used by the companies in the Group.

Boards of Directors of the companies verify and agree on the management policies for each of the risks. They monitor the market price risk for all financial instruments held by them.

#### **15. Completed and planned investment projects**

In the first half of 2017, the Group carried out several investment projects. The most important of them are as follows:

- the purchase and assembly of a pulp-making centrifuge;
- the upgrade of the starch packing node to ensure automatic palletizing;
- the system of filling tanks with starch using BIG-BAGs;
- the upgrade of the starch collection system after sieves;
- a screw conveyor over rasp bins;
- the purchase of the 1-step column for WIEGAND evaporator;
- the upgrade of the loading sleeve of a tank truck under SCRO-13 conveyor;
- the upgrade of the potato washing and feeding station.

In the second half of the year, the Group will continue initiated investment projects and will upgrade certain machinery and production equipment.

## 16. Environmental issues

The Issuer's company is located in the region called 'Poland's Green Lungs' covering areas in north-eastern Poland, which are the cleanest in Poland and offer the greatest value in terms of their natural environment.

When doing its business, the Group makes every effort to observe environmental requirements. The Company complies with all applicable legal regulations and laws, and holds all applicable permits related to emissions of pollutants, water intake, wastewater disposal or waste production.

Waste is managed in conditions which prevent the contamination of the environment and ensure human health and safety.

The Group's companies maintain quantitative and qualitative waste management records in accordance with the adopted classification and model documents referred to in relevant regulations.

## 17. Employment in the Group

**Table 4: Employment in the Group**

Specification	Average number of employees in the first half of 2017	As at 30.06.2017		Average number of employees in the previous financial year - 2016
		Women	Men	
Administrative employees	136	72	65	129
Workers	239	23	217	290
Employees on parental leaves and unpaid leaves	2	1	1	4
<b>Total</b>	<b>377</b>	<b>96</b>	<b>283</b>	<b>423</b>

## 18. Major R&D accomplishments

In the first half of 2017, the Group did not carry out any major R&D works.

## 19. Non-typical events with a significant impact on the Group's profit/loss on business activities in the first half of 2017

During the reporting period, there were no non-typical items affecting the financial result.

## **20. Corrections of errors from previous periods and changes in accounting policies**

The Group did not change voluntarily its accounting policies and did not correct errors from previous years.

## **21. Changes of the basic principles of the Group management process**

In the first half of 2017, there were no material changes of the principles of the Group management process.

## **22. Shares and rights to shares of PEPEES S.A. and interests in the Group's companies held by members of the management and supervisory personnel**

As at 30 June 2017 and as at the publication date of this report, the following members of the management and supervisory personnel of PEPEES S.A. in Łomża held the Company's shares: President of the Board of Directors of PEPEES S.A. – 701,000 shares with the nominal value of PLN 0.06 each, i.e. with the total value of PLN 42,060.

The management and supervisory personnel do not have rights to the Company's shares.

In the period from the date of the publication of the previous quarterly report, there have been no changes in the holding of shares and rights to shares as regards the management and supervisory personnel.

None of the members of the management and supervisory personnel hold shares in the Group's subsidiaries.

## **23. The Company's quotations in the first half of 2017**

The Company's shares have been listed on the Warsaw Stock Exchange since 22 May 1997. The share price on 2 January 2017 (the opening share price on the first day of 2017) was PLN 1.13. The highest share price in the reporting period was PLN 1.49 and the lowest share price was PLN 1.11. The following graph shows share prices of PEPEES in the first half of 2017.

*Quotations of Pepees S.A. from 2017-01-01 to 2017-06-30*



**24. Agreements, known to the Issuer, which may result in future changes in the proportions of the shares held by existing shareholders**

The Issuer does not possess any information about any agreements which may result in future changes in the proportions of the shares held by existing shareholders.

**25. The holders of any securities with special control rights related to the Issuer, and a description of those rights**

The Issuer's shareholders do not have any securities with special control rights related to the Issuer.

