Polski Koncern Naftowy ORLEN
Spółka Akcyjna

Management Board Report on the Operations of the Polski Koncern Naftowy Spółka Akcyjna Group in the first half of 2008

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I. CURRENT AND PROJECTED FINANCIAL STANDING OF THE PKN ORLEN CAPITAL GROUP

1.1 Income statement

1.1.1 Revenues

In the I half of 2008 the PKN ORLEN Capital Group (the „ORLEN Group") generated total sales revenues (excluding excise tax) in the amount of PLN 40,028,169 thousand, i.e. by 35.1% more than in the I half of 2007. This increase reflects the total effect of changes in value and volumes in the core business segments of the ORLEN Group.

The increased revenues were recorded in the following segments:
Refining – by 30.5%;
Other operations – by 0.1%.

The decreased sales were recorded in the following segments:
Petrochemical – by 2.3%;
Chemical – by 0.2%.

1.1.2 Profit from operations

The gross profit on sales generated by the ORLEN Group in the I half of 2008 amounted to PLN 4,418,168 thousand and was higher by 5.8% as compared to the profit generated in the I half of 2007. The profit from operations amounted to PLN 2,211,396 thousand and was higher than the profit from operations generated in a respective period of 2007 by 544,917 thousand.

The increase in profit on sales was due to the increased volumes of sales which enabled the Group to mitigate the increased costs of finished goods, merchandise and raw materials sold by PLN 10,160,458 thousand (i.e. 39.9%). The increased profit from operations generated by the ORLEN Group was, among others, due to the higher profit from operations in Polski Koncern Naftowy ORLEN S.A. ("PKN ORLEN S.A.") and the Mazeikiu Capital Group (the "Mazeikiu Group") by, respectively, PLN 492,989 thousand and PLN 490,832 thousand. The decrease in profit from operations as compared to the respective period of the prior year was noted, among others, in the UNIPETROL Capital Group (the "UNIPETROL Group") by PLN 369,028 thousand.

In the I half of 2008, as compared to the prior year, an increase in the distribution expenses and a drop in general and administrative expenses was noted by, respectively, PLN 92,211 thousand, i.e. 6.0%, and by PLN 85,151 thousand, i.e. 11.1%. The increase in the distribution expenses has resulted from the increase mainly in PKN ORLEN S.A. and in the Mazeikiu Group by PLN 45,127 thousand and by PLN 19,266 thousand respectively. The drop in general and administrative expenses was mainly due to the decrease in PKN ORLEN S.A. and in the Mazeikiu Group by PLN 48,323 thousand and PLN 49,963 thousand, respectively.

On the other operating activities the profit of PLN 93,427 thousand was generated in the I half of 2008 while in the respective period of 2007 the loss was suffered amounting to PLN 217,360 thousand. The positive result on this type of operations recorded in the I half of 2008, as compared to the prior year, was due to reduced costs in the UNIPETROL Group that dropped by PLN 125,227 thousand as a result of a decrease in the non-current assets impairment allowance by PLN 122,786 thousand. In the I half of 2008, EBITDA amounted to PLN 3,405,627 thousand and was higher by PLN 537,892 thousand than that generated last year.

1.1.3 Financing activities

Financial revenues in the I half of 2008 amounted to PLN 1,030,860 thousand and were higher by PLN 729,508 thousand as compared to the respective period of 2007. Concurrently, financial expenses increased by PLN 99,169 thousand as compared to the I half of 2007. Consequently, profit on this type of activity in the I half of 2008 amounted to PLN 565,010 thousand (in the prior year the ORLEN Group noted a loss of PLN 65,329 thousand). The main factor affecting the profit generated on this type of activity was the currency exchange rate. In the I half of 2008 the Polish zloty was highly appreciated, which resulted in high positive exchange differences, which significantly contributed to the increase in financial revenues by PLN 741,961 thousand (PLN 192,572 thousand in the I half of 2007). Concurrently, the costs of negative foreign exchange surplus in the I half of 2008 amounted to PLN 24,187 thousand (PLN 32,753 thousand in the I half of 2007).

1.1.4 Profit before tax, income tax and net result

In the I half of 2008 the ORLEN Group generated profit before tax in the amount of PLN 2,928,176 thousand, i.e. by 69.8% more than in the I half of 2007. The net profit amounted to PLN 2,414,239 thousand and was therefore higher than that realized in the I half of prior year by 78.2%. The net profit attributable to equity holders of PKN ORLEN S.A. amounted to PLN 2,366,868 thousand.

1.2 Balance sheet

As at 30 June 2008, the ORLEN Group balance sheet totalled to PLN 48,152,549 thousand and was higher by PLN 2,003,117 thousand (by 4.3%) as compared to 31 December 2007.

The value of non-current assets decreased as compared to the situation as at 31 December 2007 by PLN 525,568 thousand (i.e. 2.0%) and amounted to PLN 26,257,376 thousand, mostly due to the drop in value of the property, plant and equipment by PLN 490,594 thousand (i.e. 2.0%), intangible assets by PLN 18,473 thousand (i.e. 3.5%) and deferred tax assets by PLN 31,807 thousand (i.e. 13.6%) as compared to 31 December 2007. The abovementioned drop in the I half of 2008 was partly balanced with an increase in long-term financial assets' value by PLN 5,898 thousand (i.e. by 9.5%) and an increase in the value shares held in entities, accounted for using equity method, by PLN 5,819 thousand (i.e. by 0.8%).

As at the end of the I half of 2008, the value of current assets increased up to PLN 21,895,173 thousand from the level of PLN 19,366,488 thousand as at 31 December 2007. The main factors triggering the current assets increase included the incrementing value of inventories by PLN 1,423,121 thousand (by 13.7%) and the increase in trade and other receivables by PLN 1,332,149 thousand (by 19.4%). The increase in inventories and receivables was due to the increase in crude oil and fuel prices. Concurrently, a material decrease in the income tax receivables was noted, namely by PLN 63,519 thousand (by 55.1%), in the value of non-current assets classified as held for sale - by PLN 162,006 thousand (by 86.1%), and in the value of cash and cash equivalents - by PLN 108,856 thousand, i.e. by 7.3% as compared to the prior year.

As at the end of the I half of 2008 the net working capital (current assets minus short-term liabilities except for loans and borrowings) amounted to PLN 8,594,210 thousand where the net working capital as at the end of 2007 amounted to PLN 8,647,048 thousand. This decrease was due to the increased trade and other liabilities and accrued expenses.

The total equity as at 30 June 2008 amounted to PLN 23,505,465 thousand and increased by PLN 886,098 thousand, i.e. by 3.9% as compared to the end of 2007, mainly as a result of an increase in retained profits, by PLN 1,673,156 thousand. The equity was negatively influenced by increased foreign exchange differences on subsidiaries from consolidation in an amount of PLN (-) 632,419 thousand.

The long-term liabilities amounted to PLN 10,473,575 thousand and decreased as compared to the end of 2007 by PLN 617,827 thousand, mainly due to a decrease in long-term loans and borrowings by PLN 591,601 thousand and a decrease in provisions, including deferred tax liabilities, in total by PLN 43,370 thousand.

The short-term liabilities, however, increased from PLN 12,438,663 thousand recognized as at 31 December 2007 to PLN 14,173,509 thousand recognized as at 30 June 2008. As part of the short-term liabilities, the trade and other liabilities and accrued expenses significantly increased by PLN 2,496,061 thousand (by 27.2%) whereas the short-term loans and borrowings decreased by PLN 846,677 thousand (by 49.2%) and the provisions by PLN 28,337 thousand (by 3.9%). The decrease in short-term loans and borrowings has resulted from a reduction of indebtedness of the Mazeikiu Group of PLN 448,750 thousand. As at 30 June 2008, the total indebtedness of the ORLEN Group (loans and borrowings) amounted to PLN 8,883,666 thousand, which means a drop by PLN 1,438,278 thousand as compared to the end of 2007.

1.3 Statement of cash flows

1.3.1 Operating activities

The net cash flows from operating activities increased by PLN 359,105 thousand as compared to the I half of 2007 and amounted to PLN 2,267,742 thousand. The net profit realized in the I half of 2008 was higher than that realized in the I half of 2007 by PLN 1,059,284 thousand with a concurrent increase in the change of receivables by PLN (-) 794,012 thousand and an increase in the change of inventories by PLN (-) 311,131 thousand as well as an increase in the change of liabilities by PLN 987,853 thousand in the analysed periods. The net exchange rate differences recognized in the net profit was higher by PLN (-) 351,851 thousand in the I half of 2008 and amounted to PLN (-) 533,370 thousand while in the I half of 2007 it was PLN (-) 181,519 thousand.

1.3.2 Investing activities

In the I half of 2008 the net cash flows from investing activities amounted to PLN (-) 1,255,278 thousand while in the respective period of the prior year it was PLN (-) 1,421,476 thousand. In the I half of 2008 capital expenditures (spent on the acquisition of property, plant and equipment and intangible assets) amounted to PLN (-) 1,567,119 thousand as compared to PLN (-) 1,427,602 thousand in the I half of the prior year. In the I half of 2008, the interest and dividend received amounted to PLN 102,576 thousand while in the respective period of the prior year – to PLN 199,563 thousand. Moreover, in the I half of 2007, proceeds form sale of short-term securities of PLN 251,142 thousand were earned.

1.3.3 Financing activities

In the I half of 2008 the net cash flows from financing activities amounted to PLN (-) 1,121,206 thousand while in the I half of 2007 it was PLN (-) 583,268 thousand. In the I half of 2008 the proceeds from loans, borrowings and debt securities issued amounted to PLN 3,028,545 thousand and were lower by PLN 695,562 thousand than the proceeds from loans and borrowings obtained in the I half of 2007. In the I half of 2008 the expenditures on repayment of loans, borrowings and repurchase of debt securities as well as interest paid amounted to PLN (-) 4,132,048 thousand and was lower by PLN (-) 163,357 thousand than the respective expenditures made in the I half of 2007.

The total cash flows from particular activities of the ORLEN Group triggered a drop in cash and cash equivalents by PLN 108,742 thousand down to PLN 1,389,376 thousand as at 30 June 2008 (as compared to the cash and cash equivalents as at 30 June 2007 amounting to PLN 2,254,585 thousand).

1.4 Description of significant risk factors and threats

The most important risk factors having an impact on the performance of the ORLEN Group included the following:

Fluctuations in crude oil prices and refinery and petrochemical products margins

In the I half of 2008 the crude oil prices were characterised with a strong upward trend. The crude oil quotations of Brent DTG increased from the level of 90 USD/bbl at the beginning of 2008 to over 140 USD/bbl at the end of June 2008 as a result of too poor supply of crude oil and strong demand for the same. In the I half of 2008 the margin on light heating oil increased by 126.0% up to the level of 195.74 USD/t, diesel oil by 101.8% to 227.84 USD/t and Jet A-1 fuel by 79.7% to reach the level of 279.52 USD/t. Reverse tendencies were recorded in respect of gasolines where margins dropped by 25.2% down to the level of 135.95 USD/t and III heating oil – the drop in margins by 69.9% down to (-) 333.26 USD/t. In the I half of 2008 the economic situation in the petrochemical segment also decreased which was characterised with the drop in margines of almost all products. With respect to basic products provided to PKN ORLEN S.A., i.e. ethylene and propylene, the market noted, respectively, the increase by 9.9% up to the level of 756.77 USD/t and the drop by 4.2% down to the level of 610.42 USD/t as compared to the I half of 2007.

Fluctuations of foreign exchange rates

The fluctuations of foreign exchange rates have a significant impact on the revenues from sales. This mainly relates to PLN/USD and PLN/EUR. The revenues and gains are mainly dependent on the value of PLN against foreign currencies due to shaping prices on the Polish market on the basis of the so-called import parity which consists in establishing prices of refinery and petrochemical products on the basis of European quotations. Additionally, the costs of crude oil and raw materials as well as the costs of debt handling are expressed in foreign currencies. Therefore, the PLN exchange rate changes against foreign currencies affect the result generated by the ORLEN Group. In the I half of 2008 the average PLN/USD exchange rate decreased by 21.1%, down to the level of 2.29, as compared to the I half of 2007 (calculated as the arithmetic average of daily rates determined by the National Bank of Poland from 1 January to 30 June). Concurrently, the average PLN/EUR exchange rate weakened by 9.2%, down to the level of 3.49. The appreciation of PLN arose out of a macroeconomic situation which implies the acceleration of economic growth. The other factors that materially affected the exchange rate include: high production dynamics, increased investment and consumer demand as well as an improved labour market situation.

