THE LOTOS GROUP

DIRECTORS' REPORT ON THE FINANCIAL RESULTS OF THE LOTOS GROUP

IN Q2 2006

Gdańsk, August 11th 2006

Introduction

In Q2 2006, the activities of the Company's Management Board focused on preparation of the "Strategy for the LOTOS Group to 2012" ("Strategy"), which was approved by the Supervisory Board on June 27th 2006 and which provides for further growth of the shareholder value through optimum utilisation of the Company's potential in the three areas of its business, i.e. production and procurement of raw materials, oil refining and marketing. The strategy will be implemented in the particular business areas based on development programmes, in particular the Comprehensive Technical Upgrade Programme (PKRT), Trading Development and Optimisation Programme, Operational and Management Excellence Programme as well as the development programme for the exploration and production and oil supply area.

Implementation of the Strategy is expected to increase the refining volumes to 10.5m tonnes annually as of 2011 and to enhance the conversion ratio. The Company's market position, especially in the Baltic Sea region, will be strengthened, and its share in the Polish retail and wholesale markets should reach 10% and 30%, respectively.

As concerns the PKRT Project, which is of key importance for the Strategy, our efforts in Q2 2006 focused on extending the scope of the project, further work on technical development, and on updating the financial assumptions for the Project in cooperation with an independent market consultant, Purvin&Gertz. Concurrently, we revised the estimates of capital expenditure necessary to execute the Project. Taking into account the results of analyses conducted together with financial adviser BNP Paribas, and based on the updated assumptions, we decided to make appropriate changes to the structure and scope of the Project.

As regards execution of the PROSTA Programme, the activities aimed at building a modern nationwide network of LOTOS service stations concentrated on continued development of the COCO and DOFO stations network and on incorporation of the acquired ESSO and Slovnaft stations into the LOTOS network.

As for the Southern Refineries, in Q2 2006, the Company launched a project aimed at constructing a unit producing fatty acid methyl esters (FAME) – additives to biodiesel, and carried on restructuring activities to streamline the capital and organisational structure of the Group in southern Poland, particularly with respect to the auxiliary activities.

The market environment in Q2 2006 was very favourable for oil production and refining. The average price of Brent oil stood at USD 69.58/bbl, having gone up by 34.8% year on year and by 12.7% on Q1 2006. The rise went hand in hand with an increase in Ural/Brent differential from USD 3.58/bbl in Q2 2005 to USD 4.87/bbl in Q2 2006. In comparison with Q1 2006, the differential went up by 33.1%. Thanks to the favourable market conditions and strong demand for petroleum products, our capacity utilisation was very high: we exceeded the nameplate capacity and reached a nearly 103% utilisation rate.

The financial performance of the LOTOS Group in Q2 2006 improved markedly in comparison with the corresponding period of 2005. Net sales revenue went up by 52.1% to PLN 3,265.1m. The operating profit rose by 197.6%, and amounted to PLN 332.9m, while the net profit attributable to the parent undertaking's shareholders (i.e. net of minority interests) was PLN 276.0m, up by 221.2%.

In the first half of 2006, the consolidated sales revenue of the LOTOS Group amounted to PLN 5,954.7bn, the consolidated operating profit was PLN 463.6m, the net profit stood at PLN 412.4m, and the net profit attributable to the parent undertaking's shareholders was PLN 378.9m. Compared with the corresponding period of 2005, the sales revenue went up by 64.0%, the operating profit remained practically unchanged, the net profit declined only slightly (by 1.3%) and the net profit attributable to the parent undertaking's shareholders fell by 6.8%. The factor which had a decisive effect on the financial performance as compared with the corresponding period of the previous year was the PLN 266.6m negative goodwill (relating to the recognition of an excess of the share in net assets of the Southern Refineries and Petrobaltic acquired on February 3rd 2005 over the acquisition cost), which drove up the Q1 2005 operating profit.

If negative goodwill recognition is taken into account and the Company's H1 2005 financial results are adjusted for its impact before they are compared with the H1 2006 results, it turns out that the operating profit for H1 2006 increased by PLN 266.9m (up by 135.6%), while the net profit attributable to the parent undertaking's shareholders rose by PLN 239.0m (up by 170.8%).

Strategy for the LOTOS Group to 2012

On June 27th 2006, the Company's Supervisory Board approved the Strategy for the LOTOS Group to 2012, which provides for further growth of shareholder value through optimum utilisation of the Company's potential in three areas of its business.

