

## **REPORT OF THE SUPERVISORY BOARD OF IZOSTAL S.A.**

**on the results of the assessment of the following documents submitted by the Management Board:**

- **financial statement of Izostal S.A. for 2011**
- **Management Board's report on the Company's activity in 2011**
- **Management Board's motion on appropriation of net profit for 2011,**

**including the assessment of the Company's situation in 2011**

Supervisory Board examined the financial statement of IZOSTAL S.A. for 2011 and analyzed the report and opinion of the chartered auditor, Kancelaria Porad Finansowo-Księgowych dr Piotr Rojek Sp. z o.o. seated in Katowice who examined the Company's financial statement for that period.

On this basis the Supervisory Board states that the financial statement of Izostal S.A. for 2011 comprising:

- introduction to financial statement,
- financial position statement prepared as on December 31, 2011 showing the amount of PLN 272,426 thousand (say: two hundred and seventy-two million four hundred and twenty-six thousand zlotys) under assets and liabilities,
- comprehensive income statement for the financial year from January 1, 2011 to December 31, 2011, showing a comprehensive income of PLN 19,134 thousand (say: nineteen million one hundred and thirty-four thousand zlotys),
- statement of changes in equity for the financial year from January 1, 2011 to December 31, 2011 showing an increase of equity by PLN 18,930 thousand (say: eighteen million nine hundred and thirty thousand zlotys),
- cash flow statement for the financial year from January 1, 2011 to December 31, 2011, showing an increase in net cash by PLN 3,510 thousand (say: three million five hundred and ten thousand zlotys),
- notes and explanations,

was prepared in line with the effective accounting regulations, and complies with the books and documents. Therefore the business results for 2011 and the material and financial standing of the Company are shown correctly and reliably and the presented facts based on figures reflect the actual condition.

Given the results of the aforementioned analyzes, the Supervisory Board passed a resolution requesting the Annual General Meeting to approve the following documents submitted by the Management Board:

- the financial statement of Izostal S.A. for 2011,
- the Management Board's report on the Company's activity in the financial year 2011.

Supervisory Board also read and accepted a proposal concerning the appropriation of profit for 2011 in the amount of PLN 19,133,666.78 (say: nineteen million one hundred and thirty-three thousand six hundred and sixty-six zlotys $\frac{78}{100}$ ), to be submitted for approval by the Annual General Meeting, with the following profit appropriation:

- Company's spare capital: PLN 13,567,186,78 (thirteen million five hundred and sixty-seven thousand one hundred and eighty-six zlotys, 78/100);
- payment of dividend for Company shareholders of PLN 5,566,480.00 (five million five hundred and sixty-six thousand four hundred and eighty zlotys 00/100), that is PLN 0.17 (seventeen grosz) of dividend per share. According to the proposal all the shares issued by the Company (32,744,000 shares) should be eligible for the dividend.

The Supervisory Board has no reservations as to the dividend right date falling on August 10, 2012 and the dividend payment date planned on September 3, 2012.

### **Brief assessment of the Company's situation.**

Supervisory Board is of the opinion that 2011 was a year of dynamic development of the market in the sector which resulted in a significant increase in demand for Company's products.

In January 2011 rights to K series shares were for the first time quoted in the Warsaw Stock Exchange. The price on the debut's date exceeded the issue price by 23.64%. At the closing of the session the shares price was PLN 7.07 showing an increase of 28.5% relative to the issue price. Following the public offering of 12 million K series shares at PLN 5.50 per share the company obtained PLN 66,000 thousand (gross). The Company allocated the net earnings from the offering to working capital and to the implementation of the project involving the establishment of the Research and Development Center for Steel Products and Technologies. This new Research and Development Center for Steel Products and Technologies will make it possible to introduce the new products and services, which previously were not offered by the Company, and will also have impact on the current operations of the Company by optimizing the research and development processes in progress, provision of research services to third parties and diversification of Company's production. The Company concluded a subsidy agreement with the Minister of Economy on the co-financing of the construction of the Research and Development Center for Steel Products and Technologies under the Operating Program Innovative Economy, for the amount of PLN 7,263 thousand.

The actual financial results of the Company in 2011 confirm an increase in demand on the infrastructural market of materials for the construction of gas infrastructure and a significant share of IZOSTAL S.A. in this market. The fact of placing 880,165 m<sup>2</sup> of the Company's main product being the steel pipes' coating makes an increase in sales level of 87.8% against 2010.

In 2011 Company's revenues amounted to PLN 259,732 thousand, which was by 88% higher than in 2010. With these revenues, net profit of PLN 19,134 thousand was recorded, being by 257% higher than in 2010. Company's development finds confirmation also in carrying amount, which amounted to PLN 272,426 thousand on December 31, 2011, which was by PLN 68,960 thousand higher than at the end of 2010.

The Supervisory Board is of the opinion that the Company succeeds in implementing its strategy and achieves the target financial revenues.

While assessing the system of managing risk significant for the Company, the Supervisory Board underlines the indirect dependence of Izostal S.A. on PGNiG S.A. (prospecting for resources, exploration, trade and distribution of gas) and OGP Gaz-System S.A. (operator of

the transmission system), as well as on the investments planned and implemented by the above-mentioned companies in the aspect of structural characteristics of the Polish market. To minimize risk, Izostal S.A. looks for new sales markets, both in Poland (private investors, development of technology for coating the pipes to be used for drillings), and abroad.

Moreover, the Supervisory Board is of the opinion that the Company's financial situation is correlated with macroeconomic situation in Poland. Financial results recorded by the Company are also shaped by general factors such as the pace of GDP growth, pace of investment growth, changes in inflation level, exchange rates, unemployment rate and personal income, as well as fiscal and monetary policy of the state. This risk however is minimized by the strategy of diversifying gas supply sources adopted by Poland, and restrictive regulations in scope of environmental protection and CO2 emission imposed by the European Union. Those factors enforce large investments in the gas and petrochemical sectors in Poland which are an opportunity for the Company to increase the sales of its products. Furthermore, the risk is mitigated by a necessity to utilize aid funds from multiple sources within the deadline prescribed, including among others European Energy Program for Recovery (EEPR, the so-called Recovery Plan), Operational Program Infrastructure and Environment 2007-2013, Trans-European Networks – Energy (TEN-E) Program and Operational Program Innovative Economy.

Profitability of anticorrosion coating services depends on changes in prices of production components required for production. To minimize the risk connected with changing prices of production components, the Company follows diversification strategy based on co-operation with several entities at each production stage and builds its stocks.

The Supervisory Board also assessed the risk connected with changes in the price of pipes. In order to avoid the risk related to high volatility in steel pipes' prices, the Company optimizes its stocks levels adapting them to the scope of the conducted business.

In special cases steel pipes are purchased for stock at current prices to supplement the product mix in volumes making it possible to sell goods and make profit.

The risk of exchange rate changes assessed by the Supervisory Board also has a considerable impact on the profitability of sales. The Company concluded the treasury limit agreements which make it possible for the Company to conclude foreign exchange hedging transactions with banks without encumbrances.

In view of the very good financial results of the Company in 2011 and huge involvement of the Management Board in the operating management, and especially in the development processes, the Supervisory Board considers it justified to request the General Meeting to grant a vote of approval to management Board members of Izostal S.A. for performance of their duties in 2011.

Zawadzkie, 3.04.2012

**Signatures of Supervisory Board Members**

Jerzy Bernhard, SB Chairman

Zdzisław Mendelak, SB Vice-Chairman

Jan Chebda, SB Secretary

Jan Kruczak, SB Member

Lech Majchrzak, SB Member

Adam Matkowski, SB Member