In the I half of 2008, the average LTL/USD exchange rate dropped by 13.1% down to the level of 2.26 LTL/USD as compared to the I half of 2007. The LTL/EUR exchange rate amounting to 3.45 LTL/EUR remained at the same level as in 2007. In the I half of 2008, the average CZK/USD exchange rate decreased by 22.2% as compared to the prior year, down to 16.48 CZK/USD. Concurrently, the average CZK/EUR exchange rate dropped by 10.5% down to 25.19 CZK/EUR.

Economic growth and unemployment rate

The I half of 2008 witnessed a further acceleration of GDP economic growth. The estimated GDP increase reached the level of 6.0% given 6.5% in the I half of 2007. The economic growth is mainly due to the domestic demand, capital expenditures and a dynamic growth of exports. According to the preliminary data of the Central Statistical Office, in the I half of 2008 exports amounted to EUR 47.5 billion and as compared to the I half of 2007 increased by 17.1%. The advantageous tendencies on the labour market have strengthened. Employment in the I half of 2008 was higher by 5.6% than in the I half of 2007 and the unemployment rate dropped down to 9.6%, i.e. by 2.7 pp. as compared to the prior year. In the Czech Republic and Lithuania the estimated GDP dynamics in the I half of 2008 amounted, respectively, to 4.5% and 6.2% while in the I half of 2007 it was 6.5% and 8.1% respectively. The GDP dynamics in Germany in the I and II quarter of 2008 amounted, respectively, to 1.8% and 3.1% given 3.4% and 2.5% in the prior year. The improved situation on the labour market and favourable macroeconomic tendencies have materially affected the sales level in respect of the ORLEN Group's products.

Inflation

In the I half of 2008 the prices were increasing faster than during the respective period of the prior year. The I half of 2008 saw the inflation of 4.2% as compared to 2.2% in the I half of 2007 (y/y). The consumer goods and services prices increased due to the strong domestic demand. In the Czech Republic and Germany the inflation in the I half of 2008 amounted to 5.4% and to 3.5% as compared to 2.1% and 2.1%, respectively, in the I half of 2007. In Lithuania the average annual inflation amounted in June 2008 to 9.3% as compared to 4.4% in June 2007.

Interest rates

In the I half of 2008 the Polish money market saw the base interest rates rising four times: in January, February, March and June each time by 0.25 pp. As at the end of the I half of 2008 the interest on Lombard credits attained the level of 7.50%, and bill of exchange rediscount rate the level of 6.25% (as at the end of the I half of 2007 it was respectively 6.00% and 4.75%). WIBOR 3M rate increased from the level of 4.31% in the I half of 2007 up to the level of 6.10% in the I half of 2008. In the Czech Republic the interest on Lombard credits as at the end of the I half of 2008 amounted to 4.75% and the bill of exchange rediscount rate – 2.75% (as at the end of the I half of 2007 it was respectively 3.75% and 1.75%). PRIBOR 3M rate increased from 2.67% in the I half of 2007 up to 4.07% in the I half of 2008. In Lithuania the interest on Lombard credits in the I half of 2008 attained the level of 8.06% as compared to 7.94% in the I half of 2007. VILIBOR 3M rate amounted in the I half of 2008 to 5.19% as compared to 4.32% in the I half of 2007. The interest rate for loans on the European market (including German market) EURIBOR 3M rate amounted in the I half of 2008 4.67%, while in the I half of 2007 it equalled 3.94%. The interest rates have directly affected the debt handling costs. Loans and debt securities denominated in PLN represent app. 21% of the total interest liabilities in PKN ORLEN S.A. The remaining part is denominated in EUR, USD and CZK.

Mandatory reserves

Entrepreneurs operating on the Polish fuel market are under obligation to create, by the end of 2008, mandatory reserves in the quantity equivalent to at least the 76-day average daily internal consumption of crude oil and petroleum products. Moreover, the Material Reserves Agency is responsible for creating State reserves of crude oil and liquid fuels in the quantity equal to the 14 day fuel consumption and net imports of crude oil in a given year. In total, Polish entrepreneurs and the Material Reserves Agency create reserves equivalent to at least 90-day average daily internal consumption of crude oil and petroleum products.

The way how the mandatory liquid fuel reserves in Poland are to be created and how the quantities of such reserves are set has been defined in detail in the Ministry of Economy Regulation of 24 April 2007 (Journal of Laws 81 Items 546, 547).

The way how the mandatory liquid fuel reserves in the Republic of Lithuania are to be created and how the quantities of such reserves are set has been defined in detail in Regulation no. 1901 of 5 December 2002 on approving the procedure for the construction, gathering and maintaining warehouses of crude oil derivative products and oils and the minimum quantities of crude oil derivative products (Official Journal, 2002, no. 117-5255). By the end of 2009 the mandatory reserves must be created at the level of 90-day average daily sales of fuels on the internal market. The entrepreneurs are responsible for assuring 50% of these mandatory reserves and the other 50% is secured by the State Agency which obtains funds for this purpose from the State budget.

The way how the mandatory liquid fuel reserves in the Czech Republic are to be created and how the quantities of such reserves are set is regulated by the Act no. 189/1999 "Mandatory reserves of crude oil" issued by the Parliament of the Czech Republic on 29 July 1999 and amended by Regulation no. 560/2007 of 24 September 2004. The

mandatory reserves are maintained by the State Agency at the level of the 90-day net imports of crude oil and are funded from the State budget.

As at 30 June 2008 and 31 December 2007 the value of mandatory reserves in the ORLEN Group amounted respectively to PLN 5,969,208 thousand and PLN 4,802,805 thousand.

For further details regarding the mandatory reserves see Note 13 to the consolidated financial statements.

Fuel consumption

A change of tendencies in the domestic fuel consumption may have a significant impact on the volume of sales of core products of the ORLEN Group's members operating on the Polish market and, thus, it translates to an overall financial situation of PLN ORLEN S.A. On the basis of preliminary data provided by Agencja Rynku Energii S.A. ("ARE") (Power Market Agency), the overall domestic consumption of fuel (gasoline, diesel oil and light heating oil ("LHO")) in the I half of 2008 achieved the level of 7,462 thousand tonnes and was higher than the consumption in the I half of 2007 by approx. 6%.

The consumption of gasoline was maintained at the same level as in the I half of 2007. The stable situation on this market has been achieved due to a fast pace of economic growth and increasing retail prices of diesel oil which has contributed to the increased gasoline demand.

In the I half of 2008 the consumption of diesel oil was higher by almost 11% as compared to the I half of 2007. The development of this market was due to a continuous fast economic growth pace and the relating need for transportation services. The stable factor enhancing the diesel oil consumption increase was also a growing share of diesel motor cars in the Polish car fleet.

The consumption of LHO decreased by almost 12% as compared to the I half of 2007. A slower than in the prior year drop in the domestic consumption of LHO has resulted from a low reference level due to a material cut in illegal use of LHO for traction purposes in 2007 (fuel quality inspections, refunds of agricultural fuel). The falling tendency in the domestic LHO consumption has been continuing since 2005 when the material rise of crude oil prices caused the LHO to become less competitive as the heating fuel than alternative sources of heating energy. Also the weather conditions (high temperatures) in the I quarter of 2008 was a disadvantage.

According to estimates from the German retail market the gasoline consumption in the I half of 2008 amounted to 10,090 thousand tonnes and was lower by 4.2% than this consumption in the I half of 2007. The consumption of diesel oil on the other hand increased by 3.9% up to the level of 5,755 thousand tonnes.

On the basis of the figures coming from the Lithuanian market, the consumption of gasolines in the I half of 2008 decreased by 5.5% and achieved the level of 197 thousand tonnes. The opposite tendencies occurred in respect of diesel oil the consumption of which increased by 4.7% and equalled 531 thousand tonnes.

Fuel import

According to the estimates of ARE, in the I half of 2008 the total imports of fuels to Poland dropped, as compared to the I half of 2007, by 115 thousand tonnes, i.e. by 7%. The gasoline imports decreased by 13% and achieved the level of 316 thousand tonnes, which represents approx. 21% of the overall fuel imports. In the I half of 2008 the biggest gasoline imports were from Germany (approx. 54%), Slovakia (approx. 28%) and Hungary (approx. 14%).

It is estimated that in the I half of 2008 approx. 1,188 thousand tonnes of diesel oil were imported to Poland, i.e. 5% less than in the I half of 2007. The import of this type of fuel represented almost 79% of the total volume of fuel imports. The biggest imports of diesel oil came from Germany (44%), Finland (17%) and Slovakia (10%).

According to ARE, the overall imports of light heating oil in the I half of 2008 amounted to 4 thousand tonnes (while a year before it was 7 thousand tonnes). In the I half of 2008, LHO was imported from Germany (71%) and Lithuania (29%).

Amendments to Applicable Laws

The European Union power summit, which was held in March 2007, identified new goals and formulated new challenges for member states in the area of biofuels. It follows from the arrangements agreed that in 2020 the share of recoverable power should be as high as 20 power percent and for biofuels in transport 10 power percent. The fuel directive, which is being amended provides for new standards for fuels with the possibility to use biocomponents in

fuels up to 10 vol. (currently, up to 5 vol.). Thus, the fuel concerns will have to increase biocomponents in fuels introduced in the market. In accordance with the Act on Biocomponents and Liquid Biofuels of 25 August 2006 the fuel producers will be obliged to implement the National Target Ratio (NTR) in respect of the biocomponents share in fuels.

PKN ORLEN S.A., as a fuel producer, starting from 2008, has been obliged to use biocomponents in fuels to follow the National Target Ratios (NTR). Under the Council of Ministers Regulation on NTR for 2008-2013, PKN ORLEN S.A. is obliged to introduce in 2008 at least 3.45% of biofuels as translated to calorific value, which represents one of the highest levels in the whole European Union. The "Long-term Programme for Promoting Biofuels and Other Recoverable Fuels in 2008-2014" adopted by the Council of Ministers in July 2007 sets out the strategy and solutions to ensure the increase in production and the use of biocomponents and liquid biofuels in Poland. In accordance with the Council of Ministers Regulation of 15 June 2007 on NTR for 2008-2013, the proposed NTR level increases gradually in subsequent years so as to achieve the level of 5.75 percent in 2010 and, finally, of 7.10 percent in 2013. In order to meet the index of 5.75 percent in 2010, approx. 370 thousand tonnes of ethanol and 620 thousand tonnes of esters will be needed.

Both, the Czech Republic and Lithuania are the European Union member states; therefore they have also introduced their index targets and imposed the obligation on the fuel producers to meet these targets. Both foreign Groups are fully prepared to introduce biocomponents to their fuels. Relevant investments, mainly in the area of logistics, were implemented in these countries. Similarly as in PKN ORLEN S.A., the installations for methyl tert-butyl ether (MTBE) operating in Kralupy and Mazeikiu, were adjusted to manufacture ethyl tert-butyl ether (ETBE). In accordance with the EU directive no. 2003/30/EC, incorporated by the Czech legislature, a limit on biocomponents' share in the overall sales of fuels for engines will be at least 5.75% of the power content in 2010. The preparations of Ceska Rafinérska a.s. to meet the above limits relate to the implementation of two investment projects in Litvinov and Kralupy relating to:

- Dosing of MERO (rapeseed oil methyl ester) to diesel oil in the proportion of maximum 5 volume percent of the total volume of the diesel oil production;
- Adding of bioethanol to gasoline in the proportion of maximum 10 volume percent of the total gasoline volume.

Supplies of crude oil

Under the signed agreements, since the first quarter of 2007 PKN ORLEN S.A. has been supplying crude oil to all its refineries in Poland, the Czech Republic and Lithuania. In the I half of 2008 the crude oil supplies were undisturbed and performed as scheduled. Due to the stoppage of a pipeline supplying crude oil to Lithuania in July 2006 the crude oil to the Mazeikiu refinery has been delivered only by sea. This fact triggers another risk factor for the safety and stability of supplies, which is weather conditions, particularly in winter.

In July 2008 the company Lanturno appointed by the Russian party to coordinate supplies to the Czech direction has significantly reduced the crude oil supplies to the Czech refineries without quoting official reasons. According to the information provided to the company UNIPETROL a.s., the reduced supplies were caused by technical problems on the Russian part. The decreased crude oil supplies from Russia did not affect the production volume of the UNIPETROL Group and were replaced with the crude oil from domestic reserves and from increased supplies through TAL-IKL pipeline via port in Trieste. On the first days of August 2008 the crude oil supplies were restored to the previous level.

