

MANAGEMENT BOARD REPORT
ON THE ACTIVITIES OF THE PROCHEM S.A.
CAPITAL GROUP
IN THE FIRST HALF OF 2017

Warsaw, 29 August 2017

1. Principles of presentation of financial statements

Principles of presentation of consolidated financial statements of the PROCHEM S.A. Capital Group for the first half of 2017 have been included in the Explanatory Notes to the Financial Statements.

2. Basic economic and financial data disclosed in the interim financial report and presentation of development prospects of Capital Group of the Issuer until the end of 2017

In the first half of 2017 the PROCHEM S.A. Capital Group achieved revenues from basic activities in the amount of PLN 53.7 million. They are by over PLN 26 million lower than those achieved in the first half of 2016. The decline in revenues is a consequence of a significant downturn in the construction and assembly services market as a result of the reduction in the level of planned and undertaken investments by companies in recent years.

The macroeconomic environment will continue to impact significantly activity until the end of 2017, and in particular the level of investment, which in the opinion of many analysts, should gradually improve. In PROCHEM S.A. in 2017, the implementation of a program which consists in adapting of operating costs to the planned revenues, which was introduced in the fourth quarter of 2016 has begun to bring effects. Of a great importance for the Group's financial situation will be the consideration by the court, in the coming months, of the appeal lodged by PERN SA, against the verdict of October 22, 2015, in which the court adjudged the amount of PLN 90 million (including default interest) for the benefit of the consortium with the participation of the Issuer. The Issuer's share in this amount is approximately 50%.

3. Significant risk factors and threats to activity of the PROCHEM S.A. Capital Group

Companies from the PROCHEM S.A. Capital Group in their operations are exposed to the following types of risks and threats:

3.1 Economic situation fluctuations on the investment market

Part of companies from the Capital Group provide services on the investment market, which is characterized by a large scale of fluctuations in demand, which is strongly linked to general macroeconomic situation of the country. Methods used by the Group to reduce

the negative impact of this factor on the financial results (the accumulation of financial reserves, diversification of services provided), may not fully neutralize this risk.

3.2 Dependence on the staff

Risk of dependence on staff occurs particularly in the Parent Entity. Raising the quality of services provided, undertaking the implementation of complicated technological projects, the use of modern information systems, and the work for renowned clients require from workers the highest professional qualifications. Acquiring of such persons, especially in the situation of the liberalization of the European labor market can be difficult. The company is trying to minimize this threat by raising qualifications of the employed staff and using incentive programs associating employees with the company.

3.3 Exchange rate risk

Part of contracts (mainly of the parent company) for the sale of services is concluded with foreign companies in foreign currencies (EUR, USD). In the event of a significant strengthening of the domestic currency, this can have an adverse effect on the Group's results. This risk is partially mitigated in a natural way through the purchase of equipment and services necessary for the execution of these contracts abroad, as well through the acquisition of relative financial instruments.

3.4 The risk of disadvantageous settling the litigation with PERN SA

In view of the considerable extension of the court proceedings initiated in 2006 against the PERN SA, which is currently conducted by the District Court in Warsaw on the accounting for the contract in the formula of GRI (the Management Contracting), which was suspended on 10 November 2005, for the investment task under the name of "Rurociąg w relacji ST-1 Adamowo - Baza Surowcowa Plebanka", PROCHEM S.A. was forced to fulfil the obligations concerning the seized guarantee deposits of subcontractors prior to their receipt from PERN S.A.

In case of unfavorable verdict in the legal proceedings, the Management Board of PROCHEM S.A. takes into account the possibility of non-recovery of financial means allocated to these payments.

4. Organization the Capital Group with indication of consolidated entities

The Capital Group of PROCHEM S.A. (hereinafter "the Capital Group", "the Group") in addition to the data of the Parent Entity includes the following subsidiaries directly and indirectly:

Subsidiaries covered by full consolidation:

- Prochem Inwestycje Sp. z o. o. seated in Warsaw – subsidiary directly (100.0%);
- PRO-INHUT Sp. z o. o. seated in Dąbrowa Górnicza – subsidiary indirectly (93.2%);
- Przedsiębiorstwo Konsultingowo-Inżynieryjne PREDOM Sp. z o. o. seated in Wrocław – subsidiary indirectly (80.7% of capital and profit, 71.1% of votes);
- Prochem Zachód Sp. z o. o. seated in Słubice – subsidiary directly (80.0%);
- ELPRO Sp. z o. o. seated in Krakow – subsidiary indirectly (92.7%, including 85.4% share in 50% share of Elektromontaż Kraków);
- Elmont Inwestycje Sp. z o. o. seated in Krakow – subsidiary indirectly (92.7%, including 85.4% share in 50% share of Elektromontaż Kraków);
- Elektromontaż Kraków SA seated in Krakow – subsidiary indirectly (85.4%), including 73.0% of capital and votes belongs to company Prochem Inwestycje subsidiary in 100%. Elektromontaż Kraków S.A. prepares consolidated financial statements, which contain data of a subsidiary in 100%: ELMONT-POMIARY Sp. z o. o. seated in Krakow and two associated companies ELPRO Sp. z o. o. and Elmont-Inwestycje Sp. z o. o.;
- IRYD Sp. z o. o. seated in Warsaw – subsidiary indirectly 100%;
- ATUTOR Integracja Cyfrowa Sp. z o. o. seated in Warsaw – subsidiary indirectly (87.3% of share holds Prochem Inwestycje Sp. z o. o. subsidiary in 100%);
- Prochem RPI Sp. z o. o. seated in Warsaw – subsidiary directly and indirectly in 100%;

1.1.

Associated entities and jointly-controlled entities consolidated with the equity method:

- IRYDION Sp. z o. o. in Warsaw – 50.0% of share in voting rights and in share capital,
- ITEL Sp. z o. o. seated in Gdynia – 42.0% of share (18.7% of share in voting rights and in capital holds directly PROCHEM S.A. and 23.3% holds Prochem RPI Sp. z o. o. subsidiary (in 100%).

The principle adopted at consolidation consists in not including in consolidation of such companies, which are not conducting activity. Companies not included in the consolidation:

- Predom Projektowanie Sp. z o. o. seated in Wrocław – subsidiary

Subsidiaries, associates and jointly-controlled entities covered by consolidation were included in the consolidated financial statements from the date of acquisition of control by the parent company.

5. Effects of changes in the capital group structure, including mergers of economic entities, acquisitions or sale of the entities from the issuer's capital group, long-term investments, division, restructuring and discontinued operations

In the first half of 2017 there were no changes in the structure of the Capital Group.

6. Management Board's position in relation to the possibility of accomplishment of previously published forecast of results for the given year, in the light of results presented in the interim report with respect to the forecasted results

Company PROCHEM S.A. did not publish any forecasts of financial results neither for the Company nor for the PROCHEM S.A. Capital Group for 2017.

7. Shareholders having directly or indirectly through subsidiaries, at least 5% of the total number of votes at the General Meeting of the Issuer at the date of the quarterly report, including the number of shares owned by those entities, their percentage of the share capital, the number of votes resulted from them and their percentage share in the total number of votes at the general meeting, and changes in the ownership of large blocks of shares of the Issuer since the previous report

According to the Company's knowledge at the date of this report, the following shareholders hold at least 5% of votes at the General Meeting of Shareholders:

ITEM No.	DESCRIPTION	NUMBER OF SHARES HELD (IN PCS)	NUMBER OF VOTES HELD	% OF VOTES IN TOTAL NUMBER OF VOTES	% OF SHARE CAPITAL
1	Porozumienie PHC	662,663	662,849	17.04	17.02

2	Steven Tappan	817,500	817,500	20.98	20.99
3	Legg Mason TFI S.A.	560,549	560,549	14.39	14.39
4	Otwarty Fundusz Emerytalny PZU S.A. „Złota Jesień“	387,521	387,521	9.95	9.95
5	Quercus TFI S.A.	415,532	415,532	10.67	10.67
6	Value Fund Poland Activist Fundusz Inwestycyjny Zamknięty	203,455	203,455	5.22	5.22

In the period since the previous report, there has been no change in the structure of shareholding of the issuer's shares by shareholders holding at least 5% of votes at the general meeting of shareholders.

8. Statement of changes in the shareholding of the issuer's shares or rights to them (options) by the Management Board and the Supervisory Board, in accordance with the knowledge of the issuer, in the period since submission of the previous report

On the submission date of this report the following members of the Management Board and Supervisory Board held shares of PROCHEM SA:

- Jarosław Stępniewski – 80,943 pcs
- Marek Kiersznicki – 70,393 pcs
- Krzysztof Marczak – 43,700 pcs
- Andrzej Karczykowski – 115,186 pcs
- Marek Garliński – 88,000 pcs

In the period since the publication of the annual report for 2016 there was no change in the shareholding of the issuer's shares by members of the Management Board and the Supervisory Board.