- As regards production and procurement of raw materials, the Company plans to fully integrate and consolidate Petrobaltic, maximize its value, and gain direct access to foreign hydrocarbons reserves. In the Strategy the Company assumed that it would execute projects which meet appropriate financial parameters and involve an acceptable level of risk and which contribute to improved security of oil supplies by diversifying the supply sources so as to ensure that no more than 60% of total supplies come from a single source. By 2012 the LOTOS Group plans to increase its annual production in the Baltic Sea region from 300 thousand tonnes to 1m tonnes.
- In the area of oil refining, the key tool in the implementation of the Strategy will be the PKRT Project, which provides for the construction of an atmospheric and vacuum distillation unit, with a designed annual capacity of 4.5m tonnes of oil, vacuum and atmospheric residue deasphalting unit (SDA/ROSE), MHC unit (producing engine fuels components, in particular for diesel oils), and a gasification and energy production unit (IGCC) to be used for own needs. As part of the Strategy for the oil refining area, Grupa LOTOS S.A. also plans to construct a new diesel oil hydrotreating unit, which will produce diesel oils with sulphur content of 10 ppm, and to expand the capacity of the existing hydrocracking unit and units producing motor gasolines. Additionally, the Company plans to construct a new xylene fraction separation unit. The new units are to help the Gdańsk refinery to enhance its complexity ratio and increase its capacity (to 10 – 10.5m tonnes annually). They are to be placed in service successively in 2010.

- As for the marketing area, the Group plans to develop its retail sales and increase its market share to 10%, provided that the number of service stations grows to approx. 500, sales volumes at service stations increase as a result of the implementation of loyalty programmes for retail and fleet customers, and the range of products offered by the COCO stations is expanded to include a modern branded fuel. With respect to wholesale, the Company plans to achieve a market share of 30%, with the assumption that sales to business customers are increased, a market based on long-term trading contracts is developed, the annual fuel sales volume goes up from 4m tonnes to 8m tonnes in 2012, biofuels are introduced to trading, and the share in the Jet fuel market rises, e.g. as a result of offering direct deliveries to airports.

The capital expenditure required to execute the strategy is planned at up to PLN 7.3bn in 2006–2012.

In accordance with the objectives of the financial strategy, upon execution of the key strategic projects the debt to equity ratio should stay within the range of 0.3-0.4, while ROACE and the EBITDA margin should not fall below 12% and 9%, respectively. In 2012, ROACE and the EBITDA margin of Grupa LOTOS S.A. are expected to stand at 15.6% and 13.5%, respectively, whereas the debt to equity ratio, which in the peak period of the investment outlays, i.e. in 2009, should not exceed 0.8, will be reduced to 0.11. The dividend policy will be subject to the objective of optimising the financing structure of the Group. During execution of the key strategic projects, dividend payments will not exceed 10% of the net profit. Afterwards, the dividend is intended to be increased to 30% of the net profit.

Comprehensive Technical Upgrade Programme

As concerns execution of the Comprehensive Technical 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 Q2 2006 were focused on expanding the Project scope, further technical development work, and updating the financial assumptions for the Project.

Given the rapid changes in the international oil market, rising prices of oil and oil products, as well as higher costs of materials, equipment and services necessary to carry our investment projects in the oil industry, Grupa LOTOS S.A. commissioned Purvin&Gertz, an independent market consultant, to formulate updated assumptions for the financial model of the Project. Concurrently, we revised our estimates of the capital expenditure on the Project.

Having considered the modelling results based on the updated assumptions, we decided to make certain necessary changes to the structure and scope of the Project. In addition to the units originally planned to be constructed under the PKRT Project (IGCC, MHC and ROSE), a new CDU unit will be built, thanks to which we will not need to import additional feedstock for the PKRT units. Furthermore, in order to ensure a larger production of atmospheric and vacuum distillates and to meet the quality requirements which are to apply to diesel oils as of 2009 (sulphur content of 10 ppm), the Project scope was extended to include construction of a HDS unit, modernisation of the existing hydrocracking unit, and construction of storage facilities to accommodate the larger production volumes resulting from the above changes. Both production units (HDS and hydrocracker) will be constructed under a licence from Chevron Lummus Global.

Grupa LOTOS S.A. expects that upon completion of the entire investment programme based on the extended PKRT Project, the economic efficiency of oil processing will improve thanks to expansion of the processing capacity to 10.5m tonnes annually, achievement of higher conversion and desulphurisation levels, and production of fuels which meet the applicable EU quality and environmental standards. The investments related to the PKRT Project and the resulting change in production structure will be made in line with the market trends and demand patterns for particular groups of oil products.

