Ericsson Nikola Tesla d.d.

Consolidated Financial Statements and Auditor’s report 31 December 2013

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Company profile

History and incorporation

Ericsson Nikola Tesla d.d. (the Company) is a Croatian company with over sixty years of continuous operations. It is a leading supplier and exporter of specialized telecommunications equipment, software solutions and services in Central and Eastern Europe.

The Company was founded as a result of the privatisation of the enterprise Nikola Tesla - Poduzeće za proizvodnju telekomunikacijskih sistema i uređaja, po.

Principal activities

The principal activities of the Company are: the research and development of telecommunications software and services, design, testing and integration of total communications solutions, and supply and maintenance of communications solutions and systems primarily in the Republic of Croatia, Central and Eastern Europe as well as to companies within the Ericsson Group.

Ericsson Nikola Tesla d.d. is a joint stock company incorporated in Croatia. The headquarters of the Company are in Zagreb, Krapinska 45.

Company profile (continued)

Supervisory Board, Management Board and executive management

The Supervisory Board

The Supervisory Board members during 2013 and up to the release of these consolidated statements were:

Roland Nordgren	Reappointed on 5 June 2012	Chairman
Ignac Lovrek	Reappointed on 31 May 2011	Member; Vice-Chairman
Carita Jönsson	Reappointed on 5 June 2012	Member
Dubravko Radošević	Appointed on 20 May 2010	Member
Zvonimir Jelić	Reappointed on 18 June 2010	Member and employees' representative

The Management Board

The Management Board has one member:

Gordana Kovačević	Reappointed on 1 January 2010	President

Executive management

As at 31 December 2013, the Company's executive management comprised:

Gordana Kovačević	Company President
Branko Dronjić	Head, G-ITTE Engineering Services Croatia
Damir Bušić	Director, Commercial Management
Dario Runje	Head, CD RAN & Director, CC & Supply Croatia
Dragan Fratrić	Manager, General Services
Goran Ožbolt	Director, Sales and Marketing for Tele2 and Alternative Operators
Grga Mrkonjić	Director, Sales and Marketing for HT
Hrvoje Benčić	Director, Engagement Practices and ETK Customer Operations
Igor Poljanšek	Director, Business Innovation and New Opportunities
Ivan Barać	Director, Sales & Marketing for CIS Market
Jagoda Barać	Director, Sales and Marketing for Neighboring Countries
Marijana Đuzel	Head, HR&O and Legal Affairs
Milan Živković	Director, Strategy and Business Development
Miroslav Kantolić	Director, Sales and Marketing for VIPnet
Patrick Gerard Martin	Director, Research and Development Center
Rafal Rybkowski	Director, Finance
Snježana Bahtijari	Director, Communication
Tihomir Šicel	Director, Sales & Marketing for Industry and Society

Responsibilities of the Management and Supervisory Boards for the preparation and approval of the annual consolidated financial statements

The Management Board is required to prepare consolidated financial statements for each financial year which give a true and fair view of the financial position of the Group and of the results of its operations and cash flows, in accordance with applicable accounting standards, and is responsible for maintaining proper accounting records to enable the preparation of such consolidated financial statements at any time. It has a general responsibility for taking such steps as are reasonably available to it to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

The Management Board is responsible for selecting suitable accounting policies to conform with applicable accounting standards and then apply them consistently; make judgements and estimates that are reasonable and prudent; and prepare the consolidated financial statements on a going concern basis unless it is inappropriate to presume that the Group will continue in business.

The Management Board is responsible for the submission to the Supervisory Board of its annual report on the business situation of the Group together with the annual consolidated financial statements, following which the Supervisory Board is required to approve the annual consolidated financial statements which will be presented to the General Assembly of Shareholders.

The consolidated financial statements set out on pages 5 to 62 were authorised by the Management Board on 8 April 2014 for issue to the Supervisory Board and are signed below.

Gordana Kovačević
President
Ericsson Nikola Tesla d.d.
Krapinska 45
10000 Zagreb
Croatia

ERICSSON
Ericsson Nikola Tesla d.d.
Krapinska 45
HR-10 000 Zagreb
CROATIA 39

Independent Auditor's Report

To the Shareholders and Management of Ericsson Nikola Tesla d.d.

We have audited the accompanying consolidated financial statements of Ericsson Nikola Tesla d.d. and its subsidiaries (the "Group"), which comprise the consolidated statement of financial position as at 31 December 2013 and the consolidated statement of comprehensive income, statement of changes in equity and cash flows statement for the year then ended, and notes comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards as adopted in the European Union, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

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

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Group as at 31 December 2013, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted in the European Union.

PricewaterhouseCoopers d.o.o.

PricewaterhouseCoopers d.o.o.
Zagreb, 11 April 2014

Our report has been prepared in Croatian and in English languages. In all matters of interpretation of information, views or opinions, the Croatian language version of our report takes precedence over the English language version.

Consolidated statement of comprehensive income
for the year ended 31 December 2013

	Notes	**2013**	**2012**
		HRK '000	**HRK '000**
Sales revenue	*3, 4*	1,345,226	1,913,304
Cost of sales		(1,125,093)	(1,701,672)
Gross profit		220,133	211,632
Selling expenses		(60,694)	(61,095)
Administrative expenses		(32,676)	(36,080)
Other operating income		2,120	3,586
Other operating expenses		(1,644)	(1,432)
Operating profit		127,239	116,611
Finance income	*7*	17,284	24,487
Finance expense	*7*	(163)	(80)
Finance income – net		17,121	24,407
Profit before tax		144,360	141,018
Income tax	*8*	(5)	(14.105)
Profit for the year		144,355	126,913
Other comprehensive income - items that may be subsequently reclassified to profit or loss:			
Currency translation differences		13	5
Total comprehensive income for the year		**144,368**	**126,918**
Earnings per share (HRK)	*9*	108,67	95.63

The notes set out on pages 11 to 62 form an integral part of these consolidated financial statements.

Consolidated statement of financial position
as at 31 December 2013

	Notes	2013 HRK '000	2012 HRK '000
ASSETS			
Non-current assets			
Property, plant and equipment	*10*	131,616	117,026
Intangible assets	*11*	2,112	4,314
Loans and receivables	*12*	18,801	30,413
Other non-current assets		40	40
Total non-current assets		152,569	151,793
Current assets			
Inventories	*13*	51,506	33,268
Trade receivables	*14*	246,152	227,586
Receivables from related parties	*25(c)*	71,819	81,190
Other receivables	*15*	3,715	15,169
Financial assets at fair value through profit or loss	*16*	109,845	145,365
Prepayments and accrued income		1,156	3,655
Cash and cash equivalents	*17*	411,328	511,639
Total current assets		895,521	1,017,872
TOTAL ASSETS		1,048,090	1,169,665

The notes set out on pages 11 to 62 form an integral part of these consolidated financial statements.

Consolidated statement of financial position (continued)
as at 31 December 2013

	Notes	**2013 HRK '000**	**2012 HRK '000**
EQUITY AND LIABILITIES			
Equity			
Share capital	*18(a)*	133,165	133,165
Treasury shares		(9,571)	(6,928)
Legal reserves	*18(c)*	6,658	20,110
Retained earnings		540,884	608,381
Total equity		671,136	754,728
Non-current liabilities			
Interest-bearing borrowings		69	12
Employee benefits	*21(a)*	4,697	4,452
Total non-current liabilities		4,766	4,464
Current liabilities			
Payables to related parties	*25(c)*	60,936	115,690
Interest-bearing borrowings		309	1,710
Trade and other payables	*22*	148,426	123,615
Provisions	*23*	13,458	18,566
Accrued charges and deferred revenue	*24*	149,059	150,892
Total current liabilities		372,188	410,473
Total liabilities		376,954	414,937
TOTAL EQUITY AND LIABILITIES		1,048,090	1,169,665

The notes set out on pages 11 to 62 form an integral part of these consolidated financial statements.

