

NON-AUDITED  
CONSOLIDATED



# SEMI-ANNUAL REPORT PETROKEMIJA GROUP

REPORT FOR PERIOD January to June 2018  
INTERIM REPORT FOR PERIOD April to June 2018

NPK

KAN

UREA

PETROKEMIJAS

ASN

Kutina, July 2018



## Introduction

In the reporting period January - June 2018, Petrokemija d.d. continued to operate in a very complex situation of unfinished recapitalization, difficulties in liquidity and adverse conditions in the market environment. With the support of the majority owner, the natural gas suppliers and financial institutions, the Company maintained the continuity of production and its operations, is fulfilling its obligations to the customers; it is carrying out the facilities overhaul and the investments necessary to continue the business in order to prevent major damages for the stakeholders of this process.

Following an unfavorable situation in the fourth quarter of 2017, the business environment of Petrokemija in the first half of 2018 was marked by many challenges. In the reporting period, the negative effects of full openness to the global market, i.e. Petrokemija's exposure to the risks of the neighboring and wider business environment were quite apparent, which resulted in very high costs for the Company without the possibility of its influence on them. Namely, Petrokemija carried forward all the bad debts of the unfinished recapitalization process of 2017 into the first half of 2018. Furthermore, the negative financial effects are even more intensified by:

- high rise in the price of CO<sub>2</sub> allowances (new costs value adjustment of liabilities from previous years),
- further growth in natural gas purchase price,
- the fall in sales prices of mineral fertilizers on the global market,
- increase in purchasing prices of other raw materials (MAP, DAP, potassium chloride)
- decrease in total sales volumes due to lower sales of mineral fertilizers in overseas exports because current prices were significantly lower than the variable production costs realized by Petrokemija.

The biggest single impact on the financial result was the price increase of the CO<sub>2</sub> emission units (+84.8% compared to late 2017).

The risk of value adjustment of the obligation to purchase the missing CO<sub>2</sub> emission units created by 31.12.2017 could not be prevented due to the restriction of the company's liquidity, thus charging the financial result with the amount of **HRK 49.2 million** in the reporting period. When HRK 14.4 million of the fee for the first half of 2018 is added, it means that out of the **HRK 176.0 million loss in the first half of 2018, HRK 63.6 million or 36% accounts only for the CO<sub>2</sub> allowances.**



## Introduction (cont)

**The next most important impact on the loss of business is the growth of natural gas price.** The realized price of natural gas is 11.2% higher than the realized average in the same period of 2017. **This growth resulted in an additional cost of HRK 60.5 million, as compared to the same period of the previous year and accounts for 34% of the realized loss in the first half of 2018.** In addition to the existing natural gas suppliers, INA d.d. and Prvo plinarsko društvo d.o.o, as of February 2018, a new gas supplier – Hrvatska elektroprivreda d.d. (Croatian Electric Power Company) has been involved in the supply of natural gas for some of the required volumes of gas in the reporting period.

**The two items mentioned - natural gas and CO2 allowance account for 70% of the realized loss in the reporting period. These are the risks that the Company could not have had influence on in the current business model** because it could not contract a more favorable gas procurement model as the gas suppliers are also the creditors of the Company and bear the risk of collecting relatively high receivables. Due to carried-forward liabilities from the previous period, the Company was not able to regularly settle the liabilities to natural gas suppliers. Furthermore, due to the lack of financial resources for regular purchases of CO2 emission units (e.g. in the first half of the previous year, when the prices of emission units were significantly lower), the Company sustained the already mentioned additional loss of HRK 49.2 million in the first half of this year.

In the reporting period, there was also an increase in the prices of other major raw materials. The average purchasing price of the main raw materials for NPK fertilizer production - MAP was higher by 11.1% (expressed in USD) and potassium chloride by 10.4% (expressed in EUR) than in the same period of the previous year. The changes in the exchange rates of the USD and EUR against the Croatian kuna have resulted in the growth of potassium chloride share in Petrokemija's costs by about the same amount, as the EUR exchange rate was approximately at the same level (index 99.6%), while the rise in MAP price, due to the fall of the USD exchange rate, was neutralized in HRK amounts. The price of raw phosphate is below the level of the same period last year.



## Introduction (cont)

**The remaining 30% of the loss** (apart from the price of natural gas and the allowances for CO<sub>2</sub> emission units), **is made up of all other business elements** - lower revenues due to low sales prices and smaller sales volumes, interest on loans, costs of facilities standstills for technical and technological reasons and other costs that could not be covered by realized revenues.

Mineral fertilizer sales amounted to 519 thousand tons, 5.2% down on the same period of the previous year, as due to the sharp fall of sales prices in the global market it was not possible to sell under covering the direct variable production costs; simultaneous rise in raw material prices (natural gas) and fall of the price of finished products (Urea and CAN). Production of mineral fertilizers was realized at 538 thousand tons, 6.3% down on the same period of the previous year, partly due to technical and technological issues, and partly due to the unfavorable conditions on the sales market.

After a long period of preparations, in the conditions of limited funding for investments, an extensive biennial overhaul of Petrokemija's facilities is currently being conducted in order to provide good technical and technological condition of the facilities for the following period and partly to invest in modernization and increase of energy efficiency.

Due to the lack of liquidity, investments in the first half of the current year amounted to HRK 38.7 million, but another significant amount should be invested in the overhaul and other activities for which long-term sources have not been secured. All these costs are covered from the current business operations or the expected recapitalization. The completion of the recapitalization process should have a beneficial effect on balancing the Company liquidity and normalizing the investment and modernization system that is currently under significant pressure from the due liabilities towards suppliers for the delivered natural gas.

As regards market position, the adverse effects of the Agrokor Group are still present in the domestic and regional market. It is a common fact that the Agrokor Group, as the organizer of agricultural production, is the most important single factor in the entire value chain, from the production of crops to the processing industry and the food distribution chain, so that its problems have impact on numerous food producers of different profiles and sizes, from family farms to large systems. Although it does not have such great significance in the region, the disturbance of Agrokor Group's business has also had an impact on mineral fertilizer buyers on the markets of neighboring countries, primarily Slovenia, Bosnia and Herzegovina and Serbia.



## Introduction (cont)

Successful completion of the creditors' settlement process in Agrokor will probably have a positive impact on the trend of intensifying sales growth on the domestic and regional mineral fertilizer markets.

The goals of the sales strategy in 2018 and 2019 are increasing sales in the regional, and in particular in the domestic market. However, they are not being realized in the first part of the year due to unfavorable conditions in the environment. Establishing direct partnerships with as many direct customers – mineral fertilizers consumers – is one of the positive results, with the aim of strengthening long-term competitive position of Petrokemija d.d. in the domestic market and a decrease in imports of mineral fertilizers into Croatia compared to previous years.

Fertilizer manufacturers in Europe are under strong pressure from the competition of major global manufacturers who have a comparative advantage of cheap raw material sources, from natural gas to phosphate rock, potassium chloride and sulfur. In these conditions, even successful European mineral fertilizer producers, who had benefited from a favorable trend for modernization of plants and restructuring in the previous decade, experienced a fall in profit and some even losses. Accordingly, it was inevitable for Petrokemija, which has been struggling to maintain business continuity for years and operating in conditions of lower technological and energy efficiency than its European competitors, to report losses in business. The most significant negative factor for the loss in the first half of 2018 is the high rise in the price of CO<sub>2</sub> allowances and of natural gas, which accounts for about 70% of the reported loss. In the remaining part of the year the greatest uncertainty is the potentially high purchase price of natural gas, which is for Petrokemija about 10% higher than for its competitors, partly because of the terms for defining the purchase price (suppliers are also the largest creditors of the Company) and partly because of the extremely high costs of gas transport, which are among the highest in the EU.

After years of attempts of changing the ownership structure and attracting into its ownership structure large investors in the value creation chain – from production and trading with natural gas, to logistics of sales of mineral fertilizers to end users – in the reporting period, the current owners have carried out extensive and complete preparation for the implementation of the privatization process and opening of a new development cycle of the Company,



## Introduction (cont)

where all its current potentials would be exploited – from favorable location, well-maintained production and logistics systems, to skilled labor. Shortage of financial potential that manifests itself in the impossibility of changing the business model and of quick adaptation to constant market changes should be resolved in 2018 by permanent capital sources and a new management model of future investors. Loans granted by HBOR and commercial banks in 2016 and 2017 helped to fill the cash gap transferred from previous years, and recapitalization should create the preconditions for a balanced financing model for modernization of the facilities and investment in greater efficiency of all processes in the Company.

Upon an international tender, Petrokemija d.d. concluded new contracts for natural gas supply in the gas year 2018/2019 for the total quantity needed. The contract was concluded with INA d.d. Zagreb and Prvo plinarsko društvo d.o.o. Vukovar, as the most advantageous suppliers in the tender. By concluding this agreement, Petrokemija d.d. provided sufficient quantities of natural gas for stable planned production during the gas year 2018/2019.

At the time of the preparation of these Reports, activities are underway in line with the decisions of the General Meeting of 9 July 2018, which define the future model of Petrokemija d.d. Upon completion of the privatization process of the Company, it is expected that the State (i.e. CERP) will remain in the position of one of the shareholders, but without a dominant position in the structure of ownership and management rights.



## Key indicators for Petrokemija Group for January – June 2018

- ❑ Operating loss – HRK 177.6 million (the same period 2017 – 41.1 million loss),
- ❑ Loss in business operations – HRK 109.9 million, loss in financial operations – HRK 67.7 million,
- ❑ Earnings before interest, taxes, depreciation and amortization (EBITDA) – HRK 65.3 million (negative),
- ❑ Actual total revenues of Petrokemija, d.d. – HRK 934.4 million, 6.0% down on the same period 2017,
- ❑ Actual production of fertilizers – 537.5 thousand tons, 6.3 % down on the same period 2017,
- ❑ Compared to the same period 2017, production decreased: UREA by 16.2%, CAN by 8.5% and NPK fertilizers increased by 16.3%,
- ❑ Yield of currently installed plant capacities – 84.1 %,
- ❑ Actual sales of fertilizers – 519 thousand tons, 5.2 % lower sales volume compared to same period 2017,
- ❑ Share of fertilizer sales in the domestic market – 28.6%,
- ❑ Domestic sales – 148 thousand tons, exports – 371 thousand tons of fertilizers,
- ❑ Capital and reserves on 30.06.2018 for Petrokemija Group – HRK -373.1 million (negative),
- ❑ Invested in Petrokemija, d.d. – HRK 38.7 million,
- ❑ Employed on 30.06.2018: Petrokemija, d.d. – 1,568, Petrokemija Group – 1,699.



## Management Board Report for January – June 2018 for Petrokemija Group

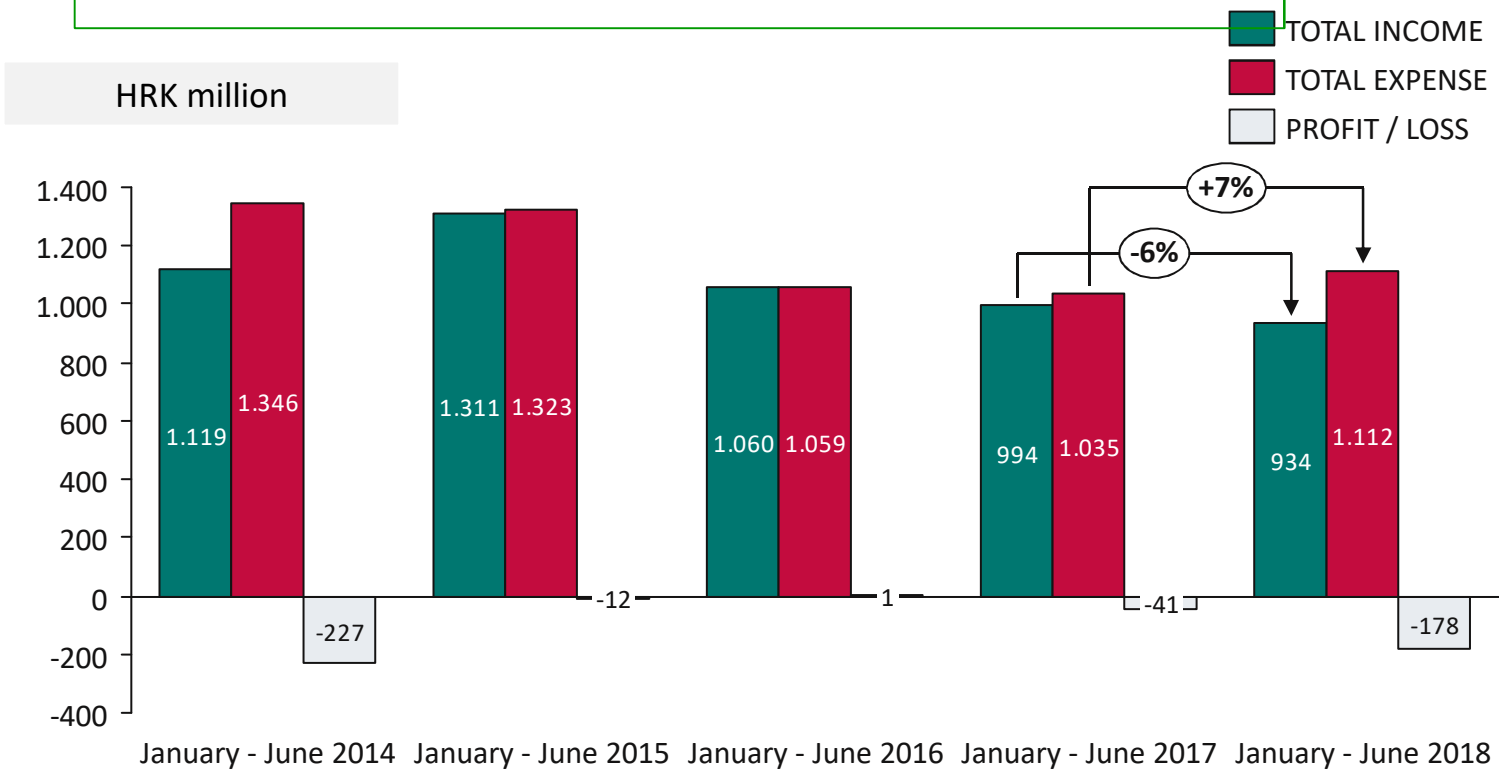
- ❑ In January – June 2018, Petrokemija Group had total income of HRK 934.4 million and total expense of HRK 1,112.0 million. The Company reported loss of HRK 177.6 million or 19.0 % of the total revenues,
- ❑ Lower sales volumes by 5.2 % and higher average sales prices by 0,7 % compared to the same period 2017,
- ❑ In the income structure, domestic sales of Petrokemija d.d. were 32.9 % or HRK 303.3 million, 6.4 % up on the same period 2017, while export accounted for 63.3 % or HRK 584.0 million, 9.3 % down on the same period 2017,
- ❑ In assortment, compared to the same period 2017, lower sales in 2018 of Urea by 11.3%, lower sales of CAN mineral fertilizers group (CAN+AN+UAN+AS/ASN) by 10.9% and higher sales of NPK fertilizers by 16.9 %
- ❑ Domestic sales at the level of realization in the same period of 2017,
- ❑ Mineral fertilizer sales in exports by 7.1% lower than in the same period of 2017,
- ❑ Sales volumes of clay-based products and liquid fertilizers – 25.7% higher than in the same period 2017,
- ❑ Average realized natural gas price (without transport costs) – 12.3% higher in HRK compared to the same period 2017 and 25.6% higher in USD,
- ❑ Liquidity indicators of Petrokemija Group are below recommended value, further aggravated compared to the previous year (on 30.06.2018. negative working capital was HRK -541 million),
- ❑ Indicator of financial stability as well as indicators of indebtedness are below recommended values, indicator of own funding negative, capital negative at the level of HRK **-373.1** million,
- ❑ Short-term assets increased by 1.2% compared to end 2017, and short-term liabilities increased by 26.5%.





