Grupa LOTOS Management's Discussion and Analysis of Q2 2020 consolidated results

This is the translated version of a document originally issued in Polish

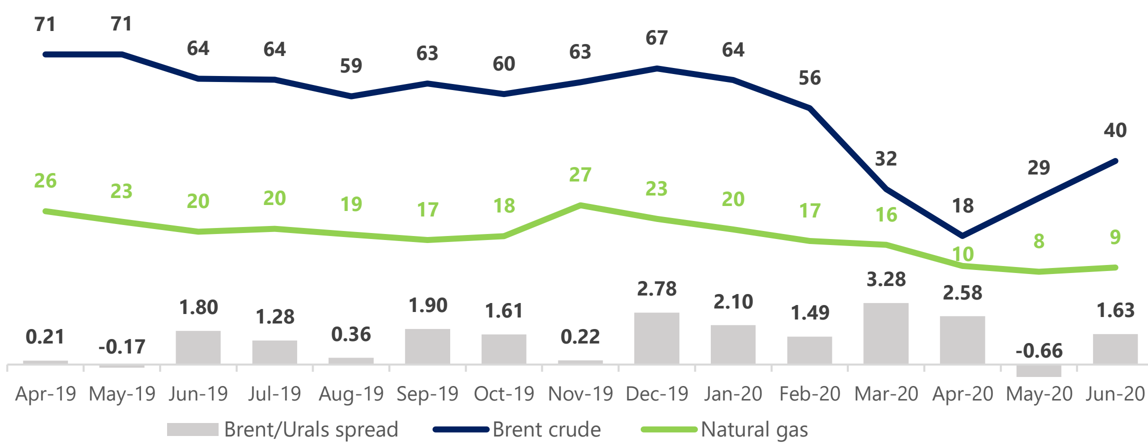
ISIN	Stock Exchange	Thomson Reuters	Bloomberg
PLLOTOS00025	LTS	LTSP.WA	LTS PW

An excel file with the operating and financial data for Q2 2020 and the previous reporting periods is published in the Investor Relations section of our website at→ https://inwestor.lotos.pl/en/ as → databook

MARKET ENVIRONMENT

- High volatility of crude oil prices in the reporting quarter; crude oil prices down year on year and quarter on quarter, by USD 39.26/bbl[1] and UDS 20.84/bbl, respectively; significant price depression in April 2020 (to USD 18/bbl on average)
- Further slide in natural gas prices, by ca. 60.3% (13.62USD /boe) year on year,[2] and 49.5% (-8.77 USD/boe) quarter on quarter
- Decrease in crack spreads[3] for diesel oil year on year (down by 31.9%, or USD -4.47/bbl) and quarter on quarter (down by 40.7%, or USD 6.56/bbl)), and for motor gasoline year on year (down by 76.7%, or USD 10.28/bbl) and quarter on quarter (down by -59.0% or USD 4.5/bbl)
- Narrowing of quarterly average diesel oil and heavy fuel oil crack spread year on year (down by 36.65%, or USD 7.89/bbl) and quarter on quarter (down by 52.32%, or USD 14.89/bbl)
- Year-on-year narrowing of quarterly average Brent/Urals spread, from USD 0.58/bbl to USD 0.05/bbl
- Year-on-year appreciation of the USD/PLN average quarterly exchange rate to PLN 4.09 (by PLN +0.28)

Figure 1. Brent prices (USD/bbl), natural gas prices (USD/boe) and the Brent/Urals spread (USD/bbl)



Source: Refinitiv.

Table 1. Brent crude prices, Brent/Urals spread and gas prices (USD/bbl)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
DATED Brent FOB prices	29.70	50.54	68.96	-41.2%	-56.9%
Brent/Urals spread	0.05	2.31	0.58	-97.8%	-91.4%
UK NBP natural gas prices[4]	8.95	17.72	22.57	-49.5%	-60.3%

Source: Refinitiv.

[1] Bbl – barrel of crude oil.
[2] Boe – barrel of oil equivalent
[3] Product crack spread is calculated as the difference between the price per barrel of a given product (price per tonne computed using the appropriate density factor) and the price of Urals crude (the Brent crude price adjusted for the Brent/Urals spread).
[4] To ensure comparability, the UK NBP natural gas prices were converted from USD/MWh to USD/boe using the conversion factor of 1.6282 MWh/boe.

Table 2. Product crack spreads (USD/bbl)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Motor gasoline	3.13	7.63	13.41	-59.0%	-76.7%
Naphtha	-2.50	-2.14	-8.93	16.8%	-72.0%
Diesel oil (10 ppm)	9.54	16.10	14.01	-40.7%	-31.9%
Light fuel oil	7.58	14.05	11.99	-46.0%	-36.8%
Aviation fuel	1.40	13.24	13.34	-89.4%	-89.5%
Heavy fuel oil	-4.03	-12.36	-7.41	-67.4%	-45.6%

Source: Refinitiv.

Table 3. USD/PLN exchange rates

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
PLN/USD exchange rate at end of period	3.98	4.15	3.73	-4.1%	6.7%
Average PLN/USD exchange rate	4.09	3.92	3.81	4.3%	7.3%

Source: National Bank of Poland.

Key external factors driving the LOTOS Group's performance in Q2 2020:

- Feedstock and products

  Refining & Marketing segment:

  The sizeable year-on-year drop in crack spreads for diesel oil and gasoline, further significant fluctuations and declines in crude oil and petroleum product prices, and lower demand due to constraints caused by the Covid-19 pandemic, adversely affected the Refining & Marketing segment's operating result: at the adjusted LIFO-based EBITDA level it came in at PLN 14.8m, down 97.5% year on year. The continuing downtrend in crude oil prices caused a material decrease in the operating result reported using the weighted average cost method. On the other hand, refining costs were down on a year-on-year decline in the price of natural gas used by the Company's refinery. The price of crude oil processed into products and used in the processing operations (consumed internally) was also down.

  A decrease in the differential between the diesel oil and heavy fuel oil crack spreads in Q2 2020 to USD 13.57/bbl (or 36.65% year on year and 52.32% quarter on quarter) affected the profitability of the Grupa LOTOS refinery's product mix, which changed after new EFRA units had been integrated into the existing refinery set-up (a shift towards a higher share of diesel oil (up 5.68pp year on year, to 53.60%) and less heavy fuel oil (down 7.79pp, to 10.04%) in the refinery's total yields). These factors translated into the Refining & Marketing segment's Q2 2020 adjusted LIFO-based EBITDA of PLN 14.8m. In Current Report No. 22/2020, the Company reported the occurrence in the LIFO valuation of the effect of old oil inventories, resulting from the use of inventories from previous periods, measured at much higher unit cost than that in Q2 2020. With the marked decline in crude oil prices in Q2 2020, that effect reduced the adjusted LIFO-based operating result by approximately PLN -369m.

  Exploration & Production segment:

  A further marked year-on-year drop in the UK National Balancing Point prices of natural gas (down 60.3%) and a 56.9% year-on-year decline in crude oil prices had an adverse effect on the Exploration & Production segment's performance. As a result, the segment's adjusted EBITDA came in at PLN 46.4m (down 74.0% year on year).

- Exchange rates

  An increase in the average USD/PLN exchange rate in the quarter (up +7.3% year on year) had a positive effect on crack spreads and thus on the operating performance of both reporting segments.

- Covid-19 pandemic

  In Q2 2020, the Company's market environment was highly volatile and unpredictable. The Company has been operating in an environment prone to rapid changes triggered by the pandemic and by measures taken to contain its impact, both in Poland and globally.