**26. The system of control of any employee share schemes**

The Group does not have any system of control of employee share schemes.

**27. Any restrictions on the transfer of the Issuer's securities, and any restrictions on voting rights incorporated in the Issuer's shares**

There are no restrictions on the transfer of the Issuer's securities.

**28. The entity authorised to audit and review the Issuer's financial statements**

PEPEES S.A. and its subsidiaries concluded the agreement concerning the review and audit of the financial statements for 2017 with **Mazars Audyt sp. z o.o.** with its registered office in Warsaw, Poland.

The agreements provide for the review of the separate and consolidated financial statements as at 30 June 2017, and for the audit of the separate and consolidated financial statements for the financial year from 1 January 2017 to 31 December 2017. The total remuneration under the agreement is PLN 60,000 plus VAT.

In the previous financial year, the total value of the auditor's services under the agreement amounted to PLN 55,000 plus VAT.

There were no other agreements concluded in the reporting period and in the previous period with the entity authorised to audit financial statements.

### **29. Information about proceedings before a court, a competent arbitration authority or a public administration body**

As at the balance sheet date, there is an unresolved case due to the lawsuit made by EPSILON Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych w Warszawie against PEPEES S.A. to repeal or to declare the invalidity of resolutions adopted on 25.04.2017 by the Annual General Meeting of Shareholders concerning the distribution of profit and the acquisition of Treasury shares. The proceedings are at an early stage and it is difficult to predict the outcome of the proceedings and to assess the chances of winning the case and thus the financial consequences.

### **30. Summary of activities in the reporting period**

From January to June 2017, PEPEES S.A. Group generated sales of PLN 116 million, which denoted an increase by 34.1% as compared to the corresponding period in the previous year. The increase in sales revenue was particularly influenced by higher export sales in PEPEES outside the European Union (an increase by 51%). Also PPZ Bronisław sp. z o.o. recorded an increase in sales by 13%.

Due to a lower growth rate for the costs of products sold (as compared to the growth rate for the revenue from the sales of products), in the first half of 2017, the Group generated gross profit from sales of PLN 30.5 million, which denoted an increase by 53% as compared to the same period in the previous year.

Selling and marketing expenses and administrative expenses in the period from January to June 2017 grew by 57% and 36% respectively relative to the comparative period.

The balance on other activities in the first half of 2017 closed at PLN 0.22 million as compared to the result of PLN 0.03 million in the comparative period.

On the other hand, the result on financing activities, understood as the balance of finance income less finance costs in the period from January to June 2017, was lower than the corresponding item in the comparative period — in 2017, it amounted to (-) PLN 2 million against () PLN 0.31 million in the period from January to June 2016.

As a consequence, gross profit after the first half of 2017 amounted to PLN 10.7 million against PLN 6.6 million of gross profit generated in the comparative period, and net profit in the period from January to June 2017 amounted to PLN 8.35 million against PLN 5.24 million of net profit in the corresponding period of 2016.

## 1. The Group's assets

Assets as at 30 June 2017 as compared to assets as at 31 December 2016 are shown in the table below.

