



Directors' Report  
on the Operations of Grupa Azoty S.A.  
and the Group  
for the 12 months ended  
December 31st 2016

This Directors' Report presents the key events which occurred in the 12 months ended December 31st 2016 at the Group and Grupa Azoty S.A., the Group's parent.

The Report contains all information which is essential for the assessment of the Group's and the parent's financial condition and assets, including results of their operations, as well as a description of relevant risks and threats. It also presents financial and non-financial indicators, if material for the assessment of the Group's and the parent's condition, as well as additional explanations on the amounts presented in the consolidated and separate financial statements.

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## 1. General information on the Group and its parent

### 1.1. Organisation and structure

#### Parent

Grupa Azoty S.A. is the parent of the Group. Its principal business activities include manufacturing, trading in and service activities related to nitrogen fertilizers, engineering plastics and intermediates. The Company operates its own R&D facilities which focus both on research into new products and technologies, and on advancing the existing products.

Grupa Azoty S.A. has been listed on the Warsaw Stock Exchange since June 30th 2008. It is included in the WIG, WIG30, mWIG 40, WIG-Poland, and WIG-CHEMIA indices, as well as the Respect Index. Its shares are also included in foreign indices: MSCI Emerging Markets, FTSE Emerging Markets, and FTSE4Good Emerging Index.

The parent's principal place of business is located at ul. Kwiatkowskiego 8 in Tarnów, Poland. Since April 22nd 2013, the Company has been trading under its new name Grupa Azoty Spółka Akcyjna (abbreviated to Grupa Azoty S.A.).

Grupa Azoty S.A. is an integrated manufacturer of polyamide 6, marketed as Tarnamid®; it also specialises in the manufacturing of nitrogen fertilizers (nitrogen-sulfur and nitrate).

**The Group** is one of Central Europe's major chemical groups with a strong presence on the market of mineral fertilizers, engineering plastics, OXO products, and other chemicals.

The Group has brought together companies with different traditions and complementary business profiles, seeking to leverage their potential to deliver a common strategy. This has led to the creation of Poland's largest chemical group and a major industry player in Europe. Thanks to its carefully designed structure, the Group offers a diverse product mix, ranging from nitrogen and compound fertilizers, engineering plastics, to OXO products and melamine.

As at December 31st 2016, the Grupa Azoty Group (the "Group") comprised Grupa Azoty S.A. (the "parent") and the following nine subsidiaries:

- Grupa Azoty Zakłady Azotowe Puławy S.A. (Grupa Azoty PUŁAWY),
- Grupa Azoty Zakłady Azotowe Kędzierzyn S.A. (Grupa Azoty KĘDZIERZYN),
- Grupa Azoty Zakłady Chemiczne Police S.A. (Grupa Azoty POLICE),
- Grupa Azoty ATT Polymers GmbH,
- Grupa Azoty Polskie Konsorcjum Chemiczne Sp. z o.o. (Grupa Azoty PKCh Sp. z o.o.),
- Grupa Azoty Koltar Sp. z o.o. (Grupa Azoty KOLTAR Sp. z o.o.),
- Grupa Azoty Kopalnie i Zakłady Chemiczne Siarki Siarkopol S.A. (Grupa Azoty SIARKOPOL),
- Grupa Azoty Folie Sp. z o.o.,
- Grupa Azoty Compounding Sp. z o.o..

Furthermore:

- Grupa Azoty PUŁAWY is the parent of nine subsidiaries and holds ownership interests in three associates,
- Grupa Azoty KĘDZIERZYN is the parent of one subsidiary and holds ownership interests in two associates,
- Grupa Azoty POLICE is the parent of nine subsidiaries, and holds ownership interests in two associates,
- Grupa Azoty PKCh Sp. z o.o. is the parent of three subsidiaries.

The parent and the Group companies were incorporated for unlimited period.

## Parent's subsidiaries

### **Grupa Azoty Zakłady Azotowe Puławy S.A.**

The company has its registered office at Al. Tysiąclecia Państwa Polskiego 13, Puławy, Poland.  
Since April 4th 2013, it has been trading under the name Grupa Azoty Zakłady Azotowe Puławy Spółka Akcyjna (abbreviated to Grupa Azoty PUŁAWY).  
Grupa Azoty PUŁAWY specialises in the manufacturing of nitrogen fertilizers and is one of the largest melamine manufacturers in the world.

### **Grupa Azoty Zakłady Azotowe Kędzierzyn Spółka Akcyjna**

The company has its registered office at ul. Mostowa 30A, Kędzierzyn-Koźle, Poland.  
Since January 11th 2013, it has been trading under the name Grupa Azoty Zakłady Azotowe Kędzierzyn Spółka Akcyjna (abbreviated to Grupa Azoty ZAK or Grupa Azoty KĘDZIERZYN).  
The company's two business pillars are nitrogen fertilizers and OXO products (OXO alcohols and plasticisers).

### **Grupa Azoty Zakłady Chemiczne Police Spółka Akcyjna**

The company has its registered office at ul. Kuźnicka 1, Police, Poland.  
Since June 3rd 2013, it has been trading under the name Grupa Azoty Zakłady Chemiczne Police Spółka Akcyjna (abbreviated to Grupa Azoty POLICE).  
Grupa Azoty POLICE is a major manufacturer of compound and nitrogen fertilizers, and titanium white.

### **Grupa Azoty ATT Polymers GmbH**

The company's registered office is located in Guben, Germany.  
Since July 10th 2013, it has been trading under the name Grupa Azoty ATT Polymers GmbH. It manufactures polyamide 6 (PA6).

### **Grupa Azoty Polskie Konsorcjum Chemiczne Spółka z ograniczoną odpowiedzialnością**

The company's registered office is located at ul. E Kwiatkowskiego 7, Tarnów, Poland.  
Since February 28th 2013, it has been trading under the name Grupa Azoty Polskie Konsorcjum Chemiczne Spółka z ograniczoną odpowiedzialnością (abbreviated to Grupa Azoty Polskie Konsorcjum Chemiczne Sp. z o.o. or Grupa Azoty PKCh Sp. z o.o.).  
Grupa Azoty PKCh provides comprehensive design services encompassing complete design support for investment projects in the chemical industry – from study and concept work, to process and structural design and working plans, to support services during the construction, commissioning and operation of process units.

### **Grupa Azoty Koltar Spółka z ograniczoną odpowiedzialnością**

The company's registered office is located at ul. Kwiatkowskiego 8, Tarnów, Poland.  
Since March 6th 2013, it has been trading under the name Grupa Azoty Koltar Spółka z ograniczoną odpowiedzialnością (abbreviated to Grupa Azoty Koltar Sp. z o.o.).  
Grupa Azoty Koltar provides nationwide rail transport services. It is one of the few organisations in Poland to hold licences required to perform comprehensive repairs of rail car chassis and tank cars used in the transport of hazardous materials (according to RID).

### **Grupa Azoty Kopalnie i Zakłady Chemiczne Siarki Siarkopol Spółka Akcyjna**

The company's registered office is located in Grzybów.  
Since February 11th 2014, it has been trading under the name Grupa Azoty Kopalnie i Zakłady Chemiczne Siarki Siarkopol Spółka Akcyjna (abbreviated to Grupa Azoty Kopalnie i Zakłady Chemiczne Siarki Siarkopol S.A. or Grupa Azoty SIARKOPOL).  
Grupa Azoty SIARKOPOL is Poland's largest producer of liquid sulfur.

### **Grupa Azoty Folie Spółka z ograniczoną odpowiedzialnością**

The company's registered office is located in Tarnów.  
Its principal business is scientific and technical R&D activities.

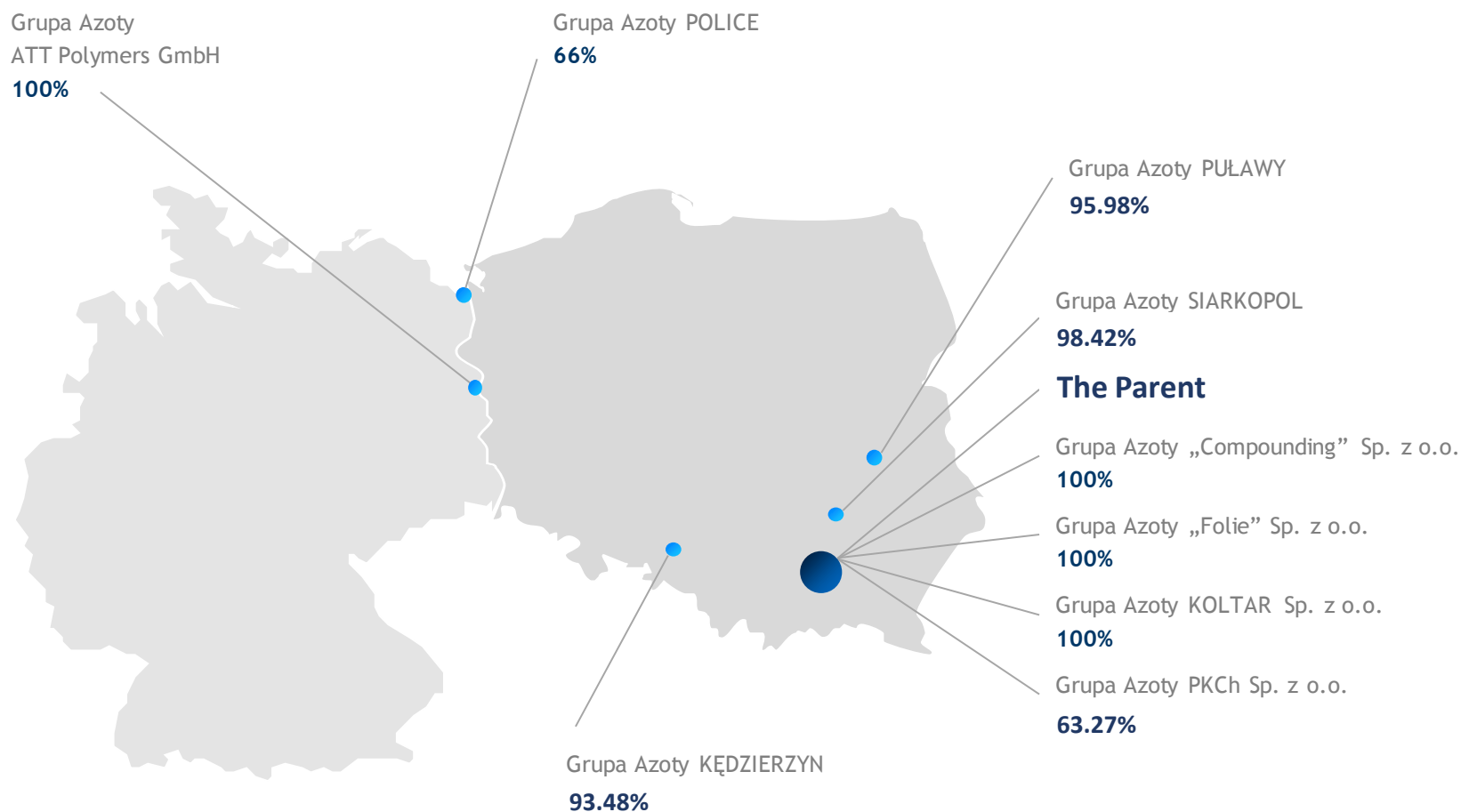
### **Grupa Azoty Compounding Spółka z ograniczoną odpowiedzialnością**

The company's registered office is located in Tarnów.  
Its business model is based on a portfolio of specialty engineering plastics manufactured through the compounding of plastics, with the use of innovative technological solutions.

**The parent's shareholdings in subsidiaries as at December 31st 2016**

Company	Registered office/address	Share capital	% of shares held directly
Grupa Azoty ATT Polymers GmbH	Forster Straße 72 03172 Guben, Germany	EUR 9,000,000	100.00
Grupa Azoty Compounding Sp. z o.o.	ul. Chemiczna 118 33-101 Tarnów, Poland	PLN 5,000	100.00
Grupa Azoty Folie Sp. z o.o.	ul. Chemiczna 118 33-101 Tarnów, Poland	PLN 5,500,000	100.00
Grupa Azoty Koltar Sp. z o.o.	ul. Kwiatkowskiego 8 33-101 Tarnów, Poland	PLN 32,760,000	100.00
Grupa Azoty PUŁAWY	al. Tysiąclecia Państwa Polskiego 13 24-110 Puławy, Poland	PLN 191,150,000	95.98
Grupa Azoty SIARKOPOL	Grzybów, 28-200 Staszów, Poland	PLN 55,000,000	98.42
Grupa Azoty KĘDZIERZYN	ul. Mostowa 30 A skr. poczt. 163 47-220 Kędzierzyn-Koźle, Poland	PLN 285,064,300	93.48
Grupa Azoty POLICE	ul. Kuźnicka 1 72-010 Police, Poland	PLN 750,000,000	66.00
Grupa Azoty PKCh Sp. z o.o.	ul. Kwiatkowskiego 7 33-101 Tarnów, Poland	PLN 85,630,550	63.27

### The parent and its subsidiaries as at December 31st 2016



Source: Company data



## 1.2. Changes in the Group

### Liquidation of Navitrans Sp. z o.o. w likwidacji (in liquidation)

On March 31st 2016, the process of winding up the business of Navitrans Sp. z o.o. w likwidacji (in liquidation) of Gdynia was completed. On March 31st 2016, the amount of cash left after conclusion of the procedure, that is PLN 35 thousand, was paid out to the shareholders. On June 30th 2016, the company was deleted from the National Court Register.

### Agreement to sell shares in Remzap Sp. z o.o.

On December 10th 2015, REMIN Sp. z o.o. and Grupa Azoty PUŁAWY executed a conditional agreement to sell shares in REMZAP Sp. z o.o. (subsequently changed in an annex of February 4th 2016). As REMIN Sp. z o.o. failed to fulfil the conditions precedent by the time prescribed, the agreement is deemed not executed.

On March 14th 2016, 156 shares previously held by the other shareholders (REMZAP Sp. z o.o. employees) were cancelled. As a consequence, Grupa Azoty PUŁAWY's share in total voting rights at the general meeting of REMZAP Sp. z o.o. increased from 95.74% to 96.33%.

## 1.3. Organisational or equity links between the Group companies and other entities

Interests held by subsidiaries in share capital of other Group companies as at December 31st 2016

### Grupa Azoty PUŁAWY

Company	Ownership interest (%)	Share capital
Agrochem Sp. z o.o.	100%	20,000
Agrochem Puławy Sp. z o.o.	100%	50,000
Elektrownia Puławy Sp. z o.o.	100%	92,148
SCF Natural Sp. z o.o.	99.99%	15,001
Gdańskie Zakłady Nawozów Fosforowych Fosfory Sp. z o.o.	99.19%	59,003
STO-ZAP Sp. z o.o.	96.15%	1,117
Remzap Sp. z o.o.	94.61%	1,812
Zakłady Azotowe Chorzów S.A.	94.32%	58,700
Prozap Sp. z o.o.	84.69%	826
Bątycka Baza Masowa Sp. z o.o.	50%	19,500
CTL Kolzap Sp. z o.o.	49%	2,000
Technochimserwis S.A. (closed joint-stock company)	25%	RUB 800 thousand

**Grupa Azoty POLICE**

Company	Ownership interest (%)	Share capital
PDH Polska S.A.	100.00	60,000
Supra Agrochemia Sp. z o.o.	100.00	19,721
Transtech Usługi Sprzętowe i Transportowe Sp. z o.o.	100.00	9,783
Grupa Azoty POLICE Serwis Sp. z o.o.	100.00	9,618
Koncept Sp. z o.o.	100.00	512
Grupa Azoty Africa S.A.	99.99	XOF 132,000 (thousand)
Zarząd Morskiego Portu Police Sp. z o.o.	99.98	32,617
African Investment Group S.A.	54.90	XOF 340,000 (thousand)
Infrapark Police S.A. w likwidacji (in liquidation)	54.43	14,986
Budchem Sp. z o.o. w upadłości likwidacyjnej (in liquidation bankructcy)	48.96	1,201
Kemipol Sp. z o.o.	33.99	3,445

**Shares in subsidiaries indirectly attributable to Grupa Azoty POLICE as at December 31st 2016**

Company	Ownership interest (%)	Share capital
African Investment Group S.A.	0.10	XOF 340,000 (thousand)
Grupa Azoty Africa S.A.	0.01	XOF 132,000 (thousand)
AFRIG Trade SARL	100.00	XOF 33,000 (thousand)

**Grupa Azoty KĘDZIERZYN**

Company	Ownership interest (%)	Share capital
ZAKSA S.A.	91.67	6,000
CTL Chemkol Sp. z o.o.	49.00	4,000
Grupa Azoty Polskie Konsorcjum Chemiczne Sp. z o.o.	36.73	85,631

**Grupa Azoty PKCh Sp. z o.o.**

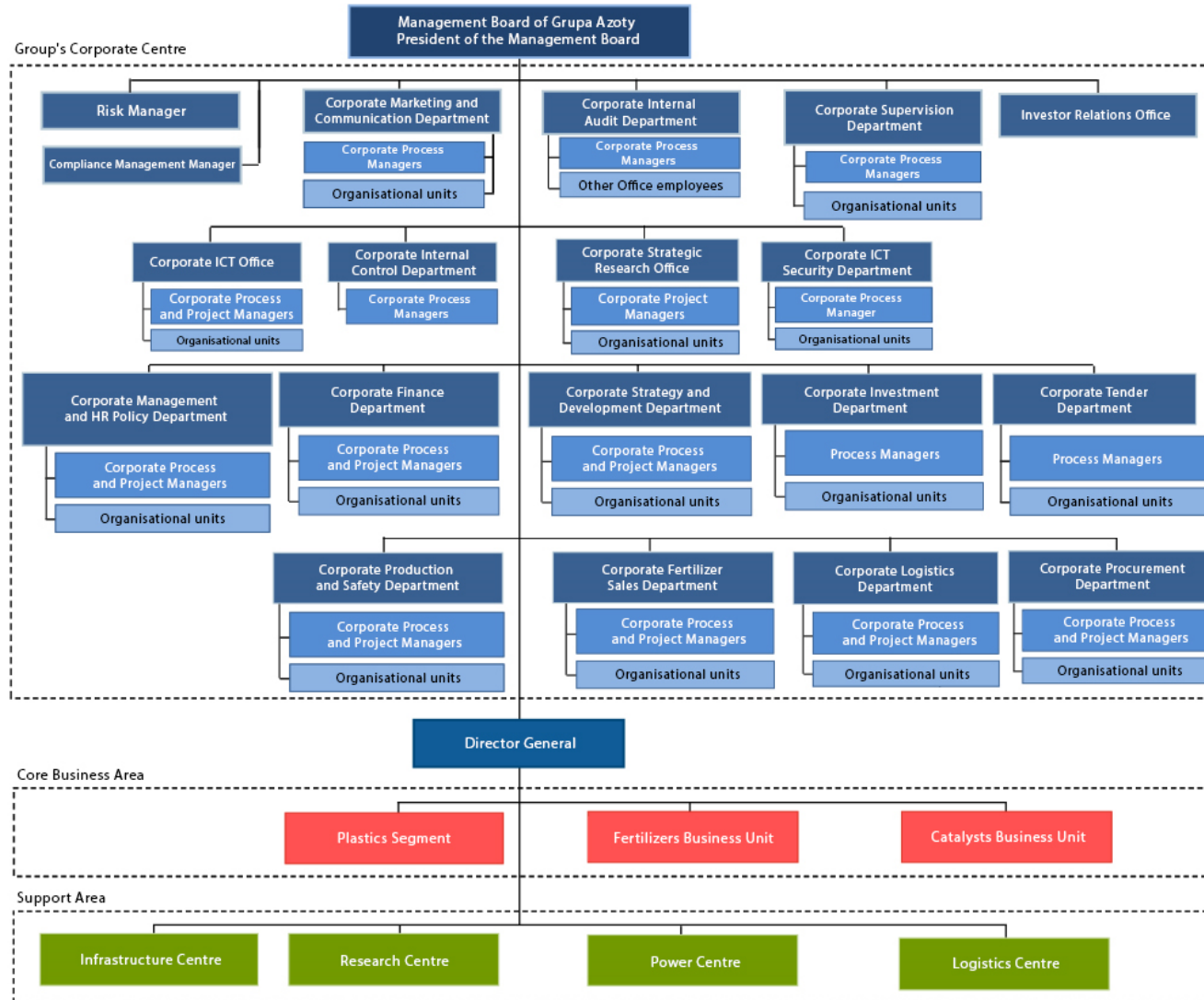
Company	Ownership interest (%)	Share capital
Grupa Azoty Jednostka Ratownictwa Chemicznego Sp. z o.o.	100%	21,749
Grupa Azoty Prorem Sp. z o.o.	100%	11,567
Grupa Azoty Automatyka Sp. z o.o.	77.86%	4,654

**Parent's material non-controlling interests as at December 31st 2016**

Company	Ownership interest (%)
Tarnowskie Wodociągi Sp. z o.o.	12.39%

## 2. Management policy

### 2.1. Parent's organisational chart



## 2.2. Workforce

### Number of employees at the Group

Employee group	as at Dec 31 2016		as at Dec 31 2015	
	Women	Men	Women	Men
blue collar employees	1,297	7,796	1,315	7,554
white collar employees	2,001	3,079	2,015	3,055
<b>Total</b>	<b>3,298</b>	<b>10,875</b>	<b>3,330</b>	<b>10,609</b>
<b>Total – the Group</b>	<b>14,173</b>		<b>13,939</b>	

### Number of employees at the parent

Employee group	as at Dec 31 2016		as at Dec 31 2015	
	Women	Men	Women	Men
blue collar employees	301	988	302	976
white collar employees	335	464	336	463
<b>Total</b>	<b>636</b>	<b>1,452</b>	<b>638</b>	<b>1,439</b>
<b>Total – the parent</b>	<b>2,088</b>		<b>2,077</b>	

### Number of employees at consolidated subsidiaries

Employee group	as at Dec 31 2016		as at Dec 31 2015	
	Women	Men	Women	Men
blue collar employees	995	6,809	1,011	6,580
white collar employees	1,665	2,616	1,677	2,594
<b>Total</b>	<b>2,660</b>	<b>9,425</b>	<b>2,688</b>	<b>9,174</b>
<b>Total – subsidiaries</b>	<b>12,085</b>		<b>11,862</b>	

### Number of employees at the Group: average for the year and as at the end of 2016

Employee group	annual average		as at Dec 31 2016	
	Women	Men	Women	Men
blue collar employees	1,295.2	7,633.9	1,297	7,796
white collar employees	1,980.8	3,057.9	2,001	3,079
<b>Total</b>	<b>3,276.1</b>	<b>10,691.8</b>	<b>3,298</b>	<b>10,875</b>

### Number of employees at the parent: average for the year and as at the end of 2016

Employee group	annual average		as at Dec 31 2016	
	Women	Men	Women	Men
blue collar employees	302.3	979.6	301	988
white collar employees	338.4	467.0	336	464
<b>Total</b>	<b>640.7</b>	<b>1,446.6</b>	<b>636</b>	<b>1,452</b>

**Number of employees at consolidated subsidiaries: average for the year and as at the end of 2016**

Employee group	annual average		as at Dec 31 2016	
	Women	Men	Women	Men
blue collar employees	990.95	6,655.06	995	6,809
white collar employees	1,642.68	2,591.00	1,665	2,616
<b>Total</b>	<b>2,633.63</b>	<b>9,246.06</b>	<b>2,660</b>	<b>9,425</b>

**Employee turnover at the Group from January 1st to December 31st 2016**

	2016	
	Women	Men
New hires	216	944
Terminations	175	652

**Employee turnover at the parent from January 1st to December 31st 2016**

	2016	
	Women	Men
New hires	21	81
Terminations	24	66

**Workforce structure at the Group by education**

Item	Year	Total workforce	University or equivalent	Secondary	Vocational	Primary
Number of employees	2016	14,173	4,144	5,881	3,363	785
Number of employees	2015	13,939	3,874	5,849	3,420	796

**Workforce structure at the parent by education**

Item	Year	Total workforce	University or equivalent	Secondary	Vocational	Primary
Number of employees	2016	2,088	588	834	566	100
Number of employees	2015	2,077	554	859	562	102

**Workforce structure at the Group by length of service**

Item	Year	up to 5 years	6-10 years	11-20 years	above 20 years
Number of employees	2016	1,814 12.8%	1,593 11.2%	2,804 19.8%	7,962 56.2%
Number of employees	2015	1,667 11.9%	1,769 12.7%	2,578 18.5%	7,925 56.9%

**Workforce structure at the parent by length of service**

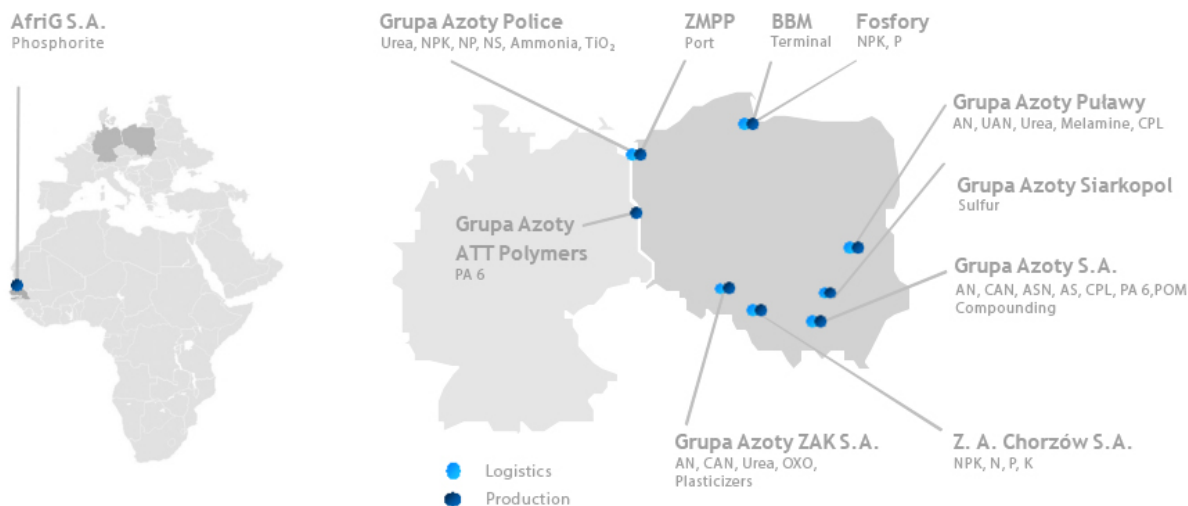
Item	Year	up to 5 years	6-10 years	11-20 years	above 20 years
Number of employees	2016	333 15.9%	132 6.3%	268 12.8%	1,355 64.9%
Number of employees	2015	298 14.4%	117 5.6%	384 18.5%	1,278 61.5%

## 3. Business overview

### 3.1. Business segments

The Group is the largest chemical group in Poland and a significant player in Central Europe. It offers mineral fertilizers and B2B products, including engineering plastics, OXO products and melamine.

#### Core business of the Group



Source: Company data

The Group's business is currently divided into the following segments:

- Agro Fertilizers
- Plastics,
- Chemicals,
- Energy,
- Other Activities.

Segments identified by the parent:

- Agro Fertilizers
- Plastics,
- Energy,
- Other Activities.

#### Agro Fertilizers

Mineral fertilizers are a particularly important area of the Group's business. The Agro Fertilizers segment manufactures nitrogen and compound fertilizers, as well as ammonia and other nitrogen-based intermediate products.

The segment's manufacturing activities are conducted by the companies in Tarnów (the parent), Puławy, Kędzierzyn, Police, Gdańsk, and Chorzów. The Group is Poland's largest and European Union's second largest manufacturer of mineral fertilizers.

#### Plastics

The segment's key products are engineering plastics (polyamide 6 (PA6) and modified plastics) and auxiliary products, such as caprolactam and other chemicals.

They are manufactured by three companies – in Tarnów, Puławy, and Guben (Germany). The Group is the leading manufacturer of polyamide 6 in Poland and the fifth largest integrated producer of PA6 in the European Union.

#### Chemicals

The Chemicals segment is an important part of the Group's business, comprising OXO products (OXO alcohols, plasticisers), technical grade urea, melamine, sulfur and other.

They are manufactured in Kędzierzyn, Puławy, Police, and Grzybów. The Group is the third largest manufacturer of melamine in the world and the second largest manufacturer in the European Union.

The Group is the only manufacturer of OXO alcohols in Poland, and the fifth largest in the EU; it is also Poland's largest and EU's fifth largest manufacturer of plasticizers.

## Energy

Electricity and heat produced by the Energy segment are sold locally, to customers in the immediate vicinity of the Group's plants.

The Group companies are the segment's key customers. Outside the Group, the segment's products are sold on the electricity and hot water markets to local customers. The Group companies operate their own electricity and energy carrier distribution networks.

## Other Activities

The Other Activities segment comprises auxiliary and support services for the Group companies. Like in the Energy segment, the main customers are the Group companies. Outside the Group, the segment provides maintenance services (automation, design, repair, etc.) and logistics services (road transport, rail transport, ports), and conducts manufacturing activities at the Catalyst Production Plant. The segment is also involved in various activities in such areas as environmental protection, administration, research, and infrastructure management.

## 3.2. Key products

### AGRO FERTILIZERS

The Group classifies mineral fertilizers as nitrogen (single-component) fertilizers and compound fertilizers, the latter including at least two of the following key components: nitrogen (N), phosphorus (P) or potassium (K).

#### Nitrogen fertilizers

Nitrogen fertilizers are substances or mixtures of substances where nitrogen is the primary plant nutrient. The Group's product range includes a number of nitrogen fertilizers: urea, nitrate fertilizers (including ammonium nitrate, calcium ammonium nitrate, UAN), nitrogen-sulfur fertilizers (obtained by blending fertilizers in the manufacturing process: ammonium sulfate nitrate, solid and liquid mixtures of urea and ammonium sulfate, and ammonium sulfate). Natural gas is the key feedstock for the production of nitrogen fertilizers.

**Urea** – a nitrogen fertilizer containing 46% nitrogen; it is produced in Puławy (PULREA®, PULGRAN®), Police (mocznik.pl®), and Kędzierzyn. Urea is a universal fertilizer - it can be used for all crops at various growth stages, both in solid state and as a solution. Outside agriculture, urea is used for technical purposes, mainly for manufacturing of adhesive resins, which find application in the chipboard industry. Urea may also be further processed into urea-ammonium nitrate solution (UAN – RSM®), a liquid fertilizer, or into melamine.

#### Nitrate fertilizers

- Ammonium nitrate is a nitrogen fertilizer easily soluble in water, containing between 30% and 34% of nitrogen. The Group offers a wide variety of the product in various granule forms and sizes, such as mechanically granulated ZAKsan® manufactured in Kędzierzyn, with excellent sowing properties; the PULAN® beaded ammonium nitrate from Puławy; or 30 makro™ ammonium nitrate manufactured in Tarnów.
- Calcium ammonium nitrate (CAN) is a nitrogen fertilizer with nitrogen content of up to 28%. It is a universal fertilizer, suitable for all types of soil, well soluble and easily absorbed by crops. The Group markets CAN in a number of granule varieties. The offering includes granulated Salmag® fertilizers (including varieties with a sulfur or boron content), manufactured in Kędzierzyn; or bead fertilizers, such as Saletrzak 27 (CAN 27) standard or Saletrzak 27 with boron.
- Urea-ammonium nitrate solution (UAN-RSM®) is a liquid nitrogen fertilizer coming in three varieties: with 32%, 30% and 28% nitrogen content. Thanks to its form, UAN-RSM® is easily absorbed by plants. It is also produced with an admixture of sulfur, as UAN-RSM®S.

#### Nitrogen-sulfur fertilizers

These fertilizers improve sulfur content in the soil, enhance arable crops' ability to absorb nitrogen, and thus increase the quality and volume of crops.

- Ammonium sulfate is a simple nitrogen fertilizer with sulfur, containing 21% nitrogen and 24% sulfur. It is a by-product in the manufacture of caprolactam and in flue gas desulfurisation processes. The Group offers a wide range of ammonium sulfate in various granule forms and sizes: selection, macro, standard, and crystalline.
- Saletrosan®, or ammonium sulphate nitrate, is a nitrogen fertilizer with sulfur, obtained by blending ammonium nitrate and ammonium sulfate. It contains 26% nitrogen and 13% sulfur.
- Polifoska® 21 is a nitrogen fertilizer with sulfur; it is an ammonium sulfate-urea mix, containing 21% nitrogen and 33% sulfur.
- PULASKA® is a liquid nitrogen fertilizer with sulfur; it is obtained by blending urea and ammonium sulfate, and has a 20% nitrogen and a 6% sulfur content.
- PULGRAN®S - urea-ammonium sulfate, is a nitrogen fertilizer in the form of white hemispherical pastilles, obtained by blending urea and ammonium sulfate. It is manufactured in two varieties: 37% nitrogen/21% sulfur and 33% nitrogen/31% sulfur.

### Compound fertilizers (NPK, NP)

NPK and NP compound fertilizers are universal fertilizers which, depending on composition, can be applied to various types of crops and soil. Aside from the primary components (nitrogen (N), phosphorous (P) and potassium (K)), these fertilizers contain secondary nutrients such as magnesium, sulfur or calcium, and may contain microelements such as boron or zinc.

Compound fertilizers may be used to provide nutrients to all types of arable crops. The Group's current offering includes more than 40 varieties of compound fertilizers, which are marketed under the following trade names: Polifoska®, Polidap®, Polimag® Super Fos Dar 40™, Amofoska®, etc. The Group also offers dedicated fertilizers, custom-made to satisfy customers' specific requirements.

**Phosphorites (phosphate rock)** – feedstock for the manufacturing of compound fertilizers, naturally occurring in various parts of the globe. Phosphate rock is a sedimentary rock containing phosphate-bearing minerals which, after being extracted and beneficiated, are used mainly to produce phosphoric acid. Phosphoric acid thus obtained is an intermediate product used to manufacture compound fertilizers (NP and NPK).

**Ammonia** – feedstock for the manufacture of fertilizers, produced in a process of direct synthesis of nitrogen and hydrogen. Ammonia is the basic intermediate product used to manufacture nitrogen fertilizers and compound fertilizers. It is also used in the chemical industry, e.g. for the manufacturing of caprolactam or polymers, or as a cooling agent. Natural gas is the key feedstock for the production of ammonia.

## PLASTICS

### Engineering plastics

Engineering plastics exhibit high thermal resistance and good mechanical properties. The wide range of the plastics' properties makes them a product of choice for many industries, including automotive, construction, electrical engineering, household appliances, and the food and textile industries.

The Group manufactures polyamide 6 (PA6) and modified plastics (with admixtures affecting the physical and chemical properties of the final plastics) based on polyamide 6 and other engineering plastics (POM, PP, PBT, PA6.6). It also offers modified plastics, custom-made to meet customers' specific requirements.

**Polyamide 6 (PA6)** is a high-quality thermoplastic in granular form used for injection processing. It is the leading product among engineering plastics. The Group's very popular brands in this segment are Tarnamid® and Alphalon®.

### Caprolactam

Caprolactam is an organic chemical compound and an intermediate product used for the manufacture of polyamide 6 (PA6). It is produced mainly from benzene and phenol. Synthesis of caprolactam yields ammonium sulfate as a by-product.



## CHEMICALS

### OXO products

This product group comprises OXO alcohols, plasticizers, and aldehydes.

#### OXO alcohols

Among OXO alcohols, the leading product is 2-ethylhexanol (2-EH), used as a semi-product for a number of processes, including esterification, manufacture of acrylates and fuel additives. They are also used in the paint and varnish industry. Other OXO alcohols manufactured by the Group include n-Butanol and Isobutanol.

#### Plasticizers

Plasticizers represent an important product group. Grupa Azoty ZAK S.A. manufactures three types of plasticizers marketed under the following trade names: Oxoviflex® (DEHT), Oxoplast Medica® (DEHP), Oxoplast® O (DEHP) and Oxoplast® PH (DPHP). They are used in the construction and automotive industries, as well as for the manufacturing of footwear, cables, wires, packaging, and medical products. The Group's flagship plasticizer is a non-phthalate plasticizer DEHT (DOTP), marketed as Oxoviflex®.

The OXO complex also manufactures aldehydes used as semi-products for the production of OXO alcohols. The product offering for third-party customers includes n-butyric aldehyde and isobutyl aldehyde.

The OXO segment also manufactures hydrogen and octanol F used as a flotation agent.

#### Sulfur

The product offered by Grupa Azoty SIARKOPOL is mined sulfur. Sulfur is mainly used to produce sulfuric acid, whose primary application at the Group is the manufacture of DAP (a two-component fertilizer). Sulfur is offered in various forms, including liquid and granulated sulfur. For the Group's needs, sulfur is also purchased from other suppliers who obtain it as a by-product from flue gas desulfurisation or crude oil refining.

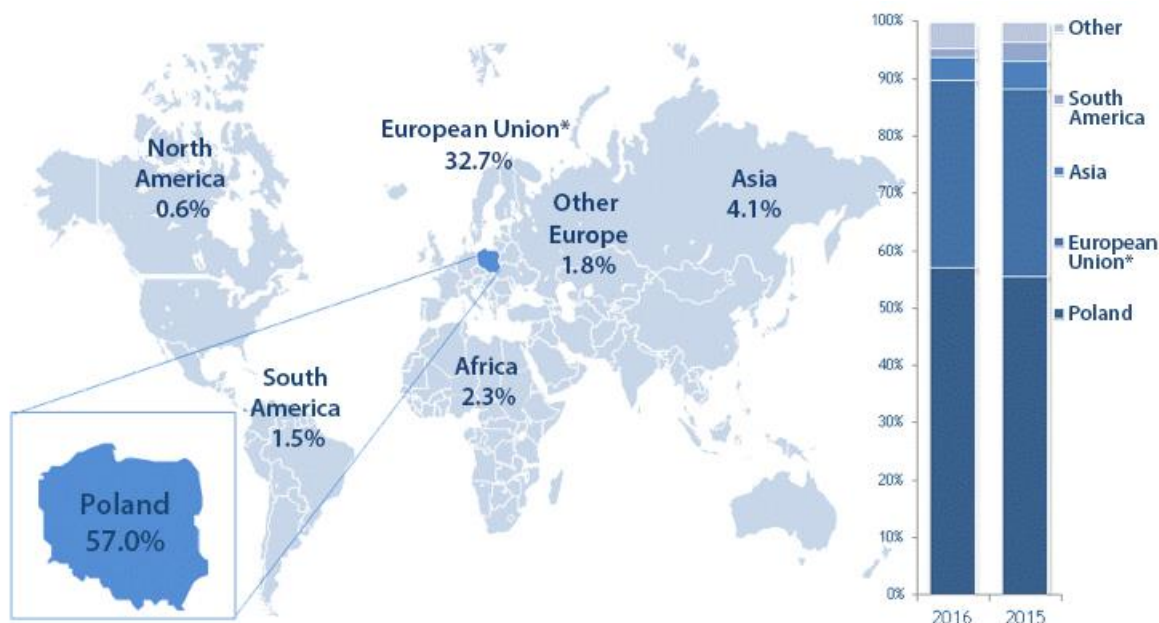
#### Melamine

It is a non-toxic, non-flammable product in the form of a white powder, used for the production of synthetic resins, thermosetting plastics, adhesives, paints, varnishes (including furnace varnishes), auxiliary materials for the textile industry, fire retardants, and other.

### 3.3. Sales markets and procurement of raw materials, merchandise and services

The Group's products are sold all over the world, mainly in the European Union, and on the domestic market.

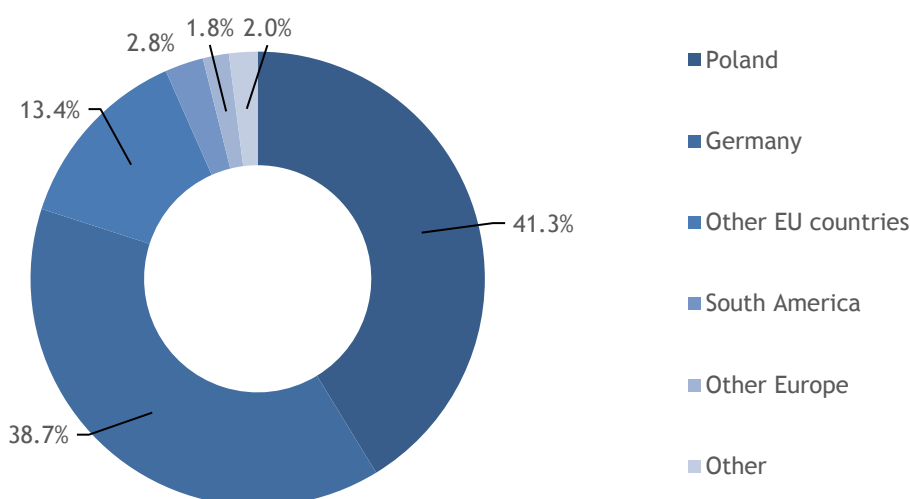
The Group's sales by geographies (by revenue)



\* Excluding Poland.

Source: Company data

The parent's sales by geographies (by revenue)



Source: Company data

In 2016, Grupa Azoty ATT Polymers GmbH, a subsidiary, was the parent's only customer which accounted for more than 10% of the parent's total revenue.

#### Sources of strategic raw materials

For the most part, the Group procures its raw materials, merchandise and services on the domestic and EU markets. Certain raw materials, such as phosphate rock or ilmenite, are purchased from non-

EU suppliers. Raw materials supplied by the Group companies, i.e. ammonia and to some extent sulfur, account for a significant share of total raw materials procured by the Group. In 2016, Polskie Górnictwo Naftowe i Gazownictwo (PGNiG S.A.) was the supplier whose share in the Group's total cost of raw materials exceeded 10%.

#### **Ammonia**

The procurement strategy is based primarily on the optimisation of intragroup supplies (which are executed on market terms). The Group is the largest ammonia manufacturer in Poland and CEE, and operates several ammonia units. It is also one of the largest consumers of ammonia in the region. Having satisfied its own needs, the Group sells surplus ammonia on the market. The Group's ability to effectively secure ammonia supplies largely depends on conditions on the fertilizer market and in the natural gas sector.

#### **Benzene**

Benzene is mainly delivered under one-year contracts, with supplementary purchases made on the spot market. Benzene is sourced chiefly from domestic and CEE suppliers. The benzene market is largely driven by the situation on the crude oil market and the demand-supply balance on global markets, particularly the level of demand for benzene outside Europe.

#### **Phenol**

The procurement strategy is based primarily on supplies from the domestic and the EU markets, with deliveries from outside Europe covering deficit if any. The situation on the phenol market in 2016 was largely driven by developments on the market of benzene (which is the principal component in the phenol pricing formulae) and the volatility of phenol prices reflecting the supply and demand situation on key European markets. The Group secures phenol supplies for its own needs under long-term contracts concluded directly with Europe's largest producers.

#### **Electricity**

The Group purchases electricity from major Polish suppliers, i.e. PGE Obrót S.A., ENEA S.A., and TAURON Sprzedaż S.A. Following a number of tenders for 2016, the Group companies signed electricity supply contracts as part of their existing framework agreements, and – thanks to the Group's procurement strategy and the large volume of supplies – secured electricity prices several per cent lower than in 2015. Given the volatility of the electricity market and its changing legal framework, the Group's policy was to purchase electricity under short-term contracts.

#### **Phosphate rock**

Phosphate rock is purchased under term contracts or on the spot market, chiefly from North African producers, given the mineral's abundance in the region and the well-developed local sea logistics infrastructure. The situation on the phosphorite market is to a large extent driven by the situation in the fertilizers sector. The Group has in place a joint phosphate rock purchase programme for Grupa Azoty POLICE and GZNF Fosfory Sp. z o.o.

#### **Natural gas**

PGNiG S.A. supplied high-methane gas and gas from local sources under long-term contracts. Supplies from other vendors were executed under short-term contracts. In 2016, the Group purchased 70.7% of its natural gas from PGNiG S.A. and the remaining 29.3% from other sources.

#### **Propylene**

The bulk of the Group's purchases of propylene are made under annual contracts, with supplementary purchases made on the spot market. To a large extent, propylene prices are driven by oil prices. The Group has a diversified procurement strategy, based chiefly on supplies from the EU, Russia and other former Soviet Union countries. Supplies from the latter largely reduce the overall cost of propylene procurement.

#### **Sulfur**

The Group is the largest producer and consumer of liquid sulfur on the Polish market and in the region. Its sulfur procurement strategy is based on optimising intragroup supplies (from Grupa Azoty SIARKOPOL) and on supplies from the petrochemical industry. This approach gives the Group considerable procurement flexibility, and significantly reduces the risk of supply shortages. The Group also operates the largest logistics facilities in Poland, which is a source of additional competitive advantage. With a centralised sulfur procurement strategy in place (a Group-wide centralised joint

purchase programme enabling aggregation of supply volumes), the Group is able to reduce the cost of this raw material.

#### **Potassium chloride**

With substantial natural resources and competitive commercial terms, producers from Russia and Belarus are the primary suppliers of potassium chloride. The Group's procurement strategy is chiefly based on framework agreements, with supplementary deliveries sourced from Western Europe. The Group has a centralised procurement strategy and aggregates supply volumes for Grupa Azoty POLICE and GZNF Fosfory Sp. z o.o.

#### **Coal**

The Group purchases coal mainly on the domestic market. Purchasing large volumes of coal of the required quality from geographically remote markets is becoming economically unviable.

On the domestic market, prices of pulverised coal used in the power sector are not directly driven by ARA rates, which only serve as pricing benchmarks for Polish coal producers.

Most of the Group companies purchase coal under short-term contracts with guaranteed prices. Only Grupa Azoty PUŁAWY, due to its coal quality requirements, purchases coal under a long term-contract with negotiable prices. The contracts cover most of the Group's needs.

### **3.4. Significant and material agreements**

The agreements are presented in chronological order.

#### **Significant agreements**

##### **Framework agreement for gas fuel supply and bilateral individual contracts**

On April 13th 2016, the parent and its subsidiaries: Grupa Azoty PUŁAWY, Grupa Azoty POLICE, Grupa Azoty KĘDZIERZYN, Grupa Azoty SIARKOPOL (the "customers") concluded a framework agreement for gas fuel supply and bilateral individual contracts with Polskie Górnictwo Naftowe i Gazownictwo S.A. The framework agreement defines the procedures, the same for all customers, for the execution and termination of individual contracts, placing orders and making payments, suspension of deliveries, reduction of supply volumes, renegotiation, and joint terms of settlement.

The framework agreement was concluded for an indefinite term and covers supplies made as of April 1st 2016. The individual contracts were signed for various supply periods, with the longest one ending on September 30th 2019.

The aggregate VAT-exclusive value of the framework agreement and individual contracts over their effective terms was estimated at ca. PLN 3.3bn.

The framework agreement and the individual contracts provide for gas fuel supplies satisfying over 50% of the Group's demand for gas. For details, see Current Report No. 23/2016.

#### **Material agreements**

##### **Material insurance agreements**

##### **Trade credit insurance at Grupa Azoty PUŁAWY**

In January 2016, the existing trade credit insurance policy with Towarzystwo Ubezpieczeń Euler Hermes S.A. (TUEH S.A.) was renewed for a period from January 1st 2016 to December 31st 2016. The policy covered domestic and export sales of caprolactam and melamine, as well as sales of other products to customers buying caprolactam, melamine, PUC-C and alcohol foreshots. Receivables were insured up to the credit limits set by TUEH (except transactions covered by bank guarantees, letters of credit, or avals).

In January 2016, a new trade credit insurance policy was executed with TUEH S.A. for a period from January 1st 2016 to December 31st 2016. The policy covered exports of fertilizers, sales of NOx<sup>®</sup>, LIKAM<sup>®</sup>, PULNOx<sup>®</sup> to CHPs, power and cement plants, waste incineration facilities, and wastewater treatment plants, as well as sales of technical grade urea on the Polish market.

Receivables were insured up to the credit limits set by the insurer (except transactions covered by bank guarantees or letters of credit). In December 2016, the validity of the insurance policies was extended until January 31st 2017, and subsequently, after the reporting period, new trade credit insurance policies (with the same cover) were concluded with Euler Hermes for the period until January 31st 2018.

### **Construction and assembly risk insurance**

In February 2016, the parent entered into a master agreement for all-risk construction and assembly insurance under an insurance pool set up by ERGO HESTIA/WARTA/PZU. The agreement, effective from February 6th 2016 to June 30th 2018, defines the terms and conditions of insurance of construction and assembly works performed as part of new and overhaul projects under contracts entered into by the Group companies. The insurance also covers construction and assembly works performed by the companies. To be covered by the insurance, construction contracts must be notified to the insurers during the agreement term.

### **Consolidated group insurance programme**

On June 30th 2016, PZU issued insurance policies for four leading companies of the Group, i.e. the parent, Grupa Azoty KĘDZIERZYN, Grupa Azoty POLICE and Grupa Azoty PUŁAWY. The policies cover:

- all-risk property insurance (ALLR),
- all-risk electronic equipment insurance (EEI),
- loss of profit insurance ALLR (BI),
- all-risk machinery insurance (MB).

Also on June 30th 2016, the ERGO HESTIA/PZU/WARTA pool issued annual policies for the Group covering business liability insurance as well as goods in transit insurance for domestic and international shipments.

The policies are valid from July 1st 2016 to June 30th 2017 and were issued under the second annual settlement period of the three-year master agreements signed by the Group's four leading companies, effective from July 1st 2015 to June 30th 2018, which provide the Group with comprehensive insurance cover against catastrophic and material risks.

In November 2016, six companies of the Group, i.e. the parent, Grupa Azoty KĘDZIERZYN, Grupa Azoty POLICE, Grupa Azoty PUŁAWY, Grupa Azoty SIARKOPOL and GZNF Fosfory Sp. z o.o. joined Towarzystwo Ubezpieczeń Wzajemnych PZUW (a mutual insurance company) as a mutual insurance union (*związek wzajemności członkowskiej*).

In November 2016, the same Group companies concluded with PZU S.A. agreements to shorten the terms of and to terminate the master agreements and the ALLR, EEI, BI and MB insurance policies, with effect as of February 28th 2017.

Subsequently, after the reporting period, these companies negotiated and concluded with TUW PZUW a new insurance programme for the two-year period from March 1st 2017 to February 28th 2019, covering:

- all-risk property insurance (ALLR),
- all-risk electronic equipment insurance (EEI),
- loss of profit insurance ALLR (BI),
- all-risk machinery insurance (MB).

### **Environmental insurance**

On July 27th 2016, the Group renewed an insurance policy under the consolidated environmental insurance agreement with AIG Europe Limited Sp. z o.o. Oddział w Polsce (Polish Branch) covering the period from August 1st 2015 to July 30th 2016. The total sum insured is PLN 20m for the Group's four key companies.

### **D&O insurance**

On September 17th 2016, the parent renewed its consolidated directors and officers (D&O) liability insurance agreement with PZU S.A. The insurance provides cover for the Group companies from September 17th 2016 to September 16th 2017. The total sum insured is PLN 200m.

