

**REPORT OF MANAGEMENT BOARD
ON ACTIVITIES OF PROCHEM S.A. CAPITAL
GROUP
IN THE FIRST HALF OF 2014**

Warsaw, 29 August 2014

1. Principles of presentation of financial statements.

Description of the rules according to which consolidated financial statements of PROCHEM S.A. Capital Group for the first half of 2014 have been prepared was included in Notes to the Statement.

2. Overview of basic economic and financial volumes disclosed in the interim financial statements and the presentation of the development prospects of Issuer's Capital Group until the end of 2014.

In the first half of 2014 Capital Group achieved revenues from sales in the amount of PLN 66.7 million. They were by 7.4% higher than those achieved in the first half of 2013. The increase in revenues was primarily recorded in the parent company - PROCHEM SA, where revenues from sale of services in the first half of 2014 after an increase of 45% amounted to over PLN 45 million. The structure of revenues has been changed – there was an increase in sale related to contracts for implementation. There has also been significant improvement in the achieved results of activity at both the result from operating activities and the profit for the period.

Macroeconomic environment will continue to have a significant impact on the operations of PROCHEM S.A. Capital Group, as well as to a large extent continuation of two projects which were launched in the first half of the current year: contract on Belarus and construction of Astrum Business Park in Warsaw.

3. Description of significant achievements and failures during the first half of 2014

In the first half of 2014 Group has focused its activities on continuing the project implemented in Belarus, as well as on projects executed for the companies belonging to Solvay Group, Ciech Group, Posco Engineering & Construction and a jointly controlled company Irydion Sp. z o.o, (development project - construction of the Centre Astrum Business Park in Warsaw).

We still strive to seek for new tenants to fill the surface of our new office complex "Astrum Business Park" in Warsaw.

4. Description of factors and events, in particular, of an unusual nature, having a significant impact on the financial results.

In the first half of 2014, there were no significant events which would have impact on the results achieved.

5. Description of risk factors and threats to the activities of Issuer's Capital Group

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

5.1 Economic fluctuations on the investment market

Some of the companies belonging to the Group provide services to the investment market, which is characterized a large scale of fluctuations in demand that 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 (accumulation of financial reserves, diversification of services provided), cannot fully mitigate this risk.

5.2 Dependence on the staff

The risk of dependence on the staff in particular occurs in the Parent Company. Raising the quality of services provided, undertaking the implementation of complicated technological projects, the use of modern information systems, and the work for reputable 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.

5.3 Exchange rate risk

Some contracts (mainly of parent company) for the sale of services were concluded with foreign companies in foreign currencies (EUR, USD). In case of significant stiffening of domestic currency this could adversely affect 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 as through the purchase of the relevant financial instruments.

5.4 The risk of an adverse outcome of litigation with PERN SA.

In view of substantial prolongation of legal proceedings in a dispute with PERN S.A. which was started in 2006, and is pending currently before the District Court in Warsaw on the settlement of the contract which was interrupted on 10 November 2005 for the implementation of an investment project under the name "Pipeline in section from the ST-1 Adamowo to Plebanka raw material base" PROCHEM SA was forced to fulfill their obligations related to retained guarantee deposits from subcontractors,

before receiving them from PERN SA. In the case of unfavorable decision in the process the Management Board of PROCHEM SA takes into consideration the lack of possibility of the recovery of financial resources allocated to these payments.

6. Description of the Capital Group with indication of consolidated entities

PROCHEM SA Capital Group consists of the following subsidiaries directly and indirectly as well as jointly controlled entities and associates:

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%);
- Pro-Organika Sp. z o.o. seated in Warsaw – subsidiary directly (91.4%);
- PROCHEM Serwis Sp. z o.o. seated in Warsaw – subsidiary indirectly (89.1%);
- PREDOM Sp. z o.o. seated in Wrocław – subsidiary indirectly (81.1% share in capital and profit, 69.4% of votes);
- PROCHEM Zachód Sp. z o.o. seated in Słubice – subsidiary directly (80.0%);
- ELPRO Sp. z o.o. seated in Kraków – subsidiary indirectly (88.4%, including 76.8% share in 50% share of Elektromontaż Kraków);
- Elmont Inwestycje Sp. z o.o. seated in Krakowie – subsidiary indirectly (88.4%, including 76.8% share in 50% share of Elektromontaż Kraków);
- Elektromontaż Kraków S.A. – subsidiary indirectly (76.8%), of which 65.1% of capital and voting rights belongs to company PROCHEM Inwestycje a 100 % subsidiary. Elektromontaż Kraków S.A. prepares consolidated financial statements, which contains data of a 100% subsidiary : ELMONT-POMIARY seated in Kraków 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 in 100% ;
- ATUTOR Integracja Cyfrowa Sp. z o.o. seated in Warsaw – subsidiary indirectly (87.3% of share belongs to company PROCHEM Inwestycje Sp. z o.o. a 100% subsidiary);
- PROCHEM RPI Sp. z o.o. seated in Warsaw – subsidiary directly and indirectly in 100%;

