

REPORT
ON THE OPERATIONS OF
THE ISSUER'S GROUP
for the first half of 2018

Łomża, 14 September 2018

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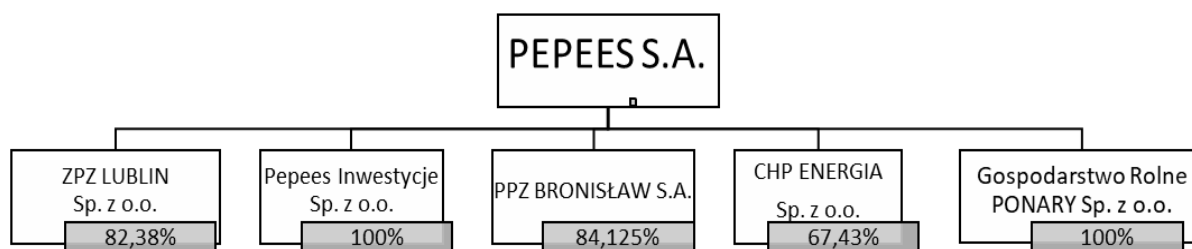
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I. Information about PEPEES Group

PEPEES Group is a modern and ever-growing corporate group specialising in the processing of potatoes to produce, among other things, potato starch, crystalline and anhydrous glucose, maltodextrin, glucose syrups, potato grits and flakes or potato protein for feed-producing purposes. Przedsiębiorstwo Przemysłu Spożywczego PEPEES S.A. (hereinafter 'PEPEES S.A.' or 'the Company') is the parent company for Zakłady Przemysłu Ziemniaczanego 'Lublin' sp. z o.o., Przedsiębiorstwo Przemysłu Ziemniaczanego 'Bronisław' S.A., CHP Energia sp. z o.o., Gospodarstwo Rolne 'Ponary' sp. z o.o. and Pepees Inwestycje Sp. z o.o. The composition of the Group as at 30 June 2018 was as follows:



All subsidiaries were consolidated with the full method.

1. Przedsiębiorstwo Przemysłu Spożywczego “PEPEES” Spółka Akcyjna in Łomża – the parent company

1.1 General information about the Company

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

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

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

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

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

The Company's share capital as at 30 June 2018 and as at the date of this report was PLN 5,700 thousand and was divided into 95,000 thousand ordinary bearer shares with the nominal value PLN 0.06 each.

As at the date of the publication of this interim report, i.e. 14 September 2018, the shareholding structure of the Company was as follows:

SHAREHOLDERS	Number of shares	Percentage of share capital %	Number of votes	Share in total number of votes at GMS
Epsilon Fundusz Inwestycyjny Zamknięty Aktywów	23,345,498	24.57	23,345,498	24.57
Mr Michał Skotnicki*	21,325,780	22.45	21,325,780	22.45
Maksymilian Maciej Skotnicki*	20,703,282	21.79	20,703,282	21.79
Mr Newth Jonathan Reginald	7,995,200	8.42	7,995,200	8.42
Richie Holding Ltd	6,133,100	6.46	6,133,100	6.46
Others**	15,497,140	16.31	15,497,140	16.31
Total	95,000,000	100.00	95,000,000	100.00

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

**None of the remaining shareholders informed about the holding of at least 5% of the share capital.

In the period from the date of the publication of the previous interim report, the Company received a notification from EPSILON Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych in Warsaw about an increase in the number of shares held by it to 23,345,498, which accounts for 24.57% of the total number of votes – detailed information is available in current report No. 25/2018. As at the date of the publication of the previous interim report, this shareholder held 22,908,328 shares entitling it to 24.11% of the total number of votes.

1.2 The Company's authorities

Board of Directors

From 1 January 2018 until 30 June 2018, the composition of the Board of Directors of PEPEES S.A. was as follows:

Mr Wojciech Faszczewski - President of the Board of Directors
Mr Tomasz Rogala - Member of the Board of Directors

On 10 April 2018, the term of office of the aforementioned managing persons was extended.

On this date, the managing persons in the Company, i.e. Mr Wojciech Faszczewski and Mr Tomasz Rogala, submitted resignations from their positions, and then the Company's Supervisory Board appointed Mr Wojciech Faszczewski as President of the Company's Board of Directors and Mr Tomasz Rogala as a Member of the Company's Management Board.

Members of the Board of Directors are appointed and dismissed by the Supervisory Board.

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

Supervisory Board

In the period from 01 January 2018 to 30 June 2018, the composition of the Supervisory Board of PEPEES S.A. was as follows:

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

In May 2018, the term of office of the aforementioned persons was extended by virtue of relevant resolutions of the Ordinary General Meeting of Shareholders.

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

General information about the Company

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

The Company's share capital as at 30 June 2018 amounted to PLN 2,761.2, and its shareholders were as follows:

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

2.2 The Company's authorities

Board of Directors

From 1 January 2018 until 30 June 2018, the composition of the Board of Directors was as follows:

Mr Piotr Kaniowski – President of the Board of Directors

Ms Małgorzata Dudzic – Member/Chief Financial Officer

Supervisory Board

In 2018, the Company's activities were supervised by the Supervisory Board composed of:

- Mr Wojciech Faszczeniowski – Chairman
- Mr Piotr Taracha – Vice Chairman
- Mr Piotr Łojko – Secretary
- Mr Mariusz – Member
- Ms Agata Czerniakowska – Member
- Mr Robert Malinowski – Member

**3. „Pepees Inwestycje” Spółka z ograniczoną odpowiedzialnością in Łomża
(formerly: OZENERGY Sp. z o.o.) - a subsidiary****3.1 General information about the Company**

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

The company's core objects include buying and selling of own real estate. As at the balance sheet date and as at the date of this report, the company did not generate any revenue. In the first half of 2018, the Company signed a preliminary agreement regarding the purchase of real estate in Warsaw and paid an advance of PLN 1,398 thousand.

