

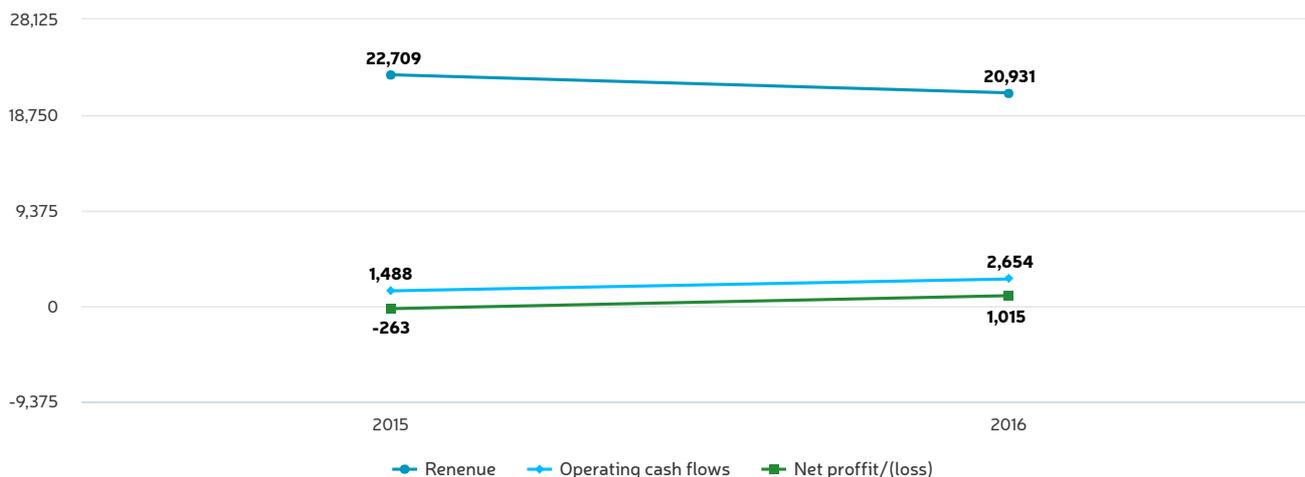
Our performance – discussion of the LOTOS Group’s financial position

[G4-EC1] [G4-9]

- In 2016, the LOTOS Group improved its operating performance again.
- Consolidated revenue amounted to PLN 20.9bn.
- Adjusted LIFO-based EBITDA was at a record high, at PLN 2.59bn.
- The LOTOS Group’s consolidated net profit was the highest on record and exceeded PLN 1bn.
- The LOTOS Group’s debt was reduced by a healthy PLN 4.8bn net.

At the LOTOS Group, we consistently strive to increase operational efficiency, which, coupled with the favourable macro environment in 2016, contributed to the LOTOS Group’s sound operating performance.