  They have upset the balance and disrupted the flows of international trade, including trade in goods and services, and passenger traffic has fallen markedly. Restrictions have been imposed on both air and road transport. Many countries have maintained restrictions on human mobility, use of services, retail outlets, institutions of culture and schools. Borders have been closed for tourist traffic and migrant workforce. In Q2 2020, the state of epidemic threat continued in Poland, with the above mentioned restrictions, which were gradually relaxed starting from April 20th 2020. Their negative impact on the Polish fuel market was the strongest in Q2 2020, resulting in a substantial decline in volumes of gasoline and LPG sold through the retail channel (service station chain). Border closures brought about a significant decrease in the consumption of aviation fuel. Given the lower domestic fuel consumption, part of the Grupa LOTOS products was exported.

  In addition, the narrowing of the diesel oil vs heavy fuel oil crack spread on global markets, coupled with deteriorated macroeconomic conditions for the refining industry in the reporting period, suppressed marginal refining margin on the EFRA project below the level assumed by the Company (i.e. below USD 2 per barrel).

EXPLORATION & PRODUCTION

- Hydrocarbon production at 20.8 thousand boe/d (up by some 10% year on year and down by 12% quarter on quarter)
- Increase in production from the B3 field as a result of the ongoing workover programme
- Segment's adjusted EBITDA at PLN 46.4m (down 74% year on year)

Crude oil and natural gas reserves, production and total sales

Table 4. Crude oil and natural gas reserves (mboe)[5]

	Jun 30 2020	Mar 31 2020	Jun 30 2019
Norway	27.7	29.1	34.7
Poland	47.0	47.5	48.7
Lithuania	2.6	2.6	2.8
Total	77.3	79.2	86.3

Source: the Company.

Table 5. Daily production (boe/d)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Norway	15,091	18,043	13,856	-16.4%	8.9%
Poland	5,177	4,871	4,335	6.3%	19.4%
Lithuania	549	626	691	-12.2%	-20.5%
Total	20,817	23,539	18,882	-11.6%	10.2%

Source: the Company.

Table 6. Quarterly production (boe)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Norway	1,373,306	1,641,873	1,260,900	-16.4%	8.9%
Poland	471,069	443,229	394,514	6.3%	19.4%
Lithuania	49,997	56,940	62,850	-12.2%	-20.5%
Total	1,894,372	2,142,042	1,718,264	-11.6%	10.2%

Source: the Company.

[5] 2P – proved and probable reserves (SPE-PRMS classification).

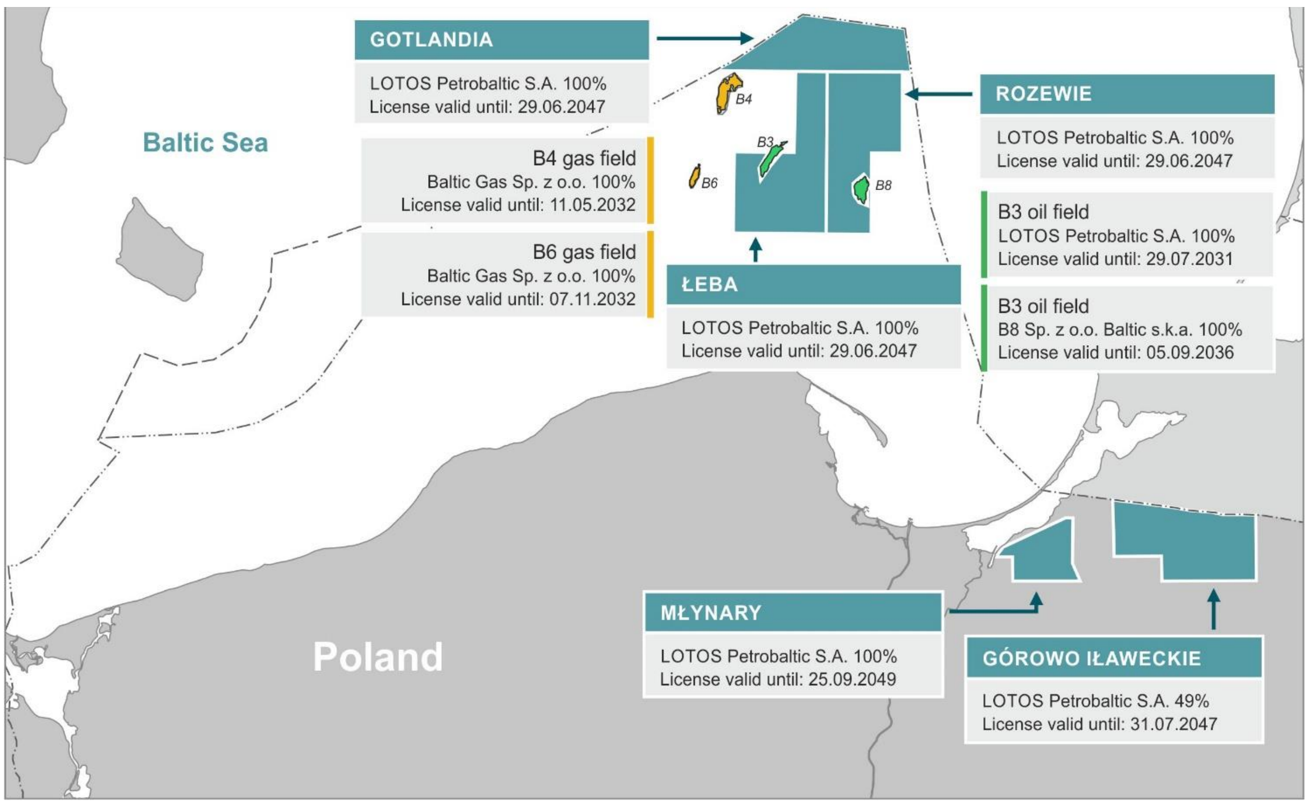
Table 6. Oil and gas sales (boe)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Norway	1,720,588	1,627,950	1,274,351	5.7%	35.0%
Poland	516,195	316,796	421,378	62.9%	22.5%
Lithuania	46,598	92,790	47,105	-49.8%	-1.1%
Total	2,283,381	2,037,536	1,742,834	12.1%	31.0%

Source: the Company.

Exploration and production activities in Poland

Map 1. Licences held by LOTOS Group companies in Poland as at June 30th 2020



Source: the Company.

In Q2 2020, LOTOS Petrobaltic S.A. ("LPB") continued to produce crude oil and associated natural gas from the B3 field in the Baltic Sea at an average rate of 1,364 boe/d (up by 9% year on year and 25% quarter on quarter). The increase in production was achieved as a result of the ongoing workover programme on the B3 field. In particular, in Q2 2020, the workover was completed and production was resumed from the B3-15B well, and workover activities were started at the PG-1 unmanned platform location: the B3-8 production well was brought online and workover was commenced on the B3-13B production well (brought online on July 2nd 2020).

B8 project

Development of a crude oil field in the Baltic Sea

In Q2 2020, crude oil and associated natural gas were being produced from the B8 field at an average rate of 3,813 boe/d. In paralel, work continued to start up further process units of the production hub. The water injection system components were delivered to the production hub site and assembly work was commenced. Preparatory work was also carried out to launch a gasfired steam generator. The possibility of completing the work, including the mobilisation of foreign services to carry out final start-up activities, was significantly limited by the Covid-19 situation.

Key parameters of the B8 project (for the LOTOS Group interest):

- LOTOS Group interest 100%
- 2P reserves 34.0 mboe as at June 30th 2020 (91% crude oil, 9% natural gas)
- current output 3.8 thousand boe/d (Q2 2020)
- full capacity of the production hub: Q4 2020
- expected average output 5.0 thousand boe/d (for 5-year period from full-scale production launch).

