

President's Letter to Shareholders

Ladies and Gentlemen, Dear Shareholders,

I present to you the Consolidated Annual Report of Stalprodukt S.A., presenting the results and the most important information about the Group's operations in 2020.

The COVID-19 coronavirus pandemic that broke out in early 2020 was the event that had an overwhelming impact on social and economic life and political ones practically all over the world, resulting in millions of victims and human drama. Many sectors of the economy have suffered from government-imposed administrative and epidemiological restrictions aimed at preventing the development of the pandemic and limiting its impact. It was most severely affected by sectors of the economy such as gastronomy, hotel industry and shopping malls, whose activities were completely suspended for a longer period or significantly reduced, which often resulted in mass layoffs of employees. Companies from other sectors of the economy, especially with an industrial profile, generally did not experience (apart from the automotive industry) such drastic limitations and drops in production, however, they also struggled with higher than usual absenteeism of their employees due to sick leave, forced quarantine or childcare.

These problems also affected the Stalprodukt Group, although their scale was fortunately quite limited and thus they did not have a significant impact on the day-to-day operation of the Company, although they had an impact on the revenues and results achieved. In the most difficult period of the pandemic for us, i.e. March and April 2020, the sales revenues of the parent company decreased by approx. 20%. in relation to the same period of the previous year, thanks to which Stalprodukt could use the funds provided for in the so-called "Anti-crisis shield", i.e. co-financing of salaries from the Voivodship Labor Office in Krakow. The Company has also introduced internal procedures, including such solutions as measuring the temperature before entering the premises, disinfecting office rooms, restrictions in business contacts, or taking up remote work by some employees, which helped to inhibit the development of diseases. In the following months, and especially in the second half of 2020, the situation began to systematically improve.

It should therefore be emphasized that despite the fact that the sales revenues obtained by the Group in 2020 were almost 13 percent lower than in 2019, they also reflected the weak demand for the Group's products, mainly in the Electrical Steels Segment and the Profiles Segment, caused by the pandemic and the administrative restrictions introduced. Despite these unfavorable conditions and lower sales, the Stalprodukt Group achieved good financial results, among others in terms of consolidated operating profit, which was only 3.7 percent lower than the achieved in 2019 and the consolidated net profit, which increased by 19.0 percent and amounted to PLN 183.8 million.

The revenues of the Electrical Sheets Segment decreased by 19.2 percent compared to 2019, while its result by 26.2 percent, which mainly reflected lower sales volumes of sheet metal due to the reduced demand as a result of the pandemic. The share of this segment in the Group's sales decreased from 22.9%. in 2019 to 21.3 percent in 2020.

In the case of the Profiles Segment, the situation was different. The drops in volumes and sales value in individual product groups were lower than in the case of the Electrical Steels Segment. This was reflected in a significant improvement in this segment's result - from a loss of PLN 12.7 million in 2019 to a positive result of PLN 13.0 million in the previous year. The share of this segment in the Group's sales remained at the level of 2019 and amounted to 17.0 percent.

The Zinc Segment was the best one in the difficult conditions of 2020, thanks to which its revenues decreased to a relatively small extent, i.e. by 9.1 percent. It should also be emphasized that it was mainly caused by a decrease of 11.1 percent of LME market prices of zinc. The decline in this segment's result was higher and amounted to 17.7 percent. The share of this area of activity in the Group's consolidated revenues is the highest among all operating segments and currently amounts to 54.6 percent.

Other activities of the Group recorded a decrease in revenues by 19.3 percent and the result by 12.3 percent, and its share in consolidated sales revenues remained at the level similar to 2019 and amounted to 7.1 percent.

The decision of the European Commission on a possible extension of the measures to protect the EU transformer sheet market in force since 2015 will have a significant impact on the further operation of the parent company. The mechanism of minimum import prices, while not an ideal solution, nevertheless constitutes a significant form of protection for European transformer steel producers against dumped imports. The lack of this solution will certainly have a negative impact on the competitive position of the Company. It should be emphasized, however, that the investments made in the past in the modernization of technological lines allow for an increase in the share of production of high-quality transformer sheets (HiB), characterized by the highest quality and thus higher market prices than conventional transformer sheets. Therefore, the Management Board intends to significantly increase the production of these products from next year in order to limit the possible effects of the decisions of the European Commission on non-renewal of existing market protection measures.

Due to the coronavirus pandemic and the top-down significant administrative restrictions in the operation of the hotel industry, Stalprodukt decided to postpone the start-up date of the newly built Hotel Ferreus in Krakow, located in an attractive location in the city center (6, Kopernika Street), where the Company had had for many years unused property. This activity will be conducted on the basis of a lease agreement by an entity established for this purpose (Hotel Ferreus Sp. z o.o.). We anticipate that the opening of this facility will take place in the third quarter of 2021.

In the Zinc Segment, in 2020 the key investment included in the development strategy for this area of the Group's operations announced in 2016 was completed, i.e. the construction of a new zinc electrolysis hall, located on the premises of the zinc smelter in Bukowno. The cost of this investment was approximately PLN 295 million. The innovative nature of the applied electrolysis technology is based on the possibility of producing zinc from raw materials that are up to 50% recycled, which gives the Zinc Segment greater flexibility in managing the supply of raw materials from various sources.

In 2020, the Management Board of the subsidiary ZGH "Bolesław" S.A. made another important decision regarding the future operation of this segment of the Group, namely the decision to terminate the mining activity by this entity and start, on January 1, 2021, the process of decommissioning of the "Olkusz-Pomorzany" mine. The main reason for the termination of mining activities is practically complete depletion of the deposit.

Taking into account the unfavorable external and internal conditions, the Management Board of the Issuer started last year the process of reviewing strategic options, which include, inter alia, such potential solutions as: sale of assets or individual operating segments of the Company, sale of other areas of activity carried out by the Group, entering into a strategic alliance with a supplier of feedstock (especially for the production of HiB sheets) or the creation of a joint-venture with a selected partner.

On behalf of the Management Board, I assure you that the best solution will be chosen from the point of view of achieving the long-term goal of the development of the Stalprodukt Group, leading to the maximization of value for the current and future shareholders of the Company. Regardless of the result of this process, we systematically restructure the basic areas of activity and optimize internal processes, especially those affecting production costs.

I hope that thanks to common vaccination it will be possible to overcome or at least significantly reduce the spread of the coronavirus pandemic and that its impact on social and economic life in 2021 will not be as severe as it was last year.

Nevertheless, the market environment around the Stalprodukt Group remains unfavorable and faces great challenges: energy costs are rising drastically and additional burdens in the form of currently record prices of CO₂ emission allowances, which is of key importance from the point of view of the high energy consumption of the technological processes used in the Group. Another problem is the large share in the apparent consumption of imported finished products. Therefore, the Management Board will make every effort to improve the Group's competitive position and results.

I would like to take this opportunity to thank the employees and management boards of all companies from the Stalprodukt Group for their commitment, work and dedication so far in this particularly difficult period in which the Group operated in 2020.

Piotr Janeczek
President – Chief Executive Officer
Stalprodukt S.A.