Strong financial performance, particularly cash flows

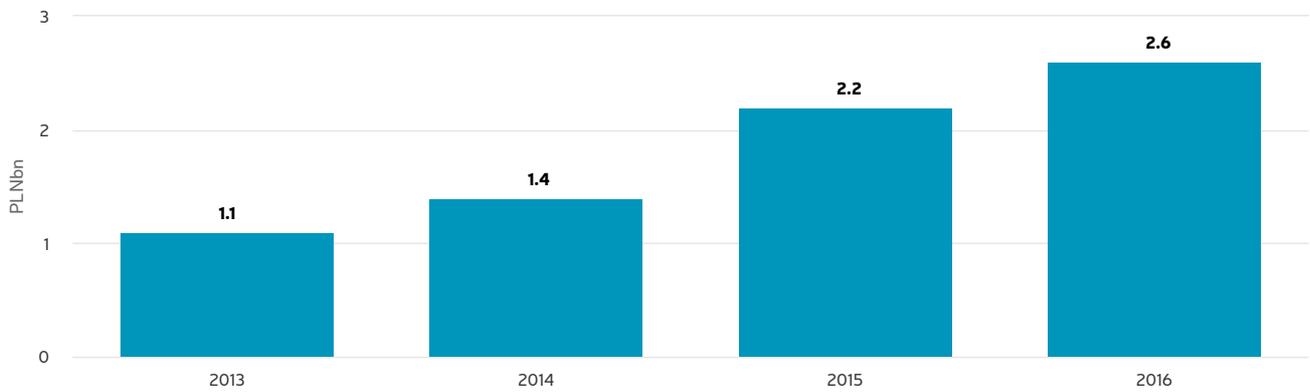


In 2016, the LOTOS Group **improved its operating performance again**. Consolidated revenue was **PLN 20,931m**. Adjusted LIFO-based EBITDA was at a record high at **PLN 2.59bn**. In 2016, the LOTOS Group earned a consolidated net profit of **PLN 1,015m**.

Record-high LIFO-based EBITDA

In 2012–2015, adjusted LIFO-based EBITDA averaged PLN 1.67bn, while in 2015 it grew to PLN 2.16bn and in 2016 to a record high of **PLN 2.59bn**. This continued growth of EBITDA lends credibility to the LOTOS Group’s objectives outlined in the new business strategy for 2017–2022: the target for 2018–2019 is average annual LIFO-based EBITDA of PLN 2.2–2.6bn, and we plan to increase it in 2020–2022 to **PLN 3.8–4.4bn**.

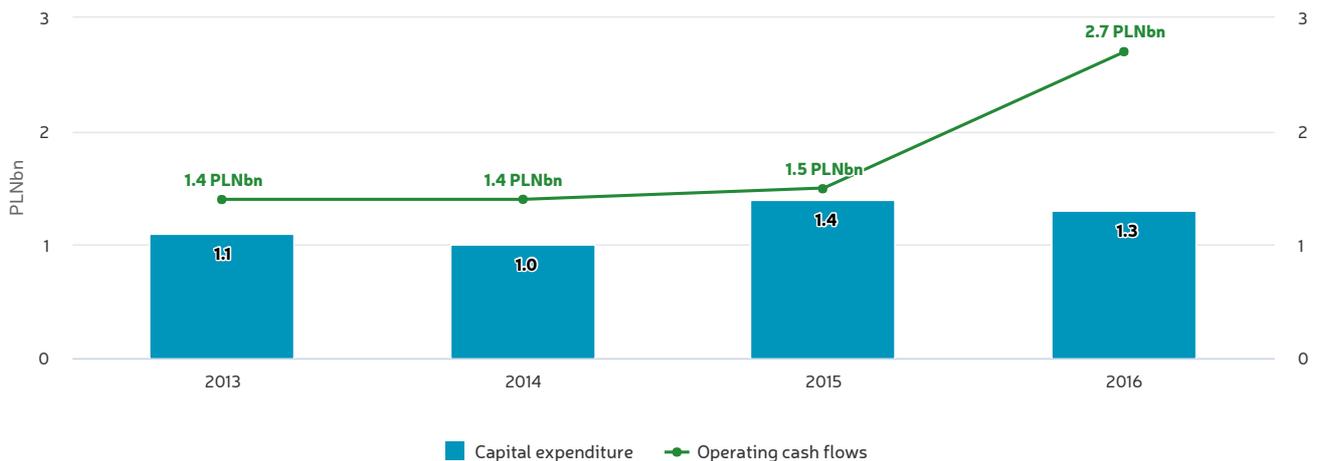
LIFO-based EBITDA



Strong operating cash flows

The LOTOS Group generated positive cash flows from operating activities of **PLN 2,653.9m** (up PLN 1,165.9m on 2015), mainly on net profit before depreciation and amortisation, income tax, and higher trade payables, which were offset by lower trade receivables. High-quality assets generate operating cash flows which are then used to finance business development projects.