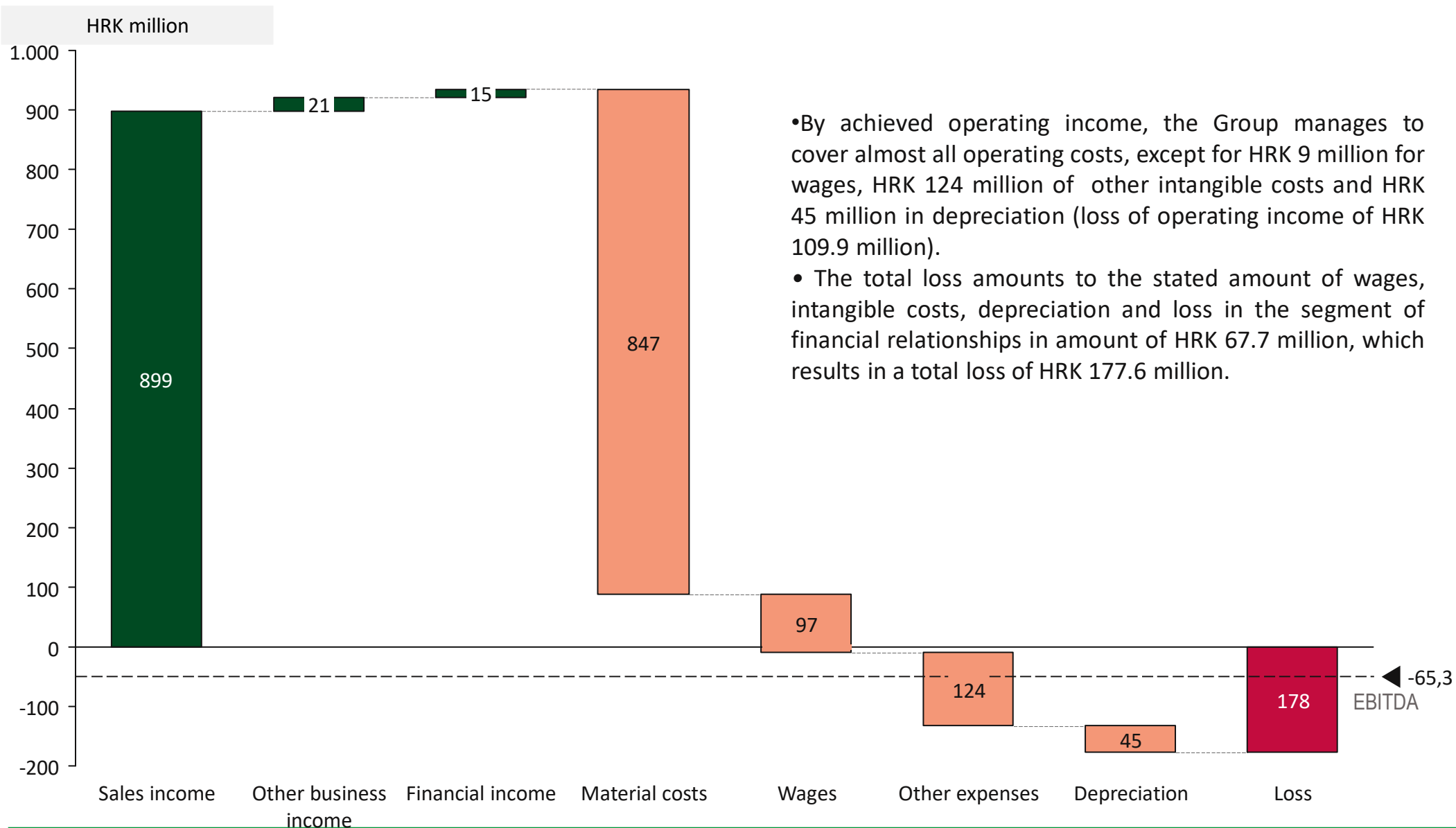
# Profit and Loss of Petrokemija Group for 2014 – 2018

■ Total income	HRK 934.4 million,
■ Total expense	HRK 1,112.0 million,
■ Loss	HRK 177.6 million,
■ EBITDA	HRK -65.3 million,
■ EBITDA margin (%)	6.9%.





## Structure of Profit and Loss for January – June 2018





## Actual financial results of subsidiaries for the period January - June 2018

- In the period from January – June 2018, all daughters of the company operated with loss.

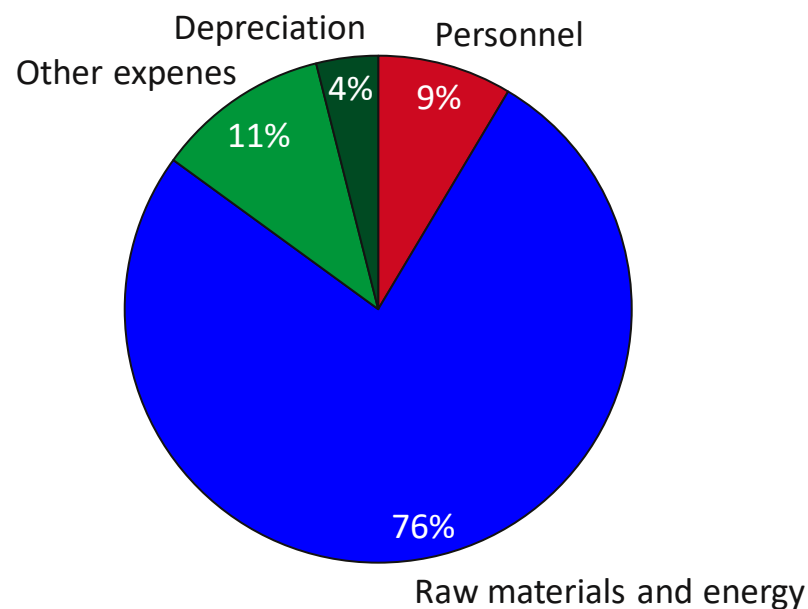
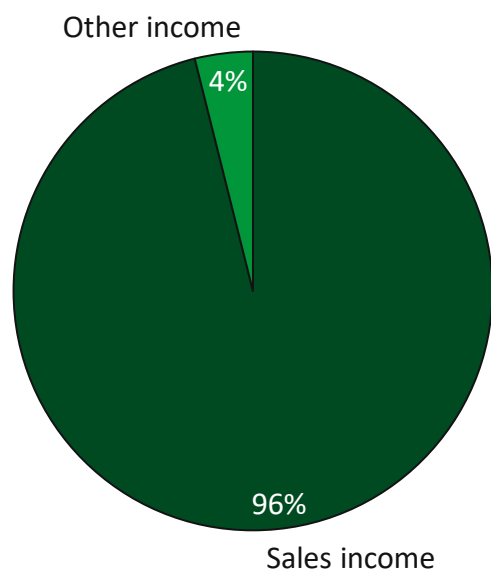
(HRK 000)

<i>Description</i>	<i>Petrokemija Novi</i>		<i>Petrokemija Agro</i>	
	<i>Sad Ltd</i>	<i>Luka Šibenik Ltd.</i>	<i>Trade Ltd.</i>	
<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	
TOTAL INCOME	24.213	9.665	2.250	
TOTAL EXPENSES	24.374	10.613	2.268	
<i>Therein:</i>				
<i>Material costs</i>	23.864	2.710	2.182	
<i>Depreciation</i>	6	622	33	
<i>Wages</i>	311	5.535	0	
<i>Other costs</i>	193	1.746	54	
<b>PROFIT OR LOSS</b>	<b>-161</b>	<b>-948</b>	<b>-18</b>	



## Structure of Profit and Loss for January – June 2018 for Petrokemija Group

- ❑ In January – June 2018 period, Petrokemija, d.d. earned 33% of income from domestic market, 63% income from export, and financial and other income account for 4% of the total revenues. Out of total, 96% of Petrokemija Group income is from sales of products and services and 4% is from other income.
- ❑ In the structure of total expenditures the dominant 76% account for the costs of raw materials, materials and energy; personnel costs account for 9%, while all other costs make 15%. Due to the specific situation of CO2 emission units value adjustment (EUA), which rose by 84.8% in the first half and created additional HRK 49.2 million in costs, the share of financial expenditures has risen to an unusually high 7.4%.





## Key financial indicators for January – June 2018 for Petrokemija Group

(HRK 000)

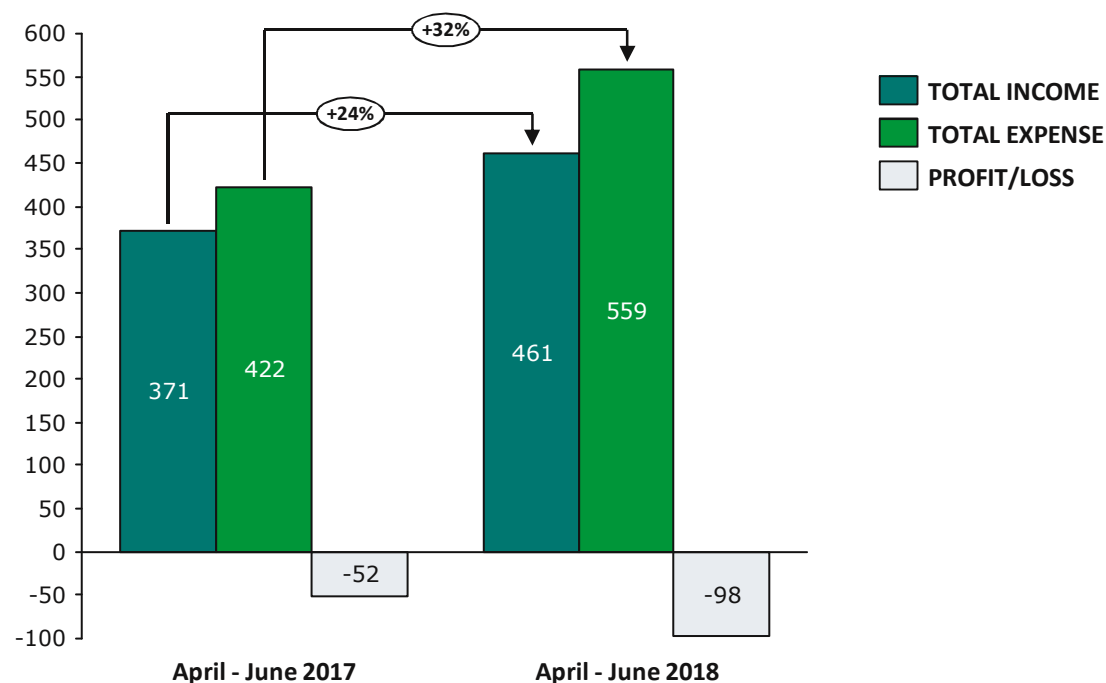
	January – June 2018	January – June 2017	Difference	% change
Operating income	919.567	960.337	-40.770	-4,25%
Operating expense	1.029.491	1.012.722	16.769	1,66%
EBITDA *	-65.274	-4.337	-60.937	1405,05%
Amortization	44.650	48.047	-3.397	-7,07%
Net financial income / (expenses)	-67.670	11.315	-78.985	-698,06%
Net extraordinary income / (expenses)	0	0	0	
Profit / loss / before taxation	-177.594	-41.069	-136.525	332,43%
	<b>30 June 2018</b>	<b>31 December 2017</b>		
Fixed assets	686.899	681.864	5.035	0,74%
Current assets	401.469	394.616	6.853	1,74%
Capital and reserves	-373.066	-195.342	-177.724	90,98%
Long-term liabilities + provisions	519.225	527.308	-8.083	-1,53%
Current liabilities + provisions	942.208	744.514	197.694	26,55%

\* Earnings before interest, taxes, depreciation and amortization



## Profit and Loss from operating activities for April – June 2014 to 2018

- In April to June 2018 period, Petrokemija Group had actual total revenues of HRK 461 million, total expenses of HRK 559 million and reported operating loss of HRK 98 million.
- On a quarterly basis, total revenues increased by 24% compared to the second quarter of 2017, while total expenses increased by 32%.





## Key financial indicators for April – June 2018

	January – March 2018	April – June 2018	January – June 2018
Operating income	462.522	457.045	919.567
Operating expense	498.932	530.559	1.029.491
EBITDA *	-13.731	-51.543	-65.274
Amortization	22.649	22.001	44.650
Net financial income / (expenses)	-42.903	-24.767	-67.670
Net extraordinary income / (expenses)	0	0	0
Profit / loss / before taxation	-79.283	-98.311	-177.594

\* Earnings before interest, taxes, depreciation and amortization

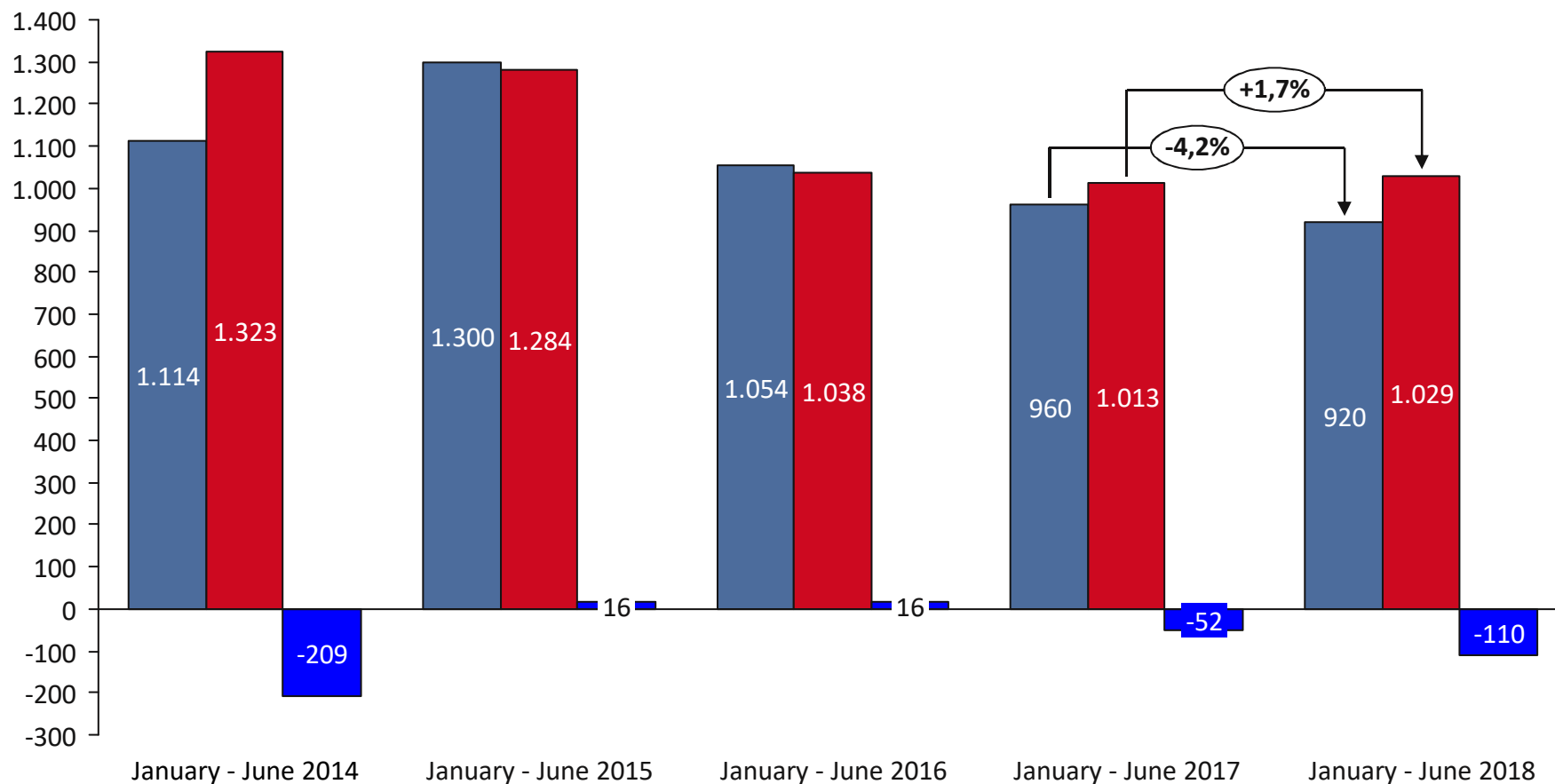
In the second quarter of 2018, a loss of HRK 98.3 million was realized.  
The EBITDA amounted to HRK -51.5 million.



