



REPORT

**ON THE OPERATIONS OF
THE ISSUER'S GROUP**

for the first half of 2016

Łomża, 30 August 2016



The Board of Directors' report on the Group's operations
for the first half of 2016

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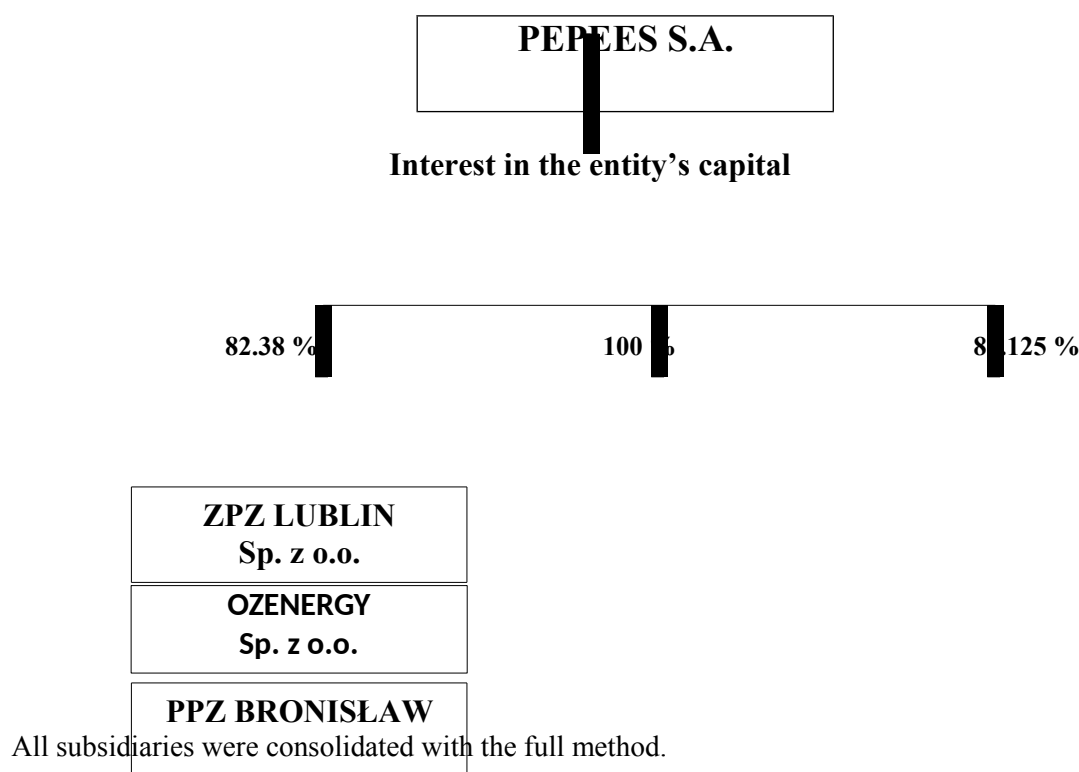
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I. Information about PEPEES Group

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. is a parent company for Zakłady Przemysłu Ziemniaczanego „ZPZ Lublin” Sp. z o.o., Przedsiębiorstwo Przemysłu Ziemniaczanego „Bronisław” Sp. z o.o. and OZENERGY Sp. z o.o.

The structure of the Group as at 30 June 2016 was as follows:



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.

It operates as a joint stock company incorporated pursuant to a notarial deed dated 21 June 1994 signed before a notary public, Mr Paweł Błaszczuk in Warsaw (Notarial Record Book A No. 14126/94).

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

It has its Tax Identification Number (NIP): 718-10-05512, assigned by the Tax Office in Łomża on 20 January 2000.

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

The Company operates pursuant to the Polish Code of Commercial Companies. 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 2016 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 the previous quarterly report, i.e. 13 May 2016, and as at the date of the publication of this interim report, i.e. 31 August 2016, the Company's shareholding structure was as follows:

–

Shareholder	No. of shares/votes	Share in the share capital/total number of votes
Maksymilian Maciej Skotnicki	19,532,088	20.56 %
Michał Skotnicki	8,600,000	9.05 %
Newth Jonathan Reginald	7,995,200	8.42 %
Krzysztof Jerzy Borkowski (control through companies, including Mazowiecka Korporacja Finansowa Sp. z o.o.)	7,923,409*	8.34 %*
Epsilon Fundusz Inwestycyjny Zamknięty Aktywów Niepublicznych	6,398,731	6.73 %
Richie Holding LTD	6,133,100	6.46 %
Others	38,417,472	40.44 %
Total	95,000,000	100 %

* including 5,397,343 shares/votes held by Mazowiecka Korporacja Finansowa sp. z o.o. representing 5.68 % of the share capital/total number of votes

1.2 The Company's authorities

Board of Directors

From 1 January 2016 until 1 June 2016, the composition of the Board of Directors of PEPEES S.A. was as follows:

Wojciech Faszczeński – President of the Board of Directors

Krzysztof Homenda – Member of the Board of Directors, Chief Financial Officer

On 25 May 2016, Mr Krzysztof Homenda resigned, as of 1 June 2016, from his membership in the Board of Directors.