Operating cash flows and capex



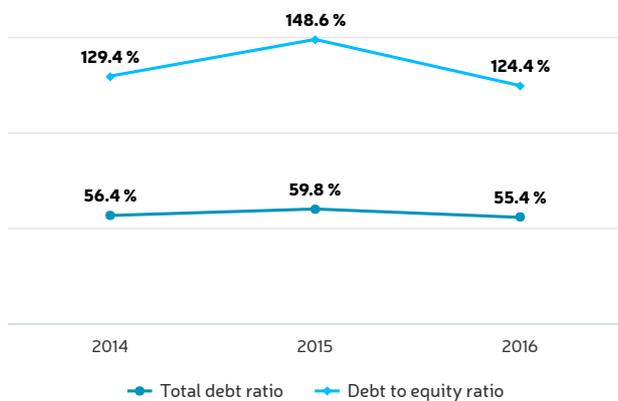
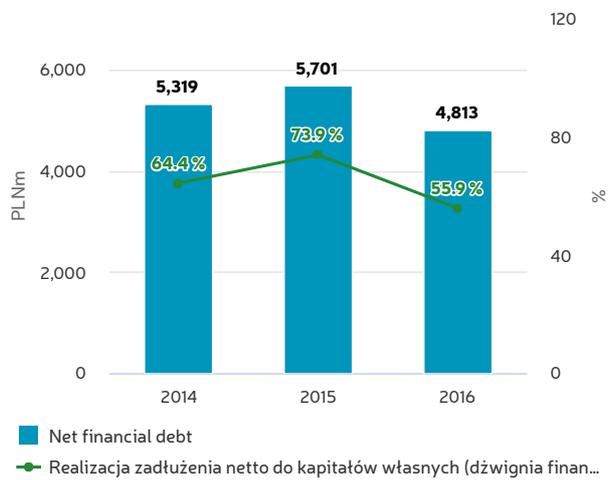
Revenue

In 2016, the LOTOS Group posted **PLN 20,931.1m** in revenue (down 7.8% on 2015), driven mainly by lower prices of crude oil and petroleum products on global markets. Average net revenue **per tonne/(toe) of products sold in 2016 was PLN 1,761** (down PLN 261, or 12.9%, on 2015). The total volume of petroleum products, merchandise and materials sold in 2016 by the LOTOS Group increased by approximately 6% on 2015.

Debt reduction

In 2016, we managed to reduce our debt to a level that will give us more comfort with implementing our strategic objectives, i.e. to **PLN 4.8bn**.

Capital structure and debt ratios (PLNm or %)



Debt fell as a result of:

- Decrease of 4.3pp in the share of liabilities in the financing of assets, as liabilities went down by 6.5% and assets grew by 0.8%,
- Decrease of 18.0pp in net debt to equity ratio (financial leverage), as net financial debt fell by 15.6% while equity grew by 11.7%,
- Decrease of 24.1pp in debt to equity ratio, as liabilities fell by 6.5% and equity went up by 11.7%.

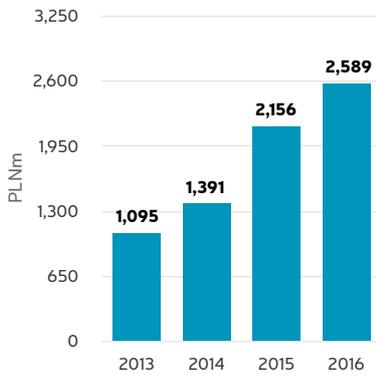
More information

[Directors' Report on the operations of Grupa LOTOS S.A. and the LOTOS Group in 2016](#)

