tel.: +48 22 543 16 00
fax: +48 22 543 16 01
e-mail: office@bdo.pl
www.bdo.pl

BDO spółka z ograniczoną odpowiedzialnością sp.k.
ul. Postępu 12
02-676 Warszawa
Polska

This document is a translation.
The Polish original should be referred to in matters of interpretation.

Independent Auditor's Report
to the General Meeting and Supervisory Board of PKP CARGO SA

Report on the Audit of the Year-end Financial Statements

Opinion

We have audited the separate financial statements of PKP CARGO SA ("the Company"), which comprise the statement of comprehensive income for the period from 1 January to 31 December 2018, the statement of financial position as at 31 December 2018, the statement of changes in equity and the statement of cash flows for the year then ended, as well as notes to the financial statements including a description of significant accounting methods and other explanations ("the financial statements").

In our opinion, the accompanying financial statements:

- give a true and fair view of the Company's financial position as at 31 December 2018, as well as of its financial result and cash flows for the financial year then ended, in accordance with the applicable International Financial Reporting Standards as adopted by the European Union, as well as the adopted accounting methods (policies);
- are consistent, in content and in form, with the applicable laws and regulations and with the Company's Statute;
- have been prepared on the basis of properly kept books of account in accordance with Chapter 2 of the Accounting Act of 29 September 1994 ("the Accounting Act"" - 2019 Journal of Laws, item 351).

The present opinion is consistent with the additional report to the Audit Committee, which we issued on the date of this report.

Basis for Opinion

We conducted our audit in accordance with the International Standards on Auditing adopted by the National Council of Certified Auditors as National Standards on Auditing ("NSA") and in compliance with the Act on Certified Auditors, Audit Firms and on Public Supervision ("the Certified Auditors Act" – 2017 Journal of Laws, item 1089 with subsequent amendments) and Regulation (EU) No. 537/2014 of 16 April 2014 on specific requirements regarding statutory audit of public interest entities ("Regulation EU" – OJ L 158). Our responsibilities under those standards are further described in the *Responsibilities of the Auditor for the Audit of the Financial Statements* section of this report.

We are independent of the Company in accordance with the Code of Ethics for Professional Accountants issued by the International Federation of Accountants ("the IFAC Code") and adopted by resolutions of the National Council of Certified Auditors, and with other ethical requirements relevant to the audit of financial statements in Poland. We have fulfilled our other ethical responsibilities in accordance with these requirements and the IFAC Code. During the audit, the engagement partner and the audit firm remained independent of the Company in accordance with the independence requirements laid down in the Certified Auditors Act and Regulation EU.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Key Audit Matters

Key audit matters are those matters that, in our professional judgment, were of the most significance in the audit of the financial statements for the current reporting period. They include the most significant assessed types of risks of material misstatements, including assessed types of risks of material misstatements resulting from fraud. We addressed these matters in the context of our audit of the financial statements as a whole and in forming our opinion thereon, and have summarized our response to these types of risks, and where relevant, presented our key observations relating to those risks. We do not express a separate opinion on these matters.

1. Valuation of rolling stock
Key audit matter
In its financial statements the Company lists PLN 3.426 million in rolling stock, constituting 57,3% of the value of its assets as at 31 December 2018. The matter has been classified as a risk of material misstatement due to the high percentage of rolling stock in the Company's assets and the significant effect of management's judgement on the values of assets disclosed in the financial statements. Because the net market value of the Company's assets is lower than their carrying amount, the Company has performed an impairment test, which did not show impairment of assets.
Disclosures in the financial statements
The details of the Company's accounting policies on the valuation of property, plant and equipment, including the methods used to perform impairment write downs and calculate depreciation charges, are disclosed in Note 5.1 to the financial statements.
Audit procedures performed in response to the risk
In response to the identified risk, we applied the following audit procedures: a) obtained an understanding and performed an assessment of the internal control system in relation to property, plant and equipment, b) assessed the applied accounting methods for compliance with the relevant accounting standards, c) checked for changes in the Company's approach to estimating property, plant and equipment write downs, determining depreciation rates and calculating the residual value of rolling stock compared to the previous year; obtained and analyzed relevant documentation, d) performed an analytical completeness test of depreciation, e) verified the Company's asset impairment test by assessing the correctness and completeness of the disclosures relating to the test made in the financial statements and evaluating the validity of the test assumptions and final conclusions, checked if the valuation model was consistent with IAS 36 "Impairment of Assets", f) assessed the effect of subsequent events on the estimates made as at the balance sheet date.

2. Provisions for employee benefits
Key audit matter
In its financial statements as at 31 December 2018 the Company presents provisions for employee benefits in the amount of PLN 621 million, which constitutes 10,4% of its total liabilities and equity. The provisions have been classified as a significant audit area due to their significant effect on the financial statements.
Disclosures in the financial statements
The Company has made disclosures relating to provisions for employee benefits in Note 5.8 to the financial statements.
Audit procedures performed in response to the risk
In response to the identified risk, we applied the following audit procedures: a) obtained an understanding of the process of calculating the provisions for employee benefits and performed an assessment of the Company's control mechanisms in this area, b) based on a random sample verified the accuracy of the data provided by the Company to the actuary, c) analyzed the report on the actuarial valuation of the provisions for employee benefits, d) evaluated the credentials of the company that prepared the actuarial valuation report, e) analyzed the key assumptions used in the valuation of the provisions, including the discount rate, f) analyzed the effect of departures from key assumptions on the value of the provisions, g) analyzed the use of short-term provisions in the year 2018 compared to the estimates made as at 31 December 2017, h) assessed the accuracy and completeness of the disclosures made in the financial statements, including the effect of provision estimation errors from previous years.