In the period from 2 June 2016 until the date of this report, the Board of Directors of PEPEES S.A. had only one member, i.e. Mr Wojciech Faszczeński, the President of the Board of Directors.

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

From 1 January 2016 until 18 May 2016, the composition of the Supervisory Board of PEPEES S.A. was as follows:

- | | |
|-------------------------|-----------------|
| 1. Maciej Kaliński | – Chairman |
| 2. Piotr Marian Taracha | – Vice-Chairman |
| 3. Krzysztof Stankowski | – Secretary |
| 4. Piotr Łuniewski | – Member |
| 5. Robert Malinowski | – Member |

On 19 May 2016, the Annual General Meeting of Shareholders appointed Ms Agata Czerniakowska as a member of the Supervisory Board.

The composition of the Supervisory Board as at 30.06.2016 and as at the date of this report:

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

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

General information about the Company

The Company's registered office is in Lublin, at the address: ul. Betonowa 9. The Company is a limited liability company established by virtue of a notarial deed on 8 November 1996 signed in the notary public's firm run by Ms Antonina Renata Bednara in Lublin, at ul. Spokojna 8, Notarial Record Book A No. 6437/96, for an indefinite lifetime. The Company is entered

in the Register of Entrepreneurs kept by the District Court in Lublin, XI Economic Division of the National Court Register (KRS) in Lublin under No. KRS 0000050886.

The Company has its Tax Identification Number (NIP): 946-15-80-419. The Company operates pursuant to the Polish Code of Commercial Companies.

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 2016 amounted to PLN 2,761,200, and its shareholders were as follows:

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

2.2 The Company's authorities

Board of Directors

From 1 January 2016 until 1 June 2016, the composition of the Board of Directors was as follows:

- Krzysztof Homenda – President of the Board of Directors
- Małgorzata Dudzic – Member of the Board of Directors/Chief Financial Officer

As of 1 June 2016, Mr Krzysztof Homenda resigned from his position of the President of the Board of Directors.

From 2 June 2016 until 19 July 2016, the Board of Directors had only one member, i.e. Ms Małgorzata Dudzic, who was the Member of the Board of Directors and the Chief Financial Officer.

On 19 August 2016, the Supervisory Board appointed Mr Piotr Kaniowski as the President of the Board of Directors.

The composition of the Board of Directors as at the date of this report was as follows:

- Piotr Kaniowski – President of the Board of Directors
- Małgorzata Dudzic – Member of the Board of Directors/Chief Financial Officer

Supervisory Board

In 2016, the Company's activities were supervised by the Supervisory Board composed of:

- Wojciech Faszczeński – Chairman
- Piotr Taracha – Vice-Chairman
- Piotr Łojko – Secretary
- Mariusz Świątlicki – Member
- Agata Czerniakowska – Member

3. OZEnergy Spółka z ograniczoną odpowiedzialnością in Łomża – a subsidiary

3.1 General information about the Company

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

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

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

The Company's objects, according to its Articles of Association, are as follows: electric power generation and supply; sewerage and waste management; remediation activities; growing of crops; production, trade, rendering of services, including export and import. As at the balance sheet date and as at the date of this report, the company has not started operations yet.

The Company's share capital as at 30 June 2016 amounted to PLN 95,000 and was divided into 1,900 equal and indivisible shares, each with the value of PLN 50.

4. Przedsiębiorstwo Przemysłu Ziemniaczanego BRONISŁAW Spółka z ograniczoną odpowiedzialnością in Bronisław – a subsidiary

4.1 General information about the Company

The Company's registered office is in Bronisław 41, 88-320 Strzelno. The Company is a limited liability company established by virtue of a notarial deed on 23 November 2001, Notarial Record Book A No. 8625/2001, for an indefinite lifetime. The Company is entered in the Register of Entrepreneurs kept by the District Court in Bydgoszcz, XIII Economic Division of the National Court Register (KRS) in Bydgoszcz under No. KRS 0000099072.