9. Information on proceedings pending before the court, competent authority for arbitration proceedings or for public administration body, including information on:

- a) proceedings relating to liabilities or receivables of the issuer or of its subsidiary, which value is at least 10% of the equity of the issuer, with the specification of: the subject of the case, the amount in dispute, date of initiation of proceedings, the parties to the proceedings and the position of the issuer,
- b) of two or more proceedings relating to liabilities and receivables with a total value, respectively of at least 10% of the equity of the Issuer, with determining total value of proceedings separately in the group of liabilities and in the group of receivables, with the position of the issuer in this case, and in relation to the most significant proceedings in the group of liabilities and in the group of receivables – with an indication of their subject, the amount in dispute, date of initiation of proceedings, as well as parties participating in the such proceeding.

PROCHEM S.A. continues to be a party to the proceedings before the court concerning the settlement of the contract which was interrupted on 10 November 2005, for the construction management of an investment project under the name "Pipeline in a section from the ST- 1 Adamowo - to raw material base Plebanka" concluded with PERN S.A. PROCHEM S.A. filed a lawsuit to the court for payment of PLN 41, 301 thousand under the final settlement of the contract, of which PLN 17,364 thousand is recognized in the statement of financial position as a receivable from seized guarantee deposit, and the remaining amount is the contingent receivable. On 18 January 2008 District Court in Warsaw issued a judgment in this case considering claim of PROCHEM S.A. as to be right in principle, while stating that this obligation is not yet due.

On 26 August 2008 the Court of Appeal in Warsaw issued a final judgment on the appeal lodged by PROCHEM S.A. from the a/m judgment of the District Court, recognizing in it that the claim filed by PROCHEM S.A. regarding accounting for the contract is not premature, and at the same time has ordered that the District Court will make the accounting for the contract mentioned above pursuant to the provisions of the contract. This finding is in compliance with position in a case of PROCHEM S.A.

On 12 August 2010 the hearing was held before the District Court in Warsaw, where the Court decided to appoint an expert - Warsaw University of Technology – Department of Civil Engineering, who according to the recommendations of Court of Appeal will make an ultimate accounting for in relation to the disputed contract. In April 2011, the case file was forwarded to the expert witness, who in an opinion published in May 2012 confirmed the amount of the claim of PROCHEM S.A. By order of May 31, 2012, the District Court granted

the Warsaw University of Technology a remuneration for opinion in the case, in relation to which the defendant PERN lodged a complaint. According to PERN SA the prepared opinion could not be the basis of the findings of facts of the case for the Court, because it is contrary to the thesis of the Court in which was determined the basis and scope of the opinion.

The Court of Appeal in Warsaw, I Civil Division has cancelled the decision of the District Court which was contested by PERN SA and the request for remuneration of an expert for the drafting of an opinion has submitted to the District Court for reconsideration.

On 5 February 2013 before the District Court in Warsaw, a hearing was held with the participation of experts, after which the court decided to oblige the parties to submit the pleadings in which the final conclusions of evidence to complement the expert opinions will be clarified, and postponed the hearing until 16 May 2013.

By order dated February 25, 2013, the District Court in Warsaw XXVI Economic Department upheld the previous decision of the Court, and finally has awarded a remuneration for the expert for drafting the opinion. In grounds for the judgment the Court determined that, at the hearing on 5 February 2013, the certified expert has carefully explained the methodology that has been adopted for the preparation of the legal opinion and it is not inconsistent with the thesis of the Court, and there are no legitimate grounds to complaint that the methodology adopted by the experts is not correct.

On 14 May 2013, the Issuer received a notice from the District Court in Warsaw of revocation hearing scheduled for 16 May 2013 and the next date of hearing has not been appointed yet.

On 9 August 2013, the Issuer received from the District Court in Warsaw, the decision as of 1 August 2013, from closed session of the Court. At the meeting, the Court decided to admit evidence of a supplementary opinion of research institute - Warsaw University of Technology in Warsaw, in the circumstance of determining the value of services, supplies, and other liabilities made by PROCHEM S.A. and directly related to the implementation of the agreement that have been made after the date of withdrawal from the contract on the basis of commitments contracted prior to the withdrawal from the contract. In November 2013 the experts appointed by the court have started the work associated with the preparation of the supplementary opinion.

On 25 February 2014, the Court received the supplementary opinion that confirms the amount of the claim of PROCHEM S.A.