### **Broker Agreement**

The broker agreement concluded on May 31st 2013 by the leading Group companies, i.e. the parent, Grupa Azoty KĘDZIERZYN, Grupa Azoty POLICE and Grupa Azoty PUŁAWY, and a broker syndicate comprising Nord Partner Sp. z o.o. and FST-Management Sp. z o.o. expired on December 31st 2016. The subject matter of the agreement was the provision of insurance brokerage and consulting services.

### **Accession to Towarzystwo Ubezpieczeń Wzajemnych Polski Zakład Ubezpieczeń Wzajemnych (TUW PZUW)**

As the broker agreement expired on December 31st 2016, the Group resolved to implement a new insurance programme and to insure the Group's assets with TUW PZUW. In December 2016, the

parent's Management Board, acting on behalf of the Group's six largest companies, signed a letter of intent and a declaration of accession to T UW PZUW.

In January 2017, the Group commenced negotiations with T UW PZUW concerning a new insurance programme and new terms of insurance cover for the Group's assets as of March 1st 2017.

In the second phase of work on the new insurance programme, the Group expects to conclude with T UW PZUW new insurance agreements to ensure effective cover of the other risks after the existing agreements and policies expire on June 30th 2017.

In the third phase, the other Group companies will be gradually transferred to T UW PZUW.

#### ***Project co-financing agreements***

- On February 2nd 2016, Grupa Azoty PUŁAWY received PLN 3,479.2 thousand under the agreement on co-financing of the 'Construction of NOx reduction units at OP-215 boilers No. 4 and 5 of Zakłady Azotowe Puławy S.A.'.
- On March 24th 2016, the parent received PLN 222 thousand as the second tranche of financing under an agreement concluded on March 30th 2015 between the National Centre for Research and Development of Warsaw and the New Chemical Syntheses Institute of Puławy, the leader of a consortium including the parent. The funds were granted to co-finance a project implemented as part of the Applied Research Programme, Path B: comprehensive processing of waste streams containing sodium sulfate with the use of electromembrane methods, with a view to obtaining a solution of soda lye and sulfuric acid.
- On September 2nd 2016, the parent and the Ministry of Development signed an agreement on a PLN 20m grant for the construction of the Research and Development Centre in Tarnów. The project's total value is almost PLN 88m. The grant received as part of the 'Support for Investment in R&D Infrastructure' measure of the Operational Programme Smart Growth covers almost 30% of the project's eligible costs. On January 31st 2017, an annex to the agreement was signed and amended the schedule of works, expenditure and payments.  
The project's principal objective is to expand the R&D infrastructure to strengthen the scale of the Group's own research activities; to create an environment where results of the research could be verified at pilot-plant scale; and to expand the Group's R&D human resources.  
The expanded R&D infrastructure is expected to facilitate research into advanced materials, modern fertilizer products, new technologies, and environmental care products.  
The scope of the project includes construction of a new laboratory and office building with pilot-plant space, and purchase of the necessary R&D equipment and software.  
In accordance with its Strategy, the Group will allocate up to 1% of its revenue to R&D projects. R&D and innovation activities will be intensified with support from the Chemical Technology and Development Centre in Tarnów.
- On September 22nd 2016, the parent received PLN 569 thousand as the third tranche of co-financing, followed on December 20th 2016 by PLN 6,191 thousand as the fourth tranche of co-financing, under the agreement concluded on June 30th 2014 with the Minister of Environment (represented by the National Fund for Environmental Protection and Water Management of Warsaw) for the project 'Flue Gas Treatment Unit at Zakłady Azotowe w Tarnowie-Mościcach S.A.'. The project was co-financed under the Norwegian Financial Mechanism 2009-2014.
- On December 6th 2016, an agreement was signed for co-financing of the project 'Development of new synthesis route for production of ε-caprolactam from cyclohexanone and hydrogen peroxide with the use of chemo-enzymatic catalysis'. The project will be implemented under the Intelligent Development Operational Programme. The amount of the grant is PLN 2,042.3 thousand.

### **Commercial contracts**

#### **Contract with Uralkali Trading SIA**

On January 21st 2016, Grupa Azoty POLICE concluded a potassium chloride supply contract with Uralkali Trading SIA of Riga, Latvia.

The contract value was estimated at PLN 288m. The contract was concluded for a definite term from January 4th 2016 to December 31st 2016. Under the contract, potassium chloride was to be supplied according to an agreed delivery schedule, in shipments of ca. 3,000 tonnes each.

#### **Contract with PGNiG Supply & Trading GmbH**

On March 11th 2016, Grupa Azoty POLICE entered into a gas supply contract with PGNiG Supply & Trading GmbH of Munich, Germany (a PGNiG subsidiary).

The estimated value of gas supplies under the contract is approximately PLN 151,600,000. The contract sets out the terms of gas supplies to the company between October 1st 2016 and October 1st 2017.

#### **Contract with Nitron Group Corporation**

On April 18th 2016, Grupa Azoty POLICE concluded a potassium chloride supply contract with Nitron Group Corporation of Greenwich, USA (as the seller).

The estimated value of supplies is PLN 176,000,000, and the contract was concluded for a definite term from April 1st 2016 to December 31st 2016. Under the contract, potassium chloride was to be supplied according to an agreed delivery schedule, in shipments of 3,000–15,000 tonnes each.

#### **Contract with PKP Cargo**

On June 23rd 2016, the Group and PKP Cargo entered into a two-year contract for transport of more than 4 million tonnes of fertilizers, chemical products and raw materials.

The contract's total value is estimated at nearly PLN 200m. The Group's cooperation with PKP CARGO is governed by a framework agreement and separate volume agreements concluded between PKP CARGO and five Group companies. These arrangements extended the scope of cooperation between the parties.

Under the new contract, PKP CARGO will provide comprehensive transport services to the Group. The carrier (Poland's largest) will transport fertilizers, chemical products and other cargo in containers to customers in Poland and will handle international shipments for the Group. Some of the shipments will also involve transport of products between the Group companies. Under the two-year contract, PKP CARGO will provide services to the parent, Grupa Azoty PUŁAWY, Grupa Azoty KĘDZIERZYN, Grupa Azoty POLICE and Grupa Azoty SIARKOPOL.

Under a separate contract with Grupa Azoty, PKP CARGO transports coal from coal mines in Silesia and from the Bogdanka mine in the Lublin region. The contract was signed in March 2016 and provides for transport of nearly 900,000 tonnes of coal.

#### **Contract with Thorø Nielsen A/S**

On November 8th 2016, Grupa Azoty POLICE concluded with Thorø Nielsen A/S of Herning, Denmark, a contract for the sale of compound fertilizers and urea.

The contract was executed for a definite period from January 1st 2017 to December 31st 2019, and sets out a specific schedule and other commercial terms of deliveries. The estimated value of the deliveries is PLN 135,295 thousand.

#### **Extension of contract with Lubelski Węgiel Bogdanka S.A.**

On December 6th 2016, Grupa Azoty PUŁAWY signed an annex to the long-term agreement for supply of thermal coal executed by Grupa Azoty PUŁAWY and Lubelski Węgiel Bogdanka S.A. of Bogdanka on January 8th 2009.

Under the agreement, thermal coal is supplied and sold to Grupa Azoty PUŁAWY. The annex extends the agreement until the end of 2021 (previously, the agreement was to expire at the end of 2019) and sets out new terms for the sale of thermal coal:

- the price and volume of thermal coal to be supplied in 2017, and
- the volume of thermal coal to be supplied in 2018–2021.

In individual years of the agreement term the price will be determined by negotiation or will be based on a price formula which takes into account prevailing market prices.

Following the signing of the annex, the estimated value of the agreement from its original date to December 31st 2021 (net of possible increases, deviations and tolerance) currently totals PLN 1,001m (VAT exclusive), including approximately PLN 343m (VAT exclusive) for coal supplies in 2017–2021.

Under the agreement, Lubelski Węgiel Bogdanka S.A. is the main supplier of coal to Grupa Azoty PUŁAWY's CHP plant. The agreement's objective is to secure long-term supplies of coal meeting the customer's specific requirements.

#### ***Commercial contracts concluded after the reporting period***

##### **Contract with Titania AS**

On January 17th 2017, Grupa Azoty POLICE and Titania AS of Hauge and Dalane, Norway, signed a contract for the purchase of ilmenite.

The value of the contract is estimated at PLN 140m. The contract was concluded for a definite term from September 1st 2016 to December 31st 2019. The contract sets out the terms of and schedule for ilmenite deliveries.

### **3.5. Significant events**

#### **The Group named the Champion of Change of Polish Industry**

On January 20th 2016, during the 'We Change Polish Industry' Forum, the Group was distinguished for its 'unprecedented investment projects' and the wide-ranging investment programme currently implemented. In the citation, the organisers emphasized that the projects under way at all of the Group's plants will ensure its stable development and improve its competitive position on foreign markets.

#### **Commissioning of new fertilizer storage facility**

A new bulk storage facility was commissioned at the Tarnów plant in February 2016. It was an important investment project in the Polish fertilizers industry. The facility is not only a part of the fertilizer process line, but also enables the parent to season and store its fertilizer products in appropriate conditions.

#### **Agreement with the Office of Technical Inspection**

On March 9th 2016, the parent and the Office of Technical Inspection (UDT) signed a cooperation agreement. The agreement provides for joint activities to improve safety of the parent's process units and equipment which are subject to technical inspections.

#### **Establishment of the Polish National Foundation**

In July 2016, 17 of Poland's largest companies, including the Group, set up the Polish National Foundation to promote the Polish economy and create a positive image of state-owned companies and their projects in Poland and abroad.

The founders are Poland's leading businesses in the key sectors of the economy: power, transport, logistics, mining, steel, fuels, insurance, chemicals, finance, property, and lotteries.

They include four power groups delivering electricity to more than 90% of customers in Poland, i.e. PGE Polska Grupa Energetyczna, Enea, Energa, and Tauron, as well as Poland's largest gas and fuel companies – Polskie Górnictwo Naftowe i Gazownictwo, PKN ORLEN, and Grupa LOTOS. Other founders are the leading providers of insurance and financial services, i.e. PZU, PKO BP, and the Warsaw Stock Exchange, as well as Totalizator Sportowy, the leader in Poland's lottery market.

The key task of the Foundation is to promote and protect the image of Poland and the Polish economy, and to promote positive reception of projects carried out by state-owned companies. The organization is to work with local communities, social institutions and economic entities, and to undertake and finance social initiatives.

#### **End of negotiations on potential consolidation of the chemical and fertilizers sector**

On July 26th 2016, the parent received from Polski Koncern Naftowy ORLEN S.A. and Anwil S.A. a notice of termination of the non-disclosure agreement executed in January 2015 by and between the parent, the State Treasury, Polski Koncern Naftowy ORLEN S.A. and Anwil S.A., governing confidentiality of negotiations between the parties towards a possible arrangement for potential integration of Poland's chemical and fertilizers sectors. Given its possible adverse effect on the course or outcome of the negotiations, the disclosure of inside information was delayed pursuant to Art. 57 of the Act on public offering, conditions governing the introduction of financial instruments to organised trading, and public companies of July 29th 2005.



### **Research facilities in Kędzierzyn-Koźle**

Grupa Azoty KĘDZIERZYN will establish advanced research facilities. On August 8th 2016, the Ministry of Development and Grupa Azoty KĘDZIERZYN signed an agreement on co-financing of an R&D centre which will focus on research into advanced plastics. Upon completion of the project, an application laboratory will be launched in Kędzierzyn-Koźle to carry out scientific research and development work with the use of the R&D infrastructure. The project's total costs are estimated at almost PLN 13m. Of that amount, PLN 2.8m will be covered by a grant received from the European Regional Development Fund.

### **Extension of exploration licence**

On August 4th 2016, Grupa Azoty POLICE was notified of the following decisions taken by the Ministry of Industry and Mining of Senegal:

- A decision to extend the licence for exploration for phosphates and related substances in the KEBEMER area (Louga region, Senegal), granted to Grupa Azoty POLICE's subsidiary African Investment Group S.A., for another three years starting from July 9th 2016. Formerly, the exploration licence was granted for the period from July 10th 2013 to July 9th 2016. The extended licence covers an area of approximately 472 km<sup>2</sup>. During the new licence term, African Investment Group S.A. is required to spend USD 3m on exploration activities. African Investment Group S.A. is also taking steps to obtain a production licence in the KEBEMER area.
- A decision to refuse to extend the licence for exploration for heavy minerals and related substances in the KAYAR OFFSHORE field (Dakar region, Senegal), held by African Investment Group S.A. The expired licence covered ilmenite as the main mineral, as well as rutile and zirconium. An estimate of mineral resources by African Investment Group S.A. showed that incurring high costs of exploration is too risky. Thus the company did not meet the minimum expenditure requirement defined in the exploration licence, which resulted in the negative decision of Senegal's Ministry of Industry and Mining.

### **New Grupa Azoty R&D centre with financial support from the Ministry of Development**

The Group will create its own Research and Development Centre in Tarnów. On September 2nd 2016, Grupa Azoty and the Ministry of Development signed an agreement for a PLN 20m grant for construction of an R&D centre, marking the launch of the project with a total amount of almost PLN 88m. The grant, received as part of the 'Support for Investment in R&D Infrastructure' measure of the Operational Programme Smart Growth, covers almost 30% of the project's eligible costs.

### **Execution of a letter of intent with Grupa Azoty POLICE**

On October 4th 2016, the parent and Grupa Azoty POLICE signed a letter of intent on the parent's equity participation in the PDH project.

The investment project (construction of a propane dehydrogenation unit for the purposes of propylene production, with an annual capacity of over 400 thousand tonnes) is being implemented by PDH Polska S.A. (the "PDH project"), Grupa Azoty POLICE's subsidiary.

Currently, following a review, the total value of the PDH project covered by a project finance plan (including capital expenditure, capital expenditure reserve, finance cost in the construction phase, debt service reserve account and PDH Polska's operating expenses in the construction phase) exceeds USD 700m (over PLN 2,693m at the mid-rate quoted by the National Bank of Poland for October 4th 2016), with the following model financing structure:

- 30% – subordinated financing (equity and subordinated loan),
- 70% – senior debt.

The letter of intent will remain valid until December 31st 2019 or until the parties resolve to terminate the cooperation. The letter of intent also provides for its optional extension upon the parties' agreement. The final amount of the PDH project's capital expenditure will be known after work is completed on the FEED documentation and the contractor for the delivery of a PFH unit is selected.

### **The Group in FTSE4Good Emerging**

The Group was included in the FTSE4Good Emerging index, following a thorough assessment of its environmental, social and corporate governance practices. The assessment was performed by FTSE Russell in April 2015 and February 2016. Its presence in the index confirms that the Group conducts its business in a transparent and compliant manner.

### Expansion of the SSE Starachowice special economic zone (SSE)

On December 30th 2016, a regulation of the Council of Ministers dated December 22nd 2016 amending the regulation on the Starachowice special economic zone (Dz.U. of December 29th 2016, item 2241) took effect. Under the new regulation, the Starachowice Special Economic Zone – Puławy Sub-Zone was extended to include a land lot located in the Puławy municipality, to which Grupa Azoty PUŁAWY holds a perpetual usufruct right and where the company located its project 'Facility for production of granulated fertilizers based on ammonium nitrate' is to be located. The regulation was issued in response an application submitted by Grupa Azoty PUŁAWY to the Minister of Economy on August 12th 2014, and enables the company to continue its efforts to obtain a licence to operate the project in the Starachowice special economic zone.

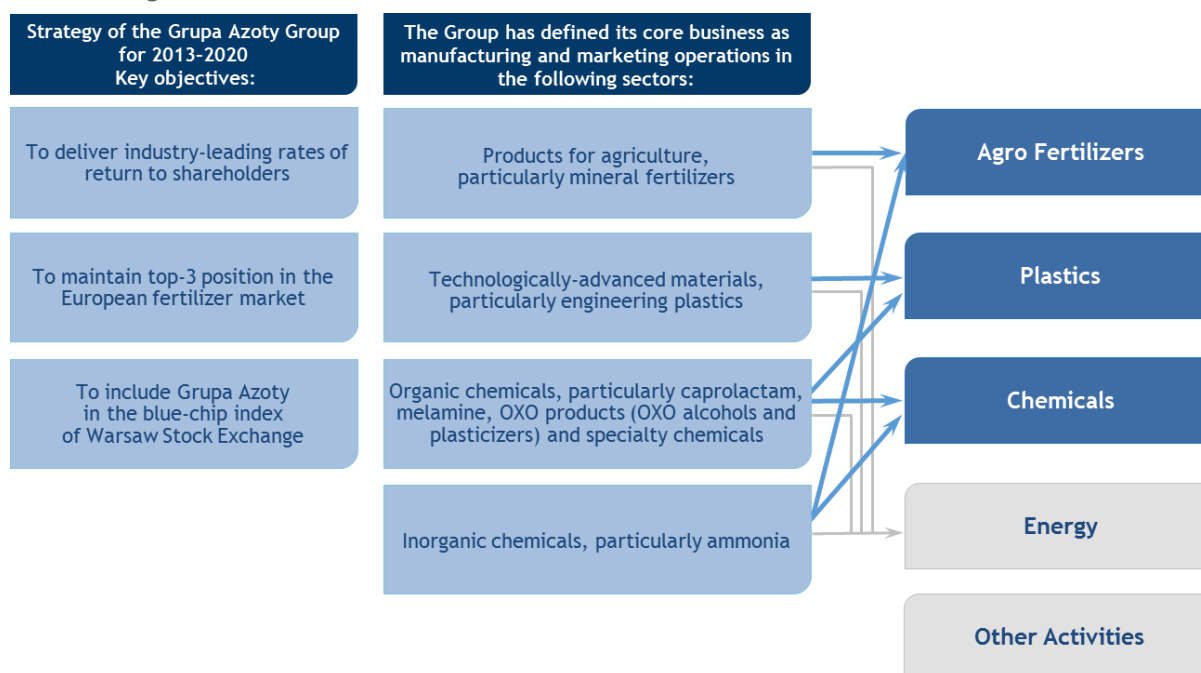
## 4. Growth strategy and policy

### 4.1. Strategy and growth directions

The Group's future growth directions are identified in the Group Strategy for 2013–2020, which sets out a vision of how the Group wants to grow its business and create value in the years ahead; and in the Operationalisation of the Strategy for 2014–2020.

The Strategy sets out the Group's key strategic objectives in the main product areas with respect to innovation, operations, sales and financial policy. The Strategy outlines the corporate management objectives and methodology applied across the Group.

#### Growth targets until 2020



Source: Company data

By 2020, the Group will have three value-creating business segments (Agro Fertilizers, Plastics, Chemicals) and two support segments (Energy - for the Group's own needs, Other Activities), with potential for entry into further areas, including new plastics and professional power generation.

The Strategy will be implemented based on three strategic pillars:

- Organic growth, with capital expenditure estimated at up to PLN 7bn over the seven years between 2014 and 2020;
- Operational excellence programme, with the annual effect on the Group's EBIT expected at PLN 300m;
- Efficiency enhancement through mergers and acquisitions (M&A).

## Strategic areas



Source: Company data

The Operationalisation of the Group's Strategy lists 68 strategic investment and/or marketing projects designed to build the value of the individual segments or of the entire Group as corporate projects – involving more than one segment or implemented at more than one location. The operationalisation also defines the directions of activity in the M&A area.

## Corporate objectives



Source: Company data

The Group's key corporate objectives under the Strategy are to:

- deliver industry-leading returns to shareholders, and
- remain one of the three leading players in the European fertilizer market.

### Mission

"We add life to the soil, and colour to life.

With our accumulated experience and expanding capabilities, we make chemicals safe and useful to people. We consistently strive to increase the value of Grupa Azoty, taking advantage of all available synergies and innovations."

### Vision

"By the end of this decade:

- We will be included in the blue-chip index of the Warsaw Stock Exchange.
- We will deliver industry-leading rates of return for our shareholders.

- We will remain one of the three leading players in the European fertilizer market.”

## 4.2. Growth prospects and market strategy

Below are presented the Group's strategic objectives in key product areas:

### Mineral fertilizers

In the period covered by the strategy, the focal area will be the mineral fertilizers sector, which is of key importance for the Group's business.

The Group is consistently adding new products to its mix of liquid and specialty fertilizers, and other products and services for the agricultural sector.

The Group intends to increase its manufacturing capacity for mechanically granulated nitrate fertilizers. Also, production lines are being upgraded, mainly to reduce energy-intensity and improve cost-effectiveness of the manufacturing processes.

### Plastics

In the period covered by the strategy, polyamides and modified plastics will remain the key elements of the Group's engineering plastics portfolio. The Group continues to increase the scale of production of polyamides and will fully balance the production capacities for caprolactam and polyamides. There are also plans to increase the scale of polyamide composite production.

### Oxoplast

Main activities in the Oxoplast area will involve further expansion of the product portfolio. Work will continue on expanding the range of plasticizers to include non-phthalate plasticizers, next-generation products.

### Pigments

The Police plant is expected to continue as the core facility in the Pigments segment. Planned work will focus on improving the plant's process flexibility and expanding the product range to include products targeted at the most demanding customer groups.

### Melamine

In the Melamine segment, the Group intends to continue its product positioning strategy while it further optimises its logistics processes and potentially adds new distribution channels.

### New areas

Construction of a propane dehydrogenation (PDH) unit is planned to be completed by 2021. Once launched, the new unit will strengthen the Group's position as a producer of oxo alcohols and plasticizers, securing supplies of propylene for the Kędzierzyn plant, with the balance to be exported, thus positioning the Group as an important producer of propylene in Europe.

### Energy

Until 2020, the existing coal-powered co-generation facilities will continue as the main source of heat and electricity for the production plants in Tarnów and Police. The existing CHP units will be gradually modernised, with the scope of upgrades adapted to the changing legal requirements, particularly the environmental regulations.

At Grupa Azoty KĘDZIERZYN, there is a plan to restore the plant's electricity and heat generation capacity, to increase its output to satisfy demand for electricity and heat, and to implement solutions that would ensure compliance with the increasingly stringent environmental requirements. March 23rd 2017 saw the completion of the first stage of construction of a new CHP plant at Grupa Azoty KĘDZIERZYN, and on April 6th the project acceptance protocol was signed with RAFAKO S.A., the general contractor.

At Grupa Azoty PUŁAWY, the project to construct a 400 MWe CCGT unit was abandoned, and a decision was made not to select any bid and to close the tender procedure. It was also announced that the project will be discontinued. On March 31st 2017, the Company's Supervisory Board authorized the Management Board to commence work on the preparation of an investment project to construct a hard coal-fired generating unit, including in particular conceptual and analytical work, followed by the preparation of the terms of reference for the contractor selection procedure. Such unit, tailored to the Company's needs, would secure electricity and heat supplies to Grupa Azoty PUŁAWY.

The Group's ability to secure long-term access to heat and electricity will mainly depend on changes in the regulatory regime and market conditions.

The Group's product and market strategy will be supported by research and development activities carried out in partnership with third parties, while the Group will also use its own R&D resources, developed around the Tarnów Chemical Technology Research and Development Centre and the Puławy Competence Centre.

The main objective of the R&D activities is to build knowledge-based competitive advantage which will facilitate development of a more innovative product, process and technology portfolio. One of the key objectives of the current activities is to increase product diversification, in particular in speciality chemicals.

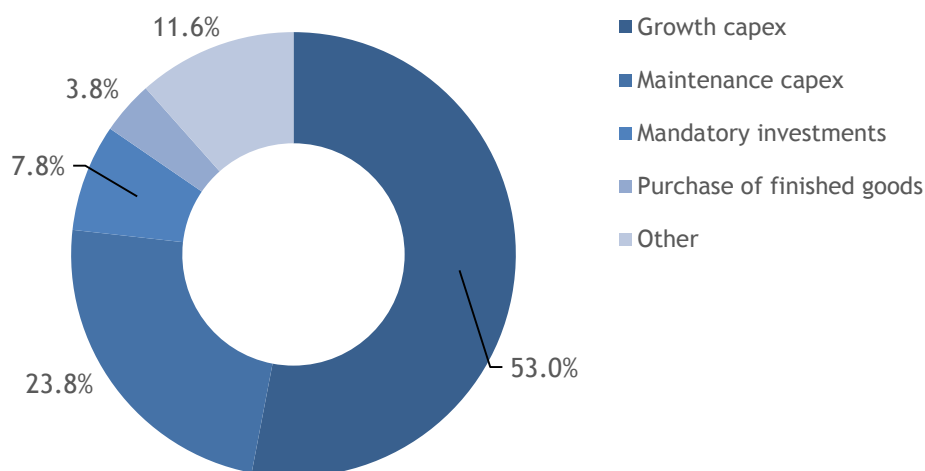
### 4.3. Key investments in Poland and abroad

The Group's capital expenditure is presented below, including amounts spent on plant and equipment, major overhaul work and improvements.

Structure of the Group's capital expenditure in 2016:

• Growth capex	PLN 701,171 thousand
• Maintenance capex	PLN 314,199 thousand
• Mandatory investments	PLN 103,213 thousand
• Purchase of finished goods	PLN 51,117 thousand
• Other (components, major overhaul work, other)	PLN 152,981 thousand

Structure of capital expenditure



Source: Company data

Capital expenditure at the Group in 2016:

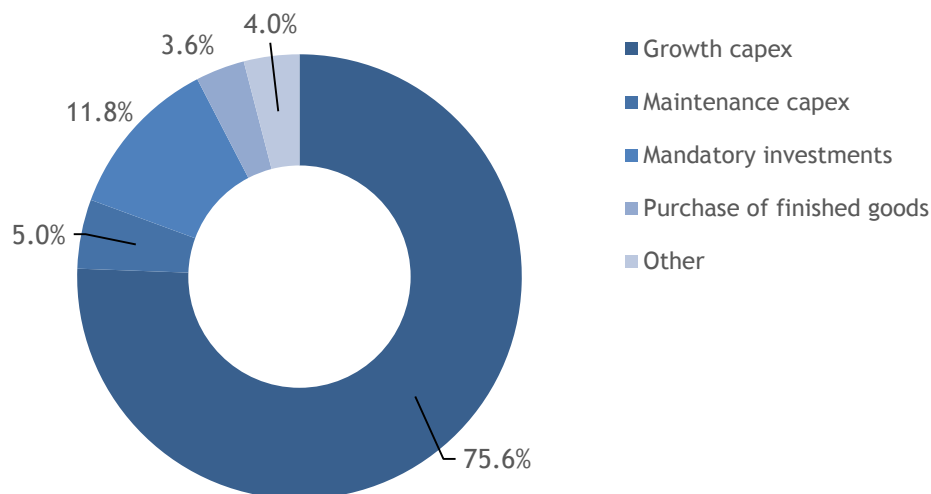
• Parent	PLN 418,218 thousand
• Grupa Azoty KĘDZIERZYN Group	PLN 198,721 thousand
• Grupa Azoty POLICE Group	PLN 402,649 thousand
• Grupa Azoty PUŁAWY Group	PLN 278,718 thousand
• Grupa Azoty SIARKOPOL	PLN 7,064 thousand
• Grupa Azoty PKCh Sp. z o.o.	PLN 6,926 thousand
• Grupa Azoty Koltar Sp. z o.o.	PLN 9,611 thousand
• Grupa Azoty ATT Polymers GmbH	PLN 774 thousand

The parent's capital expenditure is presented below, including amounts spent on plant and equipment, major overhaul work and improvements.

The parent's capital expenditure in 2016:

• Growth capex	PLN 316,057 thousand
• Maintenance capex	PLN 21,072 thousand
• Mandatory investments	PLN 49,297 thousand
• Purchase of finished goods	PLN 14,920 thousand
• Other (plant and equipment, major overhaul work, other)	PLN 16,872 thousand

Structure of the parent's capital expenditure:



Source: Company data

Key investment projects implemented by the Group - Grupa Azoty S.A.

Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
Polyamide plant II 80 thousand t/y	320,000	201,841	149,106	To utilise the Group's caprolactam output in a more efficient manner	2017
Granulation plant II	141,000	113,656	81,652	To optimise the mix of fertilizer products and to improve value added in ammonium sulfate	2017
Construction of Grupa Azoty's R&D Centre in Tarnów	74,100	115	115	To expand the R&D infrastructure to build the scale of the Group's own research activities; to create an environment where results of the research could be verified at pilot-plant scale; and to expand the Group's R&D resources.	2018
20 MW pass-out and condensing turbine generator set at the CHP Plant	63,000	50,081	20,377	To optimise the loads of the existing back-pressure turbine generators	2017
Flue gas desulfurization unit	45,400	30,635	22,353	To reduce sulfur dioxide and dust emissions from CHP Plant's Boiler No. 5, to meet the emission standards laid down in the IED Directive, and to ensure the continuity of power and heat production	2017
Flue gas denitrification unit	44,600	38,510	24,967	To reduce NOx emissions from CHP Plant's Boiler No. 5, to meet the emission standards laid down in the IED Directive, and to ensure the	2017

Directors' Report on the operations of Grupa Azoty S.A. and the Group  
for the 12 months ended December 31st 2016  
(all amounts in PLN '000 unless stated otherwise)

Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
				continuity of power and heat production	
Increase of ammonia production capacities	44,500	39,520	35,430	To increase the Group's own output of ammonia by ca. 100 t/d	2016
New iron-chromium catalyst plant	27,700	27,418	24,565	To build the scale of business in the catalyst segment, to further improve the catalyst quality, to create expansion opportunities, and to increase the customer base	2016
Utilisation of purge gases from the ammonia synthesis unit	23,000	138	138	To ensure optimum utilisation of purge gases from the Ammonia Synthesis Units 1 and 2 and to increase ammonia output	2018
Construction of a new technical-grade nitric acid storage unit - Phase 1	15,000	8,567	8,299	To replace the existing worn out technical-grade nitric acid storage unit	2017

**Key investment projects implemented by the yGroup - Grupa Azoty KĘDZIERZYN**

Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
New CHP Plant at Grupa Azoty KĘDZIERZYN - Phase 1	375,059	287,162	87,511	To restore the plant's electricity and heat generation capacity, to increase its output to satisfy demand for electricity and heat, and to implement solutions that ensure compliance with the increasingly stringent environmental requirements	Completed on Mar 23 2017
Special Esters I	43,435	4,410	3,010	To extend the range of manufactured plasticizers. To construct a new unit to produce several different esters for special applications, in response to the rapidly changing market of plasticisers, particularly plasticizers used as PVC softening agents.	2018
Raw gas compressor (GHH)	31,600	2,306	2,171	To replace the existing depreciated, failure-prone and inefficient K-102 raw gas compressor (GHH), which compresses semi-combusted process gas in the Synthesis Gas Unit, to improve the reliability and availability of the compressor section and the entire OXO Synthesis Gas Unit	2018
Upgrade of the urea unit	30,000	23,748	21,721	To reduce the unit's environmental impact, to build additional production capacity, and to increase process efficiency	2017
Upgrade of the Biological Wastewater Treatment Plant at the Wastewater Treatment and Sewage System Division of the Infrastructure Unit	16,150	8,929	8,514	To substantially improve the quality of treated wastewater - to meet the terms and conditions of the Water Law Decision which defined the permitted pollutant limits for the wastewater discharged to the Odra river, to improve work safety, and to ensure compliance with BAT requirements	2018

### Key investment projects implemented by the Group - Grupa Azoty POLICE

Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
Propane Dehydrogenation (PDH) unit and related infrastructure	2,700,000	77,936	76,936	To construct a propane dehydrogenation (PDH) unit In addition to the PDH unit, a power generating unit will be constructed and a chemicals terminal will be built at the Police port facilities	2021
Exhaust gas treatment unit and upgrade of the EC II CHP plant	226,000	175,562	40,926	To bring the operation of the CHP plant's units in line with the requirements of Directive 2010/75/EU	2017
Upgrade of the ammonia unit	155,600	150,214	82,639	To reduce energy consumption of the ammonia production process and to improve the operational reliability of individual process nodes	2017
Change of the phosphoric acid production method	67,000	27,740	25,021	To raise the efficiency of phosphoric acid production and improve the acid's quality by reducing impurities and waste generation	2018
Development of the logistics system at Grupa Azoty POLICE - stage 2	29,738	25,281	17,294	To increase the number of loading bays for loading fertilizers on pallets and in big bags onto trucks, and to expand the available stacking space for both types of fertilizer packaging	2017
Upgrade of TUP-12 (TG1) turbine generator set and auxiliary equipment	16,000	599	599	To improve reliability, safety, flexibility and quality of turbine control systems	2017
Upgrade of the floodbank around the phosphogypsum landfill site	9,500	9,194	9,067	To increase the floodbank's leak-tightness and to better secure the phosphogypsum landfill site from external waters. The work will improve environmental safety and ensure coherence with the surrounding area.	2016

### Key investment projects implemented by the Group - Grupa Azoty PUŁAWY

Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
Construction of the Puławy Power Plant*)	1,125,000 (as at Dec 31 2016)	8,859	3,842	The key function of the power plant (CCGT unit) will be high-efficiency cogeneration of heat to be used for technological/heating purposes and electricity	2020 (as at Dec 31 2016)
Upgrade of the existing and construction of new nitric acid units, neutralisation and production of new fertilizers based on nitric acid	695,000	544	482	To raise the efficiency of nitric acid production and to improve the economics of production of nitric acid-based fertilizers	2021
Facility for production of granulated fertilizers based on ammonium nitrate	385,000	51,730	42,824	To improve the quality of fertilizers by applying modern mechanical granulation	2020
Replacement of the TG-2 turbine generator set	99,000	11,390	11,068	To increase the efficiency of electricity and heat cogeneration by replacing the TG-2 30 MWe pass-out and condensing turbine with a new	2017



Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
				37 MWe turbine as part of the power system upgrade	
Replacement of the E-E3 ammonium carbamate condenser in the synthesis section of the Urea 2 unit	14,400	12,171	12,117	To improve the unit's operational stability, bring down the failure rate and reduce hydrogen consumption	2016
1,900 Nm <sup>3</sup> hydrogen compressor	12,500	11,846	985	To improve operational stability of the units, bring down the failure rate and reduce hydrogen consumption rates	2016
Construction of a fertilizer compaction unit (GZNF Fosfory Sp. z o.o.)	12,000	13,867	13,572	To expand the company's product portfolio and reduce fertilizer production costs by using less expensive raw materials and a more energy-efficient technology	2017

\*) On March 31st 2017, Elektrownia Puławy Sp. z o.o., conducting the tender procedure to select the general contractor for the construction of a 400 MWe CCGT unit, resolved not to select any bid and to close the procedure. In accordance with resolutions of the Management and Supervisory Boards of Grupa Azoty PUŁAWY of March 31st 2017, the project to construct a CCGT unit will be discontinued.  
At the same time, the Company's Supervisory Board authorized the Management Board to commence work on the preparation of an investment project to construct a hard coal-fired generating unit, including in particular conceptual and analytical work, followed by the preparation of the terms of reference for the contractor selection procedure. Such unit, tailored to the Company's needs, would secure electricity and heat supplies to Grupa Azoty PUŁAWY.

#### Key investment projects implemented by the Group - Grupa Azoty SIARKOPOL

Project	Budget	Expenditure incurred	Expenditure incurred in 2016	Objective	Scheduled completion date
Upgrade of the insoluble sulfur unit SN II	19,000	3,690	3,430	To achieve the unit's design production capacity of 5,000 tonnes pa	2018

## 4.4. Equity investments

### Share capital increase at Automatyka Sp. z o.o.

On January 27th 2016, an increase in the share capital of Automatyka Sp. z o.o. was registered at the National Court Register. The company's share capital was increased by PLN 107 thousand, to PLN 4,654 thousand, through an issue of 214 new shares with a par value of PLN 500 per share, which were all subscribed for by new shareholders (the company employees). As a result, Grupa Azoty PKCh's share in the company's share capital was reduced from 79.69% to 77.86%.

### Share capital increase at PDH Polska S.A.

On October 25th 2016, the management board of Grupa Azoty POLICE passed a resolution to acquire 12,000,000 Series B registered new issue shares in PDH Polska S.A. with a par value and issue price of PLN 10 per share, which will be paid in cash as follows:

- PLN 68,000 thousand – by December 10th 2016,
- PLN 52,000 thousand – by December 31st 2017.

The acquisition was to be effected by Grupa Azoty POLICE taking up the new shares in the increased share capital of PDH Polska S.A.

On November 8th 2016, the management board of Grupa Azoty POLICE resolved to repeal the resolution of October 25th 2016 to acquire 12,000,000 Series B registered new issue shares in PDH Polska S.A.

In the resolution of November 8th 2016, the POLICE management board also decided to acquire 6,300,000 Series B registered new issue shares in PDH Polska S.A. with a par value and issue price of PLN 10 per share, and a total value of PLN 63,000 thousand, to be paid in cash by December 10th 2016.

On November 14th 2016, the POLICE supervisory board approved the acquisition of 6,300,000 Series B registered new issue shares in PDH Polska S.A.  
The acquisition will be effected by the company taking up the new shares in the increased share capital of PDH Polska S.A.

On November 25th, the Management Board of Grupa Azoty S.A. passed a resolution on the parent's equity involvement in PDH Polska S.A.

It was decided that the parent would subscribe for 500,000 Series B registered new issue shares of PDH Polska, with a par value and issue price of PLN 10 per share, totalling PLN 5,000 thousand, with the shares to be fully paid for in cash by December 10th 2016.

The resolution was adopted in connection with the letter of intent signed by Grupa Azoty and Grupa Azoty POLICE on October 4th 2016, concerning, among other things, joint efforts to recapitalize PDH Polska S.A.

On November 30th 2016, the parent's Supervisory Board resolved to approve the equity involvement in PDH Polska S.A.

On November 22nd 2016, the general meeting of PDH Polska S.A. passed a resolution to increase the company's share capital through an issue of 6,800,000 new shares.

#### ***Events after the reporting period***

On February 2nd 2017, an increase in PDH Polska S.A. share capital, from PLN 60m to PLN 128m, was registered.

On March 29th 2017, the Management Board of Grupa Azoty POLICE resolved to acquire up to 5,200,000 new issue Series C registered shares in PDH Polska S.A. The resolution provided for the acquisition of up to 5,200,000 new issue Series C registered shares in PDH Polska S.A., with a par value and issue price of PLN 10 per share and total value of up to PLN 52,000,000.00. The acquisition will be effected by the parent subscribing for new shares in the increased share capital of PDH Polska S.A.

On March 29th 2017, the management board of Grupa Azoty POLICE passed a resolution to acquire, on the first date for exercise of pre-emptive rights, 2,917,875 new issue Series C registered shares in PDH Polska S.A., with a par value and issue price of PLN 10 per share and total value of PLN 29,178,750.00, subject to the supervisory board's approval of the acquisition of up to 5,200,000 new issue Series C registered shares in PDH Polska S.A.

On March 31st 2017, the supervisory board of Grupa Azoty POLICE passed a resolution to approve the acquisition of up to 5,200,000 new issue Series C registered shares in PDH Polska S.A. Thus the condition precedent specified in the Management Board's resolution of March 29th 2017 to acquire 2,917,875 new issue Series C registered shares in PDH Polska S.A. was satisfied.

On April 5th 2017, the parent's Management Board approved the request to be submitted to the Supervisory Board for its consent for the acquisition of non-current assets in the form of 203,125 new issue Series C registered shares in PDH Polska S.A. with a par value and issue price of PLN 10 per share and total value of PLN 2,031,250.00. The acquisition will be effected by the parent subscribing for new shares in the increased share capital of PDH Polska.

#### **Acquisition of shares in Zakłady Azotowe Chorzów S.A.**

On December 14th 2016 Grupa Azoty PUŁAWY acquired from the State Treasury 116,583 shares in Zakłady Azotowe Chorzów S.A., thus increasing its equity interest in Zakłady Azotowe Chorzów by 1.99%, to 94.32%

#### **Acquisition of shares in Grupa Azoty SIARKOPOL**

In accordance with the agreement on sale of shares in Grupa Azoty SIARKOPOL of September 25th 2013 and the provisions of the Social Package, since November 2015, the parent has been buying out SIARKOPOL shares from company employees and their heirs. Up to 825,000 shares are to be purchased as part of the buy-out. As at December 31st 2015, the parent had purchased 176,017 shares, and its share in Grupa Azoty SIARKOPOL's share capital had increased from 85% to 88.20%. In 2016, the parent purchased a further 562,029 shares in Grupa Azoty SIARKOPOL, representing 10.22% of the company's share capital, for PLN 68.45 per share, i.e. for a total amount of PLN 38,471 thousand. Thus, the parent's equity interest in SIARKOPOL was increased from 88.20% to 98.42%.

After the reporting date, the parent acquired 17,466 SIARKOPOL shares, representing 0.32% of the company's share capital, for PLN 1,139 thousand. Following the transactions, the parent holds 98.74% of Grupa Azoty SIARKOPOL's share capital.

#### 4.5. Feasibility of investment plans

In 2016, the parent incurred capital expenditure of PLN 418m (including amounts spent on plant and equipment, major overhaul work and improvements), financed with internally generated funds, proceeds from a corporate set of long-term credit facilities and, to a lesser extent, with lease contracts and grants.

The Group's total 2016 capital expenditure reached PLN 1,232m (including amounts spent on plant and equipment, major overhaul work and improvements) and was financed with internally generated funds, the corporate set of credit facilities (redistributable among Group companies), loans from the National Fund for Environmental Protection and Water Management (NFOŚiGW) and the Provincial Fund for Environmental Protection and Water Management (WFOŚiGW), lease contracts and grants. Under its centralised Financing Model, in 2016 the Group continued to use the set of long-term credit facilities for a total amount of PLN 2,200m, to finance the Group's capital expenditure and other objectives outlined in the long-term strategy. The facilities included:

- a PLN 1,500m syndicated revolving credit facility; as at December 31st 2016, funds available under the facility were PLN 783m,
- term credit facilities – from the EIB (PLN 550m) and the EBRD (PLN 150m); as at December 31st 2016, total funds available under the facilities were PLN 248m.

The Group is able to finance its investment plans using either current or expected free operating cash flows (EBITDA), as well as the corporate credit facilities specified above.

Given the maximum acceptable levels of financial ratios agreed with the strategic lenders, the parent and the Group can further increase its external funding without the risk of breaching covenants under the set of credit facilities, or secure separate financing for projects implemented by SPVs (special purpose vehicles) on a project finance basis.

Considering the above, the Group has the capacity to finance its ongoing and planned investment projects described in Section 4.3. The Group plans to finance the largest ventures, including the PDH project described in Section 3.5, partly with equity and/or subordinated loans from the Group and the SPV's other shareholders, and partly with senior loans provided on a project finance basis to the SPV, without recourse to the Group.

#### 4.6. Significant R&D achievements

##### Parent

In accordance with the Group's R&D strategy, research projects implemented in 2016 focused on:

- improving product quality,
- streamlining the operation of selected production lines,
- developing innovative product technologies.

In implementing those projects, the parent closely cooperated with a number of universities and scientific institutions.

In 2016, the research and development work focused on:

- enhancing the fertilizer manufacturing process through appropriate selection of inorganic additives, as well as anti-dust and anti-moisture agents, to maintain high quality of fertilizers, both in transport and storage,
- continued development of new fertilizer formulas using, among other components, magnesium sulfate and other additives to enhance effectiveness of fertilizers,
- development of new varieties of modified plastics, with the use of various additives to expand the range of specialist applications of the plastics,
- research into reduction of caprolactam manufacturing costs and further improvement of the product quality through optimisation of operation of selected process nodes,
- continued development of new product technologies,
- feasibility studies into possibilities of entering new areas of business,
- development of a new technology for the production of iron catalyst with enhanced properties,
- completion of a project to develop technologies for decomposition of waste sodium sulfate solutions into sulfuric acid and soda lye. The project was co-financed by the National Centre for

Research and Development, and conducted in partnership with the New Chemical Syntheses Institute in Gliwice.

### **Grupa Azoty KĘDZIERZYN**

In 2016, the R&D activities at Grupa Azoty KĘDZIERZYN focused on:

- development of R&D facilities,
- work on fertilizers and plasticizers.

Main research and development work:

- research into new types of plasticizers (non-phthalates), and potential non-alcohol processing of butyraldehydes (intermediate product of OXO synthesis). The company continued research into expanding the offering of non-phthalate plasticizers, including bio-based plasticizers;
- research into new compound fertilizers, including with fertilizers higher magnesium content;
- the National Centre for Research and Development awarded Grupa Azoty KĘDZIERZYN grants for several projects, including:
  - a project to develop technology for obtaining specialty esters ('Review of new technological and process solutions for a wide range of innovative non-phthalic polyester plasticizers in experimental development work on a pilot unit, including with the use of bio-renewable succinic acid'),
  - a project to establish R&D Centre, mainly to conduct research into product applications, and
  - two research projects in the fertilizer industry.

### **Grupa Azoty POLICE**

In 2016, the company's R&D activities focused on:

- research to develop new and enhance the existing technologies,
- pilot technical tests,
- feasibility studies, analyses and expert reports.

The R&D activities were conducted in partnership with research institutions in Poland and abroad.

The work included:

- adjustment of production processes to the requirements of the upcoming fertilizer regulation. In anticipation of the expected requirements to reduce permitted levels of fertilizer contaminants (Cd, Ni, Cr, Pb, As, Hg), the company expended extra effort to improve the quality of its phosphoric acid;
- review of the possibilities to recycle and reuse waste from the manufacturing of titanium white and phosphoric acid;
- verification of the possibility of producing NOXy® solution directly from urea solution discharged from the synthesis unit, an alternative to the currently used NOXy® production method. The new method would reduce the load on the crystallization unit by the amount of urea used in the production of NOXy®, thus enhancing the overall throughput and efficiency of the unit and reducing energy consumption;
- research into a new type of titanium white, to expand product portfolio. The work was focused on improved properties of the output pigment and on application tests;
- research into the method of manufacturing liquid fertilizers and speciality fertilizers using semi-finished products and by-products available at the company.

### **Grupa Azoty PUŁAWY**

In 2016, Grupa Azoty PUŁAWY focused on:

- developing new and enhancing existing technologies,
- improving the company's products.

The key R&D initiatives included:

- On December 6th 2016, the National Centre for Research and Development signed an agreement to co-finance a project carried out by Grupa Azoty PUŁAWY under the INNOCHEM industry programme ('Development of the process for obtaining ε-caprolactone from cyclohexanone and hydrogen peroxide with use of chemo-enzymatic catalysis' (KAPROPOL)).
- Under the INNOCHEM programme, in 2016 the company received co-financing for development and implementation of advanced process controls for the ammonia unit. The project's objective is to upgrade the unit's control system, to improve the process stability, and to ensure optimum conditions of the unit's operation.

- In 2016 the company continued the project 'Support for low-emission agriculture to adapt to climate change now and within the 2030 and 2050 timeframes (LCAgri)', co-financed by the National Centre for Research and Development. The project's objective is to improve efficiency of resource utilisation by implementing innovative low-carbon solutions and by promoting sustainable application of mineral fertilizers in the Polish farming industry.

## 5. Financial condition of the Group

### 5.1. Assessment of factors and non-typical events having a material impact on the Group's operations and financial performance

#### Impairment losses recognised by African Investment Group S.A., a subsidiary of Grupa Azoty POLICE

Further to Grupa Azoty POLICE's Current Report No. 34/2016, a complex, multidimensional process of documentation review and analyses was begun in June 2016 to present a reliable measurement of assets and liabilities associated with African Investment Group S.A., a subsidiary. Analyses and examinations focused primarily on phosphate rock deposits, which represent a material item of the Group's assets, as reported by Grupa Azoty POLICE in Current Report No. 27/2016 of May 30th 2016. Documents held by Grupa Azoty POLICE were analysed and examined in detail, attempts were made to obtain additional relevant information, and work related to impairment testing of the assets was performed, as reported by Grupa Azoty POLICE in Current Report No. 64/2016 of December 22nd 2016.

In the successive quarters of 2016, following completion of the particular stages of reviews and analyses, Grupa Azoty POLICE made adjustments to valuations of individual assets.

In the second and third quarters of 2016, in relation to African Investment Group S.A., decisions were made to recognise impairment losses on past due receivables, to write down phosphate rock inventories as having no commercial value, and to write off exploration and evaluation expenditure on the Lam-Lam deposits and the non-depreciated value of the Lam-Lam field after mining operations in that area were finally discontinued in 2014. In August 2016, a decision was received from Senegalese authorities stating that the exploration licence for the Kayar Offshore field (covering ilmenite, rutile, and zirconium) would not be extended. An estimate of the mineral resources made by African Investment Group S.A. had shown that incurring high expenditure on exploration was too risky. In consequence, intangible assets classified as exploration and evaluation assets relating to the Kayar area were written off and charged to costs.

With no prospects for profitable production from the mineral sand deposits in the Sud Saint Louis licence area (the key factor underpinning the project unprofitability was that the identified heavy minerals resources were not sufficient to ensure the project life of more than five to eight years), a decision was made to write off intangible assets classified as exploration and evaluation assets relating to the Saint Louis area.

Based on a thorough review and analysis of documents, the Grupa Azoty POLICE management board determined that a material error had been made in the final accounting for the acquisition of shares in African Investment Group S.A., which had been presented in the Group's consolidated financial statements for 2014. As a result, the Group's consolidated financial statements for 2015 also contained an error. To rectify the situation, correction of previous periods' errors was made in the 2016 financial statements.

The fundamental error made in the calculations underlying the final accounting for the acquisition was a failure to take into account the need to construct a phosphate beneficiation plant. This led to underestimation of the capital expenditure, operating expenses and time required to reach a stage of project completion where it would be possible to launch production of phosphate rock with commercial value. The change was attributable to the lower quality of phosphate rock deposits in the Kebemer area. Since it had been initially assumed that the phosphate rock would have a high content of phosphorous ( $P_2O_5$  equivalent) and as such would not require traditional flotation beneficiation, but only crushing and screening, natural drying was assumed. However, the drilling campaign carried out between December 2013 and June 2014 in the Kebemer exploration licence area revealed that the field parameters were much worse than initially assumed (with thicker overburden and lower phosphate quality).

Analysis of the documentation also revealed that the assumed size of the resources in the other field (Lam-Lam) was also wrong. To the best of knowledge, the total phosphate rock production from the

Lam-Lam field, which was discontinued in mid-2014, was 110.7 thousand tonnes of phosphate rock, and not 314 thousand tonnes, i.e. the figure used in the final accounting for the acquisition.

The above assumptions were changed as part of the correction of accounting for the acquisition. As a result of correction of the erroneous assumptions, the exploration licences disclosed as the value of mineral deposits (as at August 28th 2013) were revalued.

Following correction of the accounting for the acquisition of African Investment Group S.A. with respect to the acquired exploration licences disclosed in property, plant and equipment as mineral deposits, the net value of the acquired assets and assumed liabilities is negative.

Adjustment to the fair value of the acquired assets (mineral deposits) and the deferred tax liabilities related to those assets, resulted in recognition of goodwill in place of a gain from a bargain purchase. Goodwill of PLN 93,141 thousand, recognised as a result of the correction of the accounting for the acquisition, was allocated to the investment in the phosphate mining facility, identified as a cash-generating unit on acquisition of the majority interest in African Investment Group S.A.

