

27.6 Credit risk

Management of credit risk related to counterparties in financial transactions consists in the verification of creditworthiness of the current and potential counterparties and monitoring of credit exposures against the granted limits. The credit exposure is attributable to bank deposits and derivatives measurement.

The counterparties must have an appropriate credit rating assigned by leading rating agencies or hold guarantees from institutions meeting the minimum rating requirement. The Group enters into financial transactions with reputable firms with sound credit standing, and diversifies the group of institutions with which it maintains relationships.

As at December 31st 2018 and December 31st 2017, the concentration of credit risk exposure to any single counterparty in the Group's financial transactions did not exceed PLN 542.7m and PLN 845.7m, respectively (5.44% and 9.51% of the Parent's equity, respectively).

As regards management of counterparty risk in non-financial transactions, all customers who request trading on credit terms are subject to credit assessment, whose results determine the level of possible credit limits. In 2017, the Parent completed development of a rating model which supports assigning credit limits to counterparties. The Parent defines guidelines for managing counterparty risk in non-financial transactions to ensure that appropriate standards of credit analysis and operational security are observed across the entire Group.

As at December 31st 2018 and December 31st 2017, the concentration of credit risk exposure to any single counterparty in the Group's trade transactions did not exceed PLN 116.4m and PLN 530.5m, respectively (1.17% and 5.97% of the Parent's equity, respectively).

Credit risk is measured by the maximum exposure to risk of each class of financial assets. Carrying amounts of financial assets represent the maximum credit risk exposure.

| Maximum credit risk exposure of financial assets | Note | December 31st 2018 | December 31st 2017 |
|--|------|-----------------------|-----------------------|
| Derivative financial instruments | 23 | 24.4 | 164.5 |
| Trade receivables | 15 | 1,880.4 | 2,677.0 |
| Cash and cash equivalents | 17 | 1,941.3 | 1,920.7 |
| Other financial assets | 15 | 710.7 | 459.6 |
| Total | | 4,556.8 | 5,221.8 |

In the Management Board's opinion, the risk related to non-performing financial assets is reflected in the recognised impairment losses. For information on impairment of financial assets, see Notes 9.4 and 15.1.

For discussion of credit risk concentrations for trade receivables, see Note 15.1.
 For ageing analysis of receivables past due but not impaired, see Note 15.1.

28. Capital management

The objective of the LOTOS Group financial policy is to maintain long-term liquidity, while using an appropriate level of financial leverage to support the achievement of the principal objective of maximising the return on equity for shareholders.

This is achieved through constant effort to develop the desired capital structure at the Group level.

The LOTOS Group uses the debt to equity ratio, calculated as net debt to equity, to monitor its financing structure.

Net debt comprises bank and non-bank borrowings, notes and liabilities under finance leases less cash and cash equivalents. Equity includes equity attributable to owners of the Parent plus non-controlling interests.

| | Note | December 31st 2018 | December 31st 2017 |
|---|------|--------------------|--------------------|
| Non-current liabilities | | | |
| Bank borrowings | 22.1 | 2,158.1 | 2,633.6 |
| Non-bank borrowings | 22.2 | 42.2 | 4.4 |
| Notes | 22.3 | - | - |
| Finance lease liabilities | 22.4 | 145.0 | 100.3 |
| Total | | 2,345.3 | 2,738.3 |
| Current liabilities | | | |
| Bank borrowings | 22.1 | 1,263.1 | 1,269.4 |
| Non-bank borrowings | 22.2 | 13.6 | 63.9 |
| Notes | 22.3 | 227.0 | 313.0 |
| Finance lease liabilities | 22.4 | 35.0 | 41.3 |
| Total | | 1,538.7 | 1,687.6 |
| Cash and cash equivalents | 17 | (1,941.3) | (1,920.7) |
| Net debt | | 1,942.7 | 2,505.2 |
| Equity attributable to owners of the Parent | | 12,034.7 | 10,712.4 |
| Non-controlling interests | | 0.1 | 0.1 |
| Total equity | | 12,034.8 | 10,712.5 |
| Net debt to equity | | 0.16 | 0.23 |