The Company's share capital as at 30 June 2018 amounted to PLN 95,000 and was divided into 1,900 equal and indivisible shares, each with the value of PLN 50.

3.2 The Company's authorities

The composition of the Board of Directors as at 30 June 2018:

Mr Roman Minierski – President

**4. Przedsiębiorstwo Przemysłu Ziemniaczanego BRONISŁAW Spółka Akcyjna in Bronisław
– a subsidiary****4.1 General information about the Company**

The Company's objects are as follows:

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

The Company's share capital as at 30 June 2018 amounted to PLN 800,000 and was divided into 1,600 equal and indivisible shares, each with the nominal value of PLN 500. PEPEES is the major shareholder; it holds 84.125% of the share capital. Other shareholders are natural persons.

4.2 The Company's authorities***Board of Directors***

The composition of the Board of Directors from 01 January 2018 to 30 June 2018:

- Mr Wojciech Faszczewski – President of the Board of Directors
- Mr Roman Minierski – Vice-President of the Board of Directors

Supervisory Board

From 1 January 2018 until 30 June 2018, the Company's activities were supervised by the Supervisory Board composed of:

- | | |
|---------------------------|-------------|
| - Mr Piotr Taracha | – Chairman |
| - Ms Agata Czerniakowska | – Member |
| - Mr Grzegorz Dobrowolski | – Member |
| - Mr Gabriela Michalska | – Member |
| - Mr Robert Malinowski | – Member |
| - Mr Stanisław Bukowski | – Secretary |

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

5.1 General information about the Company

The Company's objects are as follows:

- power generation;
- electricity transmission and distribution.

The Company's share capital as at 30 June 2018 amounted to PLN 5,298,000 and was divided into 10,596 equal and indivisible shares, each with the nominal value of PLN 500. PEPEES is the major shareholder; it holds 67.43% of the share capital. Other shareholders are natural persons.

5.2 The Company's authorities

Board of Directors

The composition of the Board of Directors from 01 January 2018 to 30 June 2018:

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

Supervisory Board

The composition of the Supervisory Board from 1 January 2018 to 30 June 2018:

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

6. Gospodarstwo Rolne 'Ponary' Spółka z ograniczoną odpowiedzialnością in Łomża – a subsidiary

6.1 General information about the Company

The company's objects comprise growing of crops combined with farming of animals (mixed farming). The Company's share capital as at 30 June 2018 amounted to PLN 1,620,000 and was divided into 32,400 equal and indivisible shares of PLN 50 each.

The composition of the Board of Directors as at 30 June 2018:

Mr Tomasz Rogala – President

7. Changes in the organisation of PEPEES Group

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

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

II. Factors and events affecting the Group's operations

1. The market

Production, trade and rendering of services related mainly to the processing of potatoes and power generation were the main revenue-generating activities of PEPEES S.A. Group in the reporting period. There are three business segments in PEPEES Group, i.e.: 'processing of potatoes', 'power generation' and 'growing of crops combined with farming of animals (mixed farming)'.

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

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

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

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

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

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

All assets and liabilities of Gospodarstwo Rolne Ponary are allocated to 'growing of crops combined with farming of animals (mixed farming)' segment, but as Ponary did not generate any revenue in 2018, this segment was not separated in revenue and results.

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

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

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

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

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

3. Sales volume and structure

Table 1 presents the structure of sales revenue in the period from 01 January 2018 to 30 June 2018 as compared to the corresponding period in 2017.

Table 1: Net sales revenue structure in the first half of 2018 and the first half of 2017

(amounts in PLN 000s)

Range of products	First half of 2018	Structure in 2018	First half of 2017	Structure in 2017	Growth rate
potato-based products	96,331	82.51%	91,625	78.98%	105.14%
heat	0	0.00%	352	0.30%	0.00%
electricity	3,608	3.09%	4,884	4.21%	73.87%
animal feeds	170	0.15%	366	0.32%	46.45%
other sales, including:	16,648	14.26%	18,784	16.19%	88.63%
a) services	586	0.50%	589	0.51%	99.49%
b) trade goods and materials	16,062	13.76%	18,195	15.68%	88.28%
Total net sales revenue	116,757	100.00%	116,011	100.00%	100.64%

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

Table 2: Sales revenue by markets

(amounts in PLN 000s)

Net sales revenue	2018 first half	2017 first half
Poland, including:	79,683	79,632
- products	65,274	64,018
- trade goods	13,821	15,025
- services	588	589
EU countries - intra-Community supplies, including:	9,524	5,339
- products	9,498	4,944
- trade goods	26	395
Other countries – export, including:	27,550	31,040
- products	25,335	28,266
- trade goods	2,215	2,774
Total	116,757	116,011

- *Sales in Poland by industries and geographical regions*

The products from the potato industry were sold in 2018 throughout Poland, and the biggest sales were recorded in the following provinces: mazowieckie, wielkopolskie, lubelskie, podlaskie, małopolskie, dolnośląskie and śląskie.