To assess the goodwill recognised on the correction of the accounting for the acquisition, the goodwill was tested for impairment as at December 31st 2013.

The estimated present value of future cash flows determined based on the assumptions made using the then available data was negative. Therefore, an impairment loss was recognised for the full amount of the goodwill.

For a detailed description of the assumptions made for the purpose of impairment testing of goodwill, see the consolidated financial statements of Grupa Azoty for the 12 months ended December 31st 2016.

In the statement of financial position Grupa Azoty POLICE continues to disclose the expenditure incurred on exploration and evaluation of mineral resources from the date of acquisition of shares in African Investment Group S.A., in the amount of PLN 64,047 thousand (of which PLN 63,224 thousand is attributable to the Kebemer exploration licence area). This results from the need to continue the work on examining the geological documentation and the need to obtain a scoping study compliant with international standards, required under the reporting policy implemented by the Group. These activities are expected to be completed in the second half of 2017, and then relevant decisions concerning the future of the project will be made.

**Effect of one-off events related to African Investment Group S.A. on the 2016 net profit/(loss) \***

Item	2016
Impairment losses on receivables past due for more than one year	(20,031)
Write-down of phosphate rock inventories presented under work in progress	(10,838)
Provision for liabilities for technical consultancy related to phosphate rock supplies from Senegal	(9,411)
Write-off of exploration and evaluation expenditure relating to the Kayar area	(900)
Write-off of exploration and evaluation expenditure relating to the St. Louis area	(4,241)
Other adjustments	31
Deferred tax assets/liabilities	581
<b>Effect on net profit/(loss)</b>	<b>(44,809)</b>

\*Amounts translated into PLN at the average exchange rate for XOF in 2016.

**Effect of one-off events related to African Investment Group S.A. on the 2015 net profit/(loss)\***

Item	2015
Impairment losses on exploration and evaluation expenditure relating to the Lam-Lam area	(10,222)
Deferred tax assets/liabilities	(3,407)
<b>Effect on net profit/(loss)</b>	<b>(13,629)</b>

\*Amounts translated into PLN at the average exchange rate for XOF in 2015.

**Effect of one-off events related to African Investment Group S.A. on profit/(loss) brought forward as at January 1st 2015\***

Item	Jan 1 2015
Write-off of the value of the Kebemer deposits	(268,630)
Write-off of non-depreciated value of the Lam-Lam deposits	(2,041)
Deferred tax assets/liabilities	61,704
Exchange differences on translation	(2,977)
<b>Effect on equity</b>	<b>(211,944)</b>

\* Amounts translated into PLN at the historical exchange rate for XOF.

In the consolidated financial statements for 2016, profit before tax includes the following adjustments:

- impairment losses on African Investment Group S.A.'s receivables past due for more than one year, covering 100% of the receivables amount: PLN 20,031 thousand,
- write-down of phosphate rock inventories presented by African Investment Group S.A. as work in progress deemed slow moving inventories for over two years, due to no commercial value of the product: PLN 10,838 thousand,
- recognised provision for future liabilities for technical consultancy related to phosphate rock supplies from Senegal: PLN 9,411 thousand, allocated to other expenses,
- PLN 900 thousand write-off of intangible assets classified as exploration and evaluation assets relating to the Kayar area, following the authorities' decision not to extend African Investment Group S.A.'s exploration licence for ilmenite, rutile, and zirconium deposits in the Kayar Offshore field - an estimate made by AFRIG S.A. showed that incurring high expenditure on exploration was too risky,
- write-off of intangible assets classified as exploration and evaluation assets relating to the St. Louis area by African Investment Group S.A.: PLN 4,241 thousand.

In the consolidated financial statements for 2015, profit before tax includes the following adjustments:

- PLN 10,222 thousand write-off of intangible assets classified as exploration and evaluation assets relating to the Lam-Lam phosphate rock deposits - charged to costs following discontinuation of production.

**Impairment loss at Zakłady Azotowe Chorzów S.A., a subsidiary of Grupa Azoty PUŁAWY**

On February 13th 2017, the management board of Zakłady Azotowe Chorzów S.A. (a subsidiary of Grupa Azoty PUŁAWY) passed a resolution to recognise a PLN 10.0m impairment loss on the assets of the fat processing unit. In accordance with IAS 36, the company's management board identified indications that the recoverable amount of those assets may have decreased below their respective carrying amounts. The fat processing unit continues to operate below its full processing capacity. While the company recently recorded an increase in the average selling price of oleochemicals, prices of the key raw material (liquid animal fat) remain high, which significantly limits the company's ability to generate cash inflows from the sale of stearine and other oleochemicals.

Having considered these indications, the management board of Zakłady Azotowe Chorzów S.A. tested property, plant and equipment and intangible assets for impairment. The test confirmed the validity of recognising another impairment loss on the assets of the fat processing unit. The first impairment

loss of PLN 18.4m was disclosed in the financial statements for 2015. The current impairment loss of PLN 10.0m will be disclosed in the financial statements of Zakłady Azotowe Chorzów S.A. for 2016. The effect of the event described above on the consolidated results of the Grupa Azoty PUŁAWY Group, and thus on the consolidated financial statements of the Group (and, more specifically, on the Group's consolidated EBIT for 2016) is negative at PLN 10.7m, including PLN (0.7m) on measurement of the company's assets at the time of acquisition of Zakłady Azotowe Chorzów S.A. by Grupa Azoty PUŁAWY.

#### **Volatility of exchange rates**

The key factors with a bearing on the Group's financial results in 2016 included the downgrade of Poland's credit rating by S&P and the slowdown in the Chinese economy, followed later during the year by the Brexit referendum in the UK, Donald Trump's surprising win in the US presidential elections, and increased volatility of the emerging market currencies. All these factors spurred three waves of weakening of the Polish zloty against the euro and the US dollar, separated by short-term appreciations of the Polish currency based on the strong foundations of the Polish economy.

During 2016, the Polish currency lost approximately 3.8% against the euro and 7.1% against the US dollar over December 31st 2015. The average PLN/EUR exchange rate in 2016 was approximately 4.4% lower than in 2015, while the average PLN/USD exchange rate declined by approximately 4.5% over the same period.

Decisions by the leading rating agencies, in January 2017, to keep Poland's sovereign credit rating unchanged, coupled with forecasts predicting stable GDP growth, point to further potential strengthening of the Polish currency against the euro in 2017.

However, external risks, including the difficult condition of Italian banks, uncertainty surrounding Brexit and the US' actual policy in relations with Europe will exacerbate the risk of the zloty again depreciating against the US dollar, especially in the wake of the potential weakening of the euro against the US dollar. It can therefore be expected that in 2017 the PLN/EUR exchange rate will remain within the medium-term range (PLN 4.20-4.40), with some room for appreciation if the Polish economy continues to perform well and there is no further escalation of the external risks identified above. In the meantime, the PLN/USD exchange rate may continue to weaken, matching the volatile EUR/USD exchange rate.

Taking into consideration the Group's currency risk exposure, the current and anticipated exchange rate fluctuations are unlikely to pose a risk to the Group achieving its targets for 2017, given that the potential strengthening of the Polish zloty against the euro may entail a parallel weakening of the currency against the US dollar. Furthermore, the political risks in the US and the EU significantly limit the zloty's potential to strengthen its position.

The Group monitors the current and planned net currency exposures and reduces the resulting currency risk by applying selected hedging instruments. In the reporting period, the main tools used by the Group were: natural hedging; factoring and discounting of receivables denominated in foreign currencies; and currency forwards covering up to 80% of the remaining currency exposure with time horizons of less than 6 months, and up to 50% of the remaining currency exposure with time horizons between 6 and 12 months.

Pursuant to the 'Financial Risk Management Policy (currency and interest rate risks)', the Group may enter into hedging transactions with horizons of up to 24 months (as long as such transactions reduce the adverse effect of exchange rate fluctuations on the cash flows, and it is possible to secure the EUR/PLN or USD/PLN exchange rates higher than those assumed in the budget) and up to 3 months (if it is possible to hedge the exchange rate at which a commercial transaction was executed).

Execution of currency hedging transactions where the hedge horizon is more than 24 months or the transaction does not conform to the Financial Risk Management Policy requires approval by the Management Board based on the recommendation of the Finance Committee.

In 2016, the Group's hedging tools were EUR and USD swap forwards, reflecting its planned net exposure in both currencies. The Group's result on hedging transactions executed in the first six months of 2016 was PLN (4,264) thousand. The result on revaluation of hedging instruments was negative at PLN (6,476) thousand.

In 2016, the Group's total result on hedging transactions and revaluation of hedging instruments was negative at PLN (10,741) thousand.

On the unhedged net currency exposure, the Group reported a net gain on realised and unrealised foreign-exchange differences of PLN 10,717 thousand.

In 2016, the Group's total result on foreign exchange differences and currency derivative transactions (including revaluation as at the end of the reporting period) was negative at PLN (23) thousand.

The weakening of the average PLN/EUR and PLN/USD exchange rates relative to 2016, favourable to the Group, was accompanied by strong market volatility, which limited the exchange rates' positive



effect on the Group's financial results in the period. The loss on measurement and exercise of currency forwards was offset by gains on current currency transactions and foreign-exchange differences.

In 2016, the parent's hedging tools were EUR swap forwards, reflecting its planned net exposure. The parent's result on hedging transactions executed in 2016 was PLN (2,733) thousand. The result on revaluation of hedging instruments was negative at PLN (609) thousand.

On the unhedged net currency exposure, the parent reported a realised foreign exchange gain of PLN 1,050 thousand, and a net loss on unrealised foreign-exchange differences of PLN (495) thousand.

In 2016, the parent's total result on foreign exchange differences and currency derivatives (including revaluation as at the reporting date) was PLN (2,787) thousand (including PLN (1,683) thousand on realised foreign exchange differences and currency hedging transactions, and PLN (1,104) thousand on unrealised items and hedging).

Since September 28th 2015, the Group has applied cash flow hedge accounting. The hedged items are highly probable future income from sale transactions in the euro, which will be recognised in profit or loss in the period from December 2018 to June 2025. The hedging, covering currency risk, is a euro-denominated credit facility of EUR 100m as at December 31st 2016, repayable from December 2018 to June 2025 in 14 equal half-yearly instalments of EUR 7,143 thousand each. As at December 31st 2016, the fair value of the facility was PLN 444,874 thousand. As at December 31st 2016, the hedging reserve included PLN (7,165) thousand on account of the effective hedge. In 2016, the Group did not reclassify any hedge accounting amounts from other comprehensive income to the statement of profit or loss.

#### **Prices of CO<sub>2</sub> emission allowances.**

In the first half of 2016, prices of CO<sub>2</sub> emission allowances declined markedly, to rebound in the last quarter of the year. Some of the EUA transactions were executed by the Group at the time when the allowances traded low, which had a positive effect on total valuations of the Group's CO<sub>2</sub> futures at the end of the period. In 2016, the Group reported a PLN 3,502 thousand gain on valuation of the futures.

Some of the transactions were executed by the parent in a period when their prices were low and thus in 2016 the parent recorded a PLN (152) thousand loss on valuation of futures contracts for the purchase of CO<sub>2</sub> emission allowances.

## **5.2. Market overview**

According to the preliminary data released by the Central Statistics Office, in 2016 Poland's GDP growth rate was 2.8%, the lowest in three years. The main drivers of the growth in 2016 were domestic demand and higher total consumption. Investments in capital goods grew at the slowest rate, as the flow of EU funds for infrastructure investments decelerated and a number of projects sponsored by local authorities was put on hold due to the election cycle and the political climate in the country. Exports grew faster than imports and the average exchange rate of the Polish zloty relative to the euro and US dollar depreciated, both factors serving to improve Poland's trade balance. In 2017, the Polish economy is expected to expand by 3%, i.e. is slightly faster than in 2016, while domestic demand is forecast to grow 3.1%, just above the 2016 result. The Gdańsk Institute for Market Economics forecasts that private consumption will increase by 3.3% over the period on the back of the strong labour market and falling unemployment.

## **AGRO FERTILIZERS**

### **Economic conditions in agriculture**

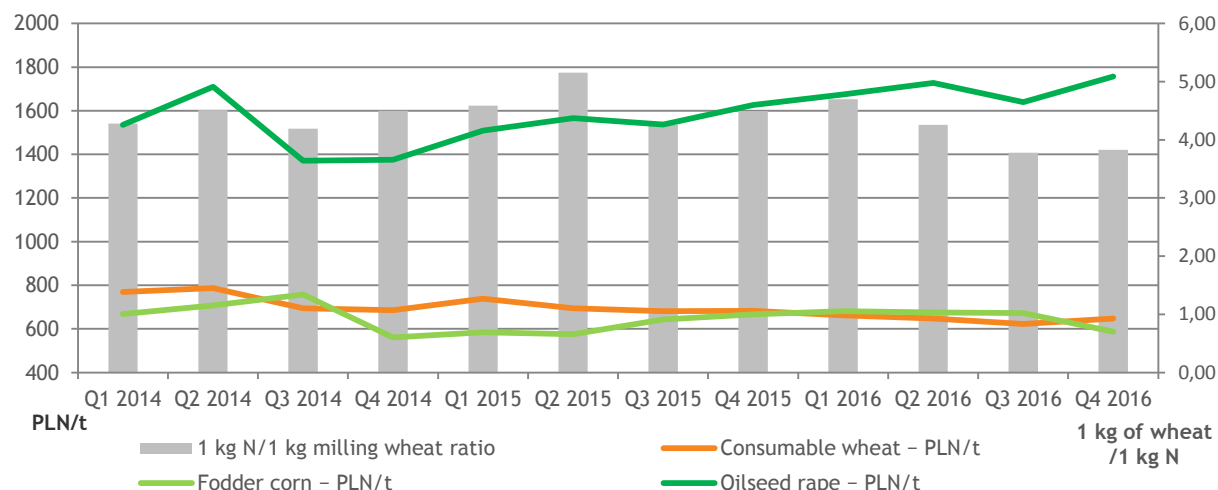
According to the Polish Institute of Agricultural and Food Economics, in 2016 market conditions for agricultural production improved slightly compared with 2014-2015. Between December 2015 and December 2016, the weighted average farm gate prices of basic agricultural produce increased by 4.3%, well above the increase seen in the previous two years and coming close to the price rises in 2013. However, the rise in farm gate prices was not accompanied by the 0.4% decline in prices of means of agricultural production observed in 2016. As a result, the aggregate equalised price differential index was 104.7 points, compared with 95.3 and 89.7 points in 2015 and 2014, respectively.

2016 saw strong crop yields and high global cumulative grain stock volumes. The grain supply pressures, on both the world and national markets, kept prices low with the weakening of the Polish

złoty improving export profitability domestically. Poland's wheat exports were particularly high in July-October 2016. Traditionally, EU subsidies provided strong financial support to farmers.

In 2017, growing prices on certain markets may drive investments in agriculture. Another meaningful factor may be the availability of funds under the 2014–2020 Rural Development Programme.

### Oilseed rape, wheat and corn prices



Source: the Ministry of Agriculture and Rural Development.

Increase in farmers' incomes in the fourth quarter of 2016 was exceptional, as in the past they would grow only in the periods of intensive agricultural activity. This was attributable to higher prices on agricultural produce markets and higher output, both observed in the preceding several months. Higher income improved the financial condition of farms, with their debts falling and the capacity to save improving. These changes were strong enough to reverse the downward trend prevailing for over two years.

Compared with 2015, prices of rapeseed and corn continued to grow, while prices of grains fell, as presented in the table below:

	Average 2015 PLN/t	Average 2016 PLN/t	yoy %	12-2016 PLN/t	MIN 2016 PLN/t	MAX 2016 PLN/t
Consumable wheat	699	645	(8)↓	660	610	677
Corn	617	654	6	610	567	716
Rapeseed	1,559	1,700	9	1,828	1,613	1,828

Source: the Ministry of Agriculture and Rural Development.

The crop balance in Europe and around the world will not support increases in prices of agricultural produce. Competition between crop exporters is strong, particularly in the Black Sea region, and will further intensify following harvests in the Northern hemisphere. Exports from the European Union have slowed down compared with the previous season, a trend attributable to lower crop production, particularly in France.

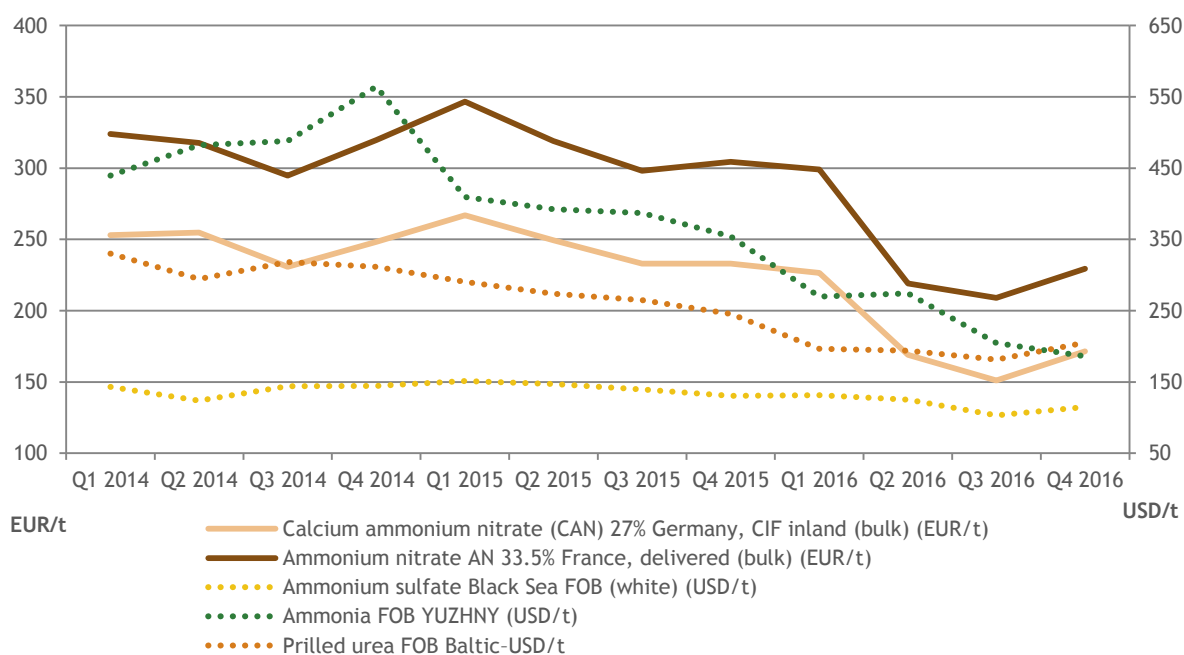
Given the dwindling global supply of rapeseed in the 2016/2017 season, production of oilseeds, mainly soy, cotton, sunflower, groundnuts, oil palm seeds and copra, is expected to grow. Among the less significant crops, sesame output will increase, whereas linen and castor-oil plant production will decline. In terms of supply and demand, the 2016/2017 season should be marked by the strengthening of average prices, especially of plant oils, with palm oil as the main growth driver, and sunflower oil prices exhibiting the least volatility.

### Nitrogen fertilizers

In the first half of 2016, demand in the nitrogen fertilizer market remained strong. Solid demand was particularly salient in the first quarter, i.e. during the spring application season, while the second

half of the year saw a slowdown attributable to lower seasonal demand and continuing low prices of agricultural produce. The higher demand for nitrogen fertilizers in spring had no effect on their prices. The lowest prices of the fertilizers were observed in the third quarter of 2015, during harvest and when cheaper, competing imported nitrogen fertilizers entered the Polish market. From mid-October until the end of 2016, nitrogen fertilizer prices were rising. This coincided with improvement in the financial condition of farmers on the back of advance disbursements of direct subsidies in October 2016.

### Prices of nitrogen fertilizers (urea, CAN, AN, AS,) and ammonia



Source: ICIS, Argus FMB, Profercy

In 2016, FOB Yuzhny prices of ammonia, the key feedstock used to manufacture fertilizers, continued on a downward trajectory prevailing since November 2014. Year on year, prices declined by approximately 39%, mainly on account of higher gas prices, disruptions in supply (e.g. in Ukraine) and movements of the USD/EUR exchange rate. Short-term forecasts for 2017 suggest that ammonia prices will rise.

Urea remains the key product in the fertilizer segment, and has a direct and indirect effect on other nitrogen fertilizer markets. The oversupply of urea, as well as macroeconomic factors (low agricultural produce prices, high crop stocks, turmoil on financial markets) caused prices of the fertilizer to fall by 29% year on year (FOB Baltic).

In 2016, average prices of all nitrogen fertilizers on international markets declined year on year.

	Average 2015 EUR/t	Average 2016 EUR/t	yoy %	12-2016 EUR/t	MIN 2016 EUR/t	MAX 2016 EUR/t
CAN 27% Germany CIF inland (bulk)	245	179	(27)↓	196	149	230
AN 33.5% France, delivered (bulk)	317	239	(25)↓	256	209	302
	USD/t	USD/t	%	USD/t	USD/t	USD/t
Ammonia (FOB Yuzhny)	386	233	(39)↓	215	168	279
Urea (FOB Baltic)	269	194	(28)↓	215	175	215
AS (Black Sea FOB white)	142	119	(17)↓	123	99	134

Source: ICIS, Argus FMB, Profercy

March and April are traditionally a period of increased demand for fertilizers. Similarly to previous years, the distribution of demand is consistent with the forecast continuing low prices of agricultural produce, and the situation in the global market of urea. It can be expected that farmers will postpone purchases of fertilizers for subsequent applications until the last moment; however, given the nature of agricultural production no major shifts in the distribution of demand for nitrogen fertilizers should be anticipated in 2017.

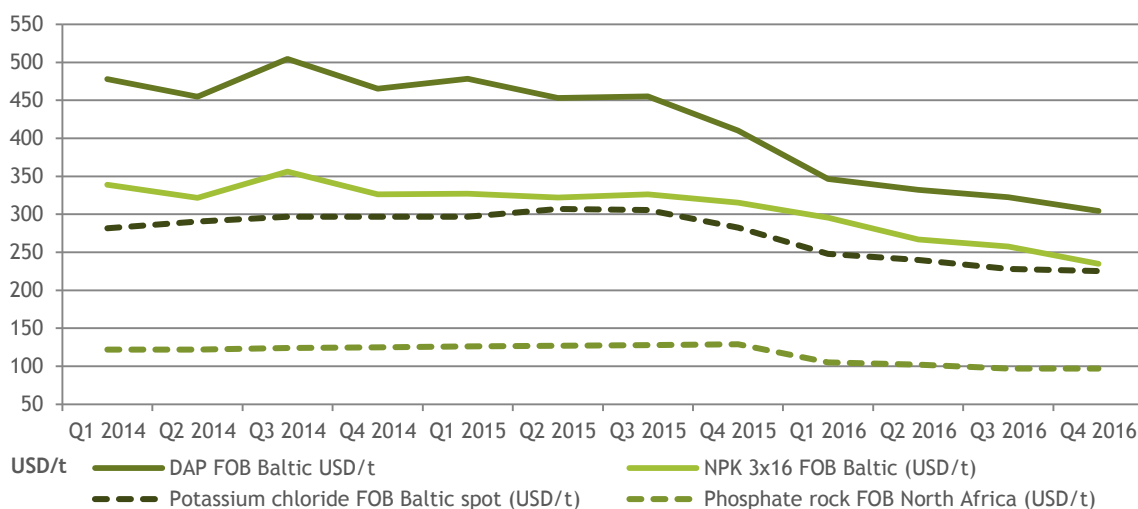
Throughout 2017, movements in prices of nitrogen fertilizers could be spurred by the considerable excess of urea production capacities on the global market and the Chinese manufacturers' decision to curb output prompted mainly by the production becoming unprofitable. In the early months of 2017, given a very low stock of urea, chiefly in India and China, demand for urea as well as its prices should markedly increase. Recently, prices of ammonia have also been on the rise, and to maintain positive margins manufacturers will seek price increases. Excessive global production capacities of ammonia and the launch of new fertilizer production units may put pressure on its prices, particularly in the second half of 2017. The fact that only 12% of produced ammonia is traded internationally, coupled with limited stockpiling capabilities, may trigger fluctuations in its prices over very short time periods, although gas prices will remain relatively stable compared with 2016.

### Market of compound fertilizers

The global compound fertilizer (NPK) market once again recorded lower sales year on year, with manufacturers and distribution networks keeping high inventory levels. Excluding short, seasonal periods of increased purchasing, demand remained low, save for the markets of India and several countries in South-East Asia. For most of the year, demand for NPK fertilizers was solid only in Russia, Ukraine and Poland. Prices of NPK fertilizers on global markets were on a downward trend in 2016 and declined by 18% (FOB Baltic).

Prices of NPK fertilizers in Poland were affected by low prices of imported NPK fertilizers and the policy of distribution companies (bundling).

### Prices of compound fertilizers (NPK, DAP), potassium chloride and phosphate rock



Source: WFM, FERTECON, Profercy

Demand for DAP, a two-component fertilizer, in the US, Europe, Brazil, China and India was weak. Many major manufacturers reduced output (e.g. China by 60%). Low internal demand in China prompted local producers to increase exports, contributing to low prices on global markets. Despite the reduced output, DAP prices could not be maintained and dropped 27% (FOB Baltic). The falling trend in compound fertilizer prices was a major contributing factor to the decline of prices of feedstock for their production.

The largest importers of salt, China and India, affected the level of feedstock prices by heavily stockpiling potassium chloride in 2015 and in the first half of 2016. In the second half of 2016, contracts were signed for deliveries of several million tonnes at fixed prices until April 2017. This prevented any further decline and later helped stabilise potassium chloride prices. However, they eventually bottomed in December, having declined by 20% (FOB Baltic) from the beginning of 2016, similarly to prices of phosphate rock.

In 2016, output of potassium chloride was also reduced. One Canadian company even permanently stopped production at a newly built mine worth PLN 2bn.

	Average 2015 USD/t	Average 2016 USD/t	yoy %	12-2016 USD/t	MIN 2016 USD/t	MAX 2016 USD/t
DAP (FOB Baltic)	449	326	(27)↓	302	302	366
NPK3x16 (FOB Baltic)	323	264	(18)↓	235	235	307
Potassium chloride (FOB Baltic spot)	298	235	(21)↓	223	223	265
Phosphate rock (FOB North Africa)	128	100	(21)↓	97	97	105

Source: WFM, FERTECON, Profercy

Prices of NPK fertilizers have been trending downwards for several years and no significant changes should be expected in 2017. Good crops and growing global crop stockpiles will not encourage any price increases; however, depending on the 2017 harvest, the situation may be reversed in the second half of the year.

In contrast to NPK fertilizers, in 2017 DAP prices will be shaped by demand factors. In Saudi Arabia and Morocco alone the first half of 2017 will see the launch of new production units with total capacities nearing 5m tonnes of DAP. These facilities will produce DAP exclusively for exports. Such a sharp increase in production capacities is likely to affect DAP fertilizer prices globally. On the other hand, planned shutdowns of DAP units in China should serve to stabilise the prices.

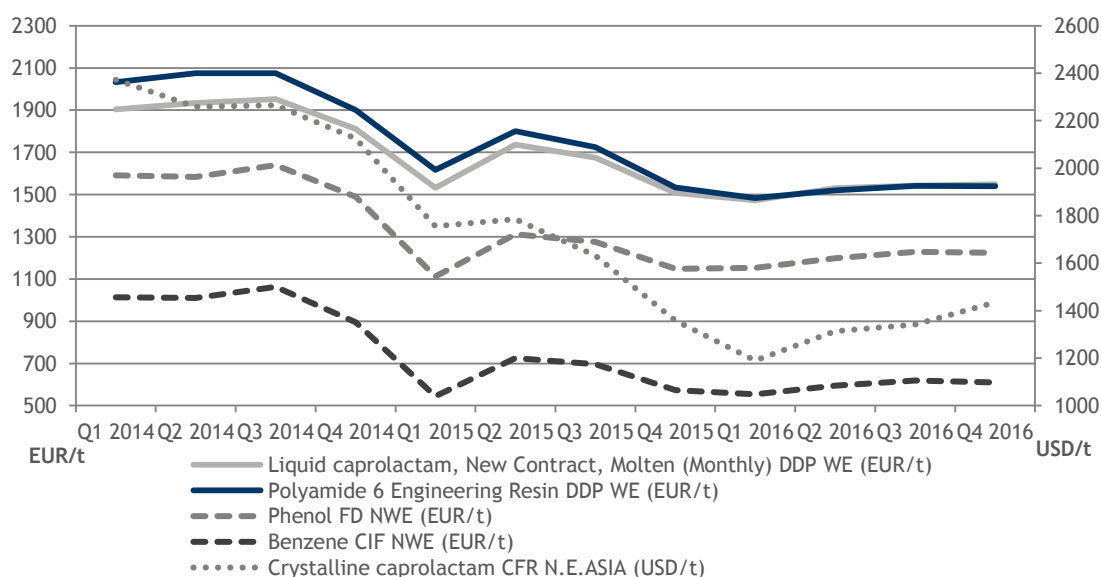
In 2016, prices of raw materials for the production of NPK fertilizers and DAP (phosphate rock, sulfur, potassium chloride), fell to their lowest levels since the 2007 crisis. In 2017, prices are expected to either stabilise or slightly increase.

## PLASTICS

### Prices of PA6, caprolactam, benzene and phenol

In the reporting period, the market situation continued to be shaped by the supply, demand and oil prices. Price declines were not as sharp as a year earlier, though. Oil prices fell ca. 17% year on year, clearly affecting the prices of benzene (down by over 6%) and caprolactam, which added to the pressure on polyamide (PA6) prices.

### Prices of PA6, caprolactam, benzene and phenol



Source: TECNON, ICIS.

During the year, the average prices of phenol decreased only slightly, by 1% (FD, NWE), an effect not only of the decline of crude prices but also of limited seasonal fluctuations of the supply and the stable demand.

During the year, the average price of caprolactam from Asia (CFR, NE Asia) was as much as 19% lower than in 2015, and prices of caprolactam from European manufacturers fell 5% in the period.

	Average 2015 EUR/t	Average 2016 EUR/t	yoy %	12-2016 EUR/t	MIN 2016 EUR/t	MAX 2016 EUR/t
Benzene (FOB, NWE)	635	594	(6)↓	631	523	652
Phenol (FD, NWE)	1,212	1,201	(1)↓	1,240	1,122	1,261
Caprolactam (Liq., DDP, WE)	1,613	1,524	(5)↓	1,570	1,453	1,570
Polyamide 6 (PA 6) (DDP, WE)	1,669	1,521	(9)↓	1,550	1,425	1,550
	USD/t	USD/t	%	USD/t	USD/t	USD/t
Caprolactam (CFR, NEAsia)	1,633	1,320	(19)↓	1,460	1,153	1,460
	USD/bbl	USD/bbl	%	USD/bbl	USD/bbl	USD/bbl
Crude oil (BRENT)	53.7	44.4	(17)↓	53.34	31.95	53.34

Source: ICIS, Tecnon, Rzeczpospolita

The relatively low caprolactam prices are expected to change as prices of oil and petrochemical commodities stabilize and the demand in the European market strengthens in the near term (the increase is currently estimated at 1.3%). The price increase may also be prompted by the manufacturers seeking to earn higher margins in the context of the growing demand and a possible impact of changes in commodity prices driven by economic growth and seasonal fluctuations.

The strong growth of production capacities in China in 2013–2016 adversely affected export opportunities for non-Asian manufacturers and strongly contributed to the oversupply of caprolactam. However, it was gradually reduced by the growing demand, a trend that is expected to continue in the coming years. Manufacturing assets on the European market need and are expected to be restructured, whereas the market itself must be optimized towards a considerable reduction of the production capacities. The process to rationalise the European caprolactam market will depend solely on consumption levels along the entire product chain in Europe. Long-term forecasts do not suggest any threat from the Asian market to European manufacturers but only indicate that the Chinese production capacities are sufficient to meet the country's demand for PA6. Thus, the Asian markets' impact on Europe will only lead to reorientation of caprolactam exports, while the polyamide market will not be affected to any significant degree.

The relatively strong demand for PA6 in Europe was driven mainly by the automotive and construction industries. The overall structure of demand for PA6 is expected to change, mainly because of the growing significance of engineering plastics, foil and flexible packaging. Therefore, within the next decade the automotive industry will be the main customer for polyamide-based engineering plastics. The polyamide producers' exposure to the transport sector is very high and may be expected to increase even more.

There were attempts to meaningfully reduce the polyamide oversupply in the European market in 2016, which noticeably improved the trade balance thanks to favourable conditions in these areas. Intense competition among integrated manufacturers of polyamide 6, further compounded by the oversupply, led to an even tighter market, with volatile benzene prices also affecting the situation. Changes in the pricing trends, reflecting seasonal fluctuations in demand, prompted producers to adjust prices. As in the case of caprolactam, the decisive factors which had an effect on the PA6 market were the drop and then stabilisation of prices of crude oil and petroleum products along the entire product chain, as well as the structure of supply and demand. In 2016, the average price of polyamide 6 (PA6, Engineering Resin Virgin, DDP, WE) was EUR 1,521 per tonne. Compared with 2015, it went down rather significantly, by 9%.

In the near future, the prices of products and raw materials used by this segment will be largely affected by commodity pressures, the balance of supply and demand in the plastics processing industry, and – to the greatest degree – the economic growth, expected by the IMF to reach 1.6% in the Eurozone. Stabilisation of crude oil prices at the levels seen in 2016 would create a favourable environment for the restoration of market equilibrium in the sector, thus supporting the anticipated increase in demand for plastics, not hampered by other factors.

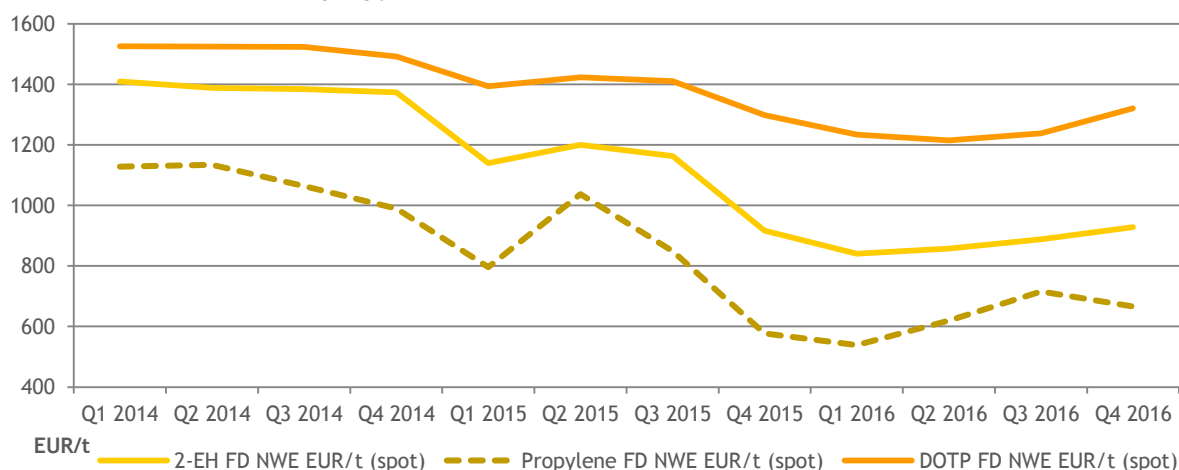
Other drivers of the increase will include stable economic growth globally and supportive economic policy in the EU.

## CHEMICALS

### OXO product chain

As in previous years, the market situation along the entire OXO chain was affected by prices of crude oil and naphtha. Demand for propylene remained broadly unchanged relative to 2015. Availability of propylene on the market significantly diminished from May 2016 due to industrial actions in the petrochemical sector in France, followed by planned maintenance shutdowns. After the summer season, the supply and demand situation improved, with propylene prices driven predominantly by the fall in crude oil prices. As a result, year-on-year spot prices of propylene fell by approximately 22%.

### Prices of 2-EH, DOTP and propylene



Source: ICIS

	Average 2015 EUR/t	Average 2016 EUR/t	yoy %	12-2016 EUR/t	MIN 2016 EUR/t	MAX 2016 EUR/t
2-EH (FD NWE spot)	1,105	879	(20)↓	933	820	940
DOTP (FD NWE spot)	1,382	1,252	(9)↓	1,365	1,201	1,365
Propylene (FD NWE spot)	815	635	(22)↓	640	523	745

Source: ICIS

The downward trend in prices of oxo alcohols at the beginning of the period was an effect of lower prices of raw materials (crude oil, propylene). In the second half of 2016, prices of oxo alcohols remained correlated with changes in propylene prices, and moved further up on the back of supply shortages. Eventually, the price of the key 2-EH alcohol reflected a downward trend in propylene prices and fell more than 20% year on year. In 2016, the 2-EH market remained balanced. Alcohol production volumes in Europe were adjusted to the current demand and the export possibilities that opened up in the context of competitive prices of petrochemical feedstock.

In 2017, prices of oxo alcohols will continue to be correlated with movements in propylene prices and will depend on demand drivers.

Demand for plasticizers grew throughout 2016. The market saw strong competition from regional suppliers and importers, which had a bearing on prices in Europe. In the fourth quarter of the year, the supply of plasticizers was limited due to production stoppages at BASF and Evonik caused by force majeure events.

In the first half of the year, product prices were affected mainly by lower prices of crude oil and petroleum commodities as well as by imports of competitively priced plasticizers from South Korea and Turkey. The second half of the year saw higher feedstock prices and lower output, which led to sharp increases in plasticizer prices. In 2017, the demand for the DEHP plasticizer will continue to decline due to REACH restrictions. In Europe, DEHP will be used mainly in medical applications that are not covered by REACH. Meanwhile, the output and consumption of the DEHT plasticizer will grow in Europe, on the back of rising demand for non-phthalate plasticizers.

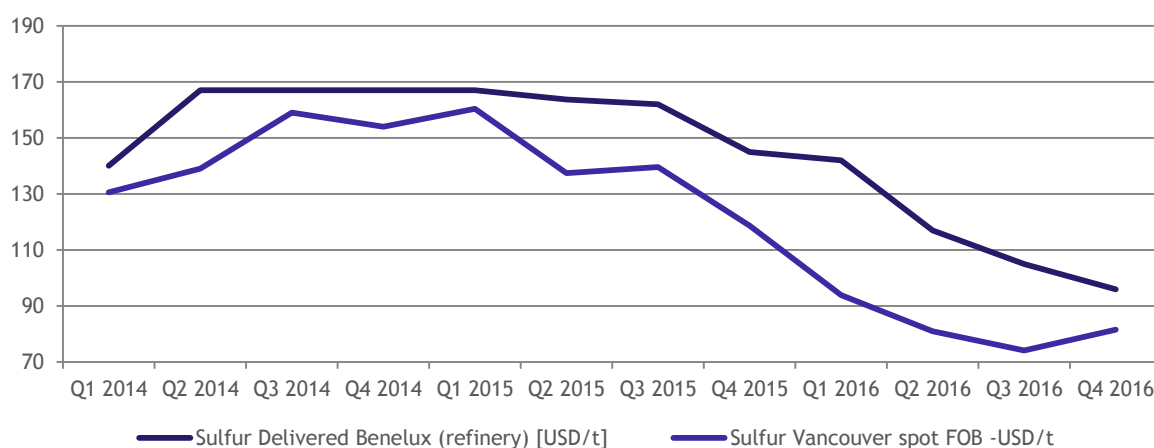
Limited availability of the DINP plasticizer on the European market in the first half of 2017 will drive the demand for DEHT.

Prices of plasticizers are forecast to grow in line with the expected increase in feedstock prices.

### Sulfur

In 2016, there was a substantial decrease in sulfur prices globally, from USD 115 per tonne in January to as low as USD 70 per tonne in August (Vancouver spot FOB), due to the weakness of the phosphate fertilizer market. In the second half of 2016, the prices rebounded to approximately USD 90 per tonne, both in the Middle East and the US.

### Sulfur prices



Source: FERTECON

	Average 2015 USD/t	Average 2016 USD/t	yoy %	12-2016 USD/t	MIN 2016 USD/t	MAX 2016 USD/t
Sulfur (Delivered Benelux refinery)	159	115	(28)↓	96	96	142
Sulfur (FOB Vancouver contract)	138	83	(40)↓	87	71	110

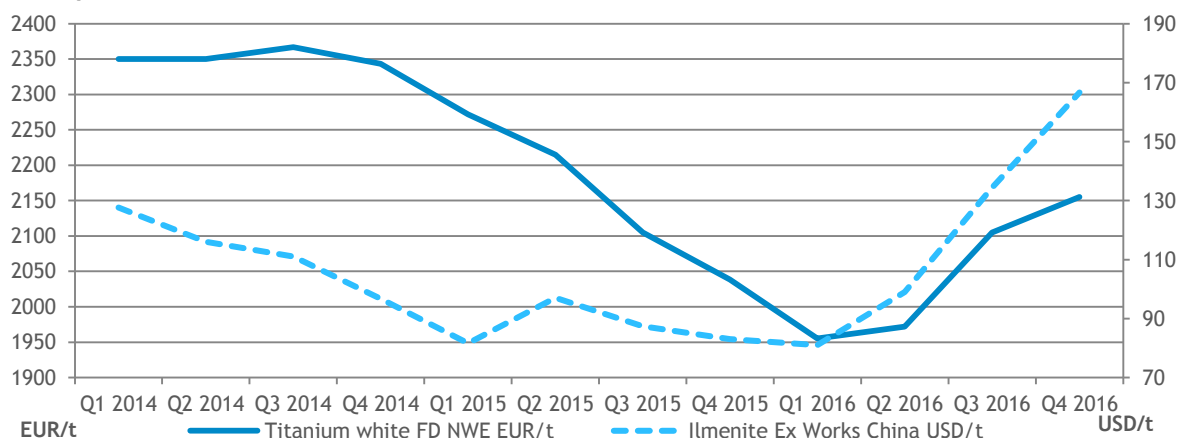
Source: FERTECON

Movements in sulfur prices in 2016 were caused by main importers of the product. There was a growing demand for this raw material in China and Morocco. The sulfur market is currently considered to be fairly balanced, as both the global supply and demand grew by approximately 5% year on year in 2016. Some changes in the supply and demand may occur upon completion of the delayed Barzan/Qatar project, originally scheduled to launch in October 2016. It is now expected to become operational in 2017. The United Arab Emirates' share in the market increased following the launch of the Shah gas project. At the same time, the supply of sulfur from Iran, Kazakhstan and Turkmenistan was reduced, indicating a shift in the market's trading model. Prices of sulfur may be expected to fluctuate slightly, but they will oscillate around ca. USD 87-92 per tonne, and the compound fertilizer market will continue to have a significant effect on them'.



## Pigment chain

### Market prices of titanium white and ilmenite



Source: ICIS, CCM

Titanium white, manufactured by Police only, is a product of particular significance for the Group. Its sales are highest in the spring-summer period (second and third quarters) on stronger demand for paints and varnishes in the construction industry.

	Average 2015 USD/t	Average 2016 USD/t	yoy %	12-2016 USD/t	MIN 2016 USD/t	MAX 2016 USD/t
Titanium white FD NWE	2,158	2,047	(5)↓	2,180	1,955	2,180
Ilmenite ex Works China	87	120	38	200	79	200

Source: ICIS, CCM

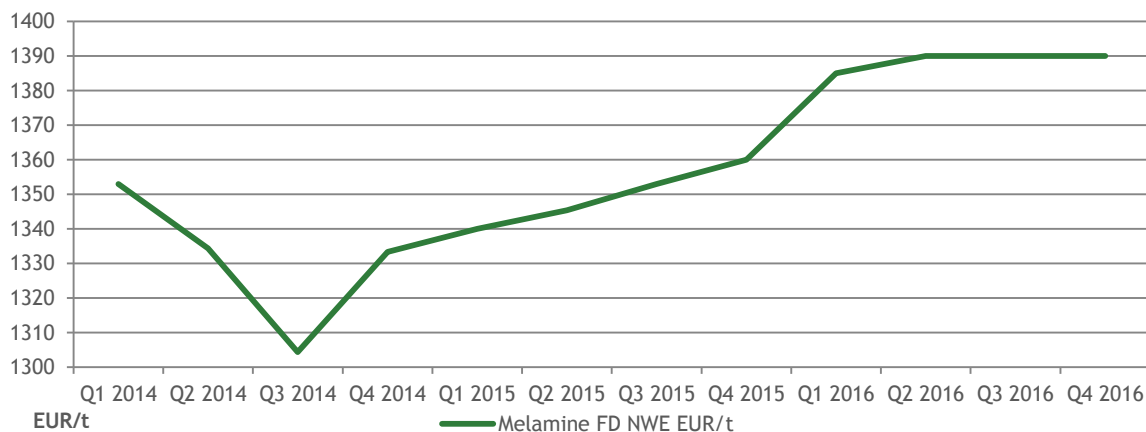
Sales of titanium white usually decline during the winter season - in the first and fourth quarters of each year. Titanium white remains a seasonal product, but given its widespread application, the demand depends chiefly on general market conditions. The successful price rise in 2016, which reversed the downward trend, is considered by the leading producers of titanium white as a turning point in the long trend of price decline (started in 2012). The growth is expected to continue in 2017. Unfortunately, the gains reported as early as in the first quarter of 2016 were not significant and, year on year, the prices declined by 5%. Due to production constraints, prices of feedstock for titanium white production (ilmenite and titanium slag) increased in 2016. In 2017, a slight upward trend may be maintained but the prices of both commodities are expected to gradually stabilize.

### Melamine

In 2016, the European market saw stable demand for melamine, with a temporary increase in demand in Eastern Europe, North and South Americas, Russia and India, driven by insufficient supplies from China and the US.

Due to solid demand, the average contract price of melamine in Europe increased by EUR 40/t (ca. 3%) compared with 2015.

## Prices of melamine



Source: ICIS, Global Bleaching Chemicals

The demand for melamine depends on the growth of the construction sector, including in particular its furniture and flooring segments. Globally, the demand is expected to grow until 2018 (by ca. 4.3%), though there will be regional variations.

	Average 2015 EUR/t	Average 2016 EUR/t	yoy %	12-2016 EUR/t	MIN 2016 EUR/t	MAX 2016 EUR/t
Melamine	1,349	1,389	3	1,390	1,375	1,390

Source: ICIS, Global Bleaching Chemicals

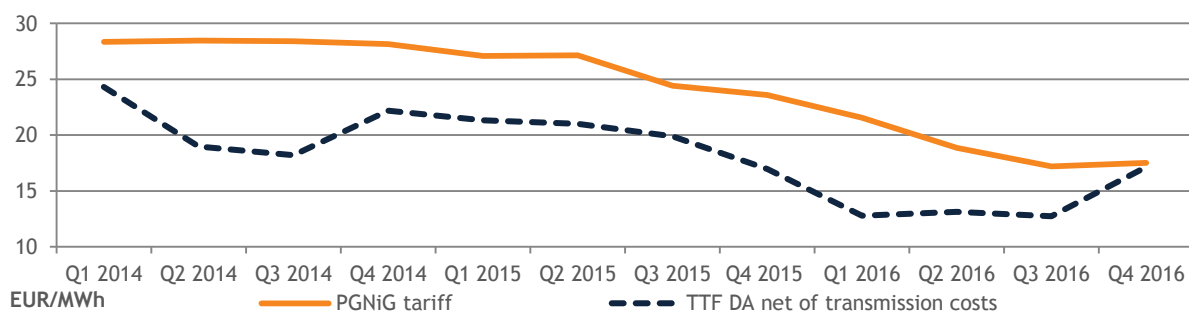
Strong demand, coupled with tightening supply in China, may undermine the stability of the global melamine market, which could contribute to a EUR 30-50/t increase in European prices in the first quarter of 2017.

## ENERGY

### Natural gas

2016 was the fourth consecutive year of declining gas prices on the European market. Over the period, the prices halved and retreated by as much as 30% relative to 2015. For most of the year, the gas market was oversupplied. An over two-fold increase in prices of coal, which began to be displaced from the energy mix by natural gas, the rise in oil prices as a result of the OPEC agreement to reduce output, and the cold start of the winter season led to a sharp rise in gas prices in the last quarter of 2016.

### Prices of natural gas



Source: PGNiG tariff, ICIS

	Average 2015 EUR/MWh	Average 2016 EUR/MWh	yoy %	12-2016 EUR/MWh	MIN 2016 EUR/MWh	MAX 2016 EUR/MWh
PGNiG tariff	25.6	18.7	(27)↓	17.5	17.0	21.3
TTF DA, net of transmission costs	19.8	14.0	(30)↓	17.7	11.9	18.0

Source: PGNiG tariff, ICIS

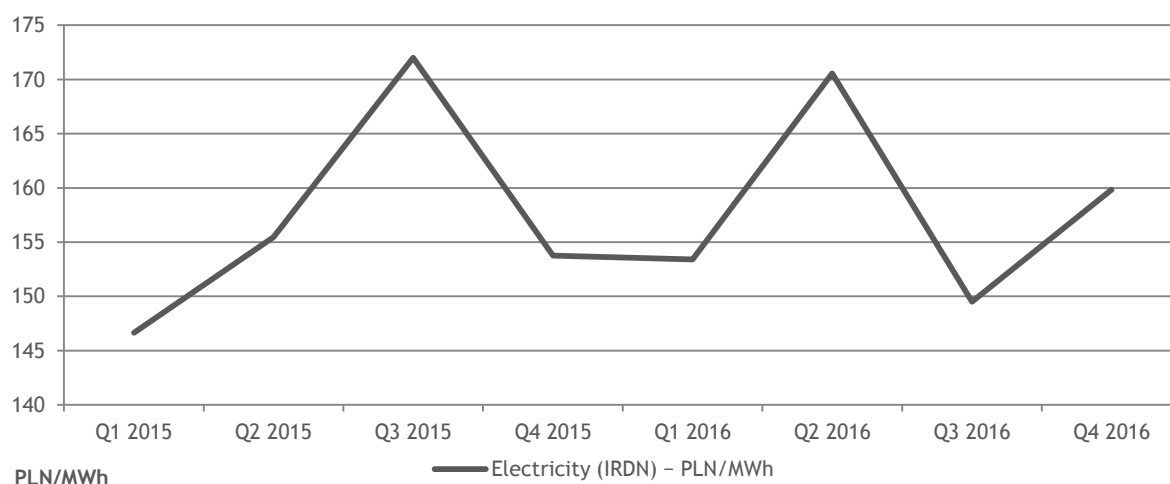
According to IHS Energy, the decline of coal prices after the winter season and the higher supply of LNG to the European market will bring gas prices to the level seen in the summer of 2016. Increased oversupply will put gas prices under pressure which will continue into the winter season. The average price of gas is expected to remain stable relative to the previous year.

On the domestic market, PGNiG changed its strategy, with a shift towards defending its market share. The Polish gas incumbent first introduced discount plans and then aligned gas prices to the market for the largest customers, which made its offering more competitive against independent imports. In addition, an amendment to the Energy Law, whereby all gas importers (including those consuming gas for own needs, such as the Group) are required to maintain mandatory stocks, will reduce the profitability of direct imports in favour of gas supplies from PGNiG, thus leading to price increases for end users.