B4/B6 development project
Development of natural gas fields in the Baltic Sea

The B4/B6 project consists in the development of natural gas deposits in the Baltic Sea, in partnership with CalEnergy Resources Poland Sp. z o.o. As at June 30th 2020, an impairment loss of PLN 114.5m was recognised on the investment in the B4/B6 fields. The difficult conditions caused by the Covid-19 pandemic coupled with the sharp declines in commodity prices were far from conducive to the taking of the final investment decision.

Key parameters of the B4/B6 project (for the LOTOS Group interest):

- LOTOS Group interest 51%
- 2C resources[6] 17.9 mboe as at June 30th 2020 (74% natural gas, 26% NGL)
- Final investment decision depending on market developments

Exploration projects
As part of exploration activities in:

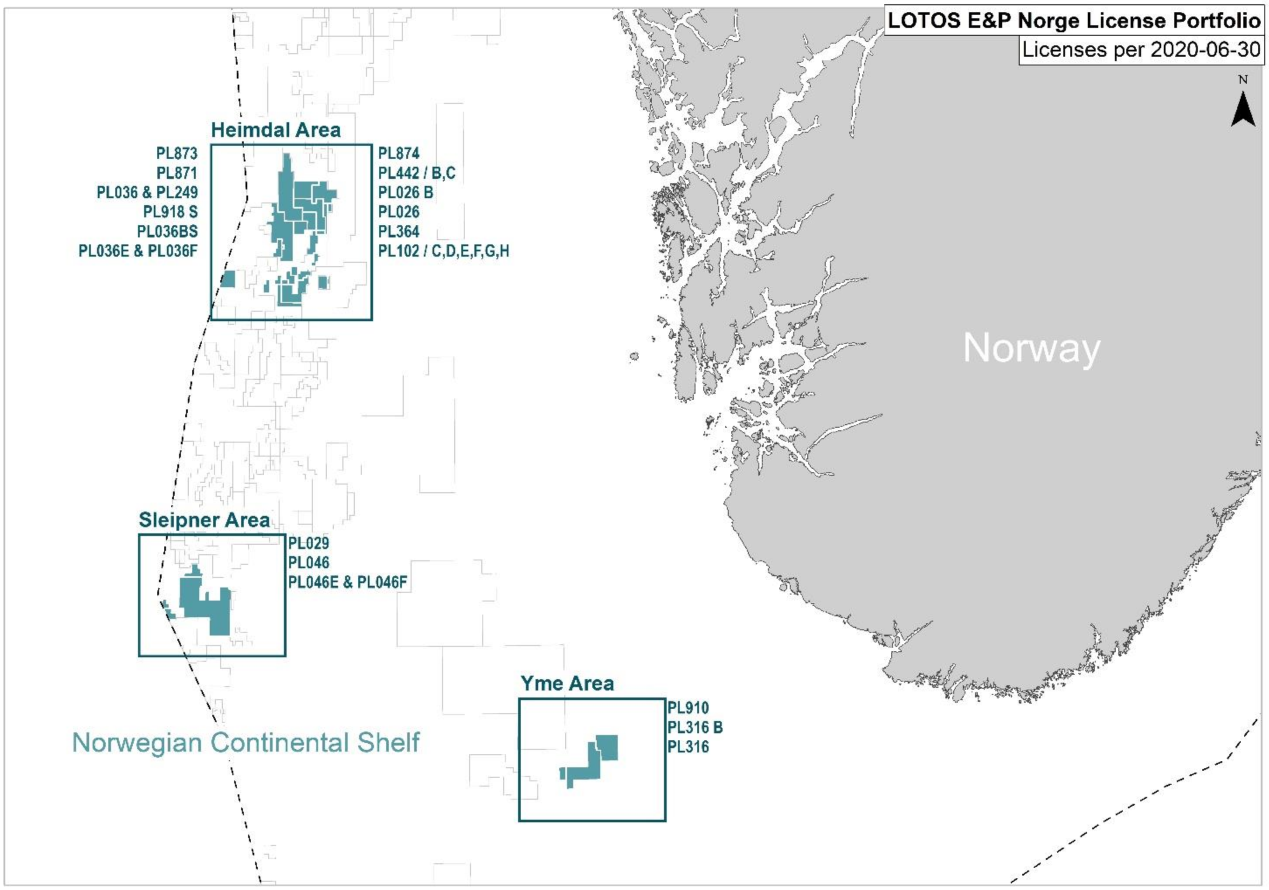
- the Gotland, Łeba and Rozewie offshore licence areas (LPB interest: 100%) – work was under way to develop a regional structure and tectonic model, including work related to the pelo structural analysis, analysis of fault integrity and petrophysical model;
- Młynary onshore licence area (LPB interest: 100%) – an attachment to the plan of geological operations for 3D seismic surveys was being developed, and in parallel the drafting of relevant graphic attachments began and the boundaries of the planned 3D seismic imaging were being analysed;
- Górowo Iławeckie onshore licence area (PGNiG operator interest: 51%, LPB interest: 49%) – work is under way on a joint decision to proceed to the exploration drilling stage.

Growth initiatives
Activities were initiated as part of the strategy to develop comprehensive and specialist services related to maritime logistics and to the potential development of the wind power segment.

[6]Contingent resources prior to PDO approval.

Exploration and production activities in Norway

Map 2. Licences held by LOTOS Exploration & Production Norge AS as at June 30th 2020



Source: the Company.

At the end of Q2 2020, LOTOS Norge held interests in 29 licences for exploration, appraisal and production of hydrocarbon reserves in the Norwegian Continental Shelf. LOTOS Norge, operating as part of a consortium, produces natural gas and condensate from fields located in the Heimdal and Sleipner areas (including the Utgard field brought on stream in Q3 2019). The average output of the Norwegian assets in Q2 2020 was 15.1 thousand boe/d (up 9% year on year and down 16% quarter on quarter). The quarter-on-quarter decline in production was due mainly to a strong downward trend in the Utgard field (down 28% quarter on quarter), where output was smaller than expected because of high volumes of water in the production wells.

At the same time, LOTOS Norge is engaged in efforts to develop new fields in Norway. Their status as at the end of Q2 2020 is presented below:

YME project
Development of an oil field in Norway

The YME project is at an advanced development stage. In Q2 2020, work was continued to convert the Maersk Inspirer platform, which will be used for production from the field. The operator (Repsol) received approval from the market regulator, Petroleum Safety Authority (PSA), to use the platform on the YME field. In addition, the Company is seeing a gradual relaxation of the Covid-19 pandemic restrictions, as well as increased availability of foreign subcontractors as mobility restrictions are being cancelled (including the planned abolition of the mandatory 10-day quarantine for those arriving in Norway from the European Economic Area countries as of July 15th 2020). The easement of the restrictions is important for the commissioning of the systems on the converted platform, and opens a chance for accelerating completion of a part of work at the Egersund shipyard. The operator currently assumes that the platform conversion work at the shipyard will be completed and the onshore completion status will be reached in Q4 2020, and production from the field will begin in Q3 2021. LOTOS' position is more conservative, with Q4 2021 estimated as the most likely time of starting production from the YME field, as reported in Current Report No. 7/2020. The project schedule may be affected by another wave of new Covid-19 cases and reinstatement of the pandemic-related restrictions, as well as extended time of work at sea related to the installation of the platform and the launch of production systems dependent on weather conditions.

Key parameters of the Yme project (for the LOTOS interest):

- LOTOS interest 20%
- 2P reserves 12.7 mboe as at June 30th 2020 (100% crude oil)
- production to be launched in Q4 2021
- expected average output 5.0 thousand boe/d (for 5-year period from production launch).