According to the information from the crude oil market it might happen that the volume of crude oil transported via "Druzhba" Pipeline to Poland and the Czech Republic will be reduced in the future (the planned implementation of BPS 2 pipeline project, improving the capacities of Russian sea export). Thus, in order to ensure the safety and stability of supplies to all its refineries and the diversification of sources, in 2007 PKN ORLEN S.A. implemented a project involving technological and economic analysis of the conditions for the diversification of the types of crude oil processed in the Płock refineries enabling an ongoing assessment of usefulness of various types of crude oil for the processing and production of such types of crude oil which are in a given period most attractive in terms of prices. This project, once implemented, will enable a prompt reaction to a fluctuating crude oil market conditions and, among others, to a counteraction to disturbances or limitations, if any, in respect of REBCO oil supplies.

Risk relating to the transfer of part of the assets and liabilities in relation to the acquisition of UNIPETROL a.s. shares

This matter was described in detail in Note 37 to the consolidated financial statements.

The main risk factors in selected entities from the ORLEN Group include:

Mazeikiu Group

- Supplies of crude oil to the Mazeikiu refineries are carried out by sea, due to the suspended transit via Butynga and exclusion of the "Druzhba" Pipeline delivering crude oil to Lithuania in July 2006. This fact triggers another risk factor for the safety and stability of supplies, which is weather conditions, particularly in winter. Thus, the main target to be achieved is to ensure safety and stability of supplies to all refineries and the diversification of sources enabling a prompt reaction to potential disturbances or limitations relating to REBCO crude oil supplies. To ensure the above, a project is being implemented in the ORLEN Group involving technological and economic analyses of the conditions for the diversification of crude oil types processed in the ORLEN Group refineries, its supplies and composing, if any. The analyses conducted for the Manufacturing Plant in Płock were implemented respectively to fit the needs and technological possibilities of UNIPETROL a.s. and AB Mazeikiu Nafta refineries. Moreover, PKN ORLEN S.A. plans to commence a construction of a product pipeline from the refinery in Mazeikiu to one of the reloading ports of the Baltic Sea. The investment will be launched once the Lithuanian parliament consents to AB Mazeikiu Nafta purchasing shares in the company Klajpedos Nafta, which is a manger of the Klaipeda terminal.

UNIPETROL a.s.

- At the end of 2007 one of the most significant companies on the Czech railway market, Ceske drahy a.s., split to form a cargo shipper, CD Cargo. The newly established CD Cargo's business focuses on approaching new clients and, thus, enhances competition on the railway transport market. This situation should not however have any adverse impact on the situation of the company UNIPETROL DOPRAVA s.r.o., which is still one of the two biggest carriers on the Czech market handling hazardous materials and is constantly working to strengthen its position. The main stress has been put on the necessity to purchase electric locomotives which should improve competitiveness of the company and enhance its cost efficiency.

Anwil S.A.

- The increased production capacities in Asia, specifically in China, triggered changes in the leading PVC producers sales tendencies. China, which is a key player on the PVC market is still planning the implementation of further investments with the aim to increase the production capacities. It is forecast that in 2010 the Chinese economy will be able to process app. 11.6 million tonnes of PVC, which will represent 22% of the overall worldwide demand. The producers' opportunities to market their goods in Asia are constantly deteriorating and therefore, they address their offers to the European markets which enhances competition and significantly affects the level of imports into Polish market, mainly from Germany and Hungary;
- Strong fluctuations of crude oil prices affect the level of prices of all basic raw materials used to produce polymers i.e. ethylene, propylene and benzene. High prices of ethylene adversely affect, however, profitability of the production and sale of PVC;
- The low level of PLN/EUR and PLN/USD exchange rates materially influences the export sales and also enhances competitiveness of import;
- The investments planned by Zakłady Azotowe Kędzierzyn S.A., including the construction of a nitrogen acid installation and the start-up of a new water treatment system may in the future strongly contribute to the competitive position of Anwil S.A. on the artificial fertilizers market;
- The prices of natural gas – a significant increase in prices of the raw material which forms the basis for the production of nitrogen fertilizers and are significant for the production of PVC may adversely affect the results of Anwil S.A. and adjust accordingly the margins obtained in this area. On 11 April 2008 Polskie Górnictwo Naftowe i Gazownictwo S.A. announced that the Power Regulatory Office approved an increase in the gas fuel tariffs and fee rates. The wholesale price of the gas fuel will rise over 15%;
- The forecast increasing need for natural gas on the part of the recipients from the European Union will exceed the production capacities of Gazprom. The shortage suffered by the gas market (approx. 100 billion cubic m) will result from a drop of the Gazprom current production capacities.

Rafineria Trzebinia S.A.

- The following proceedings are still pending relating to the contingent liabilities of Rafineria Trzebinia S.A. concerning excise tax and tax on goods and services:
  - Tax proceedings in respect of determination of excise tax liability for the period May – September 2004;
  - Control proceedings in respect of reliability of calculation and settlement of excise tax and tax on goods and services for 2002, 2003 and the period January – April 2004;

- Tax proceedings in respect of determination of tax on goods and services amount for the period January – August 2005;
- Tax proceedings in respect of determination of excise tax liability arising from excise tax for the period November - December 2004;
- Decisions in respect of excise tax liabilities for the period January – February 2007.

The aforementioned contingent liabilities of Rafineria Trzebinia S.A. were described in more detail in Note 37 of the consolidated financial statements.

- Limitation of the production and sale of parafines was due to the shortage of raw material on the market available at acceptable purchase price.

ORLEN Oil Sp. z o.o.

- Still growing competition on the domestic lubricants market;
- Increase in prices at the base oil market, specifically at the end of the I half of 2008;
- Appreciation of Polish zloty, especially against American dollar has had an adverse impact on profitability of export sales and the refinery margin value.

ORLEN Asfalt Sp. z o.o.

- The oversupply on the domestic asphalt market that occurred in 2008 triggered a strong price competition on this market. Additionally, an increase in the demand to the level of approx. 1.7 – 2.0 million tonnes expected to start in 2009, due to the necessity to adjust Polish regulations on road investments to the European standards in respect of ecological requirements may be postponed by another 1.5 year. The scope of road investments planned for the years 2008-2012 has not changed however. The expected cumulated investments, specifically in relation to express ways and highways will trigger in the years 2010-2012 a rapid growth of demand for modified asphalts;
- The price competition getting stronger on the road asphalt market in Lithuania was due to an aggressive pricing policy implemented by Lotos on this market.

ORLEN Deutschland AG

- Strong competition in 2008 has significantly affected the process of shaping margins on the German fuel market and, therefore, the financial result of ORLEN Deutschland AG. This company will be developing through the implementation of a consistent restructuring process and the expansion of a fuel station network as well as the implementation of the fuel station image improvement programme “Facelifting”;
- The financial standing of the company ORLEN Deutschland AG has been significantly affected by an economic situation in Germany, fluctuation of crude oil and fuel prices and stagnation on the volume market in Germany.

ORLEN Gaz Sp. z o.o.

- The Ministry of Finance presenting a draft amendment to the Excise Act providing for an increase in the excise tax rate from PLN 695 to PLN 1100 from 1 January 2009;
- The Act of 16 February 2007 on the Reserves of Crude Oil, Oil Products and Natural Gas and the Way of Conduct in the Situations of Threatened Fuel Safety of the State and Disturbances on the Crude Oil Market (Official Journal of 23 March 2007) which increases the costs of business operation of the LPG sector due to the mandatory fuel reserves.

For further information of risk factors and threats material for the business operations of the PKN ORLEN Group see Note 37 to the consolidated financial statements for the first half of 2008.

1.5 Production

In the I half of 2008 the crude oil processing volume in the PKN ORLEN Group companies amounted to 13,843 thousand tonnes and was by 17.5% higher as compared to the prior year. This positive dynamics was a result of a much higher, by 1.6 million tonnes, processing volume in the Mazeikiu Group.

In the I half of 2008 the volume of crude oil processed in PKN ORLEN S.A. amounted to 7,027 thousand tonnes and was by 6.1% higher as compared to the I half of 2007. The yield from white products amounted to 79.1% and was higher by 4.2 pp as compared to the I half of 2007. In turn, the yield from fuels in the I half of 2008 achieved the level of 64.6% and was higher by 3.9% as compared to the I half of 2007. The more advantageous yields in PKN ORLEN S.A. were obtained due to the better than in the first half of 2007 availability of installations and increased share in the light crude oils processing. Moreover, these factors were also affected by the following:

- A start-up in February 2008, of the Hydrorefining Installation of Diesel Oil from the Gudron Hydrodesulphurisation of a processing capacity of 55 t/h of hydrorafinate, which made possible to use this fraction to produce ready-made diesel oil or light heating oil;
- Realisation of a planned repair standstill of the Reforming VI and Diesel Oil Hydrodesulphurisation VI ("HON VI") installations with the largest scope of repair works since the start-up of the installations in 2000 in the period from 1 to 21 March 2008.

In the I half of 2008 the Olefin Installation II was operating without any major disturbances. From 24 June to 29 July 2008 the Olefin Installation II and all technologically related petrochemical installations underwent the repair standstill.

In December 2007 a reconstruction of the Vacuum Distillation Unit (VDU) was completed in the Mazeikiu refinery which had been destroyed in the fire in October 2006. In February 2007 the operation of Bitumic Distillation Unit (BDU) was launched, which partly replaced the installation destroyed by fire and, therefore, made it possible to limit the damage. The reconstruction of VDU, following the removal of the destroyed unit was started in February 2007. The launch of this unit operation took place on 20 January 2008 after the reconstructed VDU had been connected to other refinery installations. Following the start-up of the reconstructed VDU the processing capacities of the refinery achieved the level from before the fire in October 2006, i.e. of more than 10 million tonnes. In autumn 2007 also a significant general repair was carried out together with the modernisation works. Consequently, also the overhauls and repairs of more than 450 pipelines, 64 units, 16 reactors were carried out.

In order to make the Mazeikiu refinery comply with ecological and quality requirements laid down by the European Union and to save significantly on the consumption of energy an investment programme is being implemented of the total value of USD 1.6 billion. The programme is to be completed in 2012. The programme's basic principles involve the construction of new installations, among others a hydrocracking installation, a visbreaking vacuum distillation installation as well as a propylene emission and an exhaust desulphurization installation at the Heat and Power Generating Plant.

1.6 Indebtedness structure and financial resources management

As at 30 June 2008 the total value of long- and short-term loans, borrowings and issued debt securities in the ORLEN Group amounted to PLN 8,883,666 thousand and was lower by PLN 1,438,278 thousand as compared to the end of 2007. In PKN ORLEN S.A., as at 30 June 2008, a drop of financial indebtedness by 131,540 thousand was noted as compared to the situation as at 31 December 2007.

(in PLN thousand)	Indebtedness		Cash and Cash Equivalents		Net Debt	
	I half of 2008	2007	I half of 2008	2007	I half of 2008	2007
Bank loans	7,644,790	8,809,266				
Borrowings	4,198	4,285				
Debt securities	1,234,678	1,508,393				
According to their maturity:						
Long-term	8,011,120	8,602,721				
Short-term	872,546	1,719,223	1,669,839	1,666,189		
Total	**8,883,666**	**10,321, 944**	**1,669,839**	**1,666,189**	**7,213,827**	**8,655,755**

As at 30 June 2008, the net financial indebtedness in the ORLEN Group dropped as compared to the end of 2007 by PLN 1,441,928 thousand, i.e. down to PLN 7.213.827 thousand. The drop in the net indebtedness affected a net financial debt to equity ratio (loans, borrowings and debt securities in average less cash less short-term securities to equity in average) which has dropped from 37.3% as at 31 December 2007 to 34.4% as at 30 June 2008.

The high borrowing power of the ORLEN Group which provides it with a possibility to draw additional external funds in an inexpensive and relatively quick way, has a positive impact on its financial security. The ORLEN Group takes loans and borrowings both in foreign currencies and in Polish zloty, mainly subject to a floating interest rate. Sience February 2001 a system of fund concentration has been operating within the ORLEN Group. As at 31 December 2007 PKN ORLEN S.A. used a PLN cash-pooling system in two banks and a foreign currency cash-pooling system in one

bank. The work is carried out on an on-going basis to implement to these systems all the ORLEN Group companies in which PKN ORLEN S.A. is a controlling entity.

