

DIRECTORS' REPORT

ON THE GROUP'S OPERATIONS

for 2018

**(including disclosures required for the Directors' Report
in the aforementioned period)**

26 March 2019

Łomża

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Introduction

This Directors' Report on the Operations of PEPEES Group for 2018 provides disclosures whose scope was specified in § 70 and 71 of the Regulation of the Polish Minister of Finance dated 29 March 2018 on current and periodic information published by issuers of securities [...] ('the Regulation').

The consolidated annual report, which comprises the aforementioned financial statements and this Directors' Report, has been prepared pursuant to §70 and §71 in connection with §60(1)(3) and §60(2) of the Regulation.

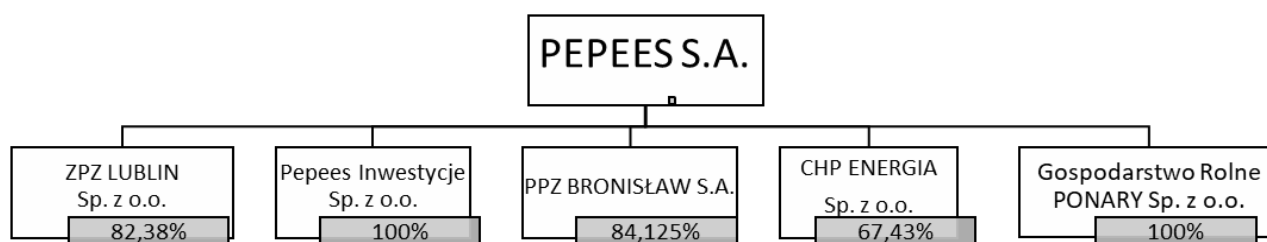
Pursuant to §71(8) of the Regulation, this report also comprises disclosures required for the Directors' report on the operations of the Parent Company referred to in §70(1)(4) of the Regulation.

The principles of the preparation of financial statements have been presented in respective financial statements, i.e. in the financial statements of the Parent Company and in the financial statements of the Group for 2018.

I. The structure of PEPEES Group

Przedsiębiorstwo Przemysłu Spożywczego PEPEES S.A. (hereinafter also 'the Issuer', 'the Company', 'PEPEES S.A.') is the parent company for: Zakłady Przemysłu Ziemniaczanego 'ZPZ Lublin' Sp. z o.o., Przedsiębiorstwo Przemysłu Ziemniaczanego 'BRONISŁAW' S.A., Pepees Inwestycje Sp. z o.o. (former OZENERGY Sp. z o.o.), Gospodarstwo Rolne Ponary Sp. z o.o. and CHP Energia Sp. z o.o.

The composition of the Group as at 31 December 2018 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.

It operates as a joint stock company incorporated under a notarial deed on 21 June 1994 signed before the notary public Mr Paweł Błaszczyk in Warsaw (Notarial Record Book A No. 14126/94).

The Company is entered in the Register of Entrepreneurs kept by the District Court in Białystok, XII Economic Division of the National Court Register (KRS) in Białystok under No. KRS 000038455.

It has its Taxpayer Identification Number (NIP): 7181005512, assigned by the Tax Office in Łomża on 20 January 2000.

The statistical office assigned the following identification number (REGON) to the Company: 450096365.

The Company operates pursuant to the Polish Commercial Code. It is a single-establishment company; it does not have any branches.

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 31 December 2018 amounted to PLN 5,700 thousand and was divided into the following series:

- series A – 83,000 thousand ordinary bearer shares with the nominal value of PLN 0.06 each;
- series B – 12,000 thousand ordinary bearer shares with the nominal value of PLN 0.06 each.

To the best of our knowledge, as at 31.12.2018, the shareholding structure was as follows:

- Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych – the number of votes: 23,345,498; percentage of total votes at the GMS – 24.57%
- Mr Michał Skotnicki – the number of votes: 21,325,780; percentage of total votes at the GMS – 22.45%
- Mr Maksymilian Maciej Skotnicki – the number of votes: 20,703,282; percentage of total votes at the GMS – 21.79%
- Mr Newth Jonathan Reginald – the number of votes: 7,995,200; percentage of total votes at the GMS – 8.42%
- Richie Holding Ltd – the number of votes: 6,133,100; percentage of total votes at the GMS – 6.46%

The Issuer would like to remember that Mr Maksymilian Maciej Skotnicki and Mr Michał Skotnicki are persons referred to in Article 87(4)(1) of the Act on public offering [...] and, thus, together they hold the total of 42,029,062 shares/votes representing 44.24% of the share capital of/the total number of votes in the Company.

To the best of the Company's knowledge, none of the remaining shareholders informed about the holding of at least 5% of the share capital and total votes at the GMS.

After the end of the reporting period, the Company received information according to which, in January 2019, there had been a change in the shareholding structure, as a result of which Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych had notified the Company about increasing its holding in the Company by acquiring the total of 3,980,000 shares. Hence,

as at the date of this report, the shareholding structure is as follows:

- Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych – the number of votes: 27,609,982; percentage of total votes at the GMS – 29.06%
- Mr Michał Skotnicki – the number of votes: 21,325,780; percentage of total votes at the GMS – 22.45%
- Mr Maksymilian Maciej Skotnicki – the number of votes: 20,703,282; percentage of total votes at the GMS – 21.79%
- Mr Newth Jonathan Reginald – the number of votes: 7,995,200; percentage of total votes at the GMS – 8.42%
- Richie Holding Ltd – the number of votes: 6,133,100; percentage of total votes at the GMS – 6.46%

To the best of the Company's knowledge, as at the date of this report, none of the remaining shareholders informed about the holding of at least 5% of the share capital and total votes at the GMS.

1.2 The company's authorities

Board of Directors

In the period from 1 January 2018 to 31 December 2018, the composition of the Board of Directors of PEPEES S.A. was as follows:

Mr Wojciech Faszczeński – President

Mr Tomasz Rogala – Member

After the end of the reporting period, there have been no changes in the composition of the Company's Board of Directors.

The Board of Directors is composed of one to five members. The Supervisory Board appoints the President of the Board of Directors and, upon the motion of the President of the Board of Directors, also other members of the Board of Directors. Members of the Board of Directors are dismissed by the Supervisory Board. The Board of Directors exercises 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. The Issuer's Board of Directors does not have any powers to issue or repurchase shares – the Company has not established any target capital.

Supervisory Board

From 1 January 2018 until 17 December 2018, 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. Ms Agata Czerniakowska – Member
5. Mr Robert Malinowski – Member

On 18 December 2018, the Extraordinary General Meeting of Shareholders dismissed the following members of the Supervisory Board: Mr Maciej Kaliński – Chairman of the Supervisory Board; Mr Piotr Taracha – Vice-Chairman of the Supervisory Board; Mr Krzysztof Stankowski – Secretary of the Supervisory Board; Ms Agata Czerniakowska – a Member of the Supervisory Board; and Mr Robert Malinowski – a Member of the Supervisory Board. Simultaneously, on the same day, the Extraordinary General Meeting of Shareholders

appointed the same persons as members of the Supervisory Board and additionally appointed Mr Tomasz Nowakowski as a member of the Supervisory Board.

Thus, the composition of the Supervisory Board as at 31 December 2018 is as follows:

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

Until the date of this report, there had been no changes in the composition of the Company's Supervisory Board.

Members of the Supervisory Board are appointed and dismissed by the General Meeting of Shareholders.

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

2.1 General information about the company

The Company's registered office is in Lublin, at the address: ul. Betonowa 9. The Company is a limited liability company established by virtue of a notarial deed on 8 November 1996 signed in the notary public's firm run by Ms Antonina Renata Bednara in Lublin, at ul. Spokojna 8, Notarial Record Book A No. 6437/96, for an indefinite lifetime. The Company is entered in the Register of Entrepreneurs kept by the District Court in Lublin, XI Economic Division of the National Court Register (KRS) in Białystok under No. KRS 0000050886.

The company has its Tax Identification Number (NIP): 9461580419. The company operates pursuant to the Polish Commercial Code.

The Company's objects are mainly the processing of potatoes and the production and sales of glucose syrup.

The Company's share capital as at 31 December 2016 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

In the period from 1 January 2018 to 31 December 2018, the composition of the company's Board of Directors was as follows:

- Mr Piotr Kaniowski – President
- Ms Małgorzata Dudzic – Member, Chief Financial Officer

Supervisory Board

The composition of the Supervisory Board as at 31.12.2018 was as follows:

- Mr Wojciech Faszczewski – Chairman

- Mr Piotr Taracha – Vice-Chairman
- Mr Piotr Łojko – Secretary
- Mr Mariusz Świetlicki – Member
- Ms Agata Czerniakowska – Member

3. Pepees Inwestycje Spółka z ograniczoną odpowiedzialnością in Łomża (former OZENERGY) – a subsidiary

The company's registered office is in Łomża, at the address: ul. Poznańska 121. The Company was established by virtue of a notarial deed (Notarial Record Book A No. 12369/2010) on 18 October 2010 signed before a notary public Tomasz Poreda in Łomża.

The Company is entered in the Register of Entrepreneurs kept by the District Court in Białystok, XII Economic Division of the National Court Register (KRS) in Białystok under No. KRS 0000370060.

The company has its Tax Identification Number (NIP): 7182123627. The company operates pursuant to the Polish Commercial Code.

The company's objects according to its Articles of Association is buying and selling of own real estate. The company had not commenced operations until the balance sheet date.

The company's share capital as at 31 December 2018 amounted to PLN 95,000 and was divided into 1,900 equal and indivisible shares, each with the value of PLN 50.

In the period from 1 January 2018 to 31 December 2018, the composition of the company's Board of Directors was as follows: Mr Roman Minierski – President.

4. Przedsiębiorstwo Przemysłu Ziemniaczanego BRONISŁAW Spółka Akcyjna in Bronisław – a subsidiary

4.1 General information about the company

Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław S.A. has been operating since 23 November 2001. On 12.12.2017 (the date of the registration in the National Court Register), Przedsiębiorstwo Przemysłu Ziemniaczanego Spółka z ograniczoną odpowiedzialnością was transformed from a limited liability company into a joint stock company called Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław Spółka Akcyjna.

The company's registered office is in Bronisław 41, 88-320 Strzelno. The company is a joint stock company established by virtue of a notarial deed on 31.07.2017, Notarial Record Book A No. 1989/2017, for an indefinite lifetime. The company is entered in the Register of Entrepreneurs kept by the District Court in Bydgoszcz, XIII Economic Division of the National Court Register (KRS) in Bydgoszcz under No. KRS 0000708945.

The company has its Tax Identification Number (NIP): 5571595182. The company operates pursuant to the Polish Commercial Code.

The company's objects are as follows:

- manufacture of starches and starch products;
- processing and preserving of potatoes;
- support activities for crop production.

The company's share capital as at 31 December 2018 amounted to PLN 800,000 and was divided into 800,000 shares, each with the nominal value of PLN 1. The shares are not preference shares.

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

In the period from 1 January 2018 to 31 December 2018, the composition of the company's Board of Directors was as follows:

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

Supervisory Board

The composition of the Supervisory Board as at 31.12.2018:

- Mr Piotr Taracha – Chairman
- Ms Agata Czerniakowska – Vice-Chairman
- Mr Grzegorz Dobrowolski – Member
- Mr Stanisław Bukowski – Member
- Ms Gabriela Michalska – Member since 04.04.2018
- Mr Robert Malinowski – Member since 21.05.2018

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

5.1 General information about the company

The company with its registered office in Wojny-Wawrzyńce was established on 27 April 2011 on the basis of the notarial deed, Notarial Record Book A No. 1163/2011. The company operates in the form of a limited liability company. The company is entered in the Register of Entrepreneurs kept by the District Court in Białystok, XII Economic Division of the National Court Register (KRS) under No. KRS 0000390180.

The company has its Tax Identification Number (NIP): 7721624470. The company operates pursuant to the Polish Commercial Code.

The company's objects are as follows:

- power generation;
- electricity transmission and distribution.

The company's share capital as at 31 December 2018 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

In the period from 1 January 2018 to 31 December 2018, the composition of the company's Board of Directors was as follows:

- Mr Andrzej Wszyński – President

- Mr Mirosław Siemieniako – Vice-President

Supervisory Board

The composition of the Supervisory Board as at 31.12.2018:

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

6. Gospodarstwo Rolne Ponary Sp. z o.o. - a subsidiary

6.1 General information about the company

The company's registered office is in Łomża, at the address: ul. Poznańska 121. The company is a limited liability company established by virtue of a notarial deed on 10 November 2015 for an indefinite lifetime. The company is entered in the Register of Entrepreneurs kept by the District Court in Białystok, XII Economic Division of the National Court Register (KRS) in Białystok under No. KRS 0000585975.

The company has its Tax Identification Number (NIP): 1132898091. The company operates pursuant to the Polish Commercial Code.

The company's objects comprise growing of crops combined with farming of animals (mixed farming).

The company's share capital as at 31 December 2018 amounts to PLN 1,620,000 and is divided into 32,400 equal and indivisible shares, each with the nominal value of PLN 500. PEPEES is the sole shareholder of the company.

6.2 The company's authorities

Board of Directors

In the period from 1 January 2018 to 31 December 2018, the composition of the company's Board of Directors was as follows:

- Mr Tomasz Rogala – President.

7. Changes in the organisation of PEPEES Group

On 4 January 2018, PEPEES entered into a conditional sales agreements with two natural persons, who are shareholders of the Company, under which the Company acquired a 32.6% stake in Gospodarstwo Rolne Ponary Sp. z o.o. Thus, the Company has become the holder of 100% of shares in Ponary.

