



November 16, 2015

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## **Q3 2015 - Management Discussion and Analysis**

Last quarter saw a decrease of prices of scrap metal, semi-finished and most of our finished products. Although, such price development might be assessed negatively we consider this to mark a turning point for the electric arc furnace (EAF) steel manufacturers for whom scrap metal constitutes a vital component in their cost structure. The dynamics of prices allowed for significant billet and product spread gains and those, we hope, are not just the episodes, rather they are likely to form a longer term pattern. Expanding spreads indicate the possible improvement of our results in near term, after the volatile price environment has stabilized.

The significance of the above noted trend relates not only to the issue of costs themselves but, more importantly, to the issue of competitive position of EAF producers vis-à-vis the basic oxygen furnace (BOF) ones. Since 2011 it has been undermined by increasingly cheaper iron ore and coking coal, both creating a big advantage of the BOF cost model over the EAF one. While we have been observing sharp scrap metal declines, no further meaningful iron ore or coking coal decreases seem possible. This should allow both Cognor S.A. (Cognor, the Company, the Group) as well as the other EAF producers to gradually regain the former competitive position within the broader steel production market. Although the drop of the global steel output in the last quarter became a fact again, also in China, Cognor is in our opinion well positioned to benefit from the strong Polish and German demand. With scrap metal and steel product prices expected to remain low as well as with energy cost reductions, the EAF producers should be better protected against the turbulences of the global market.

Meanwhile, the declining prices together with the lower sales of the combined semi-finished and finished products, had their strong and negative effect on our EBITDA. This was magnified by the foreign exchange losses related to our indebtedness and resulted in the higher net loss for the period as compared to Q3 2014. The demand for steel products remained fair and thus we managed to achieve satisfactory results of sales within our finished products' segment. The effect of the increasing shipments of those was however counterbalanced by the lesser sales of billets, affected by the competition from the BOF producers. Along with the concurrent decline of prices our scrap metal supplies suffered significantly and so the segment noted lower sales both tonnage and value-wise as well as it had lower profit as compared to Q3 2014.

## I. Reported Statement

### 1. Income Statement

As compared to Q3 2014 the Group's revenues fell by PLN 25.2 million and 6.9% entirely due to the decrease of prices of scrap metal, semi-finished and finished products while the combined shipments improved by 6.7 thousand tones and 4.0%. Gross profit fell by PLN 17.1 million and 49.4% driven by lower profitability of sales of all of those segments. The weighted average price of billets and products fell by PLN 31.6 per tonne as compared to Q2 2015 and translated into the reduction of gross profit by PLN 4.2 million. EBIT and EBITDA decreased by PLN 8.6 and 9.0 million accordingly. EBITDA margin fell down to just 2.4% from 4.7%. The FX had negligible effect on our operations with the average EUR/PLN slightly above the one in Q3 2014. It had a noticeable impact though on our net financial costs - the FX losses related to the Group's debt stood at PLN 5.0 million driven by the weakening zloty against the euro: EUR/PLN quoted at PLN 4.24 as of September 30, 2015 and at PLN 4.19 as of June 30, 2015.

AVERAGE EXCHANGE RATES		Q3 2015	Q3 2014
	PLN		
EUR/PLN		4.19	4.17
	% change	0.5%	
USD/PLN		3.77	3.15
	% change	19.7%	

EXCHANGE RATES		30-Sep-2015	31-Jun-2015	30-Sep-2014
	PLN			
EUR/PLN		4.24	4.19	4.18
	% change	1.2%		
USD/PLN		3.78	3.76	3.30
	% change	0.5%		