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

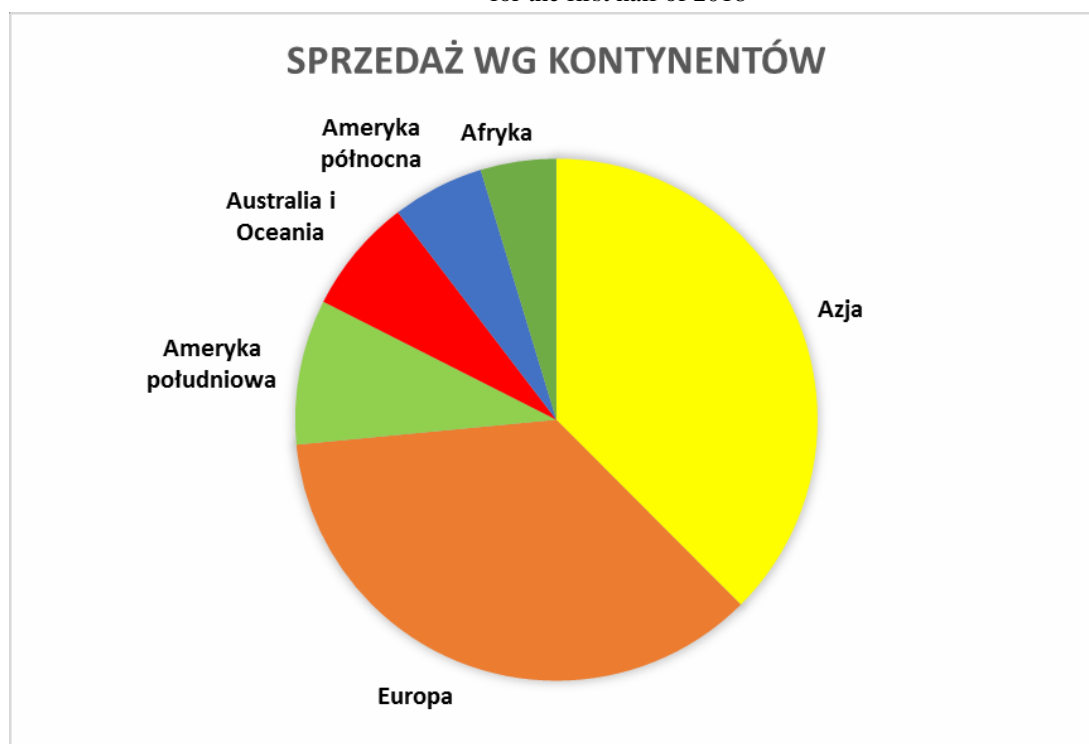
In the period, the largest share in the sales on the Polish market was recorded for potato starch, which accounts for 41.9% (in terms of value) of all products manufactured by the Group, and the next product is maltodextrin (11.3%) and glucose (6.5%). Also the share of sales of dried potato-based products (grits, flakes, cubes) in the value of sales in Poland was high (10.8%).

- *Export and intra-Community sales*

In the first half of 2018, exports and intra-Community sales amounted to 31.8% of total sales. In the corresponding period of the previous year, this share was at the level of 31.4%. This year, the Group sold its products to 16 countries in the European Union and to 24 countries from the rest of the world.

The main markets are in Asia, the Middle East, America and the countries of the former Soviet Union, i.e. Lithuania, Belarus, Kazakhstan, Uzbekistan, Russia and Latvia.

In the first half of 2018, the largest quantities of products were sold to Asia.



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

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

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

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

The basic raw material, i.e. potatoes for industrial use, is purchased from individual farmers who are not affiliated with any organisations important for the Company's business.

In 2018, materials, trade goods and services were purchased mainly from Polish companies or agencies of foreign companies. The dependence on a single supplier exists in the case of enzymes and filtering materials, as their suppliers are the only representatives in Poland of foreign companies producing the raw materials needed by the Group.

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

6. Agreements material for the Group's business

6.1 Business agreements

In 2018, the companies of PEPEES S.A. Group did not conclude agreements of substantial value.

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

- agreements regarding the modernisation of machinery and production equipment with several companies for the total amount of about PLN 14 million;
- the agreement concerning the purchase of the third block of shares in Gospodarstwo Rolne PONARY sp. z o.o. comprising the total of 32.6% of shares for PLN 3,475.2 thousand;
- a contract for the purchase of pesticides for potato plantations with the value of PLN 3,040 thousand;
- trading agreements;

6.2 Loan agreements

a) with BZ WBK S.A.:

Amendment dated 3 August 2018 to the multi-line agreement concluded between PEPEES S.A. and its subsidiaries, i.e. Zakłady Przemysłu Ziemniaczanego Lublin sp. z o.o. and Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław sp. z o.o., with Bank Zachodni WBK S.A. Pursuant to the Annex to the multi-line agreement, the total credit limit granted to the Issuer and its subsidiaries has been increased to PLN 52 million in such a way that the revolving loan granted to the Issuer, Lublin and Bronisław amounts now to PLN 16.5 million, PLN 2 million and PLN 7.8 million respectively, the revolving loan to PLN 12 million, PLN 4.25 million and PLN 4 million respectively, and the current loan to PLN 4 million, PLN 0.75 million and PLN 0.7 million respectively.

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

The remaining terms of the multi-line agreement have not been subject to any significant changes, which would differ from standard provisions used in agreements of this type.

b) with PKO BP S.A.:

The amendment dated 3 August 2018 to the multi-purpose credit limit agreement concluded between PEPEES S.A. and its subsidiaries, i.e. Zakłady Przemysłu Ziemniaczanego 'Lublin' sp. z o.o. and Przedsiębiorstwo Przemysłu Ziemniaczanego Bronisław S.A., with Powszechna Kasa Oszczędności Bank Polski S.A.