# Profit and Loss from operating activities for Petrokemija Group January – June 2014 to 2018

HRK million

- OPERATING INCOME
- OPERATING EXPENSES
- PROFIT/LOSS FROM OPERATING ACTIVITIES

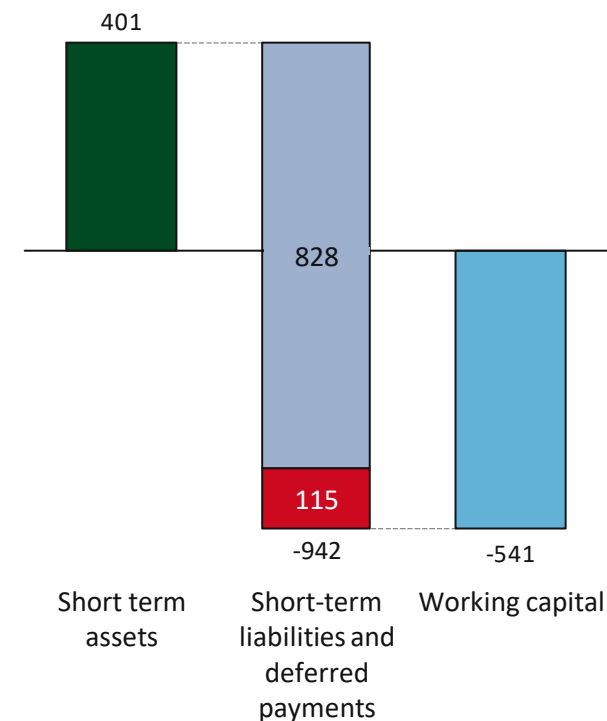




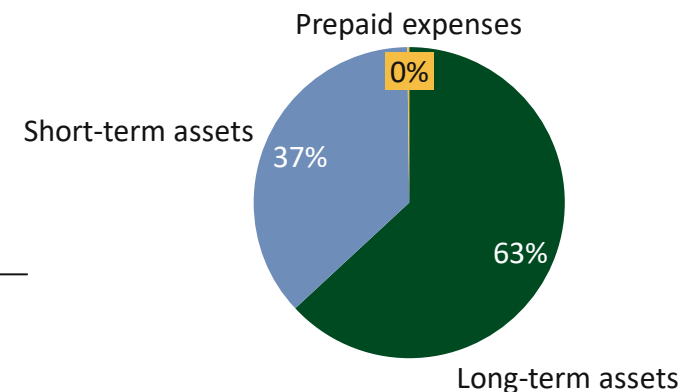
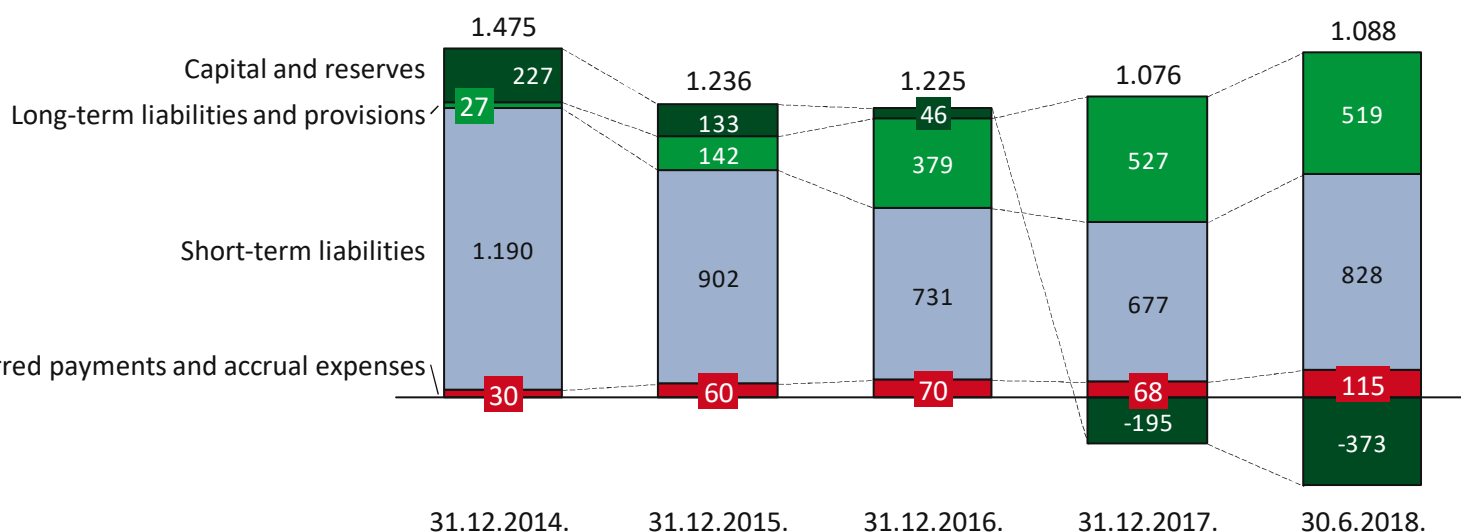


# Structure of assets and liabilities of Petrokemija Group at 30 June 2018

- At 30 June 2018, Petrokemija Group had 37% in value of short-term and 63% in long-term assets.
- The realized loss and delay in the implementation of recapitalization resulted in higher liabilities than the value of the assets, i.e. the capital level was HRK -373.1 million
- During the first half of 2018, the Group indebtedness changed its structure and maturity. Long-term liabilities decreased by HRK 8 million, and short-term liabilities and deferred payment of expenses were increased by HRK 198 million (debt to suppliers and commitments to buy CO<sub>2</sub> units).

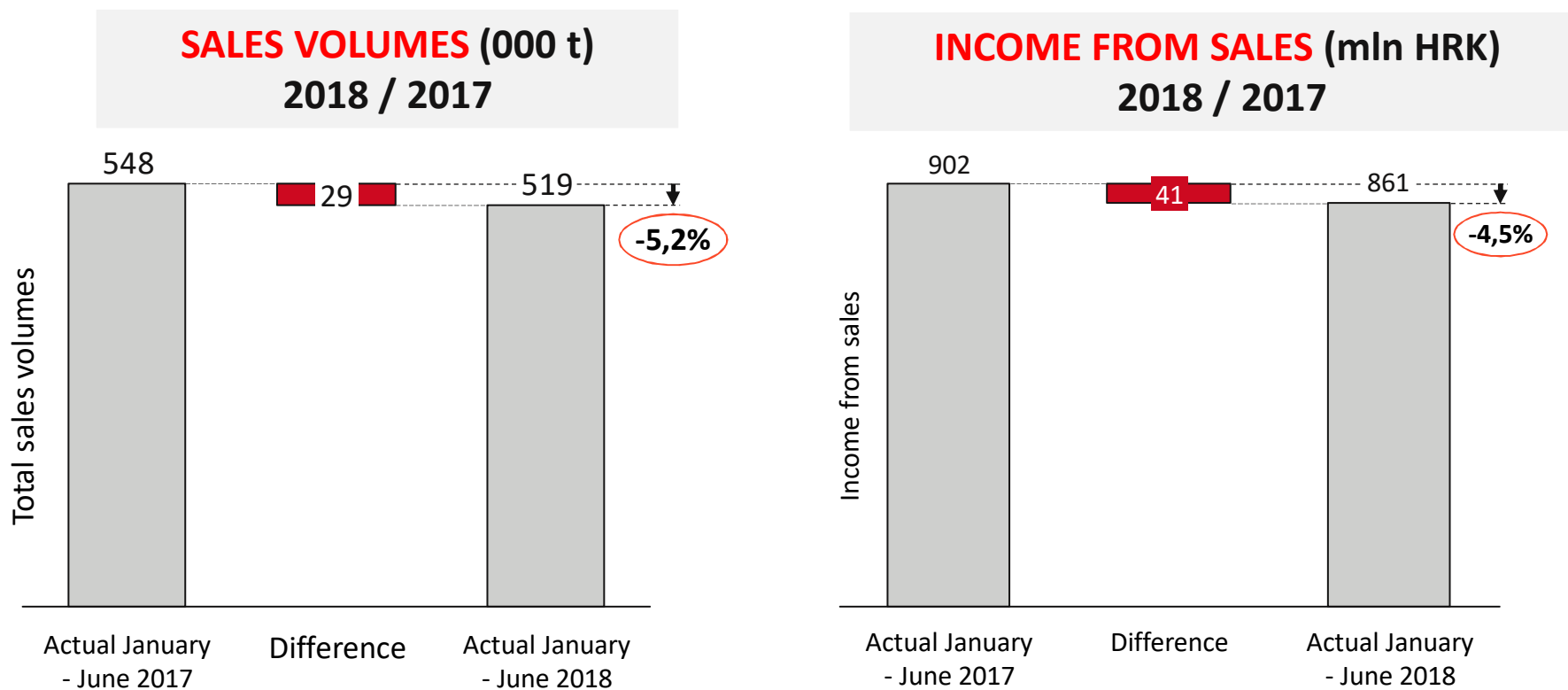


HRK million





## Total fertilizer sales



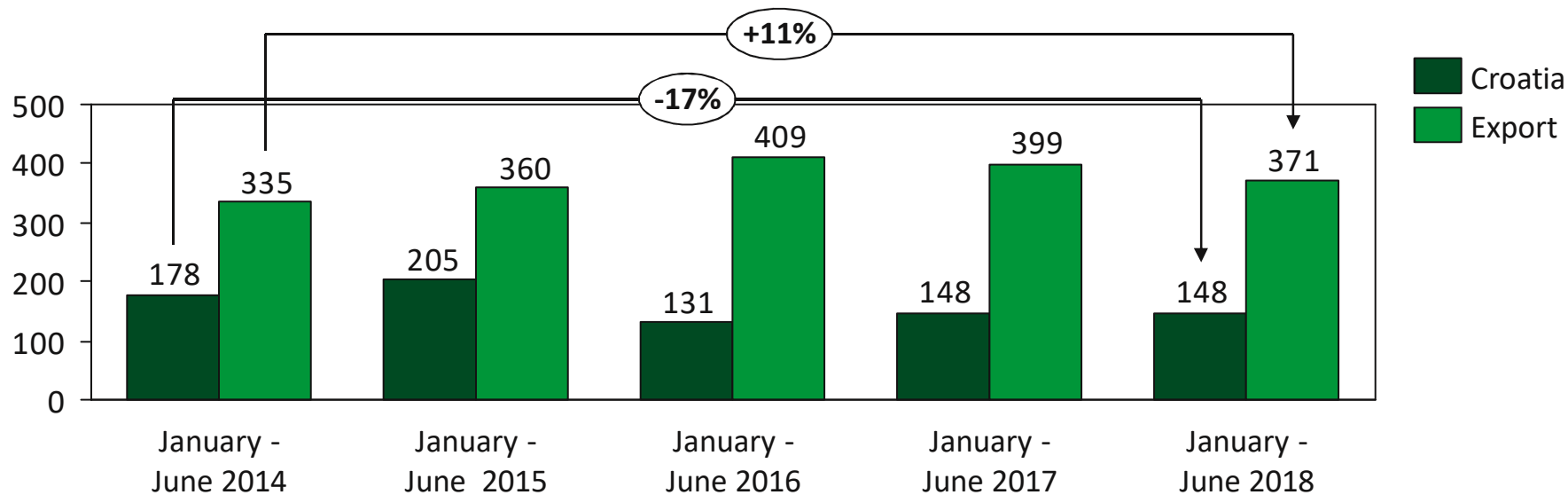
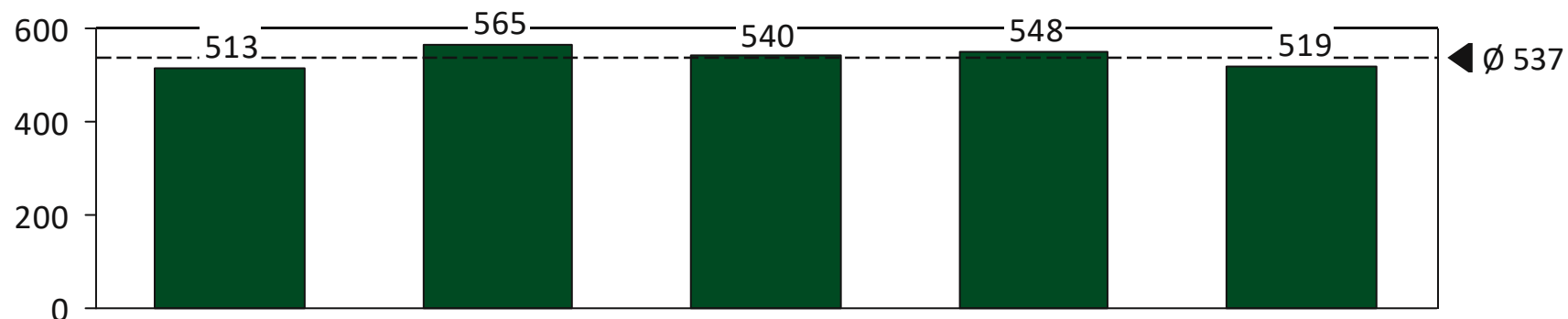
Actual fall in mineral fertilizer sales volumes of 5.2% and decrease in income from fertilizer sales of 4.5%, which indicates a rise in average selling prices of 0.7% compared to the same period 2017. (change in assortment and share of individual markets).

Note: Data for Petrokemija d.d.



# Actual fertilizer sales in January – June 2014 – 2018

total sales (000 tons)



Note: Data for Petrokemija d.d.



## Business Results of Petrokemija Group for January – June 2018

- ❑ After the consolidation of financial results of Petrokemija, d.d. and its subsidiaries - Petrokemija, d.o.o. Novi Sad, Luka Šibenik, d.o.o. and Petrokemija Agro Trade, d.o.o. Kutina – the financial results of Petrokemija Group for the period January – June 2018 are as follows:

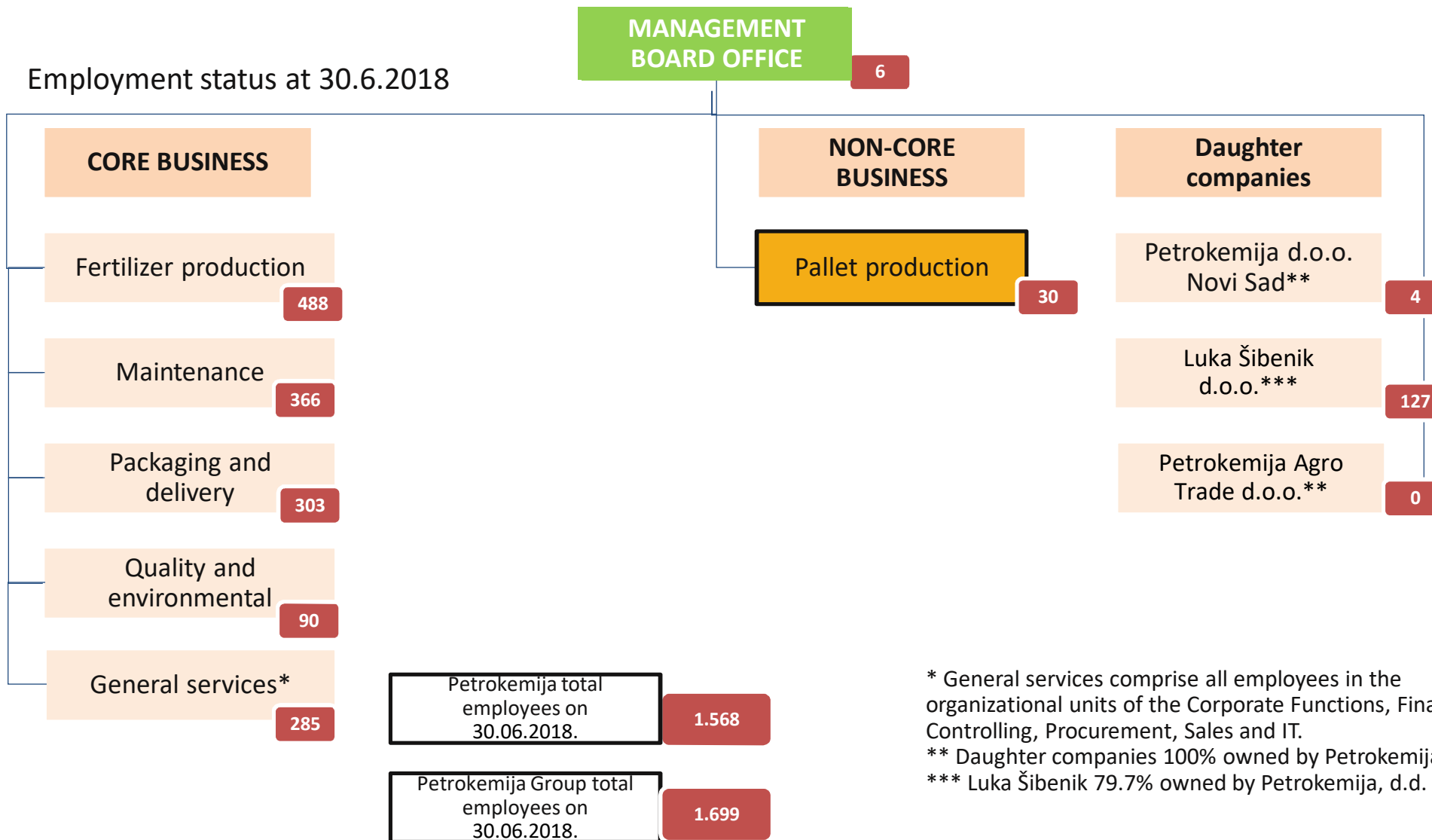
❑ Total revenues	HRK 934.4 million,
❑ Total expenses	HRK 1,112.0 million,
❑ Loss before tax	HRK 177.6 million,
❑ Profit tax	HRK 0.01 million,
❑ Loss after tax	HRK 177.61 million,

- ❑ EBITDA (earnings before interest, taxes and depreciation) was HRK 65.3 million in the negative.
- ❑ Petrokemija, d.o.o. Novi Sad sustained loss of HRK 161 thousand, while Luka Šibenik, d.o.o. reported loss of HRK 948 thousand. Petrokemija Agro Trade d.o.o. sustained a loss of HRK 18 thousand.
- ❑ Losses of subsidiaries of Petrokemija d.o.o. Novi Sad and Luka Šibenik d.o.o. are reflected in reduced turnover in relation to the planned sales volume, ie the transshipment of goods.



# Organization Chart of Petrokemija, d.d. and Petrokemija Group

Employment status at 30.6.2018



\* General services comprise all employees in the organizational units of the Corporate Functions, Finance and Controlling, Procurement, Sales and IT.