The acquisition of Ponary will make it possible for the Issuer to continue agricultural investments without the risk of losing them upon the expiry of the lease agreement. The holding of 100% of shares in Ponary ensures the implementation of the strategy in terms of the availability of the raw material through own cultivation of starch potato.

By way of the resolution of the Extraordinary General Meeting of Shareholders of OZEnergy of 10 May 2018, the name of this company was changed to: PEPEES Inwestycje Spółka z ograniczoną odpowiedzialnością. The core objects were also changed to: 'Buying and selling of own real estate'.

The name and objects have been changed due to the fact that Pepees Inwestycje is planning to launch its real estate brokerage business.

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

II. Factors and events affecting the Group's operations

1. The market

There are three segments in PEPEES Group, i.e.: 'processing of potatoes', 'power generation' and 'growing of crops combined with farming of animals (mixed farming)'. All assets and liabilities of CHP Energia are allocated to the 'power generation' segment. All assets and liabilities of Gospodarstwo Rolne Ponary are allocated to 'growing of crops combined with farming of animals (mixed farming)' segment, and all other assets and liabilities disclosed in the consolidated financial statements are allocated to the 'processing of potatoes' segment.

Due to the fact that in 2018 Ponary did not generate any sales revenue, the 'growing of crops combined with farming of animals (mixed farming)' segment was not separated in segments' revenue and net profit/loss. Due to the value of the land owned by Ponary, the third segment has been separated in the consolidated financial statements only to present its assets and liabilities.

'The processing of potatoes' segment 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. Germany is the largest manufacturer of potato starch in the EU, followed by the Netherlands and then by France and Denmark. Enterprises from the EU are large starch production plants, which process from 3,000 to 5,000 tonnes of potatoes daily. The three leading European companies (Emsland from Germany, Avebe from the Netherlands, Roquette from France) produce ca. 65% of the EU's starch.

In the EU, in recent years, the output amounted to ca. 1.9 million tonnes p.a.; 92% of that amount were 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%.

The Polish starch industry comprises 10 companies which produce potato starch and its derivatives. The Polish starch industry is heavily fragmented. There are five largest starch production plants on the Polish market with processing capacities of up to 1000-2400 tonnes of potatoes daily. These are plants located in Łomża (PEPEES S.A.), Luboń, Trzemeszno, Piła and Łobez. The remaining Polish starch production plants are much smaller and capable of processing about 300-800 tonnes of potatoes daily.

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

Potato starch

Potato starch is obtained through mechanical crushing of potatoes, extraction, refining, dehydration, drying and sifting.

Starch is one of the most multifunctional raw materials in the food industry. In some applications, its natural properties enabling the production of gels and thickening are exploited (food, chemical, textile, paper industries).

In the food and pharmaceutical industries, starch is used to give products proper texture, appearance (form), moisture, consistence and durability during their storing.

Starch hydrolysates

- Crystalline glucose

Crystalline glucose is the end product of the hydrolysis of potato starch. It is a white, fine-crystalline powder with sweet taste. Its microbiological purity is very high and it contains ca. 99.5 % of pure glucose. Crystalline glucose is a high-calorie monosaccharide, easily absorbed by human organism. It is a valuable and natural source of energy. Glucose is often used in the production of pharmaceutical and dietary products (drugs, dietary supplements). Its consumption is particularly important during intense physical workout and recovery.

The food industry takes advantage primarily of the following glucose properties: sweet flavour, and enhancing the flavour of products. It is used for the production of confectionery, ice-cream

desserts, dry food mixes, non-alcoholic beverages, fruit and vegetable products. In addition, crystalline glucose is applied in the brewing, baking, wine and meat industries.

- Anhydrous glucose

Anhydrous glucose is a product obtained in the process of the fluidized bed drying of crystalline glucose until its moisture content is below 1%. The product meets high microbiological requirements. The entire production of anhydrous glucose is used by the pharmaceutical industry. It is used mainly in the production of infusion liquids.

- Maltodextrin

Maltodextrin is a product of the depolymerization of potato starch produced as a result of enzymatic hydrolysis. It is a white powder with a slightly sweet flavour. Maltodextrin properties depend on the degree of starch hydrolysis. An increase in DE (dextrose equivalent) results in greater sweetness, which is accompanied by increased solubility and hygroscopicity, and the reduction of viscosity, bonding power and resistance to crystallization. Due to its binding and filling properties, and its ability to improve texture and stabilise flavour and aroma, maltodextrin is applied in food production. It 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. Is an important carbohydrate ingredient of milk-based formulas and nutritional powders for infants. The share of maltodextrin in the reduced-calorie food production is substantial.

- Glucose syrups

Glucose syrups are concentrated, aqueous solutions of monosaccharides (glucose, maltose) and low molecular weight polysaccharides obtained in the process of the enzymatic hydrolysis of starch. They are temperature and chemically stable, and are characterised with high osmotic pressure. Glucose syrups are used in the production of hard and soft caramel drops, chewing gums, fruit jellies, ice cream, desserts, confectionery. Glucose syrup increases plasticity, affects the durability of the colour and flavour, and provides transparency and gloss. The syrup ensures the appropriate structure and delicate sweetness, improves structural properties, inhibits sugar crystallization, preserves the natural colour of fruit, adds delicate flavour, enhances the aroma.

- Potato protein

This product is obtained from potato intracellular fluid in the process of coagulation, separation and drying. Final product is a loose grey powder with the aroma typical for dried potato protein and moisture content not higher than 10 %. The product is characterised with a high total protein content (over 80 %), and the digestible protein constitutes over 70 % of dry substance. It is a high quality, easily digestible, vegetable protein; therefore, it is a valuable ingredient of feedstuff mixes for animals and an excellent substitute for animal protein.

- Food starch

Food starch is obtained from pulped cells of potato bulbs in the process of rinsing and then purifying, drying and sifting. Commercial product contains ca. 40 % of water. Food starch is produced from potatoes for industrial use with appropriate quality properties, i.e. high starch content with the highest possible percentage of large starch grains, small quantities of non-starch substances, low protein content, round potato bulbs, crisp pulp, shallow “eyes”.

- Hydrol

Hydrol is a waste product. This is an intercrystalline juice remaining after the separation of glucose crystals from the concentrated glucose syrup – massecuite. It is a dense, dark brown liquid with a characteristic aroma. Due to its high content of carbohydrates, hydrol is used in the spirits, feed-producing and chemical industries (e.g. for tanning).

- Grits

Grits are a waste product from the food starch-producing unit. These are lumps of lumpy and gruelled starch separated from dried potato starch.

- Potato flakes

Potato flakes are produced from edible varieties of potatoes. These are ca. 0.2-0.5mm flakes first hydrated with steam and then dehydrated.

In 2018, apart from the above products, the Group also generated sales revenue in the following groups:

- seed potatoes;
- pesticides;
- the sales of heat;
- the sales of materials.

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 01.01.2018 to 31.12.2018 as compared to the corresponding period in 2017.

Table 1: Structure of net sales revenue for 2018 and 2017

Range of products	2018	Structure in 2018	2017	Structure in 2017	Growth rate
potato-based products	218,667	91.13%	197,564	88.09%	110.68%
- including the sales of the Parent Company	157,277	65.55%	140,790	62.78%	111.71%
heat	-	0.00%	352	0.16%	0.00%
electricity	7,645	3.19%	7,440	3.32%	102.76%
animal feeds	961	0.40%	1,765	0.79%	54.45%
other sales, including:	12,668	5.28%	17,152	7.65%	73.86%
a) services	1,184	0.49%	1,831	0.82%	64.66%
b) trade goods and materials	11,484	4.79%	15,321	6.83%	74.96%
Total net sales revenue	239,941	100.00%	224,273	100.00%	106.99%

Table 2: Products sales volume for 2018 and 2017

Range of products	Unit	2018	2017	Growth rate in %
potato-based products	tonne	82,741	74,397	111.22
- including for the Parent Company	tonne	61,341	56,872	107.86

In 2018, the revenue from the sale of products increased by 7%, while volume growth was at the level of 11.22%.

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

Table 3: Sales revenue by markets

Net sales revenue	2018	Sales structure in 2018	2017	Sales structure in 2017
Poland, including	154,019	64.19%	144,518	64.44%
- products	145,319	60.56%	133,222	59.40%
- trade goods	7,516	3.13%	9,465	4.22%
- services	1,184	0.49%	1,831	0.82%
EU countries - intra-Community supplies, including:	23,249	9.69%	16,090	7.17%
- products	23,223	9.68%	15,368	6.85%
- trade goods	26	0.01%	722	0.32%
Other countries – export, including:	62,673	26.12%	63,665	28.39%
- products	58,731	24.48%	58,531	26.10%
- trade goods	3,942	1.64%	5,134	2.29%
Total	239,941	100.00%	224,273	100.00%

1) Sales in Poland by industries and geographical regions

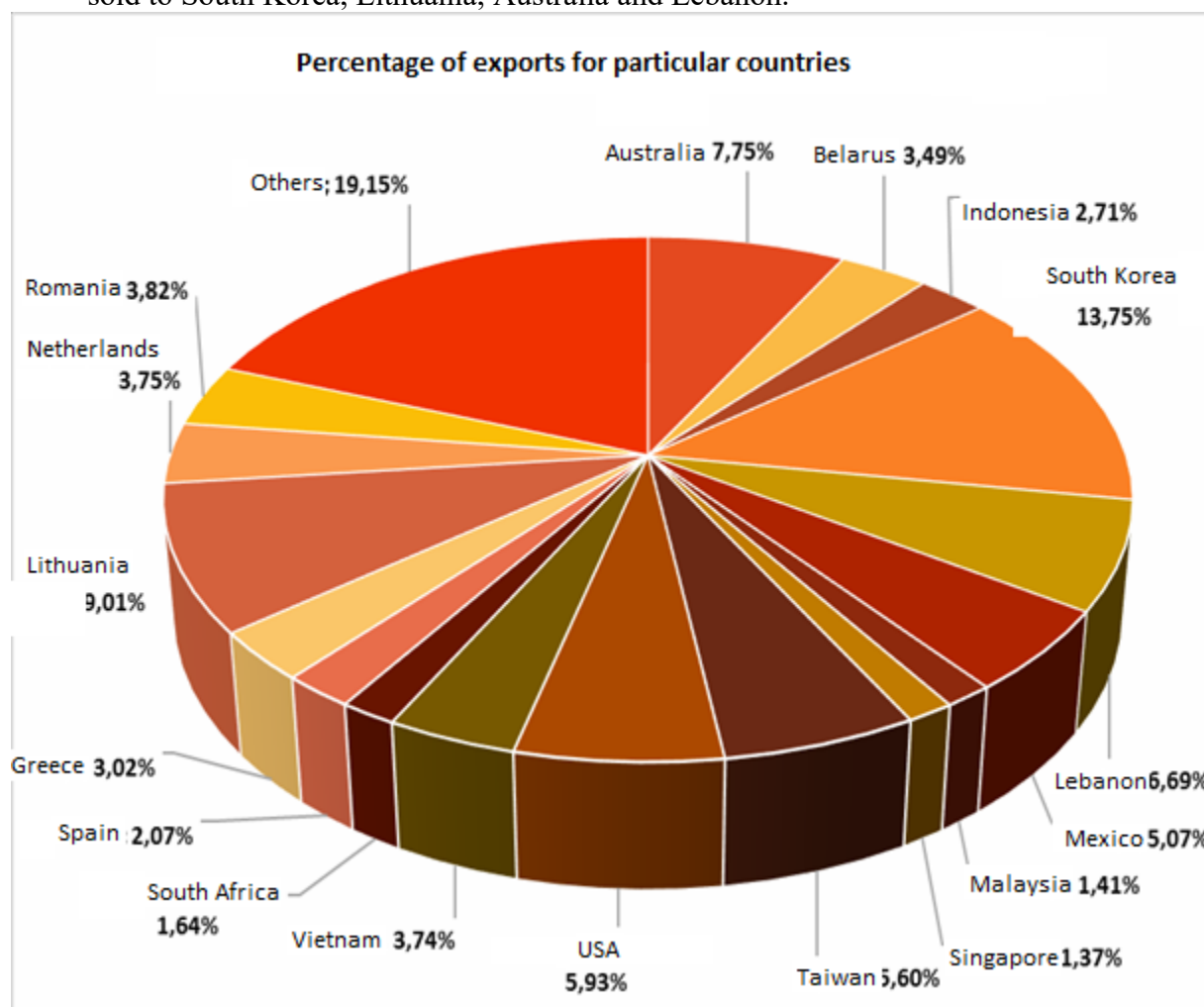
Products from the potato industry in 2018 were sold throughout Poland. The sales of the basic product on offer, i.e. potato starch, generated the largest percentage of the sales value on the Polish market (50.3%). Further products in terms of the percentage of the sales value are maltodextrin (11.72%), glucose (5.96%) and potato protein (5.39%). The majority of the main customers for the Parent Company's products on the Polish market are reputable Polish companies, which often have capital ties with large European and global companies.

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. None of the customers exceeded 10% of sales revenue of both the Group and the Parent Company.

2) Export and intra-Community sales

In 2018, the value of export and intra-Community sales amounted to PLN 85,922 thousand, i.e. it increased by 8% as compared to the previous year's figures. In 2018, the Issuer sold its products

(mainly potato starch) to over 50 countries worldwide. The highest quantities of products were sold to South Korea, Lithuania, Australia and Lebanon.



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%. The potato cultivation area in 2018 was 330,000 ha (according to the data of the Institute of Agricultural and Food Economics), where the starch potato cultivation area is ca. 5% 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 which are important from the Company's point of view.

In 2018, 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.

None of the suppliers had a 10-percent or bigger share in the Group's or the Parent Company's revenue.