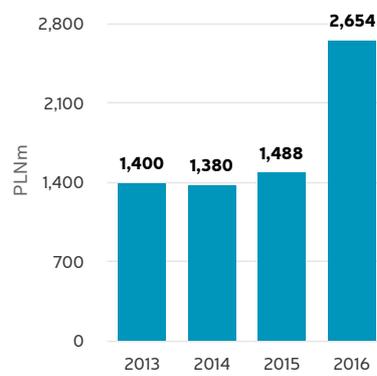
Chapter 5.3. Financing

Grupa LOTOS shares on the Warsaw Stock Exchange

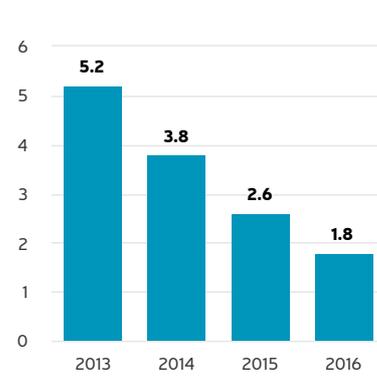
Adjusted LIFO-based EBITDA



Operating cash flow



Net debt to adjusted LIFO-based EBITDA



More information

[Directors' Report on the operations of Grupa LOTOS S.A. and the LOTOS Group in 2016](#)

Chapter 5. Financial standing of Grupa LOTOS S.A. and its Group

Grupa LOTOS shares have been listed on the Warsaw Stock Exchange since June 2005, and are included in the WIG20 index of WSE's 20 blue chips, the WIG-Paliwa index of the fuel market, and the RESPECT Index of socially-responsible companies.

Grupa LOTOS stock performance since IPO

Grupa LOTOS share price (PLN) and trading volume (number of shares)



Factors affecting the price, including key events at Grupa LOTOS:

In 2016, the situation on capital markets, including in Poland, was largely affected by global economic developments. The most important events were:

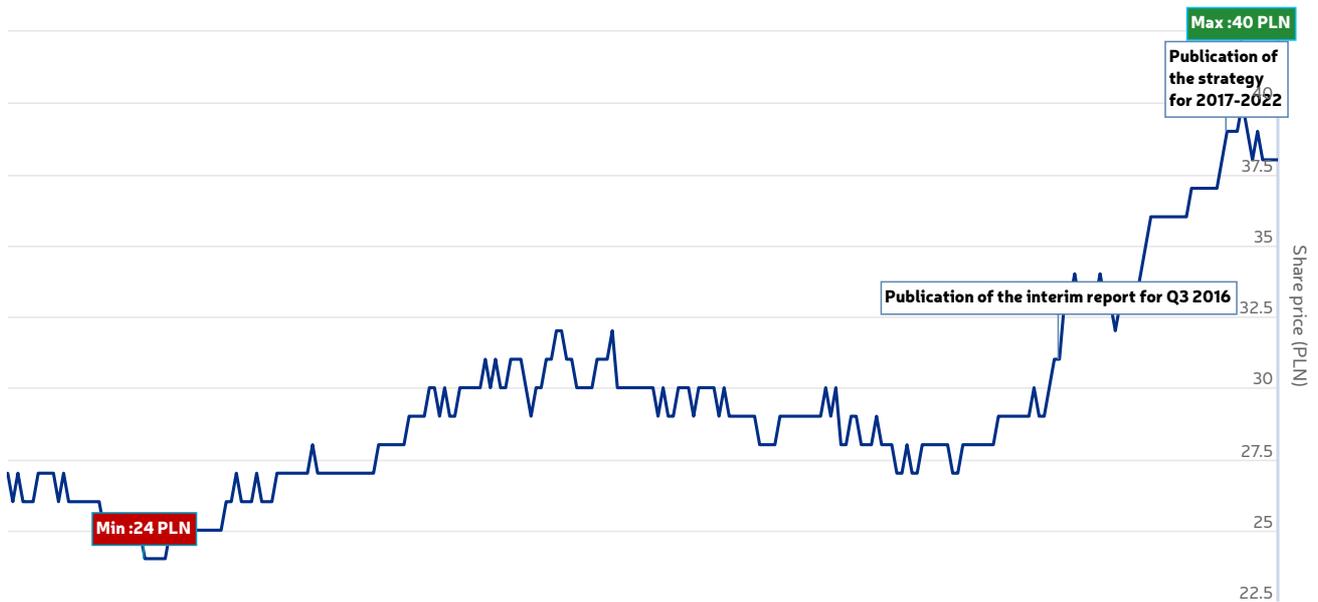
- Brexit and uncertainty about the scale of its consequences,
- The Presidential election and the prospect of interest rate hikes in the US,
- Risk of revision of Poland's credit rating by rating agencies,

- Concerns about the future of open-ended pension funds,
- Reduction of the grey market for fuels through new regulations,
- No final decision on the conversion of CHF-denominated loans.

