THE LOTOS GROUP

DIRECTORS' REPORT ON THE FINANCIAL RESULTS OF THE LOTOS GROUP

IN Q4 2005

Gdańsk, March 1st 2006

Introduction

Q4 2005 was a period of intensive work by the Company's Management Board on execution of key development projects, including the Comprehensive Technical Upgrade Programme (PKRT Project), the PROSTA Programme for the service stations network as well as the restructuring and development of the Southern Refineries' assets. As concerns the PKRT Project, our efforts focused on further work on technical development, negotiating agreements related to various aspects of the Project, and relations with selected financial institutions. As regards execution of the PROSTA Programme, activities undertaken by the Management Board of Grupa LOTOS S.A., with a view to building a modern nation-wide network of LOTOS service stations, concentrated on continued development of the CODO stations network and on the closing of the acquisition of two service stations networks – ESSO and Slovnaft. As for the Southern Refineries, in Q4 2005, the Company carried on restructuring activities to streamline the capital and organisational structure of the Group in southern Poland.

High demand for refinery products, coupled with the consolidation of the LOTOS Group's market position, contributed to the almost full (i.e. 99.2%) utilisation of the Company's production capacity, expanded to 6m tonnes annually during the first half of 2005. Nevertheless, a drop in the refining margin by 23,1%, accompanied by the Q4 2005 slide in Ural/Brent differential by 39.8% on Q4 2004, and a 7,7% decline in oil prices, compared with Q3 2005, was only partially offset by the increased production capacity.

In Q4 2005, the Company's financial results improved considerably compared with the corresponding period of 2004. Net sales revenue went up by 44.3% in Q4 2005 compared with the corresponding period of the previous year, reaching PLN 2,954.5m, while operating profit grew by 138.2%, to PLN 433.3m, and net profit increased by 133.7%, to PLN 408.1m. However, such an impressive improvement of financial results posted during the period of lower oil prices, weak refining margins and lower Ural/Brent differential relative to previous quarters, was possible mainly due to a non-recurring event, that is completion of the independent valuation of assets and liabilities and contingent liabilities of the Southern Refineries and Petrobaltic, acquired on February 3rd 2005, performed in order to establish their fair value. The revaluation increased the consolidated financial results by PLN 288.4m. The Company's financial performance in Q4 2005, adjusted for the effect of non-recurring events, deteriorated compared with the corresponding period of 2004. The operating profit fell by 20.4% to PLN 144.8m, while the net profit went down by 31.5%, to PLN 119.6m.

Simultaneously, the Company managed to significantly improve its cumulative financial performance for the four quarters of 2005, compared with the previous year. The consolidated net sales revenue went up by 29.5% and amounted to PLN 9,646.5m, operating profit grew by 79.7% to PLN 1,100.3m while net profit increased by 71.4% and reached PLN 930.3m. Even taking into account the adjustments referred to above, the financial performance improved considerably –operating profit and net profit went up by 32.6% to PLN 811.9m and 18.3% to PLN 641.9m, respectively. Due to the very good cumulative financial performance after four quarters of 2005, the Company was able to meet, almost in full, the revised forecast of the Company's consolidated financial results, which was published by the Management Board in Current Reports No. 84/2005 and No. 90/2005. Given the situation described in Note 3, the financial results do not account for the the impact of the 2005 activities of the UAB Naftos

Gavyba Group on the LOTOS Group's consolidated financial figures, which was taken into account in the forecast and which is estimated to be immaterial.

Comprehensive Technical Upgrade Programme

As concerns execution of the Comprehensive Technological Upgrade Programme (PKRT Project), which is of key importance for the Company's development and future growth of shareholder value, activities pursued by the Company in Q4 2005 were focused on further technical development work, negotiations of contracts relating to various areas of the Project and on contacts with selected financial institutions.

In Q4 2005, the licensors of three main technologies of the Project, performed design work aimed at developing basic designs of the main units to be constructed as part of the Project.

As agreed in the contract between the parties, from November 21st to November 23rd 2005, a P&ID Review Meeting was held at the offices of the engineering firm KBR, in Houston, Texas. The meeting marked the next formal phase of the basic designing procedure for the SDA/ROSE unit – one of the three main units to be constructed as part of the Project. The final delivery of the basic design of the SDA/ROSE unit took place in January 2006.

In accordance with the contract with the engineering firm Shell Global Solutions, from December 7th to December 9th 2005, a P&ID Review Meeting was held at the offices of Shell Global Solutions in Amsterdam, the Netherlands. The meeting marked the next formal phase of the basic designing procedure for the MHC unit, the second of the three main Project units. The final delivery of the basic design of the MHC unit took place in February 2006.

The basic designing procedure related to the third main Project unit, namely a gasification unit forming the main part of the IGCC unit, has entered its final phase. The design work is performed by Shell Global Solutions. From January 18th to January 20th 2006, a P&ID Review Meeting was held.