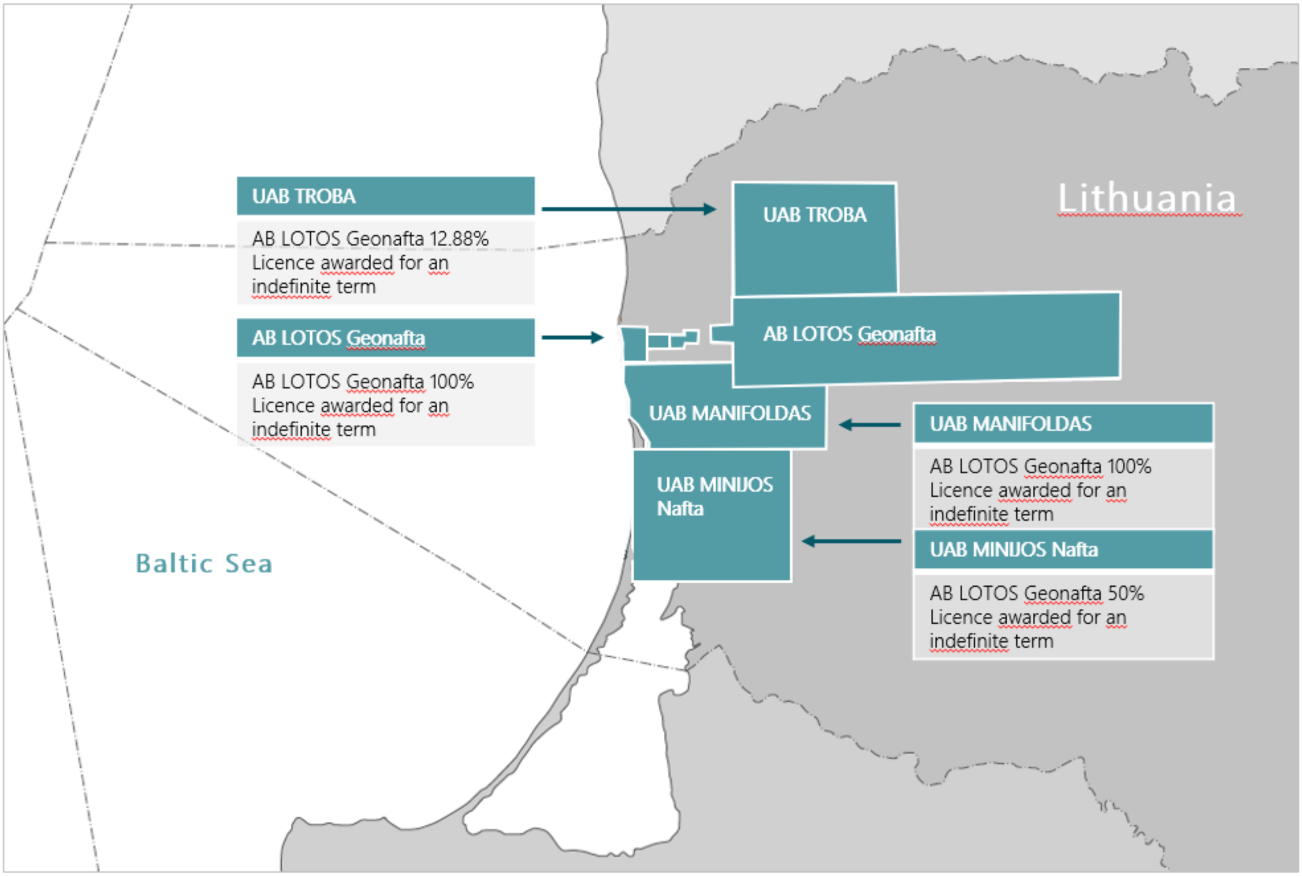
New growth projects

The development activities include development of fields north of the Heimdal hub as part of the NOAKA project. The NOAKA project involves the development of discoveries north of Heimdal: Frigg Gamma Delta, Langfjellet, Rind, Fulla and Froy, in which LOTOS holds an average interest of 10% and AkerBP is the operator, as well as the Krafla and Askja fields, where LOTOS currently has no interests and Equinor is the operator. In Q2 2020, a significant project milestones was reached – on June 11th 2020, AkerBP and Equinor entered into an agreement on the commercial terms of the project, which will be the basis for proceeding to the preparation of the Plan for Development and Operations (PDO). Submission of the PDO to the Norwegian authorities for approval is expected by the end of 2022. The agreement was triggered by a package of new tax reliefs introduced by Norway. The package offers potential for economically effective development of the NOAKA fields even if the low prices of crude oil were to continue on the market.

NOAKA will be one of the key development projects on the Norwegian Continental Shelf, with a total potential of more than 500 mboe of recoverable reserves (100% interest). For the LOTOS Group, the project will be a foundation for long-term development in Norway, in cooperation with key operators on the NCS: AkerBP and Equinor.

Exploration and production actvities in Lithuania

Map 3. Licences held by the AB LOTOS Geonafta Group as at June 30th 2020



Source: the Company.

In Q2 2020, companies of Lithuania's AB LOTOS Geonafta Group focused on optimising production from their existing onshore oilfields located in the following licence blocks: Girkaliai, Genciai, Kretinga, Nausodis, Klaipėda, and Gargždai. The output of the Lithuanian assets in Q2 2020 was 549 boe/d (down by 20% year on year and 12% quarter on quarter).

Table 7. Exploration & Production segment's key financial data (PLNm)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Revenue	213.2	329.3	307.4	-35.3%	-30.6%
EBIT	-474.9	-197.9	128.7	140.0%	-469.0%
Depreciation and amortisation	82.5	86.1	49.6	-4.2%	66.3%
EBITDA	-392.4	-111.8	178.3	251.0%	-320.1%
Adjusted EBIT[7]	-36.1	98.1	128.7	-136.8%	-128.0%
Adjusted EBITDA[8]	46.4	184.2	178.3	-74.8%	-74.0%

Source: the Company.

The year-on-year decline in the Exploration & Production segment's revenue in Q2 2020 (down 30.6% year on year and 35.3% quarter and quarter) was mainly attributable to falling natural gas prices (down 60.3% year on year and 49.5% quarter on quarter) and lower Brent Dtd crude prices (down 56.9% year on year and 41.2% quarter on quarter) The above effects were partly offset by an increase in the average USD/PLN exchange rate in the quarter (up 7.3% year on year and 4.3% quarter on quarter) and higher hydrocarbon sales volumes (up 31.0% year on year and 12.1% quarter on quarter).

The Exploration & Production segment's adjusted EBITDA for Q2 2020 fell by 74.0% on Q2 2019 and by 74.8% on Q1 2020.

[7] EBIT and EBITDA adjusted for one-off items:

in Q2 2020 (PLN -438.8m): impairment losses on the YME, Utgard, B3, and B8 field assets of PLN -129.8m, PLN 55.5m, PLN 118.3m and PLN -135.0m, respectively;

in Q1 2020 (PLN -296m): impairment losses on the YME, Utgard and Lithuanian field assets of PLN -223.6m, PLN -53.4m and PLN -19.0m, respectively.

REFINING & MARKETING SEGMENT

- Almost full utilisation of the Grupa LOTOS refinery's capacity maintained despite a significant decline in domestic demand and uncertainties in the oil market caused by Covid-19
- Adjusted LIFO-based EBITDA of the Refining & Marketing segment at PLN 14.8m, reduced by the effect of old oil inventories (measured at much higher unit cost, estimated at some PLN -369m)

Table 8. Crude oil throughput ('000 tonnes)[8]

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Crude oil throughput	2,540.8	2,597.9	2,749.5	-2.2%	-7.6%

Source: the Company.