Consolidated statement of changes in equity
for the year ended 31 December 2013

	Share capital HRK '000	Treasury shares HRK '000 Note 18 (b)	Legal reserves HRK '000	Retained earnings HRK '000	Total HRK '000
As at 1 January 2012	133,165	(8,443)	20,110	705,878	850,710
Changes in equity for 2012					
Total comprehensive income	-	-	-	126,918	126,918
Dividend distribution for 2011, Note 19	-	-	-	(225,695)	(225,695)
Purchases of treasury shares, Note 18 (b)	-	(2,462)	-	-	(2,462)
Share-based payments, Note 21 (b)	-	3,977	-	(3,977)	
Equity-settled transactions, Note 21 (b)	-	-	-	5,257	5,257
Total contributions by and distributions to owners of the parent recognised directly in equity	-	1,515	-	(224,415)	(222,900)
As at 31 December 2012	133,165	(6,928)	20,110	608,381	754,728
As at 1 January 2013	133,165	(6,928)	20,110	608,381	754,728
Changes in equity for 2013					
Total comprehensive income	-	-	-	144,368	144,368
Dividend distribution for 2012, Note 19	-	-	-	(225,851)	(225,851)
Release of legal reserves	-	-	(13,452)	13,452	-
Purchases of treasury shares, Note 18 (b)	-	(5,754)	-	-	(5.754)
Share-based payments, Note 21 (b)	-	3,111	-	(3,111)	-
Equity-settled transactions, Note 21 (b)	-	-	-	3,645	3,645
Total contributions by and distributions to owners of the parent recognised directly in equity	-	(2,643)	(13,452)-	(211,865)	(227,960)
As at 31 December 2013	133,165	(9,571)	6,658	540,884	671,136

The notes set out on pages 11 to 62 form an integral part of these consolidated financial statements.

Consolidated statement of cash flows
for the year ended 31 December 2013

	Notes	**2013** **HRK '000**	**2012** **HRK '000**
Cash flows from operating activities			
Profit before tax		*144,360*	*141,018*
Adjustments for:			
Depreciation and amortisation	*10,11*	40,282	44,619
Impairment losses and reversals		955	1,738
Net increase in provisions		5,178	16,837
Gain on sale of property, plant and equipment		(448)	(202)
Net gain on remeasurement of financial assets		(1,479)	(2,536)
Amortisation of discount		(2,003)	(3,021)
Interest income		(10,036)	(20,625)
Interest expense	*7*	163	80
Foreign exchange gains, net		(1,332)	(3,206)
Equity-settled transactions	*6*	3,645	5,257
		179,285	179,959
Decrease in receivables		10,632	65,424
Increase in inventories		(18,238)	(10,563)
(Decrease)/increase in payables		(30,333)	63,137
Cash generated from operations		*141,346*	*297,957*
Interest paid		(163)	(80)
Income taxes paid		(5)	(113)
Net cash from operating activities		***141,178***	***297,764***
Cash flows from investing activities			
Interest received		11,800	22,258
Proceeds from sale of property, plant and equipment		4,957	4,919
Purchases of property, plant and equipment, and intangible assets		(63,806)	(33,073)
Deposits collected with financial institutions - net		-	594
Purchases of financial assets at fair value through profit and loss		(103,000)	(188,500)
Proceeds from sale of financial assets at fair value through profit and loss		140,000	113,928
Net cash used in investing activities		***(10,049)***	***(79,874)***

The notes set out on pages 11 to 62 form an integral part of these consolidated financial statements.

Consolidated statement of cash flows (continued)
for the year ended 31 December 2013

	Notes	**2013**	**2012**
		HRK '000	**HRK '000**
Cash flows from financing activities			
Repayment of interest-bearing borrowings		(1,669)	(1,710)
Purchase of treasury shares	*18(b)*	(5,754)	(2,462)
Dividends paid	*19*	(225,851)	(225,695)
Net cash used in financing activities		***(233,274)***	***(229,867)***
Effects of exchange rate changes on cash and cash equivalents		1,835	(1,689)
Net decrease in cash and cash equivalents		(100,311)	(13,666)
Cash and cash equivalents at the beginning of the year		511,639	525,305
Cash and cash equivalents at the end of the year	*17*	**411,328**	**511,639**

The notes set out on pages 11 to 62 form an integral part of these consolidated financial statements.

Notes to the consolidated financial statements

1 Significant accounting policies

Reporting entity

Ericsson Nikola Tesla d.d. (the Company) is a joint stock company incorporated and domiciled in Croatia. The address of its registered office is Krapinska 45, 10000 Zagreb, the Republic of Croatia. The Company's shares are listed on the Public Joint Stock Company listing on the Zagreb Stock Exchange. The Company has prepared these consolidated financial statements as at 31 December 2013 and for the year then ended for the Company, three active subsidiaries, of which one is domiciled in Croatia, the second in Bosnia and Herzegovina and the third in Kosovo, and two inactive subsidiaries domiciled in Croatia (the Group). These consolidated financial statements were authorised for issue by the Management Board on 8 April 2014 for approval by the Supervisory Board. A summary of the Company's principal accounting policies is set out below.

Statement of compliance

The consolidated financial statements of the Group have been prepared in accordance with International Financial Reporting Standards (IFRSs) adopted by the European Union. These consolidated financial statements also comply with the Croatian Accounting Act in effect on the date of issue of these consolidated financial statements. These consolidated financial statements are a translation of the official statutory IFRS consolidated financial statements.

Basis of preparation

The consolidated financial statements are prepared on the historical cost basis, with the exception of financial instruments which are carried at fair value. These comprise derivative financial instruments and financial assets and liabilities at fair value through profit or loss. The accounting policies have been consistently applied to all periods presented in these consolidated financial statements.

The preparation of consolidated financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. The estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgements about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised if the revision affects only that period or in the period of revision and future periods if the revision affects both current and future periods. Judgements made by management in the application of IFRSs that have significant effect on the consolidated financial statements and estimates are discussed in Note 2.

Going concern

The directors have a reasonable expectation that the Group has adequate resources to continue in operational existence for the foreseeable future. The Group therefore continues to adopt the going concern basis in preparing its consolidated financial statements.

1 Significant accounting policies (continued)

Changes in accounting policies and disclosures

(a) New and amended standards adopted by the Group

The Group has adopted the following new and amended IFRS and IFRIC interpretations during the year which were endorsed by the EU. When the adoption of the standard or interpretation is deemed to have an impact on the financial statements or performance of the Group, its impact is described below.

Amendment to IAS 1 Financial Statement Presentation Regarding Other Comprehensive Income (effective for annual periods beginning on or after 1 July 2012)

The main change resulting from these amendments is a requirement for entities to group items presented in other comprehensive income ("OCI") on the basis of whether they are potentially reclassifiable to comprehensive income subsequently (reclassification adjustments). The amendments do not address which items are presented in OCI. The amendment affects presentation only and therefore did not have an impact on the Group financial position or performance.

Amended IAS 19, Employee Benefits (issued in June 2011, effective for periods beginning on or after 1 January 2013)

Makes significant changes to the recognition and measurement of defined benefit pension expense and termination benefits, and to the disclosures for all employee benefits. The standard requires recognition of all changes in the net defined benefit liability (asset) when they occur, as follows: (i) service cost and net interest in profit or loss; and (ii) remeasurements in other comprehensive income. The Group reports accumulated amount of these remeasurements in retained earnings in equity. Retrospective application of the standard did not have a material impact on the consolidated financial statements of the Group.

Amendment to IFRS 7 Financial Instruments: Disclosures on Asset and Liability Offsetting (effective for annual periods beginning on or after 1 January 2013)

This amendment includes new disclosures to facilitate comparison between those entities that prepare IFRS financial statements to those that prepare financial statements in accordance with US GAAP. This amendment did not have an impact on the Group financial position or performance.

IFRS 13 Fair Value Measurement (effective for annual periods beginning on or after 1 January 2013)

IFRS 13 aims to improve consistency and reduce complexity by providing a precise definition of fair value and a single source of fair value measurement and disclosure requirements for use across IFRSs. The requirements, which are largely aligned between IFRS and US GAAP, do not extend the use of fair value accounting but provide guidance on how it should be applied where its use is already required or permitted by other standards within IFRSs or US GAAP. IFRS 13 impacts presentation and disclosure and has no impact on measurement in the Group financial statements.