In October and November 2005, the GLSA tender committee, set up in connection with the pre-qualification tender announced on July 22nd 2005, were evaluating the bids submitted by companies interested in preparing the basic integrative design for the Project and providing engineering services related to the Project development. The tender committee finished its work on November 7th 2005, and submitted a final report and a recommendation for the Management Board. Following negotiations with the short-listed bidders (i.e. Fluor and the UHDE/Technip consortium), held in November and December 2005, the terms and conditions of co-operation in that area of the Project implementation were agreed upon. The agreements with the two contractors were signed on January 31st 2006.

On December 15th 2005, the Supervisory Board of the LOTOS Group resolved to approve an increase in the limit of liabilities to be contracted in connection with the Project's development phase. The additional funds will be spent on further development phases, including in particular the integrative design work.

As concerns the Preliminary Information Memorandum (PrePIM) sent on August 31st 2005 to the European Bank for Reconstruction and Development (EBRD), the European Investment Bank (EIB), Nordic Investment Bank (NIB), the Polish National Fund for Environmental Protection and Water Management (NFOŚiGW) and Bank Ochrony Środowiska (BOŚ), in

September 2005 all these organisations expressed their interest in the Project funding. In Q4 2005, the declarations of interest were evaluated by GLSA and the Financial Adviser (BNP Paribas).

From December 13th to December 15th 2005, the first round of visits were made under the preliminary due diligence review by EIB and NIB, which enabled the banks to learn more about the Project and to obtain such additional information as may be necessary in the future to make final decisions concerning participation in the Project funding.

A summary Information Memorandum concerning the Project was prepared for commercial banks in December 2005 and distributed on January 24th 2006. We expect the banks to express their preliminary interest in the Project funding on the basis of the Memorandum. Depending on their response, further activities will be undertaken with a view to arranging debt financing of the Project by commercial banks.

Following a tender process, on December 16th 2005 Deloitte Doradztwo Podatkowe was appointed to assist GLSA in applying for EU assistance and preferential funding, for which the Projects may be eligible given its environmental benefits.

GLSA conducted final negotiations with STASCO on a contract for supplies of supplementary feedstock for the Project units. The final version of the contract was agreed upon and the parties are currently obtaining the corporate approvals necessary to sign the contract, which is scheduled to take place in March 2006.

PROSTA Programme

The Company's activities in Q4 2005 related to the development of a retail fuel distribution network, pursued by the subsidiary undertaking LOTOS Paliwa as part of the PROSTA Programme, focused on continued expansion of own service stations, in particular by acquiring two existing networks of service stations: ESSO and Slovnaft.

December 14th 2005 saw the execution of the final agreement on the purchase of the ESSO service stations, including:

- a network of 39 service stations in very good locations, whose sales volumes are amongst the highest of those reported by network stations in Poland,
- 14 undeveloped plots for new service stations, all in good locations.

In the reporting period, the Company proceeded with consolidating the ESSO stations with the LOTOS network. As at December 31st 2005, 33 ESSO stations were incorporated into the network, whereas six of the acquired service stations were considered not yet ready to operate under the LOTOS brand. Since the acquisition, rebranding work has been carried out at the stations.

The agreement on the acquisition of Slovnaft assets is scheduled to be concluded in early March 2006.

As at December 31st 2005, the LOTOS network comprised 401 stations, of which 120 were COCO and CODO, 236 DOFO, and 45 DODO stations.

Petrobaltic and Production Activities

In Q4 2005, upstream company Petrobaltic produced over 57 thousand tonnes of crude oil from the bed of the Baltic Sea. The feedstock supplied by Petrobaltic was used in this period by the Czechowice Refinery, member of the Group, and covered 35.5% of the refinery's needs.

Southern Refineries

In Q4 2005, restructuring activities were continued to streamline the capital and organisational structure of the Group in southern Poland.

In connection with the restructuring of the Southern Refineries, the share capital of LOTOS Park Technologiczny Sp. z o.o., a key company in the restructuring of this area, was increased. On December 1st 2005, RC Remo Sp. z o.o. and CBA Racer Sp. z o.o. (subsidiaries of LOTOS Czechowice), as well as LOTOS Refinery itself, acquired equity interests in the increased share capital of LOTOS Park Technologiczny in exchange for contributions in kind.

On October 3rd 2005, LOTOS Lab Sp. z o.o. purchased all shares in Laboratorium Badacz Sp. z o.o., subsidiary of LOTOS Jasło. The transaction was effected as part of the consolidation process of the laboratory activities. As part of the same process, on December 1st 2005, LOTOS Lab acquired an organised part of CBA Racer's enterprise. The capital consolidation process in the laboratory business was completed on January 3rd 2006, when Laboratorium Badacz was incorporated into LOTOS Lab. Further consolidation measures relating to this business area will be undertaken internally at LOTOS Lab.

