

Directors' Report on the Operations of of the LOTOS Group in the first half of 2016



This is a translated version of a document originally issued in Polish

Registered office of the Parent:

Grupa LOTOS S.A.,

ul. Elbląska 135, 80-718 Gdańsk, Poland,

Contact:

Investor Relations of Grupa LOTOS S.A.:

tel. +48 58 308 73 93

e-mail: ir@grupalotos.pl

Auditor:

Ernst & Young Audyt Polska sp. z o.o. sp. k

An excel file with the operating and financial data for Q2 2016 and H1 2016 and for the previous reporting periods is published together with the half-year report in the Investor Relations section of our website as 'databook'.

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1. INFORMATION ON THE LOTOS GROUP

1.1. ORGANISATIONAL STRUCTURE OF THE LOTOS GROUP AND GRUPA LOTOS S.A. BRANCHES (BUSINESS UNITS)

As at June 30th 2016, the LOTOS Group comprised Grupa LOTOS S.A. (the Parent) and 34 production and service companies, including:

- 13 direct subsidiaries of Grupa LOTOS S.A.,
- 21 indirect subsidiaries of Grupa LOTOS S.A.

Grupa LOTOS S.A. also held shares in equity-accounted joint ventures.

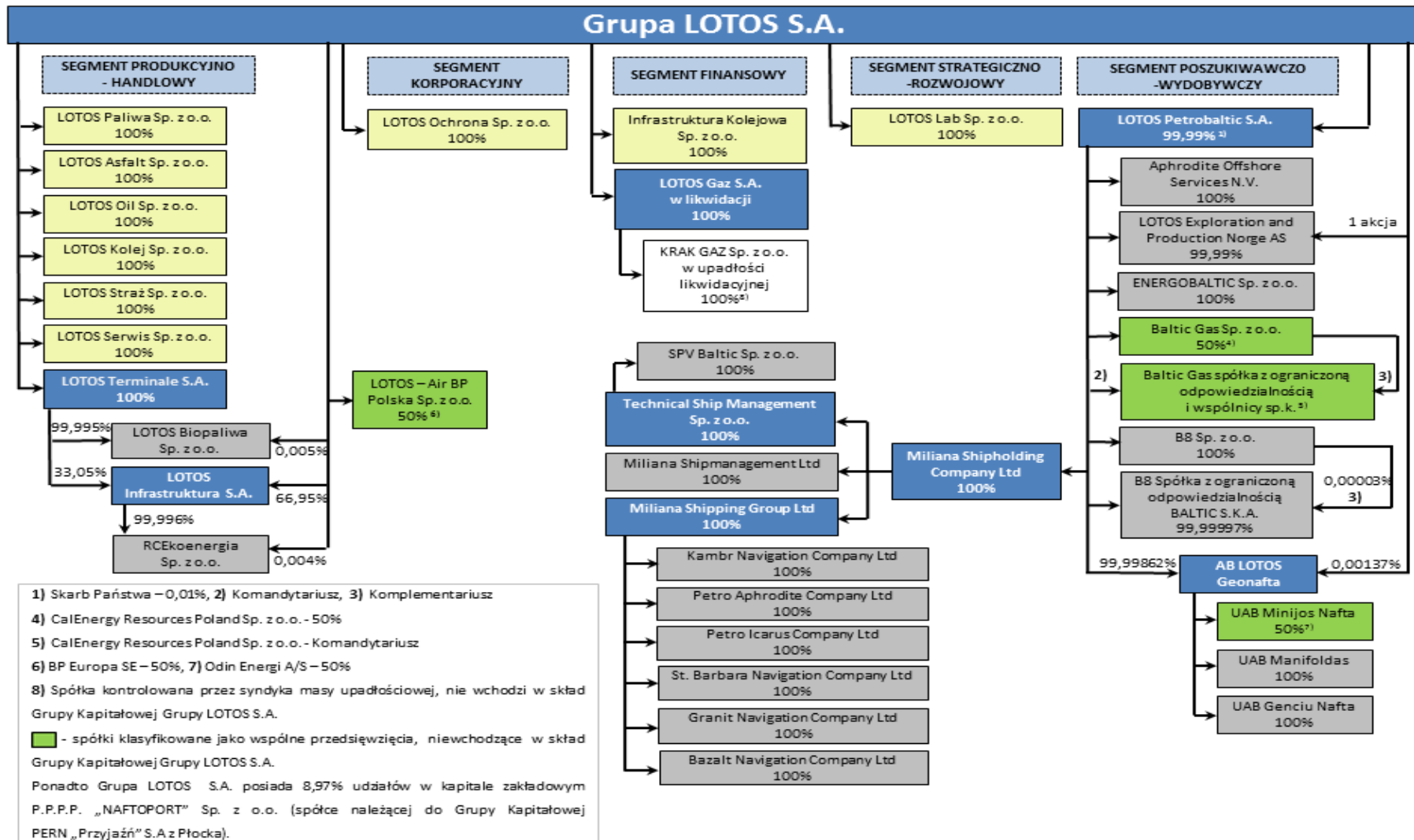
Grupa LOTOS S.A. has no divisions within the meaning of the Polish Accountancy Act.

The Group's operating activity comprises two main reportable operating segments:

- **Upstream segment** – comprising activities related to the acquisition of crude oil and natural gas reserves, and crude oil and natural gas production.
- **Downstream segment** – comprising the production and processing of refined petroleum products and their wholesale and retail sale, as well as auxiliary, transport and service activities.

For management purposes, the LOTOS Group is divided into business units which correspond to the business segments.

Fig. 1 Organisational chart of the LOTOS Group as at June 30th 2016



1.2. CHANGES IN ORGANISATIONAL OR CAPITAL LINKS BETWEEN GRUPA LOTOS S.A. AND OTHER ENTITIES

Contact data and brief description of the principal business activity of the LOTOS Group companies, as well as Grupa LOTOS S.A.'s ownership interests and the applied consolidation method are presented below.

Table 1 Companies with organisational links to Grupa LOTOS S.A.

Name	Registered office	Description of business	Group's ownership interest		
			Jun 30 2016	Dec 31 2015	Jun 30 2015
Parent					
Grupa LOTOS S.A.	Gdańsk	Manufacturing and processing of refined petroleum products (mainly fuels) and their wholesale	Not applicable	Not applicable	Not applicable
Direct fully-consolidated subsidiaries					
LOTOS Petrobaltic S.A. (parent of another group: LOTOS Petrobaltic Group)	Gdańsk	Acquisition of crude oil and natural gas deposits, extraction of hydrocarbons	99.99%	99.99%	99.99%
LOTOS Paliwa Sp. z o.o.	Gdańsk	Wholesale and retail sale of fuels and light fuel oil, management of the LOTOS service station network	100.00%	100.00%	100.00%
LOTOS Oil Sp z o.o.	Gdańsk	Manufacturing and sale of lubricating oils and lubricants, and sale of base oils	100.00%	100.00%	100.00%
LOTOS Asfalt Sp. z o.o.	Gdańsk	Manufacturing and sale of bitumens	100.00%	100.00%	100.00%
LOTOS Kolej Sp. z o.o.	Gdańsk	Railway transport	100.00%	100.00%	100.00%
LOTOS Serwis Sp. z o.o.	Gdańsk	Maintenance of mechanical and electric operations and controlling devices, overhaul and repair services	100.00%	100.00%	100.00%
LOTOS LAB Sp. z o.o.	Gdańsk	Laboratory testing	100.00%	100.00%	100.00%
LOTOS Straż Sp. z o.o.	Gdańsk	Fire service activities	100.00%	100.00%	100.00%
LOTOS Ochrona Sp. z o.o.	Gdańsk	Security services	100.00%	100.00%	100.00%
LOTOS Terminale S.A. (parent of another group: LOTOS Terminale Group)	Czechowice-Dziedzice	Storage and distribution of fuels	100.00%	100.00%	100.00%
LOTOS Infrastruktura S.A. (parent of another group: LOTOS Infrastruktura Group)	Jasło	Storage and distribution of fuels Renting and operating of own or leased real estate	100.00%	100.00%	100.00%
LOTOS Gaz S.A. (in liquidation)	Kraków	Dormant	100.00%	100.00%	100.00%
Non-consolidated direct subsidiaries ⁽¹⁾					
Infrastruktura Kolejowa Sp. z o.o.	Gdańsk	Dormant	100.00%	100.00%	100.00%
LOTOS Foundation	Gdańsk	Socially beneficial activity within the scope of public tasks defined in the Act on Public Benefit and Volunteer Work. The Foundation does not conduct any business activity.	100.00%	100.00%	100.00%
Indirect fully-consolidated subsidiaries					
LOTOS Infrastruktura Group					
RCEkoenergia Sp. z o.o.	Czechowice-Dziedzice	Production and distribution of electricity, heat and gas	100.00%	100.00%	100.00%
LOTOS Terminale Group					
LOTOS Biopaliwa Sp. z o.o.	Czechowice-Dziedzice	Production of fatty acid methyl esters (FAME)	100.00%	100.00%	100.00%