6. Agreements material for the Group's business

6.1 Business agreements

On 04.01.2018, PEPEES entered into a conditional sales agreements with two natural persons, who are shareholders of the Company, under which the Company acquired a 32.6% stake in Gospodarstwo Rolne Ponary sp. z o.o. Thus, the Company has become the holder of 100% of shares in Ponary.

Apart from the aforementioned agreement, in the reporting period the Group did not enter into any business agreements of substantial value, and did not enter into any important cooperation/collaboration agreements.

Notwithstanding the foregoing, the Issuer indicates the following agreements concluded in 2018:

- a contract for the purchase of pesticides for potato plantations with the value of PLN 2,767 thousand;
- trading agreements;
- agreements concerning the modernisation of buildings, structures, plant and machinery and repairs.

6.2 Loan agreements

In 2018, the Group entered into and made annexes to the following loan agreements:

a) with BOŚ S.A.:

An investment loan agreement using funds from foreign credit lines amounting to PLN 8,456 thousand, entered into on 20.07.2018 by Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław S.A., taken out to upgrade the starch drying department and build the protein recovery system. The final loan repayment date has been scheduled for 31 December 2027.

b) with WBK S.A.:

An annex of 03.08.2018 to the multi-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 S.A., and WBK S.A. Pursuant to the Annex to the multi-line agreement, the credit limit granted to the Issuer and its subsidiaries was increased to PLN 52 million in such a way that the revolving loan granted to the Issuer, 'Lublin' and 'Bronisław' amounts now to PLN 16.5 million, PLN 2 million and PLN 7.8 million respectively.

On the other hand, the revolving loan amounts to PLN 12 million, PLN 4.25 million and PLN 4 million respectively, and the current loan to PLN 4 million, PLN 0.75 million and PLN 0.7 million respectively.

Furthermore, under the Annex to the multi-line agreement, the repayment date of all aforementioned loans concluded with Bank Zachodni WBK S.A. has been postponed until 31 August 2019.

c) with PKO BP S.A.:

An Annex of 03.08.2018 to a 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 S.A., and PKO BP S.A. Pursuant to the Annex, the credit limit granted to the Issuer and its subsidiaries has been increased to PLN 52 million in such a way that the revolving loan granted to the Issuer, 'Lublin' and 'Bronisław' amounts now to PLN 16.5 million, PLN 2 million and PLN 7.8 million respectively. On the other hand, the revolving loan amounts to PLN 12 million, PLN 4.25 million and PLN 4 million respectively, and the current loan to PLN 4 million, PLN 0.75 million and PLN 0.7 million respectively.

No loan agreements of the companies from PEPEES Group were terminated in 2018.

6.3 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)

6.4 Leases

- A lease concerning a passenger car with the value of PLN 50 thousand concluded on 17 March 2018 for the period of 36 months with Volkswagen Leasing.
- Two leases concerning Hyster H2.5FT forklift trucks with the total value of PLN 185 thousand concluded on 3 April 2018 for the period of 36 months with PKO Leasing S.A.
- Two leases concerning Yale MP16 forklift trucks with the total value of PLN 29 thousand concluded on 3 April 2018 for the period of 36 months with PKO Leasing S.A.
- A lease concerning Yale GLP20VX forklift truck with the value of PLN 82 thousand concluded on 3 April 2018 for the period of 36 months with PKO Leasing S.A.
- A lease concerning a passenger car with the value of PLN 47 thousand concluded on 8 May 2018 for the period of 36 months with BZ WBK Leasing.
- A lease concerning a passenger car with the value of PLN 48 thousand concluded on 15 June 2018 for the period of 48 months with Volkswagen Leasing.

6.5 Surety agreements

On 30.07.2018, PEPEES guaranteed, up to PLN 12,684 thousand, an investment loan from funds from foreign lines of credit granted to a subsidiary Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław S.A. in the amount of PLN 8,456 thousand. The final loan repayment date has been scheduled for 31 December 2027.

6.6 Agreements between shareholders

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

7. Organisational or capital ties between the Issuer and other entities; its major investments in Poland and abroad

As at 31.12.2018, major investments of PEPEES S.A. include shares in subsidiaries that have been consolidated and 3,000 shares of Warszawski Rolno-Spożywczy Rynek Hurtowy S.A. ('WRSRH') with its registered office in Bronisze with the estimated value as at 31.12.2018, according to the valuation carried out using the discounted future cash flow method by an independent actuary, of PLN 5,436 thousand. The shares of WRSRH represent 2.5% of the share capital of WRSRH and 1.6% of votes at the GMS.

The State Treasury is the main owner of WRSRH with more than 59% of its share capital. PEPEES does not exercise control over WRSRH.

Basic financial figures of subsidiaries

Subsidiary	Equity	Assets	Liabilities	Revenue from sales	Profit/Loss
2017					
ZPZ LUBLIN Sp. z o.o.	2,073	14,637	12,564	17,625	(452)
PPZ BRONISŁAW S.A.	9,073	38,467	29,394	45,054	5,120
CHP Energia Sp. z o.o.	(3,464)	24,758	28,222	10,232	(2,758)
OZENERGY Sp. z o.o.	3	8	5	0	(1)
Gospodarstwo Rolne PONARY Sp. z o.o.	11,010	21,178	10,168	-	(29)
2018					
ZPZ LUBLIN Sp. z o.o.	2,582	16,702	14,120	20,632	509
PPZ BRONISŁAW S.A.	14,092	57,172	43,080	46,189	5,019
CHP Energia Sp. z o.o.	(5,196)	22,772	27,968	9,249	(1,732)
Pepees Inwestycje Sp. z o.o. (formerly OZENERGY)	(41)	1,429	1,470	-	(44)
Gospodarstwo Rolne PONARY Sp. z o.o.	11,884	21,347	9,463	-	107

In 2018, PPZ BRONISŁAW generated profit at a very similar level as in the previous year.

In 2018, ZPZ LUBLIN generated sales revenue higher by over PLN 3 million than last year, which translated into profit.

Pepees Inwestycje did not carry out any activities in 2018.

CHP Energia improved the financial result from the previous year by more than PLN 1 million; however, it still closed the financial year with a loss in 2018 of PLN 1.7 million.

PONARY did not generate any sales revenue. Profit generated in 2018 results from financial income earned each month, i.e. fees for granting a loan surety to the parent company, i.e. PEPEES.

Methods of financing subsidiaries in 2018

ZPZ LUBLIN Sp. z o.o.	self-financing and loan-based financing (bank loans and loans granted by PEPEES)
PPZ BRONISŁAW S.A.	self-financing and loan-based financing (bank loans and loans granted by PEPEES)
CHP Energia Sp. z o.o.	self-financing and loan-based financing (bank loans and loans granted by PEPEES)
OZENERGY Sp. z o.o.	loan-based financing (a loan granted by PEPEES)
Gospodarstwo Rolne PONARY Sp. z o.o.	self-financing and loan-based financing (a loan from PEPEES)

In addition, the Group, through its Parent Company, holds interests in three other entities which ensure less than 5% of the total number of votes at the General Meeting of Shareholders of these entities, and they are not material in terms of their value and the Group's investment policy.

8. Related party transactions

All related party transactions were an arm's length transactions.

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 for PLN 2,134 thousand and potato grits for PLN 6 thousand. The total value of purchases from ZPZ LUBLIN amounted to PLN 2,140 thousand.

In 2018, PEPEES sold to ZPZ Lublin starch for PLN 187 thousand, maltodextrin for PLN 13 thousand and a service for PLN 283 thousand. The total value of sales made to ZPZ LUBLIN amounted to PLN 483 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 paid interest to the Issuer of PLN 127.5 thousand on the loan granted in previous years. The amount of the outstanding loan as at the balance sheet date was PLN 3,000 thousand.

Transactions between PEPEES S.A. in Łomża and PPZ Bronisław S.A. in Bronisław

In the reporting period, the Issuer purchased from the subsidiary starch and potato flakes for PLN 5,365 thousand, and services for PLN 30 thousand. The total value of purchases from PPZ BRONISŁAW S.A. amounted to PLN 5,395 thousand.

In 2018, PEPEES sold to PPZ BRONISŁAW potatoes with the value of PLN 3,078 thousand, potato protein with the value of PLN 11 thousand, and a service for PLN 11 thousand. The total value of sales to PPZ BRONISŁAW S.A. amounted to PLN 3,100 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, PPZ Bronisław paid interest to the Issuer of PLN 177.5 thousand on the loans granted in the previous and present year, and repaid throughout 2018 two loans in the total amount of PLN 4 million.

In addition, in the reporting period, the Issuer acquired bonds in PPZ Bronisław with the nominal value of PLN 8,000 thousand.

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

Transactions of PEPEES S.A. in Łomża with its subsidiary CHP Energia Sp. z o.o. consisted in the purchase of granulated sugar beet pulp from the subsidiary for PLN 60 thousand, biocompost for PLN 159 thousand, and services for PLN 336 thousand. The total value of purchases from CHP Energia amounted to PLN 555 thousand.

PEPEES sold to CHP Energia potato pulp for PLN 61 thousand, sugar beet pulp for PLN 130 thousand and a service for PLN 52 thousand. The total value of sales made to CHP Energia amounted to PLN 243 thousand.

As at the balance sheet date, there are outstanding loans with the total amount of PLN 4,905 thousand, the interest on granted sureties of PLN 596 thousand, and advance payment of PLN 401 thousand, and trade receivables of PLN 371 thousand.

Transactions between PEPEES S.A. in Łomża and Gospodarstwo Rolne PONARY Sp. z o.o. in Łomża

PEPEES sold to its subsidiary Gospodarstwo Rolne PONARY a service for PLN 10 thousand. On the other hand, Gospodarstwo Rolne PONARY provided the Issuer with a loan surety for which the fees accrued in 2018 amounted to PLN 166 thousand.

In addition, PONARY paid interest to the Issuer of PLN 15.2 thousand on the loan granted in 2018. The amount of the outstanding loan as at the balance sheet date was PLN 553 thousand.

Transactions between PEPEES S.A. in Łomża and Pepees Inwestycje Sp. z o.o. in Łomża

In 2018, the Issuer granted a loan to PEPEES Inwestycje amounting to PLN 1,450 thousand, the interest on which was paid in the amount of PLN 25 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 1,465 thousand.

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

On 04.01.2018, the Company entered into conditional sales agreements with two natural persons, who are shareholders of the Company, under which the Company acquired a 32.6% stake in Gospodarstwo Rolne Ponary sp. z o.o. Thus, the Issuer has become the holder of 100% of shares in Ponary.

9. Borrowings

As at 31.12.2018, the Group had borrowings in PLN, which are presented in the table below:

Table 4: Borrowings as at 31.12.2018

(amounts in PLN 000s)

Loan type /Agreement/	Lending bank	Borrower	Contractual loan amount	Debt as at 31.12.2018	Repayment date
1	2		3	4	5
Investment loan for the construction of a starch drying room, an unloading node and a water treatment unit	BGŻ BNP Paribas S.A.	PEPEES	9,822	4,387	25.02.2022
Investment loan to upgrade the dust removal system for boilers	BOŚ	PEPEES	1,200	558	31.12.2020
Investment loan to finance and refinance the acquisition of 100% of shares in Gospodarstwo Rolne Ponary	Powszechna Kasa Oszczędności Bank Polski S.A.	PEPEES	10,530	9,778	30.06.2025
Syndicated investment loan to implement the investment project 'The Construction of a Biogas Plant in Szepietowo District'	Spółdzielczy Bank Rozwoju in Szepietowo and Bank Spółdzielczy in Ostrów Mazowiecka	CHP Energia	12,830	11,116	31.12.2023
Working capital loan related to business activities	Spółdzielczy Bank Rozwoju in Szepietowo	CHP Energia	800	374	31.12.2019
Working capital loan to finance current liabilities related to business activities	Spółdzielczy Bank Rozwoju in Szepietowo	CHP Energia	3,000	2,273	31.05.2022
Investment loan to finance/refinance the purchase of	Bank Zachodni WBK S.A.	PPZ Bronisław	800	472	30.11.2021

Loan type /Agreement/	Lending bank	Borrower	Contractual loan amount	Debt as at 31.12.2018	Repayment date
1	2		3	4	5
real estate by PPZ Bronisław					
Overdraft facility	Bank Zachodni WBK S.A.	PEPEES	4,000	0	31.08.20 19
Revolving working capital loan in a credit account	Bank Zachodni WBK S.A.	PEPEES	10,000	10,000	31.08.20 19
Non-revolving working capital loan in a credit account	Bank Zachodni WBK S.A.	PEPEES	16,500	16,500	31.08.20 19
Overdraft facility	Bank Zachodni WBK S.A.	ZPZ Lublin	750	0	31.08.20 19
Revolving working capital loan in a credit account	Bank Zachodni WBK S.A.	ZPZ Lublin	4,250	2,824	31.08.20 19
Non-revolving working capital loan in a credit account	Bank Zachodni WBK S.A.	ZPZ Lublin	2,000	1,676	31.08.20 19
Overdraft facility	Bank Zachodni WBK S.A.	PPZ Bronisław	700	0	31.08.20 19
Revolving working capital loan in a credit account	Bank Zachodni WBK S.A.	PPZ Bronisław	4,000	3,581	31.08.20 19
Non-revolving working capital loan in a credit account	Bank Zachodni WBK S.A.	PPZ Bronisław	7,800	6,167	31.08.20 19
Overdraft facility	Powszechna Kasa Oszczędności Bank Polski S.A.	PEPEES	4,000	35	31.08.20 19
Revolving working capital loan in a credit account	Powszechna Kasa Oszczędności Bank Polski S.A.	PEPEES	10,000	10,000	31.08.20 19
Non-revolving working capital loan in a credit account	Powszechna Kasa Oszczędności Bank Polski S.A.	PEPEES	16,500	16,500	31.08.20 19
Overdraft facility	Powszechna Kasa Oszczędności Bank Polski S.A.	ZPZ Lublin	750	0	31.08.20 19
Revolving working capital loan in a credit account	Powszechna Kasa Oszczędności Bank Polski S.A.	ZPZ Lublin	4,250	1,953	31.08.20 19
Non-revolving working capital loan in a credit account	Powszechna Kasa Oszczędności Bank Polski S.A.	ZPZ Lublin	2,000	1,790	31.08.20 19

Overdraft facility	Powszechna Kasa Oszczędności Bank Polski S.A.	PPZ Bronisław	700	0	31.08.2019
Revolving working capital loan in a credit account	Powszechna Kasa Oszczędności Bank Polski S.A.	PPZ Bronisław	4,000	3,989	31.08.2019
Non-revolving working capital loan in a credit account	Powszechna Kasa Oszczędności Bank Polski S.A.	PPZ Bronisław	7,800	7,795	31.08.2019

Loan type /Agreement/	Lending bank	Borrower	Contractual loan amount	Debt as at 31.12.2018	Repayment date
1	2		3	4	5
Working capital loan related to business activities	Spółdzielczy Bank Rozwoju in Szepietowo	CHP Energia	2,500	1,700	13.09.2019
Investment loan to finance the upgrade of the starch drying department and the construction of the protein recovery system	BOS	PPZ Bronisław	8,456	7,574	31.12.2027

Interest rates for short-term loans are based on WIBOR rate for one-month deposits plus the banks' margins, and for long-term loans on WIBOR rate for three-month deposits plus the banks' margins. All loans are denominated in PLN. In 2018, none of the Group's loans were terminated and the Group companies did not terminate any loan agreements during that period.