In its day-to-day operations, PKN ORLEN S.A. uses comprehensive services of highly credible banks, with a considerable equity and strong market position, which have gained extensive expertise in cash management on the Polish and foreign markets. This approach has made it possible for PKN ORLEN S.A. to reduce banking costs, and improve the structure of banking services. Further activities aiming at further integration and improvement of the conditions of banking services for all the ORLEN Group companies have been undertaken.

Available funds, secured sources of financing and significant borrowing power of PKN ORLEN S.A. fully secure the nearest financial needs relating to capital and property investments. The most important loans in the I half of 2008 in the ORLEN Group include mainly the loans taken up by PKN ORLEN S.A., including:

- long-term multicurrency loan facility of EUR 1 billion granted by the consortium of Polish and international banks in December 2005. The loan period is 5 years from the signing of a loan facility agreement with two extension options, each of one year (in December 2006 and 2007, respectively, PKN ORLEN S.A. took advantage of the extension option and moved the maturity date to December 2012). The loan may be used in four currencies, i.e. EUR, USD, PLN and CZK. Funds from the loan may be allocated to finance current operations of PKN ORLEN S.A.;

- revolving loan facility of EUR 800 million granted by the consortium of eight banks in November 2006. The loan period is 5 years with two extension options, each of one year (in November 2007, PKN ORLEN S.A. took advantage of the first extension option and moved the maturity date to November 2012);

- long-term loan facility in the total amount of EUR 510 million granted by the European Investment Bank (EIB) in 2007. The amount of EUR 210 million was granted by EIB to the investment involving the expansion of the fuel stations chain and environmental protection. Available currencies: EUR, USD, GBP and PLN; repayment period: 9 years with a 3-year grace period. The amount of EUR 300 million was granted by EIB to finance part of the construction costs of the installation to produce paraxylene and terephthalic acid. Available currencies: EUR, USD, GBP and PLN; repayment period: 12 years with a 4-year grace period or a one-off repayment during 8 years from the drawdown date;

- syndicated loan facility of EUR 300 million granted by a consortium of six banks in January 2008. The loan period is 3 years as of the signing of the loan facility agreement, with two extension options, each of one year. The loan may be used in three currencies, i.e. in EUR, USD and PLN;

- two loans for a total amount of EUR 115 million granted by Nordea Bank Polska S.A. in April 2008: the overdraft facility agreement up to EUR 15 million, and the revolving loan facility agreement up to EUR 100 million. The loan period relating to each loan is 3 years. The loans may be used in three currencies, i.e. EUR, PLN and USD.

For further information on the debt structure and loans and debt securities maturity dates see Note 19 of the consolidated financial statements for the I half of 2008.

1.6.1 Contingent liabilities of the ORLEN Group

The total value of contingent liabilities, as at the end of the I half of 2008, increased as compared to the end of 2007 by PLN 39,612 thousand to reach the level of PLN 1,949,832 thousand. The total value of granted guarantees and sureties, as at 30 June 2008 decreased by PLN 1.572 thousand down to PLN 112,620 thousand. In the I half of 2008 the guarantees related to contractual obligations of the ORLEN Group were raised by PLN 11,347 thousand, but the bid and other guarantee deposits dropped in general by PLN 12,935 thousand.

The remaining contingent liabilities as at the end of the I half of 2008 reached the level of PLN 1,837,212 thousand and increased by PLN 41,184 thousand, mainly due to the excise tax deposits to secure excise tax levied on harmonised products stored in warehouses during the suspension procedure and the letter of credit by PLN 92,729 thousand. The contingent liabilities rising out of legal cases decreased, in turn, by PLN 42,684 thousand.

For further information on the issued guarantees and other contingent liabilities see Note 37 of the consolidated financial statements.

1.6.2 Issue of bonds

PKN ORLEN S.A. is a party to Bond Issuance Programme with a debt limit up to PLN 2,000,000 thousand.

Under this agreement PKN ORLEN S.A. issues unsecured bearer bonds. The offer is addressed to institutional investors and not to the public. The banks chose a group of entities from amongst the investors they know to which they address a bond purchase proposal. The proposal may not be addressed to more than 99 entities. Under the programme, the issue of both non-interest bearing (zero-coupon) and interest bearing (coupon) bonds is admissible. The non-interest bearing bonds are issued with a discount for a period from 7 days to 1 year. On interest bearing bonds interest is accrued at a fixed or variable interest rate; these bonds are issued for a period of 1 to 7 years. This is a multi-currency programme, which means that the issues may be in four currencies: PLN, EUR, USD and CZK. Therefore the bonds may be addressed to foreign companies belonging to the ORLEN Group.

Under the program, PKN ORLEN S.A. is allowed to divide the issue into portions and additionally determine dates on which they will be released. It gives an opportunity to manage in a complex way the liquidity of the ORLEN Group. Funds obtained under the issue enable to finance working capital at attractive cost, diversify the sources of PKN ORLEN S.A.'s financing.

In the first half of 2008, under the issuance programme, PKN ORLEN S.A. issued only short-term bonds. In June 2008 the first issue of bonds in EUR took place addressed to PKN ORLEN S.A.'s subsidiary, ORLEN Deutschland AG.

The overall value of bonds issued by PKN ORLEN S.A., as at 30 June 2008, amounted to PLN 1,204 million. The investors are the ORLEN Group members: Anwil S.A., IKS Solino S.A., ORLEN Księgowość Sp. z o.o. and ORLEN Deutschland AG. The yield on bonds was determined in accordance with market conditions.

1.6.3 Financial instruments

The financial instruments are described in detail in Note 29 of the consolidated financial statements.

1.7 Assessment of the feasibility of investment implementation

On 16 November 2007 the Supervisory Board of PKN ORLEN S.A. approved the document "Strategy of the ORLEN Group for the years 2007-2012" which sets a target for the capital expenditures broken down by the ORLEN Group business segments:
- refining segment: PLN 8.4 billion,
- retail segment: PLN 3.2 billion,
- petrochemical segment: PLN 5.8 billion,
- chemical segment: PLN 1.7 billion,
- other operations: PLN 2.2 billion.

One of the elements of the ORLEN Group's strategy involves the internal strengthening of the company through, among others, improving the use of production capacities already installed and the modernisation of assets.

The key investments significant for the development of the ORLEN Group include:
- Development and improvement of the refinery complex in AB Mazeikiu Nafta;
- Paraxylene ("PX") and Terephthalic Acid ("PTA") Complex;
- Diesel Oil Hydrodesulphurisation Complex VII ("HON VII") with Hydrogen Installation;
- Ethylobenzene Installation;
- Modernisation and intensification of Butadiene Installation;
- Construction of the Propylene Production Plant in AB Mazeikiu Nafta;
- Modernisation and intensification of Alkylation Installation;
- Development of vinyl chloride and polyvinyl chloride production plant in Spolana.

and a number of minor tasks relating to the adjustment of the plant infrastructure to new legal and environmental requirements.

The financial standing of the ORLEN Group is maintained at a safe level which is reflected, among others, by a financial leverage index, which as at 30 June 2008 amounted to 34.4%. Taking into account the performance of the projected investments in the second half of 2008 and the current indebtedness of PKN ORLEN S.A. the expected financial leverage index as at the end of 2008 should not be more than 38.2% which is in line with the strategy objectives. Also the level of the net financial debt/EBITDA index which as at the end of the I half of 2008 amounted to 2.3, in 2008 is estimated to achieve the level of 2.2. These levels of such indices are commonly deemed to be safe and will not hinder the process of gaining new sources of investment funding.

1.8 Publication of forecast financial results

The ORLEN Group did not publish forecast financial results relating to the I half of 2008.

II. MAIN ACHIEVEMENTS IN RESEARCH AND TECHNOLOGICAL DEVELOPMENT WITHIN THE ORLEN GROUP

In the I half of 2008 PKN ORLEN S.A. carried out a number of studies relating to the development and upgrading of new production technologies, improvement of the quality of products manufactured, and limitation of the environmental impact of production activities. In aggregate, in the first half of 2008, 35 new contracts were executed and 17 were amended amounting in total to PLN 6,263 thousand.

PKN ORLEN S.A. does not carry out any R&D activities by its own; they are outsourced to independent institutions, such as research centres and institutes, universities, as well as business entities carrying out R&D activity.

The most important studies within the scope of technical R&D in the area of core production and environmental protection in PKN ORLEN S.A. in the I half of 2008 include as follows:

- "Technology of rally engine gasolines produced out of components manufactured at the PKN ORLEN S.A Production Plant in Płock" a study drawn up by the Oil and Gas Institute in Cracow. The results of the research work showed the possibility to prepare, on the basis of available components, a specific quantity of gasoline for rally engines compliant with FIA requirements. The results of this work once used and, possibly, implemented can enable PKN ORLEN S.A. to introduce a new type of ORLEN brand gasoline to a particularly requiring and prestige market of rally organizers and participants;

- "Measuring the emission of substances which were not previously identified and which are listed in Regulation No. 166/2006 of the European Parliament and of the European Council concerning the establishment of the European Pollutant Release and Transfer Register characteristic for the installation of the PKN ORLEN S.A. Production Plant" a study drawn by EMIPRO Sp. z o.o. in Cracow. As part of the works the issue of pollutants was measured on the selected emitters of the PKN ORLEN S.A. Production Plant and a chemical analysis of the burnt fuel was carried out. The outcome of the measurements will be used for the Pollutant Release & Transfer Register records which PKN ORLEN S.A. must maintain under Regulation No. 166/2006 of the European Parliament and of the European Council of 18 January 2006 and as part of ecological fees.

Significant ORLEN Group members carried out the following works and activities in the area of technical R&D:

UNIPETROL Group

- The implementation of a new technology in respect of using water in technological processes will permit to save water in the second half of 2008 in the quantity of up to 250 thousand cubic m. The implementation will come to full effect in 2009;
- The development of polypropylene production technology was directed in such a way so as to obtain the products meeting high quality standards and thus, a higher margin will be generated on copolymers:
  - A new quality type of polypropylene was developed (copolymer RCP FB 908). It is mainly applied in the area of industrial foil production;
  - A new quality type of polypropylene was specified of a high melting index elaborated mainly for the automotive industry and for the creation of composite chemical compounds. A new quality type of the product is characterised with variable production costs being lower as compared to the production costs of similar product types showing similar physical characteristics;
  - Polypropylene (HMS) was developed, which can be used with chemical foaming agents by the recipients to manufacture light-weight plates, tables and profiles;
- Studies over the development of petrochemical segment products (fractions C9, C10, DCPD);
- Technological support for Pyrotol installation after the start-up of the benzene installation.

Anwil S.A.

- Implementation of the project "Reduction of the emission of nitrous oxide from the nitric acid installation as part of the Joint Implementation (JI) programme". This project is being implemented in accordance with a mechanism indicated in the Kyoto Protocol enabling a reduction of costs of the undertaking reducing the emission of greenhouse gases. This mechanism provides for the "Emission Reduction Units" in exchange for providing funds to the projects reducing the emissions of greenhouse gases. The way of implementing the project was approved by the Ministry of Environment in the form of the Letter of Approval of 28 January 2008.

  In May 2008 the project was implemented on one of the two nitric acid lines operating in Anwil S.A. The implemented project actually resulted in the reduction of the nitrous oxide emissions. On the other line the project was implemented in July 2008.

In July 2008, Anwil S.A. signed a contract for the assembly and start-up of a complete installation of a cryogenic air separation installation (oxygen generating plant). The new oxygen generating plant will be characterised with modern technological solutions and, therefore, it will be less energy-consuming. A new feature shown by the new installation as compared to the existing installation will be the possibility to produce liquid argon, which is very rare on the technical gases market. Furthermore, the installation will assure the provision of nitrogen to the PTA installation which is now under construction. The investment completion is planned for September 2010.

ORLEN Oil Sp. z o.o.

- The implementation of Base Oils Interchange Programme ("BOI") with the use of ORLEN Oil base oils, which consists in replacing the base oils used in engine oils with alternative base oils of similar quality. Having developed the technology of high quality engine oils involving the base oils ORLEN Oil Sp z o.o. will free itself from the necessity to import base oils. The BOI Programme is expected to be completed in November 2008.