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LOTOS Petrobaltic Group					
LOTOS Exploration and Production Norge AS	Norway, Stavanger	Oil exploration and production on the Norwegian Continental Shelf, provision of services related to oil exploration and production	99.99%	99.99%	99.99%
Aphrodite Offshore Services N.V.	Curaçao	Dormant	99.99%	99.99%	99.99%
ENERGOBALTIC Sp. z o.o.	Władysławowo	Production of electricity, heat, LPG and natural gas condensate	99.99%	99.99%	99.99%
B8 Sp. z o.o	Gdańsk	Support activities for extraction and quarrying operations (dormant)	99.99%	99.99%	99.99%
B8 Spółka z ograniczoną odpowiedzialnością BALTIC S.K.A.	Gdańsk	Exploration and production of crude oil and natural gas (dormant)	99.99%	99.99%	99.99%
Miliana Shipholding Company Ltd. (parent of another group: Miliana Shipholding Group)	Nicosia, Cyprus	Storage and transport of crude oil, other sea transport services	99.99%	99.99%	99.99%
Technical Ship Management Sp. z o.o. (parent of another group: Technical Ship Management Group)	Gdańsk	Sea transport support activities. ship operation advisory services	99.99%	99.99%	99.99%
SPV Baltic Sp. z o.o.	Gdańsk	Provision of sea transport and related services	99.99%	99.99%	99.99%
Miliana Shipmanagement Ltd.	Nicosia, Cyprus	Provision of sea transport and related services	99.99%	99.99%	99.99%
Miliana Shipping Group Ltd. (parent of another group: Miliana Shipping Group Group)	Nicosia, Cyprus	Management of own assets	99.99%	99.99%	99.99%
Bazalt Navigation Company Ltd.	Nicosia. Cyprus	Ship chartering	99.99%	99.99%	99.99%
Granit Navigation Company Ltd.	Nicosia. Cyprus	Ship chartering	99.99%	99.99%	99.99%
Kambr Navigation Company Ltd.	Nicosia. Cyprus	Ship chartering	99.99%	99.99%	99.99%
St. Barbara Navigation Company Ltd.	Nicosia. Cyprus	Ship chartering	99.99%	99.99%	99.99%
Petro Icarus Company Ltd.	Nicosia. Cyprus	Ship chartering	99.99%	99.99%	99.99%
Petro Aphrodite Company Ltd.	Nicosia. Cyprus	Ship chartering	99.99%	99.99%	99.99%
AB LOTOS Geonafra (parent of another group: AB LOTOS Geonafra Group)	Lithuania, Gargždai	Crude oil exploration and production, drilling services, and purchase and sale of crude oil	99.99%	99.99%	99.99%
UAB Genciu Nafta	Lithuania, Gargždai	Crude oil exploration and production	99.99%	99.99%	99.99%
UAB Manifoldas	Lithuania, Gargždai	Crude oil exploration and production	99.99%	99.99%	99.99%
Equity-accounted joint ventures					
LOTOS - Air BP Polska Sp. z o.o. ⁽²⁾	Gdańsk	Sale of aviation fuel and logistics services	50.00%	50.00%	50.00%
LOTOS Petrobaltic Group					
Baltic Gas Sp. z o.o. ⁽³⁾	Gdańsk	Oil and gas production (support activities for oil and gas production)	49.99%	49.99%	49.99%

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Baltic Gas spółka z ograniczoną odpowiedzialnością i wspólnicy sp.k. (5)	Gdańsk	Crude oil and gas production	45.67%	43.96%	44.54%
AB LOTOS Geonafta Group					
UAB Minijos Nafta (4)	Lithuania, Gargždai	Crude oil exploration and production	49.99%	49.99%	49.99%

(1) The companies were excluded from consolidation (IFRS 10 Consolidated Financial Statements) due to immateriality of the amounts disclosed in their financial statements as at June 30th 2016.

(2) Joint venture agreement between Grupa LOTOS S.A. and BP Europe SE on joint operations consisting in supply of aviation fuel through LOTOS - Air BP Polska Sp. z o.o.

(3) Agreement on cooperation between LOTOS Petrobaltic S.A. and CalEnergy Resources Poland Sp. z o.o. providing for development of and production from gas and condensate reserves from the B-4 and B-6 fields in the Baltic Sea, performed through special purpose vehicles Baltic Gas spółka z ograniczoną odpowiedzialnością i wspólnicy sp.k. and Baltic Gas Sp. z o.o. (general partner).

Within the meaning of IFRS 11, Baltic Gas Sp. z o.o. i wspólnicy sp.k. and Baltic Gas Sp. z o.o. are the Group's equity-accounted joint ventures.

In H1 2016, Cal Energy Resources Poland Sp. z o.o. and LOTOS Petrobaltic S.A. made cash contributions to Baltic Gas spółka z ograniczoną odpowiedzialnością i wspólnicy sp. k. of PLN 18,508 thousand and PLN 19,574 thousand, respectively; as a result, the Group's ownership interest in the company changed. The expenditure, representing the cash contribution made by LOTOS Petrobaltic S.A., was disclosed in the consolidated statement of cash flows under Cash contributions – equity-accounted joint ventures.

(4) Joint venture set up for the purpose of oil exploration and production in Lithuania, operated in the form of UAB Minijos Nafta.

1.3. OWNERSHIP CHANGES AT THE LOTOS GROUP

Table 2 Important processes/developments at subsidiaries

Company	Description	Date
None		

Table 3 Changes of share capital at subsidiaries

Company	Registration date	Before	Change	After	Currency	Comments
B8 Sp. z o.o.	Feb 2 2016	205,000.00	100,000.00	305,000.00	PLN	On December 3rd 2015, the Extraordinary General Meeting of B8 Sp. z o.o. passed a resolution to increase the company's share capital through the issue of 2,000 new shares with a par value of PLN 50 per share.
Baltic Gas Sp. z o.o.	May 19 2016	145,000.00	75,400.00	220,400.00	PLN	On April 6th 2016, the Extraordinary General Meeting of Baltic Gas Sp. z o.o. passed a resolution to increase the company's share capital through the issue of 1,508 new shares with a par value of PLN 50 per share.
B8 Sp. z o.o.	Aug 8 2016	305,000.00	50,000.00	355,000.00	PLN	On June 21st 2016, the Extraordinary General Meeting of B8 Sp. z o.o. passed a resolution to increase the company's share capital through the issue of 1,000 new shares with a par value of PLN 50 per share.

Contributions to Baltic Gas Spółka z ograniczoną odpowiedzialnością i Wspólnicy sp.k.

In April 2016, the following previously agreed cash contributions were made to the company:

- PLN 7,552,607.30 – by LOTOS Petrobaltic S.A.,
- PLN 7,956,620.38 – by CalEnergy Resources Poland Sp. z o.o.

The contributions were entered in the Business Register of the National Court Register on May 30th 2016. Below are presented the contributions agreed and made as at June 30th 2016:

Table 4 Contributions to Baltic Gas Spółka z ograniczoną odpowiedzialnością i Wspólnicy sp.k.

Baltic Gas Sp. z o.o. i wspólnicy Spółka komandytowa			
Partners	Baltic Gas Sp. z.o.o.	LOTOS Petrobaltic S.A.	CalEnergy Resources Poland Sp. z o.o.
Agreed contribution	1,000.0	81,869,711.0	98,933,897.0
Contribution made, including:	1,000.0	75,862,731.8	90,278,564.1
a) cash contribution	1,000.0	24,192,731.8	90,278,564.1
b) contribution in-kind	-	51,700,000.0	-
Unpaid contribution	-	5,976,979.2	8,655,332.9

Following approval of the new Organisational Rules of Grupa LOTOS S.A., on May 16th 2016 LOTOS Ochrona Sp. z o.o. was transferred to the Corporate Segment (previously it was classified under the Strategy and Development Segment). In H1 2016, there were no other changes in the key management policies of Grupa LOTOS S.A. or the LOTOS Group.

1.4. GRUPA LOTOS S.A. SHARES

1.4.1. SHAREHOLDERS HOLDING MORE THAN 5% OF TOTAL VOTING RIGHTS AT GRUPA LOTOS S.A.'S GM

In accordance with [Current Report No. 11/2013](#) of April 29th 2013, the only shareholder (apart from the State Treasury) holding more than 5% of total voting rights at the Company's General Meeting is Nationale Nederlanden Otwarty Fundusz Emerytalny (NN OFE).

Table 5 Shareholding structure of Grupa LOTOS S.A. as at June 30th and as at the date of issue of this Directors' Report

Shareholder	Number of shares/voting rights equivalent to par value of shares	Share of total voting rights equivalent to percentage of share capital held
State Treasury	98,329,515	53.18%
NN OFE ⁽¹⁾	10,584,287 ⁽²⁾	5.73%
Other	75,959,560	41.09%
Total	184,873,362	100.0%

⁽¹⁾ Based on the annual structure of investment funds' asset as at December 31st 2015. Source: Polish Press Agency.

⁽²⁾ Company estimates based on data published by NN OFE as at December 31st 2015. Source: Polish Press Agency. The number of shares registered by NN OFE at the Annual General Meeting of Grupa LOTOS S.A. held on June 28th 2016 was 9,000,000, representing 4.87% of the Company's share capital:
http://inwestor.lotos.pl/1185/p,194,i,914/raporty_i_dane/raporty_biezace/akcjonariusze_posiadajacy_co_najmniej_5_glosow_na_zwyczynym_walnym_zgromadzeniu_grupy_lotos_sa_w_dniu_28_czerwca_2016_roku_korekta_tresci_raportu

1.4.2. GRUPA LOTOS S.A. SHARES HELD BY THE MANAGEMENT AND SUPERVISORY PERSONNEL

Based on information available to the Company as at the date of issue of the H1 2016 report, i.e. August 11th 2016, no shares in Grupa LOTOS were held by its management and supervisory personnel.

1.5. PERSONNEL

1.5.1. CHANGES IN THE COMPOSITION OF THE MANAGEMENT BOARD AND SUPERVISORY BOARD

From January 1st 2016 to April 13th 2016 the Management Board (ninth joint term of office*) was composed of the following members:

Management Board members	Position
Paweł Olechnowicz	President of the Management Board Chief Executive Officer
Mariusz Machajewski	Vice President of the Management Board Chief Financial Officer
Zbigniew Paszkowicz	Vice President of the Management Board Chief Exploration and Production Officer
Marek Sokołowski	Vice President of the Management Board Chief Operating Officer
Maciej Szozda	Vice President of the Management Board Chief Commercial Officer

**) The ninth term of office started on June 29th 2015.*

On April 13th 2016, the Supervisory Board removed the following persons from the Grupa LOTOS Management Board:

- Paweł Olechnowicz, President of the Management Board,
- Marek Sokołowski, Vice President of the Management Board, Chief Strategy and Development Officer,
- Zbigniew Paszkowicz, Vice President of the Management Board, Chief Exploration and Production Officer.