10. Cash loans, guarantees and sureties granted

Sureties granted by the parent company PEPEES S.A. as at 31.12.2018:

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 25.05.2024.

The agreement of 14 September 2017 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 working capital loan taken out by CHP Energia Sp. z o.o. The value of the working capital loan taken by CHP Energia Sp. z o.o. amounts to PLN 3,000 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 2,800 thousand (the amount of debt as at the endorsement day).

The agreement of 14 September 2017 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 working capital loan taken out by CHP Energia Sp. z o.o. The value of the working capital loan taken by CHP Energia Sp. z o.o. amounts to PLN 800 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 710 thousand (the amount of debt as at the endorsement day).

The agreement of 14 September 2017 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 working capital loan taken out by CHP Energia Sp. z o.o. The value of the working capital loan taken by CHP Energia Sp. z o.o. amounts to PLN 2,500 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 2,500 thousand.

The agreement of 30 July 2018 concerning the conditions of granting a security for a loan repayment concluded between PEPEES S.A. in Łomża and PPZ Bronisław S.A. Pursuant to the agreement, PEPEES S.A. provides security for the Investment Loan from Foreign Credit Lines taken out by PPZ Bronisław S.A. The value of the investment loan taken out by PPZ Bronisław S.A. amounts to PLN 8,456 thousand. The security granted by PEPEES S.A. is in the form of the statement on the submission to execution certified by a notary public up to PLN 12,684 thousand.

Sureties granted to the parent company PEPEES S.A. as at 31.12.2018:

Short-term loans are secured with e.g. mortgages on the assets of the subsidiaries: ZPZ LUBLIN Sp. z o.o. and PPZ BRONISŁAW S.A.

The investment loan for the purchase of shares from Gospodarstwo Rolne PONARY is secured by a mortgage of PLN 15.8 million established on land properties of PONARY.

Loans granted by the parent company PEPEES S.A. as at 31.12.2018:

A cash loan agreement of 23.11.2011 concluded between PEPEES S.A. and ZPZ Lublin Sp. z o.o. Under the agreement, PEPEES S.A. granted a loan of PLN 1.5 million to finance the purchase of potatoes and the purchase of semi-finished products for the production of syrup. The interest rate for the loan is 4.25% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 1 million.

A cash loan agreement of 31.08.2012 concluded between PEPEES S.A. and ZPZ Lublin Sp. z o.o. Under the agreement, PEPEES S.A. granted a loan of PLN 2 million to finance the company's operations. The interest rate for the loan is 4.25% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 2 million.

A cash loan agreement of 12.01.2017 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 1,537 thousand. The interest rate for the loan is 4.5% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 769 thousand.

A cash loan agreement of 28.02.2017 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 450 thousand to finance current operations of CHP Energia. The interest rate for the loan is 4.5% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 300 thousand.

A cash loan agreement of 14.12.2017 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 550 thousand for the repayment by CHP Energia of the entire debt to Centrum Elektroniki Stosowanej CES Sp. z o.o. The interest rate for the loan is 3.5% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 550 thousand.

A refinancing loan agreement of 15.12.2017 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. refinanced two loans granted previously (agreements of 21.11.2016 and 01.06.2017) as part of one refinancing loan agreement. As a result of the refinancing, PEPEES S.A. granted a special-purpose loan of PLN 1 million to finance current operations of CHP Energia.

The interest rate for the loan is 3.5% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 1 million.

A cash loan agreement of 10.01.2018 concluded between PEPEES S.A. and Gospodarstwo Rolne Ponary Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 550 thousand to finance current operations of GR PONARY. The interest rate for the loan is 3.5% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 550 thousand.

A cash loan agreement of 24.04.2018 concluded between PEPEES S.A. and Pepees Inwestycje Sp. Z o.o. (formerly Ozenergy). Under the agreement, PEPEES S.A. granted a loan of PLN 3 million. The interest rate for the loan is 4.0% p.a. The repayment date is 24.04.2019. As at the balance sheet date, the outstanding principal was PLN 1,450 thousand (only the first tranche of the loan was paid out).

A cash loan agreement of 30.04.2018 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 500 thousand to finance current operations of CHP Energia. The interest rate for the loan is 4.0% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 500 thousand.

A cash loan agreement of 26.06.2018 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 700 thousand with the option to convert the loan amount to shares of CHP Energia. The interest rate for the loan is 5.0% p.a. The repayment date is 31.12.2019. As at the balance sheet date, the outstanding principal was PLN 700 thousand.

A cash loan agreement of 24.09.2018 concluded between PEPEES S.A. and CHP Energia Sp. z o.o. Under the agreement, PEPEES S.A. granted a special-purpose loan of PLN 900 thousand to finance current operations of CHP Energia. The interest rate for the loan is 5.0% p.a. The repayment date is 30.06.2019. As at the balance sheet date, the outstanding principal was PLN 900 thousand.

Guarantees received as at 31.12.2018:

As at 31.12.2018, the parent company had 12 guarantees (performance bonds and guarantees of returning a security deposit or advance payment made) for the total amount of PLN 600 thousand and EUR 140 thousand.

Guarantees granted as at 31.12.2018:

Bank guarantee from PKO S.A. of 04.10.2018 for the amount of PLN 287 thousand issued to Danwood S.A. due to the contract on the construction of a house dated 06.04.2018. The guarantee is effective until 02.04.2020.

11. Off-balance sheet items in PEPEES Group

	20 18	20 17
Off-balance sheet assets		
Value of land used under the right of perpetual usufruct	23,336	13,603
Receivables in litigation	-	-

Off-balance sheet liabilities	20 18	20 17
Mortgages on the assets of companies	180,975	180,975
Pledge on assets	114,512	114,512
Loan surety	30,918	18,234
Assignment of receivables under an insurance policy	254,630	254,630
Possible damages related to non-competition agreements	1,224	818
Disputed obligations	-	-

12. The use of proceeds from shares issued or the acquisition of treasury shares

In the reporting period, a subsidiary PPZ BRONISŁAW S.A. issued 30 series A bonds with the nominal value of PLN 100 thousand each and 50 series B bonds with the nominal value of PLN 100 thousand each; all of them were subscribed for by the parent company, i.e. PEPEES. These bonds are convertible into shares. The interest rate is 4% p.a. The maturity date for the bonds is 31.12.2027.

PPZ BRONISŁAW S.A. used the proceeds from the issue of the bonds to upgrade the production line.

In the reporting period, the Issuer did not issue any securities and did not purchase or sell treasury shares.

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

The Company and the Group did not publish financial forecasts for 2018.

14. Financial resources management assessment

In 2018, both 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.

15. 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 2018 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. KUKE S.A. 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.

16. Completed and planned investment projects

1) Investment projects completed in 2018

In 2018, the Group implemented several investment projects of various nature and scale, including, but not limited to:

- stage II of the upgrade of the potato washing and cleaning system (an assembly of a sand catcher, a flume water band filter, construction of a new DN500 flume water pipeline),
- an upgrade of A and B starch drying departments (new product separation and feed nodes – cyclon batteries with screw conveyors systems, inlet collectors, outlet collectors, closing conveyors, chute pipes, chute hoppers; Cyclons equipped with a compressed air bus with solenoid valves and air preparation station; the upgrade of the drying pipeline and pneumatic transport);
- the upgrade of the starch drying department control and visualization system (migration of the automation system controlling the starch drying department system along with the supply of converters, two operators' stations and the use of the industrial network);
- delivery and assembly of a new storage tank for HCl 33% with a hydraulic closure;
- assembly of Foodec610T decanter for potato protein;

- the upgrade of Wiegand evaporator by installing a new droplet separator and connecting it to the existing heating column;
- preparing and commissioning a new water level control system in a tower tank at the Filter Station coupled with the diagonal pumps control system at the Intake of Surface Water from the Narew River;
- the upgrade of TPZ700 No. 2 potato rasp;
- assembly of a lime dust removal system at a whitewash preparation line;
- assembly of automatic valves shutting-off feed material on Tx and Sx separators;
- assembling a potato pulp transportation line consisting of 8 screw conveyors;
- purchasing potato unloading machines (receiving hopper, heap making machine);
- assembly of the all-year tent hall No. 6;
- purchase of agricultural machinery for potato cultivation and construction of employee facilities on a farm;
- purchase of laboratory equipment (climatic chamber, dryer);
- purchase of new production pumps;
- purchases of equipment and storage area for CHP Energia.

In 2018, the Parent Company completed additionally a wide range of repairing and construction works in production, storage and auxiliary facilities in order to improve their technical condition and to adapt them to H&S and fire requirements and to the Company's Integrated Management Systems, including works identified in post-audit and post-control recommendations. The works comprised mainly repairs of facades, walls, floors and ceilings, the replacement of the window and door woodwork as well as installation works, including electrical and sanitary works.

The total capital expenditure made in 2018 on the aforementioned projects amounted to PLN 30.5 million.

2) Investment projects planned for 2019

The investment project plan for 2019 includes:

- assembly and commissioning of a new Integra FD2 automatic starch packing machine;
- assembly and commissioning of a new BPU 42 Simplex line for packing starch in 0.5 and 1.0 kg bags;
- execution of stage III of the upgrade of the potato washing and cleaning system (including the assembly of a new potato washer, stones catcher, leaves and haulm catcher, floating parts catcher);
- expansion of the gas boiler room;
- upgrade of potato rasp No. 5;
- upgrade of four laundries at the starch production department;
- purchase of forklifts;
- assembly of heating and ventilation systems in the Finished Products Warehouse;

- expansion of the plant compressor room with the third container compressor;
- upgrade of the visualisation and control system of the wet unit of the starch production department;
- improving the stability of the slopes of sand settling tanks;
- upgrade of the utilities transmission system;
- purchase of laboratory equipment;
- purchase of agricultural machinery (a potato planter).

Planned upgrade projects will be financed with own funds, while forklifts and agricultural machinery will be acquired under leases. Capital investments are not planned.

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

The Issuer's enterprise operates the Integrated Management System, including quality management, environmental management and H&S management, and the quality management system in laboratories.

18. Employment in the Group

Table 5: Employment in the Group

Specification	Average number of employees in 2018	31.12.2018		Average number of employees in the previous financial year 2017
		Women	Men	
Administrative employees	150	82	70	142
Workers	347	58	272	358
Employees on unpaid leaves	0	0	0	4
Total	497	140	342	504

19. Major R&D accomplishments

In 2018, there were no major research and development works carried out.

20. Events with significant impact on profit/loss from the parent company's and the Group's operations in and after a particular financial year

The parent company recognised write-downs of its assets in the subsidiary CHP Energia in the total amount of PLN 2,817 thousand due to the negative capitals of this company, which resulted in lower separate profit of PEPEES.

On 15 January 2019, the Extraordinary General Meeting of Shareholders of PEPEES was held, which amended the Company's Articles of Association and authorised the Supervisory Board to adopt the consolidated text of the Company's Articles of Association.

21. Structure of major equity investments

Equity investments	<i>Amounts in PLN 000s</i>	
	20 18	20 17
Short-term bank deposits in PLN	31,891	23,813
Other financial assets	5,436	3,546

22. Corrections of errors from previous periods and changes in accounting policies

In 2018, the Group did not change any accounting policies. There were also no corrections of errors from previous periods.

23. Changes of the basic principles of the Group management process

In 2018, there were no material changes of the principles of the Issuer's and the Group's management process.

24. Any agreements between the Issuer and the members of the Board of Directors providing for a compensation if they resign or are made redundant without a valid reason or if their employment ceases because of the Issuer's merger through acquisition

There are managerial contracts concluded between the Issuer and the members of the Board of Director, which provide for compensation due to non-competition agreements for the period of 12 months from the date of their contract termination in the amount of 100% of the average monthly salary with bonuses for the past 12 months.