In Q2 2020, crude oil throughput at the Company's refinery was 2,540.8 thousand tonnes, down by 2.2% quarter on quarter due to the scheduled maintenance shutdown of the DCU unit in June.

Given the extremely strong volatility of the macro environment triggered by the Covid-19 pandemic and destabilisation on the crude oil market, intensive optimisation efforts were being undertaken to align the Company's product yields with market conditions. The Company used the technological flexibility of its refining units to adjust its product yields to the market demand. Moreover, given the Grupa LOTOS refinery's location on the sea coast, it was possible to quickly offset the adverse changes in demand on the domestic market with increased volumes of exports by sea, allowing the LOTOS refinery to maintain higher crude throughput levels and optimise refining margins in the peak period of the Covid-19 pandemic.

Demand for petroleum products shrank significantly in April as a result of population mobility restrictions and border closures. From the beginning of May, fuel sales levels gradually returned to the levels seen prior to the Covid-19 pandemic. Increased domestic travel supported growth of demand for gasoline. Also, the continuing restrictions in international air traffic and greater interest in holidays at home brought a significant drop in the consumption of aviation fuel.

In Q2 2020, Grupa LOTOS continued a few business development projects of a smaller scale. The most advanced was the Hydrogen Recovery Unit (HRU) project, whose purpose is to increase the production of hydrogen, LPG and naphtha in the refinery's total yields pool, was completed in 99%. Its commissioning date was postponed to the second half of 2020 due to difficulties related to the pandemic and technical issues.

Seeking to expand its capacity to dispatch fuels from the refinery, the Company was moving forward with the project to construct a railway loading facility, scheduled to be placed in service at the end of 2020 or at the beginning of 2021.

[8]The difference between the volume of crude oil processed and the refinery's output of products stems from the fact that, apart from crude oil, the processing units and finished product blenders receive biocomponent streams, enhancing additives and middle distillates purchased from third-party suppliers.

Table 9. Refining output structure ('000 tonnes)[9]

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q2 2019	Q2 2020 / Q2 2019
Gasolines	374.4	392.0	371.1	-4.5%	0.9%
Naphtha	155.6	135.8	131.1	14.6%	18.7%
Diesel oils	1,478.3	1,407.4	1,407.4	5.0%	5.0%
Light fuel oils	47.2	74.4	45.2	-36.5%	4.5%
Jet fuel	21.0	150.0	118.3	-86.0%	-82.2%
Heavy products[10]	276.8	229.4	523.6	20.7%	-47.1%
Petcoke	69.5	79.3	0.0	-12.4%	-
Other[11]	335.1	368.4	339.9	-9.0%	-1.4%
Total	2,757.9	2,836.6	2,936.6	-2.8%	-6.1%

Source: the Company.

Table 10. Sales structure in the Refining & Marketing segment ('000 tonnes)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Gasolines	393.3	409.7	386.1	-4.0%	1.9%
Naphtha	155.6	135.8	131.1	14.6%	18.7%
Diesel oils	1,516.9	1,437.7	1,468.3	5.5%	3.3%
Light fuel oils	46.3	72.4	41.9	-36.0%	10.5%
Jet fuel	25.6	154.9	108.9	-83.5%	-76.5%
Heavy products[11]	269.5	198.6	511.7	35.7%	-47.3%
Crude oil (commodity/material)	79.4	0.0	0.0	-	-
Other	296.8	328.1	221.8	-9.5%	33.8%
Total	2,737.2	2,776.5	2,720.1	-1.4%	0.6%

Source: the Company.

[9] The difference between the volume of crude oil processed and the refinery's output of products stems from the fact that, apart from crude oil, the processing units and finished product blenders receive biocomponent streams, enhancing additives and middle distillates purchased from third-party suppliers.

[10] Heavy fuel oil and bitumen components

[11] Other products include fuel and industrial gases, sulfur, base oils, xylene fraction, LPG, bunker fuel, extracts, refinates, and slack wax.

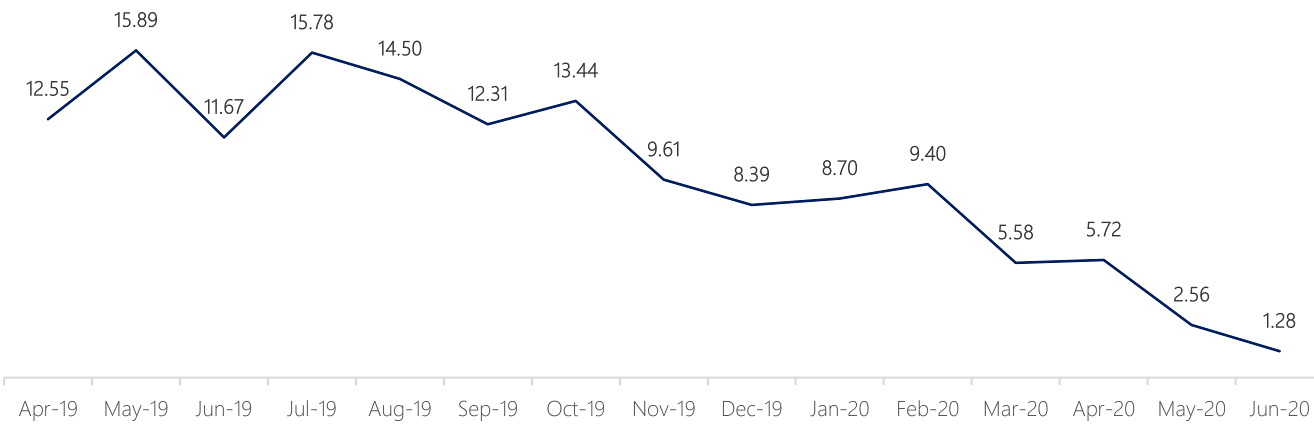
Polish fuel market[12]

In Q2 2020, consumption of liquid fuels (diesel oil, gasoline and light fuel oil) in Poland fell 11.9% year on year. The reason behind the decline were restrictions imposed in response to the Covid-19 pandemic. Motor gasoline consumption fell by 21.3% and diesel oil consumption by 9.3% year on year; the consumption of light fuel oil was on a rise (0.6%).

Motor gasoline

The LOTOS Group's total sales of gasoline rose by 1.9% year on year in Q2 2020, although domestic sales fell by 18.2%. The average crack spread for gasoline on global markets shrank by USD 10.3/bbl year on year.

Figure 2. Motor gasoline – average monthly crack spread, USD/bbl April 2019 – June 2020

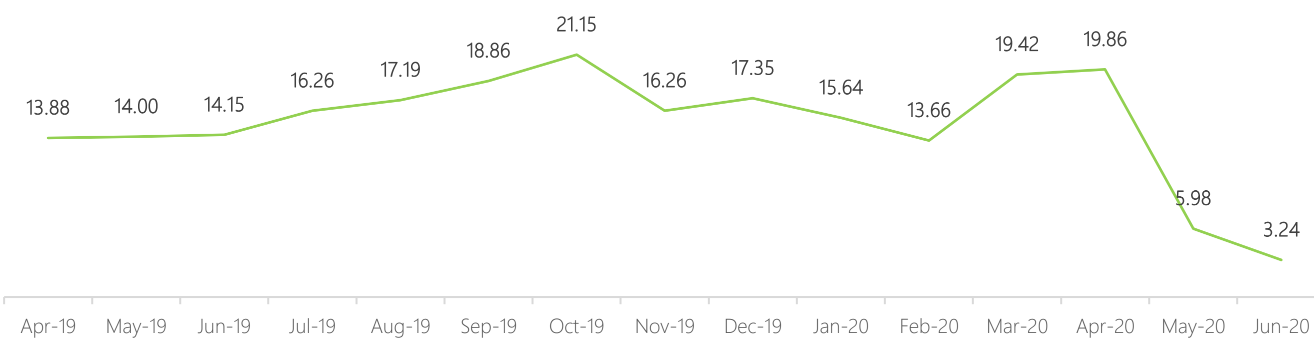


Source: Refinitiv.