Then the Supervisory Board resolved to conduct a recruitment procedure for the positions of President of the Management Board, Vice President of the Management Board – Chief Operating Officer, Vice President of the Management Board – Chief Strategy and Development Officer, and Vice President of the Management Board – Corporate Affairs, on the Management Board of Grupa LOTOS S.A. for the remaining period of the ninth joint term of office.







The Supervisory Board also resolved to delegate as of April 13th 2016 Mr Robert Pietryszyn, Chairman of the Supervisory Board of Grupa LOTOS S.A., to temporarily perform the duties of the President of the Company's Management Board until appointment of new President of the Management Board.

On May 13th 2016, following completion of the recruitment procedure, the Supervisory Board appointed four Management Board members and resolved that as of that date the Management Board of the ninth joint term of office would be composed of six members. Further, the Supervisory Board determined a new division of powers and responsibilities among the Management Board members.

The Supervisory Board appointed the following persons to the Management Board for the remaining period of the ninth joint term of office:

- Mr Robert Pietryszyn – President of the Board, with effect from May 13th 2016,
- Mr Marcin Jastrzębski – Vice President of the Management Board, Chief Operating Officer, with effect from May 13th 2016,
- Mr Przemysław Marchlewicz – Vice President of the Management Board for Corporate Affairs, with effect from May 17th 2016,
- Mr Mateusz Aleksander Bonca – Vice President of the Management Board, Chief Strategy and Development Officer, with effect from June 1st 2016.

Table 8 Composition of the Management Board of the ninth term as at June 30th 2016

Management Board members	Position	On the Management Board of the 9th term	Professional career and positions held
 Robert Pietryszyn	President of the Management Board Chief Executive Officer	May 13 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-84
 Mariusz Machajewski	Vice President of the Management Board Chief Financial Officer	Jun 29 2015 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-15
 Marcin Jastrzęski	Vice President of the Management Board Chief Operating Officer	May 13 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-83
 Mateusz A. Bonca	Vice President of the Management Board Chief Strategy and Development Officer	Jun 1 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-87
 Przemysław Marchlewicz	Vice President of the Management Board for Corporate Affairs	May 17 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-85
 Maciej Szozda	Vice President of the Management Board Chief Refining and Marketing Officer	Jun 29 2015 – Jul 21 2016	

On July 21st 2016, the Supervisory Board removed Mr Maciej Szozda from the Grupa LOTOS Management Board.

From January 1st 2016 to January 26th 2016 the Supervisory Board (ninth joint term of office) consisted of the following members:

Supervisory Board members	Position
Wiesław Skwarko	Chairman
Agnieszka Trzaskalska	Deputy Chairperson
Oskar Pawłowski	Secretary
Małgorzata Hirszel	Member
Katarzyna Witkowska	Member
Michał Rumiński	Member
Robert Pietryszyn	Member

The State Treasury, the Company's shareholder, represented by the Minister of State Treasury, in exercise of its rights set out in Art. 11.2 of the Company's Articles of Association, on January 26th 2016 removed Mr Robert Pietryszyn from the Supervisory Board.

The Extraordinary General Meeting of the Company held on January 27th 2016, convened at the request of the State Treasury, acting pursuant to Art. 385.1 of the Commercial Companies Code and Art. 9.4 of the Company's Articles of Association, changed the composition of the Grupa LOTOS Supervisory Board of the ninth term. The Extraordinary General Meeting removed five of

the six members of the Supervisory Board: Mr Wiesław Skwarko – Chairman, Ms Agnieszka Trzaskalska – Deputy Chairperson, Mr Oskar Pawłowski – Secretary, Ms Małgorzata Hirszel and Mr Michał Rumiński, and appointed the following persons to the Supervisory Board: Mr Robert Pietryszyn, as Chairman, Ms Katarzyna Lewandowska, Mr Dariusz Figura, Mr Cezary Krasodomski, and Ms Maria Sierpińska.

As a result, from January 27th 2016 to April 12th 2016 the composition of the Supervisory Board of Grupa LOTOS S.A. of the ninth term of office was as follows:

Supervisory Board members	Position
Robert Pietryszyn	Chairman
Katarzyna Lewandowska	Deputy Chairperson <i>(appointed as Deputy Chairperson of the Supervisory Board on February 24th 2016)</i>
Cezary Krasodomski	Secretary <i>(appointed as Secretary of the Supervisory Board on February 24th 2016)</i>
Dariusz Figura	Member
Maria Sierpińska	Member
Katarzyna Witkowska	Member

On April 12th 2016, the State Treasury, represented by the Minister of State Treasury, exercised its right set forth in Art. 11.2 of the Articles of Association, under which it may directly appoint and remove one member of the Supervisory Board, and appointed Mr Marcin Jastrzębski as member of the Supervisory Board of Grupa LOTOS S.A.

Following the removal of the Management Board members acting as President of the Board, Vice President of the Management Board – Chief Strategy and Development Officer, and Vice President of the Management Board – Chief Exploration and Production Officer, on April 13th 2016 the Supervisory Board decided to temporarily delegate its Chairman, Robert Pietryszyn, to act as President of the Board until a new President is appointed. Since then, Katarzyna Lewandowska, Deputy Chairperson of the Supervisory Board, has acted as Chairperson of the Supervisory Board, in accordance with the Rules of Procedure for the Supervisory Board.


On May 13th 2016, Mr Robert Pietryszyn, Chairman of the Supervisory Board of Grupa LOTOS S.A., and Mr Marcin Jastrzębski, who were appointed to the Management Board of Grupa LOTOS S.A. for the remaining period of the ninth joint term of office, submitted their resignations from the Supervisory Board of Grupa LOTOS S.A.

On May 25th 2016, the State Treasury, represented by the Minister of State Treasury, exercised its right set forth in Art. 11.2 of the Articles of Association, under which it may directly appoint and remove one member of the Supervisory Board, and appointed Ms Beata Kozłowska-Chyła as member of the Supervisory Board of Grupa LOTOS S.A. of the ninth term of office. The State Treasury subsequently removed Ms Beata Kozłowska-Chyła from the Supervisory Board on June 28th 2016.

On June 28th 2016, the Annual General Meeting of the Company made further changes in the composition of the Grupa LOTOS Supervisory Board of the ninth term of office by removing Mr Cezary Krasodomski and appointing the following new members: Mr Mariusz Golecki and Ms Beata Kozłowska-Chyła, who was appointed as the Chairperson of the Supervisory Board. On the same day the State Treasury, represented by the Minister of State Treasury, exercised its right set forth in Art. 11.2 of the Articles of Association, under which it may directly appoint and remove one member of the Supervisory Board, and appointed Ms Agnieszka Szklarczyk-Mierzwa as member of the Supervisory Board of Grupa LOTOS S.A. of the ninth term of office.

Table 9 Composition of the Supervisory Board of the ninth term as at June 30th 2016

Supervisory Board members	Position	On the Supervisory Board of the 9th term	Professional career and positions held
 Beata Kozłowska-Chyła	Chairwoman	Jun 28 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-86
 Katarzyna Lewandowska	Deputy Chairwoman (appointed Deputy on February 24th 2016)	Jan 27 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-81
 Agnieszka Szklarczyk-Mierzwa	Secretary (appointed Secretary on July 21st 2016)	Jul 28 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-89
 Maria Sierpińska	Member	Jan 27 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-82
 Dariusz Figura	Member	Jan 27 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-80
 Katarzyna Witkowska	Member	Jun 30 2015 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-75

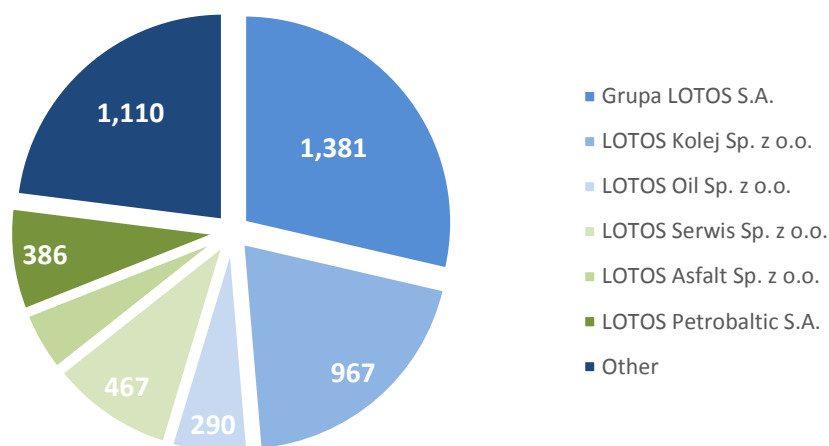
Supervisory Board members	Position	On the Supervisory Board of the 9th term	Professional career and positions held
 <p data-bbox="201 555 352 577">Mariusz Golecki</p>	Member	Jun 28 2016 -	http://inwestor.lotos.pl/1137/lad_korporacyjny/struktura_organizacyjna#person-90

1.5.2. STRUCTURE OF THE LOTOS GROUP WORKFORCE

**Table 10 Structure of the LOTOS Group workforce by job role
(as at June 30th 2016)**

Company	Number of employees as at Jun 30 2016		
	Blue-collar jobs	White-collar jobs	Total
Grupa LOTOS S.A.	500	881	1,381
LOTOS Paliwa Sp. z o.o.	0	272	272
LOTOS Kolej Sp. z o.o.	682	285	967
LOTOS Oil Sp. z o.o.	104	186	290
LOTOS LAB Sp. z o.o.	13	102	115
LOTOS Serwis Sp. z o.o.	314	153	467
LOTOS Straż Sp. z o.o.	76	14	90
LOTOS Asfalt Sp. z o.o.	105	119	224
LOTOS Gaz S.A.	0	1	1
LOTOS Ochrona Sp. z o.o.	140	21	161
LOTOS Air BP Polska Sp. z o.o.	32	17	49
LOTOS Park Technologiczny Sp. z o.o.	0	0	0
LOTOS Infrastruktura S.A.	40	33	73
LOTOS Terminale S.A.	61	50	111
RC Ekoenergia Sp. z o.o.	43	31	74
LOTOS Biopaliwa Sp. z o.o.	23	15	38
LOTOS Petrobaltic S.A.	148	238	386
ENERGOBALTIC Sp. z o.o.	3	28	31
LOTOS E&A Norge AS	0	27	27
AB LOTOS Geonafta	35	11	46
Miliana Shipping Ltd	0	1	1
Technical Ship Management	0	9	9
SPV Baltic Spółka z o.o.	7	5	12
Total	2,326	2,499	4,825