25. Remunerations, bonuses and other benefits paid and payable to members of the management and supervisory personnel in 2018

Board of Directors:

Mr Wojciech Faszczewski	PLN 790.3 thousand
Mr Tomasz Rogala	PLN 587.3 thousand
Total remunerations of the Members of the Board of Directors	PLN 1,377.6 thousand

Supervisory Board:

Mr Maciej Kaliński	PLN 115.8 thousand
Mr Piotr Taracha	PLN 79.4 thousand
Mr Krzysztof Stankowski	PLN 73.5 thousand
Mr Robert Malinowski	PLN 71.7 thousand
Ms Agata Czerniakowska	PLN 71.7 thousand
Total remuneration of the Supervisory Board	PLN 412.1 thousand

Remunerations of the members of the Board of Directors and of the Supervisory Board paid for their work in the authorities of subsidiaries:

Mr Wojciech Faszczewski – President of the Board of Directors of PEPEES – PLN 58.4 thousand due to the membership in the Supervisory Board of Zakłady Przemysłu Ziemniaczanego Lublin Sp. z o.o.; PLN 172 thousand for performing the role of the President of the Board of Directors of PPZ BRONISŁAW S.A.; PLN 8 thousand due to the membership in the Supervisory Board of CHP Energia.

Mr Tomasz Rogala – Member of the Board of Directors of PEPEES – PLN 6 thousand due to the membership in the Supervisory Board of CHP Energia.

Mr Piotr Taracha – PLN 52.6 thousand due to the membership in the Supervisory Board of Zakłady Przemysłu Ziemniaczanego Lublin Sp. z o.o.; and PLN 36 thousand due to the membership in the Supervisory Board of PPZ BRONISŁAW S.A.

Ms Agata Czerniakowska – PLN 29.2 thousand due to the membership in the Supervisory Board of ZPZ LUBLIN Sp. z o.o. and PLN 33 thousand due to the membership in the Supervisory Board of PPZ BRONISŁAW S.A.

Mr Robert Malinowski – PLN 15.5 thousand due to the membership in the Supervisory Board of ZPZ LUBLIN Sp. z o.o. and PLN 7 thousand due to the membership in the Supervisory Board of PPZ BRONISŁAW S.A.

There are no obligations arising from pensions and similar benefits payable to former members of the Board of Directors and the Supervisory Board.

26. Shares of PEPEES S.A. and of the Group's companies held by members of the management and supervisory personnel

As at 31.12.2018, the following members of the management and supervisory personnel of PEPEES S.A. in Łomża held the Company's shares:

Mr Wojciech Faszczewski – President of the Board of Directors – 701,000 shares with the nominal value of PLN 0.06 each and with the total nominal value of PLN 42,060.

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

27. The Company's quotations in 2018

The Company's shares have been listed on the Warsaw Stock Exchange since 22 May 1997. The share price at the beginning of 2018 amounted to PLN 1.44. The highest share price in 2018 was PLN 1.62 and the lowest share price was PLN 1.16. The 2018 year-end share price was PLN 1.25.

Share price of PEPEES in 2018



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

A subsidiary PPZ BRONISŁAW S.A. issued 30 series A bonds with the nominal value of PLN 100 thousand each and 50 series B bonds with the nominal value of PLN 100 thousand each; all of them were subscribed for by the parent company, i.e. PEPEES. The maturity date for the bonds is 31.12.2027. These bonds are convertible into shares. Each bond entitles PEPEES to subscribe for 5,000 series B shares of PPZ Bronisław with the nominal value of PLN 1 each, issued in connection with the increase in the share capital of PPZ Bronisław, at the issue price of PLN 20 for each share.

PEPEES may exercise this right within 7 days before the bond redemption date. PPZ Bronisław may at any time call PEPEES to exercise this right; in such a case, PEPEES will be obliged to exercise it within 7 days of the call.

29. The system of control of any employee share schemes

The Group does not have any system of control of employee share schemes or of any equity-based incentive schemes.

30. The audit firm authorised to audit and review the Issuer's financial statements

PEPEES and its subsidiaries concluded the agreement for the period of reviewing and auditing the financial statements for 2018 with WBS Audyt Sp. z o.o. with its registered office in Warsaw, Poland. The agreement was entered into on 4 July 2018. The audit company was appointed by the Supervisory Board of the Company.

The Issuer did not use the services of the appointed audit firm.

The financial statements of the Issuer and its subsidiaries for 2017 were audited by Mazars Audyt Sp. z o.o. with its registered office in Warsaw, Poland, under the agreement of 10 August 2017.

Remuneration in PLN 000s

Specification	2018	2017
Mandatory audit of the annual financial statements	41	44
<i>including: PEPEES</i>	21	31
Review of the semi-annual financial statements	19	16
<i>including: PEPEES</i>	14	9
Tax advisory services	-	-
Other services	-	-
Total remuneration	60	60

The remuneration of WBS Audyt Sp. z o.o. (audit firm) for individual works is as follows:

Review of separate financial statements of PEPEES	Review of consolidated financial statements	Review of financial statements of ZPZ Lublin	Review of financial statements of PPZ Bronisław	Review of consolidation packages of the subsidiaries not subject to audit (CHP Energia, Pepees Inwestycje, GR Ponary)	Total remuneration for the review of financial statements as at 30.06.2018
11,500.00	2,300.00	5,200.00			19,000.00

Audit of separate financial statements of PEPEES	Audit of consolidated financial statements	Audit of separate financial statements of ZPZ Lublin	Audit of separate financial statements of PPZ Bronisław	Review of consolidation packages the subsidiaries not subject to audit (CHP Energia, Pepees Inwestycje, GR Ponary)	Total remuneration for the audit of financial statements as at 31.12.2018
18,400.00	2,300.00	8,600.00	8,600.00	2,800.00	40,700.00

31. Proceedings pending before a court

There are no significant proceedings pending before a court, a competent arbitration authority or a public administration body regarding liabilities and receivables of the Company or its subsidiary.

III. Assets and financial standing

1 The Group's assets

Assets as at 31 December 2018 as compared to assets as at 31 December 2017 are shown in the table below.

Table 6: Assets as at 31.12.2018 and 31.12.2017

Asset	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	31.12.2018	31.12.2017		31.12.2018	31.12.2017
I. NON-CURRENT ASSETS	173,688	155,419	18,269	52.0	51.1
1. Property, plant and equipment	164,885	147,034	17,851	49.4	48.4
2. Intangible assets	534	211	323	0.2	0.1
3. Goodwill	3,140	3,140	-	0.9	1.0
4. Investments in other entities	113	113	-	0.0	0.0
5. Cash loans	-	-	-	0.0	0.0
6. Advances	47	72	(25)	0.0	0.0
7. Deferred tax assets	4,969	4,849	120	1.5	1.6
II. CURRENT ASSETS	160,237	148,468	11,769	48.0	48.9
1. Inventories	78,065	84,134	(6,069)	23.4	27.7
2. Biological assets	330	-	330	0.1	0.0
3. Trade receivables	27,651	23,311	4,340	8.3	7.7
4. Current income tax receivables	-	-	-	0.0	0.0
5. Other receivables	6,044	5,250	794	1.8	1.7
6. Advances	1,964	827	1,137	0.6	0.3
7. Cash loans	941	762	179	0.3	0.3
8. Investments held for trading	5,436	3,546	1,890	1.6	1.2
9. Cash and cash equivalents	39,806	30,638	9,168	11.9	10.1
Total assets	333,925	303,887	30,038	100.00	100.00

The total value of the Group's assets as at 31.12.2018 increased by 9.88% as compared to the previous year. In non-current assets, property, plant and equipment increased by 12.14%. And, in current assets, the highest increase was recorded for cash (by over PLN 9 million) and receivables.

2 Sources of financing for the Group

Sources of financing assets as at 31 December 2018 as compared to 31 December 2017 are shown in the table below.

Table 7: Sources of financing assets as at 31.12.2018 and 31.12.2017

Sources of financing	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	31.12.2018	31.12.2017		31.12.2018	31.12.2017
I. Equity	166,476	145,547	20,929	49.9	47.9
<i>Equity attributable to equity holders of the parent</i>	<i>165,399</i>	<i>141,282</i>	24,117	49.5	46.5
1. Share capital	5,700	5,700	0	1.7	1.9
2. Reserve capital and other reserves	141,857	124,418	17,439	42.5	40.9
3. Revaluation reserve	(26)	(172)	146	0.0	(0.1)
4. Retained earnings/loss	(5,223)	(2,028)	(3,195)	-1.6	(0.7)
5. Profit/loss for the year	23,091	13,364	9,727	6.9	4.4
<i>Non-controlling interests</i>	<i>1,077</i>	<i>4,265</i>	(3,188)	0.3	1.4
II. Non-current liabilities	50,293	48,684	1,609	15.1	16.0
1. Loans and borrowings	30,398	25,330	5,068	9.1	8.3
2. Liabilities related to leased assets	4,775	7,446	(2,671)	1.4	2.5
3. Deferred tax liability	6,470	6,258	212	1.9	2.1
4. Retirement and similar benefits obligations	2,381	2,249	132	0.7	0.7
5. Grants	6,269	6,901	(632)	1.9	2.3
6. Other liabilities	-	500	(500)	0.0	0.2
III. Current liabilities	117,156	109,656	7,500	35.1	36.1
1. Trade payables	13,063	15,026	(1,963)	3.9	4.9
2. Current income tax liability	1,712	2,887	(1,175)	0.5	1.0
3. Other short-term liabilities	4,749	5,317	(568)	1.4	1.7
4. Loans and borrowings	90,644	81,534	9,110	27.1	26.8
5. Finance lease payables	2,876	2,587	289	0.9	0.9
6. Retirement benefits	296	327	(31)	0.1	0.1
7. Provisions for other liabilities and other charges	3,816	1,978	1,838	1.1	0.7
Total equity and liabilities	333,925	303,887	30,038	100.0	100.0

The financing structure is very similar to the previous year's structure—equity, non-current and current liabilities structure ratios were not significantly different than in 2017.

3 The Group's financial results

The financial results from the Group's business activities for 2018 and 2017 are shown in the table below.

Table 8: The financial result for 2018 and 2017

N o.	Specification	2018	2017	Growth rate in %
1	Sales revenue	239,941	224,273	107.0
	- revenue from the sales of products	224,087	203,379	110.2
	- revenue from the sales of services	1,184	1,831	64.7
	- revenue from the sales of trade goods and materials	14,670	19,063	77.0
2	Costs of sold products, trade goods and materials	(167,530)	(160,257)	104.5
	- costs of products sold	(152,775)	(141,022)	108.3
	- costs of services sold	(241)	(654)	36.9
	- costs of trade goods and materials sold	(12,393)	(17,152)	72.3
	- profit/loss from agricultural production	(2,121)	(1,429)	148.4
3	Gross profit from sales	72,411	64,016	113.1
	- selling and marketing expenses	(10,746)	(11,475)	93.6
	- administrative expenses	(31,351)	(26,862)	116.7
	- other operating income	1,376	1,065	129.2
	- other operating expenses	(1,768)	(4,891)	36.1
4	Profit on operating activities	29,922	21,853	136.9
	- finance costs	(3,074)	(3,571)	86.1
	- finance income	3,571	369	967.8
5	Profit before tax	30,419	18,651	163.1
	- income tax expense	(7,005)	(5,460)	128.3
6	Net profit, including:	23,414	13,191	177.5
7	Profit attributable to equity holders of the parent	23,091	13,364	172.8
8	Profit attributable to non-controlling interests	323	(173)	(187)
9	Other comprehensive income	(146)	106	(138)
10	Revaluation of employee benefit liabilities	(146)	106	(138)
11	Total comprehensive income, including:	23,268	13,297	175.0
12	Net comprehensive income attributable to equity holders of the parent	22,945	13,470	170.3
13	Comprehensive income attributable to non-controlling interests	323	(173)	(187)
14	Net earnings (loss) per share	0.18	0.13	140.0

In 2018, PEPEES Group generated sales of PLN 239.9 million, which denoted an increase by 7% as compared to the corresponding period in the previous year. The increase in sales revenue resulted particularly from higher sales to European Union countries (an increase by 44.5%). Due to the lower growth rate for the cost of products sold (as compared to the growth rate for the revenue from sales of products), the Group generated in 2018 gross profit from sales of

PLN 72.4 million, which denoted an increase by 13.1% as compared to the corresponding period in the previous year.

Selling and marketing expenses decreased by 6.4%, while administrative expenses increased by 16.7% as compared to the previous year.

The balance on other activities in 2018 closed at (-) PLN 0.4 million as compared to the result of (-)PLN 3.8 million in 2017.

On the other hand, the result on financing activities, understood as the balance of finance income less finance costs, was higher in 2018 by PLN 3.7 million than the corresponding item in 2017. It is the result of the revaluation to the market value of the shares of WRSRH. As a consequence, gross profit in 2018 amounted to PLN 30.4 million against PLN 18.6 million of operating profit generated in the comparative period, and net profit attributable to shareholders of PEPEES in 2018 amounted to PLN 23.1 million against PLN 13.4 million of net profit in 2017, i.e. it increased by 59.4%.

4 Cash flows

In 2018, the balance of cash flows from operating activities was positive and amounted to PLN 30,474 thousand owing to the generated operating profit. There were negative cash flows from investing activities amounting to PLN 32,719 thousand, mainly due to the expenditure on the acquisition of property, plant and equipment. The balance of cash flows from financing activities was positive amounting to PLN 11,361 thousand due to the increase in loan debt. All in all, the balance of cash flows is positive and amounts to PLN 9,116 thousand.