3. Contingent liabilities
Key audit matter
In its financial statements the Company lists contingent liabilities relating to court proceedings resulting from claims filed against the Company. The proceedings include claims filed by two vendors for the payment of damage compensation in the amount of PLN 101 million for acts of unfair competition that one of the vendors alleges the Company practiced in the years 2010-2015, as well as for the repayment of lost benefits, credibility and good name in connection with the non-extension of a sub-lease concluded between the Company and the other vendor. The above contingent liabilities have been classified as a key audit area due to the difficulties in assessing their future outcome and their significant effect on the financial statements.
Disclosures in the financial statements
The Company has made disclosures relating to contingent liabilities in Note 7.4 to the financial statements.
Audit procedures performed in response to the risk
Our audit procedures included: a) identifying the Company's controls with regard to the classification of contingent liabilities, b) familiarizing ourselves with the current state of affairs, c) assessing the accuracy of the classification of the claims as contingent liabilities by obtaining the standpoints of the Company's legal advisors on the risk that the outcome of the disputes will be unfavorable for the Company, d) assessing whether the disclosures made in the financial statements are consistent with the provisions of IAS 37 "Provisions, Contingent Liabilities and Contingent Assets".

Responsibilities of the Company's Management and Supervisory Board for the Financial Statements

The Company's Management is responsible for the preparation, based on properly kept books of account, of the financial statements that give a true and fair view of the Company's financial position and financial result in accordance with International Financial Reporting Standards as adopted by the European Union, the adopted accounting methods (policies), the applicable binding regulations and the Company's Statute. The Company's Management is also responsible for such internal controls as it considers necessary to ensure that the financial statements are free from material misstatements resulting from fraud or error.

In preparing the financial statements the Management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, any matters related to going concern and using the going concern basis of accounting, except in situations where the Management intends to either liquidate the Company or discontinue its operations, or has no realistic alternative but to do so.

The Company's Management and members of its Supervisory Board are required to ensure that the financial statements meet the requirements of the Accounting Act. Members of the Supervisory Board are responsible for overseeing the Company's financial reporting process.

Responsibilities of the Auditor for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatements due to fraud or error, and to issue an independent auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but it is not a guarantee that an audit conducted in accordance with NSA will always detect an existing material misstatement. Misstatements can arise from fraud or error and are considered material if it could be reasonably expected that they, individually or in the aggregate, could influence the economic decisions of users made on the basis of these financial statements.

The concept of materiality is applied by the auditor at the planning stage and when performing the audit and evaluating the effect of identified misstatements on the audit and of uncorrected misstatements, if any, on the financial statements, as well as when formulating the auditor's opinion. In view of the above, all of the opinions and statements contained in the auditor's report are expressed subject to the qualitative and quantitative level of materiality set in accordance with the applicable standards on auditing and the auditor's professional judgement.

The scope of the audit does not include an assurance regarding the Company's future profitability, or regarding the Management's effectiveness in the handling of the Company's affairs now or in the future.

Throughout an audit in accordance with NSA, we exercise professional judgement and maintain professional skepticism, as well as:

- identify and assess the risks of a material misstatement of the financial statements resulting from fraud or error, design and perform audit procedures in response to such risks and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than the risk of not detecting a material misstatement resulting from error, because fraud may involve collusion, forgery, deliberate omission, misrepresentation or override of internal controls;
- obtain an understanding of the internal controls relevant to the audit in order to plan our audit procedures, but not to express an opinion on the effectiveness of the Company's internal controls;
- evaluate the appropriateness of the accounting policies used and the reasonableness of the estimates and related disclosures made by the Company's Management;
- conclude on the appropriateness of the Management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor's report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern;
- evaluate the overall presentation, structure and contents of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We provide the Audit Committee with information about, among others, the planned scope and timing of the audit and significant audit findings, including any significant weaknesses of internal controls that we identify during our audit.

We provide the Audit Committee with a statement that we have complied with the relevant ethical requirements relating to independence, and that we will communicate to them all relationships and other matters that may reasonably be considered to constitute a threat to our independence, and where applicable, inform them of the related safety measures.

From the matters communicated to the Audit Committee we determined those matters that were of the most significance to the audit of the financial statements for the current reporting period and were therefore chosen as key audit matters. We describe these matters in our auditor's report, unless law or regulations prohibit their public disclosure or when, in exceptional cases, we find that a given matter should not be presented in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such information.

Other Information

Based on the provisions of Article 55.2a of the Accounting Act and of par. 71.8 of the Minister's of Finance Decree of 29 March 2018 on the current and periodic information reported by the issuers of securities and on the conditions for recognizing as equally valid the information required by the regulations of a state that is not a member state (2018 Journal of Laws, item 757), the Company's Management prepared as a single document a consolidated report on the activities of the PKP CARGO group, on which we have reported in the auditor's report on the consolidated financial statements.

We were appointed as auditors of the Company's financial statements in a resolution passed by the Supervisory Board on 30 June 2016. We have audited the Company's financial statements continually since the financial year ended 31 December 2016, i.e. for 3 consecutive years.

The engagement partner on the audit resulting in this independent auditor's report is Leszek Kramarczuk.

BDO spółka z ograniczoną odpowiedzialnością sp.k. with its registered office in Warsaw
entered on the list of audit firms in number **3355**

represented by the engagement partner

Signed with a qualified electronic signature

Leszek Kramarczuk
Certified Auditor No. 1920

Signed with a qualified electronic signature

Dr. André Helin
Managing Partner
Certified Auditor No. 90004

Warsaw, 20 March 2019