## Electricity

In 2016, average monthly prices of electricity fell slightly relative to 2015 (by ca. 2.2%). Electricity prices were volatile over the year, and peaked in the second quarter. It was a result of disruptions in the operation and shutdowns of power generation units in Poland, unstable output of wind farms, and limited access to cheaper electricity from Scandinavia.

### Prices of electricity



Source: Polish Power Exchange

IRDN – average price weighted by the volume of all transactions on a trading day, calculated after the delivery date for the entire day.

	Average 2015 PLN/MWh	Average 2016 PLN/MWh	yoy %	12-2016 PLN/MWh	MIN 2016 PLN/MWh	MAX 2016 PLN/MWh
Electricity	157.0	161	2	156	83.4	413

Source: Polish Power Exchange

The prices of electricity in 2017 may be driven by a combination of offsetting factors:

- participation of energy companies in the restructuring of the Polish coal mining industry;
- rising prices of gas;

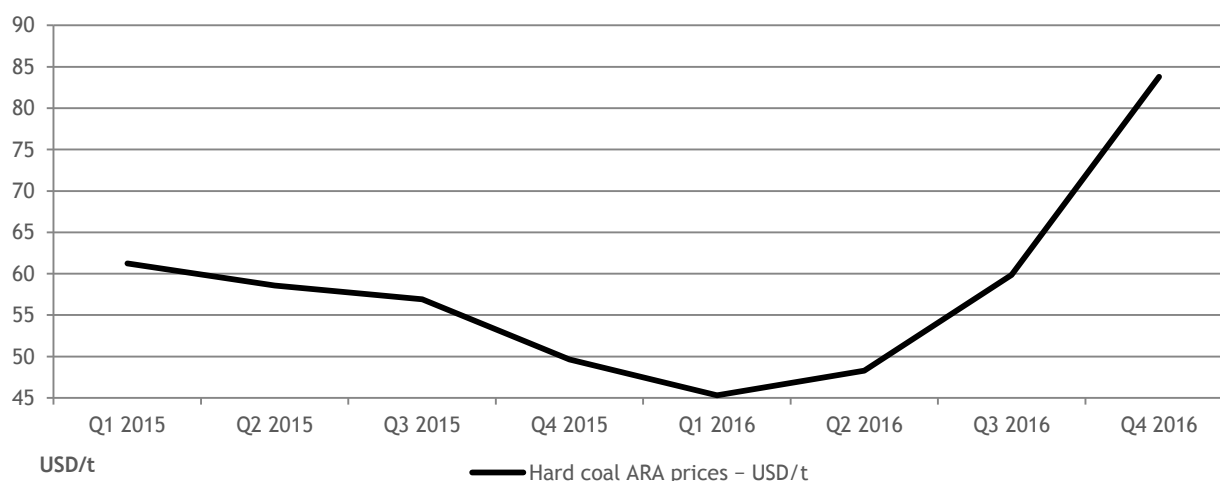
- high coal prices and regulatory regime, as the domestic market is largely affected by climate regulations and the need to continue upgrading generation capacities (expenditure on new production capacities) and to maintain the capacity reserve (effect on production costs);
- increasingly widespread use energy efficient solutions leading to reduced electricity consumption;
- end of the backloading reform (suspending some CO<sub>2</sub> emission allowances auctions) resulting in a higher volume of CO<sub>2</sub> emission allowances, which will be conducive to a decline in market prices of the allowances.

No considerable decline in electricity prices is expected in the near future.

## Coal

In line with analysts' predictions, in 2016 the average annual prices of coal rose by only 5% year on year. In the third quarter of 2016, following three years of decline, coal prices began to rise, and delivered an over 100% increase for the year. Prices grew on account of, among other factors, disruptions in the supply of Australian coal, increased demand from the Asia-Pacific countries, and oil price fluctuations (traditionally trailed by coal prices).

### Prices of hard coal



Source: ARA

The long-term oversupply of coal on the Polish market finally disappeared on the back of the ongoing restructuring of the mining industry. According to estimates, in the coming months of 2017 coal prices may remain in the upward trend.

	Average 2015 USD/t	Average 2016 USD/t	yoy %	12-2016 USD/t	MIN 2016 USD/t	MAX 2016 USD/t
Coal	57	59	5	87	43	92

Source: ARA

Analysts expect the prices to remain within the USD 60-70/t range in the second half of 2017.

## 5.3. Key financial and economic data

### 5.3.1. Consolidated financial information

In 2016, the Group earned a positive EBITDA of PLN 1,005,783 thousand and net profit of PLN 375,152 thousand.

Year on year, EBITDA decreased by PLN 303,432 thousand and the net profit decreased by PLN 303,067 thousand.

## Consolidated data

Item	2016	2015*	change	% change
Revenue	8,955,690	10,007,896	(1,052,206)	(10.5)
Cost of sales	(6,997,921)	(7,741,978)	744,057	(9.6)
<b>Gross profit</b>	<b>1,957,769</b>	<b>2,265,918</b>	<b>(308,149)</b>	<b>(13.6)</b>
Selling and distribution expenses	(669,315)	(630,248)	(39,067)	6.2
Administrative expenses	(729,629)	(736,546)	6,917	(0.9)
<b>Profit from sales</b>	<b>558,825</b>	<b>899,124</b>	<b>(340,299)</b>	<b>(37.8)</b>
Net other expenses	(72,763)	(74,719)	1,956	(2.6)
<b>Operating profit</b>	<b>486,062</b>	<b>824,405</b>	<b>(338,343)</b>	<b>(41.0)</b>
Net finance income/(costs)	(10,116)	(9,282)	(834)	9.0
Share of profit of equity-accounted investees	15,170	13,737	1,433	10.4
<b>Profit before tax</b>	<b>491,116</b>	<b>828,860</b>	<b>(337,744)</b>	<b>(40.7)</b>
Income tax	(115,964)	(150,641)	34,677	(23.0)
<b>Net profit</b>	<b>375,152</b>	<b>678,219</b>	<b>(303,067)</b>	<b>(44.7)</b>
<b>EBIT</b>	<b>486,062</b>	<b>824,405</b>	<b>(338,343)</b>	<b>(41.0)</b>
Depreciation and amortisation	519,721	484,810	34,911	7.2
<b>EBITDA</b>	<b>1,005,783</b>	<b>1,309,215</b>	<b>(303,432)</b>	<b>(23.2)</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

With revenue down 10.5% year on year and lower cost of sales (down by 9.6%), the Group reported gross profit. Gross profit decreased by PLN 308,149 thousand relative to 2015.

Gross profit net of distribution costs and administrative expenses was PLN 558,825 thousand, that is PLN 340,299 thousand less than in 2015.

In 2016, the balance of other income and other expenses was negative, at PLN (72,763) thousand, which had an adverse effect on EBIT, which amounted to PLN 486,062 thousand.

### 5.3.2. Segments' consolidated financial information

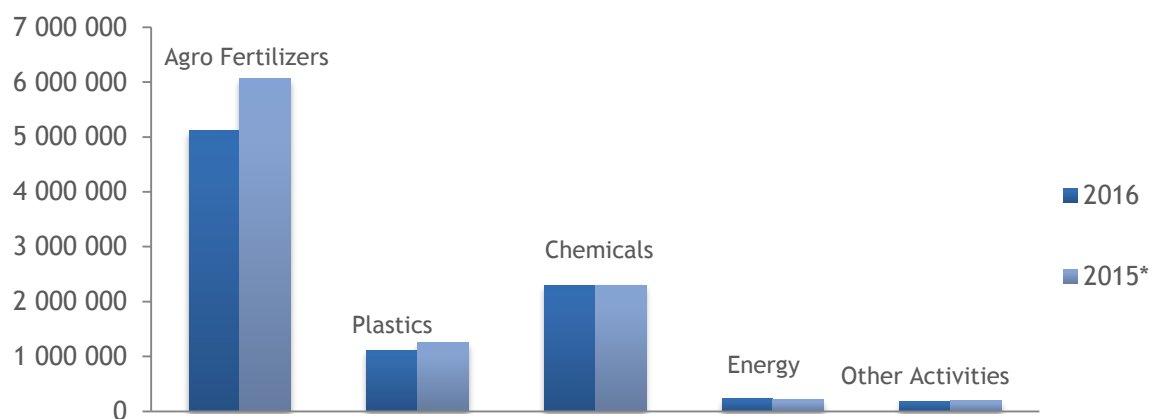
#### EBIT by segment

	Agro Fertilizers	Plastics	Chemicals	Energy	Other Activities
External revenue	5,115,652	1,117,842	2,295,327	239,748	187,121
Gross profit/(loss)	456,799	(81,239)	180,447	15,221	(12,403)
EBIT	426,618	(81,878)	170,687	14,577	(43,942)

Source: Company data

The Group's profit on sales of products in 2016 was determined primarily by the market situation in the Agro Fertilizers segment. Revenue in the Agro Fertilizers segment was down 15.6% year on year. Energy was the only segment where revenue increased, by 14.6%. Revenue of the other segments declined: by 10.4% in Plastics, by 0.3% in Chemicals, and by 1.8% in Other Activities.

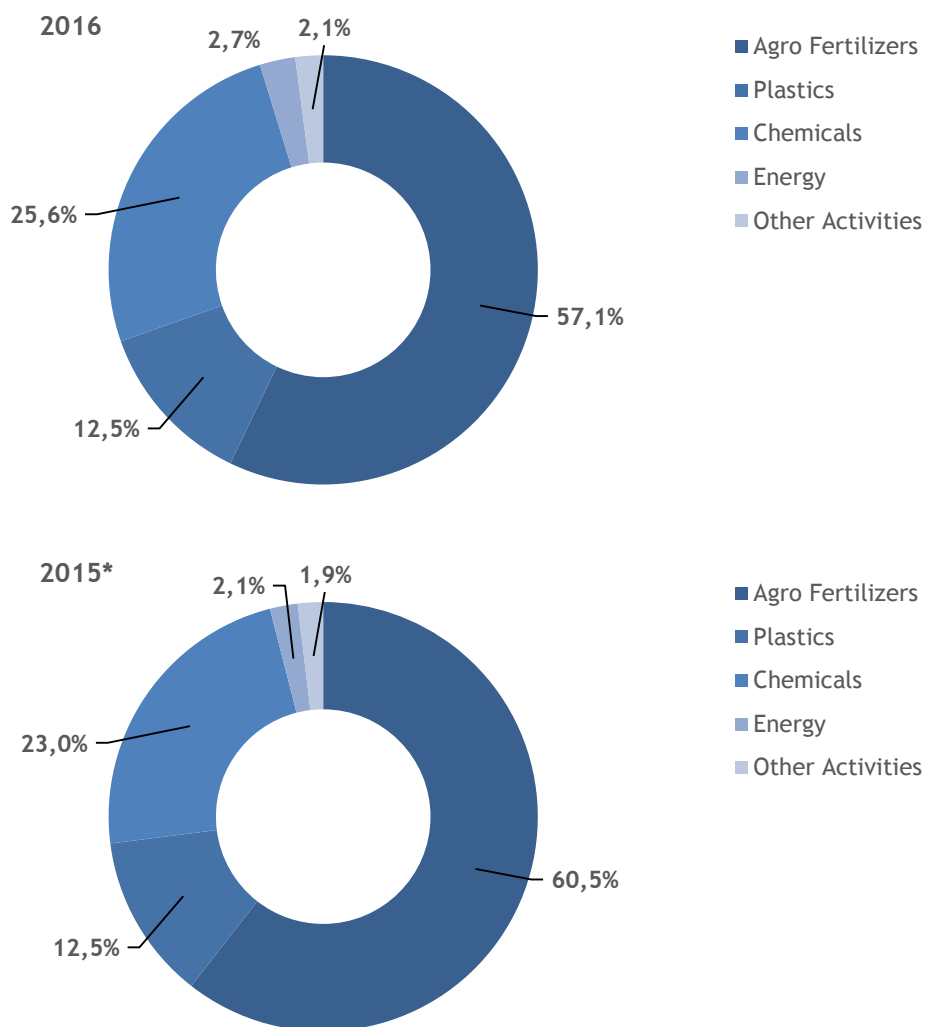
### Revenue by segment



Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

### Revenue by segment



Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

The shares of individual segments in total revenue changed slightly compared with 2015, with increased contributions from the Chemicals (2.6pp), Energy (0.6pp), and Other Activities (0.2pp) segments, and a lower share of the Agro Fertilizers (down 3.4pp) segment. The Plastics segment's share in total revenue remained unchanged.

### Agro Fertilizers

In 2016, revenue in the Agro Fertilizers segment was PLN 5,115,652 thousand and accounted for 57.1% of the Group's total revenue. The segment's revenue and its share in the Group's total revenue declined by 15.6% relative to 2015.

EBIT reported by the Agro Fertilizers segment was positive.

Domestic market accounted for approximately 70.7% of the segment's sales.

### Plastics

Revenue in the Plastics segment was PLN 1,117,842 thousand and accounted for 12.5% of the Group's total revenue. The revenue was down 10.4% year on year. The segment's EBIT decreased relative to 2015.

More than 89.0% of the segment's revenue was derived from sales on foreign markets.

### Chemicals

In 2016, revenue in the Chemicals segment was PLN 2,295,327 thousand, having fallen 0.3% year on year. The segment's revenue accounted for 25.6% of the Group's total revenue. The segment's EBIT improved significantly relative to 2015, and came in positive at PLN 170,687 thousand.

Sales on foreign markets accounted for approximately 45.2% of the Chemicals segment's revenue.

### Energy

In 2016, revenue in the Energy segment was PLN 239,748 thousand and accounted for approximately 2.7% of the Group's total revenue. The segment's revenue grew 14.6% year on year. EBIT reported by the Energy segment was positive.

### Other Activities

In 2016, revenue in the Other Activities segment was PLN 187,121 thousand, and accounted for 2.1% of the Group's total revenue, having decreased by 1.8% relative to 2015. The segment's EBIT was negative in 2016.

#### 5.3.3. Structure of consolidated operating expenses

In 2016, operating expenses were PLN 8,327,548 thousand, having decreased by PLN 618,167 thousand year on year. The decrease was attributable to lower cost of raw materials and consumables used, cost of services, as well as taxes and charges. There was an increase in depreciation and amortisation, cost of salaries and wages, including overheads and other benefits, and other costs.

#### Operating expenses by nature of expense

	2016	2015*	change	% change
Depreciation and amortisation	516,996	481,345	35,651	7.4
Raw materials and consumables used	4,980,007	5,598,647	(618,640)	(11.0)
Services	1,029,390	1,096,937	(67,547)	(6.2)
Salaries and wages, including overheads and other benefits	1,306,733	1,254,936	51,797	4.1
Taxes and charges	323,015	365,670	(42,655)	(11.7)
Other costs	171,407	148,180	23,227	15.7
<b>Total</b>	<b>8,327,548</b>	<b>8,945,715</b>	<b>(618,167)</b>	<b>(6.9)</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

### Other operating expenses

In 2016, other operating expenses, excluding raw materials and consumables used, accounted for 40.2% of total operating expenses, up from 37.4% in the corresponding period of 2015. The structure of other operating expenses changed only slightly relative to the comparative period.

#### Structure of other operating expenses (%)

	2016	2015*
Depreciation and amortisation	6.2	5.4
Services	12.4	12.3
Salaries and wages, including overheads and other benefits	15.7	14.0
Taxes and charges	3.9	4.1
Other costs	2.1	1.7
<b>Total</b>	<b>40.3</b>	<b>37.5</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

### 5.3.4. Structure of consolidated assets, equity and liabilities

In 2016, the Group's assets rose to PLN 11,051,920 thousand, by PLN 556,846 thousand relative to the end of 2015. As at December 31st 2016, non-current assets were PLN 7,651,480 thousand, and current assets were PLN 3,400,440 thousand.

Year on year, the most significant movements in assets in the preorting period included:

- a 12.8% increase in property, plant and equipment,
- an 18.6% increase in other financial assets,
- a 14.0% increase in investment property,
- a 14.8% decrease in cash and cash equivalents,
- a 10.5% decrease in inventories.

#### Structure of assets

	2016	2015*	change	% change
<b>Non-current assets, including:</b>	<b>7,651,480</b>	<b>6,942,663</b>	<b>708,817</b>	<b>10.2</b>
Property, plant and equipment	6,387,823	5,664,447	723,376	12.8
Intangible assets	530,577	522,442	8,135	1.6
Perpetual usufruct of land	485,396	492,061	(6,665)	(1.4)
Investments in subordinated entities	112,935	111,095	1,840	1.7
Investment property	59,504	52,204	7,300	14.0
Deferred tax assets	45,548	64,124	(18,576)	(29.0)
<b>Current assets, including:</b>	<b>3,400,440</b>	<b>3,552,411</b>	<b>(151,971)</b>	<b>(4.3)</b>
Trade and other receivables	1,073,396	1,096,286	(22,890)	(2.1)
Inventories	858,029	958,769	(100,740)	(10.5)
Cash and cash equivalents	641,711	753,144	(111,433)	(14.8)
Other financial assets	591,661	498,711	92,950	18.6
Property rights	214,675	226,931	(12,256)	(5.4)
<b>Total assets</b>	<b>11,051,920</b>	<b>10,495,074</b>	<b>556,846</b>	<b>5.3</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

Year on year, the most significant movements in equity and liabilities in the reporting period included:

- a 20.0% increase in non-current liabilities,



- a 31.0% increase in non-current liabilities under borrowings,
- a 56.2% decrease in current liabilities under borrowings.

#### Structure of equity and liabilities

	2016	2015*	change	% change
<b>Equity</b>	<b>7,129,265</b>	<b>6,911,448</b>	<b>217,817</b>	<b>3.2</b>
<b>Non-current liabilities, including:</b>	<b>2,072,368</b>	<b>1,727,659</b>	<b>344,709</b>	<b>20.0</b>
Borrowings	1,372,047	1,047,450	324,597	31.0
Employee benefit obligations	321,209	326,968	(5,759)	(1.8)
Deferred tax liabilities	196,805	188,381	8,424	4.5
Provisions	97,692	100,740	(3,048)	(3.0)
<b>Current liabilities, including:</b>	<b>1,850,287</b>	<b>1,855,967</b>	<b>(5,680)</b>	<b>(0.3)</b>
Trade and other payables	1,602,929	1,576,538	26,391	1.7
Other financial liabilities	67,485	56,672	10,813	19.1
Borrowings	52,034	118,880	(66,846)	(56.2)
Employee benefit obligations	39,917	33,167	6,750	20.4
Provisions	39,324	45,647	(6,323)	(13.9)
<b>Total equity and liabilities</b>	<b>11,051,920</b>	<b>10,495,074</b>	<b>556,846</b>	<b>5.3</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

#### 5.3.5. Consolidated financial ratios

##### Profitability ratios

	2016	2015*
Gross profit margin	21.9 %	22.6 %
EBIT margin	5.4 %	8.2 %
EBITDA margin	11.2 %	13.1 %
Net profit margin	4.2 %	6.8 %
ROA	3.4 %	6.5 %
ROCE	5.3 %	9.5 %
ROE	5.3 %	9.8 %
Return on non-current assets	4.9 %	9.8 %

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

##### Ratio formulas:

Gross profit margin = gross profit (loss) / revenue (statement of comprehensive income by function)

EBIT margin = EBIT / revenue

EBITDA margin = EBITDA / net revenue

Net profit margin = net profit (loss) / revenue

Return on assets (ROA) = net profit (loss) / total assets

Return on capital employed (ROCE) = EBIT / TALCL, that is EBIT / total assets less current liabilities

Return on equity (ROE) = net profit (loss) / equity

Return on non-current assets = net profit (loss) / non-current assets.

## Liquidity ratios

	2016	2015*
Current ratio	1.8	1.9
Quick ratio	1.4	1.4
Cash ratio	0.7	0.7

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

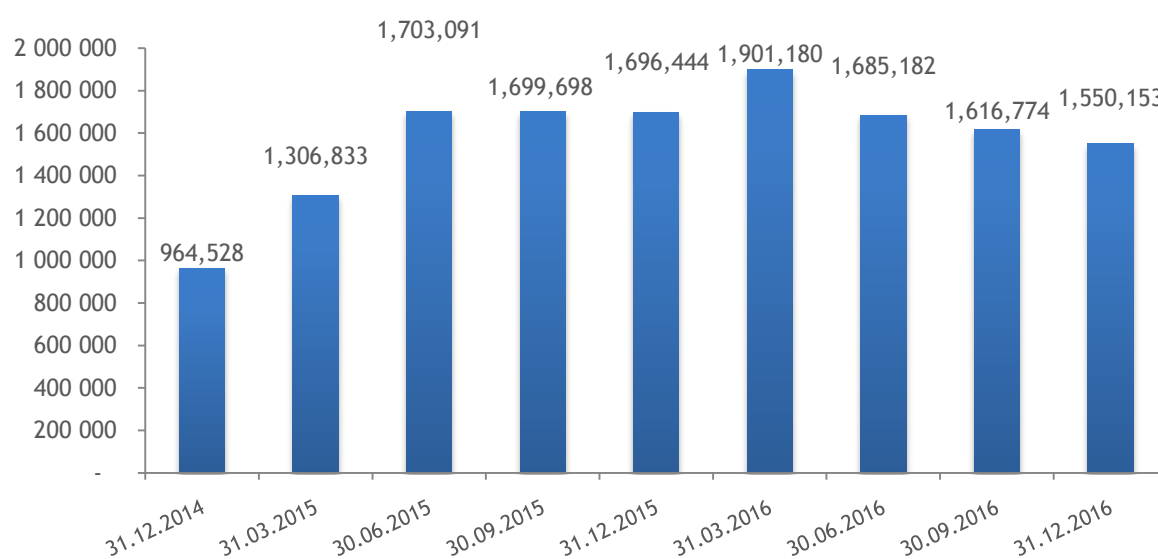
### Ratio formulas:

Current ratio = current assets / current liabilities

Quick ratio = (current assets - inventories - current prepayments and accrued income) / current liabilities

Cash ratio = (cash + other financial assets) / current liabilities.

## Changes in working capital\*



Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

## Operational efficiency ratios

	2016	2015*
Inventory turnover	44	45
Average collection period	43	39
Average payment period	83	73
Cash conversion cycle	5	11

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

### Ratio formulas:

Inventory turnover = inventories \* 360 / cost of sales

Average collection period = trade and other receivables \* 360 / revenue

Average payment period = trade and other payables \* 360 / cost of sales

Cash conversion cycle = inventory turnover + average collection period - average payment period.

## Debt ratios

Ratio	2016	2015*
Total debt ratio	35.5 %	34.1 %
Long-term debt ratio	18.8 %	16.5 %
Short-term debt ratio	16.7 %	17.7 %
Equity-to-debt ratio	181.7 %	192.9 %
Interest cover ratio	1,441.2 %	2,144.1 %

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the consolidated financial statements.

### Ratio formulas:

Total debt ratio = total liabilities / total assets

Long-term debt ratio = non-current liabilities / total assets

Short-term debt ratio = current liabilities / total assets

Equity-to-debt ratio = equity / current and non-current liabilities

Interest cover ratio = (profit before tax + interest expense) / interest expense.

## 5.3.6. Separate financial data

In 2016, Grupa Azoty S.A. earned a positive EBITDA of PLN 64,858 thousand and net profit of PLN 224,775 thousand.

Year on year, EBITDA was lower by PLN 30,638 thousand while the net profit increased by PLN 15,720 thousand.

### Separate financial data of Grupa Azoty S.A.

Item	2016	2015*	change	% change
Revenue	1,552,332	1,768,984	(216,652)	(12.2)
Cost of sales	(1,305,013)	(1,482,315)	177,302	(12.0)
<b>Gross profit</b>	<b>247,319</b>	<b>286,669</b>	<b>(39,350)</b>	<b>(13.7)</b>
Selling and distribution expenses	(92,494)	(94,088)	1,594	(1.7)
Administrative expenses	(162,346)	(160,144)	(2,202)	1.4
<b>(Loss)/Profit on sales</b>	<b>(7,521)</b>	<b>32,437</b>	<b>(39,958)</b>	<b>(123.2)</b>
Net other expenses	(21,658)	(28,082)	6,424	(22.9)
<b>Operating profit/(loss)</b>	<b>(29,179)</b>	<b>4,355</b>	<b>(33,534)</b>	<b>(770.0)</b>
Net finance income	249,086	204,581	44,505	21.8
<b>Profit before tax</b>	<b>219,907</b>	<b>208,936</b>	<b>10,971</b>	<b>5.3</b>
Income tax	4,868	119	4,749	3,990.8
<b>Net profit</b>	<b>224,775</b>	<b>209,055</b>	<b>15,720</b>	<b>7.5</b>
<b>EBIT</b>	<b>(29,179)</b>	<b>4,355</b>	<b>(33,534)</b>	<b>(770.0)</b>
Depreciation and amortisation	94,037	91,141	2,896	3.2
<b>EBITDA</b>	<b>64,858</b>	<b>95,496</b>	<b>(30,638)</b>	<b>(32.1)</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3 to the separate financial statements.

With revenue down 12.2% year on year and lower cost of sales (down by 12.0%), Grupa Azoty S.A. reported gross profit on sales. Gross profit decreased by PLN 39,350 relative to 2015. Despite the lower selling and distribution expenses, lower operating costs and only a slight increase in administrative expenses, the Group posted an operating loss. Finance income, which comprised mainly received dividends, ultimately contributed to the profit before tax.

### 5.3.7. Separate financial data by segment

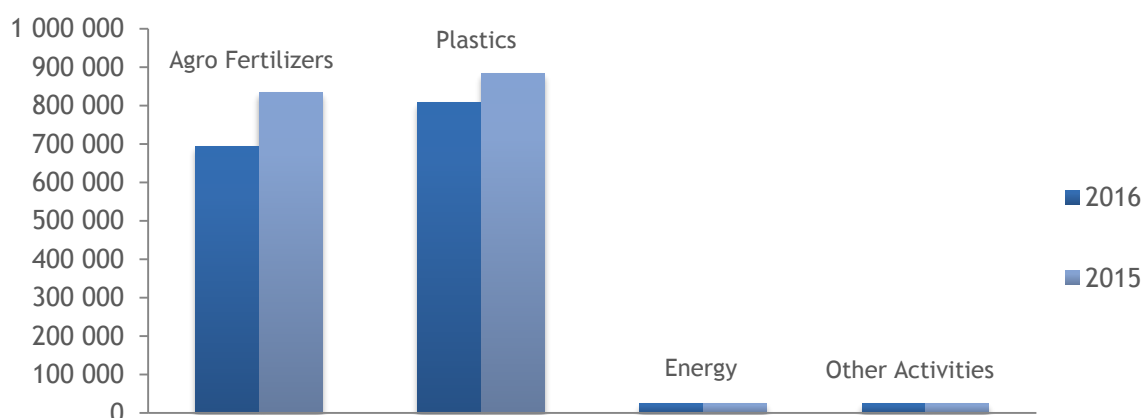
#### EBIT by segment

	Agro Fertilizers	Plastics	Energy	Other Activities
External revenue	694,659	808,824	24,784	24,065
Gross profit/(loss)	16,203	(26,741)	3,604	(587)
EBIT	12,845	(31,462)	819	(11,381)

Source: Company data

The Company's profit on sales of products in 2016 was driven primarily by the market situation in the Agro Fertilizers and Plastics segments. Compared with the previous year, revenue decreased across all segments: by 16.8% in Agro Fertilizers, by 8.4% in Plastics, by 3.4% in Energy, and by 4.8% in Other Activities.

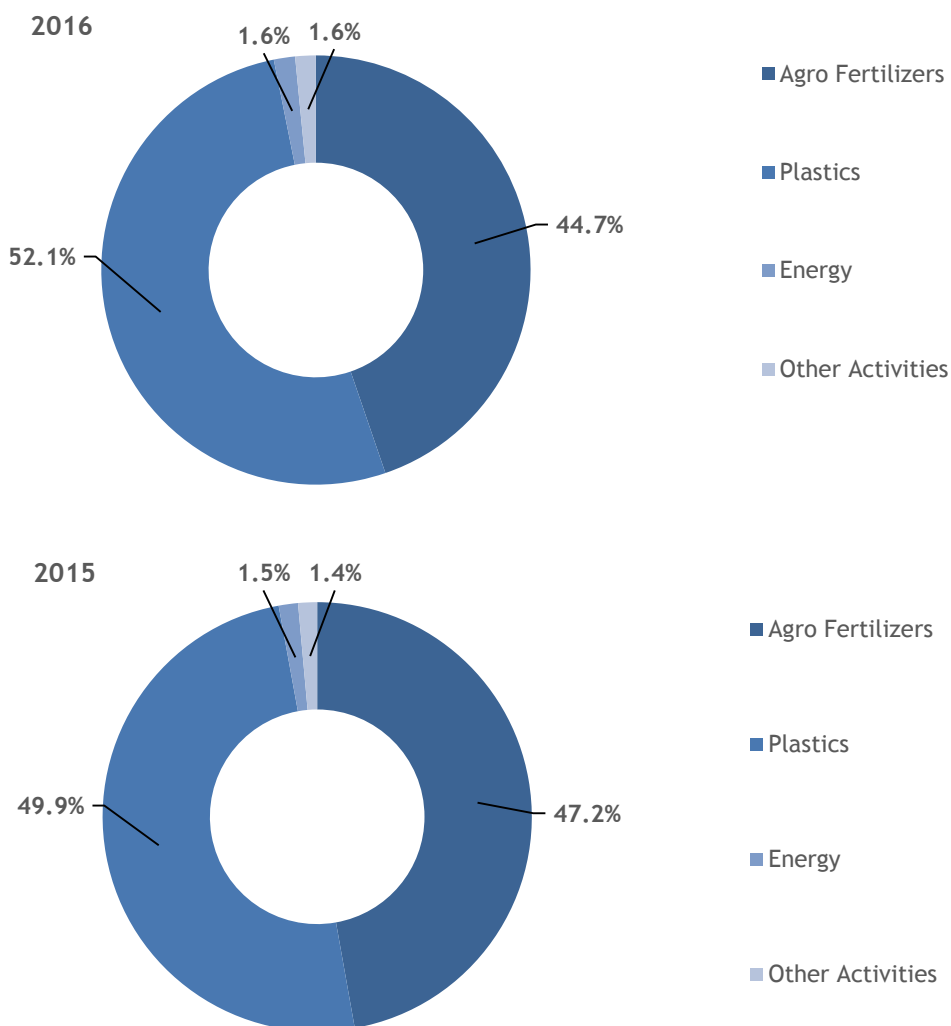
#### Revenue by segment



Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

## Revenue by segment



Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

There were slight year-on-year movements in the segments' shares in total revenue, with increased contributions from Plastics (2.2pp), Energy (0.1pp), and Other Activities (0.2pp), and a lower share of Agro Fertilizers (down 2.5pp).

### Agro Fertilizers

In 2016, revenue in the Agro Fertilizers segment was PLN 694,659 thousand and accounted for 44.7% of the parent's total revenue. Year on year, the segment's revenue and its share in the parent's revenue declined by 16.8% and 2.3pp, respectively.

EBIT earned by the segment was positive.

Sales on the domestic market accounted for approximately 70.3% of the segment's revenue.

### Plastics

In 2016, revenue in the Plastics segment was PLN 808,824 thousand and accounted for 52.1% of the parent's total revenue. Year on year, the segment's revenue decreased by 8.4%.

More than 76.7% of the segment's revenue was derived from sales on foreign markets.

The segment's loss before tax increased compared with 2015.

## Energy

In 2016, revenue in the Energy segment was PLN 24,784 thousand and accounted for approximately 1.6% of the parent's total revenue. Year on year, the segment's revenue decreased by 3.4%. EBIT reported by the Energy segment was positive.

## Other Activities

In 2016, revenue in the Other Activities segment was PLN 24,065 thousand, and accounted for 1.55% of the parent's total revenue, having decreased by 26.9% relative to 2015. The segment's EBIT was negative in 2016.

### 5.3.8. Structure of separate operating expenses

In 2016, the parent's operating expenses were PLN 1,550,610 thousand, down by PLN 139,358 thousand year on year. The decrease was attributable to lower costs of raw materials and consumables used, taxes and charges, costs of services, and salaries and wages, including overheads and other benefits.

#### Operating expenses by nature of expense

	2016	2015*	change	% change
Depreciation and amortisation	92,530	89,109	3,421	3.8
Raw materials and consumables used	908,697	1,034,121	(125,424)	(12.1)
Services	297,230	302,567	(5,337)	(1.8)
Salaries and wages, including overheads and other benefits	185,322	187,737	(2,415)	(1.3)
Taxes and charges	41,729	53,441	(11,712)	(21.9)
Other costs	25,102	22,993	2,109	9.2
<b>Total</b>	<b>1,550,610</b>	<b>1,689,968</b>	<b>(139,358)</b>	<b>(8.2)</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

#### Other operating expenses

In 2016, other operating expenses, excluding raw materials and consumables used, accounted for 41.4% of total operating expenses, up from 38.8% in the corresponding period of 2015. The structure of other operating expenses changed only slightly relative to the comparative period.

#### Structure of other operating expenses (%)

	2016	2015*
Depreciation and amortisation	6.0	5.3
Services	19.2	17.9
Salaries and wages, including overheads and other benefits	12.0	11.1
Taxes and charges	2.7	3.2
Other costs	1.6	1.4
<b>Total</b>	<b>41.4</b>	<b>38.8</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

### 5.3.9. Structure of separate assets, equity and liabilities

In 2016, the parent's assets increased to PLN 6,443,256 thousand, i.e. by PLN 586,631 thousand relative to the end of 2015. As at December 31st 2016, non-current assets were PLN 5,632,399 thousand, and current assets were PLN 810,857 thousand.

Year on year, the most significant movements in assets in the reporting period included:

- a 29.7% increase in property, plant and equipment,
- a 12.0% increase in other financial assets,
- a 191.2% increase in cash and cash equivalents,
- a 9.3% decrease in inventories.
- a 10.3% decrease in trade receivables.

#### Structure of assets

	2016	2015*	change	% change
<b>Non-current assets, including:</b>	<b>5,632,399</b>	<b>5,240,330</b>	<b>392,069</b>	<b>7.5</b>
Property, plant and equipment	1,435,521	1,106,972	328,549	29.7
Investments in subordinated entities	3,871,587	3,832,536	39,051	1.0
Other financial assets	244,220	218,115	26,105	12.0
Intangible assets	50,864	50,442	422	0.8
<b>Current assets, including:</b>	<b>810,857</b>	<b>616,295</b>	<b>194,562</b>	<b>31.6</b>
Cash and cash equivalents	326,031	111,942	214,089	191.2
Trade and other receivables	226,678	252,726	(26,048)	(10.3)
Inventories	171,256	188,843	(17,587)	(9.3)
Other financial assets	53,944	29,186	24,758	84.8
<b>Total assets</b>	<b>6,443,256</b>	<b>5,856,625</b>	<b>586,631</b>	<b>10.0</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

Year on year, the most significant movements in equity and liabilities in the reporting period included:

- a 3.1% increase in the parent's equity,
- a 22.9% increase in non-current liabilities,
- a 24.7% increase in non-current liabilities under borrowings,
- a 16.8% decrease in trade and other payables,
- a 527.8% increase in current liabilities under borrowings.

### Structure of equity and liabilities

Item	2016	2015*	change	% change
<b>Equity</b>	<b>4,517,137</b>	<b>4,382,771</b>	<b>134,366</b>	<b>3.1</b>
<b>Non-current liabilities, including:</b>	<b>1,282,420</b>	<b>1,043,852</b>	<b>238,568</b>	<b>22.9</b>
Borrowings	1,166,290	935,550	230,740	24.7
Employee benefit obligations	46,136	50,679	(4,543)	(9.0)
Provisions	25,992	24,446	1,546	6.3
Deferred tax liabilities	23,241	29,770	(6,529)	(21.9)
<b>Current liabilities, including:</b>	<b>643,699</b>	<b>430,002</b>	<b>213,697</b>	<b>49.7</b>
Borrowings	307,375	48,962	258,413	527.8
Trade and other payables	269,889	324,464	(54,575)	(16.8)
Other financial liabilities	58,131	46,055	12,076	26.2
<b>Total equity and liabilities</b>	<b>6,443,256</b>	<b>5,856,625</b>	<b>586,631</b>	<b>10.0</b>

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

### 5.3.10. Separate financial ratios

#### Profitability ratios

	2016	2015*
Gross profit margin	15.9 %	16.2 %
EBIT margin	(1.9) %	0.2 %
EBITDA margin	4.2 %	5.4 %
Net profit margin	14.5 %	11.8 %
ROA	3.5 %	3.6 %
ROCE	(0.5) %	0.1 %
ROE	5.0 %	4.8 %
Return on non-current assets	4.0 %	4.0 %

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

#### Ratio formulas:

Gross profit margin = gross profit (loss) / revenue (statement of comprehensive income by function)

EBIT margin = EBIT / revenue

EBITDA margin = EBITDA / net revenue

Net profit margin = net profit (loss) / revenue

Return on assets (ROA) = net profit (loss) / total assets

Return on capital employed (ROCE) = EBIT / TALCL, that is EBIT / total assets less current liabilities

Return on equity (ROE) = net profit (loss) / equity

Return on non-current assets = net profit (loss) / non-current assets.

#### Liquidity ratios

	2016	2015*
Current ratio	1.3	1.4
Quick ratio	1.0	1.0
Cash ratio	0.6	0.8

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.



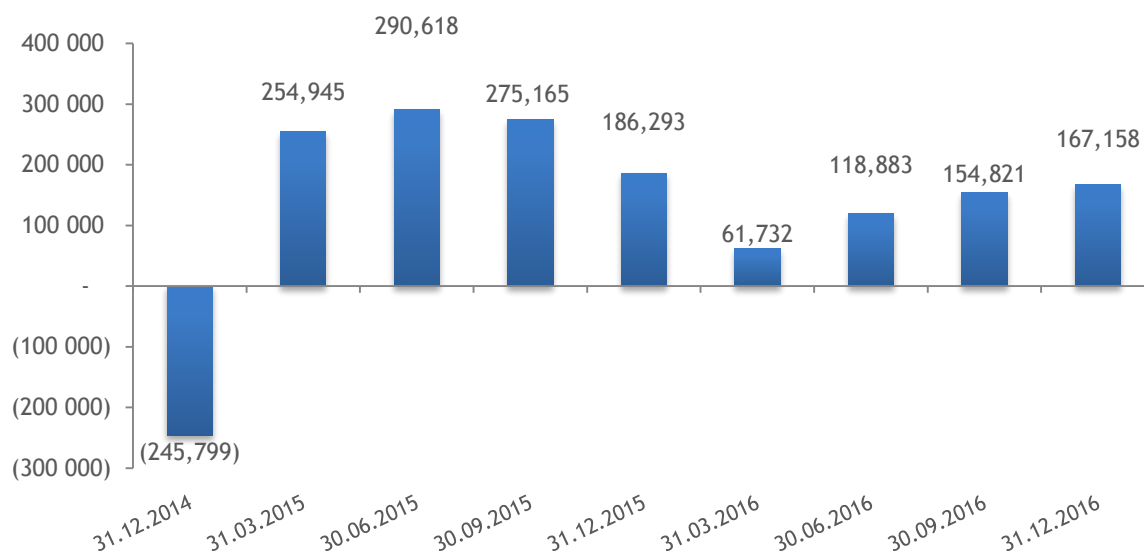
**Ratio formulas:**

*Current ratio = current assets / current liabilities*

*Quick ratio = (current assets-inventories-current prepayments and accrued income) / current liabilities*

*Cash ratio = (cash + other financial assets) / current liabilities.*

**Changes in working capital\***



Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

**Operational efficiency ratios**

	2016	2015*
Inventory turnover	47	46
Average collection period	53	51
Average payment period	74	79
Cash conversion cycle	25	18

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

**Ratio formulas:**

*Inventory turnover = inventories \* 360 / cost of sales*

*Average collection period = trade and other receivables \* 360 / revenue*

*Average payment period = trade and other payables \* 360 / cost of sales*

*Cash conversion cycle = inventory turnover + average collection period-average payment period.*

## Debt ratios

Ratio	2016	2015*
Total debt ratio	29.9 %	25.2 %
Long-term debt ratio	19.9 %	17.8 %
Short-term debt ratio	10.0 %	7.3 %
Equity-to-debt ratio	234.5 %	297.4 %
Interest cover ratio	904.4 %	792.1 %

Source: Company data

\*Financial data restated in accordance with the information presented in Note 2.3.3 to the separate financial statements.

### Ratio formulas:

*Total debt ratio = total liabilities / total assets*

*Long-term debt ratio = non-current liabilities / total assets*

*Short-term debt ratio = current liabilities / total assets*

*Equity-to-debt ratio = equity / current and non-current liabilities*

*Interest cover ratio = (profit before tax + interest expense) / interest expense.*

## 5.4. Management of capital and assets

The Group has access to umbrella overdraft limits under physical cash pooling arrangements and under a multi-purpose credit facility, which may be used by the parent at times of increased demand for funding by the Group companies. The Group also has access to bilateral overdraft limits and multi-purpose credit lines that are available to the Group companies.

The aggregate amount of available overdraft limits and multi-purpose credit facilities available to the Group as at December 31st 2016 was PLN 476,399 thousand.

As at December 31st 2016, the Group had access to available credit limits of PLN 1,030,477 thousand under a set of long-term corporate credit facilities and PLN 4,500 thousand under other borrowings.

In total, as at December 31st 2016 the Group had access to credit facilities totalling approximately PLN 1,511,376 thousand (including approximately PLN 1,104,321 thousand available to the parent).

Importantly, the Group maintains high amounts of free cash, including in bank deposits, which as at December 31st 2016 were PLN 1,220,777 thousand (PLN 326,031 thousand at the parent).

Total limits available under borrowings and the free cash represent financial resources which are sufficient to service current and future liabilities, and therefore the Group's liquidity risk is very low.

In 2016, the Group increased its borrowings from PLN 1,166,330 thousand to PLN 1,424,081 thousand, of which the parent's borrowings increased from PLN 984,512 thousand to PLN 1,473,665 thousand (including PLN 308,394 due to related parties).

The Group's short-term borrowings decreased from PLN 118,880 thousand to PLN 52,034 thousand.

In 2016, none of the Group companies defaulted on any of their liabilities or financial covenants where such default would trigger acceleration of the liabilities. In 2016, the Group was not refused any bank borrowings and none of its credit facility agreements was terminated.

In the opinion of their strategic lenders, the Group and its subsidiaries have a sound liquidity position and enjoy high credit standing. Considering the above, even if the macroeconomic situation deteriorates, the parent believes that there is no threat or risk which could materially adversely affect its liquidity position or lead to loss of liquidity.

Moreover, in 2016 the Group successfully continued its financing strategy, which included:

- using a package of corporate credit facility agreements, as a highly secure source of funding for the Group's long-term growth strategy and its day-to-day operations, ensuring uniform terms adequate to the Group's condition and potential;
- maintaining a strong liquidity position while optimising the management of free cash at the Group companies, for instance through the use of the cash-pooling arrangement, umbrella sublimits under current account overdraft facilities and multi-purpose facilities as part of the global limits available to the Group, and flexible adjustment of those sublimits to the needs of the Group companies;
- implementing an efficient mechanism for the redistribution of funds under the intra-group financing agreement with key subsidiaries, in the form of intra-group loans or note issues;
- the parent's dividend policy with respect to its subsidiaries, adapted to the financing requirements of the Group's and its subsidiaries' investment strategies;

- application of mechanisms under the Group Liquidity Management and Financing Policy consistent with the implemented centralised Financing Model.

## 5.5. Bank deposits

In 2016, the Group's short-term funds were primarily held in a current account with PKO Bank Polski S.A., linked under notional cash pooling with the Group companies' overdraft sublimits. The arrangement enables the Group to optimise its interest income and expenses. Early in the fourth quarter of 2016, the Group implemented, and has used since, a physical cash pooling service, which replaced the notional cash pooling service provided by PKO BP. Physical cash pooling allows the Group to manage the global liquidity limit and optimise its allocation across the Group.

The Group also held free cash in short-term deposits placed with reputable banking institutions offering highest interest rates, in particular rates above 1M WIBOR pa on amounts netted off as part of the cash-pooling arrangement.

As at December 31st 2016, the Group held a total of PLN 1,211,890 thousand in bank accounts and short-term deposits, of which PLN 258,066 thousand was held in the parent's consolidated current account with PKO BP linked to the physical cash pooling instrument. As at December 31st 2016, the funds were disclosed in the Group's financial statements under the following items:

- cash and cash equivalents - PLN 641,711 thousand (maturing in up to 3 months);
- other current financial assets - PLN 579,066 thousand (maturing in more than 3 months but less than 1 year).

The Group earned a total of PLN 17,131 thousand (including PLN 748 thousand attributable to the parent) in interest income on fixed-term deposits and from cash pooling services.

As at December 31st 2016, the parent held a total of PLN 326,031 thousand in bank accounts and short-term deposits, of which PLN 258,066 thousand from subsidiaries was held in the parent's consolidated current account with PKO BP linked to the physical cash pooling instrument. As at December 31st 2016, the funds were disclosed in the parent's financial statements, under 'cash and cash equivalents' of PLN 326,031 thousand (maturing in up to 3 months).

## 5.6. Credit facility and loan agreements executed or terminated during the reporting period

In 2016 and as at the date of this report, none of the Group companies defaulted on credit facilities or other borrowings or breached any material covenants under credit facility or other borrowing instruments.

Unless indicated otherwise, all credit facility and loan agreements are denominated in PLN. Interest on the PLN-denominated facilities accrues at variable rates based on WIBOR plus bank margin, and on the EUR-denominated facilities at variable rates based on EURIBOR plus bank margin.

In 2016 and as at the date of this report, the Group was a party to the following material financial agreements, arrangements and annexes (presented in the chronological order):

### **Annex to the credit facility agreement between Remzap Sp. z o.o. and Bank Millennium S.A.**

On January 25th 2016, Remzap Sp. z o.o. signed an annex to the PLN 2m credit facility agreement of January 27th 2012 concluded with Bank Millennium S.A. Under the annex, the agreement's term was extended until January 26th 2017.

### **Annex to the credit facility agreement between Agrochem Sp. z o.o. and Bank Pekao S.A.**

On January 29th 2016, Agrochem Sp. z o.o. and Bank Pekao S.A. signed an annex to the overdraft facility agreement, increasing the limit from PLN 5m to PLN 10m. The agreement was effective until January 31st 2017.

### **Factoring agreement between the parent and BGŻ BNP Paribas Faktoring Sp. z o.o.**

On February 12th 2016, the parent and BGŻ BNP Paribas Faktoring Sp. z o.o. executed a PLN 25m factoring agreement, effective until October 12th 2016, to finance deferred payment receivables due from selected domestic trading partners.

The agreement was automatically renewed for another year, until October 12th 2017.

**Amendment to the credit facility agreement between AFRIG S.A. and BGŻ BNP Paribas S.A.**

On February 25th 2016, AFRIG S.A. executed an amendment to a multi-purpose credit facility agreement signed with BGŻ BNP PARIBAS S.A. on February 18th 2014, extending the credit facility's availability until February 17th 2017 and bringing the collateral in line with the Group's standards. Subsequently, on December 20th 2016, AFRIG S.A. executed an amendment to a multi-purpose credit facility agreement signed with BGŻ BNP PARIBAS S.A. on February 18th 2014, extending the credit facility's term until February 17th 2019 and increasing the limit from EUR 13m to EUR 22m.

**Credit facility agreement between Agrochem Puławy Sp. z o.o. and Bank Pekao S.A.**

On April 21st 2016, Agrochem Puławy Sp. z o.o. and Bank Pekao S.A. signed a PLN 10m working capital facility agreement valid until December 31st 2016.

**Annex to the framework bank guarantee agreement between Grupa Azoty Prorem Sp. z o.o. and PKO Bank Polski S.A.**

On May 10th 2016, Grupa Azoty Prorem Sp. z o.o. and PKO BP signed Annex 1 to the framework bank guarantee agreement of May 15th 2015. Under the Annex, the term of the agreement was extended by another 12 months, until May 13th 2017. The available guarantee limit is PLN 2m.

**Grupa Azoty PUŁAWY's overdraft facility agreement with BZ WBK S.A.**

On May 31st 2016, the PLN 50m overdraft facility agreement with Bank Zachodni WBK S.A. expired. Having in view Grupa Azoty PUŁAWY's favourable current and expected liquidity position, and to avoid paying commission on the unused limit of the facility, the agreement was not extended.

**Loan from Provincial Fund for Environmental Protection and Water Management for Zakłady Azotowe Chorzów S.A.**

In June 2016, Zakłady Azotowe Chorzów S.A. reduced the amount of security for a loan provided by the Provincial Fund for Environmental Protection and Water Management (WFOŚiGW), by PLN 805.7 thousand, and on January 2nd 2017 Zakłady Azotowe Chorzów S.A. requested partial cancellation of the loan.

**Annexes to receivables discounting agreements with mBank S.A.**

***Annex to receivables discounting agreement with mBank S.A.***

On May 25th 2016, the parent and mBank S.A. signed an annex to the EUR-denominated receivables discounting agreement of July 30th 2010, extending its term until June 30th 2017.

***Annex to agreement for electronic purchase of receivables with mBank S.A.***

On May 25th 2016, the parent and mBank signed an annex to the agreement for electronic purchase of EUR-denominated receivables (from non-Group companies) of September 24th 2014, extending its term until June 30th 2017.

**Annex to overdraft facility agreement with PKO Bank Polski S.A.**

On September 20th 2016, the parent (acting on its own behalf and as a representative of the other Group companies) signed an annex to the overdraft facility agreement, raising the facility amount from PLN 302m to PLN 310m and extending the term of the agreement from September 30th 2016 to September 30th 2019 (for details, see Current Report No. 52/2016 of September 20th 2016).

**Annex to multi-purpose credit facility agreement with PKO Bank Polski S.A.**

On September 20th 2016, the parent, Grupa Azoty PUŁAWY, Grupa Azoty POLICE, Grupa Azoty KĘDZIERZYN and Grupa Azoty ATT Polymers GmbH signed an annex to a multi-purpose credit facility agreement with PKO BP, under which the facility amount was raised from PLN 237m to PLN 240m and:

- the term of the agreement was extended from September 30th 2016 to September 30th 2019;
- in addition to the PLN facility, a revolving credit facility denominated in EUR and USD was also made available;
- Grupa Azoty ATT Polymers GmbH, a subsidiary, acceded to the MPCF agreement as a new borrower and was provided with a non-revolving credit facility of up to EUR 7.5m, with the final repayment date falling on December 31st 2024, on condition that the MPCF agreement's provisions on security for the repayment of these liabilities remain binding until that date

(for details, see Current Report No. 52/2016 of September 20th 2016).

**Physical cash pooling agreement with PKO Bank Polski S.A.**

On September 20th 2016, the parent (acting on its own behalf and as a representative of the other Group companies) entered into a physical cash pooling agreement, which superseded the notional cash pooling agreement with PKO BP terminated with effect from September 30th 2016 (for details, see Current Report No. 52/2016 of September 20th 2016).