  In the I half of 2008 the first phase of the BOI programme implementation was completed which involved mineral engine oils designed for heavy Diesel engines. The new solutions make it possible to fully use own raw material, i.e. base oils ORLEN Oil Base 150 and ORLEN Oil Base 400. Moreover, a process was launched to obtain certificates for new technologies of diesel oils such as HDDO from equipment manufacturers, e.g.: Mercedes-Benz, MAN, Volvo, Renault, etc.

  In the I half of 2008 the second phase of the BOI programme implementation work was started which relates to the development of technology for semisyntethic oil for heavy Diesel engines: Platinum Ultor Semisynthetic 10W/40, a new oil from the Platinum products assortment using the base oils ORLEN Oil Base and Mogul HC 32/130 and attested by the equipment manufacturers, e.g. Mercedes-Benz, MAN, Renault.

- The work on developing alternative technologies in the core product groups, i.e.: high quality engine oils for heavy Diesel engines HDDO, low quality engine oils, PCMO, low quality engine oils HDDO, oils for two-stroke engines, car gear oils, hydraulic oils, and industrial gear oils;

- Extension of the assortment of oils used in industry to include:
  - oil emulsifiers for metal processing,
  - oil for explosive material production "Eksploil",
  - oil for hardening with better cooling speed Hartex 70,
  - hydraulic oil Dracon HV 46 Premium Oil,
  - hydraulic oil HLPD 22,
  - hydraulic oil HVLP 32, 46,
  - oil non-emulsifiers for metal processing Hydrocut 32 and Hydrocut Premium EP 32,
  - hutplex EP-2 – complex, calcium, high-temperature lubricant for metallurgy.

  Moreover, a technology for MES type plasticizer production was developed with the use of a transitional method based on furfurol extracts.

- Operational research carried out at Zetor Polska Sp. z o.o. in respect of oils produced by ORLEN Oil in order to enrol the company's products on reference lists of lubricating oils recommended by Zetor Polska Sp. z o.o. to be used in the cars they manufacture;

- Completion of operational research in respect of co-operation of engine oils produced by ORLEN Oil with biodiesel.

Rafineria Nafty Jedlicze S.A.

- The work on the design of the initial tower for the Piping and Tower Distillation Unit, including analysis of crude oil from PGNiG Sanok in order to define parameters of the installation operation;

- Analytical testing of raw materials from the perspective of their processing on the Solvent Installation;

- Quality analysis of waste oils at the angle of optimisation of technological processes on the Used Oil Distillation Installation and the Used Oil Hydrorefining Installation, assuming a poorer quality of used oils on the Polish market;

- Implementation, as of January 2008, of new base oil lines: series N-70-200 of a broad viscosity range;

- Analysis of solvents sold on the Polish retail market at the angle of packing own products in unit packaging.

III. DESCRIPTION OF FACTORS CRUCIAL FOR THE DEVELOPMENT OF THE CAPITAL GROUP

In accordance with the strategy applicable at the ORLEN Group, the operations of PKN ORLEN S.A. are directed to the value creation through:

- implementation of the Value Creation programme at AB Mazeikiu Nafta and strengthening of the integration with UNIPETROL a.s.;
- increase in crude oil processing capacities through the better use of own resources (to achieve, by 2012, effective processing capacities of the whole ORLEN Group at the level of 33 million tonnes per year);
- increase in the wholesale market share;
- continued implementation of two brand strategy on the Polish and Czech markets and significant improvement of retail sale efficiency through tailoring an offer to meet the needs of local markets;
- optimisation of assets through further divestments of the non-core companies.

As part of the Value Creation Programme ("VCP") and a parallel "Mazeikiu Integration" Programme the Directors of PKN ORLEN S.A. with respective Directors of AB Mazeikiu Nafta are constantly implementing integration initiatives for a period of subsequent 5 years. In total there were created more than 90 integration initiatives and 137 VCP initiatives of which the majority will be implemented by the end of 2008. As part of both projects, by the end of the I half of 2008:

- the Supply Chain Management programme was implemented under which the ORLEN Group companies can work out a uniform planning and optimisation process;
- the complex "Strategy for Baltic" programme was prepared including a project to improve logistics connections between Poland, Lithuania and a project for optimisation a logistics infrastructure at AB Mazeikiu Nafta;
- the company Mazeikiu Nafta Trading House was reorganised through AB Mazeikiu Nafta taking over the majority of this company's functions in Lithuania and PKN ORLEN S.A. – in Poland, which resulted in an improved co-ordination of the production, logistics and sales with a simultaneous decrease in the operating expenses;
- the procedures and policies were implemented which mirror best practices applicable at PKN ORLEN S.A. in order to make the operations of the companies uniform and flow of tasks to be realised in the managed segments easier;
- a new statute was introduced at AB Mazeikiu Nafta, which strengthened the position of the Management and Supervisory Boards.

Moreover, at AB Mazeikiu Nafta a new strategy was developed for the IT area; the new systems were implemented: ORACLE HRMS payroll system and a new system of management reporting as well as a cash management policy. Another element of the integration process will be the implementation of the employment restructuring programme. Until now two companies were split out – Medical Centre Mazeikiu Nafta and "Paslaugos Tau", which provides services in the area of cleaning-up and greenery keeping. At present at AB Mazeikiu Nafta, the movement maintenance area is undergoing the restructuring.

In the first half of the year the integration process of business activities at UNIPETROL a.s. was completed. At the next stage the company will focus on improving efficiency of the core business operations and on developing co-operation with PKN ORLEN S.A. A further increase in efficiency will be possible to be achieved due to the optimisation of assets and completion of Paramo a.s. integration.

The strategy adopted at the ORLEN Group assumes a material development of the production capacity of refineries owned by the ORLEN Group to achieve in 2012 the level of 33 million tonnes per year. The increase in the crude oil processing volume will be possible due to a further expansion and upgrading of refinery complexes in Płock and at AB Mazeikiu Nafta. Already today the refinery in Płock is classified as one of the four best refineries in Europe (in accordance with the "Solomon" report). The increased processing capacity will be correlated to the increase of the white product yield index and the increased production capacity of diesel oil due to new installations (HON VII).

In accordance with the adopted Development Program for the Production Plant in Płock, by 2012 a number of investments will be implemented which are crucial for the development of the ORLEN Group including without limitation Paraxylene (PX) and Terephthalic Acid (PTA) Complex and Diesel Oil Hydrodesulphurisation Complex VII ("HON VII") with Hydrogen Installation. Additionally, a number of minor tasks are planned to adjust the plant infrastructure to the new legal and ecological requirements. The investments which are implemented and planned for implementation are aimed at the optimal use of the existing resources of PKN ORLEN S.A., with a concurrent securing of the necessary technical, power and logistics infrastructure.

In turn, the investment programme at the refinery in Mazeikiu will be implemented, among others, through the increase in a refinery conversion index at the Mazeikiu Group and the investments ensuring compliance of the Mazeikiu Group refineries with the EU regulations.

In the retail segment, the strategy assumes strengthening of the current market positions and further expansion on Baltic markets. At the first stage, by the end of 2008, PKN ORLEN S.A. will focus on take-overs of selected facilities and on the pre-construction activities. At the second stage, planned for the years 2009-2010, the taking-over process will be continued and the newly constructed fuel stations will be started up. The ORLEN Group network in the Baltic States will be also supplemented with franchises. Unlike in Poland and the Czech Republic, specific features of Lithuanian and Latvian markets and consumers' expectations surveyed in market opinion polls had made the Group to decide on introducing one single premium brand for fuel stations on these markets under the logo of ORLEN joined with the name of the respective country, i.e. ORLEN Lietuva or ORLEN Latvija. The designation of the brand together with the country name enables clients to identify with the ORLEN brand as the one addressed to their particular market and, simultaneously, to take advantage of the Concern's international experience.

At the company Benzina a.s., the fuel station modernisation process will be continued. The German stations rebranding process started in 2006 is being consistently implemented to obtain better STAR brand positioning. For 2008 the rebranding of 35 stations from ORLEN to STAR was planned. This task was competed in full in the first half of 2008. Therefore, by the end of 2008 it is planned to rebrand further 8 fuel stations. Considering the new mission and vision of the company, which assume the first position amongst the most attractive, in terms of price, chains in the northern Germany, ORLEN Deutschland developed a new offer for its clients, i.e. Customer Value Proposition ("CVP"). At the same time the groups of clients were defined which are the most important for the brand, i.e. consumers with average income and new generation representatives. All the marketing and shop campaigns were oriented to achieve those two main objectives: i.e. CVP and the needs of these two specific groups of clients. Concurrently, the "Facelifting" programme was implemented in relation to the improvement of the station image. The programme should assure a better look of the stations and, therefore, improve the STAR brand positioning on the German market.

Additionally, it is planned to develop a non-fuel offer and a fleet offer relating to the introduction of a card accepted in the whole ORLEN Group.

As part of the actions aimed at improving the wholesale efficiency, a process of consolidating fuel companies was launched (Regional Market Operators – "RMO"). This process is tailored to create one company out of five existing entities. It has already triggered far reaching restructuring processes which mainly involve the cessation of retail sales through selling or leasing fuel stations held and focussing on the core business, i.e. wholesale.

The operations of PKN ORLEN S.A. in the area of upstream in the I half of 2008 were mainly focussed on the consistent implementation of upstream strategy principles taking into account external and internal factors which condition and influence the intended effects. The main activities carried out in the I half of 2008 and assumed for realisation in subsequent years include:

- Implementation of a development strategy in the area of hydrocarbon upstream by PKN ORLEN S.A. through regional concentration. The option of regional concentration enables PKN ORLEN S.A. to limit the risks relating to the upstream activities (mainly geopolitical risk) and to build competence in a stable environment;
- Implementation of upstream segment development through creating business on the basis of both organic and non-organic growth. This means that PKN ORLEN S.A. has focussed on a step-by-step building of a balanced portfolio of research and manufacturing assets, which meet certain specific criteria (edge conditions) relating to location, risk, level of employed capital, term, etc.;
- Analysis of projects enabling PKN ORLEN S.A. to participate in the entities existing on the market and holding appropriate portfolios of assets, including production assets;
- Creation of a material and organisational base for a team of experts;
- Obtaining and training personnel for the Upstream Office;
- Studies and research analyses in respect of projects;
- Comprehensive analysis of selected projects aimed at the purchase of assets;
- Obtaining another upstream project for PKN ORLEN S.A. (on the Baltic Sea shelf).

The development strategy of PKN ORLEN S.A. in the area of hydrocarbon upstream assumes a common implementation of projects with co-operation of companies operating in the area of upstream. The benefits for PKN ORLEN S.A. resulting from the co-operation with experienced partners include among others:

- Participation in investment projects prepared and implemented by the partner;
- Direct access to the information on potential upstream projects in the area of the partner's operation;
- Optimisation of the upstream operations risk due to a mutual support in selection, assessment and implementation of projects;
- Access to the partner's know-how in the upstream area;
- Access to qualified and experienced personnel.

The opportunity to work together with external partners provides PKN ORLEN S.A. with a balanced growth and optimised risk.

At present the strategy for the years 2009-2013 is being updated. Its final form will be announced at the turn of October and November 2008.

IV. STRUCTURE OF THE ORLEN GROUP AND ITS CHANGES DURING THE FIRST HALF OF 2008

As at the end of the I half of 2008, PKN ORLEN S.A. held directly or indirectly shares in the following companies:
- 99 subsidiaries,
- 6 jointly controlled companies,
- 15 associate companies.

As compared to the end of the I half of 2007 the number of subsidiaries, jointly controlled entities, as well as associate companies of the ORLEN Group has decreased from 136 by 120.

The ORLEN Group (directly related and consolidated companies in the I half of 2008) are divided into two main groups:

4.1 Core business companies

4.1.1 Segment companies (by sales volumes)

- AB Mazeikiu Nafta seated in Juodeikiai in Lithuania together with its own Capital Group,
- UNIPETROL a.s. seated in Prague together with its own Capital Group,
- Anwil S.A. seated in Włocławek together with its own Capital Group,
- Basell Orlen Polyolefins Sp. z o.o. seated in Płock together with its own Capital Group,
- Rafineria Trzebinia S.A. seated in Trzebinia together with its own Capital Group,
- ORLEN Oil Sp. z o.o. seated in Cracow together with its own Capital Group,
- ORLEN Asfalt Sp. z o.o. seated in Płock,
- Rafineria Nafty Jedlicze S.A. seated in Jedlicze together with its own Capital Group,
- Inowrocławskie Kopalnie Soli „Solino" S.A. seated in Inowrocław,
- ORLEN Upstream Sp. z o.o. seated in Warsaw,
- Etylobenzen Płock Sp. z o.o. in liquidation seated in Płock.