The Company has its Tax Identification Number (NIP): 557-15-95-182. The Company operates pursuant to the Polish Code of Commercial Companies.

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 2016 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 in 2016:

- Wojciech Faszczeński – President of the Board of Directors
- Roman Miniński – Vice-President of the Board of Directors

Supervisory Board

From 1 January 2016 until 23 May 2016, the Company's activities were supervised by the Supervisory Board composed of:

- Piotr Taracha – Chairman
- Krzysztof Homenda – Member
- Piotr Łuniewski – Member
- Grzegorz Dobrowolski – Member
- Stanisław Bukowski – Member

As of 23 May 2016, Mr Krzysztof Homenda resigned from his membership in the Supervisory Board.

From 23 May 2016 until the date of this report, the Company's activities were supervised by the Supervisory Board composed of:

- Piotr Taracha – Chairman
- Piotr Łuniewski – Member
- Grzegorz Dobrowolski – Member
- Stanisław Bukowski – Member

5. Changes in the organisation of PEPEES Group

During the year, there were no changes in the Group.

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 was the core business of PEPEES Group in the reporting period.

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 table 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.

The European market 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 EU15 states and almost 8 % by new Member States. Poland's share in the potato starch production in the EU amounts to ca. 6 %.

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

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.

3. Sales volume and structure

Table 1 presents the structure of sales revenue in the period from 01.01.2016 to 30.06.2016 as compared to the corresponding period in 2015.

Table 1: **The structure of net sales revenue for the first half of 2016 and the first half of 2015**

*(amounts in PLN
000s)*

Range of products	First half of 2016	Structure in 2016	First half of 2015	Structure in 2015	Growth rate
potato-based products	69,205	80.01	55,726	79.81	124.19 %
heat	1,757	2.03 %	1,778	2.55 %	98.82 %
other sales:	15,533	17.96	12,323	17.65	126.05 %
<i>a) services</i>	355	0.41 %	395	0.57 %	89.87%
<i>b) trade goods and materials</i>	15,178	17.55	11,928	17.08	127.25 %
Total net sales revenue	86,495	100.00	69,827	100.00	123.87

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

Table 2:

Net sales revenue	Half-year of 2016	Half- year of
Poland, including:	62,137	55,138
- products	47,593	43,317
- trade goods	14,189	11,426
- services	355	395
EU countries - intra-Community supplies, including:	5,571	4,430
- products	5,471	4,412
- trade goods	100	18
Other countries – export, including:	18,687	10,259
- products	17,798	9,775
- trade goods	889	484
Total	86,495	69,827

4.1 Sales in Poland by industries and geographical regions

The products from the potato industry were sold in 2016 throughout Poland, and the biggest sales were recorded in the following provinces: wielkopolskie, lubelskie, podlaskie, mazowieckie, małopolskie, dolnośląskie and śląskie.

„PEPEES” S.A. in Łomża 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.

Zakłady Przemysłu Ziemniaczanego „LUBLIN” Sp. z o.o. in Lublin focused its sales mainly in the south-eastern region of Poland and in mazowieckie province.

In the period, the largest share in the sales on the Polish market was recorded for potato starch, which accounts for 51.6 % (in terms of value) of all products manufactured by the Group, and the next product is maltodextrin (8.1 %) and glucose (ca. 5.1 %).

4.2 Export and intra-Community sales

In the first half of 2016, export and intra-Community sales amounted to 28 % of total sales. In the corresponding period of the previous year, this share was at the level of 21 %. This year, the Group sold its products to 16 countries in the European Union and to 19 countries from the rest of the world.

The largest amounts of products were sold to South Korea, the Netherlands, Switzerland, Taiwan and neighbouring countries such as Lithuania, Latvia and Germany.

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

Potatoes 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.

In addition, the following raw materials are procured for the production of potato-based products and starch hydrolysates: 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.

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 2016, the companies of PEPEES Group did not conclude agreements of substantial value.

Notwithstanding the foregoing, the Issuer indicates the following agreements concluded in 2016:

- a contract for the purchase of pesticides for potato plantations with the value of PLN 3,103 thousand.
- trading agreements;
- agreements concerning the modernisation of buildings, structures, plant and machinery and repairs.