**Chart 1 Structure of the LOTOS Group workforce by key companies
(as at June 30th 2016)**



**Table 11 Structure of the LOTOS Group workforce by job role
(as at June 30th 2016)**

Job type	Men	Women	Total
blue-collar jobs	2,245	81	2,326
white-collar jobs	1,473	1,026	2,499
Total	3,718	1,107	4,825

**Table 12 Structure of the Grupa LOTOS S.A. workforce by job role
(as at June 30th 2016)**

Job type	Men	Women	Total
blue-collar jobs	499	1	500
white-collar jobs	448	433	881
Total	947	434	1,381

2. FINANCIAL PERFORMANCE OF THE LOTOS GROUP

2.1. KEY FACTORS WITH A BEARING ON FINANCIAL PERFORMANCE IN H1 2016

Table 13 Crude oil and natural gas prices, differential, model refining margin (USD/bbl)

	H1 2016	H1 2015	H1 2016 / H1 2015
DATED Brent FOB prices ⁽¹⁾	39.72	57.70	-31.2%
Brent/Urals spread ⁽¹⁾	2.65	1.62	63.6%
UK NBP natural gas prices ⁽²⁾	24.60	39.27	-37.4%
Model refining margin ⁽³⁾	6.50 ⁽⁴⁾	8.73	-25.5%

⁽¹⁾ and ⁽²⁾ Source: Thomson Reuters.

⁽²⁾ To ensure comparability, the UK NBP natural gas prices have been converted from USD/MWh to USD/boe, using the conversion factor of 1.6282 MWh/boe.

⁽³⁾ In line with the methodology applied by the Company, the model margin was computed based on Thomson Reuters data, which reflect long-term trends in prices based on which the Company conducts its trading activity. In a shorter term, the prices used to compute the model margin may differ from actual trading prices

⁽⁴⁾ According to the methodology published by the company on June 26th 2016.

Table 14 Crack margins ⁽¹⁾ (USD/bbl)

	H1 2016	H1 2015	H1 2016 / H1 2015
Gasoline	16.54	17.27	-4.2%
Naphtha	3.48	0.31	1022.6%
Diesel oil (10 ppm)	12.47	20.14	-38.1%
Light fuel oil	11.27	17.22	-34.6%
Aviation fuel	12.18	18.05	-32.5%
Heavy fuel oil	-10.68	-8.94	19.5%

⁽¹⁾ Product crack margin is calculated as the difference between the price of a given product (recalculated from price per metric tonne to price per barrel, and accounting for an appropriate density factor) and the price of Urals crude (the Brent crude price adjusted for the Brent/Urals spread).

Source: Thomson Reuters.

Table 15 USD/PLN exchange rates

	H1 2016	H1 2015	H1 2016 / H1 2015
PLN/USD exchange rate at end of period	3.98	3.76	5.9%
Average PLN/USD exchange rate	3.91	3.71	5.4%

Source: In-house analysis based on National Bank of Poland data.

Upstream segment

Table 16 Crude oil and natural gas reserves, production and sales

Crude oil and natural gas reserves as at (mboe) ⁽¹⁾	Jun 30 2016	Jun 30 2015	
Norway	15.37	4.08	
Poland	39.55	41.40	
Lithuania	6.93	7.37	
Total	61.85	52.85	

Production (boe/d) ⁽²⁾	H1 2016	H1 2015	H1 2016 / H1 2015
Norway	22,057	6,723	228.1%
Poland	5,825	6,023	-3.3%
Lithuania	1,134	1,327	-14.5%
Total	29,016	14,073	106.2%

Production (boe)	H1 2016	H1 2015	H1 2016 / H1 2015
Norway	3,752,837	1,310,351	186.4%
Poland	1,033,818	555,042	86.3%
Lithuania	206,437	258,047	-20.0%
Total	4,993,092	2,123,440	135.1%

Sales of own products (boe)	H1 2016	H1 2015	H1 2016 / H1 2015
Norway	3,865,204	1,330,494	190.5%
Poland	998,296	627,686	59.0%
Lithuania	182,367	185,082	-1.5%
Total	5,045,867	2,143,262	135.4%

⁽¹⁾ 2P – proved and probable reserves (according to the SPE-PRMS classification); boe – barrels of oil equivalent (oil + gas).

⁽²⁾ Production was calculated based only on the days of mechanical availability of the production infrastructure; boe per day.

Stronger sales in the upstream segment in H1 2016 were attributable to the acquisition of interests in production licences in the Sleipner assets in Norway in Q4 2015 and launch of production from the B8 oil field in the Baltic Sea. The rise in the segment's revenue by PLN 231.6m, or 61.0%, mainly resulted from higher sales volume (up 135.4%) and the stronger US dollar (average USD/PLN exchange rate up 5.4% in the reporting period), partly offset by a 31.2% drop in the Brent dtd oil price.

Table 17 Upstream segment's key financial data (PLNm)

	H1 2016	H1 2015	H1 2016 / H1 2015
Revenue	611.0	379.4	61.0%
EBIT	-16.8	45.8	-
Depreciation and amortisation	280.6	131.9	112.7%
EBITDA	263.8	177.7	48.5%
Adjusted EBIT ⁽¹⁾	71.4	45.8	55.8%
Adjusted EBITDA ⁽¹⁾	352.0	177.7	98.1%

⁽¹⁾ Net of non-recurring items recognised in H1 2016, including mainly: write-off on expenditure related to the Gaz Poludnie licence area, including the B-21 structure in the Baltic Sea, and the PLN 75.5m impairment loss on total capitalised expenditure related to the PL643 licence.

The adjusted operating profit of the upstream segment in H1 2016 improved by 55.8% on the comparative period following the launch of production from the B8 field in the Baltic Sea and acquisition of the Sleipner assets in the North Sea.

The significantly higher depreciation and amortisation expenses resulted from the acquisition of the Sleipner assets on the Norwegian Continental Shelf in late 2015.

Downstream segment

Table 18 Crude slate ('000 tonnes)

	H1 2016	H1 2015	H1 2016/ H1 2015
Crude oil processed by the Gdańsk refinery	4,957.2	5,006.8	-1.0%
including:			
Urals crude	3,932.2	3,988.3	-1.4%
Rozewie crude	126.4	77.2	63.7%
Lithuanian crude	20.9	27.8	-24.8%
Lubiatów crude	136.7	126.3	8.2%
Other types of crude	741.0	787.2	-5.9%

Table 19 Grupa LOTOS S.A.'s product yields ('000 tonnes)

	H1 2016	H1 2015	H1 2016/ H1 2015
Total output	5,126.9	5,353.1	-4.2%
Gasolines	710.5	737.3	-3.6%
Naphtha	241.7	229.3	5.4%
Diesel oils	2,065.9	2,263.0	-8.7%
Light fuel oils	129.1	114.8	12.5%
Jet fuel	305.2	300.1	1.7%
Heavy products ⁽¹⁾	1,026.4	1,086.8	-5.6%
Other ⁽²⁾	648.1	621.8	4.2%

⁽¹⁾ Heavy fuel oil and bitumen components

⁽²⁾Other products include fuel and technical gases, sulfur, base oils, xylene fraction, LPG, bunker fuel, extracts, raffinates, and slack wax.

Table 20 Structure of sales in the downstream segment ('000 tonnes)

	H1 2016	H1 2015	H1 2016 / H1 2015
	5,054.8	5,262.3	-3.9%
Gasolines	729.9	753.1	-3.1%
Naphtha	241.7	229.3	5.4%
Diesel oils	2,186.7	2,390.7	-8.5%
Light fuel oils	129.0	118.3	9.0%
Jet fuel	311.9	312.9	-0.3%
Heavy products ⁽¹⁾	981.7	1,036.0	-5.2%
Other petroleum products ⁽²⁾	473.9	422.0	12.3%

⁽¹⁾Heavy fuel oil and bitumens

⁽²⁾Other products include fuel and technical gases, sulfur, base oils, xylene fraction, LPG, bunker fuel, extracts, raffinates, and slack wax.

A 26.7% year-on-year decline in the downstream segment's revenue in H1 2016 was mainly attributable to lower sales volumes and average net selling prices of the segment's products, which fell by 23.7%, from PLN 2,200 per tonne in H1 2015 to PLN 1,679 per tonne in H1 2016, on lower market prices of refined products. The segment's lower operating profit compared with H1 2015 is attributable to lower crack margins on fuels.

The adjusted LIFO-based EBITDA in the compared periods was significantly affected by inventory write-downs recognised in 2014-2015, which reduced cost of sales in both periods.

Table 21 Downstream segment's key financial data (PLNm)

	H1 2016	H1 2015	H1 2016 / H1 2015
Revenue	8,488.2	11,574.8	-26.7%
EBIT	706.3	750.7	-5.9%
Depreciation and amortisation	239.2	229.7	4.1%
EBITDA	945.5	980.4	-3.6%
LIFO-based EBIT	886.5	705.1	25.7%
LIFO-based EBITDA	1,125.7	934.8	20.4%
Adjusted LIFO-based EBITDA ⁽¹⁾	740.4	840.2	-11.9%

⁽¹⁾EBITDA, including the LIFO effect of inventory measurement and excluding theoretical write-downs on LIFO-measured inventories, net of inventory write-downs and exchange differences on operating activities.