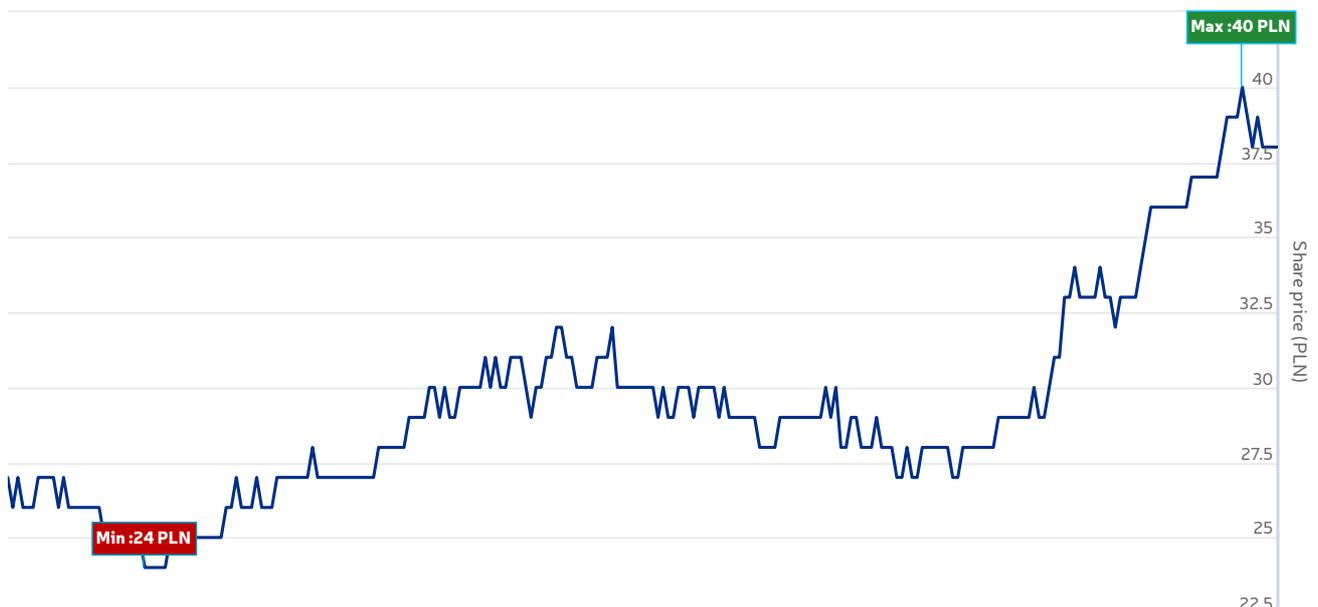
The combination of those factors drove the situation on the Warsaw Stock Exchange. For most of the year, the WSE's main index (WIG) maintained a slight (single digit) growth, to accelerate only at its end. Over the full twelve months of 2016 WIG rose **14%**.

In 2016, Grupa LOTOS traded in the range **from PLN 24.10 to PLN 40.40** (2015: from PLN 22.90 to PLN 33.50), and the year's closing price was **PLN 38.25**, compared with PLN 27 in 2015. Over the whole of 2016, the price went up **46%**.

The price of Grupa LOTOS shares increased in response to information on the **financial performance for Q3 2016**, announced towards the end of October, when the Company's **EBIT** proved better than expected. This improvement was supported by the effects of new regulations which **helped curb the grey market for fuels**, to the advantage of Grupa LOTOS. The publication of the LOTOS Group's **new business strategy for 2017–2022** on December 15th 2016 was well received by investors, pushing up the share price during the last two weeks of 2016.