6.2 Loan agreements

a) with BOŚ S.A.:

- A non-revolving loan agreement dated 18.02.2016 between „PEPEES” S.A. in Łomża and BOŚ S.A. The subject of the agreement comprises the provision of investment financing to PEPEES S.A. totalling PLN 1.2 million for the period from 18.02.2016 to 31.12.2020. The interest rate of the loan is based on WIBOR 3M rate plus the bank’s fixed margin.

b) with BZ WBK S.A.:

- Annex No. 6 of 31.05.2016 to the multi-line agreement of 7 October 2014 concluded between the companies of PEPEES” S.A. Group and BZ WBK S.A. The subject of the annex is to increase the value of the revolving loan granted to a subsidiary PPZ Bronisław Sp. z o.o. and to amend the repayment schedule for the loan by PPZ Bronisław Sp. z o.o. The multi-line total value is PLN 40.5 million.

c) with BNP Paribas Leasing Solutions Sp. z o.o.:

- A cash loan agreement of 09.06.2016 concluded between „PEPEES” S.A. in Łomża and BNP Paribas Leasing Solutions Sp. z o.o. The subject of the agreement is to provide financing to purchase an agricultural tractor Deutz-Fahr Agrottron TTV 9340. The cash loan was granted in the amount of PLN 533 thousand for the period from 09.06.2016 until 13.06.2018. The interest rate of the cash loan is 0 % (zero percent).

6.3 Lease agreements

In the first half of 2016, the Group did not enter into any lease agreements.

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.

TRADO S.A., on 9 March 2016, sold all shares of PEPEES held by it, i.e. 8,600,000 shares, to Mr Michał Skotnicki. Following this transaction, Mr Michał Skotnicki and Mr Maksymilian Skotnicki (family members) hold jointly 28,132,088 shares, which account for 29.613 % of the share capital and give them the right to 28,132,088 votes at the General Meeting of the Shareholders, which account for 29.613 % of the total number of votes at the General Meeting of the Shareholders.

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

As at 30.06.2016, major investments of „PEPEES” S.A. comprise shares in subsidiaries that have been consolidated, and in an associate CHP Energia Sp. z o.o. (with the Issuer's interest at the level of 24.9 % in the share capital/total number of votes) measured with the equity method, 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 3 other Polish entities 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 Group concluded transactions with related parties and all such transactions were made at arm's length.

Notwithstanding the foregoing, the Group presents below the information on particular transactions with related parties, and detailed information about transactions concluded with the aforementioned entities is presented in the condensed consolidated financial statements for the first half of 2016.

The Issuer's transactions with its subsidiaries:

Transactions between „PEPEES” S.A. in Łomża and ZPZ „LUBLIN” Sp. z o.o. in Lublin

Transactions between „PEPEES” S.A. in Łomża and its subsidiary ZPZ „LUBLIN” Sp. z o.o. in Lublin involved the sales of starch and services with the value of PLN 360 thousand, and the purchase from the subsidiary of potato grits and flakes for the total amount of PLN 13 thousand.

The selling price is determined using the cost-plus pricing method or on the basis of price lists used in transactions with unrelated parties.

In addition, ZPZ „LUBLIN” paid to the Issuer interest on the cash loan granted in previous years amounting to PLN 64 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 3,010 thousand.

Transactions between „PEPEES” S.A. in Łomża and PPZ Bronisław Sp. z o.o. in Bronisław

During the reporting period, the Issuer purchased from its subsidiary starch, potato flakes and services, and sold starch. The total value of purchases from PPZ „BRONISŁAW” Sp. z o.o. amounted to PLN 2,556 thousand, and the total value of sales to PLN 142 thousand.

In addition, PPZ Bronisław paid to the Issuer interest on the cash loan granted in the previous year amounting to PLN 117 thousand. The amount of the outstanding loan as at the balance sheet date was PLN 5,200 thousand.

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

As at the balance sheet date, there is an outstanding loan granted in previous years amounting to PLN 3,528 thousand.

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

In the reporting period, the Company did not enter into any transactions with shareholders or members of the management or supervisory personnel and their family members.

9. Loans and borrowings

As at 30.06.2016, the Group had loans and borrowings, which are presented in the table below:

Table 3:

Loans and borrowings as at 30.06.2016

(amounts in PLN 000s)