**Table 5: Assets as at 30.06.2017 and 31.12.2016**

*(amounts in PLN 000s)*

Asset	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	30.06.2017	31.12.2016		30.06.2017	31.12.2016
<b>I. NON-CURRENT ASSETS (long-term)</b>	<b>142,517</b>	<b>138,339</b>	<b>4,178</b>	<b>62.7</b>	<b>50.8</b>
1. Property, plant and equipment	119,859	119,315	544	52.8	43.8
2. Investment property		0	0	0.0	0.0
3. Intangible assets	112	298	(186)	0.0	0.1
4. Goodwill arising on consolidation	6,607	6,607	0	2.9	2.4
5. Investment in the associate	4,310		4,310	1.9	0.0
6. Investments in other entities	113	113	0	0.0	0.0
7. Loans granted		0	0	0.0	0.0
8. Advances	9,362	9,649	(287)	4.1	3.5
9. Deferred tax assets	2,154	2,357	(203)	0.9	0.9
<b>II. CURRENT ASSETS (short-term)</b>	<b>84,683</b>	<b>133,827</b>	<b>(49,144)</b>	<b>37.3</b>	<b>49.2</b>
1. Inventories	29,300	77,283	(47,983)	12.9	28.4
2. Biological assets	747	158	589	0.3	0.1
3. Trade receivables	32,769	25,763	7,006	14.4	9.5
4. Other receivables	1,682	2,317	(635)	0.7	0.9
5. Advances	5,845	1,398	4,447	2.6	0.5
6. Loans granted	863	182	681	0.4	0.1
7. Investments held for trading	2,550	2,550	0	1.1	0.9
8. Cash and cash equivalents	10,927	24,176	(13,249)	4.8	8.9
<b>Total assets</b>	<b>227,200</b>	<b>272,166</b>	<b>(44,966)</b>	<b>100.00</b>	<b>100.00</b>

The Group assets being the total balance of the assets as at 30 June 2017 and amounting to PLN 227,200 thousand decreased by PLN 44,966 thousand, i.e. by 16.5%, as compared to the previous year.

The decrease was recorded mainly for inventories due to the seasonal processing of potatoes and cash resulting from the repayment of short-term loans. On the other hand, trade receivables increased in connection with the sales of seed potatoes and pesticides with the payment deadline until the time of delivering potatoes for processing.

## 2. Sources of financing for the Group

Sources of financing assets as at 30 June 2017 as compared to the assets as at 31 December 2016 are shown in the table below.

Table 6: Sources of financing assets as at 30.06.2017 and 31.12.2016

(amounts in PLN 000s)

Sources of financing	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	30.06.2017	31.12.2016		30.06.2017	31.12.2016
<b>I. Equity</b>	<b>137,185</b>	<b>129,119</b>	<b>8,066</b>	<b>60.4</b>	<b>47.4</b>
<i>Equity attributable to equity holders of the parent</i>	<i>136,105</i>	<i>128,199</i>	<i>7,906</i>	<i>59.9</i>	<i>47.1</i>
1. Share capital	5,700	5,700	0	2.5	2.1
2. Reserve capital and other reserves	124,418	106,065	18,353	54.8	39.0
3. Revaluation reserve	(328)	(278)	(50)	-0.1	-0.1
4. Retained earnings/loss	(1,877)	(888)	(989)	-0.8	-0.3
5. Profit/loss for the year	8,192	17,600	(9,408)	3.6	6.5
<i>Non-controlling interests</i>	<i>1080</i>	<i>920</i>	<i>160.0</i>	<i>0.5</i>	<i>0.3</i>
<b>II. Non-current liabilities</b>	<b>41,490</b>	<b>42,696</b>	<b>(1,206)</b>	<b>18.3</b>	<b>15.7</b>
1. Loans and borrowings	22,200	22,370	(170)	9.8	8.2
2. Liabilities related to leased assets	4,340	4,677	(337)	1.9	1.7
3. Deferred tax liabilities	5,655	5,722	(67)	2.5	2.1
4. Retirement and similar benefits obligations	2,296	2,240	56	1.0	0.8
5. Grants	6,999	7,687	(688)	3.1	2.8
<b>III. Current liabilities</b>	<b>48,525</b>	<b>100,351</b>	<b>(51,826)</b>	<b>21.4</b>	<b>36.9</b>
1. Trade payables	10,618	11,956	(1,338)	4.7	4.4
2. Current income tax liabilities	1,165	3118	(1,953)	0.5	1.1
3. Other current liabilities	3,358	5,088	(1,730)	1.5	1.9
4. Loans and borrowings	29,607	76,080	(46,473)	13.0	28.0
5. Finance lease payables	1,748	1,901	(153)	0.8	0.7
6. Retirement benefit obligations	349	331	18	0.2	0.1
7. Provisions for other liabilities	1,680	1,877	(197)	0.7	0.7
<b>Total equity and liabilities</b>	<b>227,200</b>	<b>272,166</b>	<b>(44,966)</b>	<b>100.0</b>	<b>100.0</b>