Retail

Table 22 LOTOS service station network

	Jun 30 2016	Jun 30 2015	H1 2016 / H1 2015
	478	449	+29
CODO	291	274	+17
including: LOTOS OPTIMA	122	111	+11
DOFO	187	175	+12
including: LOTOS OPTIMA	76	64	+12

As at the end of H1 2016, the LOTOS retail chain comprised 478 stations, i.e. 29 more than a year before. As part of the efforts designed to optimise the retail chain, a new brand of economy stations under the trade name LOTOS OPTIMA was launched on the domestic market in 2011. As at June 30th 2016, there were 198 service stations in the chain, up by 23 on H1 2015.

Table 23 Retail segment's key financial data (PLNm)

	H1 2016	H1 2015	H1 2016 / H1 2015
Sales volume ('000 tonnes)	639.3	563.7	13.4%
Revenue	2,714.2	2,754.4	-1.5%
EBIT	18.2	16.5	10.3%
Depreciation and amortisation	34.3	31.2	9.9%
EBITDA	52.5	47.7	10.1%

Supported by optimisation efforts, despite low fuel margins the retail segment reported an EBIT of PLN 18.2m in H1 2016, up 10.3% year on year.

Other business

Table 24 EBIT of other business⁽¹⁾ (PLNm)

	H1 2016	H1 2015	H1 2016 / H1 2015
Revenue	6.7	8.2	-18.3%
EBIT	-2.1	-0.9	-
Depreciation and amortisation	3.3	3.5	-5.7%
EBITDA	1.2	2.6	-53.8%

⁽¹⁾ Includes Energobaltic Sp. z o.o. and LOTOS Gaz S.A. w likwidacji (in liquidation).

Statement of comprehensive income

In H1 2016, the LOTOS Group earned operating profit of PLN 688.3m, including PLN 706.3m operating profit in the downstream segment, PLN -16.8m operating loss in the upstream segment, PLN -2.1m operating loss from other business and PLN 0.9m from consolidation adjustments (mainly adjustment of the unrealised margin on stocks of Rozewie and Lithuanian crudes).

Table 25 Key financial results of the LOTOS Group (PLNm)

	H1 2016	H1 2015	H1 2016 / H1 2015
Revenue	8,904.9	11,773.2	-24.4%
EBIT	688.3	836.4	-17.7%
Depreciation and amortisation	522.2	364.3	43.3%
EBITDA	1,210.5	1,200.7	0.8%
LIFO effect ⁽¹⁾	180.2	-45.6	-495.2%
LIFO-based EBIT	868.5	790.8	9.8%
Adjusted LIFO-based EBIT ⁽²⁾	571.3	696.2	-17.9%
Adjusted LIFO-based EBITDA ⁽²⁾	1,093.6	1,060.5	3.1%

⁽¹⁾ LIFO effect = LIFO-based EBIT (estimated with the LIFO method) – EBIT

In line with its inventory measurement policies, the LOTOS Group uses the weighted average method to measure change in inventories. This method defers the impact of changes in crude oil prices on the prices of finished goods. Thus, an increase in crude oil prices has a positive effect on financial performance, while a decrease adversely affects the performance. Operating results computed using this inventory measurement method are presented in the EBITDA and EBIT lines of the table. The table also presents estimated inventory decreases measured using the LIFO method, as well as the LIFO effect, LIFO-based EBIT, adjusted LIFO-based EBIT, and adjusted LIFO-based EBITDA.

PLNm	H1 2016	H1 2015
LIFO effect	180.2	-45.6
including:		
Effect of LIFO-based inventory measurement	65.6	304.9
Effect of write-downs	-261.0	-450.9
(Recognition)/reversal of theoretical write-downs on LIFO-measured inventory	375.6	100.4

⁽²⁾ EBITDA including the LIFO effect of inventory valuation and excluding recognition/reversal of theoretical write-downs on LIFO-measured inventories, net of inventory write-downs. Foreign exchange differences on operating activities, and additionally in H1 2016 net of non-recurring items, including mainly: write-off on expenditure related to the Gaz Południe licence area, including the B-21 structure in the Baltic Sea, and the PLN 75.5m impairment loss on total capitalised expenditure related to the PL643 licence.

The Group's net finance loss of PLN -104.6m reported in H1 2016 was attributable mainly to a negative balance of interest on debt, commission fees and interest income (PLN -118.4m), a net loss on measurement and settlement of market risk hedging transactions (PLN -40.0m), and foreign exchange gains (PLN 56.8m).

In H1 2015, the Group's net finance loss of PLN -349.3m was caused mainly by foreign exchange losses (PLN -187.7m), interest on borrowings and commission fees paid partly offset by interest income (PLN -100.1m), and a net loss on measurement and settlement of market risk hedging transactions (PLN -58.2m).

In the first six months of 2016, net loss on settlement and measurement of derivative instruments was PLN -40.0m, including PLN -45.0m net loss on settlement and measurement of transactions hedging the interest rate risk, PLN -5.7m net loss on settlement of futures hedging the risk of changes in prices of CO₂ emission allowances, and a positive contribution from settlement and measurement of transactions hedging petroleum product prices, exchange rates and options totalling PLN 10.7m.

**Directors' Report on the operations of the LOTOS Group in
the first half of 2016**

Table 26 Transactions hedging petroleum product prices as at June 30th 2016

Period	Product/commodity	Diesel oil	Heavy fuel oil	Crude oil	Light fuel oil
		ULSD 10ppm CIF NWE (Platts)	3.5 PCT Barges FOB Rotterdam	Brent (Dtd)	Gasoil .1 Cargoes CIF NWE / Basis ARA
Q3 2016	Volume (mt/bbl for oil)		53,424	-2,098,400	-1,680
	Price range (USD/mt)		134.25-489.5	47.48-48.92	304-479.5
Q4 2016	Volume (mt)		30,753		-1,122
	Price range (USD/mt)		134.25-489.5		304-479.5
Q1 2017	Volume (mt)		2,815		-161
	Price range (USD/mt)		202.75-488.5		404-428.5
Q2 2017	Volume (mt)	-16,050.00	46,559		-3,709
	Price range (USD/mt)	410-410	183.75-488.5		371.25-626.25
Q3 2017	Volume (mt)		50,555		-3,933
	Price range (USD/mt)		183.75-488.5		371.25-466.25
Q4 2017	Volume (mt)		25,806		-2,258
	Price range (USD/mt)		183.75-380		371.25-440
Q1 2018	Volume (mt)		2,411		-222
	Price range (USD/mt)		217.5-224.75		417-432.5
Q2 2018	Volume (mt)		26,480		-2,447
	Price range (USD/mt)		217.5-260		412-486
Q3 2018	Volume (mt)		25,255		-2,335
	Price range (USD/mt)		217.5-260		412-486
Q4 2018	Volume (mt)		7,958		-736
	Price range (USD/mt)		217.5-260		412-486

Table 27 Transactions hedging foreign exchange risk as at June 30th 2016

Currency pair	Instrument	Volume	Currency	Exchange rate range
EUR/USD exchange rates	Forward	181,199,999	EUR	1.0887 - 1.1361
EUR/PLN exchange rate	Forward	-30,883,039	EUR	4.3322 - 4.4628
USD/PLN exchange rate	Forward	-121,500,000	USD	3.8304 - 4.0513

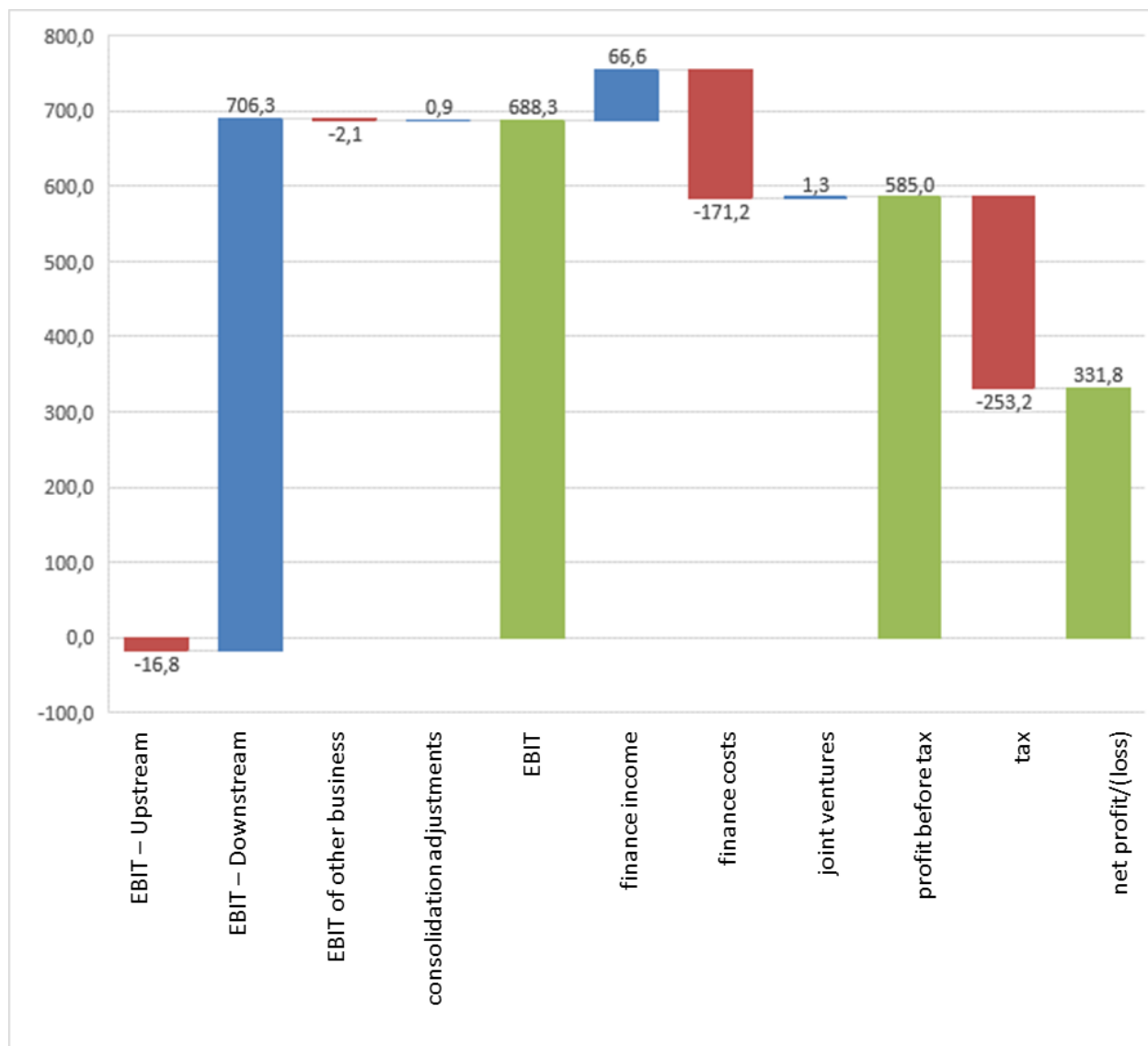
Table 28 Transactions hedging interest rate risk as at June 30th 2016