Loan type /Agreement/	Lending bank	Contractual loan amount	Debt as at 30.06.2015	Repayment date
1	2	3	4	5
Bank overdraft	Bank Zachodni WBK S.A.	4,000	0	31.08.2016
Revolving loan	Bank Zachodni WBK S.A.	6,000	0	31.08.2016
Working capital loan for the purchase of	Bank Zachodni WBK S.A.	15,000	3,750	31.08.2016
Bank overdraft	BGŻ BNP Paribas	4,000	0	31.08.2016
Revolving loan	BGŻ BNP Paribas	6,000	1,125	31.08.2016
Working capital loan for the purchase of	BGŻ BNP Paribas	15,000	5,625	31.08.2016
Subsidised investment loan	Bank Spółdzielczy S.A./Bank	3,465	642	30.06.2017
Subsidised investment loan	Bank Polskiej Spółdzielczości	1,295	534	30.11.2018
Investment loan	BNP Paribas	9,823	7,849	25.02.2022
Voivodship Fund for	BOŚ	1,200	509	31.12.2020
Cash loan	BNP Paribas Lease Group	533	533	13.06.2018
Bank overdraft	Bank Zachodni WBK S.A.	500	359	31.08.2016
Revolving loan	Bank Zachodni WBK S.A.	2,000	750	31.08.2016
Working capital loan for the purchase of	Bank Zachodni WBK S.A.	2,500	937	31.08.2016
Bank overdraft	BGŻ BNP Paribas	500	108	31.08.2016
Revolving loan	BGŻ BNP Paribas	2,000	750	31.08.2016
Working capital loan for the purchase of	BGŻ BNP Paribas	2,500	680	31.08.2016
Bank overdraft	Bank Zachodni WBK S.A.	500	0	31.08.2016
Revolving loan	Bank Zachodni WBK S.A.	2,900	2,275	31.08.2016
Working capital loan for the purchase of	Bank Zachodni WBK S.A.	7,500	1,875	31.08.2016
Bank overdraft	BGŻ BNP Paribas	500	0	31.08.2016
Revolving loan	BGŻ BNP Paribas	1,000	250	31.08.2016
Working capital loan for the purchase of	BGŻ BNP Paribas	7,500	2,466	31.08.2016

10. Cash loans, guarantees and sureties granted

In previous years, the parent company granted cash loans to related parties: PLN 6,500 thousand to PPZ BRONISŁAW (PLN 5,200 thousand still outstanding), PLN 3,000 thousand to ZPZ LUBLIN and PLN 2,664 thousand to CHP Energia. Cash loans granted to subsidiaries were eliminated from the consolidated financial statements.

In the consolidated statement of financial position, there is only the loan granted in 2013 to the associate CHP Energia with the value of PLN 3,528 thousand, which is to be repaid with interest until 31 December 2016.

Cash loans to related parties were granted in the Polish currency on financial terms similar to terms of bank loans.

PEPEES granted its guarantee for the loan taken out for the period from 25.05.2014 to 25.05.2024, to CHP up to PLN 6,000 thousand.

11. Description of the use of emission earnings

In 2016, the Group did not issue any shares and did not acquire treasury shares.

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

The Group did not publish financial forecasts for 2016.

13. Financial resources management assessment

The main financial instruments used by the Group comprised bank loans, lease agreements, short-term deposits, and cash. Other instruments arising directly in the course of business comprised trade receivables and payables.

In the first half of 2016, the Group was fully capable of meeting its 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.

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

In the first half of 2016, PEPEES S.A. Group had exposures to the following types of risks associated with its business:

- Price risk for core products. In recent years, there have been substantial fluctuations of starch prices.
- Currency risk. The risk of changes in foreign currency exchange rates is viewed as material. Substantial fluctuations of exchange rates influence generated revenue from export sales. This risk is mitigated through purchases of production materials and of the raw material, for which the payment is expressed in EUR, i.e. such as sales revenue. In the first half of 2016, the Group did not use instruments hedging changes of exchange rates.
- Liquidity risk. The liquidity risk in the Group is not deemed high as well. KUKE S.A. evaluates counterparties and insures receivables. High-risk foreign transactions are hedged with a letter of credit.

- Interest rate risk. This risk occurs in the Group due to the financing of operating and investing activities with bank loans. As long-term loans are subsidised and bear low interest rates, the interest rate risk is not high. In the first half of 2016, there was no exposure to any interest rate hedging instruments.

15. Completed and planned investment projects

In the first half of 2016, the Group carried out several investment projects. The most important of them are as follows:

- the assembly of a compressed air station;
- the construction of a water softening station to meet the production needs of the food starch-producing unit;
- the assembly of the station to pack potato protein into Big-Bag bags;
- the renovation of the pipeline used to discharge production wastewater;
- the upgrading of several machines and production equipment;
- further modernisation of the dust removal system of coal boilers.