**Credit facility agreements between Agrochem Puławy Sp. z o.o. and Bank Pekao S.A.**

On October 28th 2016, AGROCHEM PUŁAWY Sp. z o.o. and Bank Pekao S.A signed a PLN 15m working capital facility agreement valid until July 31st 2017, and a PLN 18m working-capital overdraft facility agreement expiring on October 31st 2017.

**Grupa Azoty PUŁAWY's credit facility agreements with Bank Pekao S.A.**

On November 29th 2016, Grupa Azoty PUŁAWY and Bank Pekao S.A. signed Annex No. 8 to the PLN 2m intraday overdraft facility agreement. The annex extends the term of the facility until November 30th 2017.

**Grupa Azoty POLICE's overdraft facility agreement with BGK**

On November 12th 2016, the overdraft facility agreement concluded in November 2013 between Grupa Azoty POLICE and Bank Gospodarstwa Krajowego expired. The agreement set the facility amount at PLN 80m.

After the reporting period, on January 25th 2017, Grupa Azoty POLICE and Bank Gospodarstwa Krajowego signed a new PLN 80m overdraft facility agreement for the term of three years ending on January 24th 2020.

**Annex to Grupa Azoty PUŁAWY's intraday overdraft facility agreement with Bank Pekao S.A.**

On November 29th 2016, Grupa Azoty PUŁAWY signed Annex 8 to the PLN 2m intraday overdraft facility agreement with Bank Pekao S.A. The annex extended the term of the facility until November 30th 2017.

**Investment facility agreement between Grupa Azoty Prorem Sp. z o.o. and PKO Bank Polski S.A.**

On December 20th 2016, Grupa Azoty Prorem Sp. z o.o. submitted a notice of termination of the investment facility agreement with PKO BP; the three-month notice period expired in March 2017. As at December 31st 2016, the outstanding amount of the facility was PLN 1,266 thousand.

## 5.7. Loans granted, including loans to the Group's related parties

Unless indicated otherwise, all loan agreements are denominated in PLN. Interest on the PLN-denominated loans accrues at variable rates based on WIBOR plus margin, and on the EUR-denominated loans at variable rates based on EURIBOR plus margin.

### Intragroup loans

**Loan agreement between Grupa Azoty KĘDZIERZYN and ZAKSA S.A.**

On January 7th 2016, ZAKSA S.A. repaid a loan granted under the loan agreement of November 18th 2015. The repayment was effected by set-off of mutual claims under the loan agreement and the agreement for the provision of advertising services of October 9th 2015, for the services provided from January 1st to June 30th 2016.

On November 14th 2016, Grupa Azoty KĘDZIERZYN advanced to ZAKSA S.A. a PLN 500 thousand loan to finance day-to-day operations. The loan was repaid on January 16th 2017, by set-off of mutual claims under the loan agreement of November 14th 2016 and the agreement for provision of advertising services of October 9th 2015, on the due date of the invoice issued by ZAKSA S.A. for the provision of advertising services in the period from January 1st to June 30th 2017.

**Loans advanced by the parent to Grupa Azoty KĘDZIERZYN**

Under an intragroup financing agreement of April 23rd 2015, on January 25th 2016 Grupa Azoty KĘDZIERZYN's request for a loan of PLN 2,770,232.50 was accepted. The loan is to be used to finance launch of continuous production of OXOPLAST® OT. The loan was disbursed on January 29th 2016.

Under the intragroup financing agreement of April 23rd 2015, following Grupa Azoty KĘDZIERZYN's request for a loan of PLN 209,920 thousand for the financing of the investment project "New CHP plant at GA ZAK S.A. - Phase 1", further tranches of the loan were disbursed, including:

- on March 31st 2016 – PLN 40,320 thousand,
- on June 30th 2016 – PLN 32m,
- on December 30th 2016 – PLN 5,632 thousand.

**Annex to loan agreement between Grupa Azoty PUŁAWY and BBM Sp. z o.o.**

On June 15th 2016, Grupa Azoty PUŁAWY and BBM Sp. z o.o. signed:

- Annex 1 to the consolidation loan agreement of December 23rd 2015, whereby security for the loan was created in the form of a registered pledge, blank promissory note and assignment of rights under an insurance policy,
- An agreement on creation of a registered pledge over movable property and an agreement on assignment of rights under an insurance policy, concerning security for liabilities under the consolidation loan agreement.

On September 29th 2016, BBM Sp. z o.o. made an early repayment of five instalments of the loan advanced by Grupa Azoty PUŁAWY, in an amount of PLN 555 thousand.

**Loan agreement between Grupa Azoty POLICE and African Investment Group S.A.**

On September 23rd 2016, Grupa Azoty POLICE executed a loan agreement with its subsidiary African Investment Group S.A. of Dakar under which it granted the subsidiary a loan of EUR 4,800 thousand (PLN 20,611 thousand at the mid rate quoted by the National Bank of Poland for September 23rd 2016). The loan was advanced for a period from September 23rd 2016 to the final repayment date, falling not later than 24 months after the date of the agreement. The purpose of the loan was to enable AFRIG S.A. to pay its liabilities to suppliers of goods and services and to continue its research and development activities. On December 22nd 2016, AFRIG S.A. repaid the loan, including the interest.

**Loan agreement between Grupa Azoty PUŁAWY and Zakłady Azotowe Chorzów S.A.**

In the period July–December 2016, Zakłady Azotowe Chorzów S.A. failed to pay to Grupa Azoty PUŁAWY seven PLN 560 thousand monthly instalments under the loan agreement of April 2nd 2014, and seven PLN 72 thousand monthly instalments under the loan agreement of March 13th 2015. As at December 31st 2016, Zakłady Azotowe Chorzów S.A.'s debt under the loans was PLN 42,452 thousand (principal), including PLN 4,424 thousand of past due instalments. Zakłady Azotowe Chorzów S.A. paid the due interest due in accordance with the respective agreements.

On December 22nd 2016, the management board of Zakłady Azotowe Chorzów S.A. requested the management board of Grupa Azoty PUŁAWY that the debt under the loans be consolidated and the repayment schedule be changed.

**Annex to loan agreement between Grupa Azoty PUŁAWY and SCF Natural Sp. z o.o.**

On December 27th 2016, Annex 1 to the PLN 600 thousand loan agreement of May 7th 2014 was signed. Under the Annex, the repayment schedule was changed and the loan term was extended. The agreement expires on June 30th 2022.

**Loan agreement between Grupa Azoty POLICE and Supra Agrochemia Sp. z o.o.**

Grupa Azoty POLICE disbursed further tranches of the loan originally advanced to Supra Agrochemia Sp. z o.o. in 2014:

- on July 21st 2016 – the fifth tranche of PLN 387 thousand, and
- on November 18th 2016 – the sixth tranche of PLN 250 thousand.

As at December 31st 2016, the total amount of the loan was PLN 12,237 thousand.

The loan repayment date was extended until December 31st 2017.

## Loans advanced to third parties

### *Events after the reporting period*

On February 3rd 2017, Grupa Azoty POLICE signed a PLN 1,230 thousand loan agreement with Pogoń Szczecin S.A. The loan was disbursed on February 6th 2017. The loan was repaid on March 14th 2017.

## 5.8. Guarantees and sureties, including guarantees and sureties issued to and received from related parties

### Sureties for credit facilities

#### Surety for overdraft facility with PKO BP

Following execution of Annex 2 to a multi-purpose credit facility on September 20th 2016, on the same date the Grupa Azoty S.A.'s key subsidiaries, including Grupa Azoty PUŁAWY, Grupa Azoty POLICE and Grupa Azoty KĘDZIERZYN, entered into an agreement to grant sureties in favour of PKO Bank Polski S.A. securing the repayment of debt under the PLN 240m multi-purpose credit facility, which superseded the previous surety agreement of April 23rd 2015.

Each surety provider granted a surety covering the parent's liabilities under the MPCF agreement, with the proviso that the aggregate amount of those sureties would not exceed 120% of the facility amount, that is PLN 288m in aggregate, at any time during the facility term, irrespective of whether new entities accede to the surety agreement. The share of each surety provider in the aggregate surety amount specified above is one-third (1/3), therefore the amount of surety granted by each surety provider was set at no more than PLN 96m.

Following execution of Annex 13 to an overdraft facility on September 20th 2016, on the same date the Grupa Azoty S.A.'s key subsidiaries, including Grupa Azoty PUŁAWY, Grupa Azoty POLICE and Grupa Azoty KĘDZIERZYN, entered into an agreement to grant sureties in favour of PKO Bank Polski S.A. securing the repayment of debt under the PLN 310m overdraft facility, which superseded the previous surety agreement of April 23rd 2015.

Each surety provider granted a surety covering the parent's liabilities under the overdraft facility agreement, with the proviso that the aggregate amount of those sureties would not exceed 120% of the facility amount, that is PLN 372m in aggregate, at any time during the facility term, irrespective of whether new entities accede to the surety agreement. The share of each surety provider in the aggregate surety amount specified above is one-third (1/3), therefore the amount of surety granted by each surety provider was set at not more than PLN 124m (for details, see Current Report No. 52/2016 of September 20th 2016).

### Sureties issued during the financial year upon instructions of the Group companies

Type of and parties to the surety	Issue date	Security for	Surety amount (PLN '000)	Expiry date
Surety for credit facility from PKO BP (MPCF), granted by Grupa Azoty KĘDZIERZYN to the parent	Sep 20 2016	Multi-purpose credit facility agreement	96,000	Sep 20 2019
Surety for credit facility from PKO BP (MPCF), granted by Grupa Azoty POLICE to the parent	Sep 20 2016	Multi-purpose credit facility agreement	96 000	Sep 20 2019
Surety for credit facility from PKO BP (MPCF), granted by Grupa Azoty PUŁAWY to the parent	Sep 20 2016	Multi-purpose credit facility agreement	96,000	Sep 20 2019
Surety for credit facility from PKO BP (overdraft), granted by Grupa Azoty KĘDZIERZYN to the parent	Sep 20 2016	Overdraft facility agreement	124,000	Sep 20 2019
Surety for credit facility from PKO BP (overdraft), granted by Grupa Azoty POLICE to the parent	Sep 20 2016	Overdraft facility agreement	124,000	Sep 20 2019
Surety for credit facility from PKO BP (overdraft), granted by Grupa Azoty PUŁAWY to the parent	Sep 20 2016	Overdraft facility agreement	124,000	Sep 20 2019
Surety for credit facility from BNP Paribas, granted by Grupa Azoty POLICE to AFRIG S.A.	Sep 20 2016 (annex)	Multi-Purpose Credit Facility Agreement	97,328 (EUR 22m)	Dec 18 2024

Source: Company data

### Sureties granted after the reporting period

The parent's Supervisory Board approved the grant of surety to Grupa Azoty ATT Polymers GmbH of up to EUR 1,800 thousand, as security for a grant advanced by Investitionsbank des Landes

Brandenburg (ILB) to finance 20% of capital expenditure on construction of a logistics centre in Guben, Germany.

On February 14th 2017, the parent and Grupa Azoty ATT Polymers GmbH (the parent's subsidiary) signed a surety agreement under which the parent granted to the subsidiary a surety of up to EUR 1,800 thousand.

The surety was granted to secure a EUR 1.5m grant advanced to Grupa Azoty ATT Polymers GmbH by ILB to finance 20% of capital expenditure on construction of a logistics centre in Guben, Germany (the total amount of investment project is EUR 7.47m).

### Guarantees issued upon instruction of the Group

In 2016, the Group did not issue any guarantees whose total amount would exceed 10% of the parent's equity.

### Guarantees issued during the financial year by or upon instruction of the Group companies

Type and parties	Issue date	Security for	Guarantee amount (PLN '000)	Expiry date
Bank guarantee issued to GTC Force Sp. z o.o. upon instruction of Grupa Azoty Automatyka Sp. z o.o.	Jan 5 2016	Contract No. 001/GTC/2015 – Delivery and assembly of complete C&I systems as part of two projects: 'Construction of gas compression station at the Czarna Sędziszowska gas extraction facility' and 'Delivery and assembly of additional compressor at the Dzików Gas processing facility of the Lubaczów gas extraction facility'	43	Dec 9 2018
Bank guarantee issued to PGE S.A. upon instruction of Grupa Azoty POLICE	Mar 8 2016	Performance bond under open tender	316	Apr 30 2018
Bank guarantee issued by PKO Bank Polski S.A. upon instruction of Grupa Azoty KĘDZIERZYN in favour of PGE Górnictwo i Energetyka Konwencjonalna S.A.	Mar 17 2016	Performance bond under contract for supply of 40% solution of technical-grade urea to Elektrownia Opole	135	Apr 30 2018
Bank guarantee issued by PKO Bank Polski S.A. upon instruction of Grupa Azoty KĘDZIERZYN in favour of PGE Górnictwo i Energetyka Konwencjonalna S.A.	Mar 17 2016	Performance bond under contract for supply of 40% solution of technical-grade urea to Elektrownia Turów	373	Apr 30 2018
Standby letter of credit issued to MET upon instruction of Grupa Azoty POLICE	May 4 2016	Security for payment of contract price (flue gas treatment unit at EC-II CHP plant)	5,433 (USD 1.3m)	Dec 31 2016
Bank guarantee issued to Honeywell Sp. z o.o. upon instruction of Grupa Azoty Automatyka Sp. z o.o.	May 30 2016	Sub-contractor agreement of January 28th 2016 for supply of goods and provision of services for KGHM Smelter project	76	May 30 2018
Guarantee issued to Mostostal Zabrze Realizacje Przemysłowe S.A. upon instruction of Grupa Azoty Prorem Sp. z o.o.	Jul 11 2016	Performance bond, non-related party	396	Jul 10 2019
Bank guarantee issued to INŻYNIERIA RZESZÓW upon instruction of Grupa Azoty Automatyka Sp. z o.o.	Jul 14 2016	Sub-Contractor agreement No. 24/546/2016/P for delivery and assembly of complete electrical and C&I systems, with auxiliary services as part of the investment project 'Extension and reconstruction of components of the sedimentation section of the wastewater treatment plant in Tarnów'	301	May 31 2017
Bank guarantee issued to ELEKTROBUDOWA S.A. upon instruction of Grupa Azoty Automatyka Sp. z o.o.	Jul 21 2016	Sub-Contractor agreement No. 1132-3201/Z/011/2015/PZ for delivery and assembly of complete C&I system for the investment project 'Construction of new heat generating unit with circulating	93	Jul 20 2019



Directors' Report on the operations of Grupa Azoty S.A. and the Group  
for the 12 months ended December 31st 2016  
(all amounts in PLN '000 unless stated otherwise)

Type and parties	Issue date	Security for	Guarantee amount (PLN '000)	Expiry date
		fluidized bed boiler, ca. 50-60 MWe heating and condensing turbine at the Tychy Generation Plant of TAURON Ciepło S.A.'		
Guarantee issued to SABIC (Saudi Arabia) upon instruction of Prozap Sp. z o.o.	Jul 22 2016	Advance payment guarantee	252	Mar 31 2017
Guarantee issued to Grupa Azoty PUŁAWY upon instruction of Remzap Sp. z o.o.	Aug 13 2016	Performance bond	58	Jul 1 2018
Bank guarantee issued to Valmet Automation Sp. z o.o. upon instruction of Grupa Azoty Automatyka Sp. z o.o.	Aug 25 2016.	Contract No. 198/K/PR/511591/2015 for delivery and assembly of complete C&I system for the investment project 'Construction of the Municipal Waste Disposal Plant in Białystok'	65	Jan 30 2018
Bank guarantee issued to VALMET AUTOMATION Sp. z o.o. upon instruction of Grupa Azoty Automatyka Sp. z o.o.	Aug 25 2016.	Contract No. 228/K/PR/511504_ZAK/2016 for delivery, assembly and start-up of C&I system in Phase 1 of the investment project 'Construction of new CHP plant at Zakłady Azotowe KĘDZIERZYN S.A.'	476	Jan 13 2017
Guarantee issued to urea supplier upon instruction of Grupa Azoty PUŁAWY	Sep 9 2016	The guarantee was issued under the multi-purpose credit facility agreement concluded with PKO Bank Polski S.A.	USD 500 thousand	Aug 31 2017
Bank guarantee issued to Zeppelin Systems GmbH Friedrichshafen upon instruction of Grupa Azoty Automatyka Sp. z o.o.	Nov 3 2016.	Contract for design, delivery and assembly of control equipment for the pneumatic handling system of the Polyamide Unit at Grupa Azoty's Tarnów plant	160	Jan 6 2017
Bank guarantee issued to GAZ-SYSTEM S.A. upon instruction of Grupa Azoty POLICE	Dec 1 2016	Payment guarantee for gas transmission contract	4,301	Nov 30 2017
Bank guarantee issued to PSE S.A. upon instruction of Grupa Azoty POLICE	Dec 15 2016	Payment guarantee for electricity transmission contract	300	Apr 30 2017
Bank guarantee issued by PKO Bank Polski S.A. to ENEA Wytwarzanie Sp. z o.o. upon Grupa Azoty KĘDZIERZYN's instruction Świeże Górze	Dec 21 2016	Performance bond under Contract No. RZP-WnJ.2100.2.2016/1	212	Jan 31 2018

Source: Company data

## Guarantees amended upon instruction of the Group

In 2016, the Group did not sign any annexes to amend its guarantees whose amount would exceed 10% of the parent's equity.

## Guarantees amended during the financial year upon instruction of the Group companies

Type and parties	Issue date	Security for	Guarantee amount (PLN '000)	Expiry date
Annexes to the bank guarantee issued by PKO Bank Polski S.A. to the Customs Chamber upon Grupa Azoty KĘDZIERZYN's instruction	Mar 17 2016 - Annex 1 Apr 22 2016 - Annex 2 Apr 29 2016 - Annex 3	Customs debt payment guarantee	100	Dec 31 2016 (+ 60 days, i.e. until Mar 1 2017)
Annex to the guarantee issued to the Szczecin Customs Chamber upon Grupa Azoty POLICE's instruction	Mar 18 2016	Customs debt payment guarantee	4,000	Mar 23 2017
Annex to the bank guarantee issued by PKO Bank Polski S.A. to OGP GAZ-SYSTEM S.A. upon the parent's instruction	Nov 04 2016 - Annex 5	Security deposit for gas transmission contract	63	Nov 30 2017
Annex to the bank guarantee issued by PKO Bank Polski S.A. to OGP GAZ-SYSTEM S.A. upon the parent's instruction	Nov 4 2016 - Annex 6	Security deposit for gas transmission contract	1,151	Nov 30 2017
Annex to the bank guarantee issued by PKO Bank Polski S.A. to OGP GAZ-SYSTEM S.A. upon the parent's instruction	Nov 04 2016 - Annex 5	Security deposit for gas transmission contract	841	Nov 30 2017
Annex to the bank guarantee issued by PKO Bank Polski S.A. to OGP GAZ-SYSTEM S.A. upon Grupa Azoty KĘDZIERZYN's instruction	Nov 10 2016 - Annex 2	Security for Transmission Contract No. 2012/U/1126/ZUP of December 3rd 2012, as amended	3,105	Nov 30 2017
Annexes to the bank guarantee issued by PKO Bank Polski S.A. to OGP GAZ-SYSTEM S.A. upon Grupa Azoty KĘDZIERZYN's instruction	Nov 10 2016 - Annex 1 Apr 22 2016 - Annex 2 Apr 29 2016 - Annex 3	Security for Transmission Contract No. 2014/U/9040/ZUP of March 11th 2014, as amended	90	Nov 30 2017
Annex to the guarantee issued by PKO Bank Polski S.A. to the PSE S.A. upon Grupa Azoty POLICE's instruction	Nov 15 2016	Payment guarantee for electricity transmission contract	800	Dec 31 2017
Annex to the guarantee issued to the Kraków Customs Chamber upon the parent's instruction	Nov 30 2016	Customs debt payment guarantee	450	Mar 1 2018
Annex to the standby letter of credit issued to MET upon instruction of Grupa Azoty POLICE	Dec 28 2016	Security for payment of contract price (flue gas treatment unit at EC-II CHP plant)	5,433 (USD 1.3m)	Dec 31 2017

Source: Company data

## Letters of credit

### Letters of credit issued at the request of Grupa Azoty PUŁAWY

On February 4th 2016, at the request of Grupa Azoty PUŁAWY, PKO Bank Polski S.A. issued an import letter of credit for EUR 1,496 thousand, expiring on August 19th 2016, for the benefit of an equipment vendor. The letter of credit was issued under a multi-purpose credit facility agreement. On August 23rd 2016, the letter of credit was settled.

### **Letter of credit issued at the request of Grupa Azoty POLICE**

On May 4th 2016, at the request of Grupa Azoty POLICE, PKO Bank Polski S.A. issued a standby letter of credit for USD 1,300 thousand, expiring on December 31st 2016, as payment bond for the contract for construction of a flue gas treatment unit at the EC II CHP plant.

## **5.9. Material off-balance-sheet items**

The Group companies reported blank promissory notes and guarantees issued upon their instruction. Blank promissory notes issued by the Group companies and guarantees issued by banks or insurance companies upon the Group companies' instruction as security for liabilities recognised in the statement of financial position, or liabilities with respect to which the likelihood of cash outflows to settle the liability is negligible, are not presented as contingent liabilities.

## **5.10. Financial instruments - risk management policy and risk management instruments, objectives and methods**

As part of its financial risk management policy the Group identifies the following risks and has adopted the following risk management objectives and methods:

### **Currency risk management**

In 2016, the Group applied the Financial Risk Management Policy (currency and interest rate risks), which is one of the elements of the Group's centralised Financing Model. The policy has been operated by those Group companies which are exposed to material currency and interest rate risks.

- **Identification of currency risk**  
The Group is exposed to currency risk resulting from its net exposure to the euro and the US dollar under its sale and procurement transactions, trade receivables and payables, as well as receivables and liabilities from financing and investing activities. The Group is also exposed to the risk related to periodic episodes of strong exchange rate volatility, including the effect of EUR/USD exchange rate development on the EUR/PLN and USD/PLN exchange rates.
- **Purpose of currency risk management**  
The purpose of currency risk management is to mitigate volatility of the Group's cash flows in the euro and US dollar and to hedge against adverse exchange rate movements by using instruments designed to reduce currency risk exposure and its effect on the Group's financial performance. In accordance with the policy, the objective of currency risk management at the Group is to reduce the impact of adverse exchange rate movements on the Group's cash flows to a level acceptable by the Group, determined in accordance with the VaR methodology.
- **Level of currency hedging**  
The hedging level is considered optimum if up to 80% of the planned net currency exposure is hedged for a period of up to 6 months from the transaction date, up to 50% of the planned currency exposure is hedged for a period from 6 to 12 months from the transaction date, and up to 30% of the planned currency exposure is hedged for a period from 12 to 24 months from the transaction date. Using a higher currency hedging level requires approval from the Management Board following a recommendation from the Risk Committee.
- **Rules of executing currency hedges**  
Currency hedges are executed to reduce the Group's planned currency exposure and they are classified as cash flow hedges under hedge accounting. The amount of currency in a given transaction may not be higher than the hedged item in that currency. To hedge exposure in the euro and US dollar the Group primarily uses natural hedging, which involves increasing future liabilities in the euro and US dollar through execution of procurement, investing and financing contracts and agreements in those currencies. The remaining currency exposure is mitigated by executing transactions of the following types:
  - currency forwards,
  - currency swaps, involving temporary swaps of currencies with a bank to optimise short-term currency mismatch,
  - it is also possible to execute symmetric currency collars or other symmetric combinations of longing put options and shorting call options.

Currency hedges are generally settled by physical delivery of the currency on the expiry date. The Group may enter into hedging transactions with horizons of up to 24 months if this reduces the adverse impact of exchange rate fluctuations on the cash flows, and it is possible to secure the EUR/PLN or USD/PLN exchange rate to the extent it exceeds the exchange rate planned in the budget, and up to 3 months if it is possible to hedge the exchange rate at which a commercial transaction was executed if the exchange rate was below the budgeted rate.

The Group enters into currency hedges only with banks with which it has executed framework agreements setting out comprehensive terms of execution and settlement of such transactions.

Execution of currency hedging transactions where the hedge horizon is more than 24 months or the transaction does not conform to the Financial Risk Management Policy requires approval by the Management Board based on a recommendation of the Finance Committee.

### **Interest rate risk management**

The Group is exposed to interest rate risk related to its financial liabilities (chiefly borrowings) denominated in the zloty and the euro, which are based on variable market interest rates; and financial assets (mainly bank deposits) denominated in the zloty, which earn interest at variable and fixed market interest rates.

The objective of interest rate risk management is to optimise interest rates with a view to:

- minimising the cost of interest on debt,
- ensuring the highest available profitability of financial assets and their safe allocation.

To achieve that objective it is necessary to ensure an optimum structure and cost of project financing using proceeds from issues of securities and debt, and to provide for an optimum level of working capital. The Group primarily uses natural hedging involving the use of the same reference rate for borrowings and financial assets denominated in the zloty, and maintaining its available long-term credit facilities based on a fixed interest rate in the euro.

The remaining exposure to interest rate risk may be hedged using only the following transactions:

- forward rate agreements (FRA),
- interest rate swaps (IRS),
- cross-currency interest rate swaps (CIRS).

The Group may enter into a transaction to hedge interest rate risk if it is ensured that the expected cost of the underlying instrument is limited. Execution of such a transaction requires approval by the Risk Committee. Execution of an interest rate hedging transaction must be approved by the Management Board if its hedge horizon is more than 12 months or if the transaction does not conform to the Financial Risk Management Policy.

### **Price risk management**

As there are no adequate financial instruments hedging the price risk related to the Group's key raw materials and products, or no significant correlation between the price of such hedging instruments and contract prices of the raw materials and products has been confirmed, the Group does not intend to use such instruments to hedge price volatility. The Group intends to mitigate the risk of price volatility using natural hedging, which involves linking the largest possible part of its procurement and sales volumes (in particular of phenol, benzene, caprolactam and polyamide, used in its production chain) under framework contracts with changes in ICIS prices for a given raw material.

### **Credit risk management**

The Group has a credit risk management policy in place, which has been adopted by all key companies of the Group in which such risk exists.

- Identified credit risks  
The Group's credit risk is related to:
  - placements of cash and cash equivalents with banks;
  - granting trade credit to trading partners in the ordinary course of business.
- Purpose of credit risk management  
To mitigation the risk of loss of financial assets, including loans, receivables, cash and cash equivalents.

- Limits for cash allocation and trade credits
  - a) The total amount of placements of cash or other financial assets by any Group company should not exceed:
    - PLN 100m - with the Group's strategic bank with a low credit risk and high creditworthiness,
    - PLN 50m - with a bank important for the Group's operations, with a low credit risk and high creditworthiness,
    - PLN 10m - with other financial institutions with no greater than moderate credit risk and at least good creditworthiness.
  - b) The total amount of trade credit granted to trading partners by any Group company should not exceed:
    - the amount of insured trade credit,
    - the market value of security provided by the customer,
    - the trade credit limit determined by the Group company based on assessment of the trading partner's financial condition.
- Rules of credit risk management
  - a) Execution of transactions involving placement of cash and cash equivalents
    - Group companies make cash placements following selection of the highest interest rate quotations received from at least three banks, taking into account allocation limits, except for overnight deposits, which may be placed with the bank at which the account balance shows a financial surplus.
    - Exceeding the allocation limit and/or placement of a deposit with a term of more than one year requires approval by the Management Board member in charge of finance or the President of the Grupa Azoty Management Board.
  - b) Trade credit
    - The Group determines trade credit limits based on requests received from teams responsible for execution of a sale transaction.
    - A trade credit limit does not require a separate approval if it is insured or relevant security is provided by a bank or other institution with high creditworthiness.
    - In other cases, a trade credit limit decision requires approval by the Corporate Finance Department (for limits of up to PLN 350 thousand), the Credit Risk Committee (up to PLN 2.5m) or the Management Board member in charge of finance or the President of the Grupa Azoty Management Board (over PLN 2.5m).

In the case of actual or threatened insolvency, as a result of which an impairment loss is recognised, a Group company should immediately initiate an amicable recovery procedure, or collection or enforcement proceedings to recover the threatened financial asset or relevant security.

#### **Receivables insurance agreements**

As part of trade credit risk management, the Group cooperates with leading insurance companies, taking advantage of diversification and competition between insurers by accessing specialist knowledge on financial condition of the insured trading partners and having the ability to adjust the amount of the trade credits it offers to the limits provided by individual insurers to entities which are also customers of the Group companies.

The parent (with Grupa Azoty SIARKOPOL and Zakłady Azotowe Chorzów S.A. as co-insured) and Grupa Azoty KĘDZIERZYN signed uniform global trade receivables insurance agreements with KUKE, expiring in July 2017. Grupa Azoty PUŁAWY signed a receivables insurance agreement on the same terms with EULER HERMES, expiring in January 2017, and after the reporting date it signed a new insurance agreement with the same insurer, valid until 2018. Grupa Azoty POLICE executed a global insurance agreement with ATRADIUS, based on the uniform terms of insurance, valid until November 2017.

## 5.11. Expected financial condition

The parent and key Group companies are fully solvent, with good credit standing, despite the less favourable market conditions in the third quarter of 2016. The Group is able to pay its liabilities as they fall due and to hold and generate free operating cash flows to further support payment of such liabilities in a timely manner.

In 2016, the Group paid all of its borrowing-related liabilities when due, and there is no threat to its ability to continue servicing its debt.

In 2016, the parent paid dividend from the 2015 net profit of PLN 83,324 thousand, with the balance of the net profit allocated to support the continued implementation of the investment strategy. The other Group companies also paid out dividend from their 2015 net profits, in accordance with relevant dividend resolutions passed by their respective general meetings.

The Group has access to overdraft limits under physical cash pooling, which the parent may use at times of increased demand for funding at the Group companies; and to additional multi-purpose and working capital facilities available to its subsidiaries. The Group complies with the uniform covenants of its facility agreements which enable it to significantly increase financial debt when and as needed. The Group's strategic lenders view its financial condition as sound, and there are no material threats or risks of its deterioration in the future.

The Group's budget for 2017 takes into account all market information (forecasts) available to the Group and detailed budgets of its individual business units. The budget accounts for the main assumptions and optimises economic parameters derived from trends identified in the macroeconomic environment and internally, within the organisation.

The Group intends to consistently implement the financial and investment objectives assumed in the strategy, to ensure that the return on investment expected by investors is achieved.

To mitigate the impact of adverse external factors, the Group continues to diversify its supplies of natural gas (a key feedstock), actively manages its foreign exchange risk and the risk related to increasing prices of CO<sub>2</sub> emission allowances.

## 6. Risk, threats and growth prospects

### 6.1. Significant risk factors and threats

#### **Risk related to price and availability of natural gas**

In its search for alternative and competitive sources of gas, the Group companies seek to diversify both the geographical regions and the suppliers of their gas imports. Negotiations with alternative gas suppliers are conducted at the Group level, which allows the Group to leverage its stronger bargaining position.

The Group takes steps to satisfy its overall gas demand through a combination of a long-term contract with its strategic supplier (PGNiG S.A.), annual or shorter contracts with a number of other suppliers, and transactions on energy exchanges and the OTC market to meet its short-term demand. Currently, gas purchased by the Group is priced based on gas prices quoted on energy exchanges, which means that the Group purchases gas at prices paid by its competitors in the European Union.

The gas interconnector and gas storage facility extension projects, currently being implemented in Poland, and the launch of the LNG terminal in Świnoujście have minimised the risk of disruptions in gas supply.

The Group companies are also taking steps to reduce gas consumption.

#### **Risks associated with the planning and execution of strategic projects**

The Group companies are working on investment projects commenced in previous years, while embarking on new strategic ones, important for the Group's interests, including investments in property, plant and equipment. Delivery of the Strategy depends on a range of factors, including those outside of the Group's control. The risks to the implementation of the Strategy are external developments in the Group's environment, such as macroeconomic factors, market conditions, business environment and activities of the main competitors. They could adversely affect the Group's ability to develop its business as planned and to deliver its strategic objectives.

The Operationalisation of the Group's Strategy for 2014–2020 lists the strategic projects pursued by the Group. The risk inherent in the execution of strategic projects, including investment and other projects, lies in the possibility that major growth-oriented initiatives will not be completed according to plan or will not deliver the expected results, and that the objectives they are intended to achieve

will not be adequately translated into the project planning, monitoring or execution processes. In order to minimise the risks to the execution of strategic projects at the Group, internal procedures have been put in place to define and govern the preparation and execution of investment projects. Oversight has been introduced over strategic projects and their assumptions, and regular updates are provided on projects' status.

The execution of investment projects includes change management, where special attention is given to changes in foreign exchange rates, commodity prices, as well as the requirements to be met by newly constructed units. As a result, execution timetables and expenditure budgets can be updated on an ongoing basis. In addition, controlling officers monitor progress of financing of the projects to identify potential threats. These policies also take into account the obligations and requirements imposed on beneficiaries of public funding.

As part of the planning and execution of strategic projects, in the fourth quarter of 2016 the Group began the process of reviewing its growth strategy. The work will involve a review of rationale and scope of the strategic projects, and analysis of potential new strategic objectives.

### **Risk associated with new legal requirements relating to production processes, including environmental regulations**

#### **Risk associated with the implementation of the Industrial Emissions Directive (IED)**

Following the implementation of the Industrial Emissions Directive (IED) in January 2014, the Group will be required to bring its production facilities into compliance with the new regulations. The Group will have to undertake specific adaptation work, and bear its costs. To ensure that there is sufficient time for taking appropriate steps to adapt the Group's facilities to the changing regulations, the parent continuously monitors all planned and actual changes in the legal environment which could affect the Group's business. Any necessary projects are provided for in the Group's investment plans and subsequently executed.

#### **Risk associated with greenhouse gas emissions**

Greenhouse gas emissions are covered by legal regulations governing the European Union's emissions trading scheme (EU ETS). The system is based on the allocation of free greenhouse gas emission allowances for emitting installations and, if free allowances are not sufficient, on the purchase thereof in auctions. Each year, the number of the allowances allotted decreases by several percent. If the actual CO<sub>2</sub> emissions are not covered by the free allowances, the Group may need to incur additional capital expenditure on projects designed to reduce NO<sub>x</sub> and CO<sub>2</sub> emissions. The volume of CO<sub>2</sub> emissions depends on the energy intensity of production processes. In order to mitigate the risk, the companies have been taking steps to reduce the energy intensity of production processes and the greenhouse gas or NO<sub>x</sub> emissions.

#### **Risk related to BAT (Best Available Techniques) conclusions**

Following the scheduled review of the regulations on the Best Available Techniques for the Manufacture of Large Volume Inorganic Chemicals: Ammonia, Acids & Fertilisers, there is a risk of implementing stricter and broader requirements relating to the air pollution emissions standards. Similarly, there is a risk that new BATs will be defined for the installations for which so far no BATs have been specified. The period for adapting production installations to the emission requirements specified in the BAT conclusions is four years.

In order to meet the BAT requirements, companies should monitor on an on-going basis any drafts of new laws and regulations and actively present their opinions on the proposed legislation. The measures taken by the Group in this respect include:

- analysing the effectiveness of the technologies used in the context of trends prevailing in the competitive environment,
- planning and implementing projects designed to bring the production installations into compliance with the BAT/BREF standards,
- searching for new solutions used in the processes, in particular to improve efficiency and reduce energy intensity in the context of regulations in place and the current level of technology,
- developing and extending the product range by adding new fertilizers based on components produced in the existing units.

## Risk of adverse changes in the supply-demand balance

### In the Agro Fertilizers segment, the Group identifies risks related to:

- increased imports of nitrogen and compound fertilizers, produced from cheaper raw materials, to Poland and the EU, and consequently persisting oversupply and aggressive pricing policies pursued by importers struggling to maintain their shares in the fertilizer market;
- launch of significant new manufacturing capacities, particularly in the urea market (USA, Algeria) where oversupply periodically affects prices of other nitrogen fertilizers;
- increase of production capacities of nitrate fertilizers in Hungary and stronger impact of this product on the market in southern Poland;
- ban on trade in nitrate and CAN in Turkey, introduced for an indefinite period in response to terror attacks in the country – search for EU markets to sell products manufactured in or imported by Turkey;
- M&A activity in the chemical sector, which might enable chemical producers to exert stronger pressures on the EU fertilizer market;
- stronger competition as new products are marketed and more effective technologies are applied.

In order to mitigate the identified risks and to strengthen and consolidate its leadership in the segment, the Group has been taking steps to optimise its cost base and broaden the portfolio of products and services.

Measures taken by the Group to strengthen its competitive advantages in the fertilizers segment:

- implementation of the Group's updated distribution strategy,
- implementation of projects designed to improve the efficiency of production processes,
- strengthening the Group's market position through acquisitions and placement of new products in the market,
- taking active part in the consolidation processes in the chemical industry,
- initiation of anti-dumping proceedings,
- active participation in the work of Fertilizers Europe,
- cooperation with universities and research institutes,
- supporting agricultural producers by providing them with access to state-of-the-art fertilizing and production solutions.

### In the Plastics segment, the Group identifies risks related to:

- global oversupply of caprolactam and polyamide – excess volumes from the Far East are shipped to Europe, as a result of which EU manufacturers' traditional export markets begin to shrink and prices decline to unsatisfactory levels;
- M&A activity in the chemical sector, which might enable chemical producers to exert stronger pressures on the EU market.

To minimise the effect of the expected market trends, the Group has undertaken a number of initiatives to strengthen its competitive position:

- construction of a new PA6 production unit in Tarnów, which will fully balance caprolactam production within the Group and eliminate the need to sell a less processed product;
- the parent is finalising the details of the project to construct a new modified plastics facility in Tarnów, within the Kraków special economic zone, that will help further expand the product chain;
- continuation of the policy to diversify sales of caprolactam and polyamide;
- preparation of a long-term caprolactam manufacturing cost reduction programme;
- leveraging the synergies between Tarnów's and Puławy's units following the integration of the companies' production capacities and sales potential;
- adaptation to customer expectations by offering new products tailored to specific customer needs;
- the Group seeks to optimise the pool of raw material suppliers, with particular emphasis on direct partnerships with producers under long-term strategic contracts, and to develop an optimum procurement logistics model;
- the Group monitors the situation for any possible threats to be able to take necessary steps and mitigate adverse effects of such negative developments.



**In the Chemicals segment, the Group has identified risks related to:**

- weaker demand for titanium white from paint and varnish manufacturers, higher quality requirements in the plastics and paper industries, and significant increase in the production capacities of Chinese manufacturers;
- higher supply of OXO alcohols on balanced European markets, driven by heavy inflows of cheaper alcohols, especially from the Russian market;
- import of plasticisers to the balanced and highly competitive EU market, on which a wide range of plasticisers are available – the risk related to imports of non-phthalate plasticizers from the Korean and Turkish markets is particularly significant.

**The Group protects its business against those risks:**

- by adapting its product mix to the market requirements and needs, for instance by launching a unit producing Oxoviflex™, a non-phthalic plasticizer and, as production capacities grow, by seeking new customers for this product; by ensuring high purity of OXO alcohols and identifying market niches – e.g. improving DEHP plasticizer for medical applications or arranging deliveries tailored to the needs of end users (flexitanks for deep-sea freight of small volumes of products);
- through initiatives designed to minimise production costs;
- through active participation in marketing initiatives and trade associations.

**Currency risk**

The Group has a positive exposure to the euro and the US dollar which is hedged based on on-going monitoring of movements in the euro and US dollar exchange rates. The Group hedges its currency exposures using currency forwards and natural hedging.

In 2015, having implemented the new centralised Financing Model, the Group extended its hedge time horizon by using a portion of long-term financing in the form of a euro-denominated facility. In line with its accounting policy, for such currency instruments (maturing in more than one year) the Group uses hedging relationships with future revenue planned to be generated in foreign currencies.

The Group's Risk Committee analyses and sets consolidated targets for currency exposure of the Group as a whole and for its leading companies, and recommends target levels and horizons of hedges, types of currency instruments, and exchange rates for hedge transactions. Hedging transactions are executed by those Group companies where the exposure actually occurs.

The applied risk management methods enable the Group to limit the existing risk by using selected hedging instruments and strategies, based on long-term and one-year currency exposure plans and their updates to account for quarterly operational plans and short-term projection of currency flows and currency expenditures, and based on the transactions already registered in the financial and accounting system. However, these methods do not eliminate that risk completely. In addition, currency risk may affect the domestic nitrate fertilizer market in the context of bilateral trade with other EU countries. Strong fluctuations in exchange rates may affect the Group's business, financial condition or results of operations.

**Risk related to availability and efficiency of capital and other sources of funding**

One of the factors important for the successful development of the Group's business is the implementation of strategic projects and availability of capital for the financing of such projects, as discussed in Operationalisation of the Strategy for 2014–2020. There is a risk that insufficient access to capital or other sources of funding, or availability of such capital or other sources of funding at excessive cost, might adversely affect prospects for the Group's development and delivery of its strategy or that the Group might use the available capital in an inefficient manner and thus achieve returns that fall short of investors' expectations.

Under the consolidated financing model implemented in 2015, the Group executed a harmonised package of corporate financing agreements, thus enhancing its long-term security, based on uniform financing covenants agreed with banks, including a net debt to EBITDA ratio, which should not exceed 3.0x.

The Group also intends to pursue major investment projects via SPVs and to secure their financing in the form of project finance (without recourse to the Group), which may lead to a significant increase in debt in the future and require optimising selected covenants of the existing corporate financing agreements.

### **Risk of negative effect of CO<sub>2</sub> trading prices on the financial result**

The Group has in place a monitoring system for emissions covered by the EU ETS. It also performs ongoing balancing of greenhouse gas emissions. The Group monitors its actual emissions and the market prices of emission allowances, and takes appropriate steps in response to their fluctuations. The Group may be forced to incur higher-than-expected costs if it reports a deficit in emission allowances as at the end of the year and faces an increased demand for EUAs on the market.

The Group mitigates the risk of an adverse effect of EUA prices on the carbon market by averaging the price of emission units purchased on the spot market and by purchasing CO<sub>2</sub> emission allowances in financial derivatives with physical delivery in the future, in accordance with the purchase strategy in force from time to time. The Group effectively implements its strategy of rolling purchases of emission allowances, to ensure full coverage of any deficit of emission allowances that should be allocated for a given year and subsequently redeemed, with exercise prices not higher than projected. The Group has appointed the EU ETS Management Committee comprising representatives of all key Group companies. Its main objective is to supervise a joint model for managing CO<sub>2</sub> emission allowances at the Group companies, in particular the CO<sub>2</sub> emissions trading strategy, and subsequently the implementation of the emissions trading strategy across the Group.

### **Risk of major industrial accidents or technical failures disrupting the continuity of processes and operation of key production units**

The Group has reliable safety systems and preventive measures in place at all organisational and technological levels, including occupational health and safety as well as protection against industrial accidents; however, no assurance can be given that these will completely eliminate the risk of such accidents and ensure the continuity of production processes. Their relevance is assessed by external and internal inspection authorities, as well as accreditation/certification bodies.

Prevention of industrial accidents at the Group companies is achieved through a range of activities, including:

- identification of hazards inherent in technological processes, storage and transport, and implementation of technical solutions and organisational measures to minimize the risk of an accident,
- ongoing monitoring of operations of plant and equipment and evaluation of their technical condition,
- fitting of plants and units with safety and protection systems to minimise the risk of major accidents and environmental contamination, as well as risks to life and health,
- implementation of new projects and upgrades based on technical and organisational solutions designed to ensure occupational health and safety (the Group's facilities are compliant with the Best Available Techniques (BAT) reference documents, which are the source of the world's strictest safety requirements, including environmental regulations),
- carrying out scheduled technical stopovers and maintenance shutdowns to ensure that the units are kept in a proper working order,
- continuous improvement of the employees' qualifications through training courses, etc.
- introduction across the Group of corporate rules on how to report industrial accidents and failures, as well as how to investigate them and take preventive measures to mitigate the risk of their recurrence in the future,
- analysis and periodic update of technical and technological risks at Grupa Azoty,
- implementation of an operational excellence programme,
- implementation of the Product Stewardship standard, covering all stages of the fertilizer lifecycle, which has been confirmed by the issuing of a certificate.

### **Risk related to maintaining continuity of ammonia production and availability of ammonia at economically viable prices**

To mitigate the risk and to strengthen and consolidate its leading position, the Group takes steps to:

- diversify suppliers of natural gas and ammonia,
- maintain ammonia stocks at optimum levels across the Group, to ensure continuity of supplies and production of ammonia and caprolactam,
- prepare reduced-output scenarios based on break-even points for key products,
- analyse on an ongoing basis maximum ammonia purchase prices to achieve product profitability,
- analyse on an ongoing basis fixed and variable costs of production to determine economic viability of purchasing ammonia outside the Group,
- maintain the operational reliability of units by carrying out overhauls, upgrades and investments, in particular in areas covered in the technical risk analysis.

### **Risk of implementation/tightening of EU or local regulations which would restrict the use or application of the company's products**

The Group monitors and implements new regulatory requirements on an ongoing basis. The Group takes an active part in the work of registration consortia and European associations to obtain advance information about upcoming changes in the legislation. In each case the Group reviews the impact of new regulations on its products. Potential risks associated with the tightening of laws, restricting the use of the company's products are related to EU Directives or Regulations such as Regulation (EC) No. 2003/2003 of the European Parliament and of the Council of 13 October 2003 relating to fertilizers certified with a certificate of conformity. The Group is currently in the process of identifying threats associated with the new draft of the fertilizers regulation, which is designed to implement the principles of the Circular Economy package. The proposal assumes an uninterrupted flow of goods on the single EU market, preceded by the mandatory harmonisation of fertilizing products (CE marking). The European Commission's proposal also covers the use of organic waste and bio-waste as raw materials to manufacture fertilizers. The new rules will apply to all types of fertilisers to ensure the highest level of soil protection. The Regulation introduces strict limits for heavy metal contamination, including cadmium content in phosphate fertilizers. The European Commission assumes that this will reduce health and environmental risks. Moreover, in this way the EU intends to reduce the dependence of the fertilizer industry on imports of phosphorus-bearing materials. Work is under way to implement into Polish law the Directive of the European Parliament and of the Council on the reduction of national emissions of certain atmospheric pollutants and amending Directive 2003/35/EC (NEC Directive, COM(2013)92). The draft proposes that ammonia emissions be reduced. The agricultural sector can expect new requirements for ammonia emissions from different types of mineral fertilizers, primarily those based on ammonia (especially urea) rather than nitrate fertilizers. The Group also monitors other aspects of EU regulations, such as free trade agreements (DCFTA Ukraine, TTIP). The parent also takes steps to ensure that the entire manufacturing and distribution process meets the safety requirements applicable to trading in its products.

### **Risk of failure to meet deadlines for reduction of NOx, SOx and particulate matter emissions**

The Group takes steps to ensure its compliance with the requirements of the IED Directive (on industrial emissions) which entered into force as of January 1st 2016 and defined new emission standards for the combustion of fuels in installations (Regulation of Minister of the Environment of November 4th 2014 on emission standards for certain units, fuel combustion sources, as well as waste incineration and co-incineration equipment). The new standards in particular apply to SOx, NOx and particulate matter emission limits.

The IED Directive and the Environmental Protection Law provide for postponing the effective date of the more restrictive emissions standards. One such mechanism is the Transitional National Plan (TNP). The fuel combustion facilities operated by the Group have also been submitted for inclusion in the TNP.

The following investment projects have been undertaken to meet the above standards:

- Grupa Azoty KĘDZIERZYN Group - new coal-fired generating unit;
- Parent - wet flue gas desulfurization unit;
- Grupa Azoty POLICE Group - flue gas desulfurization unit.

When the projects are completed, the Group will achieve compliance with the emission requirements under the IED Directive and Polish regulations.

## **6.2. Significant external and internal growth factors**

### **Market overview**

The World Bank estimates that in 2016 the global GDP grew by 2.3%. According to forecasts presented in the 'Global Economic Prospects' report, in 2017 the global economy will expand at a pace of 2.7%, driven mainly by emerging and developing economies. In 2017, developed economies are expected to grow at a rate of 1.8%, a modest improvement on the 1.6% recorded in 2016, with an outlook to maintain this growth rate in 2018. The World Bank estimates that in 2016 Poland's GDP grew by 2.5%, down on the 3.9% recorded in 2015. The World Bank further predicts that the growth of the Polish economy will again exceed the 3% mark in 2017, when it will expand at a rate of 3.1%.

The growth of the chemical industry will continue to depend on changes in the global economy. Following a stagnation in 2016, CEFIC estimates that in 2017 chemical production in the EU will

increase by 0.5%, despite the impact of globalisation and challenges related to the growing costs of doing business in the EU. It is expected that internal demand will compensate for weaker demand for European chemical exports. Despite the forecast growth of chemical production in Europe, the share of the European chemical industry in the global market is diminishing as it currently ranks third, trailing behind Asia and the US. Zacks Investment Research predicts that given the current economic environment, chemical manufacturers around the world may seek opportunities to improve their competitive positions through such measures as further cost synergies, expanding activity in market segments offering the best growth potential, and building the scale of business through consolidation. Factors which will affect results of the Group's operations over at least the next reporting period include:

- situation on the markets of natural gas, coal, electricity and petroleum products (mainly propylene, benzene and phenol) and the continuing low price environment,
- situation in agriculture and the fertilizers industry, including prices of agricultural produce staying low in the long term,
- conditions prevailing in the main sectors which purchase the Group's products and on the markets where those sectors sell their products.

### External factors

In line with the Strategy until 2020, the main objective of the Group's development initiatives is to improve its competitive position and reduce exposure to negative macroeconomic factors, such as growing costs of energy and environmental protection.

In the Fertilizers segment, the key initiatives will focus on the optimisation of production structure, and on leveraging the segment's synergies with caprolactam production. The Group plans to increase the output of granulated fertilizers, reduce production costs, and improve the quality of fertilizers.

In the Plastics segment, the key initiatives will be to increase the output of polyamides, to balance the production capacities for caprolactam and polyamides, and to reduce caprolactam production costs. The main goals are to utilise the caprolactam output of the Group in a more efficient manner, to increase sales of caprolactam, and to reduce costs of its production.

In the Oxoplast segment, the range of plasticizers will be expanded to include next-generation products - non-phthalate plasticizers.

In the years ahead, the focus will be on projects related to upgrading the Group's power generating assets. The plants in Tarnów, Police, and Puławy will be brought into compliance with the requirements of the IED Directive on industrial emissions, and a new energy source will be built at the Kędzierzyn plant.

### Interest rates in Poland

In 2016, interest rates in Poland did not change. As announced by the Governor of the National Bank of Poland, despite inflationary impulses, partly attributable to the rising prices of energy carriers and partly to stronger consumer demand, interest rates should remain at their current level until the end of 2017. Some analysts expect interest rate increases in the fourth quarter of 2017, if domestic inflation exceeds PLN 2.5%, i.e. moves above the target set by the Monetary Policy Council.

Accordingly, the Group's base interest rate (1M WIBOR) should stay at 1.7%, which has a positive effect on stabilising the Group's borrowing costs at a relatively low level. Moreover, it ensures secure debt service also if the borrowing grows to finance investing activity.