After the FEED-PB agreement with Fluor and the UHDE/Technip consortium was signed in the first quarter of 2006, the second quarter was a time of intensive work on the development of the Front End Engineering Design for the PKRT Project and on drawing up the proposals for the Project implementation by the two companies. Currently, we are completing the tender processes for design and construction of the HDS unit and for preparation of the engineering design for the new CDU unit.

In Q2 2006, we also worked on preparing applications for subsidies for the HDS unit under the Sector Operational Programme – Enhancement of Companies' Competitiveness. The work was completed with filing an application with the Ministry of Economy in June 2006.

On June 27th 2006, the Supervisory Board of Grupa LOTOS S.A. authorised the Company to issue letters of intent, which will have the same financial effect as execution of agreements, for the provision of four reactors for the MHC unit, whose construction is part of the PKRT Project. Taking on the financial obligations related to the provision of MHC reactors is a milestone in the PKRT Project implementation schedule.

PROSTA Programme

The Company's activities in Q2 2006 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 COCO stations, in particular by incorporating the ESSO and Slovnaft service stations, acquired in 2005 and 2006, into the LOTOS network, commencing construction of two service stations in Gdynia and Tychy, and expanding the DOFO network.

In the reporting period, the Company completed the consolidation of the ESSO and Slovnaft stations with the LOTOS network. As at June 30th 2006, all 39 ESSO stations acquired in 2005 and 12 Slovnaft stations acquired under the final agreement of March 9th 2006 were incorporated into the LOTOS network. Since the acquisition, rebranding work has been carried out at the stations.

In Q2 2006, the Company added another two DOFO stations to its network and concluded four DOFO commercial partnership agreements.

As at June 30th 2006, the LOTOS network comprised 403 stations, of which 132 were CODO, 221 DODO, and 50 DOFO stations.

Petrobaltic and Production Activities

In Q2 2006, Petrobaltic continued test production on the B-8 oil field, producing over 18.3 thousand tonnes of crude oil. In Q2 2006, the production from the B-3 and B-8 oil fields totalled over 72.9 thousand tonnes of crude oil. As a result of the discontinuation – as of the end of Q1 2006 – of crude processing at LOTOS Czechowice, which had previously processed crude oil produced by Petrobaltic, almost all of the oil produced in Q2 was supplied to the refinery in Gdańsk.

Southern Refineries (LOTOS Czechowice and LOTOS Jasło)

In Q2 2006 restructuring activities were carried out to adapt LOTOS Jasło and LOTOS Czechowice to operate within the LOTOS Group.

LOTOS Biopaliwa Sp. z o.o., a subsidiary of LOTOS Czechowice established to carry out an investment project, commenced work on the construction of a plant for the production of methyl esters of fatty acids used as biodiesel additives (FAME). The turn-key contract for the execution of the investment project was concluded with MAN Ferrostal on May 22nd 2006. The provider of the technology, Novaol and Oelmühle Leer Connemann of Germany, has long-standing experience in the development of biofuel production units. The project is valued at PLN 71m. The plant, with the annual production capacity of 100 thousand tonnes, will commence production in 2008.

Also in Q2 2006, the Group completed consolidation of its maintenance activities. RCRemo Sp. z o.o. and Monto-Rem Sp. z o.o. maintenance companies were incorporated into LOTOS Serwis Sp. z o.o., which then established its branches in Czechowice-Dziedzice and Jasło.

Market Environment and Operations

Market environment in Q2 2006 was favourable both for the oil production and refining business. The average price of Brent oil stood at USD 69.58/bbl and was higher by 34.8% than in Q2 2005. Compared with Q1 2006, the oil price grew by 12.7%. The rise in oil prices in Q2 2006 was accompanied by a growing Ural/Brent differential. The Ural/Brent differential increased from USD 3.58/bbl in Q2 2005 to USD 4.87/bbl in Q2 2006. The increase on Q1 2006 amounted to 33.1%.

Q2 2006 saw an increase in the average refining margin to USD 6.80/bbl, compared with USD 4.12/bbl in Q1 2006. At the same time the Q2 refining margin increased by USD 0.96/bbl year on year. Compared with Q1 2006, the crack margins for all the key oil products increased in Q2 2006. The crack margin for gasoline grew by 82.8%, for diesel oil – by 15.8%, for light fuel oil – by 14.7%, and for jet fuel – by 12.5%. Over the same period the margin on heavy fuel oil dropped by 20.4%. Compared with Q2 2005, Q2 2006 saw an increase in crack margins for gasolines and light fuel oil, by 57.2% and 3.1%, respectively, while the crack margins for diesel oil, jet fuel and heavy fuel oil decreased by 14.2%, 0.5% and 33.3%, respectively.