In the second half of the year, the Group will continue initiated investment projects and will upgrade central heating and certain 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 Company 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 and recycling. The Company monitors environmental impacts through periodical measurements and recording of the size and characteristic parameters of the streams of air pollutant emissions and waste, and of the water intake and discharged wastewater. The present scope of the monitoring, determined in the administrative permits held by the Company, should be regarded as sufficient to assess the operation of the systems.

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

The Company maintains quantitative and qualitative waste management records in accordance with the adopted classification and model documents referred to in relevant regulations.

The Company operates the Integrated Management System, including quality management, environmental management and H&S management, and the quality management system in laboratories.

17. Employment in the Group

Specification	Average number of employees in the first half of 2016	As at 30.06.2016		Average number of employees in the previous financial year - 2015
		Women	Men	
Administrative employees	122	65	57	117
Workers	201	18	187	274
Employees on parental leaves and unpaid leaves	5	1	5	4
Total	328	84	249	395

18. Major R&D accomplishments

In 2016, 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 2016

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.

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

In the first half of 2016, there were no material changes of the principles of the Group management process.

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

From among the management and supervisory personnel of „PEPEES” S.A. in Łomża, as at 30.06.2016 and as at the date of the publication of this report, the President of the Board of Directors of PEPEES held 701,000 shares of the Company with the nominal value of PLN 0.06 each and 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 quarterly 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 2016

The Company's shares have been listed on the Warsaw Stock Exchange since 22 May 1997. The share price on 04.01.2016 (the opening share price on the first day of 2016) was PLN 0.54. The highest share price in the reporting period was PLN 0.63 and the lowest share price was PLN 0.51. The following graph shows share prices of PEPEES in the first half of 2016.

Quotations of Pepees S.A. from 2016-01-01 to 2016-06-30



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 and its subsidiaries concluded the agreement concerning the review and audit of the financial statements for 2016 with **Mazars Audyt Sp. z o.o.** with its registered office in Warsaw, Poland.

The agreements provide for the review of the separate and consolidated financial statements as at 30.06.2016, and for the audit of the separate and consolidated financial statements for the financial year 01.01-31.12.2016. The total remuneration under the agreement is PLN 54,000 plus VAT.

In the previous financial year, the total value of the auditor's services under the agreement amounted to PLN 64,000 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 date of this report, there are no proceedings carried out concerning commitments or debts of the Company or its subsidiary, the value of which accounts for at least 10 % of the equity of PEPEES S.A.; and the Company or its subsidiary is not a party to two or more proceedings concerning commitments and debts, the total value of which accounts for at least 10 % of the equity of PEPEES S.A.

At the same time, the information about the Group's settlements due to litigation in the reporting period was published in the condensed consolidated financial statements for the first half of 2016.

III. Assets and financial standing.

1. The Group's assets

Assets as at 30 June 2016 as compared to 31 December 2015 are shown in the table below.

Table 4:

Assets
as at 30.06.2016 and 31.12.2015

(amounts in PLN 000s)

Asset	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	30.06.2016	31.12.2015		30.06.2016	31.12.2015
I. NON-CURRENT ASSETS (long-term)	101,711	102,971	(1,260)	58.38	46.62
1. Property, plant and equipment	88,757	89,196	(439)	50.94	40.38
2. Investment property					
3. Intangible assets	117	460	(343)	0.07	0.21
4. Goodwill arising on consolidation	486	486		0.28	0.22
5. Investment in the associate					
6. Investments in other entities	113	113		0.07	0.05
7. Loans granted					
8. Advances	10,020	10,391	(371)	5.75	4.77
9. Deferred tax assets	2,218	2,325	(107)	1.27	1.05
II. CURRENT ASSETS (short-term)	72,522	117,917	(45,395)	41.62	53.38
1. Inventories	25,324	64,111	(38,787)	14.53	29.02
2. Biological assets	830	172	658	0.48	0.08
3. Trade receivables	28,425	18,118	10,307	16.31	8.20
4. Current income tax receivables					
5. Other receivables	647	4,237	(3,590)	0.37	1.92
6. Advances	4,838	1,085	3,753	2.78	0.49
7. Loans granted	2907	2,806	101	1.67	1.27
8. Investments held for trading	2,550	2,550		1.46	1.15
9. Cash and cash equivalents	7,001	24,838	(17,837)	4.02	11.25
III. Non-current assets held-for-sale					
Total assets	174,233	220,888	(46,655)	100.0	100.0

The Group's assets as indicated by total assets as at 30.06.2016 amounting to PLN 174,233 thousand, decreased by PLN 46,655 thousand, i.e. by 21 % 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

The sources of financing assets as at 30 June 2016 as compared to 31 December 2015 are shown in the table below.