Annual improvements 2011 (effective for annual periods beginning on or after 1 January 2013)

These annual improvements, address six issues in the 2009-2011 reporting cycle. It includes changes to:

IFRS 1 First time adoption
IAS 1 Financial statement presentation
IAS 16 Property plant and equipment
IAS 32 Financial instruments; Presentation
IAS 34 Interim financial reporting

These improvements did not have an impact on the Group financial statements.

1 Significant accounting policies (continued)

Changes in accounting policies and disclosures (continued)

(b) Standards and interpretations issued but not yet effective

IFRS 10 Consolidated Financial Statements (effective for annual periods beginning on or after 1 January 2014)

The objective of IFRS 10 is to establish principles for the presentation and preparation of consolidated financial statements when an entity controls one or more other entities to present consolidated financial statements. It defines the principle of control, and establishes controls as the basis for consolidation. It sets out how to apply the principle of control to identify whether an investor controls an investee and therefore must consolidate the investee. It also sets out the accounting requirements for the preparation of consolidated financial statements. Management is currently assessing the impact that IFRS 10 will have on the financial statements but does not expect any impact on them, and plans to adopt this new standard on its effective date.

IFRS 11 Joint Arrangements (effective for annual periods beginning on or after 1 January 2014)

IFRS 11 is a more realistic reflection of joint arrangements by focusing on the rights and obligations of the arrangement rather than its legal form. There are two types of joint arrangement: joint operations and joint ventures. Joint operations arise where a joint operator has rights to the assets and obligations relating to the arrangement and therefore accounts for its interest in assets, liabilities, revenue and expenses. Joint ventures arise where the joint operator has rights to the net assets of the arrangement and therefore equity accounts for its interest. Proportional consolidation of joint ventures is no longer allowed. Management does not expect IFRS 11 to have an impact on the financial statements of the Group, and plans to adopt this new standard on its effective date.

IFRS 12 Disclosures of Interests in Other Entities (effective for annual periods beginning on or after 1 January 2014)

IFRS 12 includes the disclosure requirements for all forms of interests in other entities, including joint arrangements, associates, special purpose vehicles and other off balance sheet vehicles. Management does not expect IFRS 12 to have an impact on the financial statements of the Group, and plans to adopt this new standard on its effective date.

IAS 27 (revised 2011) Separate Financial Statements (effective for annual periods beginning on or after 1 January 2014)

IAS 27 (revised 2011) includes the provisions on separate financial statements that are left after the control provisions of IAS 27 have been included in the new IFRS 10. Management is currently assessing the impact that IAS 27 will have on the financial statements but does not expect any impact on them, and plans to adopt this new standard on its effective date.

IAS 28 (revised 2011) Associates and Joint Ventures (effective for annual periods beginning on or after 1 January 2014)

IAS 28 (revised 2011) includes the requirements for joint ventures, as well as associates, to be equity accounted following the issue of IFRS 11. Management does not expect IAS 28 to have an impact on the financial statements of the Group, and plans to adopt this new standard on its effective date.

1 Significant accounting policies (continued)

Changes in accounting policies and disclosures (continued)

(b) Standards and interpretations issued but not yet effective (continued)

Amendments to IFRSs 10, 11 and 12 on Transition Guidance (effective for annual periods beginning on or after 1 January 2014)

These amendments provide additional transition relief to IFRSs 10, 11 and 12, limiting the requirement to provide adjusted comparative information to only the preceding comparative period. For disclosures related to unconsolidated structured entities, the amendments will remove the requirement to present comparative information for periods before IFRS 12 is first applied. Management is currently assessing the impact of the amendment on its financial statements, and plans to adopt this amendment on its effective date.

Amendments to IFRS 10, IFRS 12 and IAS 27 – on Consolidation for Investment Entities (issued on 31 October 2012 and effective for annual periods beginning 1 January 2014)

These amendments mean that many funds and similar entities will be exempt from consolidating most of their subsidiaries. Instead, they will measure them at fair value through comprehensive income. The amendments give an exception to entities that meet an 'investment entity' definition and which display particular characteristics. Changes have also been made in IFRS 12 to introduce disclosures that an investment entity needs to make. Management does not expect this amendment to have an impact on the financial statements of the Group, and plans to adopt this new standard on its effective date.

Amendments to IAS 32 Financial Instruments: Presentation on Asset and Liability Offsetting (issued in December 2012 and effective for annual periods beginning on or after 1 January 2014)

These amendments are added to the application guidance in IAS 32 Financial instruments: Presentation, and clarify some of the requirements for offsetting financial assets and financial liabilities on the statement of financial position. Management does not expect this amendment to have an impact on the financial statements of the Group, and plans to adopt this new standard on its effective date.

Amendment to IAS 36 Impairment of Assets on Recoverable Amount Disclosures (issued on 29 May 2013 and effective for annual periods beginning 1 January 2014)

This amendment addresses the disclosure of information about the recoverable amount of impaired assets if that amount is based on fair value less costs of disposal. The amendment could have an impact on disclosure only, but not on measurement and recognition of the assets in the Group financial position or performance. Management plans to adopt this amendment on its effective date.

IFRS 9 Financial Instruments (effective for annual periods beginning on or after 1 January 2015)

IFRS 9 is the first standard issued as part of a wider project to replace IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortised cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The guidance in IAS 39 on impairment of financial assets and hedge accounting continues to apply. Management does not expect IFRS 9 to have an impact on the financial statements, and plans to adopt this new standard on the effective date as of and when endorsed by the EU.

1 Significant accounting policies (continued)

Changes in accounting policies and disclosures (continued)

(b) Standards and interpretations issued but not yet effective (continued)

IFRIC 21 Levies (issued on 20 May 2013 and effective for annual periods beginning on or after 1 January 2014)

This is an interpretation of IAS 37 Provisions, contingent liabilities and contingent assets. IAS 37 sets out criteria for the recognition of a liability, one of which is the requirement for the entity to have a present obligation as a result of a past event (known as an obligating event). The interpretation clarifies that the obligating event that gives rise to a liability to pay a levy is the activity described in the relevant legislation that triggers the payment of the levy. Management does not expect IFRIC 21 to have an impact on the financial statements, and plans to adopt this new standard on the effective date as of and when endorsed by the EU.

Amendment to IAS 19 – Defined benefit plans: Employee contributions (issued in November 2013 and effective for annual periods beginning 1 July 2014)

The amendment allows entities to recognise employee contributions as a reduction in the service cost in the period in which the related employee service is rendered, instead of attributing the contributions to the periods of service, if the amount of the employee contributions is independent of the number of years of service. The Group is currently assessing the impact of the amendment on its financial statements.

Annual Improvements to IFRSs 2012 (issued in December 2013 and effective for annual periods beginning on or after 1 July 2014, unless otherwise stated below)

The improvements consist of changes to seven standards.

IFRS 2 was amended to clarify the definition of a 'vesting condition' and to define separately 'performance condition' and 'service condition'; The amendment is effective for share-based payment transactions for which the grant date is on or after 1 July 2014.

IFRS 3 was amended to clarify that (1) an obligation to pay contingent consideration which meets the definition of a financial instrument is classified as a financial liability or as equity, on the basis of the definitions in IAS 32, and (2) all non-equity contingent consideration, both financial and non-financial, is measured at fair value at each reporting date, with changes in fair value recognised in profit and loss. Amendments to IFRS 3 are effective for business combinations where the acquisition date is on or after 1 July 2014.

IFRS 8 was amended to require (1) disclosure of the judgements made by management in aggregating operating segments, including a description of the segments which have been aggregated and the economic indicators which have been assessed in determining that the aggregated segments share similar economic characteristics, and (2) a reconciliation of segment assets to the entity's assets when segment assets are reported.

The basis for conclusions on IFRS 13 was amended to clarify that deletion of certain paragraphs in IAS 39 upon publishing of IFRS 13 was not made with an intention to remove the ability to measure short-term receivables and payables at invoice amount where the impact of discounting is immaterial.

