

Annual report of the Board of Directors to the Shareholders' meeting, corresponding to fiscal year 2021



Dear shareholders:

As Chairman of the Board of Directors of Industrias Peñoles, S.A.B. de C.V., and on its behalf, I present this report based on an analysis of the information provided by the Chief Executive Officer in his Annual Report on the company's performance, the financial and operating results obtained in fiscal year 2021, material aspects relating to the environment, safety and health, relations with the communities where we operate, and corporate governance, as well as a report on the main activities of the Board of Directors.

In 2021, after the economic crisis caused by the COVID-19 pandemic, industrial activity gradually regained growth, particularly during the first half of the year. The recovery was stronger in advanced economies, while lower-income countries were hit harder by the sanitary, economic and social effects of the crisis.

The recovery of industrial production was a strong stimulus for metals demand. Because of its status as a safe haven for investment, the price of gold held steady, while the price of silver—along with those of base metals—grew at average double-digit rates over the previous year.

During the year, Peñoles continued its emergency plan to avoid propagation of COVID-19 and protect the life and health of its employees through the application of sanitary protocols, testing, work from home, support and medical follow-up on detected cases. In collaboration with the authorities, we set up vaccination centers at our facilities, where more than 163,000 vaccine doses were given to people in the communities where we operate and to employees. We also continued our donations of medical supplies, personal protection equipment, staple food supplies and facemasks. Our social investment in the period, in addition to the payment of mining rights to the nation, totaled US\$ 8 million.

Industrias Peñoles reiterates its priority commitment to its employees' health and safety and to protecting the environment. To this end, we reinforced safety and environmental programs, with special attention paid to the tailings storage facilities.

We invested US\$ 171 million in exploration last year (21.2% more than in 2020). We carried out drilling programs at the operating mines and in their areas of influence to generate resources and strengthen reserves. In

addition, we resumed field work in several projects and continued to assess our portfolio of prospects.

The pace of operations in 2021 improved in comparison to 2020. For instance, we were able to complete construction of the processing plant at the Juanicipio gold-silver mining unit in Zacatecas. This was our largest development project during the year, but its final startup depends on its connection to the electrical grid. Since mid-year the ore extracted at this project has been processed at the Fresnillo beneficiation plant to produce gold and silver in concentrates. On the other hand, the tailings flotation plant at Fresnillo was unable to start up operations in the third quarter of 2021 as planned, because of delays in the electrical connection permit. At the Capela mining unit in Guerrero, which began operations in 2020, process stabilization continued to move toward the expected production levels. Investments in fixed assets in fiscal year 2021 totaled US\$ 762 million, 35.8% more than in the previous year.

Gold mining production totaled 812.0 thousand ounces, slightly less than the year before. Silver production was 64.4 million

Construction of the processing plant at the Juanicipio gold-silver project in Zacatecas was completed.

We reviewed and validated the Strategic Plan update and risk matrix, and reinforced workplace and environmental safety.

ounces, above 2020, thanks to higher head grades at San Julián and Sabinas, as well as the contributions from Juanicipio and Capela. Copper production in concentrates rose thanks to higher recovery rates at Capela.

In the metallurgical business, gold production volume increased by 16.8% to 1,118,200 ounces. Silver production totaled 75.2 million ounces and lead production 120,355 metric tons, 6.5% and 7.9% higher, respectively, due to higher grades in the concentrates treated and the cements received from the zinc refinery. In the latter, refined zinc production saw a marginal growth of 3,423 metric tons (+1.3%) over the previous year, for various reasons: difficulties in the process of stabilizing the zinc plant and the silver recovery plant, which are taking more time than expected; disruptions in the supply of energy and natural gas due to the freezing weather in Texas in February 2021, and the lack of liquid oxygen, which is attributed to the emergency conditions caused by the pandemic. For these reasons, a plan is in place for this plant to reach its nameplate capacity over the course of 2022.