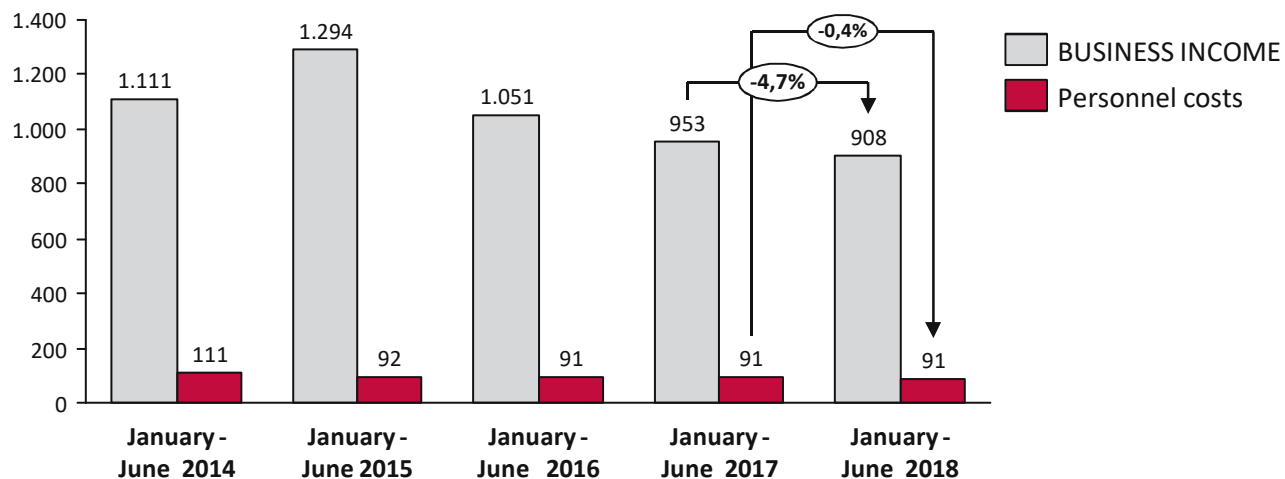
\*\* Daughter companies 100% owned by Petrokemija, d.d.

\*\*\* Luka Šibenik 79.7% owned by Petrokemija, d.d.



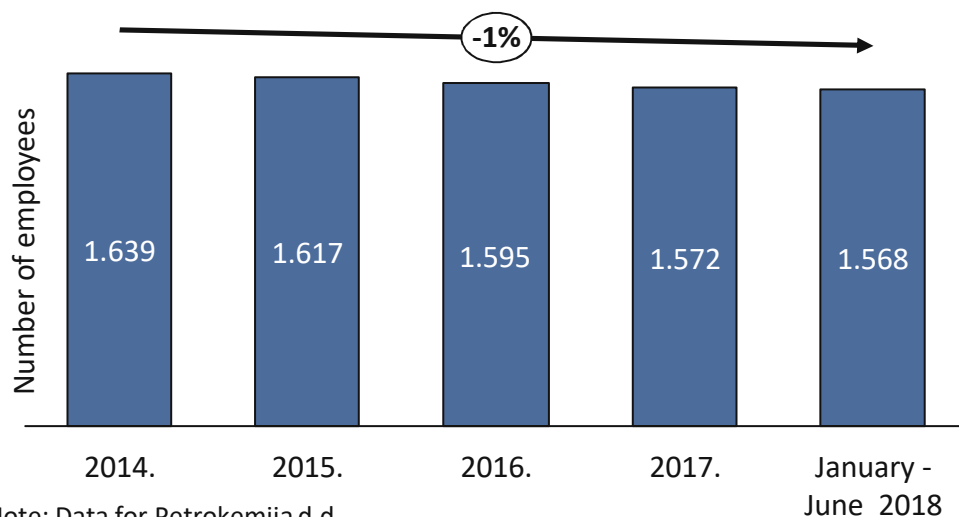
# Operational income, personnel costs and number of employees

HRK million

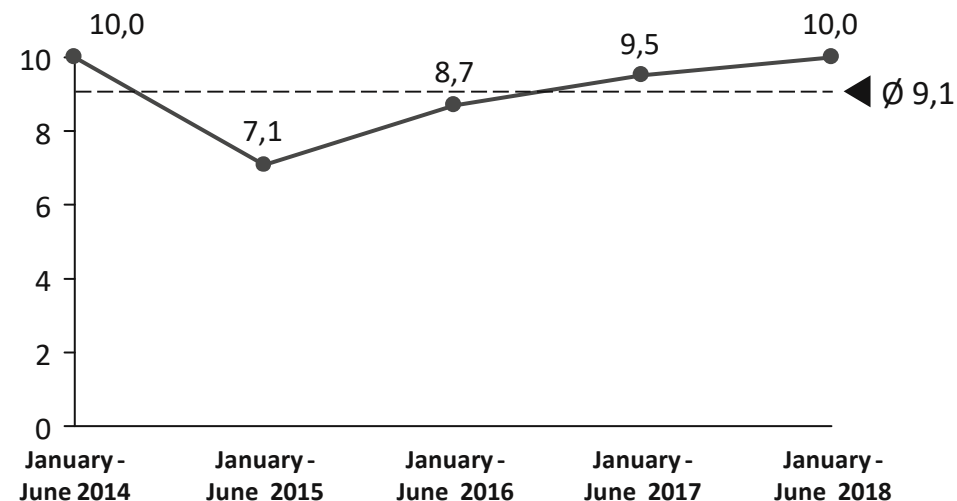


As at **30.06.2018**, Petrokemija, d.d. had **1.568 employees**, and daughter companies - members of Petrokemija Group - had 131 employees, which is a total of 1,699 employees.

Personnel costs share in operating revenues was 10.0%, 0.5% higher, compared to the previous year due to the decline in business income of 4.7% and the mass of gross wages is 0.4 % lower.

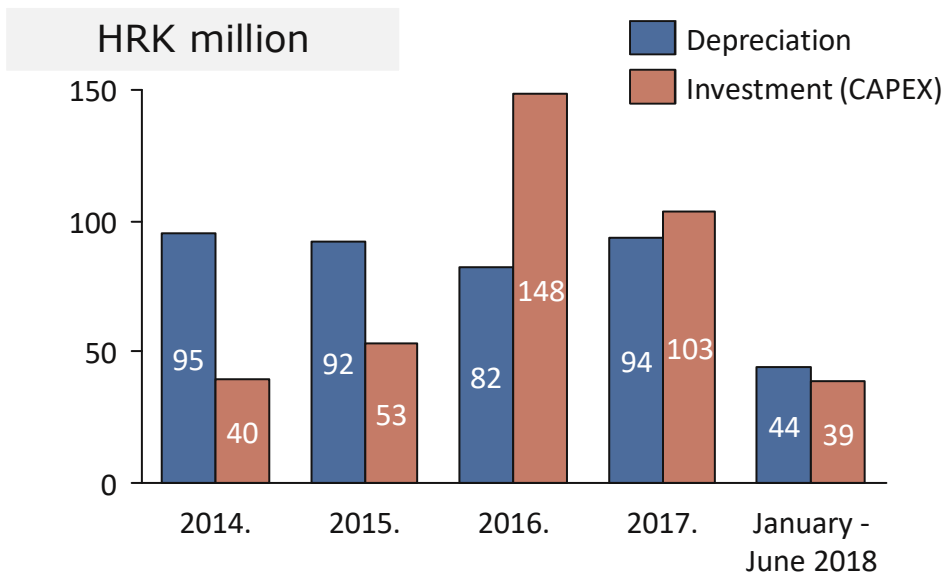


Note: Data for Petrokemija d.d.



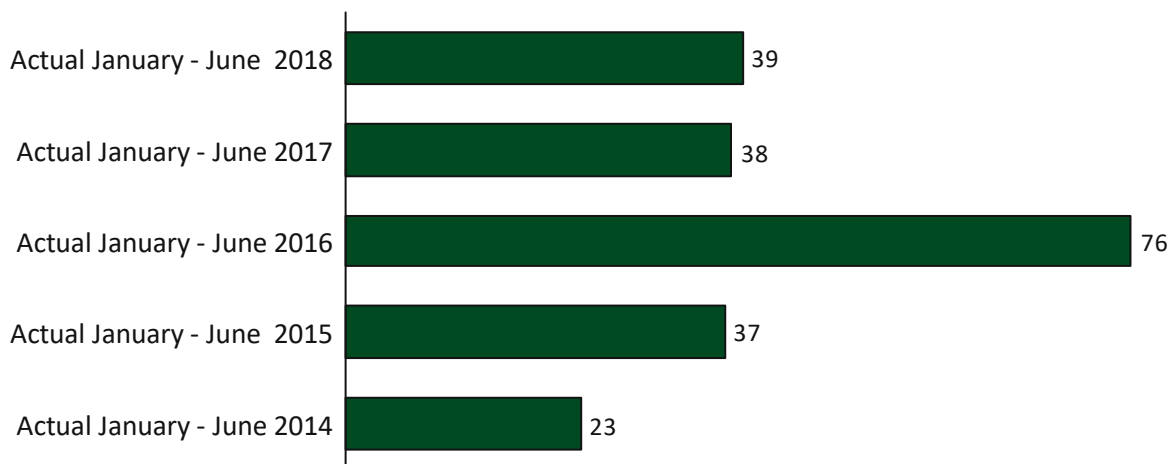


## Realized investment



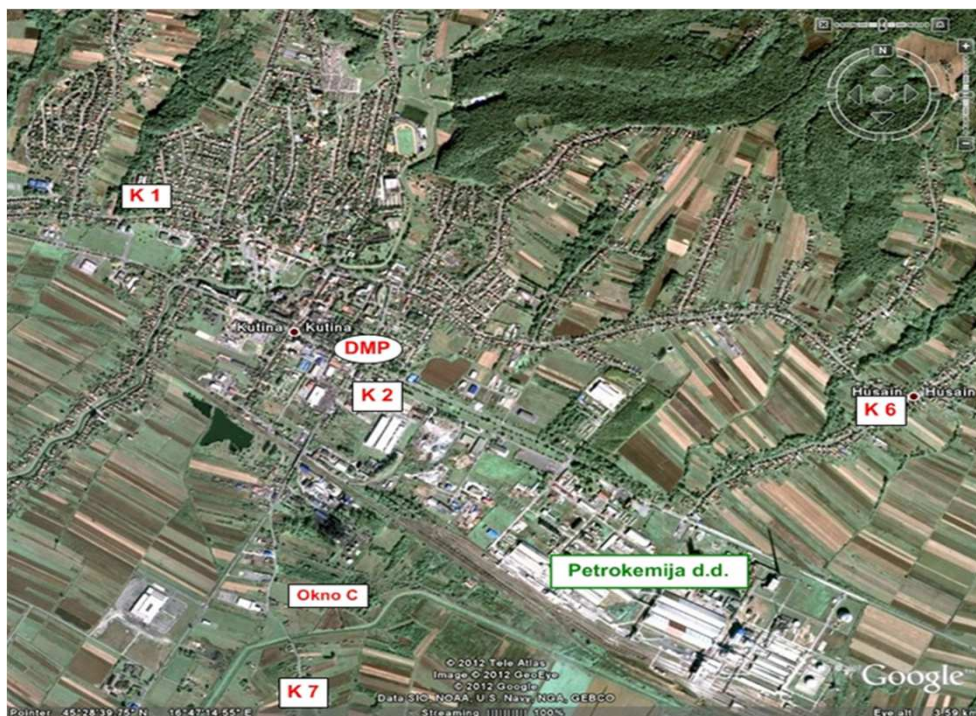
- Investment realized in reporting period 2018 amounted to HRK 38.7 million.
- Compared to the same period of the previous years, investments are approximately at the same level (index 102.9), but in the course of 2018 significant investments are planned, which will be realized in substantial part also through the complete annual overhaul of the facilities.
- On investments related to the meeting the requirements of the Environmental Permit and deadlines for execution of certain investment projects, which were significantly delayed and not completed within the prescribed deadline by 31.12.2017, talks are held with the competent authorities of the Government of Croatia.

### HRK million



Note: Data for Petrokemija d.d.

# Air quality in the Kutina area for January to June 2018 period at local monitoring station (K1,K2,K6 i K7) and the state monitoring station (DMP)



Clean or slightly polluted air	Polluted air	Pollutants
1 <sup>st</sup> category C<LV	2 <sup>nd</sup> category C>LV	
K2,DMP		Sulphur dioxide (SO <sub>2</sub> )
K1,K2,K6,K7		sediment
K1, K2, K6, K7,DMP		Ammonia (NH <sub>3</sub> )
K2,DMP		Nitrogen dioxide (NO <sub>2</sub> )
DMP		Hydrogen sulphide (H <sub>2</sub> S)
DMP		PM10

**Note:**

The categorization of air quality at DMP may be changed after validation of data that has not been made by the competent institution.

Note: Data for Petrokemija d.d.

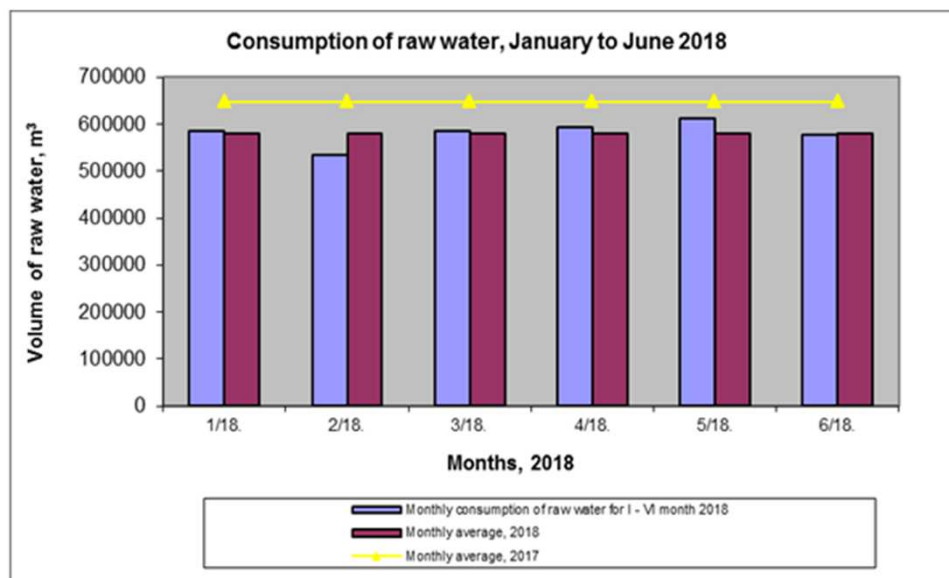


## Ambient air limit value (LV) exceedance of AMMONIA in the January to June 2018 period (local network) and Water Management

Monitoring station	The number of limit value (LV) exceedances in the <u>January to June 2018 period</u> /permitted exceedance number
K 1 - Dom zdravlja	3 / 7
K 2 - Vatrogasni dom	4 / 7
K 6 - Husain	6 / 7
K 7 - Krč	1 / 7
<b>TOTAL</b>	<b>14</b>

**Water mangement** - Petrokemija d.d. regulary monitors quantity and quality of waste water at discharge points according to Enviromental Permit. Also, the external authorized house performs the water quality analysis and the results are sent to the state authority.

In the period from January to June 2018, monthly average consumption of raw water is smaller than the average value in the same period of 2017.



Note: Data for Petrokemija d.d.



## Company share capital, share market value, changes in Supervisory Board, important events in the Company

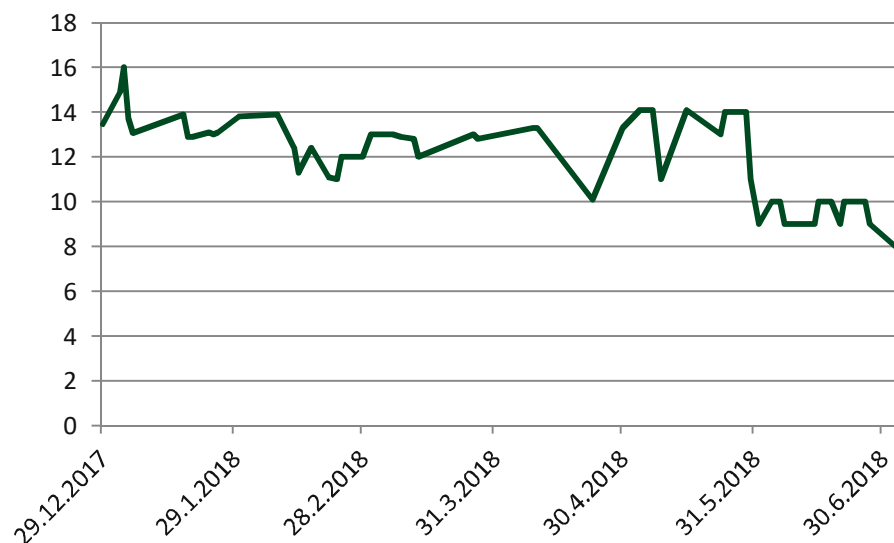
- At the General Meeting of 11 October 2017, the Company adopted the decision to reduce the share capital from HRK 386,135,400.00 by HRK 343,231,470.00 to the amount of HRK 42,903,930.00, by reducing the individual nominal value of PTKM-R-A ordinary share from HRK 30.00 to HRK 3.333, with at the same time merging ordinary shares at the 3:1 merger ratio, in such a way that 3 (three) ordinary shares of a single nominal amount of 3.333 HRK will be merged into 1 (one) ordinary share, ticker PTKM-RA, of HRK 10.00 nominal value. The last trading day of the existing 12,871,180 ordinary shares of the PTKM-RA was October 25, 2017, the first trading day with a new quantity, i.e. with the 4,290,393 regular shares of PTKM-R-A for which the settlement was made in the CDCC, on October 26, 2017
- On December 29, 2017, the average value of the share was HRK 13.47, and on June 27, 2018 HRK 9.00 (down 33.18 %).
- After the reporting period, the Supervisory Board issued a decision on terminating the mandate of Nenad Zečević, member of the Management Board as of 2 January 2018. As of 3 January 2018, the Board of Petrokemija d.d. acts as a two-member board consisting of Đuro Popijač, MS, Managing Director and Davor Žmegač, MS, Member of the Board.
- In addition to the existing natural gas suppliers, INA d.d. and Prvo plinarsko društvo d.o.o, as of February 2018, a new gas supplier – Hrvatska elektroprivreda d.d. (Croatian Electric Power Company) will be involved in the supply of natural gas for some of the required volumes of gas in the next period.
- At the end of May 2018 Petrokemija d.d. received a statement of interest for participation in recapitalization by INA Industrija nafte and Prvo plinarsko društvo.
- Following the Government Decision of 24 May 2018 on granting the power to conclude a contract on the transfer and sale of claims against Petrokemija d.d. Fertilizer Company, the Management Board of Petrokemija d.d. signed additional loan agreements with Erste & Steiermarkische Bank, Hrvatska poštanska banka and Bank for Reconstruction and Development (HBOR) with a new lender – the Republic of Croatia, totaling HRK 450 million.