As regards consolidation of the maintenance activities, Q4 2005 was a time of preparatory work related to the acquisition of 100% of shares in Monto-Rem Sp. z o.o., subsidiary of LOTOS Jasło, and 100% of shares in RC Remo by LOTOS Serwis Sp. z o.o. Both transactions were effected on January 5th 2006 and were preceded by a purchase of a minority interest in Monto-Rem by the Jasło Refinery. Efforts are under way to incorporate the acquired companies into LOTOS Serwis.

On October 26th 2005, as part of the restructuring of the production and sale of bitumens, LOTOS Asfalt Sp. z o.o. acquired bitumen production assets from the Jasło Refinery.

On December 16th 2005, Grupa LOTOS acquired an interest in LOTOS Parafiny Sp. z o.o. for ca. PLN 15.5m. The shares were acquired from LOTOS Jasło, Rafineria Czechowice Parafiny Sp. z o.o. (wholly-owned by LOTOS Czechowice), and CHEMIPETROL Sp. z o.o. (wholly-owned by LOTOS Jasło). As a result of the agreement, Grupa LOTOS' shareholding in LOTOS Parafiny Sp. z o.o. rose from 26% to 100%.

Also in December 2005, LOTOS Oil S.A. purchased CBA Racer's assets related to low-volume production of oil.

Market Environment and Operations

In Q4 2005 the average price of Brent oil stood at USD 56.90/bbl, and was up on the previous year figure by 29.7%. Compared with Q3 2005, in Q4 2005 oil prices fell significantly, by USD 4.77/bbl, or 7.7%. The drop was accompanied by a falling Ural/Brent differential, resulting from lower supply of this commodity due to difficult weather conditions, in particular the harsh winter which hindered loading of tankers in the port in Novorossijsk, and problems with passage through the Bosphorus Strait. The Ural/Brent differential decreased to USD 3.67/bbl in Q4 2005, down from USD 6.09/bbl in Q4 2004. Compared with Q3 2005, the decrease amounted to USD 0.84/bbl, or 18.8%.

The equilibrium which was restored on the oil products market in Q4 2005 after a period of very high demand and high prices, partly attributable to the consequences of abnormal weather conditions in the United States (hurricanes), brought about a decrease in the average refining margin to USD 5.92/bbl in Q4 2005, compared with USD 7.0/bbl in Q4 2004 and USD 7.7/bbl in Q3 2005. Crack margins for diesel and light fuel oil rose in Q4 by 0.7% and 2.5%, respectively, compared with the Q3 figures, while the crack margins for gasoline and jet fuel fell by 36.3% and 3.3%, respectively, in the reporting period. Compared with Q4 2004, Q4 2005 saw an increase in crack margins for most refinery products – by 23.7% in the case of gasoline, by 3.6% in the case of light fuel oil, and by 12.3% in the case of jet fuel, while the crack margin for diesel decreased by 17.3%.

In Q4 2005, the Gdańsk Refinery processed 1,499.7 thousand tonnes of oil, thus reaching 99.2% of its installed capacity. 100% of the distilled oil was Ural crude. All of the Rozewie oil extracted by Petrobaltic was supplied to the refinery in Czechowice-Dziedzice. In Q4 2005, the LOTOS Group sold 418 thousand tonnes of motor gasolines, 596 thousand tonnes of diesel, 126 thousand tonnes of light fuel oil, 71 thousand tonnes of jet fuel, and 209 thousand tonnes of heavy fuel oil.

Compared with Q3 2005, in Q4 2005 employment in the LOTOS Group rose by 143 persons, up to 5,435 staff. The increase was mainly attributable to the growth in headcount resulting from the PROSTA Programme executed by LOTOS Paliwa, and an increase in the number of employees in the LOTOS Group Production Division.

It is estimated that the domestic consumption of fuels in the first 12 months of 2005 was at a level similar to the corresponding period in 2004, and the market share of the LOTOS Group stood at 22.5%, for gasolines, at 23.0% for diesel, and at 22.6% for light fuel oil. The estimated total share of the LOTOS Group in the domestic fuel market in 2005 was 22.8%.

Review of the Consolidated Results of the LOTOS Group for Q4 2005

<u>Profit and Loss Account</u>

In Q4 2005, the sales revenue was up by 44.3% on Q4 2004, and amounted to PLN 2,954.5m. The increase was driven mainly by higher sales volume reported by the Group and higher unit selling prices. The cost of sales in Q4 2005 stood at 2,557.6m, which represents a 53.7% rise compared with the corresponding 2004 figure. The net profit on sales in Q4 2005 totalled PLN 396.9m, representing a 3.8% increase on the Q4 2004 figure (up by PLN 14.6m).