INCOME STATEMENT		Q3 2015	Q2 2015	Q3 2014
	'000 PLN			
Revenue		341 788	353 147	366 967
Cost of sales		-324 249	-322 714	-332 330
<b>Gross profit</b>		<b>17 539</b>	<b>30 433</b>	<b>34 637</b>
Other income		1 328	703	-831
Distribution expenses		-11 426	-11 881	-11 102
Administrative expenses		-8 288	-8 376	-11 064
Other gains/(losses) – net		1 645	1 426	238
Other expenses		-1 375	-1 409	-3 891
<b>EBIT</b>		<b>-577</b>	<b>10 896</b>	<b>7 987</b>
Financial income		-5 466	-10 899	1 799
Financial expenses		-13 011	-10 305	-15 750
<b>Net financing costs</b>		<b>-18 477</b>	<b>-21 204</b>	<b>-13 951</b>
Share of profits of associates		-86	-46	33
<b>Profit before tax</b>		<b>-19 140</b>	<b>-10 354</b>	<b>-5 931</b>
Income tax expense		4 889	3 452	1 034
<b>Profit for the period</b>		<b>-14 251</b>	<b>-6 902</b>	<b>-4 897</b>
Depreciation and amortization		-8 824	-8 649	-9 286
<b>EBITDA</b>		<b>8 247</b>	<b>19 545</b>	<b>17 273</b>

The spreads for our semi-finished and finished products remained below the levels of Q3 2014. The combined product spread for Ferrostal went down by PLN 37 per tonne and for HSJ by PLN 40 per tonne. The Ferrostal's billet spread fell by just PLN 2 per tonne which was rather the effect of the concentration on production and sales of the profitable steels while some of the billet grades sold in Q3 2014 would have proved unprofitable in the last quarter and therefore were not produced and sold.

The analysis of spreads is a measure of current condition and trends in the steelmaking business. As indicated by the above spread calculation, the market offered more space for profitability a year ago however, the last quarter brought a very meaningful enhancement as compared to Q2 2015. We are currently observing a continuation of the improvement of those spreads, which originates from the greater magnitude of the decrease of scrap metal price as compared to the decrease of prices for our billets and finished products.

Since our inventory cycle equals almost a period of three months and because we use the FIFO valuation method, the development of the spreads gets reflected in the accounts with an approximately quarterly time lag. We therefore expect the contribution of any spread development in the following quarter. The improvement in Q3 2015 indicates the possible increase in profitability in the coming quarters.

The negative spread development was partially offset by the higher efficiency of our steel plants resulting from the decrease of some of our production costs.

PRICES AND SPREADS	Q3 2015	Q2 2015	Q1 2015	Q4 2014	Q3 2014	Q2 2014
<i>(pln/ tonne)</i>						
<b>FERROSTAL</b>						
<b>SCRAP METAL</b> - all purchases	861	961	938	966	966	972
<b>BILLETS</b> - sales to external customers	1 677	1 751	1 817	1 929	1 784	1 744
<b>BILLET SPREAD</b>	<b>816</b>	<b>790</b>	<b>879</b>	<b>963</b>	<b>818</b>	<b>772</b>
<b>FINISHED PRODUCTS</b> - sales to external customers	1 848	1 917	1 935	1 971	1 989	2 066
- plain bars	1 950	1 966	1 970	2 015	2 051	2 076
- flat bars	1 965	1 992	1 998	2 022	2 040	2 070
- squares	1 951	1 946	1 957	2 014	2 034	2 056
- rebars	1 651	1 749	1 802	1 870	1 846	1 938
- angles	1 963	1 946	1 973	2 052	2 083	2 120
- other	2 094	3 029	2 158	0	3 971	3 475
<b>PRODUCT SPREADS</b>	<b>986</b>	<b>956</b>	<b>998</b>	<b>1 006</b>	<b>1 023</b>	<b>1 095</b>
- plain bars	1 089	1 005	1 032	1 049	1 085	1 105
- flat bars	1 104	1 031	1 061	1 057	1 074	1 099
- squares	1 090	985	1 020	1 048	1 068	1 087
- rebars	796	788	864	904	880	966
- angles	1 102	985	1 035	1 086	1 117	1 148
- other	1 233	2 068	1 220	0	3 005	2 502
<b>HSJ</b>						
<b>SCRAP METAL</b> - all purchases	881	1 000	995	1 024	1 048	1 034
<b>FINISHED PRODUCTS</b> - sales to external customers	2 688	2 649	2 810	2 876	2 900	2 950
- big rounds	2 576	2 548	2 737	2 726	2 761	2 808
- thick sheets	2 218	2 376	2 573	2 649	2 912	6 420
- thin sheets	10 540	10 570	11 144	11 247	11 379	11 126
- other	20 052	25 271	22 924	23 514	29 635	25 941
<b>PRODUCT SPREADS</b>	<b>1 807</b>	<b>1 649</b>	<b>1 815</b>	<b>1 852</b>	<b>1 852</b>	<b>1 916</b>
- big rounds	1 695	1 548	1 742	1 702	1 713	1 774
- thick sheets	1 337	1 376	1 578	1 625	1 864	5 386
- thin sheets	9 659	9 570	10 149	10 223	10 331	10 092
- other	19 171	24 271	21 929	22 490	28 587	24 907