Under the Annex, the credit limit granted to the Issuer and its subsidiaries has been increased to the total amount of PLN 52 million, and in the case of individual companies: the Issuer – up to PLN 32.5 million; Lublin – up to PLN 12.5 million; and Bronisław – up to PLN 7 million. Within the aforementioned limit, the following loans were granted:

- overdraft facility: the Issuer – PLN 4 million; Lublin – PLN 0.7 million; and Bronisław – PLN 0.75 million;
- revolving working capital loan: the Issuer – PLN 12 million; Lublin – PLN 4 million; and Bronisław – PLN 4.25 million;
- non-revolving working capital loan: the Issuer – PLN 16.5 million; Lublin – PLN 7.8 million; and Bronisław – PLN 2 million.

The limit was granted until 31 August 2019.

The remaining terms of the multi-purpose credit line agreement have not been subject to any significant changes, which would differ from standard provisions used in agreements of this type.

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

6.3 Leases

- A lease concerning a passenger car with the value of PLN 50 thousand concluded on 17 March 2018 for the period of 36 months with Volkswagen Leasing GmbH.
- A lease concerning five forklift trucks with the total value of PLN 296 thousand concluded on 3 April 2018 for the period of 36 months with PKO Leasing S.A.
- A lease concerning a passenger car with the value of PLN 47 thousand concluded on 8 May 2018 for the period of 36 months with BZ WBK Leasing.
- A lease concerning a passenger car with the value of PLN 48 thousand concluded on 15 June 2018 for the period of 48 months with Volkswagen Leasing GmbH.

6.4 Insurance contracts

The companies concluded the following insurance contracts:

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

6.5 Agreements between shareholders

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

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

As at 30 June 2018, major investments of PEPEES S.A. comprised shares and bonds in subsidiaries that are subject to consolidation, and 3,000 shares of Warszawski Rolno-Spożywczy Rynek Hurtowy S.A. with the value of PLN 2,550 thousand.

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

8. Related party transactions

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

The Issuer's transactions with its subsidiaries:

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

Transactions between PEPEES S.A. in Łomża with a subsidiary ZPZ 'LUBLIN' sp. z o.o. consisted in the purchase from the subsidiary of starch and potato grits for PLN 1,001 thousand. PEPEES S.A. sold ZPZ Lublin sp. z o.o. starch and maltodextrin for PLN 111 thousand and a service for PLN 141 thousand. The selling price is determined using the cost-plus pricing method or on the basis of price lists applicable in transactions with unrelated parties. In addition, ZPZ Lublin sp. z o.o. paid to PEPEES S.A. interest on the cash loan granted in previous years amounting to PLN 63 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 3 million.

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

PEPEES S.A. bought bonds of PPZ Bronisław for PLN 3 million and purchased in the reporting period from the subsidiary starch, potato flakes and services, and sold a service to it. The total value of purchases in PPZ Bronisław S.A. amounted to PLN 2,702 thousand, and of sales to PLN 2 thousand. In addition, PPZ Bronisław S.A. paid to PEPEES S.A. interest on cash loans granted in previous years amounting to PLN 58 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 4 million.

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

PEPEES S.A. purchased from CHP Energia sp. z o.o. beet pulp for PLN 60 thousand, bio-compost for PLN 95 thousand and a service for PLN 193 thousand; and sold to CHP Energia sp. z o.o. a service with the value of PLN 5 thousand. In addition, PEPEES S.A. paid a down payment to CHP Energia on account of property rights and an advance payment for drying and granulation of potato pulp with the total value of PLN 228 thousand. In addition, CHP Energia was granted, in the first half of 2018, two loans in the total amount of PLN 1.2 million. As at the balance sheet date, CHP Energia has outstanding loans for the total amount of PLN 3,919 thousand and unpaid fees on granted guarantees of PLN 412 thousand.

Transactions between PEPEES S.A. and Gospodarstwo Rolne 'Ponary' Sp. z o.o.

PEPEES S.A. sold to GR Ponary a service for PLN 5.1 thousand and granted a loan to it of PLN 550 thousand. GR Ponary paid interest of PLN 8.7 thousand on this loan. In addition, PEPEES S.A. pays to Ponary fees for the granted surety – the value of fees charged for the first half of 2018 amounted to PLN 87.4 thousand. As at the balance sheet date, GR Ponary has an outstanding loan of PLN 550 thousand and PEPEES has outstanding fees on granted sureties of PLN 26.3 thousand.

PEPEES S.A. granted to Pepees Inwestycje a loan of PLN 1,450 thousand. Interest of PLN 10.5 thousand was accrued on this loan and, as at the balance sheet date, they are still outstanding.

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

The Company purchased from two shareholders, who are related persons and hold the total of 44.24% of the total number of votes at the General Meeting of Shareholders of Pepees, the third block of shares in Gospodarstwo Rolne Ponary sp. z o.o. comprising the total of 32.6% shares with the nominal value of PLN 527.85 thousand for the price of PLN 3,475.2 thousand. Thus, the Company has become the holder of 100% of shares in Ponary.

9. Loans and borrowings

As at 30 June 2018, PEPEES S.A. Group had borrowings, which are presented in the table below:

Table 3: Borrowings as at 30.06.2018

(amounts in PLN
000s)