IAS 16 and IAS 38 were amended to clarify how the gross carrying amount and the accumulated depreciation are treated where an entity uses the revaluation model.

IAS 24 was amended to include, as a related party, an entity that provides key management personnel services to the reporting entity or to the parent of the reporting entity ('the management entity'), and to require to disclose the amounts charged to the reporting entity by the management entity for services provided.

The Group is currently assessing the impact of the amendments on its financial statements.

1 Significant accounting policies (continued)

Changes in accounting policies and disclosures (continued)

(b) Standards and interpretations issued but not yet effective (continued)

Annual Improvements to IFRSs 2013 (issued in December 2013 and effective for annual periods beginning on or after 1 July 2014)

The improvements consist of changes to four standards.

The basis for conclusions on IFRS 1 is amended to clarify that, where a new version of a standard is not yet mandatory but is available for early adoption, a first-time adopter can use either the old or the new version, provided the same standard is applied in all periods presented.

IFRS 3 was amended to clarify that it does not apply to the accounting for the formation of any joint arrangement under IFRS 11. The amendment also clarifies that the scope exemption only applies in the financial statements of the joint arrangement itself.

The amendment of IFRS 13 clarifies that the portfolio exception in IFRS 13, which allows an entity to measure the fair value of a group of financial assets and financial liabilities on a net basis, applies to all contracts (including contracts to buy or sell non-financial items) that are within the scope of IAS 39 or IFRS 9.

IAS 40 was amended to clarify that IAS 40 and IFRS 3 are not mutually exclusive. The guidance in IAS 40 assists preparers to distinguish between investment property and owner-occupied property. Preparers also need to refer to the guidance in IFRS 3 to determine whether the acquisition of an investment property is a business combination. The Group is currently assessing the impact of the amendments on its financial statements.

1 Significant accounting policies (continued)

Functional and presentational currency

Items included in the financial statements of each of the Group's entities are measured using the currency of the primary economic environment where the entity operates ('the functional currency'). The consolidated financial statements are presented in Croatian kuna (HRK), which is the Company's functional and the Group's presentation currency.

Property, plant and equipment

Items of property, plant and equipment are shown at cost or deemed cost, less accumulated depreciation and impairment losses.

The Group recognises in the carrying amount of an item of property, plant and equipment the cost of replacing part of such an item when that cost is incurred if it is probable that the future economic benefits embodied with the item will flow to the Group and the cost of the item can be measured reliably. All other expenditure on repairs and maintenance is expensed as incurred. Where parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items of property, plant and equipment.

Land is not depreciated. Depreciation on other assets is provided on a straight-line basis to allocate their cost over the estimated economic useful life of the assets. The estimated useful lives are as follows:

	Useful lives
Buildings	5 - 30 years
Plant and equipment	2 - 10 years
Other	5 - 7 years

The depreciation method, useful lives and residual values are reviewed, and adjusted if appropriate, at each balance sheet date. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. Gains and losses on disposals are determined by comparing proceeds with carrying amount, and are included in the consolidated statement of comprehensive income.

1 Significant accounting policies (continued)

Intangible assets

Intangible assets are stated on initial recognition at cost and subsequently at cost less accumulated amortisation and impairment losses.

Amortisation is provided on a straight-line basis over the estimated useful lives of intangible assets. Intangible assets include acquired computer software, and are amortised on a straight-line basis over their useful life of 2 - 4 years. Cost associated with maintaining computer software is recognised as an expense as incurred.

Impairment of assets

Property, plant and equipment, intangible assets, financial instruments and receivables are reviewed for impairment at each balance sheet date or whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. Whenever the carrying amount of an asset exceeds its estimated recoverable amount, an impairment loss is recognised in the consolidated statement of comprehensive income for items of property, plant and equipment, intangible assets, financial instruments and receivables.

The recoverable amount of property, plant and equipment and intangible assets is the higher of an asset's fair value less costs to sell or value in use. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash flows (cash-generating units). In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset or cash-generating unit. Non-financial assets that suffered impairment are reviewed for possible reversal of the impairment at each reporting date. Impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount and to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation, if no impairment loss had been recognised.

The recoverable amount of receivables carried at amortised cost is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset. The Group assesses at the end of each reporting period whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred only if there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

Evidence of impairment may include indications that the debtors or a group of debtors is experiencing significant financial difficulty, default or delinquency in interest or principal payments, the probability that they will enter bankruptcy or other financial reorganisation, and where observable data indicate that there is a measurable decrease in the estimated future cash flows, such as changes in arrears or economic conditions that correlate with defaults.

1 Significant accounting policies (continued)

Impairment of assets (continued)

For loans and receivables category, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced and the amount of the loss is recognised in the consolidated income statement. If a loan or held-to-maturity investment has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract. As a practical expedient, the Group may measure impairment on the basis of an instrument's fair value using an observable market price.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the debtor's credit rating), the reversal of the previously recognised impairment loss is recognised in the consolidated statement of comprehensive income.

Short-term receivables are not discounted. The recoverable amount of financial assets is the higher of the asset's net selling price and its value in use.

An impairment loss in respect of held-to-maturity investments and receivables is reversed if the subsequent increase in recoverable amount can be related objectively to an event occurring after the impairment loss was recognised.

Financial instruments

The Group classifies its financial instruments in the following categories: financial assets and financial liabilities at fair value through profit or loss, loans and receivables, available-for-sale financial assets or held-to-maturity investments. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its financial instruments at initial recognition and re-evaluates this at every reporting date.

Financial instruments at fair value through profit or loss category have two sub-categories: "financial instruments held for trading", and those designated by management at fair value through profit or loss at inception. Financial instruments acquired principally for the purpose of generating a short-term profit are classified as held for trading and included in current assets. These include derivative financial instruments, which do not qualify for hedge accounting. Financial instruments at fair value through profit or loss include debt and equity securities and investments in investment funds.

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than those that the Group intends to sell immediately or in the near term, which are designated at fair value through profit or loss or as available for sale. These include non-current receivables and deposits with financial institutions.

1 Significant accounting policies (continued)

Financial instruments (continued)

Financial instruments with fixed or determinable payments and fixed maturity that the Group has positive intent and ability to hold to maturity are classified as held-to-maturity investments. All other financial instruments are classified as available for sale. Financial instruments at fair value through profit or loss, held-to-maturity investments and available-for-sale financial assets are recognised on the trade date, which is the date that the Group commits to purchase or sell the instrument. Loans and receivables and other financial liabilities are recognised on the day they are transferred to the Group.

Financial assets are initially measured at the fair value of the consideration given for them, including transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets and financial liabilities at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the consolidated statement of comprehensive income. All financial assets and financial liabilities at fair value through profit or loss and available-for-sale financial assets are subsequently carried at fair value without any deduction for transaction costs that the Group may incur on sale or other disposal. Available-for-sale financial assets for which fair value cannot be reliably measured are stated at cost, including transaction costs, less impairment losses.

The fair value of financial instruments at fair value through profit or loss or available for sale is based on their quoted market price at the balance sheet date, without any deduction for transaction costs. The fair value of derivatives that are not exchange-traded is estimated at the amount that the Group would receive or pay to terminate the contract at the balance sheet date. Realised and unrealised gains and losses arising from changes in the fair value of financial assets at fair value through profit or loss are recognised in the consolidated statement of comprehensive income in the period in which they arise.

Changes in the fair value of monetary securities denominated in a foreign currency and classified as available for sale are analysed between translation differences resulting from changes in amortised cost of the security and other changes in the carrying amount of the security. The translation differences are recognised in profit or loss, and other changes in carrying amount are recognised in equity. Changes in the fair value of other monetary securities classified as available for sale and non-monetary securities classified as available for sale are recognised in equity. When securities classified as available-for-sale are sold or impaired, the accumulated fair value adjustments recognised in equity are included in the consolidated statement of comprehensive income as ‘realised gains and losses from available-for-sale securities’.

Interest on available-for-sale securities calculated using the effective interest method is recognised in the consolidated statement of comprehensive income. Dividends on available-for-sale equity instruments are recognised in the consolidated statement of comprehensive income when the Group’s right to receive payments is established.