5 Economic ratios

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

Table 9: Economic ratios

Ratio	Commercial substance	2018	2017
Return on Assets	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{total assets}}$	6.92%	4.40%
Return on Equity	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{equity}}$	13.96%	9.46%
Net Profit Margin	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	9.62%	5.96%
Return on Sales	$\frac{\text{gross profit/loss from sales} \times 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	30.18%	28.54%
Cash Ratio	$\frac{\text{total current assets}}{\text{current liabilities}}$	1.37	1.35
Quick Ratio	$\frac{\text{total current assets} - \text{inventories}}{\text{current liabilities}}$	0.70	0.59

Ratio	Commercial substance	2018	2017
Receivables Turnover** in days	$\frac{\text{average trade receivables} \times 365}{\text{net revenue from the sales of products, services, trade goods and materials}}$	38.76	39.93
Accounts Payable Turnover** in days**	$\frac{\text{average trade payables} \times 365}{\text{costs of trade goods and services sold} + \text{value of trade goods and materials}}$	30.60	30.73
Inventory Turnover in days**	$\frac{\text{average inventories} \times 365}{\text{costs of products and services sold} + \text{value of trade goods and materials}}$	176.69	183.82
Equity to Fixed Assets	$\frac{\text{equity attributable to the shareholders of the Company} \times 100}{\text{total non-current assets}}$	0.95	0.91
Gearing Ratio	$\frac{(\text{equity attributable to equity holders of the Company} + \text{non-current provisions} + \text{non-current liabilities}) \times 100}{\text{total equity and liabilities}}$	0.59	0.55

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

As demonstrated in the table above, profitability ratios increased in 2018, as the Group generated higher net profit as compared to the previous year. Liquidity ratios remained at the level recorded in the previous year. Trade receivables turnover ratio decreased and the inventory turnover ratio remained at the level similar to 2017 level. The latter ratio is always high in the Group due to the seasonality of its production.

6 The Parent Company's assets

<i>ASSETS</i>	<i>31.12.2018</i>	<i>31.12.2017</i>
Non-current (long-term) assets	134,271	118,847
Property, plant and equipment	95,368	91,659
Intangible assets	534	211
Investments in subsidiaries	26,632	15,122
Investments in other entities	113	113
Long-term advances	8,212	8,979
Deferred tax assets	3,412	2,763
Current (short-term) assets	123,505	118,054
Inventories	52,180	56,386
Biological assets	330	-
Trade receivables	23,791	19,807
Other receivables	3,866	4,076
Advances	1,309	1,279
Loans granted	8,412	8,381
Other financial assets	5,436	3,546
Cash and cash equivalents	28,181	24,579
Total assets	257,776	236,901

7 Sources of financing for the Parent Company

<i>EQUITY AND LIABILITIES</i>	<i>As at 31.12.20 18</i>	<i>As at 31.12.20 17</i>
Equity	156,700	139,112
Share capital	5,700	5,700
Reserve capital and other reserves	133,584	121,265
Revaluation reserve	(26)	(172)
Retained earnings/loss from previous years and the present year	17,442	12,319
Non-current liabilities	26,611	28,474
Loans and borrowings	11,554	11,248
Liabilities related to leased assets	4,601	7,029
Deferred tax liabilities	6,350	6,133
Retirement and similar benefits obligations	1,888	1,752
Grants	2,218	2,312
Current liabilities	74,465	69,315
Trade payables	8,623	7,552
Current income tax liabilities	1,362	2,757
Other current liabilities	2,263	2,626
Loans and borrowings	56,204	52,573
Liabilities related to leased assets	2,670	2,225
Retirement and similar benefits obligations	202	274
Provisions for other liabilities and other charges	3,141	1,308
Total equity and liabilities	257,776	236,901

8 The Parent Company's financial performance

<i>Revenue and expenses</i>	<i>01.01.20 18- 31.12.201 8</i>	<i>01.01.20 17- 31.12.2017</i>
<i>Profit and loss</i>		
Sales revenues, including:	175,798	162,454
Revenue from the sales of products	158,257	141,142
Revenue from the sales of services	792	792
Revenue from the sales of trade goods and materials	16,749	20,520
Costs of sold products, trade goods and materials, including:	(119,340)	(113,368)
Cost of products sold	(101,319)	(92,220)
Cost of services sold	(446)	(361)
Costs of trade goods and materials sold	(15,454)	(19,358)
Profit/loss from agricultural production	(2,121)	(1,429)
Gross profit from sales (I-II)	56,458	49,086
Selling and marketing expenses	(9,115)	(10,017)
Administrative expenses	(23,866)	(19,366)

Revenue and expenses	01.01.20	01.01.20
Profit and loss	18-	17-
	31.12.201	31.12.2017
	8	
Other operating income	649	493
Other operating expenses	(1,477)	(628)
Operating profit	22,649	19,568
Finance costs	(4,498)	(4,833)
Finance income	4,306	937
Profit before tax	22,457	15,672
Income tax expense	(5,015)	(3,353)
Net profit	17,442	12,319
Other net comprehensive income	(146)	106
Effects of the valuation of financial assets	-	-
Revaluation of employee benefit liabilities	(146)	106
Total net comprehensive income	17,296	12,425

9 Non-typical events affecting the Parent Company's financial performance

In 2018, the Parent Company recognised write-downs of loans granted to CHP Energia and receivables due to fees for sureties granted to CHP Energia.

The amount of recognised write-downs as compared to the previous year:

Write-downs related to CHP Energia	2018	2017
goodwill	-	4,346
shares	-	2,875
receivables – interest on sureties	365	231
trade receivables	-	196
loans	2,452	
advance	-	162
Total	2,817	7,810

IV. The development of the Issuer and of the Group

1. Description of underlying risks and threats and of external and internal drivers of the development of the Parent Company and PEPEES Group

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. Adverse weather conditions contribute to the reduction of potatoes harvest and of the starch content.

- **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 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. Substantial fluctuations of currency exchange rates adversely affect the profitability of foreign transactions.

- **Interest rate risk**

Due to the financing of operating and investing activities with bank loans, the Group is exposed to the interest rate risk. Due to quick repayment of working capital loans within 8-9 months, the Group significantly reduces the impact of the interest rate risk on its financial result.

- **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. Financial products offered on the market are expensive and significantly prolong transactions.

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

The Group manufactures foodstuffs. 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 successful development of the Issuer and the Group

The development of the Issuer and its Group 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 successful development are as follows:

- The development of the Polish potato industry. For many years now, the Polish potato industry has been undergoing thorough structural remodelling. These changes result in greater professionalism of the potato production, which, in the future, may contribute to greater competitiveness of the Polish potato industry. The total number of farms producing potatoes is on the decrease, while, at the same time, the production is more concentrated and specialised.
- 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;
- area payments for starch potatoes.

1.3 Internal drivers of the successful development of the Issuer and the Group

The most vital internal drivers important for their further development are as follows:

- Regular investments in and gradual upgrade of production departments in order to boost the efficiency and innovation of products, and to reduce operating costs.
- Active response to market needs and requirements.
- Implemented Corporate Food Quality and Safety Management System with appropriate certificates.
- Implemented GMP (good manufacturing practice) system for manufacturers of active substances.
- The Company's compliance with Smeta; the presence on SeDeX platform.
- Very good cooperation with growers throughout the year.
- the possibility of producing hydrolysates to meet specific customers' needs;
- low costs of the disposal of industrial wastewater;
- High production capabilities.
- The implementation of investment strategies and taking investment measures.
- The expansion of the product range.
- Employees' expertise and experience.

2. Development prospects for the Issuer and the Group

The Parent Company and the Group link their development not only with the processing of potatoes, but also with power generation in a biogas plant located in a subsidiary CHP Energia. This company combines the generation of electricity and heat ([the so-called 'co-generation'](#)), which is characterised with the highest efficiency of the conversion of primary energy into final energy. Moreover, the generation of biogas results in the production of digestate, which is a

very good fertiliser for cultivation purposes. In addition, weather-independent efficiency of the production of this fuel is a great advantage of power generation from biogas. The present global situation poses new challenges in terms of the reduction of costs of heat and electricity consumption. Energy carriers are rapidly becoming more and more expensive. Investors must face an important issue of abandoning traditional sources and using instead, for example, renewable energy from biogas, which is becoming more and more popular with Polish investors and enterprises. In addition, in the area of ecological safety, the benefit lies in the disposal of waste in agricultural production and agricultural and food processing, e.g. of potato pulp, which is waste from the production of potato starch.

The processing of potatoes will still remain the Group's most important line of business; last year, this segment recorded a major increase in its production and sales. The Group has begun to expand into new foreign markets, especially in East Asia, South-East Asia, Africa, South America and developing European countries. This objective is being accomplished through the implementation of the export growth programme as part of the announced strategy. The Group will continue its research and development works in the cooperation with research institutes which specialise in research on the processing of starch and its derivatives, both as regards issues related to the company's current business and a new range of products.

The main objective of the Group is the maximum rate of return on investment while maintaining a moderate level of investment risk. As a result, the strategy of PEPEES Group assumes carrying out parallel development activities by increasing the efficiency of the operations of the Group companies and minimising the risks to which they are exposed as well as carrying out further investing activities. In the case of the emergence of attractive offers on the market, we will continue investing activities both in and outside the Group.

3. The development strategy of the Company and PEPEES Group

Further fast development of the company and increased production are the key objectives of PEPEES S.A. development strategy. The Company is able to achieve these goals mainly due to its numerous innovative activities, primarily new production lines ensuring higher production efficiency. The Company intends to expand the range of products on offer, diversify target markets and, above all, expand the base of materials used.

PEPEES Group intends to significantly increase starch production, which will allow it to compete with foreign enterprises. The Group's strategy provides for short-term tasks, such as those related to the improvement of the starch market in Poland and conditions for the functioning of growers, but also long-term activities to consolidate the starch industry. The Group is interested in maintaining good relations with growers, which will make it possible to build a group of permanent suppliers of materials thanks to the application of a clear and understandable contracting system.

Surplus products will be directed to foreign markets, with particular emphasis on developing markets, e.g. Asian markets. The new market strategy of the Group is based on the intensification of sales on external markets (especially on the markets of East Asia, Southeast Asia, South America and developing European countries).

This objective should be accomplished through the continuation of the Export Development Programme project, which will encompass the identification of foreign outlets key for the

Group and the creation of a selling system for them. The global demand for starch has been growing, so PEPEES Group is creating effective tools for the distribution and sales of domestic products.

The development strategy of PEPEES Group provides for the steady improvement of quality and cost competitiveness in relation to the leading Polish companies from the potato processing industry.

4. The policy regarding directions of the development of the Issuer's Group

The Group, taking into consideration its well-established competitive position on the market, extensive experience and good economic performance, will strive in 2019 and subsequent years to accomplish the following goals:

- enhancing the competitive position in all areas within its current scope of specialisations, including potato processing;
- focusing activities on the implementation of the Export Development Programme project;
- taking actions aimed at extending the product offer both in terms of quantity (new foreign markets) and quality;
- improving profitability and ensuring optimal liquidity in the context of fierce market competition.

PEPEES Group assumes continuous development and optimisation of the product range, bearing in mind customers' changing expectations and preferences. Product development will be based on research and implementations carried out primarily by the Quality, Technology and Innovation Function on its own.

V. THE COMPLIANCE WITH CORPORATE GOVERNANCE PRINCIPLES

I. Corporate governance principles the Issuer is governed by and the place where the text of the set of principles is publicly available

Pursuant to § 29 of the Rules of Giełda Papierów Wartościowych w Warszawie S.A. ('Warsaw Stock Exchange'), the Company complies with the corporate governance principles contained in the document titled **Best Practice of GPW Listed Companies 2016**, which is an Appendix to Resolution No. 26/1413/2015 of the Supervisory Board of the Warsaw Stock Exchange dated 13 October 2015 ('Best Practice'), available at: https://www.gpw.pl/pub/GPW/o-nas/DPSN2016_EN.pdf

The Company's Board of Directors hereby declare that, appreciating the importance of corporate governance principles contained in the aforementioned document and the role played by these principles in enhancing the transparency of listed companies, they have made every effort to ensure the Company's compliance with the aforementioned principles to the greatest extent possible.

Section II indicates the sections and the description of the principles in accordance with the Best Practice which are not complied with by the Company, and the reasons for non-compliance.

II. The extent to which the Issuer failed to comply with corporate governance principles, indicating such principles and explaining the reasons for such non-compliance

In 2018, PEPEES complied with all the recommendations and principles of the Best Practice, except for the following recommendations and principles:

I. Disclosure policy, investor communications

I.Z.1. A company should operate a corporate website and publish on it, in a legible form and in a separate section, in addition to information required under the legislation:

I.Z.1.3 “a chart showing the division of duties and responsibilities among members of the management board drawn up according to principle II.Z.1”

The principle is not fully complied with. The division of duties is provided for in the by-laws of the Board of Director available on the Company’s website.

I.Z.1.9 “information about the planned dividend and the dividend paid out by the company in the last 5 financial years, including the dividend record date, the dividend payment date and the dividend amount, in aggregate and per share”

The principle will be complied with if the General Meeting of Shareholders adopts the resolution on payment of dividend. In the last 5 years, no dividend has been paid.

I.Z.1.15 “information about the company’s diversity policy applicable to the company’s governing bodies and key managers; the description should cover the following elements of the diversity policy: gender, education, age, professional experience, and specify the goals of the diversity policy and its implementation in the reporting period; where the company has not drafted and implemented a diversity policy, it should publish the explanation of its decision on its website”

The Company has not developed and does not implement any diversity policy. When selecting members of the Board of Directors and of the Supervisory Board, the Company is invariably guided by the highest standards and, in this respect, does not discriminate against candidates because of their gender or other non-work-related traits. The authorities of the Company are selected taking into account primarily high competences, skills and professionalism of candidates.

I.Z.1.16. “information about the planned transmission of a general meeting, not later than 7 days before the date of the general meeting”

The Company is not planning any transmissions of the General Meeting of Shareholders.

I.Z.1.20. “an audio or video recording of a general meeting”

In accordance with applicable regulations, the Company draws up detailed records of general meetings of shareholders in the form of notarized minutes. In addition, by publishing required current reports and posting appropriate information on its website, the Company provides the shareholders with all relevant information concerning

general meetings of shareholders. The Company believes that such principles ensure the transparency of general meetings of shareholders.