In Q2 2006, the Gdańsk Refinery processed 1,537.6 thousand tonnes of oil, thus reaching 102.7% of its designed capacity. The refinery processed 1,479.9 thousand tonnes of Ural crude, which accounted for 96.2% of total crude oil processed by the refinery. The balance was comprised of the Rozewie oil produced by Petrobaltic – 42.9 thousand tonnes (2.8% of the processing volume) and imported SLEIPNER oil condensate – 14.8 thousand tonnes (1.0% of the processing volume). In Q2 2006, the LOTOS Group sold 371 thousand tonnes of motor gasolines, 623 thousand tonnes of diesel oil, 89 thousand tonnes of light fuel oil, 136 thousand tonnes of heavy fuel oil, 109 thousand tonnes of jet fuel, and 364 thousand tonnes of other products.

In Q2 2006, employment at the LOTOS Group rose to 5,547 staff and was higher by 46 persons compared with Q1 2006. The increase resulted from the service station network development carried out by LOTOS Paliwa, and an increase in the number of employees at the LOTOS Group Production Division, related to a planned change in the organisation of working time, as well as from business expansion by LOTOS Parafiny.

Review of the Consolidated Results of the LOTOS Group for Q2 2006

Profit and Loss Account

In Q2 2006, the consolidated sales revenue of the LOTOS Group reached PLN 3,265.1m and was up by 52.1% on Q2 2005. The increase was driven mainly by 53.6% higher sales volume reported by the parent undertaking (Grupa LOTOS S.A.) and higher unit selling prices. The cost of sales in Q2 2006 stood at 2,700.8m, having gone up by 46.6% on the 2005 figure. As a result, the net profit on sales in Q2 2006 increased to PLN 564.2m and was higher by 86.1% relative to Q2 2005.

The increase in selling costs to PLN 149.1m in Q2 2006, or by 18.9% compared with the previous year figure, was driven mainly by higher sales volume. The Q2 2006 consolidated operating profit amounted to PLN 332.9m and was up by PLN 221.1m on the Q2 2005 figure.

The Q2 2006 profit before tax amounted to PLN 362.6m, which represents an increase of PLN 253.4m (231.9%) year on year. The Q2 2006 profit before tax was driven up by the PLN 29.8m positive balance on financial activities.

The Q2 2006 net profit amounted to PLN 294.8m, which means an increase of PLN 198.3m relative to Q2 2005. The profit of the parent undertaking's shareholders, net of profit attributable to minority interests, reached PLN 276.0m.

On a semi-annual basis, the H1 2006 consolidated sales revenue reached PLN 5,954.7bn, the operating profit amounted to PLN 463.6m, the net profit stood at PLN 412.4m, and the net profit attributable to the parent undertaking's shareholders was PLN 378.9m. Compared with the corresponding period of the previous year, the revenue was up by 64.0%, the operating profit remained virtually unchanged, the net profit declined slightly, by 1.3%, and the net profit attributable to the parent undertaking's shareholders fell by 6.8%. The above results were driven mainly by the negative goodwill of PLN 266.6m, which increased the Q1 2005 operating profit and was related to the recognition of an excess of the share in net assets of the Southern Refineries and Petrobaltic (acquired on February 3rd 2005) over their acquisition cost.

After considering the aforementioned negative goodwill recognition and adjusting the Company's H1 2005 financial results for the impact of the negative goodwill recognition, a comparison of the adjusted results with the H1 2006 results shows that the H1 2006 operating profit grew by PLN 266.9m (up by 135.6%) and the net profit attributable to the parent undertaking's shareholders went up by PLN 239.0m (up by 170.8%).

Balance Sheet

As at June 30th 2006, the balance-sheet total was PLN 7,620.8m, up by PLN 631.2m on December 31st 2005. The increase was driven by a PLN 191.0m rise in tangible fixed assets, a PLN 266.9 growth in trade receivables, and a PLN 182.8m increase in inventories, attributable to higher prices of raw materials and products and higher sales volume. At the same time, in H1 2006 current financial assets declined by PLN 121.0m.