Instrument	Start date	End date	Notional amount	Currency	Interest rate range	Reference rate
IRS	from Jul 15 2011 to Sep 21 2021	from Dec 21 2016 to Dec 21 2021	559,000,019	USD	1.52% - 4.045%	3M LIBOR – 6M LIBOR

Table 29 Futures contracts hedging the risk related to prices of carbon dioxide (CO₂) emission allowances as at June 30th 2016

		2016		2017		2018		2019	
		Volume (mt)	Price range (EUR/mt)	Volume (mt)	Price range (EUR/mt)	Volume (mt)	Price range (EUR/mt)	Volume (mt)	Price range (EUR/mt)
EUAs	Futures	201	4.92-7.83	689,000	4.86-8.29	905,000	5.54-5.67	33,000	8.57-8.6

Chart 2 Structure of LOTOS Group's consolidated results (PLNm)



Profit before tax earned in H1 2016 was PLN 585.0m, and consolidated net profit of the LOTOS Group was PLN 331.8m.

Table 30 EBIT, profit/(loss) before tax, and net profit/(loss) of the LOTOS Group (PLNm)

	H1 2016	H1 2015	H1 2016 / H1 2015
EBIT	688.3	836.4	-17.7%
Finance income	66.6	13.7	386.1%
Finance costs	-171.2	-363.0	-52.8%
Other	1.3	-0.9	-244.4%
Profit/(loss) before tax	585.0	486.2	20.3%
Net profit/(loss)	331.8	377.2	-12.0%

Consolidated statement of financial position

Table 31 Consolidated statement of financial position – assets (PLNm)

	Jun 30 2016	Dec 31 2015	Change	%
Total assets	19,082.8	19,169.3	-86.5	-0.5%
Non-current assets	12,465.8	12,437.7	28.1	0.2%
Property, plant and equipment	10,664.6	10,568.4	96.2	0.9%
Goodwill	46.7	46.7	0.0	0.0%
Other intangible assets	632.7	617.7	15.0	2.4%
Equity-accounted joint ventures	91.5	70.7	20.8	29.4%
Deferred tax assets	768.3	924.5	-156.2	-16.9%
Derivative financial instruments	30.4	8.7	21.7	249.4%
Other non-current assets	231.6	201.0	30.6	15.2%
Current assets	6,607.7	6,723.2	-115.5	-1.7%
Inventories	3,323.2	3,235.8	87.4	2.7%
Trade receivables	1,944.3	1,550.9	393.4	25.4%
Current tax assets	5.5	12.0	-6.5	-54.2%
Derivative financial instruments	26.1	208.5	-182.4	-87.5%
Other current assets	722.8	856.3	-133.5	-15.6%
Cash and cash equivalents	585.8	859.7	-273.9	-31.9%
Assets held for sale	9.3	8.4	0.9	10.7%

As at June 30th 2016, total assets of the LOTOS Group were PLN 19,082.8m, having decreased by PLN 86.5m in H1 2016.

Key changes in assets:

- PLN 393.4m increase in trade receivables, mainly due to higher product prices and a higher US dollar exchange rate in June 2016 compared with December 2015,
- PLN 273.9m decline in cash and cash equivalents and PLN 133.5m decrease in other current assets, mainly due to the implementation of the EFRA Project,
- PLN 160.7m decrease in positive fair value of financial instruments,
- PLN 96.2m increase in property, plant and equipment due to implementation of investment projects.

Table 32 Consolidated statement of financial position – sources of funding (PLNm)

Equity and liabilities	Jun 30 2016	Dec 31 2015	Change	%
	19,082.8	19,169.3	-86.5	-0.5%
Equity	8,016.6	7,712.2	304.4	3.9%
Share capital	184.9	184.9	0.0	0.0%
Share premium	2,228.3	2,228.3	0.0	0.0%
Cash flow hedging reserve	-728.3	-700.9	-27.4	3.9%
Retained earnings	6,260.3	5,928.5	331.8	5.6%
Translation differences	71.3	71.3	0.0	0.0%
Non-controlling interests	0.1	0.1	0.0	0.0%
Non-current liabilities	5,753.2	6,031.2	-278.0	-4.6%
Borrowings, other debt instruments and finance lease liabilities	4,216.6	4,454.5	-237.9	-5.3%
Derivative financial instruments	66.4	54.3	12.1	22.3%
Deferred tax liabilities	38.4	47.6	-9.2	-19.3%
Employee benefit obligations	188.2	182.2	6.0	3.3%
Other liabilities and provisions	1,243.6	1,292.6	-49.0	-3.8%
Current liabilities	5,313.0	5,425.9	-112.9	-2%
Borrowings, other debt instruments and finance lease liabilities	1,900.5	2,544.8	-644.3	-25.3%
Derivative financial instruments	79.4	110.8	-31.4	-28.3%
Trade payables	1,580.0	1,232.5	347.5	28.2%
Current tax payables	6.7	11.8	-5.1	-43.2%
Employee benefit obligations	100.5	122.2	-21.7	-17.8%
Other liabilities and provisions	1,645.9	1,403.8	242.1	17.2%

Consolidated equity increased by PLN 304.4m as at June 30th 2016, mainly due to:

- PLN 331.8m increase in retained earnings attributable to the net profit earned in H1 2016,
- PLN -27.4m foreign exchange losses on measurement of cash flow hedges adjusted for the tax effect and charged to reserve capital.

In H1 2016, liabilities decreased by PLN 390.9m, mainly due to:

- PLN 882.2m decrease in interest-bearing borrowings, other debt instruments and finance lease liabilities, mostly related to repayment of investment credit facilities (mainly at Grupa LOTOS S.A. and upstream companies) and lower amounts outstanding under overdraft facilities (mainly at Grupa LOTOS S.A.),
- PLN 347.5m increase in trade payables related to oil purchases,
- PLN 193.1m higher other liabilities and provisions, including mainly liabilities to the state budget (VAT at Grupa LOTOS S.A.).

As at June 30th 2016, the LOTOS Group's financial debt totalled PLN 6,117.1m, down PLN 882.2m on December 31st 2015. The ratio of financial debt adjusted for free cash (including cash earmarked to pursue the objectives of the issue of Series D shares) to equity was 66.9% (down 7.0pp on December 31st 2015).

Consolidated statement of cash flows

Table 33 Cash flows (PLNm)

PLNm	H1 2016	H1 2015	Change
Cash flows from operating activities	950.0	521.3	428.7
Cash flows from investing activities	-436.5	-809.1	372.6
Cash flows from financing activities	-279.6	606.5	-886.1
Effect of exchange rate fluctuations on cash held	-1.5	1.1	-2.6
Change in net cash	232.4	319.8	-87.4
Cash and cash equivalents at beginning of period	278.1	-166.7	444.8
Cash and cash equivalents at end of period	510.5	153.1	357.4

As at June 30th 2016, the LOTOS Group's cash balance (including current account overdrafts) was PLN 510.5m.

In H1 2016, net cash flows from operating activities were positive at PLN 950.0m, driven mainly by net profit before depreciation and amortisation. They also reflect higher trade receivables offset by an increase in trade payables.

The negative balance of cash flows from investing activities of PLN -436.5m was mainly attributable to acquisition of property, plant and equipment and other intangible assets, mostly in connection with the EFRA Project as well as oil and gas production from the B8 field in the Baltic Sea. Some of the investment expenditure incurred in H1 2016 on the EFRA Project was financed with cash held in a separate bank account; the transfer of funds to the separate bank account was reflected in the cash flows from investing activity in H1 2015.

Net cash flows from financing activities, of PLN -279.6m, mainly comprise net repayments of borrowings and related outflows on principal and interest payments of PLN -423.8m, offset in part by gain on settlement of financial instruments of PLN 158.1m.

Financial resources management

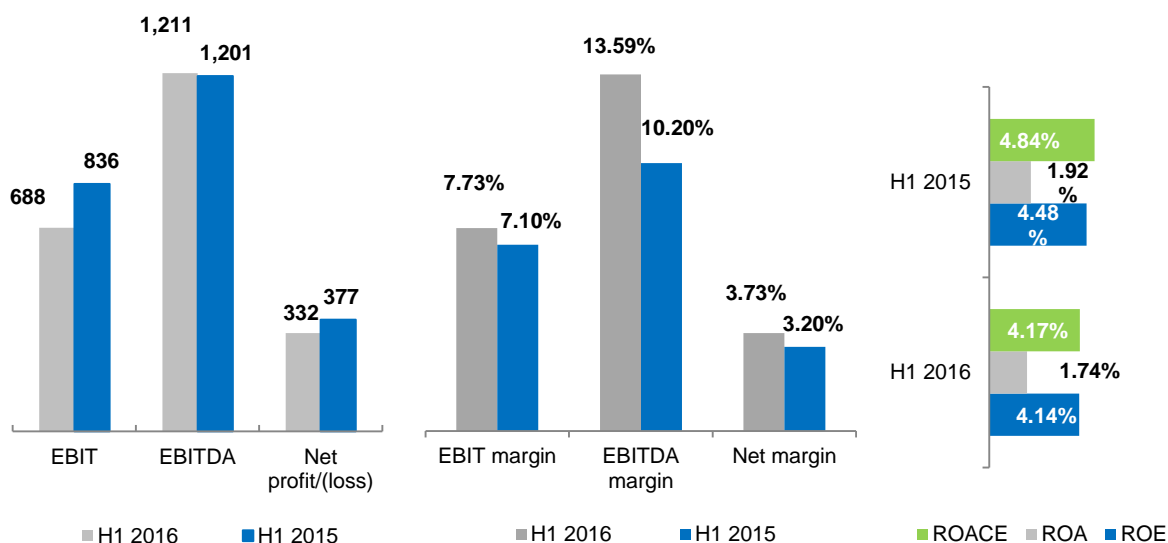
Ability to meet obligations

In H1 2016, the LOTOS Group was able to meet all its liabilities towards third parties.