II. Management board, supervisory board

II.Z.2. A company's management board members may sit on the management board or supervisory board of companies other than members of its group subject to the approval of the supervisory board.

Conflicts of interest are resolved in accordance with generally applicable laws, particularly pursuant to Article 380 of the Polish Commercial Code.

II.Z.3. At least two members of the supervisory board should meet the criteria of being independent referred to in principle II.Z.4.

Decisions concerning the selection of members of the Supervisory Board are made by the General Meeting of Shareholders. The Company's Board of Directors do not have any influence on such appointments and do not have information on the independence of the members of the Supervisory Board. In the Company's opinion, such a method of selecting members of the Supervisory Board properly protects the interests of the Company's shareholders.

II.Z.4. Annex II to the European Commission Recommendation 2005/162/EC of 15 February 2005 on the role of non-executive or supervisory directors of listed companies and on the committees of the (supervisory) board applies to the independence criteria of supervisory board members. Irrespective of the provisions of point 1(b) of the said Annex, a person who is an employee of the company or its subsidiary or affiliate or has entered into a similar agreement with any of them cannot be deemed to meet the independence criteria. In addition, a relationship with a shareholder precluding the independence of a member of the supervisory board as understood in this principle is an actual and significant relationship with any shareholder who holds at least 5% of the total vote in the company.

The principle is not complied with. The Supervisory Board works primarily in accordance with applicable regulations, the Articles of Association and the By-laws of the Supervisory Board.

II.Z.5. Each supervisory board member should provide the other members of the supervisory board as well as the company's management board with a statement of meeting the independence criteria referred to in principle II.Z.4.

The principle is not complied with. The Supervisory Board works primarily in accordance with applicable regulations, the Articles of Association and the By-laws of the Supervisory Board.

III. Internal systems and functions

III.R.1. The company's structure should include separate units responsible for the performance of tasks in individual systems or functions, unless the separation of such units is not justified by the size or type of the company's activity.

The separation of organisational units responsible for internal control, risk management,

compliance and internal audit is not justified due to the scale of the Company's activities.

III.Z.4. The person responsible for internal audit (if the function is separated in the company) and the management board should report to the supervisory board at least once per year with their assessment of the efficiency of the systems and functions referred to in principle III.Z.1 and table a relevant report.

In PEPEES, there is no separate internal audit function.

IV. General meeting, shareholder relations

IV.R.2. If justified by the structure of shareholders or expectations of shareholders notified to the company, and if the company is in a position to provide the technical infrastructure necessary for a general meeting to proceed efficiently using electronic communication means, the company should enable its shareholders to participate in a general meeting using such means, in particular through:

- 1) real-life broadcast of the general meeting;*
- 2) real-time bilateral communication where shareholders may take the floor during a general meeting from a location other than the general meeting;*
- 3) exercise of the right to vote during a general meeting either in person or through a plenipotentiary.*

In the opinion of the Board of Directors, there is no need to broadcast General Meetings or ensure real-time bilateral communication. General Meetings of Shareholders are held in the Company's registered office at convenient times; therefore, the participation in them is not hindered in any way for shareholders interested in them, who want to take floor or exercise their voting rights (either in person or through a plenipotentiary). Extremely high attendance at General Meetings of Shareholders is proof of the same. In addition, the Company is of the opinion that, despite advanced technology, there is always the risk, for various reasons (including the reasons beyond the control of the Company, shareholders or third parties), of not being able to guarantee the technical and legal security of the real-time bilateral communication, or of exercising voting rights using electronic communication means, and any damage arising from related disruptions might result in an unreasonable increase in the costs of the Company's operations.

IV.Z.2. If justified by the structure of shareholders, companies should ensure publicly available real-time broadcasts of general meetings.

In the opinion of the Board of Directors, there is no need to broadcast General Meetings or ensure real-time bilateral communication. General Meetings of Shareholders are held in the Company's registered office at convenient times; therefore, the participation in them is not hindered in any way for shareholders interested in them, who want to take floor or exercise their voting rights (either in person or through a plenipotentiary). Extremely high attendance at General Meetings of Shareholders is proof of the same. In addition, the Company is of the opinion that, despite advanced technology, there is always the risk, for various reasons (including the reasons beyond the control of the

Company, shareholders or third parties), of not being able to guarantee the technical and legal security of the real-time bilateral communication, or of exercising voting rights using electronic communication means, and any damage arising from related disruptions might result in an unreasonable increase in the costs of the Company's operations.

IV.Z.12. The management board should present to participants of an ordinary general meeting the financial results of the company and other relevant information contained in the financial statements to be approved by the general meeting.

In the opinion of the Board of Directors, there is no need to present and discuss results. Members of the Board of Directors are present at General Meetings of Shareholders and are ready to answer shareholders' questions.

V. Conflict of interests, related party transactions

V.Z.6. In its internal regulations, the company should define the criteria and circumstances under which a conflict of interest may arise in the company, as well as the rules of conduct where a conflict of interest has arisen or may arise. The company's internal regulations should among others provide for ways to prevent, identify and resolve conflicts of interest, as well as rules of excluding members of the management board or the supervisory board from participation in reviewing matters subject to a conflict of interest which has arisen or may arise.

The Company's practice does not indicate that such regulations are necessary. In the case of conflicts of interest, the Company applies generally applicable laws.

VI. Remunerations

VI.R.1. The remuneration of members of the company's governing bodies and key managers should follow the approved remuneration policy.

The Company adopted its remuneration policy, but members of the company's authorities are not subject to it.

VI.Z.4. In this activity report, the company should report on the remuneration policy including at least the following:

- 1) general information about the company's remuneration system;*
- 2) information about the conditions and amounts of remuneration of each management board member broken down by fixed and variable remuneration components, including the key parameters of setting the variable remuneration components and the terms of payment of severance allowances and other amounts due on termination of employment, contract or other similar legal relationship, separately for the company and each member of its group;*
- 3) information about non-financial remuneration components due to each management board member and key manager;*
- 4) significant amendments of the remuneration policy in the last financial year or information about their absence*

The aforementioned principle was not fully complied with by the Company. The reports disclose the remunerations of each member of the Board of Directors and of the Supervisory Board, but not broken down by fixed and variable remuneration components.

The scope and form of disclosed information about the remuneration policy result, in particular, from generally applicable laws to be observed by issuers of securities.

III. Report on the remuneration policy

PEPEES has the remuneration policy which determines the form, structure and amounts of remunerations of the Company's employees, including components depending on the Company's results and the commitment of particular employees. Remunerations of members of the Company's Board of Directors are determined by the Supervisory Board based on the qualifications, experience and responsibilities of a particular member of the Board of Directors. Remunerations of members of the Board of Directors include variable components, the amounts of which depend on accomplished financial results and on the level of the accomplishment of objectives set by the Supervisory Board. Remunerations of members of the Board of Directors are paid by the Company and by subsidiaries, depending on the involvement of a given Board member in operating activities of individual subsidiaries. Remunerations of members of the Supervisory Board are determined by the General Meeting of Shareholders and they do not include variable components. In its Directors' report, the Company discloses the total remuneration of members of the Board of Directors (not broken down into fixed and variable components) and of the Supervisory Board, broken down into amounts paid by the Company and jointly by the remaining entities from the Group.

In addition to their remuneration components, members of the Board of Directors and key employees use company cars and mobile phones, and participate in training courses financed by the Company. Last year, there were no significant amendments to the remuneration policy.

In the opinion of the Board of Directors, the remuneration policy is attuned to the achievement of the Company's goals, in particular long-term shareholder value growth and the company's stability.

IV. Sponsorship

PEPEES is a sponsor of many cultural, sporting and ecological events. In an effort to meet growing social, economic, cultural, educational and sports needs, principles have been adopted that may focus assistance on those areas where it can be used effectively. The sponsorship activities taken by the Company involve the financial and material support of regional and local initiatives. The primary direct goal of PEPEES sponsorship is to build and enhance brand awareness and to create a positive image of the initiative in which PEPEES participates as a sponsor.

AREAS OF ACTIVITIES

The Company is committed to the following areas of life:

1. Sport and education

- Promoting initiatives to support the development of science and education
- Supporting the development of physical culture and sports education

2. Culture

- Sponsoring local and regional events

3. Charity

- Supporting organisations working for people in need

V. The description of the main features of any internal controls and risk management systems in relation to the process of preparing financial statements and consolidated financial statements

The effectiveness of the internal controls and risk management system in the process of preparing consolidated financial statements is ensured through the development, implementation and supervision of the application, in the companies of PEPEES Group, of consistent accounting policies. The Group's companies submit required data in the form of reporting packets in order to prepare the consolidated financial statements of the Group. The scope of the disclosures in the Group is defined and results from disclosure requirements specified in IAS/IFRS. Changes in accounting standards are monitored on an ongoing basis in order to determine the need to update the scope of the reporting. All financial statements are verified by the Board of Directors of the parent company PEPEES. The Group's companies have their financial statements reviewed every 6 months and audited on an annual basis by an independent certified auditor. Also, consolidated financial statements are subject to an audit. By the time of the publication of the financial statements and of the consolidated financial statements, the information is made available only to the employees involved in the process of their preparation, verification and authorisation, ensuring data confidentiality.

VI. VI. Shareholders holding, directly or indirectly, qualifying holdings

To the best of our knowledge, as at 31.12.2018, the shareholding structure was as follows:

SHAREHOLDERS	No. of shares/votes	Percentage of share capital/total votes at GMS
	[pcs]	[%]
Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych	23,345,498	24.57 %
Mr Michał Skotnicki*	21,325,780	22.45 %
Mr Maksymilian Maciej Skotnicki*	20,703,282	21.79 %
Mr Newth Jonathan Reginald	7,995,200	8.42%
Richie Holding Ltd.	6,133,100	6.46%
Others	15,497,140	16.31 %
Total	95,000,000	100.00 %

** Mr Maksymilian Maciej Skotnicki and Mr Michał Skotnicki are persons referred to in Article 87(4)(1) of the Act on Public Offering [...] and, thus, together they hold the total of 42,029,062 shares/votes representing 44.24% of the share capital of/the total number of votes in the Company.*

After the end of the reporting period, the Company received information according to which, in January 2019, there had been a change in the shareholding structure, as a result of which Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych increased its holding in the Company.

The shareholding structure as at the date of this report is presented below.

SHAREHOLDERS	No. of shares/votes	Percentage of share capital/total votes at GMS
	[pcs]	[%]
Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych	27,609,982	29.06 %
Mr Michał Skotnicki*	21,325,780	22.45 %
Mr Maksymilian Maciej Skotnicki*	20,703,282	21.79 %
Mr Newth Jonathan Reginald	7,995,200	8.42%
Richie Holding Ltd.	6,133,100	6.46%
Others	11,232,656	11.82 %
Total	95,000,000	100.00 %

** Mr Maksymilian Maciej Skotnicki and Mr Michał Skotnicki are persons referred to in Article 87(4)(1) of the Act on Public Offering [...] and, thus, together they hold the total of 42,029,062 shares/votes representing 44.24% of the share capital of/the total number of votes in the Company.*

VII. The holders of any securities with special rights

The Company did not issue any securities with special rights.

VIII. Any restrictions on voting rights

The Company's Articles of Association do not provide for such restrictions. However, the prohibition for a shareholder to exercise his voting rights may result from Article 89 of the Act of 29 July 2005 on public offering and the conditions for introducing financial instruments to an organised trading system, and on public companies (hereinafter referred to as the '**Offering Act**'), if the shareholder violates specific provisions of Chapter 4 of the Offering Act. In turn, pursuant to Article 6 §1 of the Polish Commercial Code, if the parent company fails to notify its subsidiary of the emergence of the relationship of control within two weeks from the date of the emergence of this relationship, the voting rights attached to the shares of the parent company representing more than 33% of the share capital of the subsidiary will be suspended.

IX. Any restrictions on the transfer of securities

The Company's Articles of Association do not provide for such restrictions. However, they result from the law, including Articles 11 and 19 of Chapter 4 of the Offering Act referred to above; and Part VI of the Act of 29 July 2005 on trading in financial instruments; the Act of 16 February 2007 on competition and consumer protection; and Council Regulation (EC) No. 139/2004 of 20 January 2004 on control of concentrations between undertakings.

X. The rules governing the appointment and dismissal of board members, and their powers

1. The Board of Directors is composed of one to five members. The term of office of the Board of Directors is three years, except for the term of office of the first Board of Directors, which is two years. The Supervisory Board appoints the President of the Board of Directors and, upon the motion of the President of the Board of Directors, also other members of the Board of Directors. The Supervisory Board determines the number of the members of the Board of Directors. The Supervisory Board may dismiss the President of the Board of Directors, a member of the Board of Directors or all members of the Board of Directors prior to the expiration of the term of office of the Board of Directors. The Board of Directors exercises all the powers related to the management of the Company, except for the powers reserved by the law or the Articles of Association to other Company's authorities.
2. The operation of the Board of Directors, and the matters that can be assigned to its particular members, are determined in detail in the By-laws of the Board of Directors. The By-laws of the Board of Directors are adopted by the Company's Board of Directors and approved of by the Supervisory Board.
3. The following persons are authorised to make declarations and sign documents on behalf of the Company:
 - (i) if the Board of Directors is composed of one member – President of the Board of Directors; (ii) if the Board of Directors is composed of more than one member – two members of the Board of Directors acting jointly or one member of the Board of Directors acting jointly with a proxy.
4. The Supervisory Board enters into, on behalf of the Company, agreements with the members of the Board of Directors and represents the Company in disputes with the members of the Board of Directors. The Supervisory Board may authorise, by virtue of its resolution, one or more its members to perform such legal acts.
5. The Company's employees are subordinate to the Board of Directors. The Board of Directors enters into and terminates their contracts of employment and determines their remunerations.
6. The decision on the issue or redemption of shares is made by the General Meeting of Shareholders by way of its resolution.