As at June 30th 2006, the equity amounted to PLN 5,219.8m. The PLN 411.6m increase in equity recorded in H1 2006 resulted chiefly from a PLN 378.9m growth in retained earnings and a PLN 30.9m growth in minority interests.

Non-current liabilities rose slightly in H1 2006 as a result of an increase in loans and borrowings, and amounted to PLN 717.2m as at the end of June 2006. During the first six months of 2006, current liabilities also grew by PLN 218.2m and reached PLN 1,683.8m as at the end of the period. The increase was driven mainly by higher prices of raw materials and increased capacity available to the Company. The structure of external capital changed as there was a slight increase in the share of current liabilities and a decline in the share of non-current liabilities.

Cash Flows

As at the end of Q2 2006, cash balance amounted to PLN 827.0m, having increased by PLN 266.1m relative to the balance as at the end of Q2 2005.

In Q2 2006, net cash provided by operating activities amounted to PLN 334.5m, up by PLN 63.9m on the amount of net cash flows provided by operating activities in Q2 2005. The increase in Q2 2006 was driven primarily by the net profit of PLN 294.8m earned in Q2 and an increase in liabilities of PLN 183.7m.

In Q2 2006, net cash used in investing activities amounted to PLN 13.1m, and changed by PLN 748.2m relative to Q2 2005, when net cash used in investing activities stood at PLN 761.3m. The substantial difference between net investing cash flows in Q2 of the current and previous year was caused by significant spending on purchases of non-current and current financial assets in Q2 2005, related to short-term placements of the proceeds from the public offering of Grupa LOTOS S.A. shares and the acquisition of shares in the Southern Refineries and Petrobaltic. In Q2 2006, the balance of non-current financial assets sold and purchased was close to zero.

In Q2 2006, net cash used by the LOTOS Group in financing activities amounted to PLN 72.0m. The negative cash flows from financing activities were driven primarily by the repayment of loans and borrowings. In the corresponding period of 2005, the LOTOS Group's financing activities generated a substantial amount of net cash, which was mainly due to the issue of the Company shares.

Q2 and H1 2006 Operating Profit/Loss of the LOTOS Group by Business Segment

The operating activities of the LOTOS Group are divided into four business segments: crude oil production, refining and marketing, retail network, and other business. A detailed description of the business segments is provided in the Directors' Report on the Financial Results of the LOTOS Group in Q1 2006.

The sales revenue and operating expenses of the individual business areas are presented before eliminations of transactions between business segments.

The adjustments related to the results on intra-group transactions were appropriately allocated to the business segment which acts as the seller in a given transaction.

(PLNm)	Business segments							
	Crude oil production		Refining and marketing		Retail		Other business	
	Q2 2006	H1 2006	Q2 2006	H1 2006	Q2 2006	H1 2006	Q2 2006	H1 2006
Sales revenue	124	206	3 225	5 887	262	464	65	128
Operating expenses	(51)	(80)	(2 922)	(5 504)	(275)	(485)	(61)	(115)
Adjustments	(35)	(37)	(1)	(1)	1	1	-	(1)
Operating profit	38	89	302	382	(12)	(20)	4	12
Amortisation and depreciation	10	21	53	106	11	17	2	4

Source: LOTOS Group.

Crude Oil Production

The Q2 2006 revenue on crude oil production was PLN 124m. Net of the operating expenses of PLN 51m and after adjustments, the operating profit amounted to PLN 38m, and earnings before interest, depreciation, income tax and amortization (EBITDA) reached PLN 48m.

The key driver of the Q2 2006 revenue in the production segment was the rise in light crude oil prices on international markets, as these provide the basis for calculation of the price of Rozewie crude produced by Petrobaltic and purchased by the LOTOS Group. In Q2 2006, the average price quoted for the Brent oil was 69.58 USD/bbl, up by 12.7% on Q1 2006 and 34.8% on Q2 2005. The Q2 2006 results of the crude oil production business were significantly affected by the fact that despite the significant increase in Petrobaltic's crude oil production to 72.9 thousand tonnes, due to the physical and chemical properties of the Rozewie crude a significant portion of the oil produced by Petrobaltic was stored by the LOTOS Group to be processed in winter. This caused an adjustment to a portion of the margin in the upstream segment in Q2 2006. Petrobaltic's actual production in Q2 2006 rose by 21.5% relative to the corresponding period of 2005.

Refining – Production and Marketing

In Q2 2006, the refining segment generated sales revenue of PLN 3,225m, operating profit of PLN 302m, and earnings before interest, depreciation, income tax and amortization (EBITDA) of PLN 355m. The segment's operating margin in Q2 2006 was 9.4%, while the EBITDA margin was 11.0%.