Grupa LOTOS share price in 2016



Structure of broker recommendations on Grupa LOTOS shares in 2016

The target price of Grupa LOTOS shares in brokers' research reports fluctuated from PLN 24.00 to PLN 41.20, compared with PLN 22.90 to PLN 33.50 in 2015. The average target price in 2016 was PLN 31.26 (2015: PLN 30.47).

Brokers issued 12 recommendations on the Company shares in 2016:

- 4 BUY recommendations
- 3 ACCUMULATE recommendations
- 2 HOLD recommendations
- 2 NEUTRAL recommendations
- 1 SELL recommendation.

Broker recommendations and moving average of target prices against the market price of Company shares

Zoom

From To



Grupa LOTOS share price performance vs WIG, WIG20, WIG Paliwa and RE-SPECT Index [%]



In 2016, Grupa LOTOS outperformed the market as a whole.

More information

[Directors' Report on the operations of Grupa LOTOS S.A. and the LOTOS Group in 2016](#)

Chapter 8.1. Grupa LOTOS shares on the Warsaw Stock Exchange

Dividends paid by Grupa LOTOS

One of the objectives of the Company's 2017–2022 strategy is to maintain dividend payment capacity.

In 2006–2016, the Company paid a dividend twice. The first distribution was for 2006 and totalled PLN 40,932 thousand, with dividend per share at PLN 0.4 and dividend yield of 0.7%. On June 14th 2017, the Annual General Meeting of Grupa LOTOS resolved to pay a dividend for 2016, in the amount of PLN 184,873.4 thousand. Dividend per share was PLN 1.0 and dividend yield was 2.61%.

Dividend and dividend yield in 2005–2016

Financial year	Dividend (PLN)	Dividend per share (PLN)	Share price at the year end (PLN)	Dividend yield (%)
2005	0	0	44,2	-
2006	40,932,000	0,36	49,3	0,73
2007	0	0	44,5	-
2008	0	0	12	-
2009	0	0	31,8	-
2010	0	0	36,4	-
2011	0	0	23,3	-
2012	0	0	41,2	-
2013	0	0	35,3	-
2014	0	0	25,5	-
2015	0	0	27	-
2016	184,873,362	1	38,25	2,61

Historical dividend per share (PLN)

Financial year	Dividend per share (PLN)	% of net profit	Dividend record date ¹	Dividend payment date ²
2005	0	0.00	-	-
2006	0,36	10,06	Jun 11 2007	not later than Jul 31 2007
2007	0	0	-	-
2008	0	0	-	-
2009	0	0	-	-
2010	0	0	-	-
2011	0	0	-	-
2012	0	0	-	-
2013	0	0	-	-
2014	0	0	-	-
2015	0	0	-	-
2016	1	15,92	Sep 12 2017	Sep 29 2017

¹ Dividend record date is the date as at which the list of shareholders entitled to receive a dividend for a given financial year is determined.

² Dividend payment date is the date on which a dividend is paid to the Company's shareholders.

More information

Directors' Report on the operations of Grupa LOTOS S.A. and the LOTOS Group in 2016

Chapter 8.3, 8.4, 8.5

Grupa LOTOS included in the index of socially-responsible companies for the 10th time

In 2016 again, for the 10th time, Grupa LOTOS shares became a constituent of the WSE's RESPECT Index – an index of responsible companies operating in accordance with exacting CSR standards in the areas of corporate governance, information policy and relations with investors, the environment, society and employees.

Grupa LOTOS has been present in the RESPECT Index since its inception in 2009. To date, the WSE has announced ten editions of the index. The most recent one, announced at the end of 2016, includes 25 companies. Since its first publication in 2009, the RESPECT index has increased by 50%.