1 Significant accounting policies (continued)

Financial instruments (continued)

A financial asset is derecognised when the Group loses the contractual rights that comprise that asset. This occurs when the rights are realised, expire or are surrendered. A financial liability is derecognised when it is extinguished. Financial instruments at fair value through profit or loss, available-for-sale financial assets and held-to-maturity investments are derecognised and corresponding receivables from the buyer for the payment are recognised as of the date the Group commits to sell the assets. The Group uses the specific identification method to determine the gain or loss on derecognition. Loans and receivables are derecognised on the day they are transferred by the Group. Other financial liabilities are derecognised when the Group's contractual obligations are discharged, cancelled or expire.

The Group uses derivative financial instruments to hedge economically its exposure to foreign exchange risk arising from operational activities. Hedge accounting has not been applied and those derivative instruments are accounted for as financial instruments held for trading. Derivative instruments are measured initially at fair value and the related transaction costs are recognised in the consolidated statement of comprehensive income and subsequent to initial recognition, are stated at fair value. The gain or loss on remeasurement to fair value is recognised immediately in profit or loss. The fair value of a forward exchange contract is its quoted price at the balance sheet date, being the present value of the quoted forward price.

Trade and other receivables

Receivables are initially recognised at the fair value of consideration given and are carried at amortised cost, using the effective interest rate. Receivables are written down to their estimated realisable value through an impairment allowance.

Service contract work-in-progress is stated at cost plus profit recognised to date less a provision for foreseeable losses and less progress billings on long-term contracts. Cost includes all expenditure related directly to specific projects and an allocation of fixed and variable overheads incurred in the Group's contract activities based on budgeted capacity.

Cash and cash equivalents

Cash comprises cash held at banks and on hand. Cash equivalents include demand deposits and time deposits with maturities up to three months.

Trade and other payables

Trade and other payables are initially recognised at fair value and subsequently measured at amortised cost using the effective interest rate.

1 Significant accounting policies (continued)

Inventories

Inventories are stated at the lower of cost and net realisable value. Net realisable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses. The cost of other inventories is based on the First In First Out (FIFO) principle and includes expenditures incurred in acquiring the inventories and bringing them to their existing location and condition. In case of manufactured inventories the cost includes materials, labour and related overhead, and expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. Slow-moving and obsolete inventories have been written down to their estimated realisable value.

Share capital

Share capital is stated in HRK at nominal value.

Incremental costs directly attributable to the issue of new ordinary shares or options are shown in equity as a deduction, net of tax, from the proceeds. Where the Group purchases its own equity share capital (treasury shares), the consideration paid, including any directly attributable incremental costs (net of income taxes) is deducted from equity attributable to the Group's equity holders until the shares are cancelled or reissued. Where such ordinary shares are subsequently reissued, any consideration received, net of any directly attributable incremental transaction costs and the related income tax effects, is included in equity attributable to the Group's equity holders.

Income tax

The tax expense for the period is based on taxable profit for the year and comprises current and deferred tax. Income tax is recognised in the consolidated statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. The current income tax charge is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the company and its subsidiaries operate and generate taxable income. Management periodically evaluates positions taken in tax returns with respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised by using the balance sheet liability method on temporary differences arising between tax basis of assets and liabilities and their carrying amount in the financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred tax assets and liabilities are not discounted and are classified as non-current assets and/or liabilities in the balance sheet. Deferred tax assets are recognised when it is probable that sufficient taxable profits will be available against which the deferred tax assets can be utilised. At each balance sheet date, the Group reassesses unrecognised deferred tax assets and the carrying amount of deferred tax assets.

1 Significant accounting policies (continued)

Income tax (continued)

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. Deferred tax assets and liabilities are measured by using the tax rates expected to apply to taxable profit in the years in which those temporary differences are expected to be recovered or settled based on tax rates enacted or substantially enacted at the balance sheet date.

The measurement of deferred tax liabilities and deferred tax assets reflects the tax consequences that would follow from the manner in which the enterprise expects, at the balance sheet date, to recover or settle the carrying amount of its assets and liabilities.

Foreign currencies

Transactions denominated in foreign currencies are translated into HRK at the rate prevailing at the date of the transaction. Monetary assets and liabilities denominated in foreign currency at the balance sheet date have been translated to HRK at the foreign exchange rate ruling at that date. Foreign exchange differences arising from translation are included in the consolidated statement of comprehensive income. Non-monetary assets and liabilities denominated in foreign currencies that are stated at fair value are translated to HRK at foreign exchange rates ruling at the dates the values were determined. Non-monetary assets and items that are measured in terms of “historical cost of a foreign currency” are not retranslated.

Items included in the financial statements of each of the Group’s entities are measured using the currency of the primary economic environment where the entity operates (‘the functional currency’). The consolidated financial statements are presented in Croatian kuna (HRK), which is the Company’s functional and the Group’s presentation currency.

The results and financial position of all Group entities with a functional currency different from the presentation currency are translated into the presentation currency as follows:

(i) assets and liabilities for each balance sheet presented are translated at the closing rate at the date of that balance sheet;
(ii) income and expenses for each income statement are translated at average exchange rates; and
(iii) all resulting exchange differences are recognised in other comprehensive income.

On consolidation, exchange differences arising from the translation of the net investment in foreign operations are taken into other comprehensive income. When a foreign operation is sold, exchange differences that were recorded in equity are reclassified from other comprehensive income to the income statement as part of the gain or loss on sale.

1 Significant accounting policies (continued)

Recognition of revenues

Sales revenue represents the value of goods and services supplied to customers during the period, excluding value added taxes, trade discounts and rebates. Revenue is recognized with reference to all significant contractual terms when the product or service has been delivered, when the revenue amount is fixed or determinable, and when collection is reasonably assured. Specific contractual performance and acceptance criteria may impact the timing and amounts of revenue recognized.

The Group uses 3 main contract types with end customers as follows:

- <u>Delivery-type contracts</u>: Contracts for delivery of a product or a combination of products to form a whole or a part of a network as well as delivery of stand-alone products. Medium-size and large delivery type contracts generally include multiple elements. Such elements are normally standardized types of equipment or software as well as services such as network rollout.

  Revenue is recognized when risks and rewards have been transferred to the customer, normally stipulated in the contractual terms of trade. For delivery-type contracts that have multiple elements, revenue is allocated to each element based on relative fair values.

- <u>Construction-type contracts:</u> Contracts where the Group supplies to a customer a complete network, which to a large extent is based upon new technology or includes major components which are specifically designed for the customer.

  Revenues from construction-type contracts are recognized according to the stage of completion, using either the milestone output method or cost incurred method. Long-term construction contracts are assessed on a contract by contract basis and reflected in the consolidated statement of comprehensive income by recording revenue and related costs in line with contract activity.

- <u>Service contracts</u>: Contracts for various services such as: training, consulting, engineering, installation, and multi-year managed services.

  Revenue is generally recognized when the services have been provided. Revenue for fixed price service contracts covering longer periods is recognized pro rata over the contract period.

The majority of the Group's products and services are sold under delivery-type contracts including multiple elements, such as base stations, base station controllers, mobile switching centers, routers, microwave transmission links, various software products and related installation and integration services. Such contract elements generally have individual item prices in agreed price lists per customer.

The profitability of individual contracts is periodically assessed, and provisions for any estimated losses are made immediately when losses are probable.

1 Significant accounting policies (continued

Employee benefits

a) Long-term service benefits

The Group provides employees with jubilee and one-off retirement awards. The obligation and costs of these benefits are determined by using the Projected Unit Credit Method. The Projected Unit Credit Method considers each period of service as giving rise to an additional unit of benefit entitlement and measures each unit separately to build up the final obligation. The obligation is measured at the present value of estimated future cash flows using a discount rate that is similar to the interest rate on government bonds where the currency and terms of the government bonds are consistent with the currency and estimated terms of the benefit obligation.

b) Share-based payments

The Group operates an equity-settled, share-based compensation plan allowing the Group's employees to receive shares. The fair value of the employee services received in exchange for the grant of the Group's shares is recognised as an expense with a corresponding increase in equity. The fair value is measured at grant date and spread over the period during which the employees become unconditionally entitled to the shares. The total amount to be expensed over the vesting period is determined by reference to the fair value of the shares granted. At each balance sheet date, the Group revises its estimates of the number of shares that are expected to become granted. It recognises the impact of the revision of original estimates, if any, in the consolidated statement of comprehensive income, with a corresponding adjustment to equity. When distributed upon vesting date, treasury shares are credited at average purchase cost and recorded against retained earnings.

c) Bonus plans

The Group recognises a liability and an expense for bonuses as a provision where contractually obliged or where there is past practice that has created a constructive obligation.