Note: Data for Petrokemija d.d.

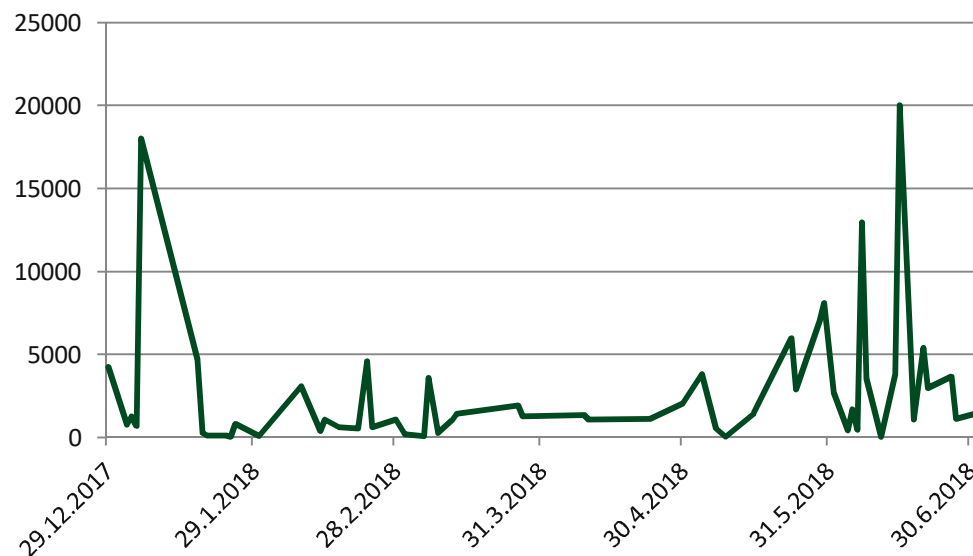


# Petrokemija, d.d. share price and daily turnover movements

PETROKEMIJA'S SHARE PRICE MOVEMENTS for  
January – June 2018 (HRK/share)



PETROKEMIJA'S DAILY SHARE TURNOVER MOVEMENTS for  
January – June 2018 (HRK)



Note: Data for Petrokemija d.d.



## Implementation of the Recapitalization program in 2017 and 2018

- ❑ With the help of financial and legal advisers in the first half of 2017, the Restructuring Program of Petrokemija d.d. - Concretization of the Proposal of Restructuring Concept by Recapitalization with Private Investors was drafted and adopted by Supervisory Board and the competent state institutions.
- ❑ At its 33rd session on 27 April 2017, the Government of Croatia adopted the Decision on exclusion from the sales of shares of companies: Hrvatski telekom d.d. Zagreb, Podravka Food Industry d.d. Koprivnica, Croatia Airlines d.d. Zagreb and Đuro Đaković Group d.d. Slavonski Brod. Petrokemija, d.d. had requested a loan of HRK 350 million from the Croatian Bank for Reconstruction and Development and the Croatian Government approved the institution of a lien on the shares of the above companies owned by the State for securing the loan repayment. Croatian Government passed the Decision on securing loan repayment to ensure the stability of Petrokemija's operations and maintenance of business processes, but also to create preconditions for the preparation and realization of the Company privatization.
- ❑ Following the decision of the Government of Croatia on securing loan repayment of 27 April 2017, Petrokemija d.d. signed longterm loan agreements with the Croatian Bank for Reconstruction and Development and the Croatian Postal Bank d.d., as well as a short-term financing agreement with Erste & Steiermarkische Bank d.d. in the total amount of HRK 350 million. The loan was used to secure the stability of Petrokemija's operations and to maintain business processes.
- ❑ On 31 May 2017, CERP established the obligation of the Management and Supervisory Board of Petrokemija d.d. to publicly announce the Call for Recapitalization and invite interested investors to engage in the Company restructuring and privatization process. In accordance with the above decisions and the contractual obligations assumed, the Management and Supervisory Board of Petrokemija are continuing the restructuring and recapitalization process of the Company based on the following strategic assumptions:
  - Modernization of production facilities with the aim of raising the level of energy and technological efficiency, as well as meeting the environmental requirements in accordance with EU regulations,
  - Providing financing sources of permanent working capital,

Note: Data for Petrokemija d.d.



## Implementation of the Recapitalization program in 2017 and 2018 (cont)

- more active appearance and strategic positioning on the market of Croatia and the region,
  - raising the level of efficiency of maintenance, logistics and other service processes in the Company that will ensure a positive financial result, stability and development of the Company.
- ❑ On 5 June 2017, upon approval of the Supervisory Board, the Management Board of Petrokemija, d.d. adopted the Decision on the Publication of Call for Indication of Interest in Recapitalization as one of the measures in preparation for the Restructuring Program and the Company privatization. The Call is in accordance with the Decision of the Government of the Republic of Croatia on the securing of loan repayment of 27 April 2017, long- term loan agreements with the Croatian Bank for Reconstruction and Development and the Croatian Postal Bank d.d. and the contract on short-term financing with Erste & Steiermarkische Bank d.d. in the total amount of HRK 350 million, which, among other things, determined the obligation of the Restructuring and Sale Center (CERP) to initiate the restructuring and privatization process of Petrokemija d.d.
  - ❑ Deadline for delivery of Letter of Intent to Petrokemija d.d. was 19 June 2017, but the Management Board of Petrokemija d.d. with the approval of Supervisory Board, issued a Decision on the amendment of the deadline, so the deadline for delivery of the Letter of Intent was extended by 30 June 2017. After the period from 5 to 30 June 2017, in which all interested investors could express their indicative interest in the recapitalization of Petrokemija d.d., the Company received a certain number of bids as well as requests for conducting due diligence analyses.
  - ❑ At its session held on July 5, 2017, Supervisory Board of Petrokemija d.d., gave its consent to the Management Board for implementing due diligence process of the Company and for opening the data room in accordance with established data lists and pre-signed confidentiality contracts. The due diligence was conducted in the period from 10 July to 15 August 2017. After completion of the process, interested investors were invited to submit binding bids by September 1, 2017, in accordance with the Restructuring Program of Petrokemija d.d. – Concretization of the Proposal of the Restructuring Concept by Recapitalization with a Private Investor, which is an integral part of the documentation in the process of due diligence.

Note: Data for Petrokemija d.d.



## Implementation of the Recapitalization program in 2017 and 2018 (cont)

- ❑ As some of the potential investors requested the extension of the deadlines for the due diligence analysis process, the Management Board, with the approval of Supervisory Board, issued a Decision on prolongation of Petrokemija's due diligence procedure until 31 August 2017 and of receiving binding bids in the recapitalization process by 22 September 2017.
- ❑ Following the stated indicative interest in the recapitalization of Petrokemija d.d., after the completion of the due diligence, interested investors were invited to submit binding offers in accordance with the Restructuring Program of Petrokemija d.d. – Concretization of the Proposal of Restructuring Concept by Recapitalization with Private Investor by September 22, 2017. After the publicly announced Call for Submitting Binding Offers in Recapitalization of Petrokemija d.d., the Company received binding bids from several interested bidders by the deadline stated in the Call and the notice of extension of the bidding deadline. Potential investors' offers were submitted to the Restructuring and Sale Center and the State Property Ministry for further proceedings.
- ❑ With the approval of the Supervisory Board and the Restructuring and Sale Center, the Company allowed potential strategic and non-strategic investors who submitted bids for participation in recapitalization within the Petrokemija restructuring process to conduct additional due diligence analyses in the period from 4 to 23 October 2017.
- ❑ The Extraordinary General Meeting on December 11, 2017 issued a Decision on the increase of the Company's registered capital. The entry of new shares will be conducted through the procedure of public offering by entering and paying in one round. The right to subscribe for New Shares would have all interested investors up to a maximum of 45,000,000 New Shares, or up to HRK 450,000,000 of share capital.
- ❑ The General Meeting held on 9 July 2018 put the decisions of the General Meeting of 11 December 2017 on the company share capital increase out of force and passed new decisions related to the final completion of the recapitalization process that are in accordance with the Decision of the Croatian Government on granting of the power to conclude a contract for the transfer and sale of claims toward the Petrokemija d.d. Fertilizer Company, passed on 24 May 2018.
- ❑ Due to the complexity of the process and the demands of potential strategic investors towards the majority owner (solving of debt issue, state aid, environmental permits, investment program, assets value and other open issues) the process has been extended to the second half of 2018. At the time of the preparation of these Reports, activities are underway, in line with the decisions of the General Meeting of 9 July 2018, which will define the future business model of Petrokemija d.d. This delay has put an additional burden to the relations with the natural gas suppliers in terms of debt repayment dynamics from the previous period and current payments.



## Significant financial risks in 2018

The overall business position of Petrokemija, d.d. in the first half of 2018 depends on a number of factors, whose impact is very difficult to estimate. Agreements reached on new natural gas procurement terms and repayment of natural gas debt have reduced part of the risk transferred from the previous period. However, according to the current market situation, it is estimated that in 2018 there will be an ongoing pronounced influence of variable levels of fertilizer prices in the world market and a relatively high level of natural gas price in Europe and Croatia. Also, the level of financial expense and operational management of the business will have a significant impact on the Company's insufficient liquidity and the high costs of CO<sub>2</sub> charges, financing costs and the exchange rate of the USD and EUR exchange rates. The financial result for the business year 2018 is likely to depend on the pace and scope of potential measures for restructuring of the Company and Petrokemija Group. In addition to the above, caution is still suggested due to the following risks:

- ❑ Petrokemija d.d. is highly dependent on the movements of fertilizers and their raw materials prices in the global market, the exchange rate of the HRK against USD and EUR and their interdependence,
- ❑ Natural gas as the most important raw material is still procured on the domestic market, according to contracts concluded with three suppliers – INA, d.d. Zagreb, Prvo plinarsko društvo d.o.o. Vukovar and as of February 2018, a new gas supplier – HEP d.d. Croatian Electric Power Company. The price of natural gas is linked to the EUR exchange rate and to the movement of natural gas prices on the European spot market. Reducing the price of natural gas transport on the basis of the 2017 tariff would have a positive effect on the financial result in 2018, although inadequate given the level of the same type of costs with EU competitors,
- ❑ The sales prices of fertilizers in the global market are still very low, short-term also influenced by cyclical and seasonal changes. The price of nitrogen fertilizer Urea has been at a low level for a long time, fluctuating sharply during the year and in the situation of a more pronounced growth of natural gas prices on the European spot market, manufacturing profitability may again be questioned.
- ❑ Lower VAT in 2017 had positive effects on mineral fertilizer sales in the domestic market, but the level of state incentives in agriculture and purchasing price of major crops will still have the key effect.

Note: Data for Petrokemija d.d.



## Significant financial risks in 2018 (cont)

- ❑ Purchasing prices of most primary raw materials are higher than in the previous period (except for raw phosphate). However, fluctuations in raw material prices in the world market, which have so far been present, will continue to have impact on material costs in the next period,
- ❑ Petrokemija d.d. in its production process inevitably emits a certain amount of greenhouse gases whose emissions cost about HRK 25 to 30 million a year. Given the limited sources of financing, the Company cannot purchase ETS units at the most favorable time, which significantly increases the risk of higher cost of greenhouse gas emission fees depending on the movement of the ETS market price in the open market. This was also the case in 2017 and in the first half of 2018;
- ❑ High costs of working capital – because of insufficient own working capital, financing costs will continue to be significant in the next period,
- ❑ In 2018, there are pronounced risks in finding new long-term sources of financing investment, and it is very difficult to set aside resources from operations to continue the intensive investment process. The deadlines for realization of a part of the so called ‘environmental investments’, according to the Decision on Integrated Environmental Protection Requirements have expired (31.12.2017), so most investments, due to funding difficulties, are transferred to 2018;
- ❑ The most important issue of the current operating business - the debt to natural gas suppliers – in the reporting period is again sharpened, so that the challenges of maintaining financial and business stability until the completion of the restructuring process are still present;
- ❑ Natural gas price fluctuations on the European spot market in the first half 2018 call for caution due to the high exposure of Petrokemija's business results to the so-called ‘price scissors’ risk - simultaneous rise of prices of raw materials, primarily natural gas, and the fall in sales prices of mineral fertilizers based on this raw material (Urea, CAN / AN);
- ❑ The business loss realized in 2017 and in the first half of 2018 indicates caution in forecasting financial and operating results for the business year 2018. Therefore, the Company's restructuring and recapitalization process as soon as possible is essential for business continuity in 2018 and the oncoming years.

Note: Data for Petrokemija d.d.





## Statement of management liability

In line with Articles 462 through 468 of Capital Market Act (OG 65/2018) the Managing Board of Petrokemija, d.d. Kutina, A. Vukovar 4, make a:

### Statement on Management Liability

Financial reports were made in accordance with International Financial Reporting Standards (IFRS). Financial reports are also compliant to Croatian Accounting Act, effective at the time of issuing of the reports.

Financial reports for the **January 1 to June 30, 2018 period**, make an exact and true account of the Company and the Group of Petrokemija financial status and the business and cash flow results, in compliance with the applicable accounting standards. This report may contain certain statements relating to the future business of Petrokemija, d.d. and Petrokemija Group, their strategy, plans and intentions which express a certain degree of uncertainty.

They reflect the current position of the Company with regard to risks, uncertainties and assumptions about the future. Currently, the results, effects and achievements of Petrokemija, d.d. or Petrokemija Group are heavily dependent on a large number of factors which may influence their being quite different from the originally set ones.

President of the Board:  
Đuro Popijač, MS

Member of the Board:  
Davor Žmegač, MS



## Attachments:

- Company Quarterly Financial Report - TFI-POD Grupa Petrokemija:
  - Balance Sheet
  - Profit and Loss Account
  - Report on Cash Flow
  - Report on Capital Change
  - Notes

**Attachment 1.**

Reported period:

01.01.2018.

to

30.06.2018.

**Quarterly financial statements TFI-POD**

Registration number (MB): 03674223

Registration number of subject  
(MBS): 080004355Personal identification  
number (OIB): 24503685008

Issuer company: PETROKEMIJA GROUP

Postal code and city: 44320

KUTINA

Street and number: ALEJA VUKOVAR 4

E-mail: [fin@petrokemija.hr](mailto:fin@petrokemija.hr)Internet address: [www.petrokemija.hr](http://www.petrokemija.hr)

Code and city/municipality: 220 KUTINA

Code and county name: 3 SISAČKO-MOSLAVAČKA

Number of employees: 1.699

(at the end of the year)

Consolidated Report: YES

Code of NKD: 20.15

Entities in consolidation (according to IFRS):

Registered seat:

Registration number (MB):

PETROKEMIJA d.o.o.

NOVI SAD

08754608

LUKA ŠIBENIK d.o.o.

ŠIBENIK

03037525

PETROKEMIJA AGRO TRADE d.o.o.

KUTINA

4424085

Book-keeping office:

Contact person: MARINA MARIĆ

(name and surname of the contact person)

Telephone number: 044-647-829

Fax: 044-682-795

E-mail: [marina.maric@petrokemija.hr](mailto:marina.maric@petrokemija.hr)

Name and surname: ĐURO POPIJAČ, DAVOR ŽMEGAČ

(authorized representatives)

**Documentation to be published:**

1. Financial Statements (Balance Sheet, Profit and Loss Account, Cash Flow Statement, Change in Capital Statement and Notes to Financial Statements)
2. Management Board's Report
3. Statement of persons in charge of making Financial Statements

(seal)

(signature of authorized representative)

## BALANCE SHEET

as at 30.06.2018.