Loan type /Agreement/	Lending bank	Amount of the contractual loan	Debt as at 30.06.2018	Repayment date
1	2	3	4	5
Overdraft facility (Pepees)	Bank Zachodni WBK S.A.	4,000	1,861	31.08.2018
Revolving loan (Pepees)	Bank Zachodni WBK S.A.	10,000	1,750	31.08.2018
Working capital loan for the purchase of potatoes (Pepees)	Bank Zachodni WBK S.A.	16,000	4,000	31.08.2018
Overdraft facility (Pepees)	PKO BP S.A.	4,000	606	31.08.2018
Revolving loan	PKO BP S.A.	10,000	3,750	31.08.2018
Working capital loan for the purchase of potatoes (Pepees)	PKO BP S.A.	16,000	6,000	31.08.2018
Subsidised investment loan (Pepees)	Bank Polskiej Spółdzielczości S.A.	1,295	115	30.11.2018
Investment loan (Pepees)	BNP Paribas	9,822	5,079	25.02.2022
Investment loan (Pepees)	PKO BP S.A.	1,200	721	31.12.2020
Investment loan (Pepees)	BNP Paribas Lease Group sp. z o.o.	10,530	10,530	30.06.2025
Overdraft facility (ZPZ Lublin)	Bank Zachodni WBK S.A.	500	14	31.08.2018
Revolving working capital loan in a credit account (ZPZ Lublin)	Bank Zachodni WBK S.A.	3,000	1,125	31.08.2018
Non-revolving working capital loan in a credit account (ZPZ Lublin)	Bank Zachodni WBK S.A.	1,500	375	31.08.2018
Overdraft facility (PPZ Bronisław)	Bank Zachodni WBK S.A.	500	0	31.08.2018

Loan type /Agreement/	Lending bank	Amount of the contractual loan	Debt as at 30.06.2018	Repayment date
Revolving working capital loan in credit account (PPZ Bronisław)	Bank Zachodni WBK S.A.	5,000	3,125	31.08.2018
Non-revolving working capital loan in a credit account (PPZ Bronisław)	Bank Zachodni WBK S.A.	8,000	1,456	31.08.2018
Overdraft facility (ZPZ Lublin)	PKO BP S.A.	500	0	31.08.2018
Revolving working capital loan in a credit account (ZPZ Lublin)	PKO BP S.A.	3,000	1,125	31.08.2018
Non-revolving working capital loan in a credit account (ZPZ Lublin)	PKO BP S.A.	1,500	562	31.08.2018
Overdraft facility (PPZ Bronisław)	PKO BP S.A.	500	0	31.08.2018
Revolving working capital loan in a credit account (PPZ Bronisław)	PKO BP S.A.	3,000	1,119	31.08.2018
Non-revolving working capital loan in a credit account (PPZ Bronisław)	PKO BP S.A.	8,000	3,000	31.08.2018
Working capital loan to finance current liabilities associated with business activities (CHP Energia)	Spółdzielczy Bank Rozwoju Branch in Szepietowo	3,000	2,494	31.05.2017
Syndicated investment loan to implement the investment project "The Construction of a Biogas Plant in Szepietowo District" (CHP Energia)	1. Spółdzielczy Bank Rozwoju Branch in Szepietowo 2. Bank Spółdzielczy in Brańsk 3. Bank Spółdzielczy Branch in Andrzejów	12,830	11,511	31.12.2023
Working capital loan related to business activities (CHP Energia)	Spółdzielczy Bank Rozwoju Branch in Szepietowo	800	518	31.12.2019
Investment loan to finance/refinance the purchase of a real property (PPZ Bronisław)	Bank Zachodni WBK S.A.	800	553	30.11.2021
Working capital loan associated with business activities (CHP Energia)	Spółdzielczy Bank Rozwoju Branch in Szepietowo	2,500	1,700	13.09.2018

10. Cash loans, guarantees and sureties granted

Sureties granted by the parent company PEPEES S.A.

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

The agreement of 14 September 2017 concerning the conditions of granting a security for a loan repayment concluded between PEPEES S.A. in Łomża and CHP Energia Sp. z o.o. Pursuant to the agreement, PEPEES S.A. grants the security for the repayment of the working capital loan taken out by CHP Energia Sp. z o.o. The value of the working capital loan taken by CHP Energia Sp. z o.o. amounts to PLN 3,000 thousand. The security granted by PEPEES S.A. is in the form of an endorsement on bills of exchange up to the amount of PLN 2,800 thousand (the amount of debt as at the guarantee day).

The agreement of 14 September 2017 concerning the conditions of granting a security for a loan repayment concluded between PEPEES S.A. in Łomża and CHP Energia Sp. z o.o. Pursuant to the agreement, PEPEES S.A. grants the security for the repayment of the working capital loan taken out by CHP Energia Sp. z o.o. The value of the working capital loan taken by CHP Energia Sp. z o.o. amounts to PLN 800 thousand. PLN. The security granted by PEPEES S.A. is in the form of an endorsement on bills of exchange up to the amount of PLN 710 thousand (the amount of debt as at the guarantee day).

The agreement of 14 September 2017 concerning the conditions of granting a security for a loan repayment concluded between PEPEES S.A. in Łomża and CHP Energia Sp. z o.o. Pursuant to the agreement, PEPEES S.A. grants the security for the repayment of the working capital loan taken out by CHP Energia Sp. z o.o. The value of the working capital loan taken by CHP Energia Sp. z o.o. amounts to PLN 2,500 thousand. PLN. The security granted by PEPEES S.A. is in the form of an endorsement on bills of exchange up to the amount of PLN 2,500 thousand PLN.

The statement of 30 July 2018 on the granting of the surety for the investment loan from the funds originating from foreign credit lines amounting to PLN 8,456 thousand. The loan was granted to PPZ Bronisław by Bank Ochrony Środowiska S.A.

Surety granted to the parent company PEPEES S.A.

The agreement of 12 December 2017 concerning the conditions of granting a security for a loan repayment concluded between PEPEES S.A. in Łomża and Gospodarstwo Rolne Ponary sp. z o.o. Pursuant to the agreement, GR Ponary granted its security for the repayment of the investment loan taken out by PEPEES S.A. The value of the investment loan taken out by PEPEES S.A. for the purchase of shares in GR Ponary amounts to PLN 10,530 thousand. The security granted by GR Ponary is in the form of a mortgage up to the amount of PLN 15,795 thousand on the company's land properties for the period until 30 June 2025.