Provisions

A provision is recognised when the Group has a present obligation (legal or constructive) as a result of a past event and it is probable (i.e. more likely than not) that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Provisions are reviewed at each balance sheet date and adjusted to reflect the current best estimate. The most significant provisions in the consolidated financial statements are provisions for warranty claims, penalty claims and litigation. If the effect is material and if the obligation is expected to be settled in a period of over 12 months, provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability. A provision for warranties is recognised when the underlying products or services are sold. The provision is based on historical warranty data and a weighting of all possible outcomes against their associated probabilities. The increase in the provision due to passage of time is recognised as interest expense.

Net financial income

Interest income is recognised using the effective interest method. When a loan and receivable is impaired, the company reduces the carrying amount to its recoverable amount, being the estimated future cash flow discounted at the original effective interest rate of the instrument, and continues unwinding the discount as interest income. Interest income on impaired loan and receivables is recognised using the original effective interest rate.

1 Significant accounting policies (continued)

Segment reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-maker. The chief operating decision-maker, who is responsible for allocating resources and assessing performance of the operating segments, has been identified as the Management Board that makes strategic decisions.

Borrowings

Borrowings are initially recognized at fair value, net of transaction costs incurred. Borrowings are subsequently stated at amortized cost; any difference between the proceeds (net of transaction costs) and the redemption value is recognized in the consolidated statement of comprehensive income over the period of the borrowings using the effective interest method.

Government grants

Grants from the government are recognised at their fair value where there is reasonable assurance that the grant will be received and the group will comply with all attached conditions.
Government grants relating to costs are deferred and recognised in the statement of comprehensive income over the period necessary to match them with the costs that they are intended to compensate.
Government grants relating to property, plant and equipment are included in non-current liabilities as deferred government grants and are credited to the statement of comprehensive income on a straight-line basis over the expected lives of the related assets and presented within “other income”.

Leases

Leases on terms in which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition, the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that type of asset, although the depreciation period must not exceed the lease term.

Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases, and the leased assets under such contracts are not recognized on the balance sheet. Payments made under operating leases (net of any incentives received from the lessor) are recognized in the consolidated statement of comprehensive income on a straight-line basis over the term of the lease.

Dividend distribution

Dividend distribution to the Group’s shareholders is recognized as a liability in the Group’s consolidated financial statements in the period in which the dividends are approved by the Group’s shareholders.

1 Significant accounting policies (continued)

Consolidation

Subsidiaries are all entities (including special purpose entities) over which the Group has the power to govern the financial and operating policies generally accompanying a shareholding of more than one half of the voting rights. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether the Group controls another entity. Subsidiaries are fully consolidated from the date on which control is transferred to the Group and are de-consolidated from the date that control ceases.

The Group applies the acquisition method to account for business combinations. The consideration transferred for the acquisition of a subsidiary is the fair values of the assets transferred, the liabilities incurred and the equity interests issued by the Group. The consideration transferred includes the fair value of any asset or liability resulting from a contingent consideration arrangement. Acquisition related costs are expensed as incurred. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date. On an acquisition-by-acquisition basis, the Group recognises any non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the recognised amounts of identifiable acquiree's net assets.

Goodwill is initially measured as excess of the aggregate of the consideration transferred and the fair value of non-controlling interest in the acquiree and acquisition-date fair value of any previous equity interest in the acquiree over the fair value of the Group's share of the identifiable net assets acquired. If this is lower than the fair value of the net assets of the subsidiary acquired in the case of a bargain purchase, the difference is recognised directly in the consolidated statement of comprehensive income.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

2 Critical accounting estimates and judgements

Accounting estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. The Group makes estimates and assumptions concerning the future. The resulting accounting estimates will, by definition, seldom equal the related actual results. The estimates and assumptions that have a significant risk of causing a material adjustment to the carrying amounts of assets and liabilities within the next financial year are discussed below.

(a) Impairment losses on loans and receivables

The Group reviews its receivables to assess impairment on a monthly basis. In determining whether an impairment loss should be recorded in the consolidated statement of comprehensive income, the Group makes judgements as to whether there is any observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of loans and receivables before the decrease can be identified with an individual loan or receivable in that portfolio. This evidence may include observable data indicating that there has been an adverse change in the payment status of borrowers in a Group, or national or local economic conditions that correlate with parameters relevant to assets in the Group.

2 Critical accounting estimates and judgements (continued)

(b) Deferred income tax asset recognition

The net deferred tax asset represents income taxes recoverable through future deductions from taxable profits. Deferred income tax assets are recorded to the extent that realisation of the related tax benefit is probable. In determining future taxable profits and the amount of tax benefits that are probable in the future, management makes judgements and applies estimation based on previous years taxable profits and expectations of future income that are believed to be reasonable under the existing circumstances. Due to the fact that the parent Company utilises research expenditure tax relief which is higher than taxable profits, no deferred tax assets are recognised in the financial statements.

Judgements

The Group has entered into several service contracts combining features and elements of other contracts for which management has had to use judgement to determine the appropriate accounting treatment.

Certain service contracts under which the Group also provides financing to the contracts are separated into sales revenue and financial income. The financial income is recognised using the effective interest over the life of the contract.

3 Sales revenue

	2013 HRK '000	**2012 HRK '000**
Sales revenue from products	528,056	1,131,034
Sales revenue from services	817,170	782,270
	1,345,226	1,913,304

4 Segment reporting

The Group has determined the operating segments based on the reports reviewed by the Management Board that are used to make strategic decisions. The Management Board assesses the performance of the operating segments based on a measure of adjusted Operating profit. The measurement basis excludes the effects of gains/losses on operating exchange rate differences and administration expenses.

When determining the operating segments, the Group has looked at which market and to what type of customers the Group's products are aimed, and through what distribution channels they are sold, as well as to commonality regarding technology, research and development. Segment results and liabilities include items directly attributable to a segment as well as those that can be allocated on a reasonable basis.

The Group is organised into business units and has three primary reportable operating segments as follows:

- Networks include products and solutions for mobile and fixed broadband access, core networks, and transmission.
- Professional Services include managed services, consulting and systems integration, customer support and network rollout services.
- Support Solutions provide enablers and applications for operators.

Segments are managed in Europe, the Middle East and Africa. Revenues determined based on the geographic location of customers are disclosed in this note. All the Group’s assets are located in Croatia.

	2013	**2012**
	HRK ‘000	**HRK ‘000**
Sales revenue in domestic market	340,972	268,095
Sales revenue in Russia, Belarus, Kazakhstan, Georgia, Kyrgyzstan, Moldova, Uzbekistan and Armenia	169,101	876,890
Sales revenue to Ericsson, Note 25 (a)	568,749	551,998
Sales revenue in Bosnia and Herzegovina, Montenegro, Macedonia and Kosovo	256,630	204.925
Other export sales revenue	9,774	11,396
	1,345,226	1,913,304

4 Segment reporting (continued)

	Networks		Professional services		Support solutions		Unallocated		**Total**	
	2013	**2012**	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**	**2013**	**2012**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Sales revenue - gross	775,217	1,250,541	539,336	523,312	40,986	146,396	-	-	1,355,539	1,920,249
Inter-segment sales	(6,151)	(2,170)	(4,113)	(4,771)	(49)	(4)	-	-	(10,313)	(6,945)
Sales revenue -- net	769,066	1,248,371	535,223	518,541	40,937	146,392	-	-	1,345,226	1,913,304
Operating profit/(loss)	51,013	62,642	106,430	79,721	1,545	5,479	(31,749)	(31,231)	127,239	116,611
Finance income									17,284	24,487
Finance expense									(163)	(80)
Profit before tax									144,360	141,018
Income tax									(5)	(14,105)
Profit for the year									**144,355**	**126,913**
Other segment information:										
Segment liabilities	125,253	148,075	80,911	69,913	5,918	21,334	164,872	175,615	376,954	414,937
Segment assets	189,156	214,528	153,265	83,914	11,763	22,089	693,905	849,134	1,048,090	1,169,665

Revenues of approximately HRK 568,748 thousand (2012: HRK 1,349,489 thousand) are derived from external customers whose single revenues represent 10 percent or more of the Group's sales revenues, and they are realised in all three segments.