The structure of the financing changed in the first half of the year. The share of equity increased due to the generated net profit. On the other hand, current liabilities decreased. The biggest decrease was recorded for loan commitments due to the repayment of loans taken out to purchase potatoes in autumn last year.

### 3. The Group's financial results

The financial results for the Group's business activities for the first half of 2017 and the first half of 2016 are shown in the table below.

Table 7: The financial result for the first half of 2017 and of 2016

(amounts in PLN 000s)

No.	Specification	Actual results for the first half of 2017	Actual results for the first half of 2016	Growth rate in %
<b>1.</b>	<b>Sales revenue</b>			
	Revenue from the sales of products	98,044	70,962	138.2
	Revenue from services	589	355	165.9
	Revenue from the sales of trade goods and materials	17,378	15,178	114.5
	<b>Total sales revenue, including:</b>	<b>116,011</b>	<b>86,495</b>	<b>134.1</b>
	- revenue from continuing operations	116,011	86,495	134.1
	- revenue from discontinued operations			
	<b>Cost of sales</b>			
	Cost of products sold	(69,627)	(52,027)	133.8
	Cost of services sold	(349)	(74)	471.6
	Costs of trade goods and materials sold	(15,041)	(14,076)	106.9
	Profit/loss from agricultural production	(457)	(388)	117.8
	<b>Total cost of sales, including:</b>	<b>(85,474)</b>	<b>(66,565)</b>	<b>128.4</b>
	- cost from continuing operations	(85,474)	(66,565)	128.4
	- cost from discontinued operations			
	<b>Gross profit from sales (I-II)</b>	<b>30,537</b>	<b>19,930</b>	<b>153.2</b>
	Selling and marketing expenses	(5,450)	(3,460)	157.5
	Administrative expenses	(12,626)	(9,285)	136.0
	Other operating income (net profit)	487	241	202.1
<b>2.</b>	Other operating expenses (net loss)	(272)	(214)	127.1
	<b>Operating profit (loss)</b>	<b>12,676</b>	<b>7,212</b>	<b>175.8</b>
	Finance costs (net losses)	(2,147)	(802)	267.7
	Finance income (net profit)	150	497	30.2
	Share of profit (loss) of an associate	(2)	(276)	0.7
<b>3.</b>	<b>Profit (loss) before tax, including:</b>	<b>10,677</b>	<b>6,631</b>	<b>161.0</b>
	- profit (loss) before tax from continuing operations	10,677	6,631	161.0
	- profit (loss) before tax from discontinued operations			
	Income tax expense	(2,325)	(1,393)	166.9
	<b>Net profit (loss), including:</b>	<b>8,352</b>	<b>5,238</b>	<b>159.5</b>
<b>4.</b>	- attributable to non-controlling interests	160	59	271.2
	- attributable to the equity holders of the parent, including:	8,192	5,179	158.2
	- net profit (loss) from continuing operations	8,192	5,179	158.2
<b>5.</b>	- net profit (loss) from discontinued operations			
	<b>Net earnings (loss) per share, including:</b>	0.06	0.05	
<b>6.</b>	- net earnings per share from continuing operations	0.06	0.05	120.0
	- net earnings (loss) per share from discontinued operations			

Sales revenue for the first half of the year increased as compared to the same period in the previous year by 34.1%. The margin on the sales of products increased, owing to which the operating profit increased by 75.8%, while net profit attributable to equity holders of PEPEES rose by 58.2%.