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

Apart from the aforementioned surety granted by GR Ponary, in the first half of 2018, the subsidiaries neither granted nor obtained any sureties.

In the first half of 2018, the companies form PEPEES S.A. Group neither granted nor obtained any sureties.

11. Description of the use of emission earnings

In 2018, the Company and the Group did not issue any shares and did not acquire any Treasury shares.

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

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

13. Financial resources management assessment

In the first half of 2018, the Parent Company and the Group were fully capable of meeting their obligations towards both suppliers and financial institutions. There was no risk of default. Also, in the next reporting period, there should be no risk of losing financial liquidity by the Group. Any cash surpluses were placed in short-term deposits.

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

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

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

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

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

The main financial risks in 2018 include the risk of changes in market prices of products manufactured by the Group, and the currency risk. The Company's main objective in the area of the management of these risks is their elimination or mitigation.

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

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

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

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

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

15. Completed and planned investment projects

In the first half of 2018, the Group carried out several investment projects. The most important of them are as follows:

- the purchase of shares in PONARY,
- the upgrade of the potato washing and feeding station.
- the modernisation of a starch drying room;
- the upgrading of other machines and production equipment.

In the second half of the year, the Group will continue initiated upgrades of machinery and production equipment.

16. Environmental issues

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

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

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

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

17. Employment in the Group

Table 4: Employment in the Group

Specification	Average number of employees in the first half of 2018	As at 30.06.2018		Average number of employees in the previous financial year 2017
		Women	Men	
Administrative employees	149	83	69	142
Workers	254	24	233	358
Employees on parental leaves and unpaid leaves	-	-	-	4
Total	403	107	302	504

18. Major R&D accomplishments

In the first half of 2018, the Group did not carry out any major R&D works.

19. Non-typical events with a significant impact on the Group's profit/loss on business activities in the first half of 2018

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

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

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

The Company's financial statements (separate and consolidated respectively) are prepared in accordance with IAS/IFRS.

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

In the first half of 2018, control was strengthened in Gospodarstwo Rolne Ponary through the purchase of all remaining shares and obtaining 100% of voting rights at the general meeting of shareholders. There were no other changes in the Group's management policies.

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

As at 30 June 2018 and as at the publication date of this report, the following members of the management and supervisory personnel of PEPEES S.A. in Łomża held the Company's shares: President of the Board of Directors of PEPEES S.A. – 701,000 shares with the nominal value of PLN 0.06 each, i.e. with the total value of PLN 42,060.

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

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

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

23. The Company's quotations in the first half of 2018

The Company's shares have been listed on the Warsaw Stock Exchange since 22 May 1997. The share price on 3 January 2018 (the opening share price on the first day of 2018) was PLN 1.44. The highest share price in the reporting period was PLN 1.62 and the lowest share price was PLN 1.23. The following graph shows share prices of PEPEES in the first half of 2018.

Quotations of Pepees S.A. from 2018-01-01 to 2018-06-30**24. Agreements, known to the Issuer, which may result in future changes in the proportions of the shares held by existing shareholders**

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

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

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

26. The system of control of any employee share schemes

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

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

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

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

PEPEES S.A. and its subsidiaries concluded the agreement concerning the review and audit of the financial statements for 2018-2019 with **WBS Audyt sp. z o.o.** with its registered office in Warsaw, Poland.

The agreement provides for the review of the separate and consolidated financial statements as at 30 June 2018 and 30 June 2019, and for the audit of the separate and consolidated financial statements for the financial year 2018-2019. The total remuneration under the agreement payable for 2018 is PLN 59,700 plus VAT.

In the previous financial year, the total value of the auditor's services under the agreement concluded with Mazars Audyt sp. z o.o. amounted to PLN 60,000 plus VAT. There were no other agreements concluded in the reporting period and in the previous period with the entity authorised to audit financial statements.

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

As at the balance sheet date, there is an unresolved case due to the lawsuit of EPSILON Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych w Warszawie against PEPEES S.A. to repeal/annul resolutions adopted on 11.05.2018 by the Annual General Meeting of Shareholders concerning the distribution of the Company's net profit for the financial year 2017 and the appointment of members of the Supervisory Board.

At the meeting on 10 August 2018, the Court dismissed the Plaintiff's request to prohibit any factual or legal acts aimed at transferring the Company's profit for 2017 to reserves – investment fund within the scope covered by Resolution No. 12. And, within the remaining scope, i.e. regarding the suspension of the registration proceedings by the District Court in Białystok, XII Economic Division of the National Court Register regarding the entry in the Register on the basis of resolutions Nos. 25 and 29, the Company's claim has been dismissed. The decision of the Court is final and binding.

Within the remaining scope, there are no other significant proceedings before a court, a competent arbitration authority or a public administration body regarding liabilities and receivables of the issuer or its subsidiary.

30. Summary of activities in the reporting period

From January to June 2018, PEPEES S.A. Group generated sales of PLN 116.8 million, which is a similar figure as compared to the corresponding period in the previous year (PLN 116.0 thousand). There was an increase in the sales of potato products by 5% with the simultaneous drop in the sales of electricity by 26%.

Due to a higher growth rate for the costs of products sold (as compared to the growth rate for the revenue from the sales of products), in the first half of 2018, the Group generated gross profit from sales of PLN 30.1 million, which denoted a decrease by 1.5% as compared to the same period in the previous year.

From January to June 2018, sales and marketing expenses decreased by 12%, while general administrative expenses increased by more than 14% as compared to the comparative period.