Information material for assessment of the Group's assets, financial standing and financial performance

A brief assessment of the LOTOS Group's overall economic and financial standing has been prepared in the form of a ratio analysis covering margins, liquidity, turnover and debt levels.

Profitability ratios

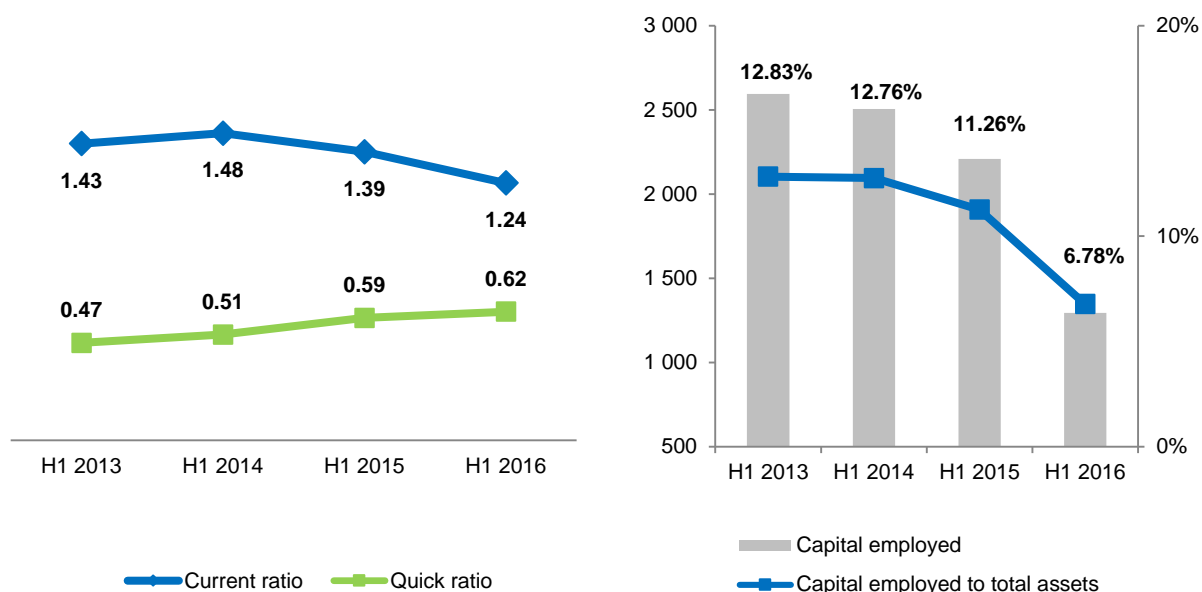


- operating and net profit ratios improved due to stronger decline in revenue (down 24.4%) than in operating profit (down 17.7%) and net profit (down 12.0%) compared with H1 2015,
- ROE and ROA decreased as net profit fell more (down 12.0%) than equity (down 4.8%) and assets (down 2.8%).

Profitability ratio formulas

EBIT margin	operating profit/(loss) to net sales
EBITDA	EBIT before amortisation/depreciation
EBITDA margin	EBITDA to net sales
Net margin	net profit/(loss) to net sales
ROE	net profit/(loss) to equity at end of period
ROA	net profit/(loss) to assets at end of period
Return on average capital employed (ROACE)	operating profit/(loss) after tax to equity plus net debt at end of period

Liquidity ratios



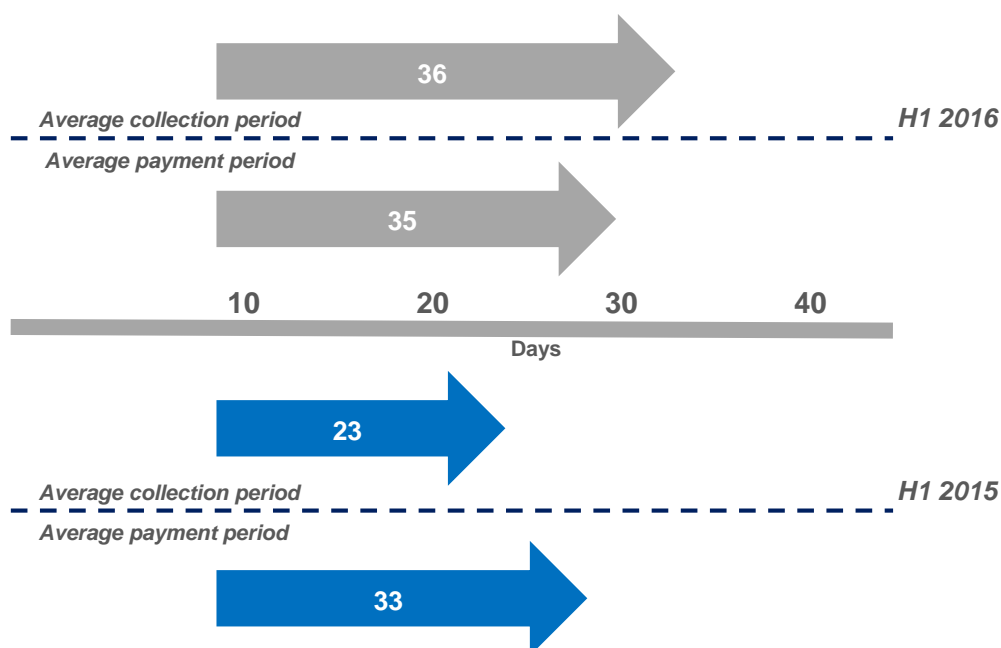
- lower current ratio (down 10.8%) as current assets decreased more (down 16.2%) than current liabilities (down 6.5%),
- higher quick ratio (up 5.1%) following slight decrease in current assets excluding inventories (down 2.1%) compared with the decrease in current liabilities (down 6.5%),
- 41.4% decrease in capital employed, following stronger decrease in current assets (down PLN 1,281.4m) than the decrease in current liabilities (down PLN 366.9m), and decrease of the share of capital employed in total assets.

Liquidity ratio formulas

Current ratio	current assets to current liabilities (at period end)
Quick ratio	current assets less inventory to current liabilities (at period end)
Capital employed	current assets less current liabilities (at period end)
Capital employed to total assets	capital employed to total assets (at period end)

Collection and payment periods

(days)



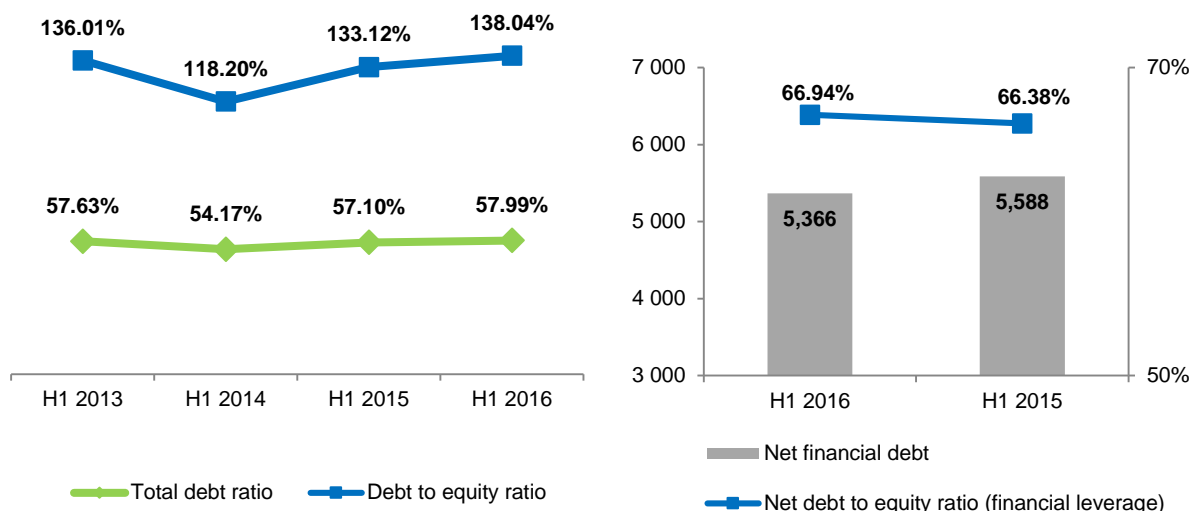
longer collection period (by 13 days) as average trade receivables increased (up 15.8%) while revenue decreased (down 24.4%),

longer payment period (by 2 days) as average trade payables decreased (down 22.7%) less than cost of sales (down 27.7%).

Collection and payment period formulas

Average collection period (days)	average trade receivables to net sales times 182/181 days in the period
Average payment period (days)	average trade payables to cost of sales times 182/181 days in the period

Capital structure and debt ratios



- 0.9pp increase in debt ratio as assets decreased (down 2.8%) more than liabilities (mainly bank borrowings) (down 1.3%),
- lower net financial debt (down PLN 222.1m) mainly related to lower amounts outstanding under overdraft facilities and repayment of investment credit facilities,
- increase in debt to equity ratio by 4.9pp, mainly due to stronger decrease in equity.