Financial results for the year were substantially better than the year before. Sales rose above their 2020 level due to the recovery in metal prices and higher sales volume. Costs and expenses also rose, however, due to the acceleration of operations and the impact of inflation on certain inputs. Financial expenses were lower, after an upturn in 2020 due to the extraordinary expense of bond placements and debt restructuring. There were no losses from impairment of long-lived assets as there had been in 2020 caused mainly by the shutdown of three mining units. Net sales totaled US\$ 5.97 billion—a 27.8% increase—

while gross income rose 24.6% to US\$ 1.56 billion; EBITDA increased 16.4% to US\$ 1.70 billion, and operating income grew 30.8% to US\$ 971 million. The bottom line shows net profits of US\$ 391 million for 2021, an improvement compared to the net loss of US\$ 34 million reported in fiscal-year 2020. The company paid dividends totaling US\$ 149 million to shareholders, and the balance sheet remains solid and conservative with a net debt/EBITDA ratio of 0.7 times.

The Board of Directors adheres to solid corporate governance practices. In the discharge of its duties, the Board relies on the support of committees that have been created as recommended in the Code of Best Principles and Practices for Corporate Governance. The Board met six times in 2021. Among the topics discussed and approved during those sessions, the most important were the following:

- ▶ Follow-up on the COVID-19 emergency plan.
- ▶ Reinforcement of workplace and environmental safety programs.
- ▶ Strategic Plan update.
- ▶ Review of the risk matrix.
- ▶ Metal hedging and exchange rate program.
- ▶ Analysis and adjustments to the investment and financing programs.
- ▶ Review of the budget for the 2021 and 2022 fiscal years.
- ▶ Amendments to the company's Code of Conduct.
- ▶ Actions necessary for complying with the new law on outsourcing.

The most relevant activities of the committees, whose members are listed in the Corporate Governance section of the Annual Report, include the following:

- ▶ The Executive Committee reviewed budgets and operating and financial performance for each business, including safety data. It also followed up on actions to prevent COVID-19 contagion and validated the bases of the Strategic Plan.
- ▶ The Audit and Corporate Governance Committee reviewed the operating and financial results, performance, and the internal and external audit plans and the plan of the Compliance Department. It evaluated the external audit services and validated compliance with regulatory requirements. It also reviewed accounting policies, transactions with related parties and legal matters.
- ▶ The Finance and Planning Committee reviewed financial projections, evaluated investment projects and reviewed the company's financial position.
- ▶ The Nomination, Evaluation and Compensation Committee conducted its annual evaluation of senior management performance, in accordance with policy, and authorized increases in salaries and benefits, as well as bonuses and other results-based recognitions. The compensation package for senior management consists of a base salary, benefits as required by law, and other elements common to the industry in Mexico. It also validated the capacity and experience of the members of the Board of Directors and recommended their compensation.

Pursuant to the provisions in the Securities Market Law, the Audit and Corporate Governance Committee submitted its Annual Report, which is presented to this Shareholders' Meeting.

Submitted herein for the consideration of this Shareholders' Meeting is a report on the main accounting policies and criteria that served as the basis for preparing the financial statements, which include, among others, the basis of presentation and consolidation, significant accounting policies, and new accounting pronouncements, which were audited by the external auditors and are an integral part of this report. The company's financial statements were prepared in accordance with the International Financial Reporting Standards issued by the International Accounting Standards Board.

In the opinion of the Board of Directors, the report presented to this Shareholders' Meeting by the Chief Executive Officer reasonably reflects the financial position and results of the company, as well as the key developments of the business during 2021.

Through the transformation we have undertaken, we aim to become more resilient in the face of uncertainty, achieve greater operational and administrative efficiency, and improve performance, results and accountability. Whatever happens, we must not only endure, but thrive. This evolutionary process is the foundation for the sustainable future of the Company for the benefit of our stakeholders and our country.

Dear shareholders:

The passing of our Honorary Chairman, and Chairman of the Board for 54 years, on February 2, 2022, moves me to express a heartfelt recognition for the formidable legacy he left our company and Mexico. The best way to honor his memory is to preserve and build upon this legacy, a task to which I and all the other Board Members and employees of this company are firmly committed.

I want to convey my gratitude to the members of the Board of Directors for their dedication, commitment and valuable contributions. I would also like to thank our employees for their hard work and dedication. And I extend my appreciation to you, our shareholders, for your continued confidence in us.

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his formidable legacy.



Alejandro Baillères
Chairman of the Board of Directors