Table 5:

Sources of financing assets
as at 30.06.2016 and 31.12.2015

(amounts in PLN 000s)

Sources of financing	As at		Changes in amounts + increases - decreases	Structure ratios in %	
	30.06.2016	31.12.2015		30.06.2016	31.12.2015
I. Equity	115,000	109,854	5,146	66.01	49.73
<i>Equity attributable to equity holders of the parent</i>	<i>114,223</i>	<i>109,136</i>	<i>5,087</i>	<i>65.56</i>	<i>49.40</i>
1. Share capital	5,700	5,700		3.27	2.58
2. Reserve capital and other reserves	106,065	99,735	6,330	60.88	45.15
3. Revaluation reserve	(492)	(391)	(101)	(0.28)	(0.18)
4. Retained earnings/loss	(2,229)	(1,196)	(1,033)	(1.28)	(0.54)
5. Profit/loss for the year	5,179	5,288	(109)	2.97	2.39
<i>Non-controlling interests</i>	<i>777</i>	<i>718</i>	<i>59</i>	<i>0.45</i>	<i>0.33</i>
II. Non-current liabilities	22,862	23,417	(555)	13.12	10.60
1. Loans and borrowings	7,517	7,916	(399)	4.31	3.58
2. Liabilities related to leased assets	4,106	4,246	(140)	2.36	1.92
3. Deferred tax liabilities	5,974	6,018	(44)	3.43	2.72
4. Retirement and similar benefits obligations	2,609	2,509	100	1.50	1.14
5. Grants	2,656	2,728	(72)	1.52	1.24
III. Current liabilities	36,371	87,617	(51,246)	20.87	39.67
1. Trade payables	7,434	7,511	(77)	4.27	3.40
2. Current income tax liabilities	453	869	(416)	0.26	0.40
3. Other current liabilities	2,292	2,918	(626)	1.31	1.32
4. Loans and borrowings	23,501	73,114	(49,613)	13.49	33.10
6. Finance lease payables	1,244	1,243	1	0.71	0.56
7. Retirement benefits obligations	278	240	38	0.16	0.11
8. Provisions for other liabilities	1,169	1,722	(553)	0.67	0.78
Total equity and liabilities	174,2	220,8	(46,65	10	10

The structure of the financing changed in the first half of the year. The share of equity increased due to the generated net profit. And, current 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 2016 and the first half of 2015 are shown in the table below.

Table 6:

Financial result for the first half of 2016 and the first half of 2015

(amounts in PLN 000s)

N o.	Specification	Actual results for the first half of	Actual results for the first half of	Growth rate in %
1	Sales revenue			
	Revenue from the sales of products	70,962	57,505	123.4
	Revenue from services	355	394	90.1
	Revenue from the sales of trade goods and	15,178	11,928	127.2
	Total sales revenue, including:	86,495	69,827	123.9
	- <i>revenue from continuing operations</i>	<i>86,495</i>	<i>69,827</i>	123.9
	- <i>revenue from discontinued operations</i>			
	Cost of sales			
	Cost of products sold	(52,027)	(45,016)	115.6
	Cost of services sold	(74)	(116)	63.8
	Costs of trade goods and materials sold	(14,076)	(10,625)	132.5
	Profit/loss from agricultural production	(388)	(172)	225.6
	Total cost of sales, including:	(66,565)	(55,929)	119.0
	- <i>cost from continuing operations</i>	<i>(66,565)</i>	<i>(55,929)</i>	119.0
	- <i>cost from discontinued operations</i>			
	Gross profit from sales (I-II)	19,930	13,898	143.4
	Selling and marketing expenses	(3,460)	(2,921)	118.5
	Administrative expenses	(9,285)	(8,174)	113.6
	Other operating income (net profit)	241	954	25.3
2	Other operating expenses (net loss)	(214)	(186)	115.1
	Operating profit (loss)	7,212	3,571	202.0
	Financial costs (net loss)	(802)	(854)	93.9
	Finance income (net profit)	497	452	110.0
	Share of profit (loss) of an associate	(276)	(515)	53.6
3	Profit (loss) before tax, including:	6,631	2,654	249.8
	- <i>profit (loss) before tax from continuing operations</i>	<i>6,631</i>	<i>2,654</i>	249.8
	- <i>profit (loss) before tax from discontinued operations</i>			
	Income tax expense	(1,393)	(869)	160.3
	Net profit (loss), including:	5,238	1,785	293.4
4	- attributable to non-controlling interests	59	(109)	(54.1)
	- attributable to the equity holders of the parent, including:	5,179	1,894	273.4
	- <i>net profit (loss) from continuing operations</i>	<i>5,179</i>	<i>1,894</i>	273.4
5	- <i>net profit (loss) from discontinued operations</i>			
	Net earnings (loss) per share, including:	0.05	0.02	273.4
6	- <i>net earnings per share from continuing operations</i>	<i>0.05</i>	<i>0.02</i>	273.4
	- <i>net earnings (loss) per share from discontinued operations</i>			