4.1.2 Fuel and gas selling companies (by sales volumes)

- ORLEN Deutschland AG seated in Elmshorn,
- ORLEN PetroCentrum Sp. z o.o. seated in Płock,
- ORLEN PetroTank Sp. z o.o. seated in Widełka next to Kolbuszowa,
- Petrolot Sp. z o.o. seated in Warsaw,
- ORLEN Gaz Sp. z o.o. seated in Płock together with its own Capital Group,
- ORLEN PetroProfit Sp. z o.o. seated in Niemce next to Lublin together with its own Capital Group,
- ORLEN Morena Sp. z o.o. seated in Gdańsk,
- ORLEN PetroZachód Sp. z o.o. seated in Poznań,
- Ship-Service S.A. seated in Warsaw together with its own Capital Group.

4.2 Supplementary business companies

4.2.1 Shipping companies (by sales volumes)

- ORLEN KolTrans Sp. z o.o. seated in Płock,
- ORLEN Transport S.A. seated in Płock.

4.2.2 Maintenance companies (by sales volumes)

- ORLEN Automatyka Sp. z o.o. seated in Płock,
- ORLEN Wir Sp. z o.o. seated in Płock.

4.2.3 Other companies (by sales volumes)

- ORLEN Projekt S.A. seated in Płock,
- ORLEN Laboratorium Sp. z o.o. seated in Płock,
- ORLEN Budonaft Sp. z o.o. seated in Kraków,
- ORLEN Księgowość Sp. z o.o. seated in Płock,
- Petrotel Sp. z o.o. seated in Płock,
- ORLEN Administracja Sp. z o.o. seated in Płock,
- ORLEN Medica Sp. z o.o. seated in Płock together with its own Capital Group,
- ORLEN Eko Sp. z o.o. seated in Płock,

- ORLEN Prewencja Sp. z o.o. seated in Płock,
- ORLEN Insurance Ltd seated in Selima on Malta,
- Płocki Park Przemysłowo-Technologiczny S.A. seated in Płock,
- ORLEN Finance seated in Stockholm,
- ORLEN Powiernik Sp. z o.o. seated in Płock,
- ORLEN International Exploration & Production Company BV seated in Amsterdam.
- ORLEN Holding Malta Limited seated in Selima on Malta.

4.3 Ownership changes in the ORLEN Group in the I half of 2008

The structure of the ORLEN Group as regards the consolidated companies and material shares and stock held in related and other entities is presented in Notes 2, 9, 10 of the consolidated financial statements for the first half of 2008.

The main changes in organisational and capital relations in the ORLEN Group that occurred in the I half of 2008 and by the moment of preparation of this report, include:

- Registration on 2 January 2008 by the District Court for the capital city of Warsaw of the company ORLEN Transport S. A. seated in Płock. PKN ORLEN S.A. took up 65,460 thousand shares in ORLEN Transport S.A. of a nominal value of PLN 1 each, representing approx. 97.61% of the share capital and conferring 97.61% votes at the General Meeting of ORLEN Transport S.A. The company ORLEN Transport S.A. was established as a result of a merger of six subsidiaries of PKN ORLEN S.A.: ORLEN Transport Płock Sp. z o.o., ORLEN Transport Kędzierzyn-Koźle Sp. z o.o., ORLEN Transport Nowa Sól Sp. z o.o., ORLEN Transport Szczecin Sp. z o.o., ORLEN Transport Słupsk Sp. z o.o., ORLEN Transport Olsztyn Sp. z o.o. The main business activity of ORLEN Transport S.A. includes road transport with specialized vehicles, including without limitation fuel transport. The investment of PKN ORLEN S.A. in the shares of ORLEN Transport S.A. is of a long-term nature;

- Transfer, on 18 January 2008, of the ownership of 47 thousand shares in the company AGROBOHEMIE a.s. and 26,448 thousand shares of the nominal value of CZK 40 and 1,530 thousand shares of the nominal value of CZK 400 in the company Synthesia a.s., from the company UNIPETROL a.s. to the company DEZA a.s. The shares were transferred on the basis of two agreements executed on 31 October 2007 between UNIPETROL a.s., as the seller and the company DEZA a.s., as the buyer. On the basis of the agreements UNIPETROL a.s. sold to DEZA a.s.:
  - 47 thousand ordinary shares in AGROBOHEMIE a.s., representing 50% of AGROBOHEMIE a.s.'s share capital and the same number of votes at the General Meeting of AGROBOHEMIE a.s. The nominal value of one share of AGROBOHEMIE a.s. amounted to CZK 10.8 thousand (i.e. approx. PLN 1,494 at the average CZK/PLN exchange rates of the National Bank of Poland as at 18 January 2008);
  - 26.448 thousand ordinary bearer shares in Synthesia a.s., representing 24.58% of Synthesia a.s.'s share capital and the same number of votes at its General Meeting. The nominal value of one share of Synthesia a.s. amounted to CZK 40 (i.e. approx. PLN 5.5 at the average CZK/PLN exchange rates of the National Bank of Poland as at 18 January 2008);
  - 1.530 thousand ordinary bearer shares in Synthesia a.s., representing 14.21% of Synthesia a.s.'s share capital and the same number of votes at its General Meeting. The nominal value of one share of Synthesia a.s. amounted to CZK 400 (i.e. approx. PLN 55 at the average CZK/PLN exchange rates of the National Bank of Poland as at 18 January 2008).

  The total price of AGROBOHEMIE a.s. shares amounted to CZK 503 million (i.e. approx. PLN 69.6 million at the average CZK/PLN exchange rates of the National Bank of Poland as at 18 January 2008). The total price of Synthesia a.s. shares amounted to CZK 680 million (i.e. approx. PLN 94 million at the average CZK/PLN exchange rates of the National Bank of Poland as at 18 January 2008);

- The registry, on 14 March 2008, by Kamer Van Koophandel in Amsterdam, of the Dutch company under the name of ORLEN International Exploration & Production Company BV seated in Amsterdam ("OIEP"). PKN ORLEN S.A. took up 180 shares in OIEP, each of the nominal value of EUR 100, representing 100.0% of the share capital and 100.0% of votes at OIEP's shareholders' meeting. PKN ORLEN S.A. covered the taken up shares with a cash contribution of EUR 18 thousand.

  The core business activities of OIEP include without limitation: crude oil mining, natural gas mining, geological activity and upstream. The PKN ORLEN S.A.'s investment is of a long-term nature;

- On 18 March 2008 ORLEN Oil Sp. z o.o., as the seller and Petro-Oil DCS as the buyer entered into an agreement for the acquisition of 264 shares in Petro-Oil DCS, representing 24.0% of the company's share capital

in order to redeem them. The nominal value of each redeemed share of Petro-Oil DCS amounts to PLN 500. The carrying value of the redeemed shares recorded in the ORLEN Oil Sp. z o.o.'s books as at 18 March 2008 amounted to PLN 132 thousand. The total compensation due to ORLEN Oil Sp. z o.o. for the redeemed shares amounts to PLN 600 thousand;

- The acquisition, on 9 April 2008, by OIEP from Odin Energi A/S seated in Hellerup, Denmark, ("Odin Energi") of shares in the company Odin Energi Latvija ("Odin Energi Latvija").

  Under the Agreement, OIEP acquired from Odin Energi 500 shares in Odin Energi Latvija, each of the nominal value of LVL 5 (i.e. approx. PLN 24.8 at the average PLN/LVL exchange rates of the National Bank of Poland as at 9 April 2008), representing 50.0% of Odin Energi Latvija's share capital and 50.0% of votes at the general meeting of Odin Energi Latvija. The agreement was executed concurrently with an agreement for the purchase of the remaining 50.0% shares in Odin Energi Latvija by PKN ORLEN S.A.'s partner, Kuwait Energy Company. Kuweit Energy Company bought the shares via its subsidiary, Kuwait Energy Netherlands Corporation.

  The price for the acquired shares amounts to USD 950 thousand (i.e. approx. PLN 2 090 thousand as at the PLN/USD average exchange rates as at 9 April 2008) and will be covered with the own funds of OIEP. The ownership of shares in Odin Energi Latvija to OIEP will be transferred upon the payment of price for the shares bought. The carrying value of the acquired shares recorded in OIEP's books will be equal to their acquisition price.

  The OIEP's investment in the Odin Energi Latvija shares is of a long-term nature. The purchase of shares in Odin Energi Latvija gives right to a 45.0% share in the concessions for crude oil and natural gas upstream activities in the Latvian economic zone of the Baltic Sea.

  The business activities of Odin Energi Latvija include mainly hydrocarbon exploring, identification and excavation;

- The registry, on 19 May 2008, with the Lithuanian commercial register, of the company UAB Mazeikiu Nafta Paslaugos Tau z o.o. The company AB Mazeikiu Nafta executed, on 10 May 2008, the Formation Deed of UAB Mazeikiu Nafta Paslaugos Tau. Mazeikiu Nafta acquired in UAB Mazeikiu Nafta Paslaugos Tau 500 thousand shares, each of the nominal value of LTL 1 (i.e. approx. PLN 0.98 at the average PLN/LTL exchange rate of the National Bank of Poland as at 19 May 2008). The acquired shares represent 100.0% of the share capital and 100.0% of votes at the General Meeting of UAB Mazeikiu Nafta Paslaugos Tau.

  The initial price of the acquired shares was paid by AB Mazeikiu Nafta with cash in an amount of LTL 125 thousand (i.e. approx. PLN 122.5 thousand at the average PLN/LTL exchange rate of the National Bank of Poland as at 19 May 2008). The remaining part of the price for the acquired shares, i.e. LTL 375.0 thousand (i.e. approx. PLN 367.5 at the average PLN/LTL exchange rate of the National Bank of Poland as at 19 May 2008) will be covered by AB Mazeikiu Nafta in cash within 12 months of the date of signing the UAB Mazeikiu Nafta Paslaugos Tau Formation Deed.

  The core business activities of UAB Mazeikiu Nafta Paslaugos Tau include among others: catering services, cleaning and maintenance services and gardening services.

V. CHANGES IN ORGANISATION AND MANAGEMENT OF PKN ORLEN S.A. AND THE ORLEN GROUP MEMBERS

In the beginning of the I half of 2008 the Organisational Rules and Regulations of PKN ORLEN S.A. approved by the Management Board by resolution on 16 May 2007, amended by annex no. 1 on 14 August 2007 and annex no. 2 of 31 October 2007, were in force at PKN ORLEN.

At the meeting held on 28 February 2008, the Supervisory Board of PKN ORLEN S.A. passed a resolution on suspending for indefinite time Mr Piotr Kownacki in performance of his duties as the President and Member of the Management Board of PKN ORLEN S.A. On the same day the Supervisory Board resolved on appointing the Management Board Member to take over the powers of the Management Board President. In accordance with the Supervisory Board's decision, for the period of suspension of Mr Piotr Kownacki, the powers of the Management Board president were taken over by the Management Board Vice President, Mr Wojciech Heydel.

Further to the above described changes the Management Board, on 4 March 2008, re-assigned duties and powers amongst the Management Board Member in the following way:
- Vice-President of the Management Board Members, Sales – wholesale, retail sale, marketing, sales planning and analysis, logistics, alternative energy sources, human resources, strategy and development, public relations, Management Board service and audit;
- Vice-President of the Management Board, Upstream and Crude Trading – crude oil trading, upstream, exploration, capital investment and divestment;
- Vice-President of the Management Board, Chief Financial Officer – accounting and controlling, finance and cost management, taxes, supply chain management and investor relations;
- Member of the Management Board, Procurement and IT – IT, procurement, legal department, regulatory risk, information control and security;
- Member of the Management Board, Production – refinery production, chemistry production, petrochemistry production, oil production, energy production, engineering, technology and property investments;
- Member of the Management Board, Organisation and Capital Group – organisation and integration of owned assets, health and safety at work and environmental protection, relations with trade unions and formal and legal supervision over the ORLEN Group companies.