Reportable segments' liabilities are reconciled to total liabilities as follows:

	2013	**2012**
	HRK '000	**HRK '000**
Segment liabilities	212,082	239,322
Unallocated:		
Non-current liabilities	4,766	4,464
Current liabilities:		
Interest-bearing borrowings	309	1,710
Trade and other payables	80,742	96,541
Accrued charges and deferred revenue	65,597	54,334
Provisions	13,458	18,566
Total liabilities per the consolidated statement of financial position	376,954	414,937

4 Segment reporting (continued)

Reportable segments' assets are reconciled to total assets as follows:

	2013	2012
	HRK '000	**HRK '000**
Segment assets	354,185	320,531
Unallocated:		
Non-current assets	152,569	151,793
Current assets:		
Trade receivables	15,292	21,513
Other receivables	3,715	15,169
Financial assets at fair value through profit or loss	109,845	145,365
Prepayments and accrued income	1,156	3,655
Cash and cash equivalents	411,328	511,639
Total assets per the consolidated statement of financial position	1,048,090	1,169,665

5 Expenses by nature

	2013	2012
	HRK '000	**HRK '000**
Changes in contract work in progress (Note 13)	(17,757)	(11,062)
Material and external services (1) (2)	728,877	1,294,605
Personnel expenses (Note 6)	478,194	477,263
Depreciation and amortisation (Notes 10,11)	40,282	44,619
	1,229,596	1,805,425

1) Including audit fee expenses of HRK 455 thousand (2012: HRK 420 thousand).

2) Material and external services costs do not include the effect of reclassifying other income and other operating expenses to material and external services amounting to HRK 11,133 thousand (2012: HRK 12,240 thousand).

6 Personnel expenses

	2013	2012
	HRK '000	HRK '000
Net salaries	235.130	236,339
Taxes and contributions	219.262	209,903
Other payroll-related costs	20,157	25,764
Equity-settled transactions (Note 21 (b))	3,645	5,257
	478,194	477,263

Other payroll-related costs mainly relate to transportation expenses and holiday bonus.
Personnel expenses include HRK 78,471 thousand (2012: HRK 69,756 thousand) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries (Gross II).

In addition, Personnel expenses include HRK 2,564 thousand (2012: HRK 11,939 thousand) in respect of voluntary redundancy costs. The movements in provisions related to these costs are described in Note 23, Provisions.

As at 31 December 2013, total number of employees was 1,740 (2012: 1,621).

7 Finance income and expense

Finance income

	2013	2012
	HRK '000	HRK '000
Interest income (Note 7 (a))	10,033	20,625
Net gains from remeasurement of financial assets at fair value through profit or loss (Note 7 (c))	1,493	2,536
Amortization of discount (Note 7 (b))	2,003	3,021
Net foreign exchange (loss)/gain	3,755	(1,695)
	17,284	24,487

Finance expense

	2013	2012
	HRK '000	HRK '000
Interest expense	163	80
	163	80

7 (a)

	2013	2012
	HRK '000	HRK '000
Interest income		
- on loans to customers	1,511	2,806
- on debt securities	436	660
- on term deposits	4,459	15,215
- on other receivables	3,627	1,944
	10,033	20,625

7 (b)

The Group released HRK 2,003 thousand (2012: HRK 3,021 thousand) into finance income due to amortisation of discount related to receivables impairment provision.

7 Finance income and expense (continued)

7 (c)

	HRK ’000	HRK ’000
Net gains/(losses) from remeasurement of financial assets at fair value through profit or loss		
- Equity securities	-	(224)
- Investment in investment funds	1,559	2,050
- Debt securities	(66)	710
	1,493	2,536

8 Income tax expense

Income tax has been calculated on the taxable income at statutory tax rates applicable to profits in the respective countries.

Income tax expense recognised in the consolidated statement of comprehensive income comprises:

	2013 HRK ‘000	2012 HRK ‘000
Current income tax expense	(5)	(113)
Total deferred tax expense relating to the origination and reversal of temporary differences	-	(13,992)
Total income tax expense	(5)	(14,105)

Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through future taxable profits is probable. The Group did not recognise deferred income tax assets of HRK 50,581 thousand (2012: HRK 53,474 thousand) in respect of tax losses amounting to HRK 252,908 thousand (2012: HRK 267,372 thousand) that can be carried forward against future taxable income.

Tax incentives included in the tax return for 2011 were inspected during 2013 by the Ministry of Science. Out of HRK 151,230 thousand of tax incentives recorded by the Company, HRK 108,629 thousand were approved by the Ministry. Consequently, the Company adjusted its tax loss for 2011 to HRK 9,478 thousand. A tax loss may be carried forward for five years subsequent to the year in which it was incurred. The availability of tax losses against future periods, subject to review by the Ministry of Finance, is as follows:

	HRK ‘000
Tax loss for 2009 – expires 31 December 2014	64,449
Tax loss for 2010 – expires 31 December 2015	151,549
Tax loss for 2011 – expires 31 December 2016	9,478
Tax loss for 2012 – expires 31 December 2017	190
Tax loss for 2013 – expires 31 December 2018	27,242
	252,908

As disclosed in Note 2, Critical accounting estimates and judgements, due to the fact that the Group utilises research expenditure tax relief which is higher than taxable profits, in 2012 the Group released deferred tax assets of HRK 13,992 thousand. No deferred tax assets are recognised in the consolidated financial statements for the year ending 31 December 2013.

8 Income tax expense (continued)

The tax on the Group's profit before tax differs from the theoretical amount that would arise using the weighted average tax rate applicable to profits of the consolidated entities as follows:

	2013 HRK ‘000	2012 HRK ‘000
Profit before tax	144,360	141,018
Tax calculated at domestic tax rates applicable to profits in the respective countries	28,851	28,131
Tax effects of:		
Expenses not deductible for tax purposes	3,875	2,674
Tax incentives	(32,640)	(27,279)
Utilisation of tax losses	(81)	(3,413)
Tax charge	5	113
Effective tax rate	0.0%	0.1%

Tax incentives include only part of additional tax allowances for certain expenditure totaling HRK 32,640 thousand (2012: HRK 27,279 thousand) which meets research and development incentives definitions under Croatian tax legislation. The underlying research and development expenditure is included in cost of sales.

In accordance with local regulations, the Tax Authority may inspect books and records of the parent Company and its subsidiaries’ at any time within 3 years following the end of the year in which the tax liability is reported and may impose additional tax assessments and penalties. The Group's management is not aware of any circumstances which may give rise to a potential material liability in this respect.

9 Earnings per share

	2013	2012
Profit for the year (HRK ‘000)	144,355	126,913
Weighted Average Number of Shares Outstanding at the year-end	1,328,428	1,327,157
Earnings per share (HRK)	108.67	95.63

Basic and fully diluted earnings per share are the same since the Group does not have any dilutive potential ordinary shares.