The refining segment's operating profit for Q2 2006 was determined to a large extent by market conditions. The Ural/Brent differential increased by 33.1% relative to Q1 2006 and by 36.0% relative to the corresponding period of the previous year, and amounted to USD 4.87/bbl. The refining margin stood at USD 6.8/bbl, up by 65.0% relative to Q1 2006 and 16.4% compared with Q2 2005. At the same time, in Q2 2006 crack margins for all the key refining products increased relative to Q1 2006. Significant increases were recorded in crack margins for gasolines (up by 82.8%), diesel oil (up by 15.8%), light fuel oil (up by 14.7%) and jet fuel (up by 12.5%).

Important factors with a positive impact on the refining segment's performance in Q2 2006 included the high utilisation rate of the refining capacity and the favourable product portfolio structure. Due to the significant demand for oil products, in Q2 2006 the LOTOS Group sold record volumes of refining products, reaching 1,692.0 thousand tonnes, while the utilisation of the designed processing capacity (6m tonnes annually) reached 102.7% (the Gdańsk Refinery processed 1,537.6 thousand tonnes of oil). As the Group entered the spring/summer season, there was a radical switch in the product portfolio, both in volume and value terms. In volume terms, in Q2 2006 there was a 28.0% drop in sales of light fuel oil, a 65.7% decline in heavy fuel oil, with a concurrent substantial increase of 34.5% in sales of jet fuel and an impressive 1,342.1% growth in sales of bitumens, compared with Q1 2006.

Retail Operations (Service Stations Network)

In Q2 2006, sales revenue in the retail segment amounted to PLN 262m. The segment reported operating loss of -PLN 12m and negative EBIDTA of -PLN 1m.

The operating loss of the retail segment was significantly affected by the retail margins at CODO stations, which grew by 9.4% versus Q1 2006, however fell by 10.9% Q2 2005. In Q2 2006, the average annual throughput was 2.4m litres at the CODO stations and 1.5m litres at the DOFO stations.

The disappointing financial performance in the retail segment is mainly due to the restructuring and upgrading work being undertaken at the LOTOS service stations, and is also related to the cost of operational acquisition of the ESSO and Slovnaft stations and the cost of preparing the loyalty programmes which will be launched by the end of 2006.

As at the end of Q2 2006, the number of COCO/CODO stations was 132, the number of DOFO stations reached 50, and the number of DODO stations fell to 221.

Other Business

In Q2 2006, the sales revenue on other business reached PLN 65.0m, the segment's operating profit was PLN 4.0m, and EBITDA amounted to PLN 6.0m.

<u>Impact of the LIFO Inventory Valuation on the Q2 and H1 2006 Consolidated Results of the LOTOS Group</u>

Presented below is information on the impact of the LIFO (last in, first out) inventory valuation method on the consolidated operating profit of the LOTOS Group for Q2 2006 and H1 2006.

In line with its inventory valuation policies, the LOTOS Group uses the weighted average of the acquisition cost to measure decrease in inventories. This method of stock valuation defers the effects of changes in oil prices on the prices of finished products. Thus, an increase in oil prices on the global market has a positive impact on the financial performance of the Group, while a decrease drives such performance down. The operating profit accounting for the impact of this valuation method is presented as item 1 in the table below.

The consolidated operating profit of the LOTOS Group for Q2 2006 and H1 2006 accounting for the estimated impact of using the LIFO method for inventory valuation (along with the comparable data for Q2 2005 and H1 2005) is presented as item 2

No.	(PLNm)	Q2 2006	Q2 2005	Change	H1 2006	H1 2005	Change
1.	**Operating profit**	332.9	111.9	197.6%	463.6	463.4	0.1%
2.	**Operating profit (LIFO method)**	253.3	4.6	5 447.5%	363.4	316.1	15.0%

Source: LOTOS Group.

It should be noted that the negative goodwill of PLN 266.6m (connected with the purchase of shares in the Southern Refineries and Petrobaltic on February 3rd 2005) posted in Q1 2005 and increasing the operating profit had a significant positive effect on the H1 2005 results (i.e. the operating profit calculated using the weighted average of the acquisition cost and the LIFO method).

The assumptions made in calculating the Q2 and H1 2006 operating profit of the LOTOS Group accounting for the estimated impact of using the LIFO method for inventory valuation (along with the comparable data for Q2 and H1 2005) are described in Current Report No. 29/2006.