The Q4 2005 consolidated operating profit stood at PLN 433.3m, up by PLN 251.4m, or 138.2%, from Q4 2004. The growth is partly attributable to PLN 288.4m being excess of company's share in net assets over acquisition cost (negative goodwill) recognised following completion of an independent valuation of assets, liabilities, and contingent liabilities of the Southern Refineries and Petrobaltic, acquired on February 3rd 2005. Furthermore, the last quarter of 2005 saw a rise of selling costs (up by 19.2%) relative to the corresponding last year figure, primarily due to the consolidation of the Southern Refineries and Petrobaltic.

Financial income in Q4 2005 stood at PLN 29.3m, representing an increase by PLN 4.2m on Q4 2004. The group also recorded a PLN 17.9m rise in financial expenses relative to the corresponding 2004 figure.

The consolidated pre-tax profit totalled PLN 454.2m in Q4 2005, having grown by PLN 238.6m compared with the corresponding period of the previous year. The after-tax profit was additionally reduced by the profit attributable to minority shareholders (mainly of Petrobaltic), amounting to PLN 10.4m, and stood at PLN 408.1m, which means a 133.7% growth on the Q4 2004 figure.

The net profit for the four quarters of 2005 was PLN 930.3m, and was PLN 387.5m higher than the 2004 profit.

Balance Sheet

As at the end of Q4 2005, the assets of the LOTOS Group totalled PLN 7,044.2m, up by 75.1% on December 31st 2004. The non-current assets grew by PLN 1,342.0m in 2005, mainly as a result of a PLN 1,190.6m increase in property, plant and equipment, attributable partly to the consolidation of the Southern Refineries and Petrobaltic.

The Group's current assets as at the end of December 2005 were higher by PLN 1,679.7m, primarily thanks to the higher production capacity of the Parent Undertaking, higher prices of raw materials and products, and a higher balance of cash due to proceeds from the share issue.

The Group saw its equity rise by PLN 2,169.0m relative to the December 31st 2004 figure, which resulted chiefly from a PLN 35.0m growth in the share capital and a nearly PLN 971.0m growth in reserve funds following the share capital increase, as well as a PLN 918.2m growth in retained earnings.

As at December 31st 2005, the non-current liabilities stood at PLN 697.8m, having increased by PLN 321.0m (85.2%) in the four quarters of 2005, mainly due to a loan contracted to carry out the PROSTA Programme and an increase in long-term provisions in connection with the consolidation of the Southern Refineries and Petrobaltic. High prices of crude oil, combined with larger inventories built due to the increased production of oil by the Parent Undertaking, contributed to a rise in the balance of current liabilities, which as at the end of Q4 2005 stood at PLN 1,519.9m, up by PLN 531.7m from December 31st 2004.

Cash Flows

As at December 31st 2005, cash amounted to PLN 774.4m, having declined by PLN 11.9m in the fourth quarter. In the corresponding period of 2004, it was PLN 618.1m lower and stood at PLN 156.3m.

Net cash flows from operating activities in Q4 2005 amounted to PLN 123.0m, up by PLN 31.8m on Q4 2004. The increase was driven primarily by the PLN 408.1m net profit earned in the fourth quarter, PLN 135.5m corporate income tax paid, and PLN 100.8m increase in inventories.

In Q4 2005, the LOTOS Group reported negative cash flows from investing activities, totalling PLN 225.9m (down by PLN 164.9m year on year). The negative balance was caused mainly by the purchase of tangible and intangible assets, as well as acquisition of current financial assets in Q4 2005.

Net cash provided by financing activities in Q4 2005 stood at PLN 91.2m, relative to net cash used in financing activities of PLN – 74.8m in Q4 2004. The Q4 2005 balance of cash resulted from a loan contracted by LOTOS Paliwa and expenditure on early repayment of loans by the Parent Undertaking.

Opinion of the Management Board of Grupa LOTOS S.A. on Meeting the 2005 Financial Forecasts Presented in Current Report No. 84/2005

The 2005 financial performance presented in these financial statements for Q4 2005 does not differ materially from the forecast disclosed in the Current Report No. 84/2005, with the exception that it does not take into account the impact of the measurement of the fair value of assets, equity and liabilities of the Southern Refineries and Petrobaltic S.A. on the consolidated financial result. In Current Report No. 84/2005, the Company estimated the fair value measurement's impact on the consolidated net profit at PLN 200m, and the amount finally disclosed in the Q4 2005 financial statements is PLN 288.4m. Moreover, in connection with the situation described in Note 3, the financial performance disclosed herein does not include the impact of the UAB Naftos Gavyba Group's 2005 activities on the consolidated financial result of the LOTOS Group. The impact was included in the forecast but is deemed to be immaterial.