Issuer: PETROKEMIJA GROUP			
Position	AOP code	Previous year (31.12.)	Current year
1	2	3	4
<b>A) RECEIVABLES FOR SUBSCRIBED BUT NOT PAID-IN CAPITAL</b>	<b>001</b>		
<b>B) LONG-TERM ASSETS (003+010+020+029+033)</b>	<b>002</b>	<b>681.863.501</b>	<b>686.898.972</b>
I. INTANGIBLE ASSETS (004 do 009)	<b>003</b>	<b>8.491.092</b>	<b>8.465.053</b>
1. Expense for development	<b>004</b>		
2. Concessions, patents, licences, trade and service marks, software and other rights	<b>005</b>	3.088.056	2.397.558
3. Goodwill	<b>006</b>		
4. Advances for intangible assets	<b>007</b>		
5. Intangible assets in progress	<b>008</b>	5.403.036	6.067.495
6. Other intangible assets	<b>009</b>		
II. TANGIBLE ASSETS (011 do 019)	<b>010</b>	<b>673.016.860</b>	<b>677.701.046</b>
1. Land	<b>011</b>	48.712.613	48.298.594
2. Buildings	<b>012</b>	207.105.451	192.885.730
3. Plant and equipment	<b>013</b>	301.611.693	330.968.894
4. Tools, plant inventory and transportation assets	<b>014</b>	18.299.524	17.246.504
5. Biological assets	<b>015</b>		
6. Advances for tangible assets	<b>016</b>	4.841.543	13.630.937
7. Tangible assets in progress	<b>017</b>	89.074.432	70.302.686
8. Other tangible assets	<b>018</b>	3.371.604	4.367.701
9. Investments in real estates	<b>019</b>		
III. LONG-TERM FINANCIAL ASSETS (021 do 028)	<b>020</b>	<b>7.536</b>	<b>7.536</b>
1. Investments (shares) in related companies	<b>021</b>		
2. Loans given to related companies	<b>022</b>		
3. Participating interest (shares)	<b>023</b>	7.536	7.536
4. Loans given to companies with participating interest	<b>024</b>		
5. Investment in securities	<b>025</b>		
6. Loans given, deposits and similar assets	<b>026</b>		
7. Other long-term financial assets	<b>027</b>		
8. Investments accounted for using the equity method	<b>028</b>		
IV. TRADE RECEIVABLES (030 do 032)	<b>029</b>	<b>197.676</b>	<b>575.000</b>
1. Receivables from related companies	<b>030</b>		
2. Receivables for sales on loan	<b>031</b>		
3. Other receivables	<b>032</b>	197.676	575.000
V. DEFERRED TAX ASSETS	<b>033</b>	150.337	150.337
<b>C) SHORT-TERM ASSETS (035+043+050+058)</b>	<b>034</b>	<b>394.547.931</b>	<b>399.422.407</b>
I. INVENTORIES (036 do 042)	<b>035</b>	<b>288.644.481</b>	<b>311.957.001</b>
1. Raw and other material	<b>036</b>	115.470.877	108.318.802
2. Work in progress	<b>037</b>	9.087.290	38.484.845
3. Finished products	<b>038</b>	162.787.924	163.271.380
4. Merchandise inventory	<b>039</b>	626.412	686.171
5. Advances for inventories	<b>040</b>	671.978	1.195.803
6. Long-term assets intended for sale	<b>041</b>		
7. Biological assets	<b>042</b>		
II. TRADE RECEIVABLES (044 do 049)	<b>043</b>	<b>70.842.783</b>	<b>56.063.351</b>
1. Receivables from related companies	<b>044</b>		
2. Receivables from customers (buyers)	<b>045</b>	22.480.210	5.911.132
3. Receivables from participating interest	<b>046</b>		
4. Receivables from employees and members	<b>047</b>	8.350	41.614
5. Receivables from state and other institutions	<b>048</b>	47.134.233	47.419.370
6. Other receivables	<b>049</b>	1.219.990	2.691.235
III. SHORT-TERM FINANCIAL ASSETS (051 do 057)	<b>050</b>	<b>5.749.727</b>	<b>20.614.329</b>
1. Investments (shares) in related companies	<b>051</b>		
2. Loans given to related companies	<b>052</b>		
3. Participating interest (shares)	<b>053</b>		
4. Loans given to companies with participating interest	<b>054</b>		
5. Investment in securities	<b>055</b>		
6. Loans given, deposits and similar assets	<b>056</b>	5.749.727	20.614.329
7. Other financial assets	<b>057</b>		
IV. CASH IN BANK AND IN HAND	<b>058</b>	29.310.940	10.787.726
<b>D) PREPAID EXPENSES AND ACCRUED INCOME</b>	<b>059</b>	<b>68.383</b>	<b>2.046.329</b>
<b>E) TOTAL ASSETS (001+002+034+059)</b>	<b>060</b>	<b>1.076.479.815</b>	<b>1.088.367.708</b>
<b>F) OFF BALANCE SHEET ITEMS</b>	<b>061</b>	740.969.603	1.152.615.143

<b>LIABILITIES</b>			
<b>A) CAPITAL AND RESERVES (063+064+065+071+072+075+078)</b>	<b>062</b>	<b>-195.341.805</b>	<b>-373.066.015</b>
I. SUBSCRIBED CAPITAL	063	42.903.930	42.903.930
II. CAPITAL RESERVES	064	3.923.969	3.923.969
III. RESERVES FROM PROFIT (066+067-068+069+070)	065	-11.600	-11.060
1. Legal reserves	066		
2. Reserve for treasury shares	067		
3. Treasury shares and investment (deductible item)	068	11.600	11.060
4. Statutory reserves	069		
5. Other reserve	070		
IV. REVALUATION RESERVES	071		
V. RETAINED EARNINGS OR LOSS CARRIED FORWARD (073-074)	072	-2.375.151	-245.053.745
1. Retained earning	073		
2. Loss carried forward	074	2.375.151	245.053.745
VI. PROFIT OR LOSS FOR THE BUSINESS YEAR (076-077)	075	-242.751.528	-177.605.500
1. Profit for the year	076		
2. Loss for the year	077	242.751.528	177.605.500
VII. MINORITY INTEREST	078	2.968.575	2.776.391
<b>B) PROVISIONS (080 do 082)</b>	<b>079</b>	<b>20.866.586</b>	<b>19.528.902</b>
1. Provisions for pensions, severance pay and similar liabilities	080	12.558.732	11.268.232
2. Provisions for tax liabilities	081		
3. Other provisions	082	8.307.854	8.260.670
<b>C) LONG-TERM LIABILITIES (084 do 092)</b>	<b>083</b>	<b>506.441.081</b>	<b>499.696.541</b>
1. Liabilities to related companies	084		
2. Liabilities for loans, deposits and similar	085	1.455.436	1.455.436
3. Liabilities to banks and other financial institutions	086	504.985.645	146.774.438
4. Liabilities for advances	087		
5. Liabilities to suppliers	088		
6. Liabilities for securities	089		
7. Liabilities to companies with participating interest	090		
8. Other long-term liabilities	091		351.466.667
9. Deferred tax liability	092		
<b>D) SHORT-TERM LIABILITIES (094 do 105)</b>	<b>093</b>	<b>676.563.111</b>	<b>827.573.983</b>
1. Liabilities to related companies	094		
2. Liabilities for loans, deposits and similar	095	182.030.213	242.324.277
3. Liabilities to banks and other financial institutions	096	126.656.256	10.192.952
4. Liabilities for advances	097	78.255.286	82.677.807
5. Liabilities to suppliers	098	264.758.956	468.107.725
6. Liabilities for securities	099		
7. Liabilities to companies with participating interest	100		
8. Liabilities to employees	101	11.204.085	10.929.744
9. Liabilities for taxes, contributions and other payments	102	7.968.864	11.709.540
10. Liabilities as per share in result	103		
11. Liabilities as per long-term assets intended for sales	104		
12. Other short-term liabilities	105	5.689.451	1.631.938
<b>E) ACCRUED EXPENSES AND DEFERRED INCOME</b>	<b>106</b>	<b>67.950.842</b>	<b>114.634.297</b>
<b>F) TOTAL LIABILITIES (062+079+083+093+106)</b>	<b>107</b>	<b>1.076.479.815</b>	<b>1.088.367.708</b>
<b>G) OFF BALANCE SHEET ITEMS</b>	<b>108</b>	<b>740.969.603</b>	<b>1.152.615.143</b>
<b>APPENDIX TO BALANCE SHEET (to be completed by companies that prepare consolidated financial statements)</b>			
<b>A) CAPITAL AND RESERVES</b>			
1. Credited to parent company capital owners	109	-198.310.380	-375.842.406
2. Credited to minority interest	110	2.968.575	2.776.391

Note 1.: The appendix to the balance sheet i to be filled if consolidated financial statements are to be compiled.

## PROFIT AND LOSS ACCOUNT

for the period 01.01.2018. to 30.06.2018.

Issuer: PETROKEMIJA GROUP					
Position	AOP code	Previous year		Current year	
		Cumulative	Quarterly	Cumulative	Quarterly
1	2	3	4	5	6
<b>I. OPERATING REVENUES (112+113)</b>	<b>111</b>	<b>960.337.225</b>	<b>366.071.494</b>	<b>919.567.332</b>	<b>457.014.933</b>
1. Sales revenues	112	936.013.911	354.618.602	899.009.135	444.023.490
2. Other operating revenues	113	24.323.314	11.452.892	20.558.197	12.991.443
<b>II. OPERATING EXPENSES (115+116+120+124+125+126+129+130)</b>	<b>114</b>	<b>1.012.721.696</b>	<b>410.692.261</b>	<b>1.029.491.171</b>	<b>530.558.841</b>
1. Changes in value of work in progress and finished products	115	4.668.720	-43.273.575	-29.881.010	16.686.793
2. Material costs (117 do 119)	116	822.610.330	363.416.161	877.093.790	421.252.261
a) Cost of raw and production materials	117	784.573.012	345.464.635	826.961.140	396.662.717
b) Cost of goods sold	118	6.599.266	1.223.691	12.458.362	4.844.928
c) Other external costs	119	31.438.052	16.727.835	37.674.288	19.744.616
3. Employees costs (121 do 123)	120	97.401.092	49.142.358	96.873.090	48.881.650
a) Net salaries and wages	121	61.894.375	31.194.697	61.411.508	30.947.112
b) Costs for taxes and contributions from salaries	122	21.300.528	10.779.947	21.374.746	10.840.428
c) Contributions on salaries	123	14.206.189	7.167.714	14.086.836	7.094.110
4. Depreciation	124	48.047.418	23.870.079	44.649.970	22.001.127
5. Other costs	125	39.891.470	17.434.992	39.784.509	20.922.969
6. Value adjustments (127+128)	126	102.666	102.246	868.006	711.225
a) of long-term assets (except for financial assets)	127	95.400	95.400	580.629	423.849
b) of short-term assets (except for financial assets)	128	7.266	6.846	287.377	287.376
7. Provisions	129			102.816	102.816
8. Other operating expenses	130				
<b>III. FINANCIAL REVENUES (132 do 136)</b>	<b>131</b>	<b>33.872.137</b>	<b>4.788.983</b>	<b>14.826.513</b>	<b>3.811.343</b>
1. Interest, exchange rate fluctuations, dividends and similar from associated companies	132				
2. Interest, exchange rate fluctuations, dividends and similar from non-associated companies and others	133	18.002.476	7.357.530	14.822.340	3.807.554
3. Part of revenue from associated companies and participating interests	134				
4. Unrealised gains (revenues) from financial assets	135				
5. Other financial revenues	136	15.869.661	-2.568.547	4.173	3.789
<b>IV. FINANCIAL EXPENSES (138 do 141)</b>	<b>137</b>	<b>22.557.148</b>	<b>11.686.507</b>	<b>82.496.603</b>	<b>28.578.483</b>
1. Interest, exchange rate fluctuations and other costs with associated companies	138				
2. Interest, exchange rate fluctuations and other costs with non-associated companies	139	20.792.393	11.686.507	33.319.581	17.623.750
3. Unrealised losses (costs) from financial assets	140				
4. Other financial expenses	141	1.764.755		49.177.022	10.954.733
<b>V. PORTION IN PROFIT OF ASSOCIATED COMPANIES</b>	<b>142</b>				
<b>VI. PORTION IN LOSS OF ASSOCIATED COMPANIES</b>	<b>143</b>				
<b>VII. EXTRAORDINARY - OTHER REVENUES</b>	<b>144</b>				
<b>VIII. EXTRAORDINARY - OTHER EXPENSES</b>	<b>145</b>				
<b>IX. TOTAL REVENUES (111+131+142 + 144)</b>	<b>146</b>	<b>994.209.362</b>	<b>370.860.477</b>	<b>934.393.845</b>	<b>460.826.276</b>
<b>X. TOTAL EXPENSES (114+137+143 + 145)</b>	<b>147</b>	<b>1.035.278.844</b>	<b>422.378.768</b>	<b>1.111.987.774</b>	<b>559.137.324</b>
<b>XI. PROFIT OR LOSS BEFORE TAXATION (146-147)</b>	<b>148</b>	<b>-41.069.482</b>	<b>-51.518.291</b>	<b>-177.593.929</b>	<b>-98.311.048</b>
1. Profit before taxation (146-147)	149	0	0	0	0
2. Loss before taxation (147-146)	150	41.069.482	51.518.291	177.593.929	98.311.048
<b>XII. PROFIT TAX</b>	<b>151</b>	<b>6.896</b>	<b>-93.991</b>	<b>11.571</b>	<b>-6.080</b>
<b>XIII. PROFIT OR LOSS FOR THE PERIOD (148-151)</b>	<b>152</b>	<b>-41.076.378</b>	<b>-51.424.300</b>	<b>-177.605.500</b>	<b>-98.304.968</b>
1. Profit for the period (149-151)	153	0	0	0	0
2. Loss for the period (151-148)	154	41.076.378	51.424.300	177.605.500	98.304.968

<b>APPENDIX TO PLA (to be completed by companies that prepare consolidated financial statements)</b>					
<b>XIV. PROFIT OR LOSS FOR THE PERIOD</b>					
1. Credited to parent company capital owners	155	-40.925.940	-51.403.390	-177.413.316	-98.208.385
2. Credited to minority interest	156	-150.438	-20.910	-192.184	-96.583
<b>STATEMENT OF COMPREHENSIVE INCOME (to be completed by company obligated to apply IFRS)</b>					
<b>I. PROFIT OR LOSS OF THE PERIOD (= 152)</b>	<b>157</b>	<b>-41.076.378</b>	<b>-51.424.300</b>	<b>-177.605.500</b>	<b>-98.304.968</b>
<b>II. OTHER COMPREHENSIVE GAINS/LOSS BEFORE TAXES (159 do 165)</b>	<b>158</b>	<b>32.290</b>	<b>32.290</b>	<b>0</b>	<b>0</b>
1. Exchange rate differences from translation of foreign currency operations	159	32.290	32.290		
2. Change in revaluation reserves of fixed tangible and intangible assets	160				
3. Gain or loss from revaluation of financial assets held for sale	161				
4. Gain or loss from effective cash flow hedge	162				
5. Gain or loss from effective hedge in net investments in abroad	163				
6. Portion in other comprehensive gain/loss of associated companies	164				
7. Actuarial gains / losses on defined benefit plans	165				
<b>III. TAX ON OTHER COMPREHENSIVE GAINS OR LOSSES FOR THE PERIOD</b>	<b>166</b>				
<b>IV. NET OTHER COMPREHENSIVE GAINS OR LOSSES FOR THE PERIOD (158-166)</b>	<b>167</b>	<b>32.290</b>	<b>32.290</b>	<b>0</b>	<b>0</b>
<b>V. COMPREHENSIVE GAIN OR LOSS FOR THE PERIOD (157+167)</b>	<b>168</b>	<b>-41.044.088</b>	<b>-51.392.010</b>	<b>-177.605.500</b>	<b>-98.304.968</b>
<b>APPENDIX TO STATEMENT OF COMPREHENSIVE INCOME (to be completed by companies that prepare consolidated financial statements)</b>					
<b>VI. COMPREHENSIVE GAIN OR LOSS FOR THE PERIOD</b>					
1. Credited to parent company capital owners	169	-40.893.650	-51.371.100	-177.413.316	-98.208.385
2. Credited to minority interest	170	-150.438	-21.000	-192.184	-96.583

## CASH FLOW STATEMENT - Direct method

for the period 01.01.2018. to 30.06.2018.