The balance on other activities in the first half of 2018 closed at PLN 0.05 million as compared to the result of PLN 0.22 million in the comparative period.

In turn, the result on financing activities, understood as the balance of finance income less finance costs in the period from January to June 2018, was higher than the corresponding item in the comparative period — in 2018, it amounted to (-) PLN 0.99 million against (-) PLN 2 million in the period from January to June 2017.

As a consequence, gross profit after the first quarter of 2018 amounted to PLN 9.9 million against PLN 10.7 million of gross profit generated in the comparative period, and net

profit in the period from January to September 2018 amounted to PLN 7.49 million against PLN 8.35 million of net profit in the corresponding period of 2017.

III. Assets and financial standing

1. The Group's assets

Assets as at 30 June 2018 as compared to assets as at 31 December 2017 are shown in the table below.

Table 5: Assets as at 30.06.2018 and 31.12.2017

(amounts in PLN 000s)

Asset	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	30.06.2018	31.12.2017		30.06.2018	31.12.2017
I. NON-CURRENT ASSETS (long-term)	157,044	155,419	1,625	60.5	51.1
1. Property, plant and equipment	148,348	147,034	1,314	57.1	48.4
2. Investment properties	216	211	5	0.1	0.1
3. Intangible assets	3,140	3,140	0	1.2	1.0
4. Goodwill arising on consolidation	0	0	0	0.0	0.0
5. Investments in an associate	0	0	0	0.0	0.0
6. Investments in other entities	113	113	0	0.0	0.0
7. Loans granted	0	0	0	0.0	0.0
8. Advances	414	72	342	0.2	0.0
9. Deferred tax assets	4,813	4,849	(36)	1.9	1.6
II. CURRENT ASSETS (short-term)	102,641	148,468	(45,827)	39.5	48.9
1. Inventories	36,849	84,134	(47,285)	14.2	27.7
2. Biological assets	2,251	0	2,251	0.9	0.0
3. Trade receivables	34,425	23,311	11,114	13.3	7.7
4. Other receivables	2,333	5,250	(2,917)	0.9	1.7
5. Advances	9,692	827	8,865	3.7	0.3
6. Loans granted	923	762	161	0.4	0.3
7. Investments held for trading	4,540	3,546	994	1.7	1.2
8. Cash and cash equivalents	11,628	30,638	(19,010)	4.5	10.1
Total assets	259,685	303,887	(44,202)	100.00	100.00

The Group assets being the total balance of the assets as at 30 June 2018 and amounting to PLN 259,685 thousand decreased by PLN 44,202 thousand, i.e. by 14.5%, as compared to the previous year.

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

2. Sources of financing for the Group

Sources of financing assets as at 30 June 2018 as compared to the assets as at 31 December 2017 are shown in the table below.

Table 6: Sources of financing assets as at 30.06.2018 and 31.12.2017
(amounts in PLN 000s)

Sources of financing	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	30.06.2018	31.12.2017		30.06.2018	31.12.2017
I. Equity	149,531	145,547	3,984	57.6	47.9
<i>Equity attributable to equity holders of the parent</i>	<i>148,809</i>	<i>141,282</i>	<i>7,527</i>	<i>57.3</i>	<i>46.5</i>
1. Share capital	5,700	5,700	-	2.2	1.9
2. Reserve capital and other reserves	129,538	124,418	5,120	49.9	40.9
3. Revaluation reserve	(26)	(172)	146	0.0	-0.1
4. Retained earnings/loss	6,110	(2,028)	8,138	2.4	-0.7
5. Profit/loss for the year	7,487	13,364	(5,877)	2.9	4.4
<i>Non-controlling interests</i>	<i>722</i>	<i>4,265</i>	<i>(3,543)</i>	<i>0.3</i>	<i>1.4</i>
II. Non-current liabilities	47,211	48,684	(1,473)	18.2	16.0
1. Loans and borrowings	25,528	25,330	198	9.8	8.3
2. Liabilities related to leased assets	6,418	7,446	(1,028)	2.5	2.5
3. Deferred tax liability	6,202	6,258	(56)	2.4	2.1
4. Retirement and similar benefits obligations	2,305	2,249	56	0.9	0.7
5. Grants	6,758	6,901	(143)	2.6	2.3
6. Liabilities related to the issue of securities	0	-	0	0.0	0.0
7. Other liabilities	-	500	(500)	0.0	0.2
III. Liabilities	62,943	109,656	(46,713)	24.2	36.1
1. Trade payables	15,965	15,026	939	6.1	4.9
2. Current tax liability	70	2,887	(2,817)	0.0	1.0
3. Other short-term liabilities	3,641	5,317	(1,676)	1.4	1.7
4. Loans and borrowings	37,562	81,534	(43,972)	14.5	26.8
5. Finance lease payables	2,628	2,587	41	1.0	0.9
6. Retirement benefits obligations	288	327	(39)	0.1	0.1
7. Provisions for other liabilities	2,789	1,978	811	1.1	0.7
Total equity and	259,685	303,887	(44,202)	100.0	100.0

The structure of the financing changed in the first half of the year. The share of equity increased, while short-term liabilities decreased. The biggest decrease was recorded for loan commitments due to the repayment of loans taken out to purchase potatoes in autumn last year.