Jointly controlled and associated entities covered by consolidation using equity method:

- ITEL Sp. z o.o. Gdynia – 42% of share -(18.7% share in voting rights and capitals belongs directly to PROCHEM S.A., and 23.3% belongs to PROCHEM RPI Sp. z o.o. a 100% subsidiary)
- Irydion Sp. z o.o. seated in Warsaw – 50% of share

The rule adopted at the consolidation is that the entities not leading activities are not included into consolidation - financial data of these companies do not distort information about the financial results of PROCHEM SA Capital Group. The Company not included into consolidation, and covered by write-down :

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

Subsidiaries and associates included into consolidation were included into the consolidated financial statements from the date of acquisition of control by the parent company.

7. The effects of changes in the structure of capital group, including as a result the business combination takeover or sale of entities belonging to the Issuer's capital group, long-term investments, restructuring and discontinued operations

On 4 January 2014 was completed the liquidation procedure of the subsidiary PRO-PLM Sp. z o.o. seated in Warsaw. Company PRO-PLM was a 100% subsidiary.

On 7 January 2014 the company PROCHEM Inwestycje Sp. z o.o. seated in Warsaw (100% subsidiary) on the basis of the contract of sale of shares acquired 10,000 shares with the nominal value of PLN 5 each, in company Elektromontaż Kraków S.A. seated in Krakow (subsidiary). The total sale price was set as PLN 500 thousand.

On 27 May 2014 the company PROCHEM Inwestycje Sp. z o.o. seated in Warsaw (100% subsidiary) on the basis of the contract of sale acquired 5,000 shares with the nominal value of PLN 5 each, in company Elektromontaż Kraków S.A. seated in Kraków (subsidiary). The total sale price was set as PLN 115 thousand.

In the first half of 2014 subsidiary Elektromontaż Kraków S.A. repurchased 2 024 of own shares for redemption for total amount of PLN 48 thousand. As a result of the purchase of own shares for redemption by the company Elektromontaż Kraków SA a change in structure of participation took place. The share of the Parent Company increased by 0.8% percentage point.

As at 30 June 2014 the participation of Parent Entity in share capital and voting rights in Elektromontaż Kraków increased by 6.4% percentage points to 76.8%.

On 28 March 2014 on the basis of the contract of sale PROCHEM S.A. acquired 20% shares in the company PROCHEM Zachód Sp. z o.o. seated in Warsaw (subsidiary), i.e. 32 shares with nominal vale of PLN 1 thousand with total value of PLN 320 thousand. The total sale price was

set as PLN 100 thousand. After the transaction the Issuer has 80% of share capital and 80% of total number of votes of PROCHEM Zachód.

8. Position of the Management Board in relation to the possibility of realization of previously published forecast of results for the given year, in the light of the results presented in the interim report with respect to the forecasted results

PROCHEM S.A. did not publish any forecasts of financial results neither for the company nor for PROCHEM S.A. Capital Group for 2014.

9. Shareholders holding 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 this quarterly report, including the number of owned shares, their percentage of the share capital, the number of votes 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 knowledge of the Company as at the date of this report, the following shareholders hold at least 5% of votes at the general meeting of shareholders:

Item No.	SPECIFICATION	NUMBER OF SHARES HALD	% OF VOTES IN TOTAL NUMBER OF VOTES	% OF SHARE CAPITAL
1	Agreement PHC including: Steven Tappan	1,179,483 510,000	30.31 13.09	30.28 13.09
2	Legg Mason TFI S.A.	560,549	14.39	14.39
3	Otwarty Fundusz Emerytalny PZU S.A. „Złota Jesień“	387,521	9.94	9.95
4	Noble Funds Towarzystwo Funduszy Inwestycyjnych S.A., including: - Noble Funds Fundusz Inwestycyjny Otwarty	207,792 198,446	5.33 5.09	5.33 5.09

In the period since publication of the annual report for 2013, on 7 June 2014 at the General Meeting of Shareholders, the Group was informed about change in the status of shares held:

- AGREEMENT PHC increase by 1 163 shares, including:
 - Steven Tappan by 203 shares.
- Otwarty Fundusz Emerytalny PZU „Złota Jesień” increase by 521 shares.