Comments

In 2016, cost of sales of the LOTOS Group stood at PLN 17,215.7m (down 15.0% on 2015). In the same period, the estimated unit cost of sales was PLN 1,448/t (down PLN 355/t or 19.7% on 2015). The unit sales margin in 2016 came at PLN 313/t (up 42.9% on 2015). The LOTOS Group's consolidated gross profit for 2016 was PLN 3,715.4m (up PLN 1,255.0m, or 51.0% on 2015).

Administrative expenses decreased by PLN 33.2m (down 7.5% on 2015) mainly on lower employee benefits expense.

In 2016, the LOTOS Group reported net other expenses of PLN -143.7m, including chiefly:

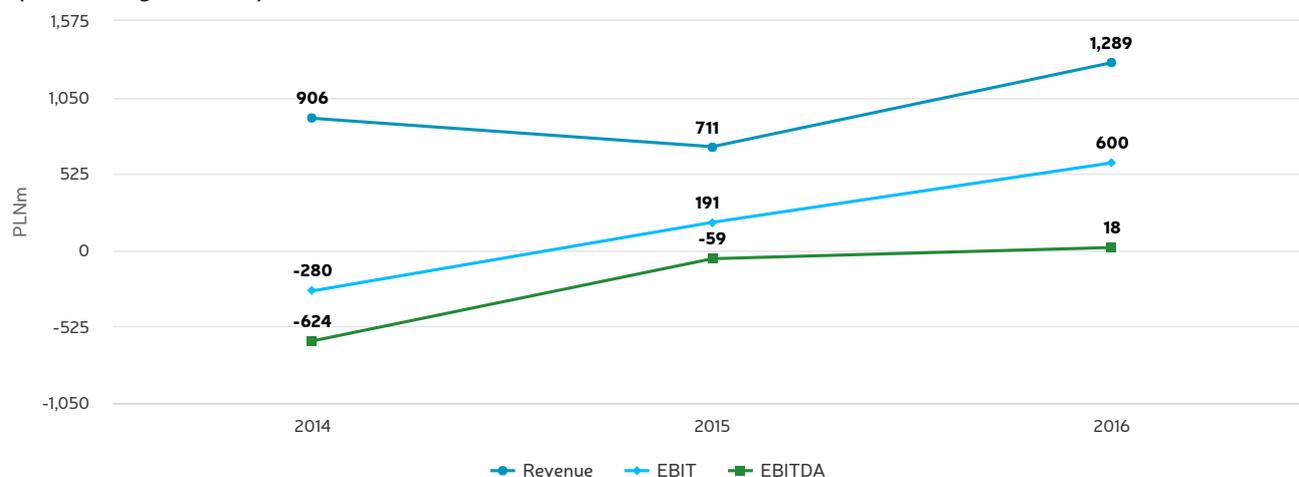
- PLN -61m in net impairment losses on exploration assets and non-current assets and revaluation of provisions related to production activities in the Baltic Sea (including PLN -65m in impairment losses on expenditure related to the Gaz Południe licence area),
- PLN -22m in net impairment losses on assets and remeasurement of provisions related to the Norwegian fields
- PLN -5m write-off of expenditure related to Lithuanian assets,
- PLN -12m in impairment losses on service stations.

The LOTOS Group's operating profit for 2016, **of PLN 1,854.7m (2015: PLN 423.4m)**, included:

- Operating profit of PLN 1,834.7m in the Downstream segment,
- Operating profit of PLN 17.8m in the Upstream segment.