3. The Group's financial results

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

Table 7: The financial result for the first half of 2018 and of 2017
(amounts in PLN 000s)

No.	Specification	Actual results for First half of 2018	Actual results for First half of 2017	Growth rate in %
1.	Sales revenue			
	Revenue from the sales of products	101,963	98,044	104.0
	Revenue from the sales of services	586	589	99.5
	Revenue from the sales of trade goods and materials	14,208	17,378	81.8
	Total sales revenue, including:	116,757	116,011	100.6
	- revenue from continuing operations	116,757	116,011	100.6
	- revenue from discontinued operations			
	Cost of sales			
	Cost of products sold	(73,649)	(69,627)	105.8
	Cost of services sold	(90)	(349)	25.8
	Costs of trade goods and materials sold	(12,066)	(15,041)	80.2
	Profit/loss from agricultural production	(907)	(457)	198.5
	Total cost of sales, including:	(86,712)	(85,474)	101.4
	- cost from continuing operations	(86,712)	(85,474)	101.4
	- cost from discontinued operations			
	Gross profit from sales (I-II)	30,045	30,537	98.4
	Selling and marketing expenses	(4,789)	(5,450)	87.9
	Administrative expenses	(14,428)	(12,626)	114.3
	Other operating income (net profit)	590	487	121.1
2.	Other operating expenses (net loss)	(538)	(272)	197.8
	Operating profit (loss)	10,880	12,676	85.8
	Finance costs (net losses)	(1,523)	(2,147)	70.9
	Finance income (net profit)	527	150	351.3
	Share of profit (loss) of an associate	-	(2)	0.0
3.	Profit (loss) before tax, including:	9,884	10,677	92.6
	- profit (loss) before tax from continuing operations	9,884	10,677	92.6
	- profit (loss) before tax from discontinued operations			
	Income tax expense	(2,430)	(2,325)	104.5
	Net profit (loss), including:	7,454	8,352	89.7
4.	- attributable to non-controlling interests	(33)	160	(20.6)
	- attributable to the equity holders of the parent company,	7,487	8,192	91.4
	- net profit (loss) from continuing operations	7,487	8,192	91.4
5.	- net profit (loss) from discontinued operations			
	Net earnings (loss) per share, including:	0.07	0.08	91.4
6.	- net earnings per share from continuing operations	0.07	0.08	91.4
	- net earnings (loss) per share from discontinued operations			

Sales revenue for the first half of the year increased as compared to the same period in the previous year by 0.6%. The cost of sales increased by 1.4%, while administrative expenses increased by 14.3%. Thus, operating profit generated by the Group is lower by 14.2% and net profit attributable to the shareholders of PEPEES by 8.6%.

4. Cash flows

In the first half of 2018, PEPEES S.A. Group recorded negative cash flow balance due to the high repayment level of short-term loans. The balance from operating activities is positive and amounts to PLN 38,310 thousand. Cash in the consolidated statement of cash flows as at 30 June 2018 is positive and amounts to PLN 9,131 thousand. The difference amounting to PLN 2,497 thousand between the cash reported in the balance sheet and the cash reported in the statement of cash flows stems from the bank overdraft balance.

5. Economic ratios

The summary of ratios characterising the Group's business and situation is presented in Table 8 below.

Table 8: Economic ratios

Ratio	Commercial substance	First half of 2018	First half of 2017
Return on Assets	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{total assets}}$	2,88%	3,61%
Return on Equity	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{equity}}$	5,03%	6,02%
Net Profit Margin	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	6,41%	7,06%
Return on Sales	$\frac{\text{gross profit/loss from sales} \times 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	25,73%	26,32%
Cash Ratio	$\frac{\text{total current assets}}{\text{current liabilities}}$	1,63	1,75
Quick Ratio	$\frac{\text{total current assets} - \text{inventories}}{\text{current liabilities}}$	1,05	1,14
Receivables Turnover in days*	$\frac{\text{average trade receivables} \times 180}{\text{net revenue from the sales of products, services, trade goods and materials}}$	44,50	45,41
Accounts Payable Turnover in days*	$\frac{\text{average trade payables} \times 180}{\text{costs of trade goods and services sold} + \text{value of trade goods and materials}}$	32,17	23,77
Inventory Turnover in days*	$\frac{\text{average inventories} \times 180}{\text{costs of products and services sold} + \text{value of trade goods and materials}}$	125,57	112,23
Equity to Fixed Assets	$\frac{\text{equity attributable to equity holders of the Company} \times 100}{\text{total fixed assets}}$	0,95	0,96
Gearing ratio	$\frac{(\text{equity attributable to equity holders of the Company} + \text{long-term provisions} + \text{long-term liabilities}) \times 100}{\text{total equity and liabilities}}$	0,67	0,70

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

Profitability ratios decreased as compared to the previous half-year due to the lower net profit. Both cash and quick liquidity ratios are at a safe level. Equity to fixed assets ratio is still relatively high, as, due to the high percentage of equity in the financing structure, it is close to 1.0.

IV. The Group's development

1. Description of underlying risks and threats and of external and internal drivers of the Group's development

1.1 Risks and threats

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

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

- **Globalisation**

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

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

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

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

- **Currency risk**

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

- **Economic fluctuations**

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

- **Limited money supply**

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

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

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

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

The risk is very limited due to the Corporate Food Quality and Safety Management System. The product recall procedure has been implemented, and recall simulations are carried out.

1.2 External drivers of the Group's successful development

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

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

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

1.3 Internal drivers of the Group's successful development

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

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

2. The Group's development prospects


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

Entering new markets resulted in a significant increase in revenue, especially from EU countries, which, as compared to the first half of 2017, increased by over 78%.

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

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

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

<i>Signatures of all Members of the Board of Directors of the Parent Company</i>			
<i>Date</i>	<i>Name</i>	<i>Title/Function</i>	<i>Signature</i>
14.09.2018	Wojciech Faszczewski	President of the Board of Directors	
14.09.2018	Tomasz Rogala	Member of the Board of Directors	