

## LETTER FROM THE PRESIDENT OF ZUE S.A.

Ladies and Gentlemen,

I am pleased to present the report of the ZUE Group for 2018.

In 2018, the Group generated sales revenue to the tune of PLN 832.7m. The risks faced by the industry have materialised and created a strong pressure on the Group's margins. The Group reported operating loss of PLN -77.9m, EBITDA of PLN -67m and net profit/loss of PLN -62.6m.

After reviewing the budgets of the construction contracts, the Company's Management Board decided to reduce projected margins on some railway construction contracts performed for PKP PLK S.A. and even recognise negative margins on several projects. The decision concerned the contracts won mainly on the difficult market in 2016 and 2017.

The aforesaid decline stemmed primarily from contractual obstacles that were beyond the Company's control (including but not limited to undefined legal status of plots, delayed administrative procedures, unavailable work sites, physical conditions differing from those assumed in the ToR, including the land survey documents and technical condition of facilities, results of specialist expert reports, changes to applicable laws or expectations of local communities) and prevented the performance of the contracts according to the original assumptions made at the tendering stage on the basis of tender documentation provided to contractors. The foregoing circumstances were accompanied by a radical increase in the costs of labour, building materials, services provided by subcontractors and logistic services as well as impediments in the supply of goods and lengthy tender procedures.

At the beginning of 2017, the Group partially protected itself against a radical increase in the prices of building materials by signing a number of master agreements for the supply of strategic materials with the manufacturers thereof. However, the Group had no influence on other cost increases faced by the construction industry, especially labour costs, and had to deal with their consequences. According to the law and the contracts signed by the Group, remuneration payable to the contractor may be changed if specific risks occur independently of the contractor. We talk to contracting authorities and lodge reasonable contract claims. The Group intends to continue and complete the projects according to the contracts but it also intends to make reasonable amendments thereto, especially to the amount of its remuneration.

The two subsidiaries within the Group produced positive financial results in 2018.

There is and there will be a significant number of orders on the tram and railway infrastructure market. In 2019, the Government amended the National Railway Programme by increasing the amount to be spent on the upgrade of railways until 2023 to PLN 69.6bn (up by PLN 3.2bn). Design documentation for the projects financed under another EU perspective is being prepared. PKP PLK reports that in 2021 it will be ready to announce tenders for contracts worth PLN 30-40bn, which is supposed to

offset the investment downturn effect between subsequent EU perspectives. Positive trends are also emerging on the urban infrastructure market. In 2018, the Company won urban contracts for the total amount of approx. PLN 236m. These are mainly the contracts performed in the "Build" formula, characterised by the ability to quickly enter the construction site and short turnaround times. After several years of stagnation, since 2018 the biggest cities with tram infrastructure have announced or planned to announce the new tenders for the projects financed under the current EU perspective.

Our backlog is worth approx. PLN 1.9bn. It includes the contracts won at the end of 2016 and at the beginning of 2017 (some with a loss recognised by the Group) and the contracts of 2018. We submitted the most economically advantageous tenders with the total value of approx. PLN 619m in 2018 and 2019 and participate in new tenders. The Company wants to leverage the industry prospects by continuing the expansion of the backlog in a selective manner taking into account the industry risks, logistic advantages and the intention to increase the share of urban contracts in its portfolio. We are also interested in international contracts, mainly on the European market. 2018 witnessed frequent cancellations of tender procedures by awarding entities due to the fact that bidders exceeded the previously created project cost estimates.

We have taken measures to become independent of third party service providers – we have expanded the structures to be able to deliver reinforced concrete projects, such as viaducts, bridges, resistance walls or noise barriers. We also invest in building equipment. The total capital expenditure incurred by the Group in 2018 amounted to PLN 20.6m.

The situation of the Group is stable despite the difficult year. ZUE did not use any available credit lines in 2018 and financed operating activities with own resources. At the end of the reporting period, the Group's cash was PLN 81.7m.

We are widely recognized by the business environment. We received the title "Pearl of the Polish Economy 2018" and as a consortium member "Infrastructure and Construction Diamond 2018" in the railway infrastructure project of the year category.

Our main strategic goal is to take a maximum advantage of the current EU perspective and to continue to strengthen the market position of ZUE and build up the Company's value for its Shareholders.

Yours sincerely,

Wiesław Nowak  
Management Board President

ZUE S.A.