XI. Amendments to the Company's Articles of Association

Amendments to the Company's Articles of Association are made by virtue of a resolution of the General Meeting of Shareholders. Such resolutions are adopted with the majority of three-fourths of the votes cast. Resolutions regarding amendments to the Company's Articles of Association, which increase the benefits of shareholders or reduce the rights bestowed personally upon individual shareholders, require the consent of all affected shareholders.

XII. The operation of the General Meeting of Shareholders and its powers

The basic principles of the operation of the General Meeting of Shareholders are as follows:

1. The Ordinary General Meeting of Shareholders is convened each year by the Board of Directors in June at the latest.
2. The agenda of the General Meeting of Shareholders is determined by the Board of Directors in consultation with the Supervisory Board.
3. The Supervisory Board and shareholders representing at least 5% of the share capital may demand to include particular items in the agenda of the General Meeting of Shareholders.
4. General Meetings of Shareholders are held in the Company's registered office.
5. The General Meeting of Shareholders may adopt resolutions regardless of the number of shareholders present at the Meeting or shares represented at it.
6. Resolutions are adopted at the General Meeting of Shareholders in voting.
7. Resolutions of the General Meeting of Shareholders are adopted with a simple majority of the votes cast, unless the Articles of Association or the law provide for otherwise.
8. Resolutions of the General Meeting of Shareholders are adopted with the majority of 3/4 of the votes cast in the case of the following matters:
 - a) amendments to the Articles of Association, including issues of new shares;
 - b) issues of bonds;
 - c) the disposal of the Company's enterprise;
 - d) the business combination of the Company with another company;
 - e) the Company's winding-up and dissolution.
9. The voting at the General Meeting of Shareholders is open. Confidential voting is ordered in the case of elections and motions concerning the dismissal of members of the Company's authorities or liquidators, and on making them accountable, and on personal matters. Resolutions on amendments to the Company's objects are adopted by an open vote by roll call.
10. Shareholders entitled to participate in the General Meeting of Shareholders are the shareholders listed in the shareholders register drawn up by the Board of Directors in accordance with the principles resulting from applicable laws, particularly in accordance with Article 406 § 2 and Articles 406¹ – 406³ of the Polish Commercial Code.
11. The following persons may also be present at the General Meeting of Shareholders: each member of the Board of Directors; each member of the Supervisory Board; the notary public and his/her aides; the certified auditor; members of the organisational

and technical support team for the General Meeting of Shareholders authorised by the Board of Directors; other persons designated by the authority convening the General Meeting of Shareholders. Persons other than those mentioned above may be present only with the consent of the Chairman of the General Meeting of Shareholders, who has the right, at all times and without justification, to order any such person to leave the room where the General Meeting of Shareholders is taking place.

12. The General Meeting of Shareholders is opened by the Chairman of the Supervisory Board or his deputy, and, in their absence, by the President of the Board of Directors or any other person designated by the Board of Directors. The person opening the General Meeting of Shareholders shall order to put forward candidates for the Chairman of the General Meeting of Shareholders, and, when such candidates are proposed, to elect the Chairman.
13. The Chairman of the General Meeting of Shareholders presents to shareholders the agenda as proposed by the Board of Directors in the notice on the convening of the General Meeting of Shareholders and, in the absence of draft resolutions, formulates and presents draft resolutions. Any shareholder may submit a draft resolution concerning any matter included in the agenda.

The Company's shareholders have no special rights, except for the rights under generally applicable laws, including those provided for in the Polish Commercial Code.

XIII. The composition and operation of the management and supervisory bodies

1. The composition of the Board of Directors of PEPEES as at 31.12.2018:

Mr Wojciech Faszczewski – President

Mr Tomasz Rogala – Member

The operation and powers of the Company's Board of Directors are governed by the Company's Articles of Association and the By-laws of the Board of Directors.

Basic principles of the operation of the Board of Directors are described in item X above.

2. The composition of the Supervisory Board of PEPEES as at 31.12.2018:

Mr Maciej Kaliński – Chairman

Mr Tomasz Nowakowski – Vice-Chairman

Mr Piotr Taracha – Secretary

Mr Krzysztof Stankowski – Member

Ms Agata Czerniakowska – Member

Mr Robert Malinowski – Member

Basic principles of the operation of the Supervisory Board are defined in the Company's Articles of Association and the By-laws of the Supervisory Board. According to these regulations, the Supervisory Board is composed of five to nine members. The term of office of the Supervisory Board is three years.

The Supervisory Board elects, from among its members, the Chairman and one or two vice-chairmen and a secretary. The Chairman of the Supervisory Board convenes the Board meetings and presides over them. The Chairman of the outgoing Supervisory Board convenes and opens the first meeting of the newly elected Supervisory Board and presides over it until the time of electing the new Chairman. The Supervisory Board holds its meetings at least once a quarter. The Chairman of the Supervisory Board or one of his/her deputies must convene the Board meeting upon a written request of at least two members of the Supervisory Board. The meeting should be convened within one week from the date of the request, on the day falling not later than the final day of the period of two weeks from the date of convening the meeting. For resolutions of the Supervisory Board to be valid, all its members must be invited to the meeting. The Supervisory Board adopts resolutions with an absolute majority of the votes present at the meeting of the members of the Supervisory Board, on condition that at least half of its members are present at the meeting. Resolutions of the Supervisory Board may also be adopted without a meeting by voting in writing if all members of the Supervisory Board agree in writing to adopting resolutions in such a manner. The Supervisory Board adopts its by-laws specifying in detail the operation of the Board. The Supervisory Board may delegate its members to perform specific supervisory activities on an individual basis. The General Meeting of Shareholders determines the remuneration of the members of the Supervisory Board.

Pursuant to the Company's Articles of Association, apart from the matters provided for in legal acts, in other provisions of the Articles of Association or in the resolutions of the General Meeting of Shareholders, the Supervisory Board has the following powers:

- 1) examining the annual balance sheet and income statement, and ensuring their verification by certified auditors chosen by it;
- 2) examining and evaluating the Board of Directors' report;
- 3) examining on an annual basis and approving of the Company's business, financial and marketing plans, and requesting the Board of Directors to present detailed reports on the implementation and accomplishment of such plans;
- 4) submitting to the General Meeting of Shareholders written reports on the results of the activities referred to in items 1-3;
- 5) expressing opinions on the proposals of the Company's Board of Directors regarding the distribution of profits, including amounts allocated to dividend, dividend payment dates or the principles governing the covering of losses;
- 6) authorising transactions involving the disposal or acquisition of shares or other assets, or the taking out of a cash loan, if the value of a given transaction exceeds 15% of the Company's net assets as per the most recent balance sheet;
- 7) appointing, suspending and dismissing members of the Board of Directors;
- 8) delegating Supervisory Board members to perform the duties of the Board of Directors in the event of the suspension or dismissal of the entire Board of Directors or when the Board of Directors is not capable of working for other reasons;
- 9) approving of the rules, adopted by the Board of Directors, governing the allocation of shares to eligible employees.

In the reporting period, within the Issuer's Supervisory Board, there operated **the Audit Committee** composed of:

Mr Maciej Kaliński – Chairman Mr

Mr Piotr Taracha – Vice-Chairman

Mr Krzysztof Stankowski – Member

It worked without interruption with these members until 31 December 2018.

All aforementioned persons who are members of the Audit Committee meet the statutory independence criteria.

Mr Piotr Taracha has the expertise and qualifications in the area of accounting, as he graduated from postgraduate studies for financial officers with the specialisation in corporate finance management, and has completed numerous courses in finance and accounting.

Mr Krzysztof Stankowski has the expertise in the industry in which the Issuer operates, as he graduated from a secondary agricultural school and performs supervisory functions in potato processing companies.

PEPEES and its subsidiaries have concluded the agreement for the period of reviewing and auditing the financial statements (including consolidation packages) for 2018 with WBS Audyt Sp. z o.o. with its registered office in Warsaw, Poland. The agreement was concluded on 4 July 2018. The audit firm was selected by the Company's Supervisory Board.

The Issuer did not use any other services of the appointed audit firm.

Pursuant to the Polish Act on statutory auditors, audit firms and public oversight (Journal of Laws of 2017 item 1089 of 11 May 2017, as amended; hereinafter 'the Act') and Regulation No 537/2014 of the European Parliament on specific requirements regarding statutory audit of public-interest entities ('Regulation No 537/2014'), the Audit Committee has adopted and applies "The policy and procedure for appointing the audit firm" and "The policy concerning the provision by the audit firm conducting the audit, by affiliates of that audit firm and by a member of the audit firm's network, of permitted non-audit services".

According to the aforementioned policies, the audit firm is appointed by the Supervisory Board acting on the recommendations of the Audit Committee. The policy defines periods of cooperation with audit firms, auditor selection criteria such as previous experience, reputation as well as qualifications and experience of persons delegated to perform auditing activities by an audit firm, knowledge of the industry in which the Company operates, pricing conditions or the proposed work schedule, and stipulates that the appointment of an audit firm should take place in an independent manner, free from any pressure or suggestions from third parties regarding the appointment, and any restrictions on appointment result from the generally applicable law.

The policy concerning the provision of permitted services by an audit firm stipulates, first of all, that all services provided by an audit firm or its affiliates require a prior assessment of risks and independence by the Audit Committee, and it also seeks to limit the possibility of a conflict of interest if an audit firm is hired to provide permitted non-audit services by defining prohibited services and permitted services. Examples of permitted services include, for example, conducting due diligence procedures related to economic and financial condition, attestation services related to *pro forma* financial information,

forecasts of results or estimated results, including the audited entity in a prospectus, examining historical financial information for the prospectus, verifying consolidation packages. In turn, prohibited services are, in particular, tax services regarding: preparation of tax forms, taxes on remunerations, customs obligations, bookkeeping and preparation of accounting records and financial statements, development and implementation of internal control procedures or risk management procedures related to the preparation or control of financial information or development and implementation of technological systems related to financial information, or services related to the internal audit function. The provision of permitted services is possible only to the extent not related to the Company's tax policy, following the Audit Committee's assessment of the risks and safeguards of the independence of the audit firm, the key statutory auditor and other members of the audit team.

The recommendation regarding the appointment of an audit firm to conduct the audit met the applicable conditions and was made as a result of the appointment procedure organised by the Issuer that met the applicable criteria.

In the period from 1 January 2018 to 31 December 2018, the Audit Committee held three meetings.

The main tasks of the Committee are as follows:

- Discussing the audit process with the auditor.
- Examining the Company's documents.
- Submitting the annual report on its activities to the Supervisory Board.
- Monitoring the financial reporting process.
- Monitoring the performance of auditing activities, in particular of the audit firm's audit of the Company's financial statements, including all requests and findings of the Audit Oversight Commission resulting from audits carried out at the audit firm.
- Controlling and monitoring the independence of the statutory auditor or the audit firm providing services to the Company.
- Informing the Supervisory Board about the results of the audit of the Company's financial statements and explaining how the audit contributed to the fairness of financial reporting in the Company, and explaining the role of the Committee in the audit process.
- Assessing the independence of the auditor and giving consent to their provision of services to the Company.
- Developing the policy of appointing an audit firm to audit the Company's financial statements.
- Developing the policy concerning the provision by the audit firm conducting the audit of the financial statements, by affiliates of that audit firm and by a member of the audit firm's network, of permitted services not being the audit of financial statements.
- Determining the procedure for the appointment of an audit firm by the Company.
- Submitting recommendations aimed at ensuring the fairness of the financial reporting process in the Company.

The mode of the operation of the Audit Committee:

- The Audit Committee holds meetings as needed, at least twice a year.
- The meetings of the Committee are convened by its Chairman, either upon his own initiative or upon the request of any member of the Audit Committee, and also upon the

request of the Board of Directors, internal or external auditor. A meeting of the Audit Committee may also be convened by the Chairman of the Supervisory Board.

- The agenda of the meeting of the Audit Committee is determined by the party convening the meeting, and it may be amended during the meeting.
- The Chairman of the Audit Committee may invite persons not being members of the Audit Committee to attend a given meeting.
- The meetings of the Audit Committee are recorded in the form of written minutes. The minutes are signed by the Chairman of the Audit Committee.
- The Audit Committee may adopt resolutions if at least half of its members participate in the meeting of the Audit Committee.
- The Audit Committee may adopt resolutions in writing, provided that all members of the Audit Committee have been notified of the texts of draft resolutions.
- Resolutions of the Audit Committee are taken by a simple majority of the votes cast.
- The Company ensures the organisational and technical support for the Audit Committee.

Apart from the Audit Committee, no other committees function within the Company's Supervisory Board.


XIV. Diversity policy

The Company has not developed and does not implement any diversity policy. When selecting members of the Board of Directors and of the Supervisory Board, the Company is invariably guided by the highest standards and, in this respect, does not discriminate against candidates because of their gender or other non-work-related traits. The authorities of the Company are selected taking into account primarily high competences, skills and professionalism of candidates.

Signatures of all Members of the Board of Directors of the Parent Company:

President of the Board of Directors – Wojciech Faszczewski


Signed by:

 Wojciech Faszczewski
Przedsiębiorstwo
Przemysłu Spożywczego
PEPPES S.A.

Date: 2019-03-26 12:20

Member of the Board of Directors – Tomasz Rogala

Signed by:

 Tomasz Krzysztof Rogala
Przedsiębiorstwo
Przemysłu Spożywczego
PEPPES S.A.

Date: 2019-03-26 10:35