Diesel oil

In Q2 2020, the LOTOS Group's sales grew 3.3%. Despite a 9% decrease in consumption, domestic sales fell by -3.5% year on year. In Q2 2020, the average global crack spread for diesel oil went down by USD 4.47/bbl year on year.

Figure 3. Diesel oil – average monthly crack spread, USD/bbl April 2019 – June 2020



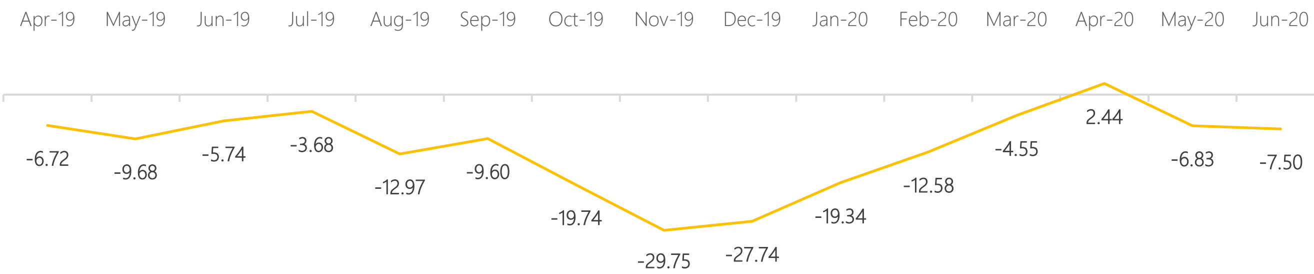
Source: Refinitiv.

Heavy fuel oil

In the reporting quarter, the LOTOS Group's sales of heavy products (bitumen components and heavy fuel oil) fell 87% year on year, as the refinery's yields were optimised following integration of the new EFRA units. In Q2 2020, the average negative crack spread for heavy fuel oil on global markets was USD -4.03/bbl, up USD 3.38/bbl year on year.

[12] Source of fuel consumption data in Poland - POPiHN.

Figure 4. Heavy fuel oil – average monthly crack spread, USD/bbl April 2019 – June 2020



Source: Refinitiv.

Table 11. Refining & Marketing segment's key financial data (PLNm)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Revenue	4,155.9	5,882.9	7,487.8	-29.4%	-44.5%
EBIT	234.6	-1,156.8	525.2	-	-55.3%
Depreciation and amortisation	190.2	189.3	163.1	0.5%	16.6%
EBITDA	424.8	-967.5	688.3	-	-38.3%
LIFO-based EBIT	-171.0	245.3	481.5	-169.7%	-135.5%
LIFO-based EBITDA	19.2	434.6	644.6	-95.6%	-97.0%
Adjusted LIFO-based EBITDA[13]	14.8	490.5	600.2	-97.0%	-97.5%

Source: the Company.

The 44.5% year-on-year decline in the Refining & Marketing segment's revenue was driven primarily by a 42.8% drop in the segment's average net selling price. In Q2 2020, the segment's average net selling price was PLN 1,493/tonne, having fallen PLN 1,116/tonne, or 42.8%, chiefly on lower prices of petroleum products. In addition, the decrease was driven by lower sales volumes.

The 29.4% quarter-on-quarter decline in the Refining & Marketing segment's revenue reported in Q2 2020 was largely attributable to a 30.5% decrease in the average net selling price (down PLN 656/tonne) driven by lower prices of petroleum products.

In Q2 2020, adjusted LIFO-based EBITDA of the Refining & Marketing segment came in at PLN 14.8m, down 97.0% quarter on quarter and 97.5% year on year.

EBIT of PLN 234.6 posted by the Refining & Marketing segment in Q2 2020 reflects the effect of reversal of inventory write-downs recognised in Q1 2020, of PLN 815.3m, on a consolidated basis. The falling trend in crude oil prices resulted in the LIFO effect on inventory measurement of PLN 409.7m. LIFO effect (as the sum of the two elements) was PLN -405.6m, so it had a positive effect on the segment's operating profit.

At the same time the Company points out that, given the fluctuations in crude oil inventory levels and differences between crude oil volumes purchased and processed in Q2 2020, the calculation of cost of oil processing using the LIFO method was based on oil inventories with a unit cost exceeding the current price – the effect of old oil inventories (measured at significantly higher unit cost) occurred. This effect reflects a shortcoming of the adopted inventory valuation model, which, in an environment with

[13] EBITDA including the LIFO effect on inventory measurement and reversal/recognition of inventory write-downs, net of foreign exchange differences on operating activities in each quarter and impairment losses on service stations in Q1 2020.

significant oil price declines, distorted the LIFO-based result for the period and has no effect on cash flows from operating activities. The Company estimates the above negative effect on LIFO-based profit/(loss) at approximately PLN 369m (for more information, see: Current Report No. 22/2020 Estimates of LOTOS Group's Q2 2020 consolidated operating results).

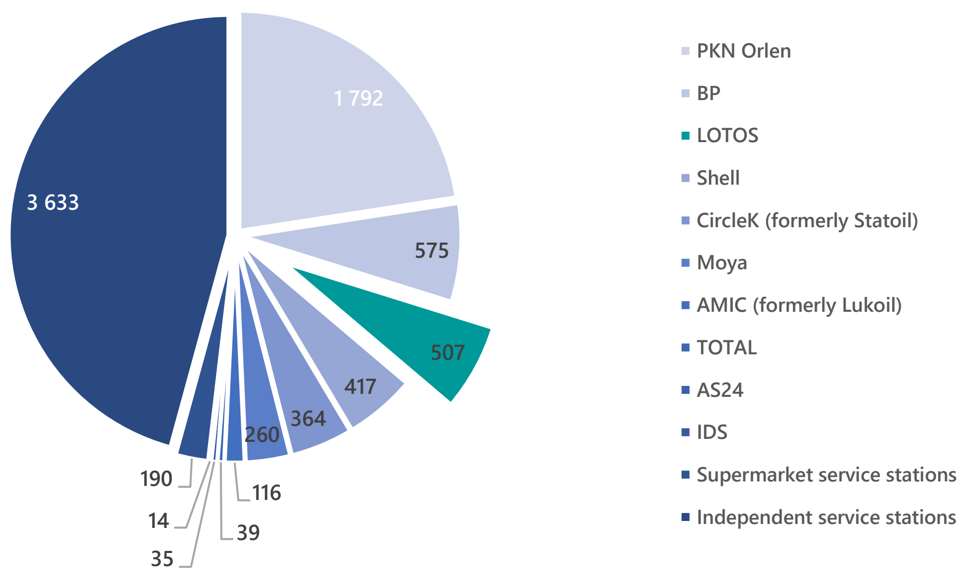
Table 12. Number of service stations within the LOTOS network as at June 30th 2020

	Jun 30 2020	Mar 31 2020	Jun 30 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
CODO	312	312	307	0	5
DOFO	195	194	186	1	9
Total	507	506	493	1	14

Source: the Company.

As at the end of June 2020, the LOTOS Group operated a chain of 507 service stations, an increase of 14 sites relative to the end of June 2019.

Figure 5. Service stations in Poland as at June 30th 2020



Source: POPiHN (Polish Organisation of Oil Industry and Trade).