Deflationary pressures continue to persist in the Eurozone and, given additional threats to economic growth related to Brexit, the European Central Bank will continue its quantitative easing programme and a policy of negative interest rates. On the other hand, the Fed is almost certain to raise interest rates for USD-denominated debt in 2017 given the sustained, stable growth of the US economy and concerns regarding increased inflationary pressures.

To conclude, any adverse changes to the current low interest rates on debt in currencies used by the Group to finance its activities (PLN and EUR) are unlikely before the end of 2017. Thus the risk of the Group's financial condition or results of operations deteriorating on higher borrowing costs is considered low.

In terms of market rates, a relatively narrow spread between credit and deposit rates available to the Group is expected to continue, although they may increase slightly following the introduction of the tax on bank assets in Poland.

Interest income earned on free cash under the cash pooling arrangement and fixed-term deposits will partially offset the borrowing costs.

As at December 31st 2016, the Group did not carry any unrealised interest rate hedges.

## 7. Shares and shareholding structure

### 7.1. Total number and par value of Grupa Azoty shares, holdings of the shares by supervisory and management personnel, and interests of such persons in the parent's related entities

Number and par value of shares as at the date of issue of this report:

- 24,000,000 Series AA shares with a par value of PLN 5 per share,
- 15,116,421 Series B shares with a par value of PLN 5 per share,
- 24,999,023 Series C shares with a par value of PLN 5 per share,
- 35,080,040 Series D shares with a par value of PLN 5 per share (issued in 2013).

The total number of Grupa Azoty shares is 99,195,484 (ISIN code PLZATRM00012).

As at December 31st 2016 and as at the date of this report, none of the members of the parent's Management or Supervisory Board held any shares in the parent's share capital.

As at the date of this report, none of the parent's supervisory or management personnel held any shares in the parent's related parties.

### 7.2. Treasury shares held by the parent, the Group companies and persons acting on their behalf

The parent holds no treasury shares. The Group companies hold no shares in the parent.

### 7.3. Grupa Azoty shares

The parent has been listed on the Warsaw Stock Exchange since June 30th 2008.

The parent's share capital amounts to PLN 495,977,420 and is divided into 99,195,484 shares with a par value of PLN 5 per share. Grupa Azoty shares (ticker: ATT) are listed on the WSE main market in the continuous trading system and are included in the WIG, WIG-Poland, WIG30 and mWIG40 domestic indices and the chemical sector index, WIG-Chemia.

The parent is included in the following foreign indices:

- MSCI Emerging Markets Index (since February 2013). The index includes large and mid cap stocks from 23 emerging markets. The index currently comprises 832 companies;
- FTSE Emerging Markets Index (since March 2015). The FTSE Emerging Markets index is part of the FTSE Global Equity Index Series (GEIS), which includes large and mid cap stocks from advanced and emerging markets. The FTSE indices are listed on the London Stock Exchange.

The parent is also included in CSR indices:

- Since November 19th 2009, the parent has been a constituent of the RESPECT index of the Warsaw Stock Exchange. The parent has been appreciated for its engagement in applying corporate social responsibility principles and having the highest standards in corporate governance, corporate disclosure discipline, and investor relations, as well as environmental, social, and employee matters. In December 2016, the Company was for the tenth time included in the elite group of companies covered by the RESPECT Index, the first CSR-focused index in Central and Eastern Europe.
- In January 2017, the parent was included in FTSE4Good Emerging, following a thorough assessment of its performance in terms of environmental, social and corporate governance practices. The assessment was performed by FTSE Russell. The index was launched in December 2016 to add companies from emerging markets to the group of companies reporting their environmental, social responsibility and corporate governance performance.

All other key information on Grupa Azoty shares, including information on voting restrictions, is presented in the sections devoted to compliance with corporate governance rules.

## Shareholding structure

Below are listed shareholders holding directly, or indirectly through subsidiaries, at least 5% of total voting rights at the parent's General Meeting as at the date of this report, along with information on the number of shares held by such entities, their respective ownership interests, the number of voting rights held, and their share in total voting rights at the General Meeting.

### Shareholding structure as at December 31st 2016

Shareholder	Number of shares	Ownership interest (%)	Number of votes	% of voting rights
State Treasury of Poland	32,734,509	33.00	32,734,509	33.00
ING OFE	9,883,323	9.96	9,883,323	9.96
Norica Holding S.à r.l. (indirectly: 19,321,700 shares, i.e. 19.47%)	71,348	0.07	71,348	0.07
Rainbee Holdings Limited <sup>)</sup>	9,820,352	9.90	9,820,352	9.90
Opansa Enterprises Limited <sup>)</sup>	9,430,000	9.50	9,430,000	9.50
TFI PZU S.A.	8,530,189	8.60	8,530,189	8.60
European Bank for Reconstruction and Development	5,700,000	5.75	5,700,000	5.75
Other	23,025,763	23.22	23,025,763	23.22
<b>Total</b>	<b>99,195,484</b>	<b>100.00</b>	<b>99,195,484</b>	<b>100.00</b>

<sup>)</sup> Direct subsidiary of Norica Holding S.à r.l.

In the period from December 31st 2016 to the date of issue of this report, the parent was not officially notified of any changes in major holdings of its shares.

## Dividend policy

The parent's dividend policy is consistent with the Strategy for 2014-2020. Distributions to shareholders depend on the parent's earnings and financial condition. The Management Board, recommending dividend payouts equal to 40–60% of the parent's non-consolidated net profit for a given financial year, takes into account a number of factors relevant to the parent and the Group, such as business prospects, future profits, cash requirement, financial position, business expansion plans and legal requirements. The dividend policy will be revised on an as-needed basis, and any decisions made by the parent in this respect will take account of a number of factors concerning both the parent and the Group.

The final decision on profit distribution for a given financial year is made each time by shareholders at the Annual General Meeting.

In the reporting period, the parent distributed net profit earned in 2015. From the net profit, PLN 83,324 thousand (PLN 0.84 per share) was allocated to dividend.

The dividend record date and the dividend payment date were set for June 20th 2016 and July 11th 2016, respectively.

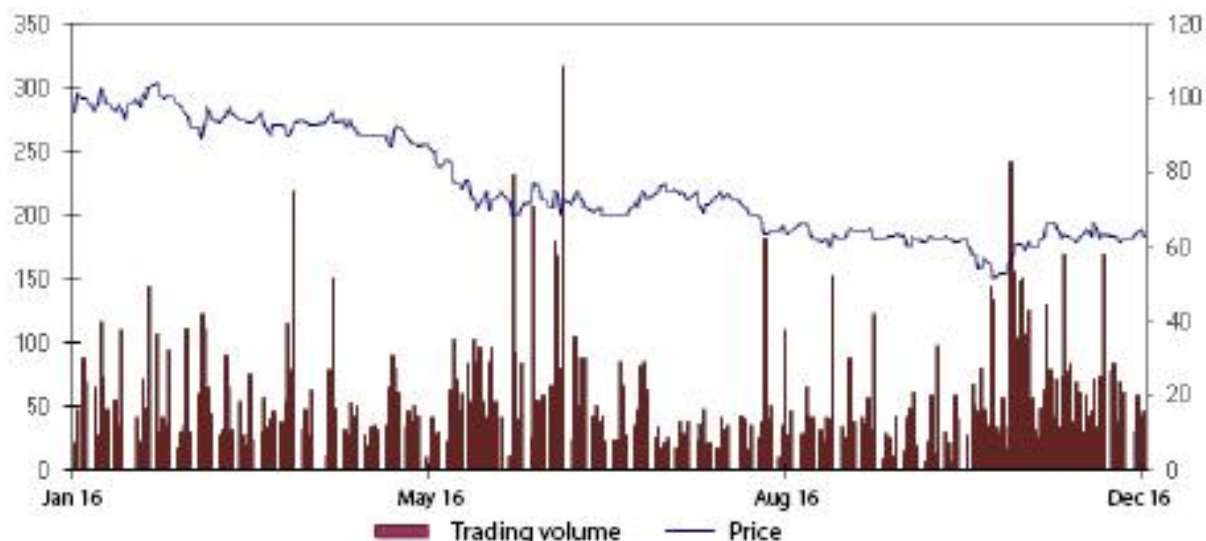
### Dividend paid in 2008–2016

Year for which dividend was paid	Record date	Payment date	Net profit	Total dividend	DPS
2008	26.06.2009	Tranche 1: August 31st 2009	PLN 61,935 thousand	PLN 39,898,749.42	PLN 1.02
		Tranche 2: November 6th 2009			
2012	22.04.2013	24.05.2013	PLN 250,692 thousand	PLN 148,793,226.00	PLN 1.50
2013	18.06.2014	09.07.2014	PLN 44,117 thousand	PLN 19,839,096.80	PLN 0.20
2015	20.06.2016	11.07.2016	PLN 209,055 thousand	PLN 83,324,206.56	PLN 0.84

## Performance of Grupa Azoty shares

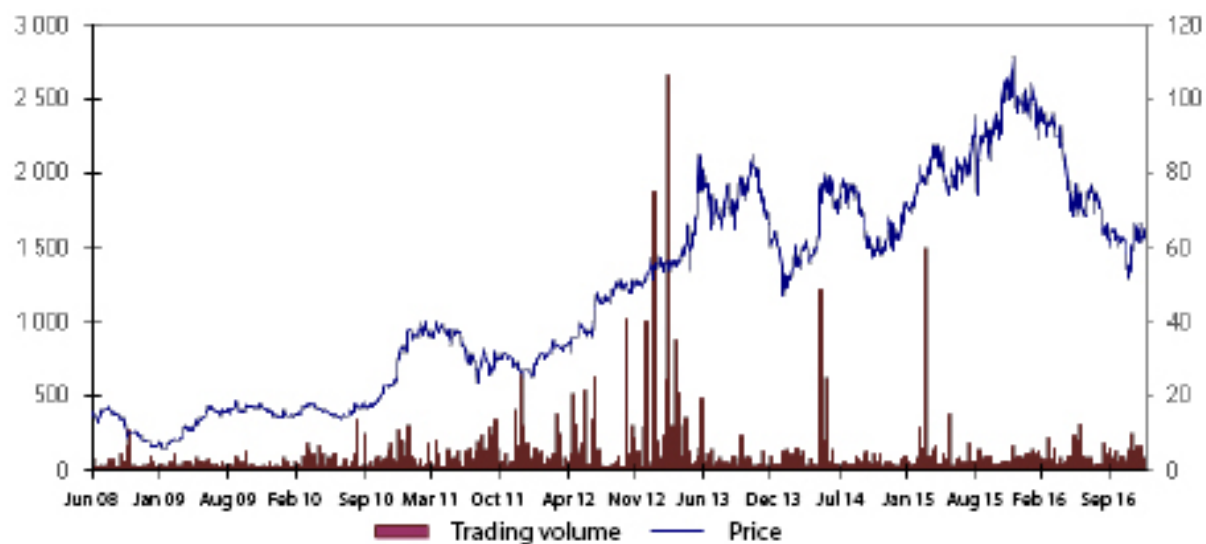
After the all-time high of PLN 113 seen in December 2015, in January 2016 the parent's share price fell to approximately PLN 100. In mid-February 2016, the share price started to decline steadily, to the all-year low of PLN 51 in mid-November, marking a turning point in the year, following which the short-lived downward trend was reversed and the price started gradual recovery. At year-end, the parent's shares traded at above PLN 62.

### Grupa Azoty share price from January 1st 2016 to December 31st 2016



Source: GPWInfoStrefa, Grupa Azoty

### Grupa Azoty share price from the IPO (June 30th 2008) to December 31st 2016



Source: GPWInfoStrefa, Grupa Azoty

## Recommendations

In 2016, analysts of 10 brokerage houses and investment banks covering the parent issued 19 recommendations for the stock.

**Analyst recommendations for Grupa Azoty shares, published between January 1st 2016 and the date of this report**

Date	Recommendation	Target price	Price at recommendation date	Broker
Feb 27 2017	hold ▲	PLN 77.00 ▲	PLN 71.70	Raiffeisen
Feb 6 2017	hold ▲	PLN 70.00 ▲	PLN 71.20	DM BOŚ
Jan 26 2017	hold ▲	PLN 73.90 ▲	PLN 71.60	DM mBank
Dec 5 2016	hold ▲	PLN 65.40 ▼	PLN 60.00	DM BOŚ
Nov 21 2016	buy ▲	PLN 64.00 ▼	PLN 53.70	Raiffeisen
Oct 21 2016	hold ▲	PLN 66.20 ▼	PLN 62.00	Trigon DM
Oct 16 2016	hold ▲	PLN 67.40 ▼	PLN 61.80	DM BOŚ
Sep 30 2016	reduce ▼	PLN 59.00 ▼	PLN 61.62	ERSTE Securities
Aug 30 2016	hold ▲	PLN 65.50 ▼	PLN 64.79	DM mBank
Jul 28 2016	reduce ►	PLN 65.80 ▲	PLN 74.00	DM BDM
Jul 21 2016	buy ►	PLN 82.10 ▲	PLN 74.21	Trigon DM
Jul 12 2016	buy	PLN 80.70	PLN 71.90	Trigon DM
Jun 23 2016	hold ▲	PLN 75.70 ▲	PLN 73.00	DM BZ WBK
Jun 21 2016	hold ▲	PLN 74.18 ▼	PLN 71.69	PKO BP
Jun 9 2016	hold ▲	PLN 82.10 ▼	PLN 76.90	ING Securities
Jun 7 2016	buy ►	PLN 86.10 ▼	PLN 72.00	DM mBank
Jun 2 2016	buy ▲	PLN 100.20 ►	PLN 68.20	DM mBank
May 18 2016	sell ►	PLN 63.90 ▼	PLN 75.60	ERSTE Securities
Apr 1 2016	hold ▲	PLN 98.00 ▼	PLN 96.30	Raiffeisen
Feb 11 2016	sell ►	PLN 56.00 ▼	PLN 95.00	Societe Generale
Feb 2 2016	hold ▲	PLN 100.20 ▲	PLN 104.00	DM mBank
Jan 5 2016	hold	PLN 91.80	PLN 96.38	DM mBank

### Investor relations

Acting in accordance with the highest standards of capital market communication and corporate governance, the parent provides all market participants, in particular current and prospective shareholders, with exhaustive and reliable information on events taking place at the parent and the Group. In its communication with investors, the parent goes above and beyond the statutory disclosure requirements and pursues an open information policy in response to the high expectations of capital market participants.

Upon the issue of periodic reports, the Group holds conferences at which the Management Board presents and discuss financial results. As part of the consolidation process, such conferences are held jointly by all issuers from the Group, to present a coherent picture of the Group to the investors and analysts. Because of the shareholding structure and significant interest they attract, earnings conferences for capital market analysts are broadcast online in real time, in Polish and in English. Conference recordings and presentations are available on the parent's website and on social networking sites.

In 2014, representatives of the Group also met with capital market participants during numerous one-on-one meetings and conferences, held both in Poland and abroad. They also attended industry conferences and conferences at which listed companies from Eastern and Central Europe were presented.

Keen to communicate with its retail investors as well, the Group holds open webchat sessions following release of its financial reports, where the shareholders are able to communicate directly with the Group's representatives and ask questions. Presentations of financial results, addressed in particular to institutional investors, investor presentations, and chat logs are available on the parent's website (the Investor Relations section).



Since its IPO, the Group has held annual meetings with retail investors during the Wall Street conference and the affiliated Targi Akcjonariat fair, both organised by the Polish Association of Retail Investors. In 2016, the Group was the main partner of the conference. In 2016, the Group representatives took part in Capital Market Games, a sports event addressed to minority investors, organised by the Polish Association of Retail Investors.

In response to the shareholders' expectations, the parent makes every effort to ensure that the published information is disseminated as widely as possible. To this end, the Group publishes its key announcements also in social media. The corporate website is a key tool for communicating with the capital market, featuring the parent's current and periodic reports, important information about AGMs and EGMs, analyst recommendations and financial results. The website, with its dedicated section for investors, was upgraded to provide more precise capital market information in a more user-friendly manner. The content and presentation quality of the IR section, as well as the use of the Internet to communicate with investors, were recognised multiple times by the jury of the Golden Website Award for Listed Companies, organised by the Polish Association of Listed Companies, achieving a high rank in the competition. The website already received the Golden Website Award in the past, during its 7th and 8th edition.

On its website [www.grupaazoty.com](http://www.grupaazoty.com), the parent maintains a FAQ section, containing answers to the most frequently asked questions.

The parent's IR efforts were also recognised by investors, who praised its active participation in the Akcja Inwestor campaign in the popular Polish economic daily *Puls Biznesu*. Consequently, the parent has been honoured with the prestigious 'Responds to Investors' mark since August 2010.

Grupa Azoty S.A. participates in the '10 out of 10' Programme organised by the Polish Association of Retail Investors. The goal of the Programme is to apply best practices in communication with retail investors, based on their needs and communication models used on foreign markets. By participating in the project, the parent promises that the Company will pursue a proactive policy of communication with retail investors and respect their rights. The parent also boasts the '2014 Capital Market Hero' title in recognition of its active two-way communication with retail investors.

In November 2016, the parent was among the winners of 'Business Sharks' awards given to commemorate the 25th anniversary of the Warsaw Stock Exchange. The citation stated that "*The Management Board and the Investor Relations Team of Grupa Azoty S.A. proved that in their daily business they do not forget to communicate with the media, shareholders, investors and analysts, contributing to the development of the Polish capital market and enhancing its prestige*".

On April 6th 2017, Grupa Azoty earned the prestigious title of 'Transparent Company of the Year 2016'. The ranking is organised by the Accounting and Tax Institute and the *Gazeta Giełdy i Inwestorów Parkiet* daily to award companies included in the three main stock-exchange indices – WIG20, mWIG40, and sWIG80 – and selected based on the results of a survey covering financial reporting, investor relations, and corporate governance.

## 8. Statement of compliance with corporate governance standards

### 8.1. Corporate governance code applicable to the parent and the place where the text of the code is available to the public

Having declared compliance with the highest capital market communication standards and principles of corporate governance, in 2016 the parent applied the "Code of Best Practice for WSE Listed Companies 2016", prepared by the Warsaw Stock Exchange. Following the adoption of the new text of the "Code of Best Practice for WSE Listed Companies 2016" by way of Resolution No. 26/1413/2015 of the supervisory board of the Warsaw Stock Exchange dated October 13th 2015, the parent declares that it follows the recommendations and principles laid down in the new "Code of Best Practice" as published on the website of the Warsaw Stock Exchange at:

[http://static.gpw.pl/pub/files/PDF/RG/DPSN2016\\_\\_GPW.pdf](http://static.gpw.pl/pub/files/PDF/RG/DPSN2016__GPW.pdf)

to the extent described on the parent's website:

[http://tarnow.grupaazoty.com/files/4fbe6653/gpw\\_dobre\\_praktyki\\_grupa\\_azoty\\_2016.pdf](http://tarnow.grupaazoty.com/files/4fbe6653/gpw_dobre_praktyki_grupa_azoty_2016.pdf).

## 8.2. Information on the parent's non-compliance, if any, with the corporate governance standards and reasons for such non-compliance

Since the flotation of its shares on the WSE in 2008, the parent's aim has been to observe the best corporate governance practices, which was expressed in the declaration of the parent's Management Board contained in the issue prospectuses and confirmed in the Management Board's resolutions on the adoption of the recommendations and principles imposed by subsequent versions of the "Code of Best Practice for WSE Listed Companies".

As the new "Code of Best Practice for WSE Listed Companies" applies now, the Company's Management Board declares that as of January 1st 2016 all the recommendations and detailed principles imposed thereby are followed, with the exception of:

- recommendation IV.R.2.

"If justified by the structure of shareholders or expectations of shareholders notified to the company, and if the company is in a position to provide the technical infrastructure necessary for a general meeting to proceed efficiently using electronic communication means, the company should enable its shareholders to participate in a general meeting using such means, in particular through:

- 1) real-time broadcast of a general meeting,
- 2) real-time bilateral communication where shareholders may take the floor during a general meeting from a location other than the venue of the general meeting,
- 3) exercise of the right to vote during a general meeting either in person or through a proxy."

Explanation: The Company's Articles of Association and the Rules of Procedure for the Company's General Meeting do not provide for real-time broadcasting of General Meetings. Also, the Company believes that the way General Meetings have been documented and carried out to date ensures transparency and safeguards the rights of all shareholders. Further, information on passed resolutions is published by the Company in the form of current reports, also on its website. Therefore, investors are able to review the matters discussed at General Meetings. However, the Company may apply this principle in the future. In the opinion of the Company's Management Board, the decision not to apply the abovementioned principle will not affect the reliability of the Company's information policy, nor will it hinder shareholders' participation in General Meetings.

- and the following principles:

I.Z.1.20 "A company should operate a corporate website and publish on it, in a legible form and in a separate section, in addition to information required under the legislation, an audio or video recording of a general meeting,"

Explanation: In the Company's view, the way General Meetings have been documented and carried out to date ensures transparency and safeguards the rights of all shareholders. Further, information on passed resolutions is published by the Company in the form of current reports, also on its website. Therefore, investors are able to review the matters discussed at General Meetings. The Company may apply this principle in the future.

In the opinion of the Company's Management Board, the decision not to apply the abovementioned principle will not affect the reliability of the Company's information policy, nor will it hinder shareholders' participation in General Meetings.

IV.Z.2. "If justified by the shareholding structure, a company should ensure publicly available real-time broadcasts of general meetings."

Explanation: The Company's Articles of Association and the Rules of Procedure for the Company's General Meeting do not provide for real-time broadcasting of General Meetings. Also, the Company believes that the way General Meetings have been documented and carried out to date ensures transparency and safeguards the rights of all shareholders. Further, information on passed resolutions is published by the Company in the form of current reports, also on its website. Therefore, investors are able to review the matters discussed at General Meetings. However, the Company may apply this principle in the future.

In the opinion of the Company's Management Board, the decision not to apply the abovementioned principle will not affect the reliability of the Company's information policy, nor will it hinder shareholders' participation in General Meetings.

## Parent's report on compliance with recommendations of Best Practices in the reporting period

### I. Disclosure Policy, Investor Communications

#### I.R.1.

*Where a company becomes aware that untrue information is disseminated in the media, which significantly affects its evaluation, it should immediately publish on its website a communiqué containing its position on such information, unless in the opinion of the company the nature of such information and the circumstances of its publication give reasons to follow a more adequate solution.*

The Company declares to make every effort to prevent any damage that may be caused by disseminating untrue information about it. The Company seeks to ensure transparency by responding effectively to untrue information and limiting the negative effects of its dissemination. The Company takes care to provide its shareholders and the market with a true and accurate picture of the Group. Considering the above, the Group monitors the media, including newspapers, electronic media, and online resources.

#### I.R.2.

*Where a company pursues sponsorship, charity or other similar activities, it should publish information about the relevant policy in its annual activity report.*

The Company pursues transparent sponsorship, charity or other similar activities.  
For details, see section 8.14 of this report.

#### I.R.3.

*Companies should allow investors and analysts to ask questions and receive explanations - subject to prohibitions defined in the applicable legislation - on topics of their interest. This recommendation may be implemented through open meetings with investors and analysts or in other formats allowed by a company.*

The Company, pursuing an open information policy, provides all market participants, in particular current and prospective shareholders, with exhaustive and reliable information on events taking place at the Company and the Group.

For details, see section 7.3 of this report.

#### I.R.4.

*Companies should use best efforts, including taking all steps well in advance as necessary to prepare a periodic report, to allow investors to review their financial results as soon as possible after the end of a reporting period.*

The Company takes all necessary steps to prepare periodic reports well in advance. When planning the issue dates for periodic reports, the Company seeks to ensure that investors are able to review the Company's financial results as soon as possible.

### II. Management Board, Supervisory Board

#### II.R.1.

*To ensure the highest standards of the management board and the supervisory board of a company in efficient fulfilment of their obligations, the management board and the supervisory board should have members who represent high qualifications and experience.*

In 2016, the Management Board and Supervisory Board were composed of persons holding university degrees in law, economics, chemical engineering and technology, as well as environmental engineering.

Moreover, most of the Board members completed post-graduate programmes in corporate management, polymer chemistry and technology, management control, MBA, as well as specialist courses or trainings, including in power engineering, transport of hazardous materials, management, project management, disclosure requirements applicable to WSE-listed companies, brokerage courses, training in asset management strategy, risk management and corporate governance.

For information on members of the Management and Supervisory Boards and their CVs, see section 8.12 of this report.

#### II.R.2.

*Decisions to elect members of the management board or the supervisory board of a company should ensure that the composition of these bodies is comprehensive and diverse among others in terms of gender, education, age and professional experience.*

Pursuant to Art. 23.3 of the Company's Articles of Association, a member of the Management Board should have a university degree and at least five years of professional experience in a managerial

position, except for a candidate for the position of the Management Board member elected by the Company's employees.

Given their vast competences and professional experience, including experience in serving on supervisory bodies of chemical or financial companies, members of the Management Board and Supervisory Board manage and supervise the Company's operations properly and to a sufficient degree.

For information on members of the Management and Supervisory Boards, their gender, education, and professional experience, see section 8.12 of this report.

#### II.R.3.

*Serving on the management board of a company should be the main area of the professional activity of management board members. Additional professional activities of management board members must not require such amounts of time and effort as would adversely affect the proper performance of the members' duties and responsibilities at the company. In particular, management board members should not serve in governing bodies of other entities if the time devoted to such service were to prevent the proper performance of their duties and responsibilities at the company.*

Some of the Company's Management Board members also hold positions in governing bodies of the subsidiaries, which facilitates successful and effective enforcement of decisions made by the parent's Management Board at all Group companies with a view to maximising efficiency of the Group's operations.

In addition, holding positions in governing bodies of the subsidiaries by the Management Board members strengthens the Management Board's supervision of synergies and improves efficiency of the Group's processes.

#### II.R.4.

*Supervisory board members must be able to devote the time necessary to perform their duties.*

The Supervisory Board exercises ongoing supervision of the Company's operations in each area of its activity. Pursuant to Art. 38 of the Company's Articles of Association, the Supervisory Board meetings are held at least once every two months.

In the financial year 2016, the Supervisory Board held 12 meetings and five voting procedures using means of remote communication.

#### II.R.5.

*If a supervisory board member resigns or is unable to perform his or her duties, the company should immediately take steps necessary to ensure substitution or replacement on the supervisory board.*

If there is a threat that resignation or inability to perform his or her duties by a member of the Supervisory Board may result in a vacancy on the Board, the Company declares to take necessary steps to fill such vacancy. In the event of any temporary vacancy on the Supervisory Board, the Company will report such circumstance as a breach of the principle.

In the composition of the Supervisory Board there are members appointed by the Company employees, pursuant to Art. 14 of the Act on Commercialisation and Privatisation.

#### II.R.6.

*Being aware of the pending expiration of the term of office of management board members and their plans of further performance of duties on the management board, the supervisory board should take steps in advance to ensure efficient operation of the company's management board.*

The Company declares to apply this recommendation by ensuring continued operation of the Management Board, and by taking steps, sufficiently in advance, to ensure appropriate operation of the Company.

#### II.R.7.

*A company should allow its supervisory board to use professional and independent advisory services necessary for the supervisory board to exercise effective supervision in the company. In its selection of the advisory service provider, the supervisory board should take into account the financial condition of the company.*

Should the need arise, the Company declares to allow its Supervisory Board to use professional and independent advisory services necessary for the Board to exercise effective supervision. In its selection of the advisory service provider, the Supervisory Board takes into account the financial condition of the Company.

### III. Internal systems and functions

#### III.R.1.

*The company's structure should include separate units responsible for the performance of tasks within its systems or functions, unless the separation of such units is not justified by the size or type of the company's activity.*

The Company's structure includes separate units responsible for the performance of tasks within its systems or functions.

The Company's Management Board is responsible for the implementation, maintenance, and efficiency of internal control, risk management, and compliance systems, as well as internal audit function as recommended by good practices. Persons responsible for the operation of organisational units which perform tasks related to the above systems and functions report directly to the President of the Management Board or to a designated Member of the Management Board. The Company has in place an audit committee.

The Company organisational chart is presented in section 2.1. of this report.

### IV. General Meeting, Shareholder Relations

#### IV.R.1.

*Companies should strive to hold an ordinary general meeting as soon as possible after the publication of an annual report and set the date in keeping with the applicable legislation.*

The Company convenes a general meeting and sets its date not only in keeping with the applicable legislation, but also strives to hold it as soon as possible after issuing a full-year report. In 2016, the Company convened the Annual General Meeting for June 6th 2016.

#### IV.R.2.

*If justified by the structure of shareholders or expectations of shareholders notified to the company, and if the company is in a position to provide the technical infrastructure necessary for a general meeting to proceed efficiently using electronic communication means, the company should enable its shareholders to participate in a general meeting using such means, in particular through:*

- 1) *real-time broadcast of a general meeting,*
- 2) *real-time bilateral communication where shareholders may take the floor during a general meeting from a location other than the venue of the general meeting,*
- 3) *exercise of the right to vote during a general meeting either in person or through a proxy.*

The Company does not apply the above recommendation. The Company's Articles of Association and the Rules of Procedure for the Company's General Meeting do not provide for real-time broadcasting of General Meetings. Also, the Company believes that the way General Meetings have been documented and carried out to date ensures transparency and safeguards the rights of all shareholders. Further, information on passed resolutions is published by the Company in the form of current reports, also on its website. Therefore, investors are able to review the matters discussed at General Meetings. However, the Company may apply this principle in the future. In the opinion of the Company's Management Board, the decision not to apply the abovementioned principle will not affect the reliability of the Company's information policy, nor will it hinder shareholders' participation in General Meetings.

#### IV.R.3.

*Where securities issued by a company are traded in different countries (or in different markets) and in different legal systems, the company should strive to ensure that corporate events related to the acquisition of rights by shareholders take place on the same dates in all the countries where such securities are traded.*

This recommendation does not apply to the Company. The Company shares are listed only on the main market of the Warsaw Stock Exchange.

### V. Conflict of Interest, Related Party Transactions

#### V.R.1.

*Members of the management board and the supervisory board should refrain from professional or other activities which might cause a conflict of interest or adversely affect their reputation as members of the governing bodies of the company, and where a conflict of interest arises, immediately disclose it.*

Members of the Management Board and the Supervisory Board declare that they refrain from professional or other activities which might cause a conflict of interest. Members of the Management Board and the Supervisory Board must notify the Management Board or the Supervisory Board,

respectively, of any conflict of interest which has arisen or may arise, and should refrain from voting on a resolution on a matter which may give rise to such a conflict of interest. Any conflicts of interest are immediately and thoroughly investigated.

## VI. Remuneration

### VI.R.1.

*The remuneration of members of the company's governing bodies and key managers should follow the approved remuneration policy.*

The remuneration of members of the Company's governing bodies and key managers follows the Company's remuneration policy.

For details on the Company's remuneration policy, see section 8.13 of this report.

### VI.R.2.

*The remuneration policy should be closely tied to the company's strategy, its short- and long-term goals, long-term interests and results, taking into account solutions necessary to avoid discrimination on whatever grounds.*

The Company's remuneration policy is closely tied to the Company's strategy, its goals, interests, and results.

For details on the Company's remuneration policy, see section 8.13 of this report.

### VI.R.3.

*If the supervisory board has a remuneration committee, principle II.Z.7 applies to its operations.*

This recommendation does not apply to the Company. The Company's Supervisory Board has no remuneration committee.

### VI.R.4.

*The remuneration of members of the management board and the supervisory board and key managers should be sufficient to attract, retain and motivate persons with skills necessary for proper management and supervision of the company. Remuneration should be adequate to the scope of tasks delegated to individuals, taking into account additional duties, for instance on supervisory board committees.*

The remuneration of members of the Company's Management Board, Supervisory Board, and key managers is sufficient to attract, retain and motivate persons with skills necessary for proper management and supervision of the Company, and the remuneration is adequate to the scope of tasks delegated to those individuals.

For details on the rules of remuneration of the Management Board and Supervisory Board members, see section 8.13 of this report.

### 8.3. Internal control and risk management systems

Organisational solutions have been put in place at the parent to ensure that risks involved in the preparation of financial statements are effectively and efficiently identified, managed, and eliminated. The solutions are based on the Company's regulations, organisational rules, document circulation procedures, as well as the scopes of powers and responsibilities of the finance and accounting staff. The Company applies documented accounting policies, which relate in particular to the chart of accounts, measurement of assets and liabilities, calculation of net profit or loss, maintenance of the accounting books, rules to be followed in inventory taking, as well as data and database protection systems.

Accounting books are maintained using SAP, an integrated IT system interoperating with other complementary systems. All systems in place are protected against unauthorised access with periodically changed passwords and function-based access control. Underlying source documents are inspected by organisational units responsible for their review based on the division of duties and authority. Before any accounting entries are made, documents are subject to a final review performed by the accounting and tax personnel.

The Group takes care to ensure that its financial statements are prepared properly, that is in compliance with applicable regulations setting forth the reporting rules and procedures, and in accordance with the principles of fairness and completeness. Data sourced from the accounting records is based on entries made on the basis of appropriate source documents, which are verified through an inventory-taking of assets and review of transactions and balances in individual accounts by dedicated inventory-taking and review teams.

Preparation of the financial statements is overseen by Head of the Corporate Finance Department, who supervises the financial and accounting functions responsible for reviewing and recording economic events in the Company's accounting books and generating the data necessary to prepare the financial statements.

The accounting policies meet the requirements set forth in the International Financial Reporting Standards/International Accounting Standards and the Polish Accountancy Act. The Company constantly monitors changes to the applicable financial reporting laws and regulations, and makes preparations sufficiently in advance to incorporate them into its rules and policies. Changes to accounting policies necessitated by amendments to accounting laws are made on an ongoing basis by the Company's Management Board.

Once prepared, the financial statements are presented by Head of the Corporate Finance Department to the Company's Management Board. In order to confirm that the data in the financial statements is correct and consistent with the records in the Company's accounting books, the financial statements are audited by an independent auditor, who issues an opinion on the financial statements. The auditor is selected by the Supervisory Board based on a recommendation issued by the Audit Committee (a standing committee of the Supervisory Board). As part of its activities, the Audit Committee monitors the financial reporting process, the effectiveness of internal control and risk management systems in place at the Company, the full-year separate and consolidated financial statements, as well as the work performed and reports prepared by a qualified auditor.

Financial statements adopted by the Management Board are subject to assessment by the Supervisory Board, which submits a written evaluation report to the General Meeting of Grupa Azoty.

The adopted procedures for the preparation of financial statements are intended to ensure accuracy of disclosures and their compliance with the law, and to guarantee that potential risks are identified and eliminated sufficiently in advance in order to obtain a reasonable assurance concerning the accuracy and fairness of the financial statements.

Grupa Azoty S.A. implemented the Enterprise Risk Management System based on ISO 31000 standard "Risk management principles and guidelines" and the "Enterprise Risk Management - Integrated Framework" standard developed by COSO. The "Group Enterprise Risk Management Policy" was adopted along with a range of procedures describing stages of the risk management process and detailed actions to take, which were also implemented by selected companies of the Group.

In accordance with the rules applicable at the Company, enterprise risk management consists of the following stages:

- risk identification and assessment,
- definition and implementation of risk response measures and incident management plans,
- monitoring and reporting of risk levels,
- use of information on risks in decision-making processes,
- reporting and communication,

- monitoring and evaluation of the risk management system.

Risk management is a process carried out by the Group's Corporate Centre. A Steering Committee was also established to support the process management. The Committee exchanges information, makes analyses and formulates opinions to support reaching viable solutions for the process. The Risk Management Steering Committee brings together representatives of the Group companies at which the risk management system was implemented.

The Company identifies and assesses the risks periodically, using the adopted risk model. Risk identification and assessment is performed by the respective risk owners. The assessment is performed based on a rating of the impact and likelihood of the risk occurrence adopted for a given year. Then risks are prioritised and key risks for the Company in a given period are identified. Outcomes of the process are also used to plan internal audits.

Results of periodical reviews of the risk register at individual companies are then used to prepare the Group's key risk list.

Risks are managed by the respective risk owners, who adopt risk management strategies, take day-to-day measures to analyse relevant risk factors and monitor their levels.

As a rule, once a year the parent prepares a periodic report on the enterprise risk management. The report contains a description of the key risks and information about the operation of the risk management function at the parent.

The operational risks are identified and steps are taken to mitigate their adverse effect. Internal audits of the management systems are among the tools applied by the Company to assess effectiveness of the risk mitigation measures undertaken in individual processes carried out at the Company.

## 8.4. Management standards and systems

### Management standards

The Group operates an Enterprise Management Policy. The policy defines the general plans and directions for the Group. The Enterprise Management Policy sets out the mission, vision and strategic objectives of the Group companies implemented based on management systems compliant with the highest international standards.

To accomplish this mission, the following strategic objectives have been set:

- to increase the scale of operations in core areas through organic growth, alliances and M&As, both in Poland and abroad,
- to advance integration within the Group to maximise operating synergies,
- to reduce the Group's sensitivity to energy costs through the use of technological and energy-efficient solutions,
- to reduce the Group's sensitivity to changing economic cycles and prices of natural gas and petrochemical commodities by extending product chains,
- to reduce production costs through upgrades of key production lines,
- to build stable and effective customer relations, increasing the brand awareness of leading products of the Group, and optimising product logistics and distribution,
- to improve the efficiency of key processes and of knowledge gathering and management,
- to continuously adapt product quality to customer requirements,
- to diversify horizontal, leveraging synergies with the existing product portfolio,
- to continuously improve products and services using innovative technologies.

The Group companies pursue strategic objectives based on management systems conforming to the highest international standards. Operating priorities, such as high quality, care for technical safety and environmental protection, energy efficiency, health safety of food, reducing environmental losses, giving priority to customers, are all efficiently monitored and ensure effective management. In its operations, the Group complies with all applicable laws and regulations and strives to constantly improve the results of its operations and minimise the associated risks.

### Management systems

The Group pursues a management policy which guarantees that strategic goals are achieved in reliance on an integrated management system consistent with international standards.

The operating priorities: high quality and care for technical safety and the environment, are all efficiently monitored and facilitate effective management. The Integrated Management System is structured around the following principles: giving priority to customers, reducing environmental losses and mitigating the risk of hazards, and continuous improvement.



The parent has implemented:

- Quality Management System compliant with the ISO 9001:2008 standard,
- Environmental Management System compliant with the ISO 14001:2004 standard,
- Occupational Health and Safety Management System compliant with the PN-N-18001:2004 and BS OHSAS 18001:2007 standards,
- Food Safety Management System compliant with the ISO 22000:2005 standard,
- PN-EN ISO/IEC 17025:2005 Management System (general requirements for the competence of testing and calibration laboratories),
- Automotive Industry Quality Management Standard implemented in accordance with the ISO/TS 16949:2009 standard,
- Management Standard compliant with the Fertilizers Europe Product Stewardship Standard,
- Enterprise Risk Management System based on ISO 31000 standard "Risk management principles and guidelines" and the "Enterprise Risk Management - Integrated Framework" standard developed by COSO,
- Energy Management System compliant with the ISO 50001:2011 standard.

In the reporting period, the Group companies maintained and improved their management systems. The validity of certificates confirming the systems' compliance with relevant standards and requirements was maintained. Improvements were also made based on findings of external and internal audits of the certified management systems, and conclusions of the Management Review. The Group appointed a Management Systems Integration Team to integrate its management systems, to continuously monitor changes of the standards, and to take adaptive measures to ensure that the Group's management systems compliant with the ISO 9001:2015 and the ISO 14001:2015 standards are certification-ready.

In the reporting period, the Group continued efforts to implement an ISO 50001-compliant energy management system.

## 8.5. Shareholding structure

Shareholding structure as at January 1st 2016 (in accordance with the information provided in the full-year report for 2015)

Shareholder	Number of shares	Ownership interest (%)	Number of votes	% of voting rights
State Treasury of Poland	32,734,509	33.00	32,734,509	33.00
ING OFE	9,883,323	9.96	9,883,323	9.96
Norica Holding S.à r.l. (indirectly: 19,841,700 shares, i.e. 20.0026%)	571,348	0.57	571,348	0.57
Rainbee Holdings Limited*)	9,820,352	9.90	9,820,352	9.90
Opansa Enterprises Limited*)	9,450,000	9.53	9,450,000	9.53
TFI PZU S.A.	8,530,189	8.60	8,530,189	8.60
EBRD	5,700,000	5.75	5,700,000	5.75
Other	22,505,763	22.69	22,505,763	22.69
	<b>99,195,484</b>	<b>100.00</b>	<b>99,195,484</b>	<b>100.00</b>

\*) Direct subsidiaries of Norica Holding S.à r.l.

On May 23rd 2016, the parent's Management Board received a notification from Norica Holding S.à r.l., of Luxembourg ("Norica"), given under Art. 69.1.2 and Art. 87.5.1 of the Act on public offering, conditions governing the introduction of financial instruments to organised trading, and public companies, dated July 29th 2005 (the "Public Offering Act").

Following the execution of a share sale agreement by Norica, on May 19th 2016 Norica directly and indirectly (through its subsidiaries) reduced its share in total voting rights at the parent's General Meeting. As a result, Norica holds (directly and indirectly through its subsidiaries) approximately 19.70% of total voting rights at the parent's General Meeting.

Transaction details were presented by the parent in Current Report No. 30/2016 of May 24th 2016.

Shareholding structure as at May 23rd 2016

Shareholder	Number of shares	Ownership interest (%)	Number of votes	% of voting rights
State Treasury	32,734,509	33.00	32,734,509	33.00
ING OFE	9,883,323	9.96	9,883,323	9.96
Norica Holding S.à r.l. (indirectly: 19,541,700 shares, i.e. 19.7002%)	271,348	0.27	271,348	0.27
Rainbee Holdings Limited*)	9,820,352	9.90	9,820,352	9.90
Opansa Enterprises Limited*)	9,450,000	9.53	9,450,000	9.53
TFI PZU S.A.	8,530,189	8.60	8,530,189	8.60
EBRD	5,700,000	5.75	5,700,000	5.75
Other	22,805,763	22.99	22,805,763	22.99
<b>Total</b>	<b>99,195,484</b>	<b>100.00</b>	<b>99,195,484</b>	<b>100.00</b>

\*) Direct subsidiaries of Norica Holding S.à r.l.

On June 9th 2016, the parent's Management Board received a notification from proxies to escrow accounts of Norica's subsidiaries - Opansa Enterprises Limited and Rainbee Holdings Limited, pursuant to Art. 69.1.1 in conjunction with Art. 87.1.7 of the Public Offering Act.

According to the notification, Opansa Enterprises Limited of Nicosia, Norica's subsidiary, reduced its share in total voting rights at the parent's General Meeting from 9.53% to 9.50%. Thus, Norica (directly and indirectly through its subsidiaries) reduced its share in total voting rights at the parent's general meeting from approximately 19.70% to 19.68% of total voting rights at the parent's General Meeting. Full contents of the notification were published by the parent in Current Reports No. 38/2016 and No. 39/2016 of June 9th 2016.

#### Shareholding structure as at June 9th 2016

Shareholder	Number of shares	Ownership interest (%)	Number of votes	% of voting rights
State Treasury	32,734,509	33.00	32,734,509	33.00
ING OFE	9,883,323	9.96	9,883,323	9.96
Norica Holding S.à r.l. (indirectly: 19,521,700 shares, i.e. 19.68%)	271,348	0.27	271,348	0.27
Rainbee Holdings Limited*)	9,820,352	9.90	9,820,352	9.90
Opansa Enterprises Limited*)	9,430,000	9.50	9,430,000	9.50
TFI PZU S.A.	8,530,189	8.60	8,530,189	8.60
European Bank for Reconstruction and Development	5,700,000	5.75	5,700,000	5.75
Other	22,825,763	23.02	22,825,763	23.02
<b>Total</b>	<b>99,195,484</b>	<b>100.00</b>	<b>99,195,484</b>	<b>100.00</b>

\*) Direct subsidiaries of Norica Holding S.à r.l.

On June 10th 2016, the parent's Management Board received a notification from Norica, prepared pursuant to Art. 69.1.2, Art. 69a.3 and Art. 87.5.1 of the Public Offering Act.

According to the notification, following the execution of three intra-group transactions on June 8th, resulting in the disposal, directly and indirectly, of shares in the parent, Norica reduced (directly and indirectly through its subsidiaries) its share in total voting rights at the parent's General Meeting from 19.68% to approximately 19.47%.

Transaction details were presented by the parent in Current Report No. 40/2016 of June 10th 2016.

#### Shareholding structure as at June 10th 2016

Shareholder	Number of shares	Ownership interest (%)	Number of votes	% of voting rights
State Treasury of Poland	32,734,509	33.00	32,734,509	33.00
ING OFE	9,883,323	9.96	9,883,323	9.96
Norica Holding S.à r.l. (indirectly: 19,321,700 shares, i.e. 19.47%)	71,348	0.072	71,348	0.072
Rainbee Holdings Limited*)	9,820,352	9.90	9,820,352	9.90
Opansa Enterprises Limited*)	9,430,000	9.50	9,430,000	9.50
TFI PZU S.A.	8,530,189	8.60	8,530,189	8.60
EBRD	5,700,000	5.75	5,700,000	5.75
Other	23,025,763	23.22	23,025,763	23.22
<b>Total</b>	<b>99,195,484</b>	<b>100.00</b>	<b>99,195,484</b>	<b>100.00</b>

\*) Direct subsidiaries of Norica Holding S.à r.l.

In the period from June 10th 2016 to the date of this report, the parent was not officially notified of any changes in the large holdings of its shares.

## **8.6. Special control powers of security holders**

Pursuant to Art. 16.2 of the parent's Articles of Association, the State Treasury of Poland, as a shareholder, has an individual right to appoint and remove one member of the Supervisory Board. Furthermore, in accordance with Art. 43.1.3 and 43.1.4 of the parent's Articles of Association, the General Meeting is convened by the Management Board:

- at the request of a shareholder or shareholders representing at least one-twentieth of the share capital, submitted in writing or in electronic form at least one month before the proposed date of the General Meeting,
- at the request of the State Treasury as a shareholder, irrespective of its interest in the Company's share capital, submitted in writing at least one month before the proposed date of the General Meeting.

Pursuant to Art. 45.4 of the parent's Articles of Association governing the placing of matters on the agenda of the next General Meeting by shareholders, a shareholder or shareholders representing at least one-twentieth of the Company's share capital may request that certain matters be placed on the agenda of the next General Meeting. The same right is held by the State Treasury as the Company's shareholder, irrespective of its interest in the share capital.

Pursuant to Art. 45.8 of the parent's Articles of Association, prior to the date of the General Meeting, a shareholder or shareholders representing at least one-twentieth of the Company's share capital may submit to the Company draft resolutions on the matters included or to be included in the agenda of the General Meeting, in writing or with the use of electronic means of communication. The Company promptly publishes such draft resolutions on its website.

## **8.7. Restrictions on voting rights**

In accordance with Art. 47.2 of the parent's Articles of Association, each share carries one vote at the General Meeting.

On March 15th 2013, the parent's Extraordinary General Meeting passed Resolution No. 9 to amend the Articles of Association by changing the individual rights of certain shareholders by amending Art. 47.3 to read as follows:

"Art. 47.3. As long as the State Treasury of Poland or its subsidiaries hold shares in the Company carrying at least one fifth of the total voting rights, the other shareholders' voting rights will be limited in such a manner that no shareholder may exercise more than one fifth of total voting rights at the General Meeting existing on the day of the General Meeting. The limitation on the voting rights referred to in the preceding sentence shall not apply to the State Treasury or any of its subsidiaries. For the purposes of this Art. 47.3, the exercise of voting rights by a subsidiary shall be deemed the exercise of voting rights by its parent as defined in the Act on public offering, conditions governing the introduction of financial instruments to organised trading, and public companies of July 29th 2005 (the "Public Offering Act"), and the terms "parent" and "subsidiary" shall include any entity whose voting rights attached to shares held, directly or indirectly, in the Company are aggregated with the voting rights of another entity or entities, in accordance with the Public Offering Act, in connection with the holding, disposal or acquisition of major holdings in the Company. A shareholder whose voting rights are subject to the limitation shall in any case retain the right to cast at least one vote."

## **8.8. Restrictions on the transferability of securities**

There are no restrictions on the transferability of the parent's securities.

## **8.9. Rules governing appointment and removal of the management staff; powers of the management staff, including in particular the authority to resolve to issue or buy back shares**

### **Rules governing appointment and removal of the management staff**

#### **Management Board**

In accordance with Art. 23.1 of the parent's Articles of Association, the parent's Management Board consists of no more than seven persons, including President, Vice Presidents and other members. The number of Management Board members is defined by the governing body that appoints the

Management Board. Members of the Management Board are appointed for a joint three-year term of office.

Pursuant to Art. 24 of the parent's Articles of Association, any or all members of the Management Board are appointed and removed by the Supervisory Board, subject to the provisions of Art. 25 et seq. of the Articles of Association.

Any member of the Management Board may be removed or suspended from duties by the Supervisory Board or the General Meeting. (Art. 24.2 of the parent's Articles of Association).

As long as the parent employs an annual average of above 500 employees, the Supervisory Board appoints one person elected by the parent's employees to the Management Board, for the Management Board's term of office (Art. 25.1 of the parent's Articles of Association).

The Supervisory Board has the right to remove and suspend from duties any or all members of the Management Board, for a good reason, and to delegate members of the Supervisory Board, for no longer than three months, to temporarily perform the duties of members of the Management Board who were removed from office, tendered their resignation or for any other reason are unable to perform the duties (Art. 33.1 of the parent's Articles of Association).

### **Supervisory Board**

Pursuant to Art. 35.1 of the parent's Articles of Association, the Supervisory Board is composed of five to nine members, appointed by the General Meeting, subject to the provisions of Art. 16.2 ("The State Treasury has an individual right to appoint and remove one member of the Supervisory Board.") and Art. 36 of the Articles of Association ("Part of the Supervisory Board members shall be members elected by Company employees pursuant to Art. 14 of the Act on Commercialisation and Privatisation").

Members of the Supervisory Board are appointed for a joint three-year term of office.

At least two members of the Supervisory Board should be independent members that meet the independence criteria set out in Annex II to the Commission Recommendation on the role of non-executive or supervisory directors (Art. 35.4 of the parent's Articles of Association).

The General Meeting appoints the Chairperson of the Supervisory Board.

The Deputy Chairperson and the Secretary are elected by the Supervisory Board, at its first meeting, from among its members (Art. 37.1 of the parent's Articles of Association).

### **Power to make decisions to issue or buy back shares**

Pursuant to Art. 10.1 of the parent's Articles of Association, the parent's share capital may be increased by way of a resolution of the General Meeting by issuing new shares or increasing the value of the existing shares. Pursuant to Art. 10.3 of the Articles of Association:

"3. The Management Board is authorised to increase the Company's share capital by issuing new shares with a total par value of up to PLN 240,432,915, by way of an increase in the share capital within the limits defined above ("Authorised Share Capital"). An increase in the share capital within the limits of the Authorised Share Capital may be effected only for the purpose and on the terms and conditions stipulated in Art 10.4 4 below. The Management Board's authorisation to increase the share capital and to issue new shares within the limits of the Authorised Share Capital shall expire within six months from the date of registration of amendments to the Articles of Association stipulating the Authorised Share Capital.