On 24 October 2014 the court suspended of its own motion the hearing until the removal of formal obstacles that have now been removed and on February 6, 2015, a request was made to continue the proceedings and set a date for the next meeting.

On 4 March 2015 the District Court in Warsaw has scheduled a hearing for 30 April 2015.

At the hearing on 30 April 2015, the Regional Court in Warsaw has pledged experts to supplement the opinion.

On 6 May 2015 in relation to the doubts raised against some aspects of the expert's opinions and in the interest of a faster conclusion of the case, PROCHEM limited the action for payment by the amount of PLN 139 thousand to the amount of PLN 41 162 thousand, along with statutory interest.

On 17 July 2015 the Company received a copy of the supplementary opinion expert, which in all cases had confirmed the position of PROCHEM S.A.

On 22 October 2015 the District Court in Warsaw, XXVI Commercial Division announced judgment in the above matter, in which:

- in the main action, jointly and severally for the benefit of the Issuer and a member of the consortium adjudged from PERN:
 - ✓ amount of PLN 35 086 589.26, with statutory interest from 23 March 2006 until the date of payment;
 - ✓ amount of PLN 4 879 883.58, with statutory interest from 22 March 2006 until the date of payment;
 - ✓ amount of PLN 126 400,4, with statutory interest from 16 January 2007 until the date of payment.
- in the cross action, dismissed the action of PERN entirely.

Against this sentence above, on December 7, 2015 PERN lodged an appeal. Date of the consideration of appeal was set for October 16, 2017.

Furthermore, the total value of other proceedings separately for group of liabilities and as well as for group of receivables does not exceed 10% of the equity of the Issuer.

10. Information on one or more transactions concluded by the issuer or by its subsidiary with related parties, if separately or jointly they are significant and were concluded on terms other than market terms:

- a) subject of the transaction,
- b) connections of the issuer or of its subsidiary with the entity which is the party to the transaction,
- c) the material terms of the transaction with particular emphasis on financial conditions and the indication of the specific conditions determined by the parties, characteristic

of this agreement, in particular differing from conditions commonly applied for such contracts.

In the first half of 2017 there were no material transactions with related entities in the PROCHEM S.A. Capital Group concluded on other terms than market terms.

11. Information on granting surety of loan or borrowing or guarantee by the company or by its subsidiary, to one entity or to its subsidiary, if the total value of existing sureties or guarantee is equivalent to at least 10% of the issuer's equity

In the first half of 2017 the companies of the Capital Group did not grant sureties or guarantees.

12. Other information that in the issuer's opinion is essential to the assessment of the human resources, financial position, financial results and changes in them, and information that is essential to assess the possibility of fulfilment the obligations by the companies from the issuer's capital group

In connection with a loss on operations, noted in 2016 as well as a significant decrease in turnover, was carried out a detailed analysis of existing financial resources, of obtained credit limits and was introduced the program to adapt of the operating costs to the revenues planned. In the effect, the Management of the Capital Group believes that no exists any jeopardy for the continuation of stable activity in the nearest period. In addition, on October 16, 2017 the court will consider the appeal lodged by PERN SA, against the verdict of October 22, 2015, by which was adjudged the amount of PLN 90 million (including default interest) for the benefit of the consortium with the participation of the Issuer. The Issuer's share in this sum amounts approximately 50%. According to the Management Board, it is highly probable that a positive judgement will be made.

13. Factors which in the opinion of the issuer will have an impact on the financial performance achieved by the capital group in the prospect of at least the subsequent quarter

Macroeconomic surrounding will have the significant effect on the development possibilities of the Capital Group of PROCHEM S.A. in 2017, in particular the condition of the Polish economy which in the significant way influences the undertaking of decisions on the starting of new investment objectives by the potential clients of the Capital Group of PROCHEM S.A. (in particular by industrial companies). After the slump of investment in 2016, some of the investment projects, which were previously suspended in the energy, chemical and environmental sectors, now are being launched. In many of them the companies from the Capital Group of PROCHEM S.A. have a chance to participate. This will be reflected in the number of orders obtained by the Group, and also in the financial results achieved in 2017. The Management Boards of companies from the Capital Group of PROCHEM S.A. with particular attention is monitoring the current situation and, if necessary, is prepared to take appropriate actions in order to adapt its potential to new opportunities.

A large impact on the results of the Capital Group will have the continuation of construction and commercialization of the Astrum Business Park Centre in Warsaw.

Krzysztof Marczak
Vice President
of the Management Board

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Vice President
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