#### 4. Cash flows

In the first half of 2017, PEPEES S.A. Group recorded negative cash flow balance due to the high repayment level of short-term loans. The balance from operating activities is positive and

amounts to PLN 44,119 thousand. Cash in the consolidated statement of cash flows as at 30 June 2017 is positive and amounts to PLN 10,115 thousand. The difference amounting to PLN 812 thousand between the cash reported in the balance sheet and the cash reported in the statement of cash flows stems from the bank overdraft balance.

## 5. Economic ratios

The summary of ratios characterising the Group's business and situation is presented in Table 7 below.

**Table 8: Economic ratios**

Ratio	Commercial substance	First half of 2017	First half of 2016
Return on Assets	$\frac{\text{net profit/loss attributable to equity holders of the Company} * 100}{\text{total assets}}$	3.61%	2.97%
Return on Equity	$\frac{\text{net profit/loss attributable to equity holders of the Company} * 100}{\text{equity}}$	6.02%	4.53%
Net Profit Margin	$\frac{\text{net profit/loss attributable to equity holders of the Company} * 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	7.06%	5.99%
Return on Sales	$\frac{\text{gross profit/loss from sales} * 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	26.32%	23.04%
Current Ratio	$\frac{\text{total current assets}}{\text{current liabilities}}$	1.75	1.99
Quick Ratio	$\frac{\text{total current assets} - \text{inventories}}{\text{current liabilities}}$	1.14	1.30
Receivables Turnover in days*	$\frac{\text{average trade receivables} * 180}{\text{net revenue from the sales of products, services, trade goods and materials}}$	45.41	48.43
Accounts Payable Turnover in days*	$\frac{\text{average trade payables} * 180}{\text{costs of trade goods and services sold} + \text{value of trade goods and materials}}$	23.77	20.21
Inventory Turnover in days*	$\frac{\text{average inventories} * 180}{\text{costs of products and services sold} + \text{value of trade goods and materials}}$	112.23	120.92
Equity to Fixed Assets Ratio	$\frac{\text{equity attributable to equity holders of the Company} * 100}{\text{total non-current assets}}$	0.96	1.12
Gearing Ratio	$\frac{(\text{equity attributable to equity holders of the Company} + \text{non-current provisions} + \text{non-current liabilities}) * 100}{\text{total equity and liabilities}}$	0.70	0.70

\*To calculate turnover ratios, the Group used amounts as at the beginning and as at the end of each reporting period.

Profitability ratios increased as compared to the previous half-year due to the higher net profit. Liquidity ratios deteriorated slightly, which is related to the emergence of a new related party in the Group, i.e. CHP Energia sp. z o.o., which has significant debt. Also the Inventory Turnover Ratio decreased due to higher sales. Equity to fixed assets ratio is still relatively high, as, due to the high percentage of equity in the financing structure, it is close to 1.0.

4.

**IV. The Group's development****1. Description of underlying risks and threats and of external and internal drivers of the Group's development****1.1****Risks and threats**

- **The dependence of the production on weather and seasonality**

Potatoes are the only raw material for the production process. As a result, the volume and quality of the production depends on the potatoes harvest. Weather anomalies are reflected directly in the amount of starch produced and offered for sale.

- **Globalisation**

Globalisation is noticeable mainly in terms of competitiveness. At present, there is strong competition from substitutes. In the food industry, there are a lot of products that perform similar functions (fillers and thickeners) as potato starch, i.e. wheat starch, corn starch, imported natural hydrocolloids such as guar gum, xanthan gum, gum arabic, locust bean gum and gelatin.

In the period of a limited supply of potato starch, the substitutes are gradually entering the industry. This poses a risk of a partial loss of markets for the Company's products. In addition, there is a lot of competition on the internal starch market in the European Union.

- **Dependence on the profitability of potato production**

Due to high costs of potato production, it is being supplanted by other more profitable agricultural crops. In addition, the north-eastern part of Poland became a large production region for the dairy industry, which 'steals' agricultural areas from other industries. For this reason, it is getting more and more difficult to find new growers in the areas near the plant. As a result, the Group is forced to purchase raw materials from remote regions of Poland, which results in reduced profitability.