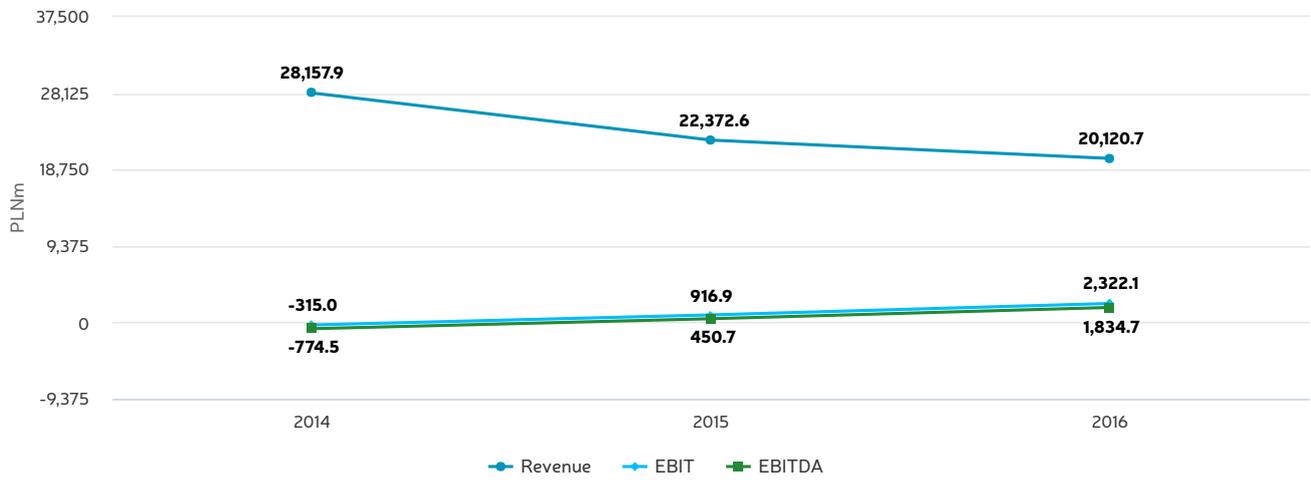
The 2016 increase in operating profit was driven mainly by the uptrend in crude oil and petroleum product prices vs the previous year's downtrend, the higher USD/PLN exchange rate in 2016, and the higher differential for the Urals crude.

Upstream segment's key financial data (PLNm)



Higher revenue in the Upstream segment posted in 2016 (up 72.8% vs 2015) was driven mainly by higher sales volumes achieved following the acquisition of interests in the Sleipner production licences in Norway in the fourth quarter of 2016; the launch of production from the B8 oil field in the Baltic Sea; and the higher average annual USD exchange rate, which was partially offset by lower crude prices on global markets.

Downstream segment's key financial data (PLNm)



The lower revenue posted by the Downstream segment in 2016 relative to 2015 was mainly due to a 10.9% fall in average selling prices caused by lower prices of oil products on global markets, offset by the higher USD/PLN exchange rate. In 2016, the LOTOS Group posted an operating profit of PLN 1,834.7m in the Downstream segment; the main contributors included rising prices, higher exchange rates, higher differential for the Urals crude, and lower cost of gas purchased by the refinery for its own needs.

Cash flows (PLNm)

	2016	2015	change
Cash flows from operating activities	2 653.9	1 488.1	1 165.80
Cash flows from investing activities	-1 003.2	-1 162.0	158.8
Cash flows from financing activities	-1 201.4	114.7	-1 316.10
Change in net cash	452.7	444.8	7.9
Cash and cash equivalents at beginning of period	278.1	-166.7	444.8
Cash and cash equivalents at end of period	730.8	278.1	452.7

As at December 31st 2016, the LOTOS Group's cash balance (including current account overdrafts) was PLN 730.8m. In 2016, net cash flows added PLN 452.7m to cash and cash equivalents. The LOTOS Group generated positive cash flows from operating activities of PLN 2,653.9m (up PLN 1,165.9m on 2015), mainly on net profit before depreciation and amortisation, income tax, and higher trade payables, which were offset by lower trade receivables.

Cash flows from investing activities of PLN -1,003.2m primarily included expenditure on acquisition of property, plant and equipment and other intangible assets. A portion of expenditure on the EFRA Project in 2016 was financed with proceeds from the issue of Grupa LOTOS Series D shares deposited in a separate bank account.

Net cash flows from financing activities of PLN -1,201.4m were due mainly to repayments of borrowings and interest payments, offset by proceeds from borrowings and a gain on settlement of financial instruments.

Profitability ratio (PLNm or %)