Issuer: PETROKEMIJA GROUP			
Position	AOP code	Previous year	Current year
1	2	3	4
<b>CASH FLOW FROM OPERATING ACTIVITIES</b>			
1. Cash increase from buyers	001	900.023.587	948.087.026
2. Cash increase from royalties, fees commissions and other	002		
3. Cash increase from insurance compensations	003	26.236.270	892.806
4. Cash increase from tax return	004	141.415.694	141.921.404
5. Other cash increase	005	317.934	427.310
<b>I. Total increase of cash flow from operating activities (001 do 005)</b>	<b>006</b>	<b>1.067.993.485</b>	<b>1.091.328.546</b>
1. Expenses to suppliers	007	1.102.777.131	848.831.025
2. Expenses for employees	008	102.661.264	98.316.415
3. Expenses for insurance compensations	009	6.066.944	4.367.735
4. Expenses for interest	010	14.477.826	25.744.057
5. Expenses for taxes	011	20.981.378	13.972.853
6. Other cash decrease	012	5.379.403	639.176
<b>II. Total decrease in cash flow from operating activities (007 do 012)</b>	<b>013</b>	<b>1.252.343.946</b>	<b>991.871.261</b>
<b>A1) NET INCREASE IN CASH FLOW FROM OPERATING ACTIVITIES (006-013)</b>	<b>014</b>	<b>0</b>	<b>99.457.285</b>
<b>A2) NET DECREASE IN CASH FLOW FROM OPERATING ACTIVITIES (013-006)</b>	<b>015</b>	<b>184.350.461</b>	<b>0</b>
<b>CASH FLOW FROM INVESTING ACTIVITIES</b>			
1. Cash proceeds from sale of non-current tangible and intangible assets	016	6.095.195	184.190
2. Cash proceeds from sale of equity and debt security instruments	017		
3. Cash proceeds from interest payment*	018		
4. Cash proceeds of dividend payment*	019		516.309
5. Other cash proceeds from investing activities	020		
<b>III. Total cash inflow from investing activities (016 do 020)</b>	<b>021</b>	<b>6.095.195</b>	<b>700.499</b>
1. Cash outflow for acquisition of non-current tangible and intangible assets	022	39.511.611	49.680.133
2. Cash outflow for acquisition of equity and debt financial instruments	023		
3. Other cash outflows from investing activities	024		
<b>IV. Total cash outflow from investing activities (022 do 024)</b>	<b>025</b>	<b>39.511.611</b>	<b>49.680.133</b>
<b>B1) NET CASH FLOW FROM INVESTING ACTIVITIES (021-025)</b>	<b>026</b>	<b>0</b>	<b>0</b>
<b>B2) NET CASH FLOW OUTFLOW FROM INVESTING ACTIVITIES (025-021)</b>	<b>027</b>	<b>33.416.416</b>	<b>48.979.634</b>
<b>CASH FLOW FROM FINANCIAL ACTIVITIES</b>			
1. Cash infows from issuance of equity and debt financial instruments	028		
2. Cash inflows from loan principals, debentures, credits and other borrowings	029	314.021.515	103.005
3. Other inflows from financial activities	030	32.620.660	5.636.410
<b>V. Total cash inflow from financial activities (028 do 030)</b>	<b>031</b>	<b>346.642.175</b>	<b>5.739.415</b>
1. Cash outflows for repayment of loan principal and bonds	032	104.590.173	54.239.269
2. Cash outflows for dividend payment	033		
3. Cash outflow for financial lease	034		
4. Cash outflows for buyback of own shares	035		
5. Other cash outflows for financial activities	036	29.623.189	20.501.011
<b>VI. Total cash outflow for financial activities (032 do 036)</b>	<b>037</b>	<b>134.213.362</b>	<b>74.740.280</b>
<b>C1) NET CASH FLOW INCREASE FROM FINANCIAL ACTIVITIES (031-037)</b>	<b>038</b>	<b>212.428.813</b>	<b>0</b>
<b>C2) NET CASHFLOW DECREASE FROM FINANCIAL ACTIVITIES (037-031)</b>	<b>039</b>	<b>0</b>	<b>69.000.865</b>
<b>Total increase of cash flow (014 – 015 + 026 – 027 + 038 – 039)</b>	<b>040</b>	<b>0</b>	<b>0</b>
<b>Total decrease of cash flow (015 – 014 + 027 – 026 + 039 – 038)</b>	<b>041</b>	<b>5.338.064</b>	<b>18.523.214</b>
<b>Cash and cash equivalents at the begining of the period</b>	<b>042</b>	<b>25.473.208</b>	<b>29.310.940</b>
<b>Increase of cash and cash equivalents</b>	<b>043</b>		<b>0</b>
<b>Decrease of cash adn cash equivalents</b>	<b>044</b>	<b>5.338.064</b>	<b>18.523.214</b>
<b>Cash and cash equivalents at the end of the period</b>	<b>045</b>	<b>20.135.144</b>	<b>10.787.726</b>

\*Inflow from interest and dividend can be listed as operating activities (MRS 7 Appendix A)



## STATEMENT OF CHANGES IN EQUITY

for the period from 1.1.2018 to 30.6.2018

Position 1	AOP code 2	Previous year 3	Current year 4
1. Suscribed capital	001	42.903.930	42.903.930
2. Capital reserves	002	3.923.969	3.923.969
3. Reserves from profit	003	-11.600	-11.060
4. Retained profit or loss carried forward	004	-2.375.151	-245.053.745
5. Profit or loss for the year	005	-242.751.528	-177.605.500
6. Revaluation of fixed tangible assets	006		
7. Revaluation of intangible assets	007		
8. Revaluation of financial assets available for sale	008		
9. Other revaluation	009	2.968.575	2.776.391
<b>10. Total capital and reserves (AOP 001 do 009)</b>	<b>010</b>	<b>-195.341.805</b>	<b>-373.066.015</b>
11. Exchange differences on translation of financial statements of foreign operations	011		
12. Current and deferred taxes (part))	012		
13. Protection of cash flow	013		
14. Changes in accounting policies	014		
15. Adjustment of significant errors from previous period	015		
16. Other changes in capital	016		
<b>17. Total increase or decrease of capital (AOP 011 do 016)</b>	<b>017</b>	<b>0</b>	<b>0</b>
17 a. Credited to parent company capital owners	018	-198.310.380	-375.842.406
17 b. Credited to minority interest	019	2.968.575	2.776.391

Items that decrease the capital are entered with a minus sign.

Items under AOP mark 001 to 009 are entered as status on balance sheet date.

## **PETROKEMIJA GROUP**

As can be seen from the data in the tables of the Profit and Loss account and Balance sheet, the subsidiaries have no significant impact on the performance of the Petrokemija Group. Subsidiaries are: Petrokemija, d.o.o. Novi Sad, Luka Šibenik, d.o.o. Šibenik and Petrokemija Agro trade, d.o.o. Kutina.

### INTRODUCTION

In the reporting period January - June 2018, Petrokemija Group continued to operate in a very complex situation of unfinished recapitalization, difficulties in liquidity and adverse conditions in the market environment. With the support of the majority owner, the natural gas suppliers and financial institutions, the Company maintained the continuity of production and its operations, is fulfilling its obligations to the customers; it is carrying out the facilities overhaul and the investments necessary to continue the business in order to prevent major damages for the stakeholders of this process.

Following an unfavorable situation in the fourth quarter of 2017, the business environment of Petrokemija in the first half of 2018 was marked by many challenges. In the reporting period, the negative effects of full openness to the global market i.e. Petrokemija's exposure to the risks of the neighboring and wider business environment were quite apparent, which result in very high costs for the Company without the possibility of its influence on them. Namely, Petrokemija carried forward all the bad debts of the unfinished recapitalization process of 2017 into the first half of 2018. Furthermore, the negative financial effects are even more intensified by:

- high rise in the price of CO<sub>2</sub> allowances (new costs and value adjustment of liabilities from previous years),
- further growth in natural gas purchase price,
- the fall in sales prices of mineral fertilizers on the global market,
- increase in purchasing prices of other raw materials (MAP, DAP, potassium chloride)
- decrease in total sales volumes due to lower sales of mineral fertilizers in overseas exports because current prices were significantly lower than the variable production costs realized by Petrokemija.

The biggest single impact on the financial result was the price increase of the CO<sub>2</sub> emission units (+84.8% compared to late 2017). The risk of correcting the value of the obligation to purchase the missing CO<sub>2</sub> emission units created by 31.12.2017 could not be prevented due to the restriction of the company's liquidity, thus charging the financial result with the amount of HRK 49.2 million in the reporting period. When HRK 14.4 million of the fee for the first half of 2018 is added, it means that out of the HRK 176.0 million loss in the first half of 2018, HRK 63.6 million or 36% accounts only for the CO<sub>2</sub> allowances.

The next most important impact on the loss of business is the growth of natural gas price. The realized price of natural gas is 11.2% higher than the realized average in the same period of 2017. This growth resulted in an additional cost of HRK 60.5 million, as compared to the same period of the previous year and accounts for 34% of the realized loss in the first half of 2018. In addition to the existing natural gas suppliers, INA d.d. and Prvo plinarsko društvo d.o.o, as of February 2018, a new gas supplier – Hrvatska elektroprivreda d.d. (Croatian Electric Power Company) has been involved in the supply of natural gas for some of the required volumes of gas in the reporting period.

The two items mentioned - natural gas and CO<sub>2</sub> allowance account for 70% of the realized loss in the reporting period. These are the risks that the Company could not have

had influence on in the current business model because it could not contract a more favorable gas procurement model as the gas suppliers are also the creditors of the Company and bear the risk of collecting relatively high receivables. Due to carried-forward liabilities from the previous period, the Company was not able to regularly settle the liabilities to natural gas suppliers. Furthermore, due to the lack of financial resources for regular purchases of CO<sub>2</sub> emission units (e.g. in the first half of the previous year, when the prices of emission units were significantly lower), the Company had the already mentioned additional loss of HRK 49.2 million in the first half of this year.

In the reporting period, there was also an increase in the prices of other major raw materials. The average purchasing price of the main raw materials for NPK fertilizer production - MAP was higher by 11.1% (expressed in USD) and potassium chloride by 10.4% (expressed in EUR) than in the same period of the previous year. The changes in the exchange rates of the USD and EUR against the Croatian kuna have resulted in the growth of potassium chloride share in Petrokemija's costs by about the same amount, as the EUR exchange rate was approximately at the same level (index 99.6%), while the rise in MAP price, due to the fall of the USD exchange rate, was neutralized in HRK amounts. The price of raw phosphate is below the level of the same period last year.

**The remaining 30% of the loss (apart from the price of natural gas and the allowances for CO<sub>2</sub> emission units), is made up of all other business elements** - lower revenues due to low sales prices and smaller sales volumes, interest on loans, costs of facilities standstills for technical and technological reasons and other costs that could not be covered by realized revenues.

Mineral fertilizer sales amounted to 519 thousand tons, 5.2% down on the same period of the previous year, as due to the sharp fall of sales prices in the global market it was not possible to sell under covering the direct variable production costs; simultaneous rise in raw material prices (natural gas) and fall of the price of finished products (Urea and CAN). Production of mineral fertilizers was realized at 538 thousand tons, 6.3% down on the same period of the previous year, partly due to technical and technological issues, and partly due to the unfavorable conditions on the sales market.

After a long period of preparations, in the conditions of limited funding for investments, an extensive biennial overhaul of Petrokemija's facilities is currently being conducted in order to provide good technical and technological condition of the facilities for the following period and partly to invest in modernization and increase of energy efficiency.

Due to the lack of liquidity, investments in the first half of the current year amounted to HRK 38.7 million, but another significant amount should be invested in the overhaul and other activities for which long-term sources have not been secured. All these costs are covered from the current business operations or the expected recapitalization. The completion of the recapitalization process should have a beneficial effect on balancing the Company liquidity and normalizing the investment and modernization system that is currently under significant pressure from the due liabilities towards suppliers for the delivered natural gas.

As regards market position, the adverse effects of the Agrokor Group are still present in the domestic and regional market. It is well known that the Agrokor Group, as the organizer of agricultural production, is the most important single factor in the entire value chain, from the production of crops to the processing industry and the food distribution chain, so that its problems have impact on numerous food producers of different profiles and sizes, from family farms to large systems. Although it does not have such great significance in the region, the disturbance of Agrokor Group's business has also had an impact on mineral fertilizer buyers on the markets of neighboring countries, primarily Slovenia, Bosnia and Herzegovina and Serbia. Successful completion of the creditors' settlement process in Agrokor will probably have a positive impact on the trend of intensifying sales growth on the domestic and regional mineral fertilizer markets.

The goals of the sales strategy in 2018 and 2019 are increasing sales in the regional, and in particular in the domestic market. However, they are not being realized in the first part of the year due to unfavorable conditions in the environment. Establishing direct partnerships with as many direct customers – mineral fertilizers consumers – is one of the positive results, with the aim of strengthening long-term competitive position of Petrokemija d.d. in the domestic market and a decrease in imports of mineral fertilizers into Croatia compared to previous years.

Fertilizer manufacturers in Europe are under strong pressure from the competition of major global manufacturers who have a comparative advantage of cheap raw material sources, from natural gas to phosphate rock, potassium chloride and sulfur. In these conditions, even successful European mineral fertilizer producers, who had benefited from a favorable trend for modernization of plants and restructuring in the previous decade, experienced a fall in profit and some even losses. Accordingly, it was inevitable for Petrokemija, which has been struggling to maintain business continuity for years and operating in conditions of lower technological and energy efficiency than its European competitors, to report losses in business. The most significant negative factor for the loss in the first half of 2018 is the high rise in the price of CO<sub>2</sub> allowances and of natural gas, which accounts for about 70% of the reported loss. In the remaining part of the year the greatest uncertainty is the potentially high purchase price of natural gas, which is for Petrokemija about 10% higher than for its competitors, partly because of the terms for defining the purchase price (suppliers are also the largest creditors of the Company) and partly because of the extremely high costs of gas transport, which are among the highest in the EU.

After years of attempts of changing the ownership structure and attracting into its ownership structure large investors in the value creation chain – from production and trading with natural gas, to logistics of sales of mineral fertilizers to end users – in the reporting period, the current owners have carried out extensive and complete preparation for the implementation of the privatization process and opening of a new development cycle of the Company, where all its current potentials would be exploited – from favorable location, well-maintained production and logistics systems, to skilled labor. Shortage of financial potential that manifests itself in the impossibility of changing the business model and of quick adaptation to constant market changes should be resolved in 2018 by permanent capital sources and a new management model of future investors. Loans granted by HBOR and commercial banks in 2016 and 2017 helped to fill the cash gap transferred from previous years, and recapitalization should create the preconditions for a balanced financing model for modernization of the facilities and investment in greater efficiency of all processes in the Company.

At the time of the preparation of these Reports, activities are underway in line with the decisions of the General Meeting of 9 July 2018, which define the future model of Petrokemija d.d. Upon completion of the privatization process of the Company, it is expected that the State (i.e. CERP) will remain in the position of one of the shareholders, but without a dominant position in the structure of ownership and management rights.

#### 1. Financial result for January – June 2018

In the January to June 2018 period, Petrokemija Group had total income of HRK 934.4 million and total expense of HRK 1,112.0 million. The Company reported loss in operations of HRK 177.6 million or 19.0% of the total revenues. In the same period previous year, the Company had a loss of HRK 41.1 million, which indicates a negative development in the financial result of HRK 136.5 million. The main causes of the losses in the first half of 2018 are high rise of price of CO<sub>2</sub> allowances, further growth of natural gas purchase price and the fall of sales prices of mineral fertilizers in the global market.

The EBITDA (earnings before interest, taxes, depreciation and amortization) is negative amounting to HRK -65.3 million and the EBITDA margin was -6.9%. The total revenues for the first half of 2018 are down by 6.0% on the same period of 2017, while total expenditures were up by 7.4%. These figures point to a fall of revenues due to a decrease in sales volumes of 5.2%, with simultaneous growth of costs for already mentioned reasons.

Basically, all the key business risks of Petrokemija's business in the first half of 2018 are the result of adverse global market situation, marked by low fertilizer prices in greater part of the reporting period, with simultaneous growth of average natural gas prices. Since Petrokemija, d.d. is exposed to the impact of global trends and has no financial strength or instruments to adapt to the emerging situation in the wider environment quickly and effectively, the situation in the European and global markets had impact on the high losses in business.

The main constraint to higher domestic sales in the remaining business year continues to be linked to the issue of demand and of customers' liquidity. Additional significant limitations come from the operational challenges that the Agrokor Group, as a major customer of mineral fertilizers, is faced with in the reporting period. In this context, business challenges that their business partners in the agricultural sector are faced with can also be seen, which can significantly affect the level of sown areas and fertilization in the autumn season of 2018 and spring season of 2019. The successful process of the Agrokor creditors' settlement spurs optimism in this respect. Due to own structure of indebtedness, Petrokemija has still no long-term sources of financing deferred payments to buyers of mineral fertilizers. Other constraints affecting the level of sales on the domestic market are the dynamics and level of incentive payments on the domestic market and the increasingly present principle of purchase at the last moment before application with direct field manipulation (without the cost of storing and re-loading).

Reducing the VAT rate in 2017 boosted demand for mineral fertilizers and helped balance the price level in the region, but the key effect will still be the extent of Government incentives in agriculture and the purchase prices of major agricultural crops, as well as the developments in the Agrokor Group crisis.

## 2. Structure of financial result

In the structure of financial result for January to June 2018, notable is the HRK 109.9 million operating loss, while HRK 67.7 million loss was generated from financial activities, resulting in the total loss of HRK 176.0 million in the reporting period. Financial loss is the result of external factors – **value correction of the CO<sub>2</sub> EU emission allowances (HRK 49.2 million)** and interest costs due to high loan debt. The price of EU emission allowances pronouncedly varied in 2017 and 2018, and had a significant impact on the quarterly financial results. In the same period last year, the impact of the fall in the prices of the emission units was HRK 15.9 million positive, and in the reporting period of 2018 it was HRK 49.2 million negative, which means that on this basis a negative movement was generated in the financial result of HRK 65.1 million kuna or 48% of the total difference in the loss level of the first half of 2018/2017.

The positive balance of foreign exchange gains had an impact on the financial result of Petrokemija d.d. of about HRK 8.9 million in the first half of 2018.

In addition to the above, the level of financial expenditures was also affected by the adverse financing structure, i.e. high debt. In the reporting period, critical liabilities to natural gas suppliers were partially resolved, most of the debt to banks was resolved by the Government decision of 24 May 2018 in a way that a part of the loan liabilities to banks (HBOR, HPB and Erste Bank) of a total of HRK 450 million was taken over by the Republic of Croatia as the new creditor. As part of the recapitalization process, activities are under way to find more

favorable sources of long-term financing of the Company and to eliminate the consequences of high indebtedness transferred from the previous period. Maintaining current liquidity in the first half of 2018 was very difficult.