4. Within the limits of the Authorised Share Capital, the Management Board shall be authorised to offer Company shares, with the existing shareholders' pre-emptive rights waived, only to the shareholders of Zakłady Azotowe Puławy S.A. of Puławy, entered in the Business Register of the National Court Register under entry No. KRS 0000011737 ("ZA Puławy"), in exchange for a non-cash contribution in the form of shares in ZA PUŁAWY, so that one share in ZA PUŁAWY shall be deemed a non-cash contribution to cover 2.5 Company shares issued within the limits of the Authorised Share Capital. A Management Board's resolution to issue shares in exchange for a non-cash contribution in the form of shares in ZA PUŁAWY shall not require approval by the Supervisory Board.

5. In the Company's interest the Management Board is authorised to waive, in whole or in part, the existing shareholders' pre-emptive rights to acquire shares issued within the limits of the Authorised Share Capital only to offer such shares to the shareholders of ZA PUŁAWY in accordance with the rules described in Art. 10.4 above.

6. Unless stipulated otherwise in Art. 10.7 or in the Commercial Companies Code, the Management Board shall decide on all matters connected with a share capital increase within the limits of the authorised share capital; in particular the Management Board is authorised to:

1) enter into agreements providing for the arrangement and the carrying out of a share issue,

2) adopt resolutions and take other actions regarding conversion of the shares and allotment certificates into book-entry form as well as to enter into agreements with the CSDP on the registration of the shares and allotment certificates,

3) adopt resolutions and take other actions regarding the issue of shares by way of a public offering or seeking admission of the shares and allotment certificates to trading on the regulated market, as the case may be.

7. A Management Board resolution on:

1) share capital increase within the limits of the Authorised Share Capital,

2) determination of the issue price for shares issued within the limits of the Authorised Share Capital, and

3) waiver of pre-emptive rights,

shall require approval by the Supervisory Board.”

## **8.10. Rules governing amendments to the parent's Articles of Association**

Pursuant to Art. 51.22 of the parent's Articles of Association, the General Meeting has exclusive authority to amend the parent's Articles of Association or change the parent's business profile.

## **8.11. Operation of the General Meeting**

The General Meeting is convened and prepared in accordance with the Commercial Companies Code, the parent's Articles of Association and the Rules of Procedure for the General Meeting.

The Rules of Procedure for the General Meeting, adopted by way of a resolution of the General Meeting of June 26th 2009, define the rules for holding the meetings.

### **Powers of the General Meeting**

The powers of the General Meeting are defined in the Commercial Companies Code and Art. 51 of the parent's Articles of Association.

In particular, the General Meeting has the authority to:

- review and approve the Directors' Report on the parent's operations, the financial statements for the previous financial year, the consolidated financial statements and the Directors' Report on the Group's operations, if prepared by the parent, as well as the annual written report of the Supervisory Board, and to grant discharge to members of the parent's governing bodies in respect of their duties,
- adopt resolutions on distribution of profit or coverage of loss,
- adopt the Rules of Procedure for the General Meeting,
- amend the parent's Articles of Association,
- change the parent's business profile,
- approve the disposal or lease of, or creation of limited property rights in, the Company's business or its organised part,
- appoint and remove members of the Supervisory Board (subject to Art.16.2 and Art. 36 of the Articles of Association), and determine the remuneration amounts for members of the Supervisory Board,
- increase or decrease the Company's share capital,
- adopt resolutions on issue of notes, including notes convertible into shares,
- merge, demerge and transform the parent,
- dissolve and liquidate the parent,
- approve buyback of Parent shares for retirement and define the conditions for share retirement,
- adopt other resolutions as provided for in applicable laws or the Articles of Association.

### **Shareholder rights and their exercise**

Shareholder rights are defined in detail in the Commercial Companies Code, the Act on Trading in Financial Instruments, the Public Offering Act and the parent's Articles of Association.

## 8.12. Composition and operation of the Company's management and supervisory bodies

### Parent's Management Board

As at January 1st 2016, the composition of the Company's Management Board was as follows:

- Paweł Jarczewski - President of the Management Board,
- Krzysztof Jałosiński - Vice President of the Management Board,
- Marek Kapłucha - Vice President of the Management Board,
- Marian Rybak - Vice President of the Management Board,
- Andrzej Skolmowski - Vice President of the Management Board,
- Witold Szczypiński - Vice President of the Management Board,
- Artur Kopec - Member of the Management Board elected by employees.

At its meeting held on February 19th 2016, the Company's Supervisory Board passed a resolution whereby the Management Board of the tenth term of office is to be composed of three to seven members, and resolutions on the following matters:

- to remove Paweł Jarczewski, President of the Management Board,
- to remove Krzysztof Jałosiński, Vice President of the Management Board,
- to remove Marek Kapłucha, Vice President of the Management Board,
- to remove Marian Rybak, Vice President of the Management Board,
- to appoint Mariusz Bober as President of the Management Board of Grupa Azoty S.A. of the tenth term of office.

On March 14th 2016, the Supervisory Board passed resolutions to appoint Józef Rojek and Tomasz Hinc as members of the Management Board.

On May 20th 2016, the Supervisory Board passed resolutions on the following matters:

- to remove Andrzej Skolmowski, Vice President of the Management Board,
- to appoint Tomasz Hinc and Józef Rojek as Vice Presidents of the Management Board,
- to appoint Paweł Łapiński as Vice President of the Management Board.

As a result of the above changes, in the period from May 20th 2016 to December 15th 2016, the composition of the Company's Management Board was as follows:

- Mariusz Bober - President of the Management Board,
- Witold Szczypiński - Vice President of the Management Board,
- Paweł Łapiński - Vice President of the Management Board,
- Józef Rojek - Vice President of the Management Board,
- Tomasz Hinc - Vice President of the Management Board,
- Artur Kopec - Member of the Management Board.

On December 16th 2016, the Supervisory Board passed resolutions on the following matters:

- to remove Mariusz Bober, President of the Management Board,
- to appoint Wojciech Wardacki as President of the Management Board.

As a result of the above changes, since December 16th 2016, the composition of the Company's Management Board has been as follows:

- Wojciech Wardacki - President of the Management Board,
- Witold Szczypiński - Vice President of the Management Board,
- Paweł Łapiński - Vice President of the Management Board,
- Józef Rojek - Vice President of the Management Board,
- Tomasz Hinc - Vice President of the Management Board,
- Artur Kopec - Member of the Management Board.

### Curriculum vitae of Management Board members

#### ***Wojciech Wardacki - President of the Management Board***

Appointed President of the Company's Management Board of the tenth term of office under the Supervisory Board's resolution of December 16th 2016.

Education:  
Doctor of Economics.

Professional experience:

1983 - 1995:	Assistant Lecturer and Assistant Professor in the Transport Economics Institute of Szczecin University (until August 31st 1985: Szczecin University of Technology)
1989 - 1990:	Researcher, DAAD visiting fellow in the Transportation Institute of the University of Cologne, Germany
1991 - 1993:	Member of the Lower Chamber of the Polish Parliament
1994 - 1996:	Sole proprietorship, owner of Pracownia Analiz i Badań Marketingowych of Szczecin, a marketing research company
1995 - 1996:	Lecturer in the School of Public Administration in Szczecin
1996 - April 30th 2005:	Head of Administration and Economic Affairs, Chief Financial Officer, and member of the management board of Goleniowskie Fabryki Mebli Kollektion WIM Sp. z o.o.
May 4th- October 2nd 2005:	Member of the Management Board for Restructuring at Zakłady Chemiczne Zachem S.A.
October 3rd 2005- August 1st 2006:	President of the management board and Chief Executive Officer of Zakłady Chemiczne Zachem S.A.
August 2nd 2006 - October 31st 2008:	Member of the management board of Ciech S.A.
2010-2014:	Sole proprietorship, business consultancy and lobbying
Since April 2016:	President of the management board and Chief Executive Officer of Grupa Azoty Zakłady Chemiczne Police S.A.
Since December 2016:	President of the Management Board of Grupa Azoty S.A.

Other professional experience:

1997 - 1998:	Secretary to the Team of Advisors to President of the management board of Polskie Koleje Państwowe S.A. responsible for the assessment of restructuring programmes
1998:	Chairman of the supervisory board of Polskie Koleje Państwowe S.A.
1999 - 2000:	Member of the supervisory board of Polskie Koleje Państwowe S.A.
2005 - 2008:	Chairman and member of the supervisory board of Transclean Sp. z o.o.
2006 - 2008:	Chairman of the supervisory board of Janikosoda S.A.
2006 - 2008:	Deputy Chairman of the supervisory board of Soda Mątwy S.A.
2006 - 2008:	Member of the supervisory board of Gdańskie Zakłady Nawozów Fosforowych sp. z o.o.
2007 - 2008:	Chairman of the supervisory board of Zakłady Chemiczne Zachem S.A.
Since February 15th 2016:	Chairman of the supervisory board of Bank Ochrony Środowiska S.A.
March 1st 2016 - March 30th 2016:	Member of the supervisory board of Grupa Azoty Zakłady Chemiczne Police S.A.
Since February 3rd 2017:	Chairman of the Council of the Polish Chamber of Chemical Industry

**Witold Szczypiński - Vice President of the Management Board, Director General**

Appointed Vice President of the Company's Management Board of the tenth term of office under the Supervisory Board's resolution of January 9th 2015. With effect from March 2014 appointed Director General of Grupa Azoty S.A. of Tarnów.

Previously held positions at the parent: Vice President of the Management Board of the ninth term of office under the Supervisory Board's resolution of October 20th 2011, Vice President of the Management Board of the eighth term of office under the Supervisory Board's resolution of March 18th 2011, Vice President of the Management Board of the seventh term of office under the Supervisory Board's resolution of June 11th 2008, Vice President of the Management Board of the sixth term of office under the Supervisory Board's resolution of March 11th 2008.



**Education:**

Graduate of the Production Organisation Faculty of the Silesian University of Technology. Completed studies in industry organisation and management (specialisation: chemical industry), MSc (Eng) in industry organisation.

**Training and courses:**

Training course for candidates to supervisory boards, course for members of management bodies based on the course for candidates to supervisory boards, BEST MANAGER series of seminars preparing managers for ownership transformations.

Specialist courses on work organisation, process safety, and investment projects.

**Professional experience:**

1979-1987	Foreman, Process Engineer and Senior Process Engineer at the Synthesis Plant of Zakłady Azotowe im. F. Dzierżyńskiego w Tarnowie (later renamed Zakłady Azotowe w Tarnowie-Mościcach S.A.)
1987-1990	Manager of Silicon Department at the Synthesis Plant of Zakłady Azotowe w Tarnowie-Mościcach S.A.,
1991-1999	Manager of the Synthesis Plant of Zakłady Azotowe w Tarnowie-Mościcach S.A.
1999-2001	Director of Plastics Centre of Zakłady Azotowe w Tarnowie-Mościcach S.A.
2002-2007	Director responsible for Technology and Development at Zakłady Azotowe w Tarnowie-Mościcach S.A.,
2007-2008	Member of the management board of Zakłady Azotowe w Tarnowie-Mościcach S.A.
2008	Acting President of the management board of Zakłady Azotowe w Tarnowie-Mościcach S.A.
Since 2008:	Vice President of the management board of Zakłady Azotowe w Tarnowie-Mościcach S.A. (at present Grupa Azoty S.A.)

Represented Zakłady Azotowe w Tarnowie-Mościcach S.A. (at present Grupa Azoty S.A.) on supervisory boards of: Przedsiębiorstwo Innowacyjno-Wdrożeniowe UNISIL Sp. z o.o. (1997-1999), Tarnowskie Wodociągi Sp. z o.o. (2007-2008), Biuro Projektów Zakładów Azotowych "BIPROZAT" Sp. z o.o. and Grupa Azoty PKCh Sp. z o.o. (2008-2016), Grupa Azoty ATT Polymers GmbH (2011-2013 and since 2015), Grupa Azoty ZAK S.A. (2012-2016), Grupa Azoty "Siarkopol" S.A. (2013-2016).

**Additional information:**

- Member of the Chemical and Process Engineering Committee of the Polish Academy of Sciences (2011-2015),
- Member of the Steering Committee of the 'Advanced power generation technologies', a strategic scientific research and development programme of the National Centre for Research and Development (2012-2015)
- Member of the Scientific Board of the Blachownia Institute of Heavy Organic Synthesis of Kędzierzyn-Koźle (2011-2015)
- Chairman of the management board of SITPChem Branch of Tarnów (2007-2010)
- Author and co-author of nearly 40 implemented specialist improvement concepts (including six patent protected) for the manufacturing of ammonia, hydrogen, food-grade carbon dioxide, polyoxymethylene, polycrystalline silicon and catalysts; and for energy infrastructure.

***Paweł Łapiński – Vice President of the Management Board***

Appointed Vice President of the Company's Management Board of the tenth term of office under the Supervisory Board's resolution of May 20th 2016.

**Education:**

- Graduate of the Management and Marketing Department of the Faculty of Economic Sciences and Management of the Nicolaus Copernicus University in Toruń (major in manufacturing process management and industrial enterprise management).
- Completed a post-graduate course in commercial law at the Nicolaus Copernicus University in Toruń.
- Completed a post-graduate course in value based management, business psychology and negotiation at the Warsaw School of Economics.

**Training and courses:**

Various courses in management, finance, taxes, cost analysis and subjects related to the power industry.

**Professional experience:**

1997-2007	Boryszew S.A., Elana Branch in Toruń (last position held: Deputy Managing Director, Economic Director)
2005-2007	Elana-Energetyka Sp. z o.o. (last position held: Vice President of the management board, Economic and Finance Director),
2007-2016	Struga S.A. (President of the management board)

**Other:**

2006-2007	Chairman of the supervisory board of ELANA-PET Sp. z o.o.
2008-2013	Chairman of the supervisory board of BUMAR-HYDROMA S.A.
2013-2016	Chairman of the supervisory board of VEROBUD S.A.

***Józef Rojek - Vice President of the Management Board***

Appointed Vice President of the Company's Management Board of the tenth term of office under the Supervisory Board's resolution of May 20th 2016.

**Education:**

- Post-secondary course in I&C and automation in the chemical industry (5 semesters),
- Kraków University of Technology – Faculty of Mechanical Engineering, major: construction of equipment used in chemical and food industries (10 semesters),
- Małopolska School of Economics in Tarnów, specialisation: management and marketing.

**Professional experience:**

1968-1969	Gminna Spółdzielnia Samopomoc Chłopska of Ropczyce (farmers communal cooperative)
1972-1985	Zakłady Azotowe w Tarnowie
1985	Wojewódzki Związek Spółdzielni Rolniczych (association of agricultural cooperatives)
1985-1986	Management board of Spółdzielnia Transportu Wiejskiego (rural transport cooperative)
1986-1987	Spółdzielnia Transportu Wiejskiego in Dąbrowa Tarnowska
1987-1994	Zakłady Azotowe w Tarnowie
1994-1998	Chief Designer at Biuro Projektów Zakładów Azotowych Biprozat Tarnów Sp. z o.o.
1994-2005	Member of the Tarnów City Council
1998-2002	Mayor of Tarnów
2002-2005	Chief Specialist at Biuro Projektów Zakładów Azotowych Biprozat Tarnów Sp. z o.o.
2003-2004	Member of the supervisory board of Biuro Projektów Zakładów Azotowych Biprozat Tarnów Sp. z o.o.
2005-2006	Member of the Sejm (lower chamber of the Polish Parliament) – member of the State Treasury Committee and the Environmental Protection, Natural Resources and Forestry Committee
2006-2007	Adviser to Director General of Zakłady Azotowe w Tarnowie-Mościcach S.A.
2006-2007	Member of the supervisory board of Przedsiębiorstwo Uzdrowiskowe Ustroń S.A. of Ustroń
2006-2007	Member of the Social Council at Mościckie Centrum Medyczne Samodzielny SPZOZ (public medical centre in Mościce)
2007-2015	Member of the Sejm (2007–2015: member of the State Treasury Committee, 2008–2009: member of the Justice and Human Rights Committee, 2009–2011: member of the Physical Culture, Sports and Tourism Committee, 2015: member of the Petitions Committee)

***Tomasz Hinc - Vice President of the Management Board***

Appointed Vice President of the Company's Management Board of the tenth term of office under the Supervisory Board's resolution of May 20th 2016.

**Education:**

Graduate of the University of Szczecin.

Professional experience:

- 1997–2007 – University teacher at schools of higher education in Szczecin, lecturing on organisation and management, human resources management, sociology and public relations
- Since 2007 – Adviser to the management board of Totalizator Sportowy Sp. z o.o. of Warsaw and then Head of the Szczecin Branch; 2008 – acting Head of the Zielona Góra Branch; from 2013 also Head of the Koszalin Branch
- Since 2006 – Member of the Szczecin City Council in three consecutive terms; since 2014 Deputy Chair of the Council
- Since 2015 – Representative of Szczecin in the Pomerania Euroregion Council
- 2013–2015 – Member of the Szczecin Council of Public Benefit Activities
- 2007–2014 – Member of the Security and Order Committee of the Mayor of Szczecin
- Since 2003 – Member of the Social Council of the Regional Oncology Hospital in Szczecin of the Zachodniopomorskie Oncology Centre

**Artur Kopeć - Member of the Management Board**

Appointed member of the Company's Management Board of the tenth term of office nominated by Grupa Azoty S.A. employees, under the Supervisory Board's resolution of February 26th 2015.

Prior to the appointment: Member of the Company's Management Board of the ninth term of office nominated by Grupa Azoty S.A. employees under the Supervisory Board's resolution of February 17th 2012.

Education:

- Graduate of the Chemical Technology Faculty of Wrocław University of Technology (2002),
- Completed postgraduate course in entrepreneurship at Cracow University of Economics,
- Completed managerial course organised by Rudzka Agencja Rozwoju and Training Partners.

Training and courses:

Completed a number of training courses in management, health and safety, ISO and environmental protection.

In 2010 completed a course for members of supervisory boards of state-owned companies.

Professional experience:

- 2003 – employment with State Vocational School of Tarnów
- Since October 1st 2003 employed by Zakłady Azotowe w Tarnowie-Mościcach (now Grupa Azoty S.A.) in the following positions:
  - technician at the Department of Ammonia (2003–2005),
  - shift master at the Department of Catalysts (August–November 2005),
  - ammonia synthesis technician at the Fertilizers Centre (2006–2009),
  - fertilizer specialist technologist and engineer supervising the construction of Mechanical Fertilizer Granulation Unit (2006–2009),
  - testing and commissioning manager at the Mechanical Fertilizer Granulation Unit (2008–2009),
  - ammonia and hydrogen management specialist at the Ammonia Department (2010–2011),
  - since 2011 – head of the Ammonia Department and commissioning manager at the hydrogen production unit,
  - since February 2012 – Member of the Management Board of Grupa Azoty S.A.

Additional information:

- Since 2006 - member of the Polish Association of Chemical Engineers,
- In 2013–2014 - Deputy Chairman of the supervisory board of ŻSSA Unia Tarnów.
- Major professional accomplishments included successful launch of production of Saletrosan, a new fertilizer. Co-authored of the "Process of preparation of ammonium nitrate-sulfate" invention filed in European and Polish patent applications, and a number of improvement concepts.
- Major accomplishments on the Management Board include:
  - contribution to work on consolidation of the Polish chemical industry,
  - negotiation of social packages at the Puławy and Grzybowo plants,
  - integration of occupational health and safety, environmental protection and fire protection functions,
  - establishment of the Fire Protection Team (ZOP),
  - establishment of the Grupa Azoty Rescue Education Centre (CERGA),

- significant reduction of the accident rate at the Group,
- implementation of DuPont's STOP™ programme.

### **Powers and responsibilities of the Management Board members**

A detailed division of powers and responsibilities of the Management Board members is defined in a separate resolution of the Management Board.

Based on Resolution No. 271/X/2016 of February 23rd 2016, the division of powers and responsibilities within the Management Board members is as follows:

- Mariusz Bober - President of the Management Board, responsible for managing and coordinating the work of the Management Board and the Grupa Azoty Council, overseeing the implementation of the Company's and the Group's strategies, supervising the Agro Business Centre; also responsible for the information policy, HR policy, internal audit functions, risk management, and management of structural and ownership changes at the Group,
- Andrzej Skolmowski - Vice President of the Management Board, responsible for finance, accounting and IT, oversight of investor relations; liaising with the Vice President in charge of integration of production processes, plastics and organic synthesis, with the Management Board member in charge of social dialogue, plant safety and environmental protection, and with the Managing Director in respect of the Company's day-to-day operational management; also responsible for developing and implementing the logistics strategy, managing the supply logistics for raw materials, intermediate materials and finished products, and for developing and implementing the procurement strategy,
- Witold Szczypiński - Vice President of the Management Board, Director General of the Company, responsible for strategy and development, integration of production processes, plastics and organic synthesis, strategic feedstock procurement, developing and implementing the Company's and the Group's strategies, overseeing strategic procurement at the Company and the Group; also liaising with the Vice President in charge of integration of production processes, plastics and organic synthesis, with the Management Board member in charge of social dialogue, plant safety and environmental protection, and with the Managing Director with respect to management of the Company,
- Artur Kopeć - Member of the Management Board, responsible for project execution, social dialogue, plant safety and environmental protection; also liaising with the Vice President in charge of integration of production processes, plastics and organic synthesis, with the Vice President in charge of finance and with the Managing Director with respect to management of the Company.

Following the changes in the composition of the Management Board, at its meeting held on March 21st 2016 the Management Board passed Resolution No. 291/X/2016, under which the division of powers and responsibilities among the Management Board members was as follows:

- Mariusz Bober - President of the Management Board, responsible for overall supervision and management of the Group, as well as for the strategy and corporate governance, including exercise of majority shareholder power, human resources management, communication and corporate image (which also covers public relations and CSR),
- Andrzej Skolmowski - Vice President of the Management Board, responsible for finance, IT, logistics and investor relations,
- Witold Szczypiński - Vice President of the Management Board, Director General of the parent, responsible for integration of production processes, the Agro Segment, and the Plastics Segment,
- Tomasz Hinc - Member of the Management Board, responsible for procurement,
- Artur Kopeć - Member of the Management Board, responsible for production assets, plant safety, environmental protection, infrastructure and social dialogue,
- Józef Rojek - Member of the Management Board, responsible for investment projects and for R&D programmes.

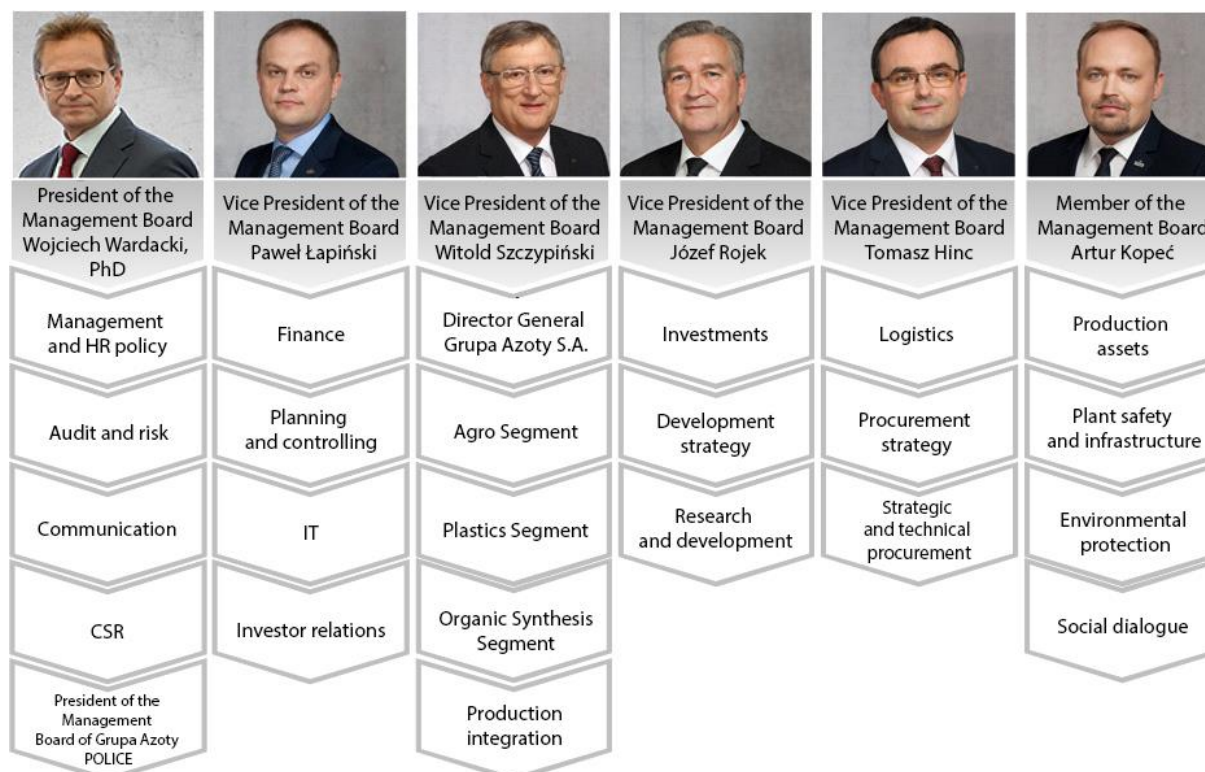
On May 24th 2016, the Management Board passed Resolution No. 358/X/2016, under which the division of powers and responsibilities between the Management Board members was as follows:

- Mariusz Bober - President of the Management Board, responsible for overall supervision and management of the Group, as well as for the strategy and corporate governance, including exercise of majority shareholder power, human resources management, communication and corporate image (which also covers public relations and CSR),
- Witold Szczypiński - Vice President of the Management Board, Director General of the parent, responsible for integration of production processes, the Agro Segment, and the Plastics Segment,

- Tomasz Hinc - Vice President of the Management Board, responsible for procurement and logistics,
- Paweł Łapiński - Vice President of the Management Board, responsible for finance, controlling, IT and investor relations,
- Józef Rojek - Vice President of the Management Board, responsible for investment projects and for R&D programmes,
- Artur Kopeć - Member of the Management Board, responsible for production assets, plant safety, environmental protection, infrastructure and social dialogue.

On the date of his appointment to the Company's Management Board (December 16th 2016), Dr. Wojciech Wardacki, President of the Management Board, took over the duties and responsibilities of the previous President, Mariusz Bober.

#### Division of duties and responsibilities among Management Board members



#### Supervisory Board

Composition of the Supervisory Board as at January 1st 2016:

- Monika Kacprzyk-Wojdyga - Chairman of the Supervisory Board,
- Jacek Obłąkowski - Deputy Chairman,
- Robert Kapka - Member,
- Tomasz Klikowicz - Member,
- Artur Kucharski - Member,
- Przemysław Lis - Member,
- Marek Mroczkowski - Member,
- Zbigniew Paprocki - Member,
- Ryszard Trepczyński - Member.

At its meeting on January 15th 2016, the Supervisory Board appointed Zbigniew Paprocki as Secretary of the Supervisory Board.

On January 29th 2016, by way of a letter from the Minister of State Treasury, Przemysław Lis was removed from the Supervisory Board, and Marek Grzelaczyk was appointed in his place.

On February 1st 2016, by way of resolutions of the Company's Extraordinary General Meeting, Monika Kacprzyk-Wojdyga and Marek Mroczkowski, Jacek Obłąkowski and Ryszard Trepczyński were removed from the Company's Supervisory Board, while Maciej Baranowski, Tomasz Karusewicz, Przemysław Lis

and Bartłomiej Litwińczuk were appointed as the new members (Przemysław Lis was appointed as the Chairman of the Supervisory Board).

On February 19th 2016, the Supervisory Board appointed Marek Grzelaczyk as Deputy Chairman of the Supervisory Board of the ninth term of office.

On March 31st 2016, Marek Grzelaczyk tendered his resignation as Deputy Chairman. At its meeting held on April 15th 2016, the Supervisory Board appointed Tomasz Karusewicz as Deputy Chairman.

As a result of the above changes, in the period April 15th 2016-July 4th 2016, the composition of the Supervisory Board was as follows:

- Przemysław Lis - Chairman,
- Tomasz Karusewicz - Deputy Chairman,
- Zbigniew Paprocki - Secretary,
- Maciej Baranowski - Member,
- Marek Grzelaczyk - Member,
- Robert Kapka - Member,
- Tomasz Klikowicz - Member,
- Artur Kucharski - Member,
- Bartłomiej Litwińczuk - Member.

As the ninth term of office of the Supervisory Board expired, the parent held elections to the Supervisory Board of the tenth term. The election was held on March 11th-23rd 2016 (1st round) and on March 30th-April 14th 2016 (2nd round).

The following persons were nominated by the employees to the Supervisory Board of the tenth term:

- in the 1st round: Robert Kapka and Zbigniew Paprocki,
- in the 2nd round: Roman Romaniszyn.

Pursuant to resolutions of the Company's Annual General Meeting of July 5th 2016, the following persons were appointed members to the Supervisory Board of the tenth term:

- Przemysław Lis - Chairman,
- Maciej Baranowski,
- Robert Kapka,
- Tomasz Karusewicz,
- Artur Kucharski,
- Bartłomiej Litwińczuk,
- Zbigniew Paprocki,
- Roman Romaniszyn.

Acting pursuant to Art. 16.2 of the Articles of Association of Grupa Azoty S.A., the Minister of State Treasury, by letter of June 30th 2016, appointed Marek Grzelaczyk to the Company's Supervisory Board, effective from July 5th 2016.

On July 18th 2016, the Supervisory Board elected Tomasz Karusewicz as its Deputy Chairman and Zbigniew Paprocki as its Secretary.

Following the above changes, from July 18th 2016 to December 2nd 2016, the composition of the Supervisory Board was as follows:

- Przemysław Lis - Chairman,
- Tomasz Karusewicz - Deputy Chairman,
- Zbigniew Paprocki - Secretary,
- Maciej Baranowski - Member,
- Marek Grzelaczyk - Member,
- Robert Kapka - Member,
- Artur Kucharski - Member,
- Bartłomiej Litwińczuk - Member,
- Roman Romaniszyn - Member.

On December 2nd 2016, by way of resolutions of the Company's Extraordinary General Meeting, Przemysław Lis and Maciej Baranowski were removed from the Supervisory Board, while Monika Fill and Ireneusz Purgacz were appointed as new members of the Supervisory Board. The Extraordinary General Meeting also appointed Marek Grzelaczyk as Chairman of the Supervisory Board.

As a result of the above changes, from December 2nd 2016 to the date of this report, the composition of the Supervisory Board was as follows:

- Marek Grzelaczyk - Chairman,
- Tomasz Karusewicz - Deputy Chairman,
- Zbigniew Paprocki - Secretary,
- Monika Fill - Member,
- Robert Kapka - Member,
- Artur Kucharski - Member,
- Bartłomiej Litwińczuk - Member,
- Ireneusz Purgacz - Member,
- Roman Romaniszyn - Member.

***Marek Grzelaczyk - Chairman of the Supervisory Board***

Marek Grzelaczyk is a graduate of the Catholic University of Lublin, where he earned an MA in law. He completed an Executive Master of Business Administration programme at the Warsaw Management University. He also completed a course and passed a state exam for members of management and supervisory boards of state-owned companies, as well as a receivership course run by the Association of Polish Receivers in Bankruptcy. During his professional career he has held the positions of Deputy Director of the district power utility in Krasnystaw, President of the management board of the Health Practitioners Housing Cooperative of Zamość, Zamość Governor, Mayor of Zamość, President of the management boards of CONSEIL DEVELOPMENT ALFA Sp. z o. o., INWEST-FS Sp. z o.o., Wikana Bioenergia Sp. z o.o. of Lublin, and EURO-PROJEKT Zwierzyniec Sp. z o.o.

Currently, he serves as President of the management boards of the Perła Sztuki Foundation of Lublin, PBL DEVELOPMENT Sp. zo.o., and LUBELSKI CHMIEL INVESTMENT Sp. z o.o. He sat on the supervisory boards of Zakład Energetyczny Łódź - Teren S.A., WIKANA S.A. and POL-MOT AUTO S.A. of Warsaw. Marek Grzelaczyk was also a member, and since February 22nd 2017 has been Chairman of the supervisory board of Interbud Lublin S.A. From February 19th 2016 to March 31st 2016, he served as Deputy Chairman of the Supervisory Board of Grupa Azoty S.A., and since December 2016 has held the position of the Board's Chairman.

***Tomasz Karusewicz - Deputy Chairman of the Supervisory Board***

Economist, graduated in business management from Szczecin University. Mr Karusewicz is a qualified comptroller, certified by the Ministry of Finance. He is also qualified to serve on supervisory boards of the state-owned companies. Completed a number of internal audit and control courses and training programmes.

In 2003-2005, Mr Karusewicz worked at the Internal Control Department of the Szczecin City Hall, and also served as comptroller. Then employed as an expert at Nafta Polska S.A. In 2006-2008, Mr Karusewicz worked at the Ciech Group, first as deputy director at the owner supervision office of Ciech S.A. and member of supervisory boards of Zakłady Chemiczne Alwernia S.A. and Ciech Polfa Sp. z o.o. (both Ciech Group companies). Then he moved on to serve as member of the supervisory board of Ciech S.A. In 2007-2009, he worked as deputy director at the Business Development Office and the Foreign Investments Office of PZU S.A. In 2010-2012, Mr Karusewicz worked at Telewizja Polska S.A. as director of the Audit and Internal Control Office. Also served on supervisory boards of Enea S.A. of Poznań (2007-2008), IKS "Solino" S.A. of Inowrocław and Zakład Wodociągów i Kanalizacji Sp. z o.o. of Szczecin (2015).

In 2006, Mr Karusewicz held the position of chairman of the supervisory board of Zakłady Azotowe w Tarnowie-Mościcach S.A. Currently employed as member of the management board of PZU Życie S.A., a PZU Group company.

***Zbigniew Paprocki - Secretary of the Supervisory Board***

Mr Paprocki graduated from the Academy of Agriculture in Kraków with a master's degree in environmental engineering. He completed a post-graduate MBA programme at the Faculty of Mechanical Engineering at the Institute of Business Studies, and a course for members of supervisory boards of state-owned companies. He has worked for Grupa Azoty S.A. (formerly Zakłady Azotowe w Tarnowie-Mościcach S.A.) for over 20 years. First as Shift Foreman, then as Deputy Head of the Power Engineering Department, Deputy Chief Production Coordination Engineer, and from 2012 as Head of the Production Management and Coordination Office at the Corporate Production Coordination and Safety Department. Since 2010, he has worked as Chairman of the Association of Chemical Industry Engineers and Technicians, Tarnów Branch, and member of its Executive Board.

On the Supervisory Board of Grupa Azoty S.A. Mr Paprocki served from November 2010 to April 2013, and since June 2013 (elected by the employees). He was also deputy chairman of the supervisory board of ELZAT Sp. z o.o. and chairman of the supervisory board of PROREM Sp. z o.o.

***Monika Fill - Member of the Supervisory Board***

In 1996, Ms Fill graduated from the Institute of English Studies at the Jagiellonian University in Kraków. In 1996-1998, she studied in London, where she obtained a master's degree in Modern European Studies at the University of North London. Having returned to Poland, she started working in finance. In 1999-2006, she worked with Prudential, a US company, PZU S.A., and Golden Egg Niezależni Doradcy Finansowi, holding managerial positions in marketing and sales, with a large portfolio of successful sales and advertising campaigns. In 2004, she completed sociology studies at the Institute of Applied Social Sciences of the University of Warsaw, and in 2008 - a post-graduate course in insurance at the Academy of Finance in Warsaw.

From 2006 to 2010 she was a member of the supervisory board and then vice president and president of the management board of Pocztove Towarzystwo Ubezpieczeń Wzajemnych (a mutual insurance company). In 2015-2016, she held a managerial position on the Warsaw Stock Exchange, and was also president of the management board of the Warsaw Stock Exchange Foundation.

She is authorised by the Ministry of State Treasury to serve on supervisory boards of state-owned companies. Since 2012, Ms Fill has run her own consulting company.

***Robert Kapka - Member of the Supervisory Board***

On the Supervisory Board of Grupa Azoty S.A. since June 2013. Member of the Supervisory Board elected by the employees.

Graduate of the Cracow University of Technology, Faculty of Chemical Engineering and Technology, principal field of study: light chemical technology, master of science. He also completed a post-graduate course in Polymer Chemistry and Technology at the Rzeszów University of Technology. In 2013, he passed the exam for candidates to supervisory boards of state-owned companies.

Mr Kapka has been employed at Grupa Azoty S.A. (formerly Zakłady Azotowe w Tarnowie-Mościcach S.A.) since 1999, at the following positions: Process Engineer, Manager of comprehensive tests and commissioning of the Polyamide Plant, Head of Caprolactam Polymerisation Division, Head of Production at the Plastics Centre, and Head of Production at the Plastics Production Unit, Plastics Business Segment. From December 2014, Head of Plastics Production Unit in Tarnów, Plastics Business Segment. From July 2016 to March 17th 2017, chairman of the supervisory board of Grupa Azoty ATT Polymers GmbH.

***Artur Kucharski - Member of the Supervisory Board***

On the Supervisory Board of Grupa Azoty S.A. since October 2011. Mr Kucharski graduated from the University of Central London with a master's degree in Electronic Engineering, and from the Faculty of Electrical Engineering of the Warsaw University of Technology. In 2011, he completed an Executive MBA Programme at the Warsaw University of Technology Business School.

Between 1995 and 2002, he was employed with PricewaterhouseCoopers Sp. z o.o. of Warsaw, where he held positions from assistant to manager in the Financial Audit Department. In 2002-2007, he was a lecturer in International Accounting Standards, MBA Programme at the Warsaw University of Technology Business School. From 2002 to 2010, he worked in the Consulting Department of PwC Polska Sp. z o.o., holding positions from Senior Manager to Director. In 2010-2012, he served as member of the management board and chief strategy officer at Kopex S.A. Prior to the appointment, deputy chairman and chairman of the supervisory board, Director for Internal Control Systems, Structure and Organisation Development at Kopex S.A.

He served on the supervisory boards of Mostostal Zabrze Holding SA, Hydrapres SA, Globe Trade Centre SA, and Asseco Poland SA. Since 2015, member of the supervisory board of Prime Car Management S.A.



***Bartłomiej Litwińczuk - Member of the Supervisory Board***

Mr Litwińczuk is a graduate of the University of Warsaw, Faculty of Law and Administration (master's degree, commercial public law). In 2009, he completed legal training as an attorney-at-law at the regional bar association in Warsaw, and passed the bar examination. In May 2010, he was entered in the register of attorneys-at-law. Mr Litwińczuk owned a law firm. In his legal practice, he specialised in the protection of personal rights, commercial companies law, criminal law, penal fiscal law, civil law, and administrative law. Provided legal services to businesses, also in the field of corporate governance. Since February 1st 2016, he has served as Member of the Supervisory Board of Grupa Azoty S.A.

***Ireneusz Purgacz - Member of the Supervisory Board***

Mr Purgacz is a graduate of the Law and Administration Faculty at the University of Warsaw. He completed legal training for court judges in the Ciechanów Provincial Court, and legal training as an attorney-at-law at the Regional Bar Association in Płock.

He worked as an assistant judge in the Ciechanów Provincial Court, and then practiced law at Zespół Adwokacki Nr 1 in Ciechanów. Since January 1995 to date, Mr Purgacz has run his own law firm in Ciechanów. As part of his practice as attorney-at-law, he offers legal services to individuals and businesses, in civil, commercial, administrative and criminal law. From 2009 to 2011, he served on the supervisory board of Przedsiębiorstwo Wodociągów i Kanalizacji Sp. z o.o. in Wyszaków.

***Roman Romaniszyn - Member of the Supervisory Board***

Graduate of the Faculty of Electrical Engineering, Automatics and Electronics, majoring in power generation, at the AGH University of Science and Technology of Kraków. He completed also a post-graduate course in energy audit at the AGH University of Science and Technology of Kraków. In 2015, he passed the exam for candidates to supervisory boards of state-owned companies. Member of the Supervisory Board elected by the employees.

In 1996, he joined Grupa Azoty S.A., where he held the positions of process engineer at the Electrical Engineering Department, deputy manager, and from 2003 - manager, of the Power Supply and Security Division at the Power Centre. Member of the management board of the Association of Polish Electrical Engineers, Branch No. 3 in Tarnów, member of the Polish Association of Chemical Engineers, Tarnów Branch.

**Powers and responsibilities of the Supervisory Board**

The Supervisory Board operates on the basis of:

- the Commercial Companies Code of September 15th 2000 (Dz.U. No. 94, item 1037, as amended),
- the Act on Commercialisation and Privatisation (...),
- the Accountancy Act,
- the Company's Articles of Association (Art. 33),
- Rules of Procedure for the Company's Supervisory Board.

**Audit Committee**

To streamline its work and improve control of the parent and the Group, on July 4th 2013 the Supervisory Board passed Resolution No. 21/IX/2013 on appointment of the Audit Committee.

Composition of the Audit Committee as at January 1st 2016:

- Jacek Obłękowski - Chairperson,
- Marek Mroczkowski,
- Tomasz Klikowicz.

Following the removal of Jacek Obłękowski and Marek Mroczkowski from the Supervisory Board by way of resolutions of the Company's General Meeting of February 1st 2016, on February 19th 2016 the Supervisory Board appointed the following persons to the Audit Committee: Tomasz Karusewicz, Maciej Baranowski and Artur Kucharski (as Chairman of the Audit Committee).

Following the resignation of Tomasz Karusewicz from the Audit Committee on March 8th 2016, on March 14th 2016 the Supervisory Board resolved to appoint Marek Grzelaczyk to the Committee.

As a result of the above changes, as of March 14th 2016, the Audit Committee was composed of:

- Artur Kucharski - Chairperson,
- Maciej Baranowski,
- Marek Grzelaczyk,
- Tomasz Klikowicz.

As the ninth term of office of the Supervisory Board expired, the Supervisory Board of the tenth term, at its meeting held on July 18th 2016 appointed an Audit Committee consisting of:

- Artur Kucharski - Chairperson,
- Robert Kapka,
- Marek Grzelaczyk,
- Maciej Baranowski.

Following the removal of Maciej Baranowski from the Supervisory Board (by way of a resolution of the General Meeting of December 2nd 2016) and Marek Grzelaczyk's resignation from the Committee, the Supervisory Board, at its meeting held on December 16th 2016, appointed Monika Fill and Ireneusz Purgacz to the Audit Committee.

As a result of the above changes, from December 16th 2016 to the date of issue of this report, the composition of the Audit Committee was as follows:

- Artur Kucharski - Chairperson,
- Monika Fill,
- Robert Kapka,
- Ireneusz Purgacz.

#### **Responsibilities of the Audit Committee**

The Audit Committee operates pursuant to the Rules of Procedure for the Audit Committee, adopted by the Supervisory Board by way of Resolution No. 21/IX/2013 of July 4th 2013. The main tasks of the Committee include:

- monitoring of the financial reporting process,
- monitoring the effectiveness of the Company's internal control, internal audit and risk management systems,
- monitoring of financial audit,
- monitoring of the independence of the auditor and the entity qualified to audit financial statements,
- monitoring the audit of full-year and consolidated financial statements,
- monitoring the work and reports of the independent qualified auditor.

### **8.13. Diversity policy**

The Group has no formalised diversity policy. However, in its operations it follows clear rules of employment and promotion. It also seeks to achieve diversity in terms of gender, education, age and professional experience of its entire workforce, including in particular members of the governing bodies and key management personnel.

*In accordance with the non-discrimination rule stipulated in Art. 11<sup>3</sup> of the Polish Labour Code, any form of employer discrimination, whether direct or indirect, on grounds of gender, age, disability, race, religion, nationality, political views, trade union membership, ethnicity, religious denomination, sexual orientation, or whether an employee is employed under a fixed-term or indefinite term full-time or part-time contract is prohibited.*

The Company's Articles of Association define rules for appointment of the Management Board and for election of Management Board members by employees. The Collective Labour Agreement set forth the employment and promotion criteria for managerial positions, based on a competence model and psychological tests verifying candidates' management abilities.

Also the Work Rules of Grupa Azoty S.A. contain a section devoted to equal treatment in employment.

Over the years, the Group has developed rules that support non-discrimination and diversity, and ensure equal opportunities for professional development of the workforce, and thus contribute to higher work efficiency and the Group's development.

## 8.14. Remuneration policy

### Remuneration system at Grupa Azoty S.A.

The parent's remuneration policy is based on a negotiation system. Remuneration is set by way of negotiation between the Management Board and the trade unions. As part of the process, the average remuneration growth rate in a given year and the remuneration components to which the growth rate will apply are determined. By the end of February every year, the Management Board and the trade unions sign a remuneration agreement defining the remuneration growth rate and the remuneration components to which the growth rate will apply, as well as the incentive policy for the year. The key principles governing the terms of employment and remuneration are provided for in the Collective Bargaining Agreement and the Work Rules. Persons holding key managerial positions at the parent are hired under management contracts and are not covered by the remuneration policy. Their remuneration comprises a monthly base salary and an annual bonus, whose amount depends on the degree of achievement of individual targets set for the year.

### Remuneration policy for members of the Management Board

Remuneration of Management Board members comprises:

- a fixed monthly salary, which includes also remuneration for sitting on management or supervisory boards of the Group subsidiaries (this does not apply to the Management Board member elected by employees, whose remuneration comprises a fixed monthly salary including remuneration for serving on the Management Board and remuneration due under the employment contract),
- a variable performance-based component, paid in accordance with the rules approved by the Supervisory Board,
- additional employee benefits granted each time by the Supervisory Board.
- a special bonus (the Management Board member elected by employees is not entitled to receive the bonus).

Additional benefits may be awarded to the Management Board members by the Supervisory Board, including:

- a length-of-service award, granted not more frequently than every five years,
- a severance pay if employment is terminated due to old age or disability retirement,
- partial reimbursement of the cost of using an apartment made available to a Management Board member, including a company apartment (up to PLN 2,000 per month),
- benefits consisting in using partly paid telecommunication services,
- additional health, property and personal insurance,
- personal indemnity cover, including in connection with share issues,
- the right to use the company car free of charge,
- the right to use the hardware and software owned by the parent to perform the duties of a Management Board member.

The employment contracts of the former Management Board members: Andrzej Skolmowski, Paweł Jarczewski, Marek Kaptucha, Marian Rybak, and Krzysztof Jałosiński, provide for a severance pay amounting to three months' fixed monthly salary equivalent in the event of removal from the Management Board prior to the expiry of the term of office. Members of the Management Board are not entitled to severance pay if their removal from the Management Board results from justified termination of the employment contract without notice for reasons attributable to the employee, pursuant to Art. 52.1 of the Polish Labour Code.

In the case of employment contracts with Mariusz Bober, Tomasz Hinc, Józef Rojek, Witold Szczypiński, and Paweł Łapiński, the payment of severance pay for removal or resignation from the Management Board must be approved by the Supervisory Board.

Additionally, the Management Board members are bound by non-competition agreements which remain in force upon termination of employment. Upon termination of their employment contracts, Mariusz Bober, Tomasz Hinc, Józef Rojek, and Witold Szczypiński are entitled to compensation amounting to 50% of their fixed monthly salary provided for in their employment contracts, paid out over a period of six months.

Upon termination of employment contracts, Andrzej Skolmowski, Paweł Jarczewski, Marek Kaptucha, Marian Rybak, and Krzysztof Jałosiński are entitled to compensation amounting to 100% of their fixed monthly salary provided for in their employment contracts, paid out over a period of twelve months. The right to receive the compensation expires on breach of the non-competition agreement.

Artur Kopeć is bound by an agreement on holding the position of the employee-elected Management Board member. The agreement, effective only for the duration of the employment term, does not provide for any severance pay for removal from the Management Board.

#### **Changes in rules of remuneration**

The rules of remuneration for members of the Management Board were changed on February 6th 2017. Total remuneration of members of the Management Board comprises a fixed component in the form of a monthly base pay (fixed remuneration) and a variable component representing additional remuneration for the Company's financial year (variable remuneration). The monthly remuneration of a Management Board member is the product of the average monthly remuneration in the business sector, net of bonuses paid from profit, in the fourth quarter of the previous year, as announced by the President of the Central Statistics Office of Poland (GUS). Starting from the calendar month following the month in which the President of GUS announced the amount of the average monthly remuneration, the amount of the fixed remuneration is changed accordingly.

The fixed remuneration is reduced by the amount payable for the days on which no work was performed by a Management Board member.

The variable (additional) remuneration depends on the progress of management objectives and is paid in accordance with the rules stipulated in Resolution No. 8 of the Company's General Meeting of December 2nd 2016, and in the Act on rules of remunerating persons who manage certain companies of June 9th 2016 (Dz.U. of 2016, item 1202).

Variable remuneration is paid after:

- approval of the Directors' Report on the Company's operations and of the financial statements for the previous financial year,
- the General Meeting has granted a Management Board member discharge in respect of performance of their duties in a given financial year,
- a Management Board member has submitted a report on performance of the management objectives,
- the Supervisory Board has approved performance of the management objectives by the Management Board member in a given year,
- the Supervisory Board has adopted a resolution on performance of the management objectives and the amount of variable remuneration due.

#### **Rules governing remuneration of key management personnel**

Persons holding key managerial positions at the parent are hired under management contracts. Under management contracts, the managers are entitled to the following perquisites: a company car, provided on the terms and conditions specified in the parent's internal regulations, parking space for a private car, a portable computer with Internet access and a mobile phone with unlimited business calls, a fixed amount to cover the cost of accommodation (for some managers).

#### **Evaluation of the remuneration policy**

The remuneration policy, established through negotiations with the social partners, is closely linked to the parent's financial results. In accordance with the Collective Bargaining Agreement, the parent's current and forecast economic condition is the basis for determining the remuneration growth for any given year. In addition, the amounts of certain remuneration components, such as the incentive bonus and the annual bonus, depend directly on the financial results of the parent and the degree of achievement of the targets set for the individual managers.

## Remuneration of the parent's Supervisory Board members

	Remuneration paid		Total	Remuneration potentially due
	fixed remuneration components	variable remuneration components		
Maciej Baranowski	128	5	133	-
Marek Grzelaczyk	132	6	138	-
Monika Kacprzyk-Wojdyga	34	-	34	-
Robert Kapka*	422	1	423	-
Tomasz Karusewicz	145	1	146	-
Tomasz Klikowicz**	176	1	177	-
Artur Kucharski	154	6	160	-
Ewa Lis	10	-	10	-
Przemysław Lis	187	9	196	-
Bartłomiej Litwińczuk	128	-	128	-
Marek Mroczkowski	25	-	25	-
Jacek Obłękowski	29	-	29	-
Zbigniew Paprocki***	317	1	318	-
Roman Romaniszyn****	160	-	160	-
Ryszard Trepczyński	25	-	25	-

\* including remuneration under employment contract with the Company - PLN 268 thousand,

\*\* including remuneration under employment contract with the Company - PLN 85 thousand,

\*\*\* including remuneration under employment contract with the Company - PLN 140 thousand,

\*\*\*\* including remuneration under employment contract with the Company - PLN 97 thousand.