On 29 April 2008 the Supervisory Board of PKN ORLEN S.A. appointed Wojciech Heydel to the position of PKN ORLEN S.A. Management Board President and on 15 May 2008 Dariusz Jacek Krawiec – to the position of PKN ORLEN S.A. Management Board Vice President. Additionally, the Supervisory Board, at its meeting held on 28 May 2008 appointed the following persons to the position of the PKN ORLEN S.A. Management Board Member:
- Sławomir Robert Jędrzejczyk,
- Wojciech Robert Kotlarek,
- Krystian Pater,
- Marek Serafin

for a common 3-year term of office of the Management Board starting upon the expiry of the preceding term of office of PKN ORLEN S.A. Management Board.

Further to the election of the Management Board Members for a new term of office, on 17 June 2008 the Management Board of PKN ORLEN S.A. passed a resolution on new assignment of duties amongst the Management Board Members which was as follows:
- President of the Management Board, Chief Executive Officer, responsible for human resources, strategy and development, corporate communication, Management Board service, audit, confidential information protection and health and safety at work and environmental protection,
- Vice-President of the Management Board, Upstream and Capital Group responsible for crude oil trading, upstream and exploration, organization and integration of owned assets, procurement, legal department, corporate risk management, control and safety, relations with trade unions and formal and legal supervision over the ORLEN Group companies,
- Member of the Management Board, Chief Financial Officer, responsible for accounting and controlling, finance management, taxes, investor relations, capital investments and divestments, supply chain management and IT,
- Member of the Management Board, Sales responsible for wholesale of refinery products, retail sale, marketing, sales planning and analysis, logistics and alternative sources of energy,
- Management Board Member, Refinery responsible for refinery production, oil production, energy production, engineering, technologies and production plant in Płock,
- Member of the Management Board, Petrochemistry responsible for petrochemical and chemical production, sales of petrochemical and chemical products and property investments.

On 18 September 2008 Wojciech Heydel, the President of the Management Board of PKN ORLEN S.A. submitted his resignation to the Chairman of the Supervisory Board. Following the decision, on 18 September 2008 the Supervisory

Board appointed Dariusz Jacek Krawiec to the position of the President of the Management Board of PKN ORLEN S.A.

Additionally, in the I half of 2008 the work was completed to create a modern Accounting Service Centre for PKN ORLEN S.A. and the ORLEN Group. The last stage of the restructuring and reorganization process in the finance and accounting area consisted in transferring to the company ORLEN Księgowość Sp. z o.o. the settlements of fuel stations.

In the I half of 2008 the works were continued in respect of the organisational restructuring of the UNIPETROL Group. As part of the work implementing Corporate Governance the statutes of individual companies were amended with the aim to change organisational and legal forms and to appoint PKN ORLEN S.A. representatives to the companies' authorities. In the company UNIPETROL a.s. the number of Supervisory Board Members was reduced from twelve to nine and the number of members of Committees operating at the Supervisory Board from four to three.

Further crucial changes in the corporate documents of the company involved the Supervisory Board powers having been extended to include consenting to the Management Board's activities relating not only to UNIPETROL a.s. taking loans and borrowings from third parties but also to UNIPETROL a.s. extending loans or borrowings to third parties. Also the duties of the Management Board Members have been defined precisely in a conflict of interests situation.

In the I half of 2008 also the activities were carried out in order to adjust the UNIPETROL Group to the segment structure of PKN ORLEN S.A. through transferring a support function to the company UNIPETROL Services, sales – to UNIPETROL RPA s.r.o., splitting UNIPETROL RPA s.r.o. up into two parts: production and commerce, and restructuring of UNIPETROL Trade a.s. and Paramo a.s.

Still the acquisition processes are continued with the aim to put in order the assets of UNIPETROL Group. In January this year a transaction relating to the settlement agreement with DEZA a.s. in respect of the transfer of 50.0% of shares in AGROBOHEMIE a.s. and 38.8% of shares in Synthesia a.s. which resulted in DEZA a.s. having waived any accrued liquidated damages, compensation and interest, was closed.

On 30 April 2008 the General Meeting of Shareholders of AB Mazeikiu Nafta approved the new statute which introduced Corporate Governance through strengthening the position of the Management and Supervisory Boards. Moreover, the principle of double representation of the company was introduced and the company's structure was modified so as to improve the cooperation between the segments of PKN ORLEN S.A. and of the Mazeikiu Group and the involvement of PKN ORLEN S.A. managers to set targets and supervise their performance. In the first half also the annex to the Shareholders' Agreement was amended to make the Agreement's provisions comply with the regulations of the new statute of the company.

In the I half of 2008 at the Rafineria Jedlicze S.A. Capital Group the work was continued relating to the segment management system implementation. It involved the uniform procedural regulations having been implemented in the key segments of the ORLEN Group's operations. Moreover, in the I half of 2008 the "Procedure for the Conduct during the Implementation of Capital Investment Projects and Capital Divestment Projects" was implemented. As part of the bonus system an MBO model was implemented for the managerial staff of Rafineria Jedlicze S.A. and Management Boards of the companies – members of Rafineria Nafty Jedlicze Capital Group.

VI. DECLARATION OF THE MANAGEMENT BOARD CONCERNING THE APPLICATION OF CORPORATE GOVERNANCE

Since 1 January 2008 at the Warsaw Stock Exchange the amended corporate governance principles applicable on the capital market have applied. They have been announced in the form of "Best Practices of the Companies Listed at Stock Exchange". The amended Best Practices provide for a slightly different, as compared to the formerly applicable ones, approach to the notification by a company of its compliance with corporate governance principles. Since 1 January 2008 the companies have not declared, as before, their compliance with best practices in the form of a table but they submit relevant annual compliance reports.

PKN ORLEN S.A. submitted the Report on its compliance with corporate governance principles in the form of a separate attachment to the unconsolidated annual report for 2007.

VII. ADDITIONAL INFORMATION

7.1 Information on material agreements

The material agreements in excess of 10% of equity of PKN ORLEN S.A. executed by the ORLEN Group companies in the I half of 2008 include:

- On 16 January 2008 PKN ORLEN S.A. signed an annual agreement with Lukoil Warsaw Sp. z o.o. ("Lukoil Warsaw"). Under this agreement PKN ORLEN S.A. sells to Lukoil Warsaw gasoline and diesel oil in a period from 16 January 2008 to 31 December 2008. The value of the agreement during its term is estimated to amount to approx. PLN 1,287 million;

- On 31 January 2008 the company AB Mazeikiu Nafta executed annual agreements for the sale of gasoline and diesel oil by sea to GT Trading OY with its seat in Finland. The estimate value of these agreements amounts approx. to USD 950 million (i.e. approx. PLN 2,321 million at the average USD/PLN exchange rates of the National Bank of Poland as at 31 January 2008). The execution of these agreements stabilizes the sale of the AB Mazeikiu Nafta fuel products by sea;

- On 29 January 2008 ORLEN Deutschland AG executed an annual contract with Deutsche BP Aktiengesellschaft. The contract concerns the sale of fuels to ORLEN Deutschland AG in the period from 1 January 2008 to 31 December 2008. The estimate value of the transaction amounts to approx. EUR 1,200 million (i.e. approx. PLN 4,342 million at the average EUR/PLN exchange rates of the National Bank of Poland as at 29 January 2008);

- On 28 May 2008 ORLEN Deutschland AG signed an agreement with Shell Deutschland Oil GmbH for the supply of fuel to the ORLEN Deutschland AG stations in Germany in a period from 1 January 2008 to 31 December 2008. The estimate value of the agreement amounts to approx. EUR 1,050 million (i.e. approx. PLN 3,567 million at the average EUR/PLN exchange rates of the National Bank of Poland as at 28 May 2008).

7.2 Information about basic products and services as well as sales markets and sources of supply with indication of individual suppliers

The basic products of the ORLEN Group include:
1. Refinery products: gasolines, diesel oils, light heating oil, Jet fuel, liquid gas, heavy heating oil;
2. Petrochemical products: ethylene, propylene, polyetylene, polypropylene, benzene, butadiene, acetone, phenol, glycols, toluen, ortoxylene, paraxylene;
3. Chemical products: PVC, ammonium nitrate, PVC granulate, caustic soda, soda lye.

The volume sales of the ORLEN Group in the I half of 2008 achieved the level of 17,631 thousand tonnes and was higher by 16.5% than that generated in the prior year. The sales in the refinery segment recorded the level of 13,642 thousand tonnes, i.e. by 22.8% above the level noted in the I half of 2007. In this area the volume of gasoline sales increased by 23.8% and of diesel oil by 23.1%. Positive tendencies were also noted in respect of the sales of the other refinery segment products (light heating oil, Jet A-1 fuel, sulphur, heavy diesel oil, etc.), the volume sales of which increased by 19.9%.

In the I half of 2008 the petrochemical segment noted a 4.7% growth in the volume sales and in terms of value it decreased by PLN 243 million. The products which showed the higher increase in sales include, among others: ethylene by 11.3%, polyetylene by 13.9%, benzene by 116.0% and glycols by 20.2%.

The sales in the chemistry segment in the I half of 2008 dropped in terms of volume by 6.0% and increased in terms of value by PLN 19.4 million. The highest increase in sales was noted in the area of artificial fertilizers, namely ammonium nitrate and Canwil, i.e. by 11.5%. The sales of PVC, however, decreased by 11.9%.

The consolidated sales of the Capital Group broken by geographical markets for the I half of 2008 and 2007 are presented in Note 28 of the consolidated financial statements for the I half of 2008.

From the first quarter of 2007, PKN ORLEN S.A., under agreements it executed, has been delivering crude oil to its all refineries in Poland, Czech Republic, and Lithuania. In the I half of 2008 the crude oil supplies were realised smoothly and as scheduled.

The supplies of crude oil to PKN ORLEN S.A. were realised mainly from the area of Russia (95.5%). Low-sulphur crude oils bought in the I half of 2008 came from Azerbaijan (2.9%) and Norway (1.6%). The suppliers were the companies operating on the Russian market and international crude oil traders. In the I half of 2008, PKN ORLEN S.A. suppliers that exceeded the 10% share in its overall raw material supply included J&S and Petraco. In total the

percentage share in crude oil supplies to the refinery in Płock for these companies amounted to 45.9% and 26.0%, respectively.

The crude oil sent to the Mazeikiu refinery originated mainly from the area of Russia (97.9%). The remaining part came from Norway (2.1%). The suppliers of crude oil to the Mazeikiu refinery in the I half of 2008 included the companies with an established position on the crude oil market, however in the I half of 2008 none of the crude oil suppliers to the Mazeikiu Group exceeded the level of 10% of the consolidated revenue from the total sales of the ORLEN Group. Due to the ceased operation of the pipeline delivering crude oil to Lithuania July 2006, the supplies of raw material to the Mazeikiu refinery were exclusively made by sea via Butynga harbour.

In the I half of 2008 the crude oil sent to the UNIPETROL Group came from the area of Russia (74.0%), Azerbaijan (20.7%) and Kazakhstan (5.3%). The suppliers included the companies established on the crude oil market but in the I half of 2008 none of the crude oil suppliers of the UNIPETROL Group exceeded the threshold of 10% of the overall consolidated revenue from the sales of the ORLEN Group.