Table 13. Retail's key financial data (PLNm)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Sales volume ('000 tonnes)	260.0	284.6	316.4	-8.6%	-17.8%
Revenue	1,175.6	1,511.7	1,786.3	-22.2%	-34.2%
EBIT	20.1	9.7	51.0	107.2%	-60.6%
Depreciation and amortisation	29.0	28.1	27.5	3.2%	5.5%
EBITDA	49.1	37.8	78.5	29.9%	-37.5%
Adjusted EBIT	20.1	18.3	51.0	9.8%	-60.6%
Adjusted EBITDA	49.1	46.4	78.5	5.8%	-37.5%

Source: the Company.

EBIT posted in Retail for Q2 2020 reached PLN 20.1m.

CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

Table 14. Key financial results of the LOTOS Group (PLNm)

	Q2 2020	Q1 2020	Q2 2019	Q2 2020 / Q1 2020	Q2 2020 / Q2 2019
Revenue	4,245.5	6,095.8	7,662.0	-30.4%	-44.6%
EBIT	-249.4	-1,358.9	658.7	-81.6%	-137.9%
Depreciation and amortisation	272.7	275.4	212.7	-1.0%	28.2%
EBITDA	23.3	-1,083.5	871.4	-	-97.3%
LIFO effect[14]	-405.6	1,402.1	-43.7	-	-
LIFO-based EBIT	-655.0	43.2	615.0	-1,616.2%	-206.5%
Adjusted LIFO-based EBIT	-220.6	395.1	570.6	-155.8%	-138.7%
Adjusted LIFO-based EBITDA[15]	52.1	670.5	783.3	-92.2%	-93.3%

Source: the Company.

In line with its inventory measurement policies, the LOTOS Group uses the weighted average cost method to measure changes in inventories. This method defers the impact of changes in crude oil prices on the prices of finished goods. Thus, an increase in crude oil prices has a positive effect on financial performance, while a decrease adversely affects the performance.

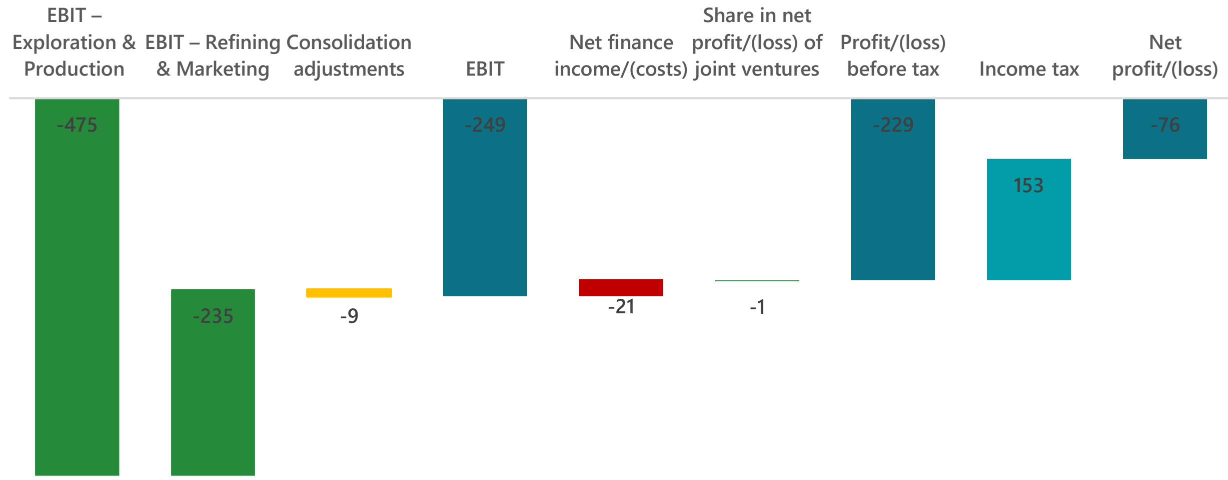
Operating results computed using this inventory measurement method are presented in the EBITDA and EBIT lines of the table. The table also presents estimated inventory decreases measured using the LIFO method, as well as the LIFO effect, LIFO-based EBIT, adjusted LIFO-based EBIT, and adjusted LIFO-based EBITDA.

In Q2 2020, the LOTOS Group posted an operating loss (EBIT) of PLN -249.4m, being the combined result of the Exploration & Production segment's EBIT of PLN -474.9m, the Refining & Marketing segment's EBIT of PLN 234.6m, and PLN -9.1m in consolidation adjustments. LIFO-based EBITDA, net of exchange differences on operating activities and other non-recurring items (adjusted LIFO-based EBITDA), was PLN 52.1m.

The operating performance was adversely affected by a significant decline in crude oil prices and petroleum product crack spreads.

[14] LIFO effect = LIFO-based EBIT (estimated with the LIFO, or Last In First Out, method) - EBIT.
[15] LIFO-based EBITDA, including one-off items described in the segment discussion.

Figure 5. Structure of the LOTOS Group's consolidated results in Q2 2020 (PLNm)



Source: the Company.

In Q2 2020, the LOTOS Group reported net finance income of PLN 21.0m, chiefly attributable to foreign exchange gains of PLN 69.6m, a PLN 115.0m gain on measurement and settlement of hedging transactions, impairment losses on investment in the B4/B6 fields of PLN -114.5m, and negative net balance of interest on debt, interest income and commissions of PLN -50.6m.

In Q2 2020, the effect of measurement and settlement of market risk hedging transactions at the LOTOS Group included mainly a PLN 60.9m net gain on settlement and measurement of transactions hedging currency risk and a PLN 60.5m net gain on measurement of transactions hedging the commodity price risk.

Market risk management

Presented below is the market risk management process, including the measures undertaken in Q2 2020.

In its core business activities, the LOTOS Group is exposed to market risk manifest in:

- risk related to commodity and petroleum product prices,
- risk related to prices of carbon dioxide emission allowances,
- currency risk,
- interest rate risk.

As part of the risk related to commodity and petroleum product prices, certain key risk factors have been identified at the LOTOS Group, including volatility of the refining margin, volatility of prices of stocks held in excess of the mandatory emergency stock volumes, volatility of differentials used in trade contracts (e.g. Urals vs Brent), and the use of non-standard pricing formulas in trade contracts.

In Q2 2020, commodity swaps were entered into as part of the adopted policy of managing the commodity and petroleum product price risk. The contracts were concluded in order to preserve the original price risk profile in connection with the fact that bitumen components are offered for sale at fixed prices. In addition, transactions were carried out to take advantage of the favourable structure of diesel oil future prices.

The risk related to prices of carbon dioxide emission allowances is managed at Grupa LOTOS on an ongoing basis, in line with the assumptions set forth in the strategy for managing the risk. The Group balances its future CO_2 emission allowance shortages and surpluses depending on the market situation and within defined limits.

In Q1 2020, the Company managed its position in CO_2 emission allowances based on a strategy to adapt to the situation prevailing at a given time on the EUA Futures market. At present, Grupa LOTOS S.A. has reduced the surplus of CO_2 emission allowances relative to Q1 2020.

In its business activities, the LOTOS Group is exposed to exchange rate movements in connection with its commodity and petroleum product trading activities, investing cash flows, financing cash flows (including deposits and credit facilities), and measurement of derivative instruments. The parent actively manages its currency exposure based on an adopted policy and within defined limits, using Cash-Flow-at-Risk (CFaR) as the principal risk measure. In Q2 2020, as part of the currency risk management process, in order to optimise the value of expected cash flows, the Group entered into spot, FX forward and FX swap contracts taking into account prevailing market conditions.