The non-recurring items had some positive effect on EBITDA and negative on our net result. The following adjusted EBITDA and net profit figures facilitate an analogous assessment of the Group's results achieved from the ordinary course of business:

DESCRIPTION	Q3 2015	Q2 2015	Q3 2014
	'000 PLN		
<b>Reported EBITDA</b>	<b>8 247</b>	<b>19 545</b>	<b>17 273</b>
Non-recurring items including:	1 529	1 444	-2 917
- costs of sales	0	0	-19
- other income	219	72	184
- distribution expenses	-97	132	-579
- other gains/losses	1 149	882	66
- operational FX result	496	544	91
- other impairments	-238	-186	-2 660
<b>Adjusted EBITDA</b>	<b>6 718</b>	<b>18 101</b>	<b>20 190</b>
<b>Reported net result</b>	<b>-14 251</b>	<b>-6 902</b>	<b>-4 897</b>
Non-recurring items including:	-3 888	-7 148	-3 449
- EBITDA adjustments	1 529	1 444	-2 917
- FX result on debt	-5 040	-10 640	-1 462
- share of associate result	-86	-46	49
- result on own debt repurchase	0	2 368	403
- pro-forma income tax adjustment	-291	-274	478
<b>Adjusted net result</b>	<b>-10 363</b>	<b>246</b>	<b>-1 448</b>

According to the above, the Q3 2015 adjusted EBITDA stood at PLN 6.7 million and the adjusted net result was a loss at PLN 10.4 million – a deterioration as compared to the figures of Q3 2014.

The main entities of the Group made the following contribution to the consolidated results for Q3 2015:

	FERR	ZW-WB	PROFIL	HSJ	ZLMET
	'000 PLN				
Revenues	155 944	6 873	12 547	119 524	89 728
- incl. Internal	655	6 762	12 536	329	40 557
EBIT	-1 437	429	1 731	-172	-543
EBITDA	1 178	651	2 141	3 273	39
<b>Profit for the period</b>	<b>-3 449</b>	<b>403</b>	<b>1 691</b>	<b>-17 654</b>	<b>-820</b>

## 2. Balance Sheet

The amount of total assets decreased by 0.9% in comparison to Q3 2014 primarily due to the 7.3% decrease in value of fixed assets caused by the provision against the entire amount of the claim owed by the Republic of Croatia at the amount of EUR 10.0 million (other receivables). The increase in current assets, by 4.6%, was mostly fueled by the 11.7% increase of inventories. Reverse relations with respect to current assets can be observed when compared with the figures of Q2 2015 where there was a decrease in value of inventories by 12.8%; non-current assets saw a stabilization.

ASSETS	Q3 2015	Q2 2015	Q3 2014
<i>'000 PLN</i>			
<b>A. TOTAL NON-CURRENT ASSETS</b>	<b>417 572</b>	<b>412 701</b>	<b>450 334</b>
I. Intangible assets	10 826	10 772	11 776
II. Property, plant and equipment	280 856	280 140	294 515
III. Other receivables	85	67	42 113
IV. Investment property and other investments	16 683	16 878	2 196
V. Prepaid perpetual usufruct of land	22 314	22 450	24 471
VI. Deferred tax assets	86 808	82 394	75 263
<b>B. TOTAL CURRENT ASSETS</b>	<b>542 251</b>	<b>596 815</b>	<b>518 638</b>
I. Inventories	277 839	318 455	248 807
II. Receivables	244 767	250 281	227 228
1. Trade receivables	240 081	245 847	204 494
2. Current income tax receivable	10	10	47
3. Other investments	4 676	4 424	22 687
III. Cash and cash equivalents	14 097	20 969	33 828
IV. Assets classified as held for sale	5 548	7 110	8 775
<b>TOTAL ASSETS</b>	<b>959 823</b>	<b>1 009 516</b>	<b>968 972</b>