7.3 Transactions executed by PKN ORLEN S.A. with related entities

A specification of transactions between PKN ORLEN S.A. and its related parties, where the single or aggregate value of the transactions executed by the related party in a period of 6 months of 2008 exceeds the PLN equivalent of EUR 500,000:

No.	Party to the transaction	Sale in PLN thousand	Purchase in PLN thousand
1.	AB Mazeikiu Nafta	7 668 516	129 464
2.	UNIPETROL RPA a.s.	3 548 879	304 671
3.	ORLEN PetroCentrum Sp. z o.o.	1 562 160	3
4.	Basell Orlen Polyolefins Sp. z o.o.	1 248 133	10 093
5.	Petrolot Sp. z o.o.	469 077	3 773
6.	ORLEN Oil Sp. z o.o.	277 130	85 644
7.	ORLEN Asfalt Sp.z o.o.	219 632	1 435
8.	ORLEN Gaz Sp. z o.o.	206 103	395 690
9.	Anwil S.A.	193 413	2 640
10.	Ship-ServiceS.A.	106 737	243
11.	Rafineria Nafty Jedlicze S.A.	96 909	133 429
12.	ORLEN PetroTank Sp. z o.o.	43 041	18 855
13.	ORLEN Morena Sp. z o.o.	25 365	210
14.	ORLEN PetroProfit Sp. z o.o.	20 919	926
15.	ORLEN PetroZachód Sp. z o.o.	14 067	218
16.	ORLEN Transport S.A.	13 120	50 453
17.	ORLEN KolTrans Sp. z o.o.	5 378	50 693
18.	Polkomtel S.A.	3 324	30 194
19.	Mazeikiu Nafta Trading House Sp. z o.o.	2 891	22 055
20.	SPOLANA a.s.	2 558	0
21.	Platinum Oil Sp. z o.o.	1 974	14 136
22.	ORLEN Eko Sp. z o.o.	1 540	6 464
23.	ORLEN Ochrona Sp. z o.o.	1 459	17 384
24.	ORLEN Laboratorium Sp. z o.o.	1 164	17 856
25.	Petro-Oil Wielkopolskie Centrum Sprzedaży Sp. z o.o.	982	19 656
26.	ORLEN Administracja Sp. z o.o.	724	8 910
27.	ORLEN Centrum Serwisowe Sp.z o.o.	664	20 348
28.	Inowrocławskie Kopalnie Soli "Solino" S.A.	626	19 079
29.	ORLEN Księgowość Sp. z o.o.	617	18 185

No.	Party to the transaction	Sale in PLN thousand	Purchase in PLN thousand
30.	ORLEN Budonaft Sp. z o.o.	371	18 369
31.	Rafineria Trzebinia S.A.	364	257 301
32.	Petrotel Sp. z o.o.	325	3 115
33.	ORLEN Prewencja Sp. z o.o.	274	4 250
34.	ORLEN Wir Sp. z o.o.	251	2 046
35.	ORLEN Automatyka Sp. z o.o.	250	13 250
36.	ORLEN Medica Sp. z o.o	79	2 633
37.	ORLEN Projekt S.A.	76	30 497
38.	P.P.H.U. ARBUD Sp. z o.o.	0	3 520
39.	Petro-Oil Dolnośląskie Centrum Sprzedaży Sp. z o.o.	0	9 888
	Total	15 739 092	1 727 576

Transactions with related parties were valued at the exchange rate representing an arithmetic average of the average exchange rates set by the National Bank of Poland as at the last day of each month ended in a period from 1 January 2008 to 30 June 2008 – 3.4776 PLN/EUR; 2.2531 PLN/USD; 0.1384 PLN/CZK.

a) Transactions with PKN ORLEN S.A. Management and Supervisory Boards members, their spouses, siblings, ascendants, descendants, or other relatives

During a period of 6 months ended on 30 June 2008 the ORLEN Group companies did not pay any advances, grant loans, credits, issue any guarantees or sureties to, or executed any other agreements with, the persons fulfilling managing and supervisory functions and their relatives that would impose any obligation for any performances to the benefit of PKN ORLEN S.A. and its related parties.

As at 30 June 2008 the ORLEN Group companies did not extend any loans to the persons fulfilling managing or supervisory functions or to their relatives.

During a period of 6 months ended on 30 June 2008 no material transactions were executed with PKN ORLEN S.A. Management or Supervisory Boards members, their spouses, siblings, ascendants, descendants, or other relatives.

b) Transactions with related entities via persons fulfilling supervisory functions in PKN ORLEN S.A. and in the ORLEN Group companies

During a period of 6 months ended on 30 June 2008 the persons fulfilling supervisory functions in PKN ORLEN S.A. or in the ORLEN Group companies submitted declarations relating to the transactions executed with related entities, within the extended meaning of this term in accordance with the updated IAS 24 “Related Parties Disclosures”.

	Sale	Purchase	Receivables	Liabilities
Legal persons *	300 090	255 745	33 578	50 517
Natural persons	-	-	-	-

* Transactions in the period when the persons fulfilled functions in the supervisory authorities of PKN ORLEN S.A.

c) Transactions with related entities via persons fulfilling management functions in PKN ORLEN S.A. and in the ORLEN Group companies

During a period of 6 months ended on 30 June 2008 the Management Board members of PKN ORLEN S.A. or of the ORLEN Group companies submitted declarations relating to the transactions executed with related entities, within the extended meaning of this term in accordance with the updated IAS 24 “Related Parties Disclosures”.

	Sale	Purchase	Receivables	Liabilities
Legal persons	-	-	-	-
Natural persons	-	6	-	

d) Transactions executed by the key executive personnel of PKN ORLEN S.A. and of the ORLEN Group companies with related entities

During a period of 6 months ended on 30 June 2008 the key executive personnel of PKN ORLEN S.A. and the ORLEN Group companies submitted declarations relating to the transactions executed with related entities, within the extended meaning of this term in accordance with the updated IAS 24 "Related Parties Disclosures".

	Sale	Purchase	Receivables	Liabilities
Legal persons	-	-	-	-
Natural persons	48	7	-	-

7.4 Remuneration, including profit distribution paid and due or potentially due to the Management Board, Supervisory Board and members of key executive personnel, in accordance with IAS 24

The payments to the Management Board, Supervisory Board and members of key management include short-term employees' benefits, benefits due after the employment ends, other long-term benefits and compensation due in relation to the termination of employment, which have been paid, are due or, are potentially due in the period.

	for 6 months ended 30 June 2008 (unaudited)	for 6 months ended 30 June 2007 (unaudited)
Remuneration of the Management Board Members of PKN ORLEN S.A.	12 164	15 854
remuneration of the Management Board Members performing the function in the reporting period	7 934	8 234
remuneration of the former Management Board Members	4 230	7 620
Remuneration of the Supervisory Board Members of PKN ORLEN S.A.	519	510
Remuneration of the key executive personnel of PKN ORLEN S.A. *	19 593	21 019
Remuneration of the Management Board Members, Supervisory Board Members and key executive personnel of the subsidiaries of the PKN ORLEN Group **	58 439	50 455
	---	---
Total	**90 715**	**87 838**
	======	======

* including post-employment benefits of the former key executive personnel of PKN ORLEN S.A. in the amount of PLN 1,545 thousand in the period of 6 months ended 30 June 2008 and PLN 2,675 thousand in the period of 6 months ended 30 June 2007.
** Remuneration of the Management Board Members, Supervisory Board Members and key executive personnel of the subsidiaries consolidated using proportionate method was presented in 100%.

7.5 Remuneration due under non-compete clause and for termination of an agreement as a result of removal from the position

a) Management Board Members whose term of office ended on 7 June 2008:

The contracts executed between the issuer and the managerial staff provide that these persons are obliged, for a period of 6 or 12 months counting from the agreement termination or expiry date, to refrain from any competitive activity. In this period the Management Board Members are entitled to their monthly base pay due for six or twelve months, payable in equal monthly instalments.
Moreover, the contracts provide for a compensation if the agreement is terminated due to removal from the position held. In this case the payment will be equal to six or twelve time the monthly base pay.

b) Management Board Members whose term of office started on 7 June 2008:

The contracts executed between the issuer and the managerial staff provide that these persons are obliged, for a period of 6 or 12 months counting from the agreement termination or expiry date, to refrain from any competitive activity. For this refraining the Management Board Members are entitled to their monthly base pay due for six or twelve months, payable in equal monthly instalments.

Should the contracts be terminated due to removal from the position held, the Management Board Members will be entitled to the payment equal to six or twelve time the monthly base pay.

7.6 Changes in the composition of the management and supervisory bodies in PKN ORLEN S.A. and other companies of the ORLEN Group in the I half of 2008

The Members of PKN ORLEN S.A. Management Board are appointed and removed by the Supervisory Board. In a period from 1 January 2008 to 30 June 2008 the Management Board of PKN ORLEN S.A. was composed of the following persons:

Piotr Kownacki	President of the Management Board, Chief Executive Officer to 6 June 2008. Suspended in performance of duties of the President and Member of the Management Board on 28 February 2008.
Wojciech Heydel	Vice-President of the Management Board, Sales to 6 June 2008. Acting President of the Management Board, Chief Executive Officer from 28 February 2008 to 6 June 2008. President of the Management Board, Chief Executive Officer from 7 June 2008.
Cezary Filipowicz	Vice-President of the Management Board, Upstream to 6 June 2008.
Waldemar Maj	Vice-President of the Management Board, Chief Financial Officer to 6 June 2008.
Krzysztof Szwedowski	Member of the Management Board, Procurement and IT to 6 June 2008.
Dariusz Formela	Member of the Management Board, Organisation and Capital Group to 6 June 2008.
Krystian Pater	Member of the Management Board, Production from 20 March 2007 to 6 June 2008. Member of the Management Board from 7 June 2008. Member of the Management Board, Refinery from 17 June 2008.
Dariusz Jacek Krawiec	Vice-President of the Management Board from 7 June 2008. Vice-President of the Management Board, Upstream and Capital Group from 17 June 2008.
Sławomir Jędrzejczyk	Member of the Management Board from 7 June 2008. Member of the Management Board, Chief Financial Officer from 17 June 2008.
Wojciech Kotlarek	Member of the Management Board from 7 June 2008. Member of the Management Board, Sales from 17 June 2008.
Marek Serafin	Member of the Management Board from 7 June 2008. Member of the Management Board, Petrochemistry from 17 June 2008.

The Supervisory Board Members of PKN ORLEN S.A. are appointed by the General Shareholders' Meeting. In the I half of 2008 the operations of PKN ORLEN S.A. were supervised by the Supervisory Board composed of:

Małgorzata Ślepowrońska	Chairman of the Supervisory Board to 7 February 2008.
Maciej Mataczyński	Chairman of the Supervisory Board from 7 February 2008.
Raimondo Eggink	Member of the Supervisory Board by 13 June 2008. Vice-Chairman of the Supervisory Board to 7 February 2008.
Marek Karabuła	Member of the Supervisory Board from 7 February 2008. Vice-Chairman of the Supervisory Board from 15 February 2008.
Krzysztof Rajczewski	Member of the Supervisory Board to 7 February 2008. Secretary of the Supervisory Board to 7 February 2008.
Ryszard Stefański	Member of the Supervisory Board from 7 February 2008 to 13 June 2008. Secretary of the Supervisory Board from 15 February 2008 to 13 June 2008.
Angelina Sarota	Member of the Supervisory Board from 13 June 2008. Secretary of the Supervisory Board from 13 June 2008.
Robert Czapla	Member of the Supervisory Board to 7 February 2008.
Marek Drac-Tatoń	Member of the Supervisory Board to 7 February 2008.
Zbigniew Macioszek	Member of the Supervisory Board to 7 February 2008.
Agata Mikołajczyk	Member of the Supervisory Board to 7 February 2008.
Janusz Zieliński	Member of the Supervisory Board from 6 July 2007.
Grzegorz Borowiec	Member of the Supervisory Board from 7 February 2008.
Krzysztof Kołach	Member of the Supervisory Board from 7 February 2008.
Piotr Wielowieyski	Member of the Supervisory Board from 7 February 2008.
Grzegorz Michniewicz	Member of the Supervisory Board from 6 June 2008.
Jarosław Rocławski	Member of the Supervisory Board from 13 June 2008.

7.7 Number of PKN ORLEN S.A. shares and shares in other ORLEN Group companies held by the persons fulfilling management or supervisory functions in PKN ORLEN S.A.

As at 30 June 2008, Grzegorz Borowiec, Member of the Supervisory Board, held 100 shares in PKN ORLEN S.A.
As at 30 June 2008, Janusz Zieliński, Member of the Supervisory Board, held 407 shares in PKN ORLEN S.A.

7.8 Shareholding of PKN ORLEN S.A.

The shareholding structure of PKN ORLEN S.A. as at 30 June 2008.

	Number of shares	Number of votes	Nominal value of shares (in PLN)	Share held in the share capital
Nafta Polska S.A.	74,076,299	74,076 299	92,595,374	17.32%
State Treasury	43,633,897	43,633,897	54,542,371	10.20%
Other	309,998,865	309,998,865	387,498,581	72.48%
Total	427,709,061	427,709,061	534,636,326	100.00%

We are not aware of any agreements or contracts that could in the future affect the proportions of shares held by the existing shareholders and bondholders.

Management Board Report

on the Operations of the Polski Koncern Naftowy ORLEN Spółka Akcyjna Capital Group

for the I half of 2008

is submitted by the Management Board composed of:

……
Dariusz Krawiec
President of the Board

……
Sławomir Jędrzejczyk
Vice-President of the Board

……
Wojciech Kotlarek
Member of the Board

……
Krystian Pater
Member of the Board

……
Marek Serafin
Member of the Board

Płock, 23 September 2008