Sales revenue for the first half of the year increased as compared to the same period in the previous year by 23.9 %. The biggest increase was recorded for export income – 80 %. The margin on the sales of products increased, owing to which the Group's operating profit doubled and net profit attributable to shareholders of PEPEES increased 2.7 times.



4. Cash flows

In the first half of the year, the 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 35,794 thousand. Cash in the consolidated statement of cash flows as at 30.06.2016 is positive and amounts to PLN 6,533 thousand. The difference between cash reported in the balance sheet and in the statement of cash flows stems from the bank overdraft balance.

5. Economic ratios

The ratios characterising the Group's business and situation are presented in Table 7 below.

Table 7:

Economic ratios

Ratio	Commercial substance	First half of 2016	First half of 2015
Return on Assets	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{total assets}}$	2.97 %	1.10 %
Return on Equity	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{equity}}$	4.53 %	1.79 %
Net Profit Margin	$\frac{\text{net profit/loss attributable to equity holders of the Company} \times 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	5.99 %	2.71 %
Return on Sales	$\frac{\text{gross profit/loss from sales} \times 100}{\text{net revenue from the sales of products, services, trade goods and materials}}$	23.04 %	19.90 %
Cash Ratio	$\frac{\text{total current assets}}{\text{current liabilities}}$	1.99	1.53
Quick Ratio	$\frac{\text{total current assets} - \text{inventories}}{\text{current liabilities}}$	1.30	0.79
Receivables Turnover in days*	$\frac{\text{average trade receivables} \times 180}{\text{net revenue from the sales of products, services, trade goods and materials}}$	48.43	49.74
Accounts Payable Turnover	$\frac{\text{average trade payables} \times 180}{\text{costs of trade goods and services sold} + \text{value of trade goods and materials}}$	20.21	40.21
Inventory Turnover in days*	$\frac{\text{average inventories} \times 180}{\text{costs of products and services sold} + \text{value of trade goods and materials}}$	120.92	163.36
Equity to Fixed Assets Ratio	$\frac{\text{equity attributable to the shareholders of the Company} \times 100}{\text{total non-current assets}}$	1.12	1.04
Gearing Ratio	$\frac{(\text{equity attributable to the shareholders of the Company} + \text{long-term provisions} + \text{non-current liabilities}) \times 100}{\text{total equity and liabilities}}$	0.70	0.79

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

Profitability ratios increased more than twice as compared to the previous year due to the higher net profit. Liquidity ratios also increased substantially, which is related to the repayment of short-term loans. In addition, inventory turnover ratio decreased thanks to higher sales. Equity to fixed assets ratio is high, as, due to the high share of equity in the financing structure, it exceeds 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's 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 prolong transactions.

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

The Group manufactures food. 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 2016, PEPEES S.A. Group pursued its strategic objectives consistently, which made it possible to generate excellent 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 international markets, which, as compared to the first half of 2015, increased by 65 %.

The development plans aim at 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.

In addition, after the balance sheet date, i.e. on 7 July 2016, the Issuer was notified about the selection by the Energy Regulatory Office (URE) of the bid made by the Company in the tender procedure concerning the selection of projects to improve energy efficiency. As a result, the Issuer was granted PMEF energy efficiency certificates (the so-called 'white certificates') with the net value, i.e. after deduction of costs and fees, of ca. PLN 1.2 million according to the current valuation of this category of certificates on the Polish Power Exchange (TGE). The bid submitted by the Issuer listed the projects, implemented in 2012-2015, regarding the assembly of a heat recovery ventilation in a protein recovery station, and the upgrade of the corporate heat distribution network. The aforementioned certificates were submitted to the Company in July 2016. By the date of this report, the Company has sold at TGE certificates with the total value of ca. PLN 1,790 thousand, generating income of PLN 973 thousand.

Signatures of the Members of the Board of Directors

<i>Date</i>	<i>Name</i>	<i>Title/Function</i>	<i>Signature</i>
30.08.2016	Wojciech Faszczewski	President of the Board of Directors	