- **Currency risk**

Such risk arises as a result of the international trade in currencies other than the Polish złoty. Fluctuations of foreign currency exchange rates adversely affect the profitability of foreign transactions; however, the materiality of this risk is slight due to the purchases made in the currencies of sales.

- **Economic fluctuations**

The state of the economic activity in the world, in Poland and in a particular sectors, affects the operations of a company through a variety of indicators and ratios (GDP, prices, wages, employment).

- **Limited money supply**

Less and less available and more and more expensive money on the market is the effect of the global crisis. This hits manufacturers very hard. They are forced to grant trade credits to their customers and extend payment deadlines.

- **Too expensive instruments that increase sales safety**

Granting credits to customers increases the risk of the failure to get paid for deliveries. Related financial products offered on the market are expensive and contribute to the extension of the transaction execution stage.

- **The sale of a product posing a risk to consumer health and life**

The Group manufactures food. In the case of the sale of a product posing a risk to consumer health or life, the Group's image would be severely tarnished, and the Group would have the obligation to pay compensations to customers and consumers, and to cover the costs related to the product recall and disposal.

The risk is very limited due to the Corporate Food Quality and Safety Management System.

The product recall procedure has been implemented, and recall simulations are carried out.

## **1.2 External drivers of the Group's successful development**

The Group's development as regards the potato industry depends primarily on the agricultural policy of the European Union and of Poland, and on the creation of proper conditions for the operation of the agricultural and food industry.

The main drivers of the Group's successful development are as follows:

- the development of the Polish food industry (in the long-term assessment of market analysts, the food industry is a growing industry);
- the possibility of obtaining financial means from EU funds to finance investment projects;
- the market demand for modified potato starch products;
- the access to new and modern technologies;
- the development of markets in international trade;
- the development of specialised agricultural holdings;

- a wide range of the applications of starch and its derivatives.

### 1.3 Internal drivers of the Group's successful development

The most vital internal Group-dependent drivers important for the Group's further development are as follows:

- gradual modernisation of production departments in order to boost the efficiency and innovation of products, and to reduce operating costs;
- active policy concerning sales and the acquisition of new markets;
- implemented Corporate Food Quality and Safety Management System;
- implemented Test and Research Quality Management System;
- the Company's compliance with Smeta; the presence on SeDeX platform;
- acquired so-called 'promotional emblem' licences;
- a good cooperation with growers;
- the possibility of producing hydrolysates to meet specific customers' needs;
- low costs of the disposal of industrial wastewater;
- high production capabilities.

## 2. The Group's development prospects

In the first half of 2017, PEPEES S.A. Group pursued its strategic objectives consistently, which made it possible to generate excellent financial and operating results. The directions of the development of PEPEES Group still comply with the Strategy for 2013 -2018 published in autumn 2013.

Entering new markets resulted in a significant increase in revenue, especially from international markets, which, as compared to the first half of 2016, increased by over 50%.

The development plans aim at ensuring further capital commitment and improving the Group's competitive position on the market by boosting sales, optimising costs and increasing shareholder value.

## 3. Factors likely, in the issuer's opinion, to influence the results generated by the Company in the period of at least one quarter

In the next quarter, the Group will launch 'the autumn potato campaign.' The quantities of purchased potatoes, which is the basic raw material for the production of the Group's companies, will have a significant impact on the production volume and the sales value in the next quarter, and hence the level of financial results.

<i>Podpisy wszystkich Członków Zarządu</i>			
<i>Data</i>	<i>Imię i Nazwisko</i>	<i>Stanowisko/Funkcja</i>	<i>Podpis</i>
30.08.2017	Wojciech Faszczewski	Prezes Zarządu	
30.08.2017	Tomasz Rogala	Członek Zarządu	