## Remuneration of the parent's Management Board members

	Remuneration paid		Total	Remuneration potentially due*
	fixed remuneration components	variable remuneration components		
Mariusz Bober	687	18	705	427
Paweł Jarczewski	640	240	880	-
Tomasz Hinc	541	-	541	340
Krzysztof Jąłosiński	120	45	165	-
Marek Kaptucha	883	210	1,093	-
Artur Kopeć	750	-	750	267
Paweł Łapiński	463	-	463	272
Józef Rojek	553	-	553	340
Marian Rybak	371	15	386	-
Andrzej Skolmowski	599	210	809	-
Witold Szczypiński	1,153	-	1,153	462

\* Remuneration potentially due corresponds to a provision created for performance-based annual bonuses, granted in accordance with the rules approved by the Supervisory Board. The annual bonus is planned to be paid in 2017.

## Remuneration of the parent's management and supervisory personnel for holding office at the Group's subsidiaries

	Remuneration paid		Total
	fixed remuneration components	variable remuneration components	
Dr. Wojciech Wardacki	51	-	51
Krzysztof Jałosiński	440	-	440
Marian Rybak	520	-	520
Andrzej Skolmowski	171	-	171
Witold Szczypiński	30	-	30

### Further information on remuneration

In the reporting period, the Group did not recognise any retirement or similar benefit obligations with respect to former members of management, supervisory or administrative bodies.

## 8.15. Sponsorship, charitable or similar activities

The Group treats its social responsibilities and cooperation with the communities in which operates as matters of strategic and long-term importance. Social, sponsorship, and charitable initiatives are key elements contributing to the implementation of the long-term development strategy of the Group. Through its engagement in such initiatives, the Group promotes its image of both financially strong and socially responsible business.

The multifaceted and advanced nature of these activities make the Group companies active participants of the local community life, providing support where it is most needed.

### Social and sponsorship policy

The social and sponsorship activities are pursued in compliance with the "Group Policy and Rules of Social and Sponsorship Activities", formulated and implemented in 2013, and charitable initiatives are governed by the "Group Donation Policy" and the "Grupa Azoty S.A. Donation Policy", adopted in 2013.

Directions for the social and sponsorship activities:

- Investments benefiting the local community, solving social issues, charitable assistance in the form of cash and non-cash donations and services, addressed directly to the communities or to charitable organisations, NGOs and non-profit organisations,
- Social and sponsorship projects relating to local initiatives, often with a supraregional, or even international, media coverage,
- Social and sponsorship projects relating to nationwide or international initiatives, going beyond the framework of local initiatives.

Objectives of the social and sponsorship activities:

- Building a positive image of the Group as a people- and environmentally-friendly business,
- Building the Group's and its companies' image as socially responsible businesses supporting local initiatives,
- Promoting the Grupa Azoty brand by increasing its recognition outside the group of its customers and buyers of its products,
- Communicating Grupa Azoty's message to circles which are important for the Company, with focus on the importance of high standards of projects and initiatives implemented by the Group,
- Building the Group's and its companies' reputation, and gaining recognition and favourable perception among the public, particularly for the positive role the Group plays in solving social and environmental issues of today's world,
- Enhancing attractiveness of the regions in which the Group operates as places to live, work, pursue passions, fulfil ambitions; and offering young people the best possible education, health and wellbeing opportunities,
- Supporting promotional and commercial activities.

Social and sponsorship activities of Grupa Azoty PUŁAWY in 2016 were conducted in accordance with a plan adopted by the Company's Management Board and approved by the Supervisory Board. The Company acted in line with the adopted rules on types and forms of assistance.

Grupa Azoty POLICE's sponsorship activities include sponsoring agreements, agreements for promotional and advertising activities, and donations. Image building and product promotion are carried out through various cultural, educational, scientific, sports and other initiatives.

At Grupa Azoty SIARKOPOL, sponsorship activities form a material component of the company's promotional efforts. The key projects involve brand promotion, building of positive image, support of the local community, and contribution to the development of the Province of Kielce.

#### **Charitable giving policy**

The Group-wide donation policy specifies the rules of granting donations. Through donations, the Group seeks to actively respond to the needs of foundations, associations, schools, non-profit organisations and individuals in difficult circumstances. In particular, the Group supports projects contributing to the enhancement of medical care, social and educational development of children and youth, as well as other initiatives benefiting local communities.

The Group builds its socially responsible image in the region by supporting:

- both professional and amateur sports,
- cultural initiatives, including mass cultural events,
- educational institutions for children and youth,
- healthcare institutions providing services to employees and their families,
- research programmes,
- regional environmental initiatives,
- social campaigns.

The Group builds its business-like image by sponsoring:

- professional sports, including sports clubs,
- sports associations, national and international sports competitions, including sports leagues in team sports,
- the Polish Olympic Committee,
- individual athletes, subject to approval by respective national sports associations.

All donations are granted in line with the Group-wide donation policy as well as individuals companies' rules for granting donations.

In 2016, Grupa Azoty gave donations for initiatives related to: religious worship activities, maintaining and promoting national tradition, support for veterans and victims of repression, health protection and promotion, social welfare, support for the disabled, support for families, motherhood and parenthood, education, activities fostering development of local communities.

Projects supported with Grupa Azoty KĘDZIERZYN's donations in 2016 involved: health protection and promotion, assistance in difficult situations, support of the World Youth Day, treatment and rehabilitation, support for the disabled, religious worship activities, protection of cultural property, etc.

Grupa Azoty PUŁAWY engages in projects contributing to better quality of medical care, promoting healthy lifestyles, fostering social and educational development of children and youth, as well as events designed to maintain and promote national tradition, cultivate the Polish national identity, and develop national, civic and cultural awareness. In 2016, organisations supported by the Company included:

- 'Dajmy Szansę' Foundation of Milejów, raising funds to finance medical equipment for the independent public healthcare facility in Łęczna;
- 'Chemik' Puławy Society for the Promotion of Physical Culture, organising recreational and sports activities for the Company's employees;
- The Company's PTTK (Polish Tourist Association) Branch, organising and promoting tourist activities among the Company's employees;
- Association of Friends of the Puławy Technical School Complex;
- Divine Mercy RC Parish in Puławy, as the organiser of the World Youth Day 2016 in Puławy;

- 'Przeszłość-Przyszłości' Association, as the organiser of celebration of the '70th Anniversary of Pacification and Burning of Wąwolnica';
- Foundation for the Support of the Historical Garden in Puławy, which is carrying out revitalization of the courtyard at the Czartoryski Palace in Puławy.

Through donations, Grupa Azoty POLICE actively responds to the needs voiced by the employees, associations, foundations and other organisations in the region. In 2016, organisations supported by Grupa Azoty POLICE included:

- The Municipality of Police, as the organiser of the 2016 Police-Kraków Racing Pilgrimage;
- John Paul II Medical Institute of Szczecin, raising funds for the financing of the final stage of construction and launch of the Rehabilitation Hospital in Szczecin;
- 'Academia' Association of Pomerania Instrumentalists, as the organiser of the Sacrum Non Profanum Musical Festival;
- St John the Evangelist Hospice Foundation, raising funds to finance care of terminal cancer patients;
- Elementary schools in Sławęcín, Różnowo Nowogardzkie and Izbica, winners of the 'Chemistry in Agriculture' artistic contest;
- Hospital Medical Centre in Goleniów, raising funds for the financing of purchases of anti-bedsore pneumatic mattresses;
- Zbyszek Ulatowski Walrus Club of Winter Swimming Enthusiasts, as the organiser of the Expedition to the Polar Circle project;
- Tanowo Children's Home, as the organiser of summer holidays for its charges.

#### **Social and sponsorship initiatives for culture**

Grupa Azoty S.A. supports a number of cultural events (such as the Grupa Azoty International Jazz Contest, the Tarnów Film Prize) and cultural institutions, including the Krzysztof Penderecki European Centre for Music in Lusławice, the Mościce Arts Centre, the Girls Cathedral Choir Puellae Orantes Association, the City Art Gallery Biuro Wystaw Artystycznych in Tarnów, and the Tarnów Fine Arts Association Zachęta.

Grupa Azoty PUŁAWY also engages in activities fostering development of the local community by helping to organise cultural events and supporting cultural initiatives. 2016 was another year of the Company's partnership with the 'Dom Chemika' Puławy Cultural Centre, the Zamoyski Museum in Kozłówka, and the Vistula Museum in Kazimierz Dolny. The Company was again a sponsor of events held as part of the 'All Directions of the World' classical music festival as well as 'The Cursed - the Unconquered of the Lublin Region' cyclic TV programme.

Grupa Azoty POLICE sponsored local cultural institutions, including the Municipal Cultural Centre in Police, 'Słowianin' Cultural Centre in Szczecin, Baltic Neopolis Orchestra, and University of Szczecin Choir. The company also supports numerous cultural events, including the Police Day and the Chemists' Day, a local event enjoying the greatest popularity in the County of Police.

Grupa Azoty KĘDZIERZYN sponsors the protection of local cultural heritage, in particular by supporting the activities of the Koźle Region Association, which protects the history and monuments of the Koźle Region and the City of Kędzierzyn-Koźle. The company also provides assistance to the Inland Navigation Youth Brass Orchestra, whose members perform on the most prominent European stages.

The cultural events sponsored by Grupa Azoty SIARKOPOL include: the Staszów Bread Day, Harvest Festivals in Osiek and Tuczępy, Szydłów Plum Festival, International Children's Day, and Krystyna Jamroz International Musical Festival in Busko-Zdrój.

#### **Social and sponsorship initiatives for education of children and the youth**

Grupa Azoty S.A. partners with schools and universities not only as part of research programmes, but also in such areas as internships, work placement opportunities and workshops for students; it also works with several other entities to support the education of children and the youth, which include SIEMACHA Association, KANA Catholic Youth Education Centre, I KROPKA Culture and Arts Foundation, General Education School Complex No. 1 of Tarnów- Mościce, Technical School Complex, Sports School Complex.



Grupa Azoty PUŁAWY continued the 'Safety is Our Common Goal' campaign, run jointly with the County Police Headquarters and the County Fire Service of Puławy since 2013, and designed to prepare children and youth to safely spend their time. In partnership with the Puławy Science and Technology Park, Grupa Azoty PUŁAWY organised fairs promoting science among children and youth as part of the Young Chemist's Day, Lublin Science Festival, and Santa Claus Science Show.

Grupa Azoty KĘDZIERZYN ran another edition of environmental protection workshops for pupils of Kędzierzyn-Koźle elementary schools. The motto of the workshops was 'How to live in harmony with Nature'. The company was also involved in the 'A Young All-Chemist' project for junior high school students in Kędzierzyn-Koźle. The participating students are asked to prepare an interesting chemical experiment. Since 2006, Grupa Azoty KĘDZIERZYN has organised the nationwide 'Catch the Hare' photo competition as part of the Responsible Care Programme.

In cooperation with schools and higher education institutions, Grupa Azoty POLICE has for a number of years arranged training placements and internships for students. The company's cooperation with local communities involves supporting educational initiatives and institutions at various levels, as well as scholarship programmes.

For a few years now, Grupa Azoty SIARKOPOL has sponsored research scholarships for participants of the 'Artystoteles' contest, initiated and organised by the Staszów Chamber of Commerce. Regular financial support is also provided to Kindergarten No. 8 with integrated groups in Staszów.

#### **Social and sponsorship initiatives for sports**

- In 2015, Grupa Azoty S.A. launched the multi-year programme Grupa Azoty START - its original comprehensive sports and social project designed to discover young talents. The following initiatives have been undertaken as part of the Grupa Azoty START Programme: Climbing Development Programme, Basketball Development Programme, Speedway Development Programme, Handball Development Programme, Cross-Country Skiing Development Programme.
- The Group also supports numerous other nation-wide and local sporting events. According to experts, the Grupa Azoty brand created through consolidation has become one of the most visible brands in Polish sports, particularly in such disciplines as ski jumping, volleyball and speedway.
- As part of additional initiatives designed to advertise and promote its brand, the Group worked with individual athletes, such as Piotr Żyła (ski jumping), Janusz Kołodziej (speedway), and sports associations, clubs, and teams: Polish Ski Federation, the Unia Tarnów speedway team, the Tarnów Handball Association, the Unia Tarnów Sports Club (football), the Jedyńka Tarnów Sports Club (women's volleyball), MLKS Dąbrowia sports club (archery), Popular Interschool Students' sports club at Junior High School No. 8 in Tarnów, and other. Moreover, Grupa Azoty became the Main Partner of the Odra Opole football club.
- Grupa Azoty PUŁAWY continued its involvement with the Azoty-Puławy and Wisła Puławy sports clubs. In 2016, the Azoty-Puławy men's handball team, sponsored by the company, fought for top positions in the best league at the national level and represented Poland in European cups. Furthermore, Grupa Azoty PUŁAWY entered into cooperation with Górnik Łęczna, a Polish premier league football club.
- Grupa Azoty PUŁAWY also provided support to various associations of sports fans and enthusiasts. In 2016, the company teamed up with the Aeoroklub of Lublin in the organisation of Poland's ballooning championships in Nałęczów, cooperated with the Azoty Yacht Club of Puławy, which organises sailing courses and training camps in the Masurian Lake District and on the Vistula river, with the KYOKUSHIN Karate Club of Lublin, and with a number of local football clubs.
- Grupa Azoty KĘDZIERZYN has been a long-standing Main Sponsor of a premier league volleyball team ZAKSA Kędzierzyn-Koźle. The company has also supported Bartłomiej Mróz, a parabadminton player. As far as amateur sports are concerned, Grupa Azoty KĘDZIERZYN has provided support to a number of regional initiatives, including the 'Chemik' Sporting Society, Lewada Equestrian Club, Kluczbork Municipal Sports Club, as well as various projects undertaken for instance by the 'Koziołek' Sports Club or the Municipal Interschool Sports Club (in connection with the 'Koziołki Pływackie' championships).
- In 2016, Grupa Azoty POLICE continued its cooperation with MKS Pogoń Szczecin, a premier league football team, and with KPS Chemik Police, a top-ranking volleyball women's club. The KPS Chemik Police team ended the 2015/2016 season very successfully, by winning the Championship of Poland for the third consecutive time and the Cup of Poland for the second time in a row. The team did credit to Polish clubs in the CEV European Champions League Women. Furthermore, Grupa Azoty POLICE initiated partnership with the Chemik Police Football Club to become its Main Partner.

- Grupa Azoty POLICE also sponsors regional amateur sports by providing financial assistance to the 'WODNIK' Students' Swimming Club, 'Champion' Students' Sports Club, 'Ósemka' Students' Athletics Club, 'Promień Police' Athletics Club, and the Sports and Recreation Centre in Police.

#### **Social and sponsorship initiatives for regional promotion and development**

- In 2014, Grupa Azoty S.A. organised the first New Year's Charity Concert, whose aim was to support the construction of the Via Spei hospice. Proceeds from the 2015 concert were donated to the Tarnów Branch of the Polish Multiple Sclerosis Association. Proceeds from the 2016 charity concert were donated to the Ich Lepsze Jutro Association. In 2017, proceeds from the concert were given to the Prometeusz Association for the Assistance to the Disabled Children and Their Families of Zbylitowska Góra.
- Grupa Azoty S.A. also supports the Tarnów Branch of the Polish Tourist Association, Society of the Friends of Mościce, the Tytus Chałubiński club of Polish Red Cross Honorary Blood Donors at Grupa Azoty S.A.
- Grupa Azoty KĘDZIERZYN was involved in the organisation of the conference 'Modern Technologies, Structures and Materials for the Chemical and the Power Industries', combined with the nationwide Young Innovators Forum competition held by the Metalchem Industrial Park Association. The conference was devoted to development of the Polish chemical and power industries and to promising technologies.
- Grupa Azoty KĘDZIERZYN also lent support to the World Entrepreneurship Day organised by the Kędzierzyn-Koźle Industrial Park, and to a conference focusing on restoration of navigability of the Oder river, held by the Ministry of Water Economy and Inland Navigation.
- Furthermore, the company supported the development of road infrastructure by contributing to the cost of repair of the district road in Mostowa street. The project was part of a broader effort to create safe and modern road infrastructure to provide the company's trading partners and employees with convenient access to the company's premises.

#### **Social and sponsorship initiatives to promote protection of human life and health**

Grupa Azoty S.A. supports the Centre for Children with Special Educational Needs in Zbylitowska Góra and the Ich Lepsze Jutro Association.

The Grupa Azoty Group engages in projects which contribute to improving the quality of medical care or promote healthy lifestyles. For instance, it offered assistance to the Tanowo Children's Home, the Medical Institute in Szczecin, the Hospital Medical Centre in Goleniów, the Fundacja Dzieciom 'Zdążyć z pomocą' children's foundation, and the St John the Evangelist Hospice Foundation.

Grupa Azoty SIARKOPOL regularly provides substantial financial aid to a health care centre in Staszów (Samodzielny Publiczny Zespół Zakładów Opieki Zdrowotnej), supporting it in its efforts to replace medical equipment with new, modern devices. The company also participated in a charity campaign to raise funds to finance the treatment in the US of Staś Patrzalek from Staszów, a baby suffering from cancer of both eyeballs.

#### **Social responsibility and sponsorship programmes for the chemical industry**

Grupa Azoty joined a dozen or so Poland's largest companies that founded the Polish National Foundation, whose mission is to promote and protect the image of Poland and the Polish economy, and to foster positive social reception of investment projects implemented by state-owned companies. The new organisation is to work with local communities, social and business institutions, and to undertake and finance social initiatives.

Grupa Azoty supports the Federation of Engineering Associations FSNT-NOT, the FSNT-NOT Tarnów Council, and the Tarnów Branch of the Polish Association of Chemical Engineers SITPChem.

Grupa Azoty PUŁAWY provided financial assistance to help with the organisation of the International Technological Seminar together with the Polish Association of Chemical Engineers SITPChem.

Grupa Azoty KĘDZIERZYN supports the operations of the Kędzierzyn-Koźle Branch of the Polish Association of Chemical Engineers SITPChem, as well as selected events aimed at promoting entrepreneurship, carried out or organised by the Kędzierzyn-Koźle Industrial Park.

#### **Corporate social responsibility**

The Group's CSR initiatives are related to:

- amateur sports, including:
  - financial support mainly for: schools, youth clubs and associations, and initiatives undertaken using publicly available sports facilities,

- sponsorship of disabled athletes (including the Polish Paralympic Committee),
- support for sports initiatives in the region, seeking to ensure equal opportunities for all communities across the region,
- cultural initiatives, including mass cultural events,
- education, including public schooling,
- science and research projects furthering and promoting the history and tradition of Poland's chemical industry and supporting its development,
- environmental initiatives,
- healthcare institutions providing services to employees and their families,
- social campaigns.

#### ***Scholarship programme at Grupa Azoty S.A.***

The initiative launched in 2014 is addressed to students of the master's programme of the Faculty of Chemical Engineering and Technology of the Cracow University of Technology. It provides for two scholarships of PLN 1,000 per month each. The scholarships will be awarded until the grantees complete the master's programme and obtain a master's degree in engineering, up to the age of 26. Scholarships are awarded in accordance with the 'Group Scholarship Policy' as well as scholarship programmes and rules separately approved by management boards of individual Group companies. The competition winners receive scholarships of PLN 1,000 a month, are guaranteed employment at the Group, and are offered the opportunity to participate in joined projects conducted by scientific institutions and industrial organisations.

#### **Scholarship programme at Grupa Azoty Kędzierzyn**

In 2016, Grupa Azoty KĘDZIERZYN granted 27 scholarships to the most talented students of School Complex No. 3 of Kędzierzyn-Koźle.

As the school's chemical patron, Grupa Azoty KĘDZIERZYN also donated the third piece of equipment to the school's laboratory - this year it was the spectrophotometer VIS, which will be used for laboratory work during vocational classes on Chemical Analysis.

Scholarships are granted on the basis of the Grupa Azoty Group's scholarship policy as well as scholarship programmes and Rules for Scholarship Granting, a separate document approved by the Company's Management Board. Students of the school's chemical forms are guaranteed the possibility of completing their work placements and learning one of their vocational subjects at Grupa Azoty KĘDZIERZYN facilities.

#### ***Collaboration with educational institutions***

Grupa Azoty S.A. actively supports its local community through partnership with educational institutions. The parent also works with scientific and research centres on joint educational initiatives. For several years now, it has been partnering with the Cracow University of Technology, particularly in running internship programmes, assisting in bachelor's and master's theses, student and doctoral placements and, more generally, in getting some of the greatest minds in the industry to educate students.

The partnership with the Cracow University of Technology involves the 'Technology as a carrier of business' seminar dedicated to students in the last semester of their master's programmes at the Faculty of Chemical Engineering and Technology of the Cracow University of Technology. After the seminar conducted by practitioners employed with Grupa Azoty S.A. in Tarnów, all attendees receive a certificate.

Cooperation with the State Higher Vocational School in Tarnów includes organisation of student internships, diploma internships, workshops and laboratories at the Group's business units, educational field-trips for students, and lectures given by Group experts.

Cooperation with the Technical School Complex of Tarnów includes: employment of ten school leavers each year, granting scholarships for best-performing students, sponsoring awards for olympiad, contest, and competition winners, organisation of work placements, preparation of dedicated instruction classes conducted by Grupa Azoty experts, organisation of educational field trips, organisation of teacher training in cutting-edge technologies, and co-financing purchases of teaching aids. The initiatives are implemented in partnership with the Ignacy Mościcki Foundation.

The Group was also a partner of the 'We build the value of Polish Economy. Work for us!' contest, organised by the Ministry of State Treasury, whose winner completed a three-month internship at Grupa Azoty KĘDZIERZYN.

Grupa Azoty PUŁAWY continued to support the Technical School Complex of Puławy, the Maria Curie-Skłodowska University in Lublin (its branch campus in Puławy) with respect to its Technical Chemistry

programme, and the Warsaw University of Life Sciences with respect to a post-graduate course in trading in fertilizers and crop protection chemicals in sustainable agriculture. The company also sponsored scientific conferences, including the 'Biodiversity in Areas Affected by Industrial Pollutants – Innovative Protection Methods' conference organised by the Cardinal Wyszyński University in Warsaw.

Moreover, Grupa Azoty KĘDZIERZYN partners with the Opole University of Technology and the University of Opole, offering help in organising work placements at the Company's facilities and writing academic papers. As part of the cooperation, in 2016 an educational visit was organised for students of the Wrocław University of Technology's Chemical Faculty who also take an engineering course in Chemical Technology.

Grupa Azoty SIARKOPOL sponsored state-of-the-art equipment for the chemical laboratory at the Cardinal Stefan Wyszyński General Secondary School in Staszów, which enables the school to conduct university-level classes.

Grupa Azoty POLICE and the West Pomeranian University of Technology in Szczecin signed an agreement on workforce education, which is directly linked to the construction of a unit for propylene production based on propane dehydrogenation (PDH). The agreement will make it possible to train future employees for the project. Furthermore, as part of the cooperation, a laboratory was created to address the need to educate students in the field of olefin production processes. It will also be used to improve employee qualifications, mainly for the personnel of PDH Polska S.A., a special purpose vehicle of Grupa Azoty POLICE established to construct a propane dehydrogenation (PDH) unit.

#### ***Competitions and programmes***

The Group launched the second edition of the 'Grounded in knowledge' programme. The aim of this three-year scheme is to promote optimum farm management, with particular focus on fertilizer application technologies. The programme envisages testing of 6,300 soil samples.

To showcase the importance of chemistry in our lives, in February 2016 the Group organised the 'Chemistry is all around us' arts competition, and thus invited children and teenagers to take part in an exciting and creative fun activity. The winners went on a trip to the Copernicus Science Centre in Warsaw.

The competition was addressed to primary and junior schools of those towns and cities where strategic Group companies, i.e. Grupa Azoty S.A., Grupa Azoty PUŁAWY, Grupa Azoty KĘDZIERZYN, Grupa Azoty POLICE, and Grupa Azoty SIARKOPOL are located. Its purpose was to enhance the participants' knowledge of the chemical sector, the role chemistry plays in everyday life.

Grupa Azoty PUŁAWY also participated in the activities of the Secretariat of the international Responsible Care Programme. In 2016, on the initiative of chemical companies, the twelfth 'Tree for a Bottle' campaign was held, addressed to children of the Puławy region.

Once again, the nationwide 'Catch the Hare' photo competition was organised for employees and children of employees of the companies participating in the Responsible Care Programme.

In 2016, Grupa Azoty POLICE celebrated 20 years of its participation in the Responsible Care programme, focusing on health protection, process safety, and environmental protection.

## 9. Other material information and events

### 9.1. Qualified auditor

#### Parent

The agreement with KPMG Audyt Sp. z o. o., executed on July 10th 2012, and the following annexes thereto:

- Annex 1 of October 15th 2013,
- Annex 2 of December 23rd 2014,

cover the following:

- audit of separate and consolidated financial statements for the 12 months ended December 31st 2012, December 31st 2013, December 31st 2014, December 31st 2015 and December 31st 2016,
- review of separate and consolidated financial statements for the six months ended June 30th 2012, June 30th 2013, June 30th 2014, June 30th 2015 and June 30th 2016,
- organisation of workshops.

Other services included primarily RES, Art. 44 of the Energy Law, derogations, accounting opinions, translation of financial statements, and preparation of a report on meeting financial covenants.

#### The remuneration of KPMG Audyt Sp. z o.o. for services rendered to the parent

Item	2016	2015
Audit of the full-year separate and consolidated financial statements of the parent and the Group	187	187
Review of the half-year separate and consolidated financial statements of the parent and the Group	107	89
Other services	95	267
<b>Total</b>	<b>389</b>	<b>543</b>

The remuneration for the audit of other companies of the Group is paid pursuant to separate agreements executed between the qualified auditor of financial statements and each company.

#### The remuneration of KPMG Audyt Sp. z o.o. for services rendered to companies of the Group (without the parent)

Item	2016	2015
Audit of the full-year separate and consolidated financial statements of the company and audit or review of consolidation package	782	849
Review of the half-year separate and consolidated financial statements of the company and review of consolidation package	209	178
Other services	153	239
<b>Total</b>	<b>1,144</b>	<b>1,266</b>

## 9.2. Environmental performance

### Sustainable development policy

Grupa Azoty has implemented a strategic approach to sustainable development, based on its long-term Sustainable Development Strategy. The Strategy was developed on the basis of the Company's existing good practices as well as research and analyses conducted both internally within the Company and among its stakeholders. It is founded on the business strategy. This approach allows the Group to enhance its economic value and to build value for the stakeholders.

The strategy reflects an integrated approach to:

- economic efficiency,
- responsibility towards staff and the natural environment,
- relationship with the environment.

The Sustainable Development Strategy rests on three pillars:

- sustainable production (mitigation of environmental impacts, creation of sustainable products, and increasing environmental awareness),
- dialogue and relationship building (active dialogue with all stakeholder groups, implementing a code of ethics),
- workplace (improving employee satisfaction and workplace safety).

### Respect Index

The purpose of the RESPECT project is to bring to light the companies that excel in communication with the market through current and periodic reports and through websites. Inclusion in the RESPECT Index depends on, among other things, socially responsible conduct vis à vis the environment, the community and the employees.

The selection of companies to be included in the Index is a three-stage process. The criteria evaluated in the selection process include financial condition, strategy, management processes, environmental factors, human resources policy and employee relations, as well as market impact and customer relations. Thus, Grupa Azoty S.A. has become a member of an elite group of stable, reliable and trustworthy organisations. Grupa Azoty S.A.'s inclusion in the RESPECT Index provides investors with an additional assurance that Grupa Azoty S.A. is a stable and safe enterprise, managed to the highest standards of sustainable development. In 2016, the parent participated in yet another evaluation of corporate social responsibility in public companies and was awarded a diploma as a Respect Index constituent.

The Company has been a constituent of the RESPECT Index since November 19th 2009, which stands as a testament to Grupa Azoty S.A.'s care for sustainable development and responsible management.

### Legal requirements

In accordance with the Environmental Protection Law, companies of the Group are required to adjust the permits they hold to the requirements stipulated in applicable laws.

In the reporting period, Grupa Azoty S.A. obtained the following decisions:

- Amendment to a decision of the Governor of the Province of Kraków of July 29th 2011, Ref. No. SW.II.1.AJ.7673-10/09, granting an integrated permit to the parent for the Technical Grade Nitric Acid Unit, Calcium Ammonium Nitrate and Ammonium Nitrate Unit, Nitrogen Fertilizer Granulation Unit, and Dolomite Milling Unit, valid for an indefinite term (permit amended by Decision of August 16th 2016, Ref. No. SR-II.7222.2.8.2016)
- Decision of the Marshal of the Province of Kraków dated January 20th 2016, Ref. No. SR-III-1.7244.4.9.2015.AG, granting a permit to the parent for waste collection and processing, valid until January 19th 2026.

In terms of environmental protection, Grupa Azoty POLICE operates based on an integrated permit for the operation of process units, granted by the Marshal of the Province of Szczecin on January 9th 2014. By way of decision issued by the Marshall of the Province of Szczecin on September 21st 2016, another amendment was made to the company's integrated permit. As regards greenhouse gas emissions, in 2016 the Company obtained new emission allowance decisions issued by the Marshal Office of the Province of Szczecin under the Act on Trading System for Greenhouse Gas Emission Allowances of June 12th 2015.

Grupa Azoty PUŁAWY is authorised to conduct industrial operations under the integrated permit for the operation of process units of December 31st 2004, issued by the Governor of the Province of Lublin

and subsequently extended in 2016 under a decision by the Marshal of the Province of Lublin of February 26th 2016, amending the integrated permit for a combustion plant - CHP plant.

### Safety

The Group's business requires compliance with the most exacting safety standards, which minimise the risk of industrial incidents. Relevant solutions applied across the Group ensure appropriate conditions for the manufacture, storage, transport and distribution of substances to meet the natural environment protection requirements. The Group companies operate in the chemical industry and are classified as facilities with a high risk of a serious industrial incident. Being aware of the possible consequences of their operations, the Group companies strive to mitigate their negative environmental impact.

Advanced technological solutions enable the Group companies to actively engage in pro-environmental efforts, which are often a source of economic benefits as well. Ensuring the responsibility and safety of production processes is a fundamental principle of the Group. The companies have devised and implemented appropriate incident prevention programmes, and safety matters are subject to regular reporting.

Moreover, rescue plans and safety management systems are in place for the Group facilities. Given the nature of its business, the Group is subject to the requirements of the Environmental Protection Law, the Water Law, the Waste Act, and other regulations on environmental protection, OHS and fire safety. The legislation imposes certain obligations on Group companies with respect to production activities, investment projects, site restoration and creating appropriate conditions for the manufacture, storage, transport and distribution of products.

The Group companies were distinguished with the Gold Card of Safe Work Leader, which is awarded to businesses that operate effective OHS management systems and have effective OHS prevention programmes in place.

The Group has implemented the STOPTM Safety Monitoring Programme, designed to raise the degree of involvement in OHS matters among managers and employees of all ranks, develop hazard identification skills, improve communication with respect to OHS matters, raise awareness of the importance of occupational safety by building new attitudes.

In 2016, joint inspections were carried out at the Group by three national supervision and inspection bodies: National Fire Service, Provincial Inspectorate for Environmental Protection, and National Labour Inspectorate. The inspections revealed no omissions or irregularities.

In 2016, the parent updated, and adapted to the current legal requirements, the Safety Report – General Section, as well as analyses of process risk for units posing a major risk of serious chemical plant failure, Internal Rescue Operation Plan, Industrial Accident Prevention Programme and High Risk Establishment Notification. The documents were approved in January 2017 by the Province Commander in Chief of the National Fire Service. Following the implementation of the Seveso III Directive and the amendment of the Environmental Protection Law, in 2016 the “Grupa Azoty S.A. Safety Guidelines” were updated.

In 2016, the following documents were updated at Grupa Azoty POLICE: the ‘High Risk Establishment Notification’, the ‘Safety Report’, and the ‘Internal Rescue Operation Plan’, which were provided to the Province Commander in Chief of the National Fire Service. The ‘Safety Measures and Procedures to be Followed in the Case of a Serious Industrial Accident’ were also revised.

In January 2016, Grupa Azoty PUŁAWY was awarded a distinction from the Minister of Family, Labour and Social Policy for the study entitled ‘Systemic approach to improving occupational safety and comfort of employees of Grupa Azoty Zakłady Azotowe Puławy S.A.’, prepared for the 44th edition of the Nationwide Working Conditions Improvement Competition. In 2016, all workstations were subject to occupational risk reassessment.

The Group companies have appropriate organisational and technical safety measures in place, such as CCTV systems, safeguards, and procedures for incident prevention and mitigation of consequences. They maintain well-trained fire services capable of effective rescue operations, with additional support from supernumerary chemical rescue and technical rescue teams working in a continuous system and other services.

## **SPOT**

With the safety of people, their property and natural environment in mind, the Group's plants offer assistance in the event of incidents involving transport of hazardous materials. In 2000, the Group along with a group of other chemical manufacturers and the Polish Chamber of Chemical Industry established the Assistance System for Transport of Hazardous Materials (SPOT).

The system aids in recovery from incidents involving transport of hazardous materials. It helps to improve the safety of transport in Poland, and in case of any incidents it facilitates effective removal of their consequences by joint effort and measures of the national rescue, fire services and SPOT members. SPOT's help in actively preventing potential threats and damage to property as well as in providing assistance to rescue services allows hazardous materials to be transported in as safe and reliable a manner as possible. In 2016, SPOT drills were conducted at Grupa Azoty.

In 2016, Grupa Azoty PUŁAWY was actively involved in the SPOT System of Assistance in Transport of Hazardous Materials. On February 15th–19th 2016, together with Grupa Azoty POLICE the company participated in the pumping of ammonia from derailed rail tankers in Szczecin. The operation was carried out using a unique technology for pumping ammonia under field conditions, developed and tested by Grupa Azoty PUŁAWY.

## **Environmental projects**

The parent's key environmental projects in 2016 included:

- delivery and assembly of a new turbine generator at the CHP Plant,
- construction of a flue gas denitrification unit,
- continued work on construction of a flue gas desulfurization unit.

Following the installation of the turbine generator, the amounts of coal and pollutants emitted into the atmosphere were reduced.

The flue gas desulfurization and denitrification projects were undertaken to ensure compliance of the Company's industrial combustion sources to the requirements laid down in the Minister of Environment's Regulation on Emission Standards for Installations of April 22nd 2011 and the Industrial Emissions Directive. All projects involved upgrading the existing EC-2 CHP infrastructure and bringing it into compliance with the new emission requirements. As a result, the amount of pollutants emitted into the atmosphere by the Company's combustion sources will be reduced, improving air quality. Construction of the flue gas desulfurization and denitrification units was co-financed under the Norwegian Financial Mechanism 2009-2014, while delivery and assembly of a turbine generator was co-financed under the National Investment Plan.

The turbine generator and flue gas denitrification projects were completed in 2016 and their commissioning is under way. Completion of the flue gas desulfurization unit is planned for 2017.

Grupa Azoty KĘDZIERZYN is about to complete the first stage of construction of a new CHP Plant, which is designed to restore the plant's heat and electricity generation capacity and increase its output to satisfy demand for heat and electricity, based on solutions that ensure compliance with the growing environmental requirements.

Grupa Azoty POLICE's largest ongoing environmental project consists in the construction of a flue gas treatment unit and upgrade of the EC II CHP plant, which is to bring the co-generation operations into compliance with the NO<sub>x</sub>, SO<sub>x</sub> and particulate matter emission requirements of Directive 2010/75/EU.

In 2016, Grupa Azoty PUŁAWY launched two air pollution control projects to reduce volatile organic compounds in flue gas (Packaging Production Division), and to combust gases from benzene hydrogenation in cyclohexanol dehydrogenation furnaces. Also, the company plans to upgrade its OP-215 No. 2 steam generator to reduce NO<sub>x</sub> emissions.

In the area of water and wastewater management, a cooler was installed at Line II of the Gas Preparation Unit, which helped reduce the discharge of wastewater from Line II of the Gas Pre-Treatment System to the industrial drainage system by approximately 150 kg a day.

## **Water and wastewater management**

The Group uses water for industrial purposes, as a cooling agent, for drinking, to produce process waters, and for fire-fighting applications. The parent draws water from two sources – a surface intake on the right bank of the Dunajec river and an underground intake from Quaternary water-bearing formations (first aquifer). The allowed amounts of water drawn are specified in the relevant water-law permits.



The parent's industrial facilities generate the following types of industrial wastewater: process wastewater, sanitary sewage, spent cooling water, and stormwater. Industrial wastewater is routed for treatment via an underground industrial sewer system and trestle-supported sewer lines. Depending on origin, industrial wastewater is transported to either the Central Wastewater Treatment Plant or the Biological Wastewater Treatment Plant. Industrial wastewater and sanitary sewage undergo mechanical and chemical treatment at the Central Wastewater Treatment Plant. The Biological Wastewater Treatment Plant receives industrial wastewater containing biodegradable substances. This type of wastewater is then additionally streamed to the Wastewater Treatment Facility operated by the Tarnów Water and Sewage Utility (Zakład Oczyszczalni Ścieków Tarnowskich Wodociągów Sp. z o.o.). Stormwater and spent cooling water from Grupa Azoty S.A. are drained separately, through an EF+A0 collector, collected in a retention pond, and then discharged through a Sutro weir into the Dunajec river.

The parent is well prepared for any wastewater system failure. In order to prevent wastewater escape, the system can be entirely shut off by closing the storm water outflow valve and pumping all wastewater to the Central Treatment Plant. It is also possible to direct the entire volume of wastewater generated by Grupa Azoty S.A. to the Wastewater Treatment Facility operated by the Tarnów Water and Sewage Utility.

Relevant parameters of the industrial wastewater are monitored on an ongoing basis at individual system nodes with remote analysers. Also, wastewater samples are laboratory-tested for pollutants at a predetermined frequency. The discharged wastewater meets the parameters defined in the integrated permit.

Grupa Azoty POLICE operates a sustainable water and wastewater management programme. The company takes care to ensure that the emission parameters are compliant with the terms of its integrated permit by supervising the wastewater treatment process.

For its power-generation or industrial process purposes, the company draws water from two surface water intakes:

- Western arm of the Oder river, through a river-bank water intake located on 48+900 km of the Szczecin-Świnoujście seaway,
- The Gunica river (the water intake from the Gunica river was constructed along with a surface water storage and pressure-equalising tank, which is to secure sufficient amount of water without exploiting water resources of the river; additionally, water is periodically abstracted from the Oder river, depending on its salinity).

The water is used for industrial purposes, as a cooling agent, and for fire-fighting applications. Industrial wastewater from production processes is received by the Company Wastewater Treatment Plant. Spent cooling water and stormwater from the plant are discharged directly into the surface waters of the Oder river. Spent cooling water undergoes regular automatic pH monitoring.

Industrial wastewater, leachate from the phosphogypsum landfill site, leachate from the iron sulfate (II) landfill site, sanitary sewage, and municipal wastewater from the town of Police are treated at the company's collective mechanical and chemical wastewater treatment plant.

The treated wastewater is monitored in accordance with the terms of the integrated permit. At present, the volume of discharged wastewater is monitored on an ongoing basis, while the quality of wastewater discharged into water is regularly examined by an accredited laboratory. Tests are performed in line with reference methods set forth in the Regulation of the Minister of the Environment on conditions to be met when discharging wastewater into water or soil, and on substances particularly harmful to the water environment, dated November 18th 2014. The company meets all the requirements defined in the integrated permit for the quantities of abstracted water, volumes of discharged wastewater, pollution parameters of treated wastewater, as well as the amounts of stormwater and spent cooling water.

June 9th 2016 saw the publication of Commission Implementing Decision (EU) 2016/902, issued on May 30th 2016, establishing best available techniques (BAT) conclusions for the common waste water and waste gas treatment/management systems in the chemical sector (CWW). Accordingly, Grupa Azoty PUŁAWY, as an operator of a wastewater treatment plant, is required to comply with the BAT Conclusions by June 8th 2020. A project structure was established at Grupa Azoty PUŁAWY for a programme designed to develop comprehensive solutions related to water and wastewater management as well as sludge management. As part of the tasks performed by the wastewater management team, a contract was signed with an external company for the development of a technical concept and cost estimate for the management and discharge of all wastewater streams generated at Grupa Azoty PUŁAWY so that their quality and manner of their discharge meet the parameters of wastewater discharged to receiving waters, in line with BAT for the chemical sector

and other legal regulations. The team responsible for sludge management analysed the current status and possible options for managing the sludge generated by the company. Inspection carried out by the Marshal Office of Lublin with respect to waste management and payment of charges for landfilling of waste revealed no irregularities.

### **Solid waste management**

The main types of waste generated by the parent are ash and slag. Wet ash was reused, and fly ash was delivered to customers for use in the construction industry. Approximately 50% of the hazardous waste were spent oils and lubricants, which were collected by MIS-Polska and subsequently transferred to a refinery where the waste is used to manufacture new oil. The remaining part of the waste was hazardous packaging materials and spent catalysts containing hazardous substances.

The parent recycles its plastic waste in the Compounding PA6 and Compounding POM units. In 2016, the units recovered 74.8 tonnes of plastics.

The parent also operates a selective waste collection programme (for waste paper, plastics, wood, glass, used batteries, and used electric and electronic equipment). With environmental concerns in mind, in contracts with external providers of waste collection services and services involving generation of waste Grupa Azoty S.A. incorporates a clause requiring the providers to reuse or dispose of the waste collected from the Company in accordance with environmental protection laws and the waste act. Grupa Azoty S.A. also works with Branzowa Organizacja Odzysku S.A. and the Polish Chamber of Commerce to meet the appropriate targets applicable to recovery and recycling of packaging waste, including composite and hazardous materials packaging waste.

The main type of waste by-product generated by Grupa Azoty POLICE is phosphogypsum, which is disposed of by being deposited in the company's phosphogypsum landfill site. Waste was managed in compliance with the terms of the Company's integrated permit.

Additionally, in order to meet the appropriate targets applicable to recovery and recycling of packaging waste, including composite and/or hazardous materials packaging waste, Grupa Azoty POLICE partners with TOM Organizacja Odzysku S.A. and Polska Izba Odzysku i Recyklingu Opakowań (Polish Chamber of Recovery and Recycling of Packaging Waste).

In 2016, Grupa Azoty PUŁAWY transferred 80,221 tonnes of slag and ash from wet removal of furnace waste for recovery. An inspection carried out in June 2016 by the Marshal Office of Lublin with respect to waste management and payment of charges for landfilling of waste revealed no irregularities.

### **Emissions**

The Group has implemented a range of environmental protection solutions contributing to lower air emissions.

The air pollution control equipment reduces the amount of flue gases and particulate matter discharged into the atmosphere:

- Particulate matter emissions can be reduced thanks to the use of wet scrubbers, cyclones, multicyclones and electrostatic precipitators;
- the reduction in pollutant emissions in gases was achieved through scrubbers and thermal reducers.

The parent also measures emission volumes and pollutant concentration levels at major emitters. Measurements are taken on a continuous basis (at the CHP plant and the dual-pressure nitric acid unit) or on a periodic basis at selected process emitters. Emission volumes and pollutant concentrations are measured in keeping with the applicable legal and administrative requirements. As the in-house CHP plant and chemical plants have participated in the emissions trading scheme since 2005 and 2013, respectively, the Company reviews its annual reports and obtains rights on an annual basis.

In an effort to preserve clean air, the parent constantly monitors air quality at five sites across Tarnów. The locations of the measurement sites were selected to span the wide area that may be affected by particulate matter and gas emissions from the plant.

Grupa Azoty POLICE takes special care to ensure compliance with the terms of its integrated permit and applicable legal regulations on emissions into the air from production nodes. At present, two units are monitored by the company on a continuous basis:

- The EC II CHP plant – for SO<sub>x</sub>, NO<sub>x</sub>, and dust emissions,
- The titanium dioxide production unit (decomposition and calcination node) – for SO<sub>x</sub>, sulfuric acid mists, and dust emissions.

The company monitors the volumes of emissions of gaseous pollutants and particulate matter in accordance with the requirements defined in the integrated permit. To reduce pollutant emissions from the highly polluting units, overhaul and upgrading work is performed on gas treatment units, which requires substantial expenditure, including on replacement of filter cloths, repairs of absorbers and scrubbers, upgrades of dust filters. The company meets legal requirements pertaining to integrated air protection, and complies with the requirement to provide external supervisory authorities with relevant reports in a timely manner. Ambient concentrations are monitored on a 24/7 basis from four stations, whose location allows the company to assess the impact of pollutants generated during everyday operation of the plant.

### **CO<sub>2</sub> emission allowances**

In 2016, the average spot price of EUAs on the EU ETS market was EUR 5.28 (the highest price: EUR 8.08; the lowest price: EUR 3.91), which means a decrease of approximately 30% relative to 2015, driven chiefly by lower prices of energy commodities, including crude oil, electricity and natural gas (as EUA prices correlate with those prices).

In February 2016, distribution of free emission allowances to the participants of the EU ETS commenced. The Group companies hold a sufficient number of allowances to meet the obligations related to the settlement of CO<sub>2</sub> emissions and redemption of allowances for 2016.

### **Joint Implementation Project**

The Joint Implementation Project, launched in the second half of 2008, was successfully completed at the end of 2012. The project was run by the parent in partnership with Japan's Mitsubishi Corporation following the signing of the Kyoto Protocol, with a view to reducing GHG emissions, including nitrous oxide produced by the KDC nitric acid unit.

Over the project's duration (2008-2012), a total of 2,670,356 ERUs were generated, producing a profit in excess of PLN 100m.

Due to its importance, the project was monitored and supervised by management staff and unit operators on an ongoing basis during the entire period. The generated ERUs were subject to repeated reviews by an external company, and the units were placed for trading only after a final report was approved, confirming the correct application of the required standards and methodologies.

The company has been reducing emissions of nitrous oxide as a GHG since 2013, to the levels achieved during the Joint Implementation Project, in an effort to satisfy the BAT (Best Available Technique) criteria.

### **Noise emissions**

As production processes tend to generate noise, the Group companies select equipment with appropriate acoustic parameters for every new unit already at the design stage. In accordance with the integrated permits, noise generation must not exceed the permitted levels. This applies to both the noise at the workplace and the noise emitted outside. The Group monitors its noise emissions, and measures them in accordance with the requirements set out in the integrated permits.

The selection of equipment featuring proper noise emission parameters or methods of reducing noise applies to workplace noise as well as noise emitted to the environment. In accordance with the integrated permits, noise generation must not exceed the permitted levels.

The main sources of noise affecting the acoustic climate include sources related to the operation of process units (compressors, turbocompressors, reactor and distiller agitators, granulator drive motors), sources related to ancillary process units (such as transmission pipelines, pump systems, fans, cooling facilities, screw and belt conveyors), sources related to the operation of machinery and equipment during the start-up and shut down of process units.

Typical means of reducing noise nuisance are applied, including:

- installing soundproof enclosures,
- placing equipment in buildings and casings,
- exhaust silencers.

In 2016, noise measurements were taken in the proximity of Grupa Azoty S.A. facilities, in line with the requirements of integrated permits.

In line with the requirements of the integrated permit, the most recent measurements of noise levels in the vicinity of Grupa Azoty POLICE's plant at day- and night-time were carried out in 2015. The noise emissions were found to be within permitted levels.

## 10. Supplementary information

### Explanation of differences between actual results and the financial forecasts for 2016

As no forecast for 2016 were been published, the position of the parent's Management Board concerning achievement of such forecasts is not presented.

### Litigation

No proceedings are pending against the Group companies concerning any debt or liabilities whose amount would equal or exceed 10% of Grupa Azoty S.A.'s equity.

The total amount of all proceedings involving the Group companies does not exceed 10% of Grupa Azoty S.A.'s equity.

### Related-party transactions

In 2016, the Group companies did not execute any related-party transactions otherwise than on arm's length terms.

### Changes in the organisational structure of Grupa Azoty S.A.

There were no changes in the Company's organisational structure.

### Parent's branches

The Company does not operate non-local branches or facilities.

### Shares, share issues

In 2016, the parent did not issue, redeem or repay any debt or equity securities. The Company had spent the proceeds from Public Offerings by the end of 2013. The proceeds were used in line with the original issue objectives.

There are no agreements known to the Company which may cause future changes in the percentages of shares held by the existing shareholders and bondholders

The Company does not operate any control system for employee share ownership plan.

### Material events after the reporting period

#### *Appointment of qualified auditor of financial statements*

On March 28th 2017, the parent's Supervisory Board appointed a qualified auditor to review and audit the separate financial statements of the parent and consolidated financial statements of the Group for the financial years 2017, 2018 and 2019.

The entity appointed to perform the reviews and audits is Ernst & Young Audyt Polska Sp. z o.o. sp.k., with its registered office at Rondo ONZ 1, 00-124 Warsaw, Poland. Ernst & Young Audyt Polska Sp. z o.o. sp. k. is entered in the list of qualified auditors of financial statements under No. 130.

#### *Letter of intent for coal gasification project*

On April 20th 2017, the parent and TAURON Polska Energia S.A. of Katowice ("TAURON"), jointly referred to as the "arties", signed a letter of intent in which they outlined general terms and conditions of their cooperation aimed to execute a coal gasification project ("project").

The letter of intent was signed taking into consideration that the project may combine the satisfaction of energy needs and demand for a raw material used in the chemical industry, as it would consist in the establishment, through product streams, of interconnection between energy generation and chemical production with a coal gasification system.

Products of the project's process would include electricity and synthesis gas, with a composition enabling its direct use as feedstock for the production of hydrogen, ammonia, methanol or other chemicals. The parties determined that natural gas currently used to produce nitrogen-based fertilizers can be partly replaced with syngas obtained through coal gasification.

The project is currently at the stage of Pre-FEED (preliminary front end engineering design) and accompanying analyses, including market analyses. Estimates are putting the project's cost at between EUR 400m and EUR 600m, depending on the technology chosen.

TAURON declared that it would participate in the project on terms defined under separate agreements between the parties. TAURON's contribution would include selection and construction of a unit guaranteeing maximised utilisation of coal from the TAURON Group's coal mines. The parties agreed that additional coal may be supplied by third parties if TAURON is not able to supply coal in the quantities or with the parameters required for the process.

The letter of intent outlines the framework terms of cooperation and, at the present stage, does not give rise to any financial obligations or require the parties to make any management decisions. The parties declared their intention to cooperate and sign further agreements, including an agreement establishing a joint SPV for the project. The letter of intent will remain in force until December 31st 2017, but each party has the right to terminate it on a month's notice.

This Directors' Report on the operations of the Group for the 12 months ended December 31st 2016 contains 134 pages.

#### Signatures of Members of the Management Board

.....  
Wojciech Wardacki, PhD  
*President of the Management Board*

.....  
Witold Szczypiński  
*Vice President of the Management Board  
Director General*

.....  
Tomasz Hinc  
*Vice President of the Management  
Board*

.....  
Paweł Łapiński  
*Vice President of the Management Board*

.....  
Józef Rojek  
*Vice President of the Management  
Board*

.....  
Artur Kopec  
*Member of the Management Board*

Tarnów, April 26th 2017