As on 30 June 2018, the capital and reserves amounted to HRK -373.1 million, or HRK 177.7 million less than on 31 December 2017, corresponding to the level of the loss in business. The level of the losses of the previous and the reporting period is higher than the share capital, which indicates the necessity of urgent recapitalization as the continuation of the business is at stake.

### 3. Revenues

In the reporting period, the falling trend of mineral fertilizer prices was continued, which had a negative effect on business revenues, so that despite all the adjustments of the assortment and the increase of sales on the domestic and regional markets, there was no positive operating result. This is corroborated by the fact that at 5.2% lower mineral fertilizer sales volume, the earned operating income was 4.3% lower as compared to the previous year, although more NPK fertilizer was sold, which normally has higher price than other products.

Domestic sales in volume is at the level of the previous year (index 100.0) The level of mineral fertilizer sales in early 2018 was also influenced by Petrokemija's high sales in the fourth quarter of 2017, so a part of these volumes was transferred to the spring season. Also, it is partly the result of fertilizer import into Croatia for which there are no official statistical figures yet, but is estimated to be above the level of the volumes in the same period last year. It is estimated that the sales in Croatia are still unsatisfactory due to economic exhaustion and low liquidity of Croatian agriculture, as well as to insufficient support from commercial banks.

The consequence of the obligation of Petrokemija, d.d. to have volumes of mineral fertilizers continuously on stock under pledge due to high indebtedness to one of the natural gas suppliers, is that not even volumes of finished products for which there was market demand, were sold. Another constraint to larger domestic sales was the financial impossibility of Petrokemija to grant domestic buyers sales of mineral fertilizers with the expected margins, rebates and deferred payment of 60 to 180 days. An additional challenge in the sales of mineral fertilizers on the domestic market is the pressure to lower the prices of mineral fertilizers due to the extremely high pressure of low prices by competitive mineral fertilizers manufacturers from the region (Hungary, Bosnia and Herzegovina, Serbia and Italy) and the increase in natural gas prices in the open market.

The level of export sales volumes is down by 7.1% as a result of unfavorable prices at some regional markets and efforts to minimize the negative effects of sales on distant overseas markets where the sales price in some transactions does not cover the costs of direct raw- and production materials and indirect sales costs. Balancing the production and sales of mineral fertilizer products that had better sales prices, ensured business continuity and current liquidity. An additional challenge were the significant fluctuations of mineral fertilizer prices over the reporting period.

### 4. Expenses

Operating expenses were up by 1.7% compared to the same period of the previous year in spite of lower production and sales. It is the result of the growth in purchasing prices of a part of raw materials, in particular the growth of natural gas price in the open market. The prices of the main raw materials for the production of mineral fertilizers in the world market were by about 11% higher, with the highest rise achieved in MAP and potassium chloride (key raw materials for NPK fertilizers). The price of natural gas ranged independently of the price trend

of other raw materials, with a 11.2% higher price in the first half of 2018, compared to the previous year (the price includes transport costs, expressed in HRK). Overhead costs are mainly at the level of the previous year, with exceptions relating to the volume of production and sales, or the contracted packaging, such as cost of packaging, export services and other costs that vary according to the level of business activity. Overall, it can be estimated that sustained production continuity had positive effect on operating business performance. In the event of longer suspended production, negative effects would have been even greater due to the high fixed costs and additional costs of gas transport fees on a full-for-empty basis, as well as costs of energy products and intermediates at the shutdown and start-up of the facilities, which inevitably accompany the halt of production.

## 5. Natural gas supply

In the reporting period, Petrokemija, d.d. supplied natural gas from two permanent suppliers - INA d.d. Zagreb and Prvo plinarsko društvo d.o.o. Vukovar, pursuant to earlier concluded contracts. Since February 2018, a new gas supplier – Hrvatska elektroprivreda d.d. (Croatian Electric Power Company d.d. has been included in the supply with a part of the required gas volumes in the reporting period.

The price was determined by an escalating formula based on the actual prices on the European natural gas market (CEGH hub). The average realized purchase price of natural gas (with transportation costs, expressed in HRK) in the reporting period Jan to June 2018, was 11.2% higher than in the same period of 2017 period. This percentage is subject to constant changes in 2018, in line with the price movements on the European natural gas spot market. Thus, the key risks in purchasing natural gas are price fluctuations in the spot market and changes in the EUR exchange rate since the basic prices are formed in that currency.

In the course of 2017, upon an international tender, Petrokemija, d.d. concluded new contracts for natural gas supply in the gas year 2017/2018 with the existing natural gas suppliers INA d.d. Zagreb and Prvo plinarsko društvo d.o.o. Vukovar, as the most advantageous suppliers in the tender. In February 2018, a contract was signed with a new natural gas supplier – Hrvatska elektroprivreda d.d. (Croatian Electric Power Company), Zagreb.

On the basis of an international invitation to tender, Petrokemija, Plc. concluded a new contract for natural gas supply **in the gas year 2018/2019** for the total volumes required. The contract was concluded with suppliers INA d.d. Zagreb and Prvo plinarsko društvo d.o.o Vukovar as the two most competitive tenderers.

With this contract, Petrokemija has secured sufficient volumes of natural gas for the planned stable production during the gas year 2018/2019.

The negotiating position in contracting new natural gas deliveries is burdened by Petrokemija's high level of debt to the suppliers of natural gas delivered in the previous period. The growth in natural gas prices in the European spot market, especially since the last quarter of 2017, has again put into focus the imbalance between the purchase price of natural gas and the price of nitrogen fertilizers on the global market.

As a result of the decision of the Croatian Energy Regulatory Agency (HERA) as of 17 March 2017 the price of natural gas transport was reduced. However, the cost of natural gas remains to be a significant item in the cost structure of Petrokemija, since the price of natural gas transport in Croatia is among the most expensive in the EU. In the first half of 2018, Petrokemija had HRK 42.6 million in transport costs, and in the same period previous year the cost was HRK 45.0 million, i.e. a decrease of 5.3%. The cost of natural gas transport is

around HRK 85 to 90 million a year. For Petrokemija's direct competitors in Hungary and Austria, natural gas transport cost is twice or even six times lower, respectively. In order for Petrokemija d.d. to approach at least partially to direct competitors, the realistic cost of natural gas transport should be about HRK 40 million annually. It is necessary to reduce this cost in the future by active communication with all relevant authorities (the Croatian Government, the Ministry of Environmental Protection and Energy, HERA, PLINACRO) that define the natural gas transportation fee, because the cost at the existing level is unsustainable.

## 6. Production and capacity utilization

In the January to June 2018 period, Petrokemija, d.d. achieved 6.3% lower total production as compared to the previous year. Lower production is the result of alignment with the needs and dynamics of deliveries of finished products to the market and occasional facilities downtime due to technical and technological reasons.

In the production structure, the following changes occurred: 16.2% lower production of Urea, 8.5% that of CAN and 16.3% higher production of NPK fertilizers. In the reporting period, production capacity utilization was 84%, and the production range was adjusted to market conditions and constraints.

Due to market reasons, the phosphoric acid and carbon black production plants have been stalled since mid-2009. This issue was carried over into the third quarter of 2018. The crisis caused by the imbalance of input and output prices on the carbon black market is still ongoing, so that different options and solutions are being considered for both stalled plants, including calculations for the potential dismantling of equipment and site remediation. In accordance with the above considerations, when preparing the audited annual financial statements of Petrokemija d.d. for 2017, upon auditors' suggestions, significant value adjustments were made of unused assets and non-salable supplies of the spare parts charged to the loss of 2017.

## 7. Environmental protection

On 10 July 2015, following the request by the operator, Petrokemija, d.d. Fertilizer Company, the Croatian Ministry of Environment and Nature Protection passed a Decision on Integrated Environmental Protection Requirements for the operation of the existing 14 mineral fertilizer production plants at Petrokemija, d.d. Aleja Vukovar 4 in Kutina.

The Decision was issued for a period of five years and published in full on the website of the Croatian Ministry of Environment and Nature Protection. The Decision on Integrated Environmental Protection Requirements was a necessary requirement for obtaining all necessary permits related to the technical and technological operating conditions for manufacturing facilities of Petrokemija, d.d. in the next five years.

In accordance with the Decision, some of the activities were carried out during the extensive biennial overhaul in 2016 and the investment cycle was continued in 2017 (HRK 103.3 million realized investment). In the first half of 2018, only HRK 38.7 million was invested due to the lack of liquidity. However, in the course of the year, a further significant amount should be invested in the the large biennial overhaul and other activities. No long-term sources have been secured for this – everything is covered from current operations, or the expected recapitalization.

Environmental projects are becoming increasingly important in the legislative environment of EU, and the deadlines for completion were for the most part missed (31 December 2017), so in the following years Petrokemija d.d. will be forced into urgent and significant investments



in this segment. In accordance with the IPPC Directive and the Decision on Integrated Environmental Protection Requirements, in order to meet all the prescribed technical and technological requirements of environmental protection, Petrokemija must invest approx. HRK 380 million. So far, a little over a third of the total planned funds has been realized.

## 8. Liquidity

Due to the losses in previous periods, Petrokemija, d.d. has inadequate sources for funding working capital. In the reporting period, the issue of debt to suppliers was raised again, due to increasing difficulty in maintaining liquidity, i.e. the high due debt to the natural gas suppliers. In spite of its growing liquidity deficits during the first half of 2018, Petrokemija d.d. repaid HRK 53.6 million in loans and paid HRK 25 million interest on loans as well as HRK 2.4 million in interest to other suppliers.

## 9. Recapitalization

In order to mitigate the financing imbalance and maintain business continuity, in August 2016, the Company obtained a long-term loan of HRK 200 million from the Croatian Bank for Reconstruction and Development, with a 100% guarantee of the Croatian Government, thereby securing a portion of long-term sources of financing of working capital and continuity of activities in restructuring the business.

Pursuant to the decision of the Government of the Republic of Croatia, the Company Management Board initiated the preparation of the Restructuring Program that has to be submitted to competent bodies (Ministry of Economy, Ministry of Finance and CERP), so they would be able to carry out a possible pre-notification or notification procedure to the European Commission (DG Competition).

At its 33rd session on 27 April 2017, the Government of the Republic of Croatia adopted the Decision on exclusion from the sales of shares of companies: Hrvatski telekom d.d. Zagreb, Podravka Food Industry d.d. Koprivnica, Croatia Airlines d.d. Zagreb and Đuro Đaković Group d.d. Slavonski Brod. Petrokemija, d.d. had requested a loan of HRK 350 million from the Croatian Bank for Reconstruction and Development and the Croatian Government approved the institution of a lien on the shares of the above companies owned by the State for securing the loan repayment. Commercial banks were also involved in the realization of the loan. Croatian Government passed the Decision on Securing Loan Repayment to ensure the stability of Petrokemija's operations and maintenance of business processes, but also to create prerequisites for the preparation and realization of the Company privatization.

With the assistance of financial and legal advisers, Restructuring Program of the Company and the Petrokemija Group was prepared and was approved by the Supervisory Board and CERP. In the previous period, a comprehensive due diligence analyses of the business of Petrokemija d.d. and Petrokemija Group had been conducted by several interested investors, and potential investors' offers were received.

At the General Meeting of 11 October 2017, the Company adopted the decision on reduction of the share capital from HRK 386,135,400.00 by HRK 343,231,470.00 to the amount of HRK 42,903,930.00, by reducing the individual nominal value of PTKM-RA ordinary share from HRK 30.00 to HRK 3.333, with at the same time merging ordinary shares at the 3:1 merger ratio, in such a way that 3 (three) ordinary shares of a single nominal amount of 3.333 HRK will be merged into 1 (one) ordinary share, ticker PTKM-RA, of HRK 10.00 nominal value.

The Extraordinary General Meeting of 11 December 2017 adopted a Decision on the increase of the Company share capital. The subscription of the New Shares would be conducted through the procedure of public offering by subscription and payment in one

round. All interested investors would have the right to subscribe for a maximum of 45,000,000 New Shares, or up to HRK 450,000,000.00 of share capital.

The General Meeting held on 9 July 2018 put the decisions of the General Meeting of 11 December 2017 on the company share capital increase out of force and passed new decisions related to the final completion of the recapitalization process that are in accordance with the Decision of the Croatian Government on the granting of the power to conclude a contract for the transfer and sale of claims toward the Petrokemija d.d. Fertilizer Company, passed on 24 May 2018. In this respect, decisions were passed as follows: Decision on the increase of the Company share capital by stake in rights and issuance of shares with the exclusion of the pre-emptive rights of the Company shareholders, Decision on amendments to the Company Articles of Association, Decision on granting approval for acquiring shares without the obligation of publishing a takeover bid, Decision on simplified reduction of the Company share capital by merging the shares to cover the losses and transfer of funds to the capital reserves, Decision on the increase of the Company share capital by contributions in cash and issuance of new shares with the exclusion of the shareholder's priority rights and changes to the Company's Articles of Association, and the Decision on granting the acquisition of shares without obligation to publish takeover bids, all in accordance with the decision proposals published in the Invitation to the said General Meeting published on 29 May 2018 on the web pages of the Zagreb Stock Exchange, HINA and Petrokemija d.d., in the Register of Regulated Information (Hanfa) and in the Court Register.

At the end of May 2018, Petrokemija d.d. received statements of interest to participate in the recapitalization from INA Industrija nafte and Prvo plinarsko društvo.

Following the Government Decision of 24 May 2018 on granting the power to conclude a contract on the transfer and sale of claims against Petrokemija d.d. Fertilizer Company, the Board of Petrokemija d.d. signed annexes to loan agreements with Erste & Steiermarkische Bank, Croatian Postal Bank and Croatian Bank for Reconstruction and Development with a new creditor, Republic of Croatia, totaling HRK 450 million.

Due to the complexity of the process and the demands of potential strategic investors towards the majority owner (solving of debt issue, state aid, environmental permits, investment program, assets value and other open issues) the process has been extended to the second half of 2018. At the time of the preparation of these Reports, activities are underway, in line with the decisions of the General Meeting of 9 July 2018, which will define the future business model of Petrokemija d.d. This delay has put an additional burden to the relations with the natural gas suppliers in terms of debt repayment dynamics from the previous period and current payments.

#### 10. Financial risks in the subsequent period

In addition to the above, the future trends of Petrokemija's financial result will be influenced by numerous factors. Next to the overall economic trends in Croatia, natural gas prices and terms of natural gas supply, which are predominantly defined on the domestic market, most of the future risks come from the international environment, mainly through:

1. Natural gas price trends in the European spot market;
2. Changes in price of basic raw materials in the world market (MAP, DAP, phosphate, potassium chloride and sulfur);
3. Changes in demand and sales prices of mineral fertilizers;
4. Price trends of CO<sub>2</sub> emission units;
5. Price trends of basic agricultural crops;
6. Exchange rate of EUR and USD to the local currency and their interdependence;

7. Costs of financing and cross-currency relations;
8. Agricultural policy of EU and Croatia.

The exposure of Petrokemija, d.d. and Petrokemija Group to developments in the global market opens up significant potential risks in terms of price and financial fluctuations in the remaining part of 2018. Effective risk management of natural gas price growth (contracted price is in EUR, although purchasing is done on the domestic market) and risk of USD and EUR exchange rate changes in the procurement of other imported raw materials is limited by the lack of own working capital (negative working capital of HRK -551 million, whereas on 31 December 2017 it was HRK -363 million) and by the lack of support of financial institutions in financing working capital and investments.

In its production process, Petrokemija inevitably emits greenhouse gases for whose emission it allocates significant funds, which, depending on the price of ETS units in the open market, amount to about HRK 25 to 30 million a year. Due to limited funding sources, the Company cannot purchase ETS units at the best time, which significantly increases the risk of higher cost of greenhouse gas emission fees depending on the price movement of ETS units in the open market. This was the case in 2017 and in the first half of 2018 and it significantly contributed to an increase in losses (by HRK 63.6 million).

The long-term loans from HBOR and HPB and a short-term one from ERSTE Bank secured a part of the long-term sources of financing working capital and the continuation of activities in restructuring the business in 2017. However, the challenges of maintaining financial and operational stability are still present until the completion of the recapitalization process. Most of the debt to banks was resolved by the decision of the Croatian Government of May 2018, with the purchase of part of the loan liabilities from banks (HBOR, HPB and Erste Bank), of a total of HRK 450 million in favor of the new creditor, Republic of Croatia.

Due to the Company's insufficient liquidity, advance payments are used in the sales of mineral fertilizers, which, due to the economic exhaustion of Croatian agriculture results in lower demand and therefore a poorer market position of Petrokemija, d.d. in Croatia. The market and financial results for the first half of 2018, as well as the assessment of market position at the time of the preparation of these financial statements (in particular in terms of uncertain domestic sales and the comparatively low prices of mineral fertilizers on the open market, threatened liquidity and solvency of the Company), call for caution in predicting future trends in business in 2018. The unsteady natural gas prices on the European spot market raise again the issue of the imbalance between the purchase price of natural gas and the price of nitrogen mineral fertilizers on the global market (Urea and CAN), causing constant uncertainty in the estimates of financial results, as the duration of either a positive or a negative trend is hard to predict.

The decisions of the majority owner about the future recapitalization model, in accordance with the decisions of the General Meeting of 9 July 2018, will have significant influence on reducing the risk of maintaining business continuity in the future 2018-2027 period.