In Q3 2015 the Group increased its leverage with the gross debt amounting to PLN 515.9 million and the net indebtedness at 501.8 million - more by PLN 50.5 million as compared to Q3 2014 and by PLN 14.5 million in comparison to Q2 2015. The main reason behind the enlargement of debt as compared to Q3 2014 was the increase of working capital by PLN 36.8 million. The increase of debt in comparison with Q2 2015 came from the foreign exchange loss related to the Groups' indebtedness, at PLN 5.0 million and from the net loss suffered in the period.

EQUITY AND LIABILITIES	Q3 2015	Q2 2015	Q3 2014
<i>'000 PLN</i>			
<b>A. EQUITY</b>	<b>169 356</b>	<b>186 558</b>	<b>223 115</b>
I. Issued share capital	133 542	132 444	132 444
II. Reserves and retained earnings	14 153	32 568	65 871
III. Minority interest	21 661	21 546	24 800
<b>B. LIABILITIES</b>	<b>790 467</b>	<b>822 958</b>	<b>745 857</b>
I. Non-current liabilities	454 968	448 801	461 157
1. Employee benefits obligation	9 597	9 597	9 215
2. Interest-bearing loans and borrowings	397 390	392 497	407 508
3. Other	47 981	46 707	44 434
II. Current liabilities	335 499	374 157	284 700
1. Interest-bearing loans and borrowings	94 997	110 193	72 063
2. Bank overdraft	23 493	5 574	5 510
3. Trade payables	209 682	251 936	199 866
4. Deferred government grants	117	117	117
5. Other financial liabilities	0	0	0
6. Employee benefits obligation	3 244	2 429	2 324
7. Current income tax payable	89	90	44
8. Provisions for payables	3 877	3 818	4 776
<b>TOTAL EQUITY AND LIABILITIES</b>	<b>959 823</b>	<b>1 009 516</b>	<b>968 972</b>

### 3. Cash flow

In Q3 2015 the Group had a surplus in its operating cash flow primarily as a result of positive EBITDA and an inflow from working capital at PLN 1.8 million. Cash flow from investing activities was negative in connection with the acquisition of fixed assets at PLN 6.0 million partially offset by the sale of those at PLN 4.8 million. Financial activities were negative due to the interest payments at PLN 26.0 million and the repayment of indebtedness at PLN 13.1 million.

CASH FLOW	Q3 2015	Q2 2015	Q3 2014
	<i>'000 PLN</i>		
A. OPERATING ACTIVITIES	15 673	4 976	37 130
B. INVESTING ACTIVITIES	-1 304	-2 690	-5 493
C. FINANCING ACTIVITIES	-39 164	22	-24 353
<b>NET INCREASE IN CASH</b>	<b>-24 795</b>	<b>2 308</b>	<b>7 284</b>

## II. Main Metrics

Liquidity metrics remain good. EBITDA margins deteriorated due to weaker operating performance. Receivable collection saw a stabilization and inventory turnover improved. Worsening EBITDA resulted in the increase of our leverage up to 7.1.

MAIN METRICS	Q3 2015	Q2 2015	Q3 2014
Liquidity ratio	1.62	1.60	1.79
Quick ratio	0.79	0.74	0.81
Inventories turnover (days)	77	89	81
Receivables turnover (days)	63	63	48
EBITDA margin	2.4%	5.5%	7.1%
Net profit margin	-4.2%	-2.0%	0.4%
Equity	169 356	186 558	187 286
Net debt	501 783	487 295	467 619
Net debt / LTM EBITDA	7.1	6.1	5.0

## III. Earnings call

The conference call on our Q3 2015 results will be held in English language on Friday, November 20, 2015 at 16:00 CET (15:00 London). Also on that day a special presentation will be made available for a download on the Company's website at: [www.cognor.eu](http://www.cognor.eu).

All participants are kindly requested to register in advance using the following link: <https://eventreg1.conferencing.com/webportal3/reg.html?Acc=803090&Conf=193599>