The Group is exposed to the risk of changes in cash flows caused by interest rate movements as interest income and interest expense related to certain assets and liabilities accrue based on floating interest rates, including in particular under the investment credit facility for the EFRA Project and the inventory financing and refinancing credit facilities where the amount of interest is computed by reference to the floating LIBOR USD rate. To hedge its interest rate risk, the LOTOS Group enters into interest rate swap contracts.

Table 15. EBIT, profit before tax and net profit/(loss) of the LOTOS Group (PLNm)

	Q2 2020	Q1 2020	Q2 2019
EBIT	-249.4	-1,358.9	658.7
Profit/(loss) before tax	-229.6	-1,729.9	666.1
Net profit/(loss)	-76.4	-1,311.6	500.5

Source: the Company.

In Q2 2020, the LOTOS Group reported consolidated net loss of PLN 76.4m.

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

Table 16. Consolidated statement of financial position – assets (PLNm)

	Jun 30 2020	Dec 31 2019	Nominal change	Change in %
Total	21,033.8	23,672.1	-2,638.35	-11.1%
Non-current assets	13,500.0	14,236.2	-736.2	-5.2%
Property, plant and equipment of the Refining & Marketing segment	9,523.6	9,638.4	-114.8	-1.2%
Intangible assets of the Refining & Marketing segment	172.8	160.0	12.8	8.0%
Property, plant and equipment of the Exploration & Production segment	2,892.4	3,632.4	-740.0	-20.4%
Intangible assets of the Exploration & Production segment	296.1	330.5	-34.4	-10.4%
Equity-accounted joint ventures	25.9	142.2	-116.3	-81.8%
Deferred tax assets	404.7	174.5	230.2	131.9%
Derivative financial instruments	13.2	0.1	13.1	13,100.0%
Other non-current assets	171.3	158.1	13.2	8.3%
Current assets	7,533.8	9,435.9	-1,902.1	-20.2%
Inventories	3,249.3	4,854.3	-1,605.0	-33.1%
Trade receivables	1,590.5	2,609.1	-1,018.6	-39.0%
Current tax assets	72.3	96.7	-24.4	-25.2%
Derivative financial instruments	21.4	25.1	-3.7	-14.7%
Other current assets	279.8	334.1	-54.3	-16.3%
Cash and cash equivalents	2,320.5	1,516.6	803.9	53.0%

Source: the Company.

As at June 30th 2020, the LOTOS Group carried total assets of PLN 21,033.8m (down PLN 2,638.3m on December 31st 2019).

Key changes in assets:

- PLN 1,605.0m decrease in inventories, due to a much lower volume of crude oil stocks and a significant decline in prices;
- PLN 740.0m decrease in the Exploration & Production segment's property, plant and equipment, attributable mainly to impairment losses on the YME and Utgard field assets in Norway, on the B3 and B8 fields in Poland, and on the fields in Lithuania;
- PLN 1,018.6m decrease in trade receivables, driven by lower prices and use of factoring facilities;
- PLN 116.3m decrease in equity-accounted joint ventures, due mainly to impairment losses on the B4/B6 fields;
- PLN 803.9m increase in cash and cash equivalents, due mainly to the use of factoring facilities;
- PLN 230.2m increase in deferred tax assets, chiefly related to impairment losses recognised in the Exploration & Production segment.

Table 17. Consolidated statement of financial position – sources of funding (PLNm)

	Jun 30 2020	Dec 31 2019	Nominal change	Change in %
Total	21,033.8	23,672.1	-2,638.3	-11.1%
Equity	11,140.2	12,715.4	-1,575.2	-12.4%
Share capital	184.9	184.9	0.0	0.0%
Share premium	2,228.3	2,228.3	0.0	0.0%
Cash flow hedging reserve	-172.5	-203.6	31.1	15.3%
Retained earnings	8,842.6	10,415.5	-1,572.9	-15.1%
Translation reserve	56.8	90.2	-33.4	-37.0%
Non-controlling interests	0.1	0.1	0.0	0.0%
Non-current liabilities	4,700.6	5,097.9	-397.3	-7.8%
Borrowings, other debt instruments and finance lease liabilities	3,114.7	3,142.6	-27.9	-0.9%
Derivative financial instruments	21.6	6.6	15.0	227.3%
Deferred tax liabilities	120.5	475.2	-354.7	-74.6%
Employee benefit obligations	214.4	207.5	6.9	3.3%
Other liabilities and provisions	1,229.4	1,266.0	-36.6	-2.9%
Current liabilities	5,193.0	5,858.8	-665.8	-11.4%
Borrowings, other debt instruments and finance lease liabilities	1,216.3	1,273.8	-57.5	-4.5%
Derivative financial instruments	46.4	15.3	31.1	203.3%
Trade payables	1,459.2	1,940.8	-481.6	-24.8%
Current tax liabilities	75.5	217.1	-141.6	-65.2%
Employee benefit obligations	163.1	174.3	-11.2	-6.4%
Other liabilities and provisions	2,232.5	2,237.5	-5.0	-0.2%

Source: the Company.

The reduction in the LOTOS Group's equity as at June 30th 2020 to PLN 11,140.2m (down by PLN -1,575.2m on 2019) was driven primarily by lower retained earnings (down by PLN -1,572.9m), foreign exchange gains on valuation of cash flow hedges, adjusted for the tax effect of PLN 31.1m, recognised in capital reserves, and a PLN 33.4m decrease in translation reserve.

The share of equity in total equity and liabilities fell by 0.7pp year on year, to 53.0%.

Key changes in liabilities:

- PLN 481.6m decrease in trade payables due to lower volumes of crude oil purchased outside the LOTOS Group in June 2020 compared with December 2019, and a considerable reduction in purchase prices;
- PLN 41.6m decrease in other liabilities and provisions;
- PLN 354.7m decrease in deferred tax liabilities, due mainly to the lower amount of that item recognised by the parent;
- PLN 85.4m decrease in borrowings, other debt instruments and finance lease liabilities.

As at June 30th 2020 , the LOTOS Group's debt totalled PLN 4,331.0m, down by PLN 85.4m on the end of December 2019, mainly as a result of repayment of investment credit facilities. Net debt amounted to PLN 2,010.5m. The ratio of net debt to adjusted LIFO-based EBITDA as at June 30th 2020 was 0.9x, down 0.1x relative December 31 2020.

CONSOLIDATED STATEMENT OF CASH FLOWS

Table 19. Cash flows (PLNm)

	Q2 2020	Q1 2020	Q2 2019
Cash flows from operating activities	1,445.4	340.4	243.6
Cash flows from investing activities	-164.9	-362.1	180.8
Cash flows from financing activities	-226.8	-254.6	-316.1
Effect of exchange rate fluctuations on cash held	-20.7	47.2	-11.8
Change in net cash	1,033.0	-229.1	96.5
Cash at beginning of period	1,287.5	1,516.6	2,084.0
Cash at end of period	2,320.5	1,287.5	2,180.5

Source: the Company.

As at June 30th 2020, the LOTOS Group's cash balance (including overdraft facilities) amounted to PLN 2,320.5m. Cash and cash equivalents increased by PLN 1,033.0m as a result of net cash flows in Q2 2020.

The positive net cash flows from operating activities in Q2 2020, of PLN 1,445.4m, were driven mainly by a marked decrease in trade receivables in Q2 2020 (chiefly as a result of the use of factoring arrangements), with impairment losses on assets in the Exploration & Production segment and an increase in trade payables in Q2 2020.

The negative net cash flows from investing activities of PLN -164.9m were mainly attributable to acquisition of property, plant and equipment and other intangible assets, chiefly for the Exploration & Production segment and the EFRA Project.

The negative cash flows from financing activities in Q2 2020, of PLN -226.8m, chiefly reflected a negative net balance of proceeds from borrowings and repayments of borrowings (principal and interest), and payments of liabilities under finance leases.