Capital structure and debt ratio formulas

Total debt ratio	total liabilities to total assets (at period end)
Net financial debt	current and non-current borrowings, other debt instruments, and finance lease liabilities less cash and cash proceeds from the issue of shares presented under other financial assets (at period end)
Net debt to equity ratio (financial leverage)	net financial debt to equity (at period end)
Debt to equity ratio	total liabilities to equity (at end of period)

2.2. FACTORS WHICH, IN THE COMPANY'S OPINION, WILL DETERMINE THE GROUP'S PERFORMANCE IN THE FOLLOWING QUARTERS

Key factors which, in the Company's opinion, may affect performance in the following quarters, include:

- Macroeconomic environment; in particular, prices of crude oil and petroleum products and the USD/PLN exchange rate, which has a bearing on the Group's financial performance as the prices of crude oil and of some products are quoted in the US dollar and Grupa LOTOS S.A. has US dollar-denominated debt,
- Supply of and demand for petroleum products in Poland and Europe,
- Execution of projects in the exploration and production segment,
- Completion of ongoing projects in the refining business,
- Optimisation measures in the downstream segment to maximise the refining margin of Grupa LOTOS S.A.,

- Further consolidation of the LOTOS Group's market position, with special focus on the development of, and improvement of profitability in the retail segment,
- Changes in tax regulations - the entry into force on 1 September 2016. Act of July 6, law on retail tax sales. According to this legislation monthly revenue from retail sales (excluding VAT) will be subject to taxation, ie sales to private individuals. The law provides for tax-free amount of 17 million PLN per month and provides for two rates of tax on retail sales - 0.8% of revenue between 17 and 170 million PLN per month and 1.4% on income above 170 million PLN per month.

In the reported period, work continued on the LOTOS Group's Strategy for the following years. Key assumptions of the Strategy are as follows:

- to resume dividend payments and sustain long-term dividend paying capacity,
- to sustainably and effectively develop complementary business segments,
- to continue efforts to optimise integrated margin,
- to advance Poland's energy security thanks to economic benefits from diversified supplies.

2.3. RISKS AND THREATS RELEVANT TO THE COMPANY'S BUSINESS IN THE PERIOD UNTIL THE END OF 2016

The factors discussed in Section 2.2. relate to the most important groups of risks that may affect the LOTOS Group's operations in H2 2016.

For a more detailed description of the risk management policy and of the Enterprise Risk Management (ERM) system in place at the Company, see Directors' Report on the LOTOS Group's Operations in 2015.

2.4. MANAGEMENT BOARD'S POSITION ON THE FEASIBILITY OF MEETING PREVIOUSLY PUBLISHED FORECASTS FOR 2016

Grupa LOTOS S.A. has not published any separate or consolidated forecasts for 2016.

3. MANAGEMENT BOARD'S REPRESENTATION

3.1. ON THE HALF-YEAR FINANCIAL STATEMENTS AND THE DIRECTORS' REPORT ON THE OPERATIONS OF THE LOTOS GROUP

The Management Board of LOTOS S.A., composed of:

Robert Pietryszyn – President of the Management Board, Chief Executive Officer

Mateusz Aleksander Bonca – Vice President of the Management Board, Chief Strategy and Development Officer

Marcin Jastrzębski – Vice President of the Management Board, Chief Exploration and Production Officer

Mariusz Machajewski – Vice President of the Management Board, Chief Financial Officer

Przemysław Marchlewicz – Vice-President of the Management Board for Corporate Affairs

hereby represents that, to the best of their knowledge, the half-year condensed consolidated financial statements of the LOTOS Group and the half-year condensed financial statements of Grupa LOTOS S.A. for the six months ended June 30th 2016 as well as the comparative data were prepared in compliance with the applicable accounting standards and give a true, clear and fair view of the assets, financial standing and financial performance of the LOTOS Group and Grupa LOTOS S.A.

Furthermore, the Management Board of Grupa LOTOS S.A. represents that the Directors' Report on the operations of the LOTOS Group in H1 2016 gives a true view of the Group's development, achievements and position, and includes a description of key risks and threats.

3.2. REPRESENTATION ON APPOINTMENT OF THE QUALIFIED AUDITOR OF FINANCIAL STATEMENTS

The Management Board of Grupa LOTOS S.A. represents that the qualified auditing firm which reviewed the half-year condensed consolidated financial statements of the LOTOS Group and the half-year condensed financial statements of Grupa LOTOS S.A. for the six months ended June 30th 2016 was appointed in accordance with the applicable laws, and that the auditing firm and the auditors who performed the review met the conditions necessary to issue an impartial and independent review report in accordance with the applicable regulations and professional standards.

4. OTHER INFORMATION

4.1. COURT, ARBITRATION OR ADMINISTRATIVE PROCEEDINGS

In H1 2016 no court, arbitration or administrative proceedings were pending concerning the Issuer's or its subsidiary's liabilities or debts whose value pertaining to the LOTOS Group would equal or exceed 10% of the Company's equity. Material court, arbitration or administrative proceedings and other risks are discussed in Note 23.1 to the interim condensed consolidated financial statements for the six months ended June 30th 2016.

4.2. MATERIAL RELATED-PARTY TRANSACTIONS

In H1 2016, Grupa LOTOS S.A. executed transactions with related parties at arm's length only, as presented in Note 24.1 to Grupa LOTOS S.A.'s interim condensed financial statements for the six months ended June 30th 2016.

4.3. SURETIES FOR REPAYMENT OF LOANS, GUARANTEES AND BORROWINGS, FACTORING AGREEMENTS, AND OTHER SECURITY INSTRUMENTS

On July 17th 2015, the Company deposited two promissory notes issued by the Company for up to PLN 40,000 thousand and PLN 200,000 thousand, respectively, with the Head of the Customs Office in Gdańsk. The promissory notes were deposited as lump-sum security for future liabilities related to excise duty of PLN 800,000 thousand, valid until August 19th 2017.

An unconditional and irrevocable guarantee issued by LOTOS Petrobaltic S.A. for the benefit of the government of Norway on June 17th 2008, concerning the activities of LOTOS Exploration and Production Norge AS related to its exploration and production operations on the Norwegian Continental Shelf, was effective as at June 30th 2016 and December 31st 2015. In the guarantee, LOTOS Petrobaltic S.A. undertook to assume any financial liabilities which may arise in connection with the operations of LOTOS Exploration and Production Norge AS on the Norwegian Continental Shelf, consisting in exploration for and extraction of the natural resources from the sea bottom, including their storage and transport using means of transport other than ships.

**Directors' Report on the operations of the LOTOS Group in
the first half of 2016**

Table 34. Intra-group loans advanced in the six months ended June 30th 2016 in the LOTOS Group

Lender	Borrower	Agreement date	Principal as per loan agreement		Amount outstanding as at June 30th 2016		Date of partial repayment	Financial terms (interest rate, interest payment schedule, etc.)	Type of security
			PLN	Currency	PLN	Currency			
			('000)	('000)	('000)	('000)			
Grupa LOTOS S.A.	LOTOS Petrobaltic S.A.	Feb 1 2016	36,000	-	36,000	-	Dec 31 2016	6M WIBOR + margin	blank promissory note with a 'protest waived' clause and promissory note declaration
		May 31 2016	54,000	-	30,000	-			
LOTOS Exploration and Production Norge AS	LOTOS Petrobaltic S.A.	Feb 4 2016	-	USD 15,000	59,704	USD 15,000	Jan 31 2017	6M LIBOR + margin	blank promissory note with a 'protest waived' clause and promissory note declaration
TOTAL					66,000	-			
					59,704	USD 15,000			
			90,000	USD 15,000	125,704				

4.4 REPORTABLE CONTRACTS WITH A VALUE EXCEEDING 10% OF EQUITY

- In a current report, the Company announced that in the twelve months to March 18th 2016 Grupa LOTOS executed contracts with Varo Energy Supply Trading B.V. for an aggregate amount of approximately USD 193m, VAT-exclusive (ca. PLN 731m translated at the USD/PLN mid rate quoted by the National Bank of Poland for March 18th 2016), which meets the reporting threshold for significant agreements of 10% of Grupa LOTOS' equity. On November 26th 2015, Grupa LOTOS S.A. and Varo Energy Supply Trading B.V. signed a contract for sale of unleaded gasoline to Varo Energy (the highest-value transaction from among the above contracts). Its value is estimated at approximately USD 102m, VAT-exclusive (ca. PLN 386m translated at the USD/PLN mid rate quoted by the National Bank of Poland for March 18th 2016).
For more information, see [Current Report No. 11/2016](#).
- In the period from January 29th 2015 to January 27th 2016, Grupa LOTOS S.A. entered into contracts with Petraco Group companies for an aggregate amount of approximately PLN 759m, which is above the reporting threshold for significant agreements (more than 10% of Grupa LOTOS S.A.'s equity). On July 17th 2015, Grupa LOTOS S.A. and Petraco Oil Company LLP of Lugano concluded a spot contract for the supply of crude oil to Grupa LOTOS S.A. (the highest-value contract from among the contracts with Petraco Group companies). Its value is estimated at PLN 149m. The contract does not include any condition or date precedent or provide for any contractual penalties, and its terms and conditions do not differ from the terms and conditions commonly applied in contracts of this type.
For more information, see [Current Report No. 4/2016](#).
- Further to Current Report No. [36/2013](#) of December 20th 2013, the Company announced that on January 22nd 2016 Grupa LOTOS S.A. and Rosneft Oil Company of Moscow, signed an annex ("Annex") to the term contract of December 20th 2013 for crude oil supplies to Grupa LOTOS S.A. The Annex covers supplies to be delivered in 2016–2017, providing that they should reach 5.4m–6.0m tonnes of crude oil. Pursuant to the Annex, the supplies will be transported via the Druzhba pipeline or by sea. The value of supplies covered by the Annex is estimated at approximately PLN 5.0bn as at the Annex date. The contract provides for compensation in the event of failure to deliver, or take delivery of, the crude oil, in an amount not exceeding approximately PLN 2.8m on an average monthly basis relative to the agreed annual volumes. Payment of the compensation does not preclude the parties' right to seek further damages. The terms and conditions of the contract do not differ materially from the terms and conditions customarily applied in contracts of such type.
For more information, see [Current Report No. 2/2016](#).