Moreover, on 21 August 2014 the Issuer was informed that as the result of purchase of shares in PROCHEM S.A. the participation of one of the funds managed by Nobile Funds TFI SA, i.e. Nobile Funds Fundusz Inwestycyjny Otwarty exceeded 5% of the total number of votes in the company PROCHEM SA, before the transaction the Fund held 192 446 shares which represented 4.94% of the share capital and 192 446 votes from these shares, which represented 4.94% of total number of votes. After the transaction the Fund holds 198 446 shares in PROCHEM S.A., which represents 5.09% of the share capital and 198 446 votes from these shares, which represents 5.09% of total number of votes.

10. Statement of changes in ownership of the issuer's shares or rights (options) held by Management Board and Supervisory authorities, in accordance with the Issuer's knowledge, in the period from the previous report

As at the date of the report the following members of the Management Board and the Supervisory Board held shares of PROCHEM SA:

- Jarosław Stępniewski – 80,943 units;
- Marek Kiersznicki – 70,393 units;
- Krzysztof Marczak – 42,700 units;
- Andrzej Karczykowski – 115,186 units;
- Marek Garliński – 86,400 units;
- Steven Tappan – 510,000 units.

In the period since publication of the previous annual report for 2013 the persons currently included in the Management Board and the Supervisory Board have acquired:

- Marek Kiersznicki – 250 shares
- Steven Tappan - 203 shares

11. Proceedings pending before the court, competent authority for arbitration or public administration including information on:

- a) proceedings relating to liabilities or receivables of the issuer or its subsidiary which value is at least 10% of the equity of the issuer, with the specification of the subject case, the amount in dispute, date of initiation of proceedings, the parties to the proceedings and the position of the issuer,
- b) two or more proceedings relating to liabilities and receivables with a total value respectively of at least 10% of the equity of the issuer, determining total value of proceedings separately in the group of liabilities and group of receivables together with the position of the issuer in this case and, in relation to the most significant

proceedings in the group of liabilities and the group of receivables – an indication of their subject, the amount in dispute, date of initiation of proceedings and the parties to the proceedings.

PROCHEM SA 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 SA 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.

The expert opinion was filed in the Court on 15 May 2012.

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 clarifying the final conclusions of evidence On 9 August 2013, the Issuer received the decision from District Court in Warsaw in which the Court ordered the experts to prepare the supplementary opinion in the scope of the determining the value of services and supplies made by PROCHEM S.A. as well as other liabilities made by PROCHEM S.A. which were directly related to the implementation of the agreement and 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. This finding is in compliance with position in a case of PROCHEM S.A.

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

On June 13, 2014, the Company received notice of the appointment of the meeting by the Court on October 24, 2014.

The value of this procedure exceeds 10% of the equity of the Issuer and Issuer's Capital Group.

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

12. Information on the one or more transactions concluded by the issuer or 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) relationship of the issuer or its subsidiary with the entity who is a party to the transaction,
- c) significant terms of the transaction, with particular emphasis on financial conditions and with indication the specific conditions determined by the parties which are characteristic of this agreement, in particular different from terms commonly applied this type of contracts.

In the first half of 2014 in PROCHEM S.A. Capital Group did not occur related party transactions concluded on other terms than market conditions.

13. Information on surety for loan or borrowing or guarantees granted by the issuer or its subsidiary - jointly to one entity or its subsidiary, if the total value of existing surety or guarantees is equivalent to at least 10% of the issuer's equity

None of the companies belonging to the Group has granted another party a guarantee or credit or loan of this value.

On 14 February 2014 the Company underwrote two promissory notes to the amount of PLN 831 thousand issued by subsidiary PRO-INHUT Sp. z o.o. based in Dąbrowa Górnicza in favour of the client in order to secure the claims.

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

The level of indebtedness and liquidity ratio of companies belonging to the Issuer's Capital Group does not indicate a risk of lack of possibility of fulfillment of liabilities, which makes it a reliable partner in trade.

15. Factors which in the opinion of the Issuer will have an impact on the financial performance of the capital group in at least the subsequent quarter

The results of subsequent quarters will depend mainly on the possibility of obtaining by the companies from the capital group of new contracts for the sale of their services. Large impact on the results of the Issuer Group will have a continuation of two projects launched in the past year: a contract in Belarus and the construction of the Centre Astrum Business Park in Warsaw.

Krzysztof Marczak
Vice President

Marek Kiersznicki
Vice President

Jarosław Stępniewski
President of the
Management Board