10 Property, plant and equipment

	Land and buildings HRK '000	Plant and equipment HRK '000	Other HRK '000	Total HRK '000
As at 1 January 2012				
Cost or valuation	155,455	312,636	328	468,419
Accumulated depreciation	(102,914)	(231,121)	(205)	(334,240)
Net book amount	52,541	81,515	123	134,179
Year ended 31 December 2012				
Opening net book amount	52,541	81,515	123	134,179
Additions	-	30,354	-	30,354
Disposals	-	(4,718)	-	(4,718)
Depreciation charge	(3,298)	(39.483)	(8)	(42,789)
Closing net book amount	**49,243**	**67,668**	**115**	**117,026**
As at 31 December 2012				
Cost or valuation	155,455	305,999	328	461,782
Accumulated depreciation	(106,212)	(238,331)	(213)	(344,756)
Net book amount	49,243	67,668	115	117,026
Year ended 31 December 2013				
Opening net book amount	49,243	67,668	115	117,026
Additions	2,968	49,691	-	52,659
Disposals	-	(121)	-	(121)
Depreciation charge	(3,355)	(34,585)	(8)	(37,948)
Closing net book amount	**48,856**	**82,653**	**107**	**131,616**
As at 31 December 2013				
Cost or valuation	158,423	333,364	328	492,115
Accumulated depreciation	(109,567)	(250,711)	(221)	(360,499)
Net book amount	48,856	82,653	107	131,616

Included in the cost of property, plant and equipment is HRK 190,789 thousand (2012: HRK 187,108 thousand) of fully depreciated property, plant and equipment that is still used by the Group.

As at 31 December 2013, the Group had contracts totaling HRK 5,886 thousand (2012: HRK 3,643 thousand) related to future equipment purchases.

Depreciation expense of HRK 35,040 thousand (2012: HRK 40,478 thousand) has been charged in cost of sales, HRK 1,890 thousand (2012: HRK 1,453 thousand) in selling expenses and HRK 1,018 thousand (2012: HRK 858 thousand) in administrative expenses.

10 Property, plant and equipment *(continued)*

The Group acts as a lessor under operating leases, mainly in respect of land and buildings. Property leased to others with a carrying value of HRK 14,515 thousand (2012: HRK 16,580 thousand) is included within land and buildings. These assets are depreciated at the same depreciation rates as other buildings, and are leased for a non-cancellable period of five years which commenced in 2005. Subsequent renewals are negotiated with the lessee. No contingent rents are charged. Portions of the property which is held for rental could not be sold separately or leased out separately under finance lease. Consequently, the IAS 40 criteria for separate investment property recognition are not met.

Future minimum lease payments under non-cancellable operating leases in the aggregate and for each of the following periods are:

	2013	**2012**
	HRK ‘000	**HRK ‘000**
Less than one year	3,419	3,240
Between one and five years	1,709	1,620
	5,128	4,860

11 Intangible assets

The movement on intangible assets in the year ended 31 December 2013 may be analysed as follows:

	Application software HRK '000
As at 1 January 2012	
Cost or valuation	18,395
Accumulated amortization	(14,970)
Net book amount	3,425
Year ended 31 December 2012	
Opening net book amount	3,425
Additions	2,719
Amortization charge	(1,830)
Closing net book amount	4,314
As at 31 December 2012	
Cost or valuation	10,855
Accumulated amortization	(6,541)
Net book amount	4,314
Year ended 31 December 2013	
Opening net book amount	4,314
Additions	132
Amortization charge	(2,334)
Closing net book amount	2,112
As at 31 December 2013	
Cost or valuation	9,480
Accumulated amortization	(7,368)
Net book amount	2,112

Included in cost of intangible assets is HRK 5,027 thousand (2012: HRK 3,250 thousand) of fully amortised intangible assets that are still used by the Group.

Amortisation of HRK 2,155 thousand (2012: HRK 1,731 thousand) has been charged in cost of sales, HRK 116 thousand (2012: HRK 62 thousand) in selling expenses and HRK 63 thousand (2012: HRK 37 thousand) in administrative expenses.

12 Loans and receivables

	2013 HRK '000	2012 HRK '000
Deposits with financial institutions, denominated in foreign currency	8,297	8,241
Non-current receivables from foreign customers, denominated in foreign currency	6,274	20,900
Non-current receivables from domestic customers, denominated in HRK	-	49
Receivables for sold apartments		
- denominated in foreign currency	5,615	5,529
- denominated in HRK	744	345
Total loans and receivables	20,930	35,064
Impairment allowance on loans and receivables	(2,129)	(4,651)
	18,801	30,413

Deposits with financial institutions of HRK 7,318 thousand (2012: HRK 7,230 thousand) are placed as guarantee deposits for housing loans provided to the Group's employees, earning interest at fixed rate 0.37% per annum (2012: 0.37% per annum), and with a remaining maturity of over three years. The remaining amount of HRK 979 thousand (2012: HRK 1,011 thousand) relates to guarantee deposit for customer financing, bearing interest at twelve-month USD LIBOR plus 0.50 pp per annum and maturing in 2015.

Loans and receivables from customers are partially secured with bank guarantees and letters of credit. The current portion of the non-current receivables is classified under current assets.

Non-current portion of foreign and domestic loans and receivables

Due	2013 HRK '000	2012 HRK '000
2014	-	14,667
2015	6,274	6,282
	6,274	20,949

Receivables for sold apartments are shown net of amounts due to the Croatian state. Housing loans to employees are linked to the counter value of euro, repayments are made by deduction from monthly salary and the loans are secured with charges on the house or apartment. Receivables for sold apartments and housing loans provided to a limited number of employees bear fixed interest rates of up to 5% per annum. A discount in the amount of HRK 2,130 thousand (2012: HRK 2,209 thousand) is recognised in respect of these loans and amortised through the consolidated statement of comprehensive income, using the effective interest rate method at a rate of 7% per annum (2012: 7% per annum).

13 Inventories

	2013 HRK '000	2012 HRK '000
Raw materials	2,289	2,539
Contract work in progress	58,146	40,389
Total inventories	60,435	42,928
Impairment allowance	(8,929)	(9,660)
	51,506	33,268

Slow-moving or obsolete inventories have been written down to their estimated realisable value through an impairment allowance. The impairment allowance is included within other operating expenses in the consolidated statement of comprehensive income.

14 Trade receivables

	2013 HRK '000	2012 HRK '000
Foreign trade receivables	142,998	155,282
Current portion of non-current foreign receivables	15,948	20,406
Total current foreign receivables	158,946	175,688
Domestic trade receivables	117,018	83,038
Current portion of non-current domestic receivables	883	3,370
Total current domestic receivables	117,901	86,408
Impairment allowance on receivables	(30,695)	(34,509)
	246,152	227,587

Included in trade receivables is HRK 54 thousand (2012: HRK 2,497 thousand) of contract work in progress.

Movements in impairment allowance on loans and receivables were as follows:

	2013 HRK '000	2012 HRK '000
As at 1 January (Notes 12, 14)	39,160	51,355
Provision for receivables impaired during the year	7,139	7,262
Receivables written off during the year as uncollectible	(5,367)	(9,607)
Unused amounts reversed	(6,185)	(6,829)
Amortisation of discount	(1,923)	(3,021)
As at 31 December (Notes 12, 14)	32,824	39,160

Receivables are written down to their estimated realisable value through an impairment allowance.

Of the total HRK 32,824 thousand (2012: HRK 39,160 thousand) of impairment allowances as at 31 December 2013, HRK 30,694 thousand (2012: HRK 36,950 thousand) relates to Customer loans and receivables.

15 Other receivables

	2013 HRK '000	2012 HRK '000
Net receivables for prepaid VAT	-	13,241
Receivables from employees	1,622	336
Accrued interest receivable	553	671
Other receivables	1,540	921
	3,715	15,169

16 Financial assets at fair value through profit or loss

	2013 HRK '000	2012 HRK '000
Financial assets at fair value through profit or loss		
- Debt securities, Ministry of Finance	4,129	14,195
- Equity securities	402	402
- Investment in open-ended investment funds	105,314	130,768
	109,845	145,365

17 Cash and cash equivalents

	2013 HRK '000	2012 HRK '000
Cash and demand deposits	220,387	301,116
Term deposits originated by the Group, with original maturity up to 3 months	190,941	210,523
	411,328	511,639

18 Equity

(a) Share capital

As at 31 December 2013, the share capital of the Group is represented by 1,331,650 (2012: 1,331,650) of authorised, issued and fully paid ordinary shares, with a total registered value of HRK 133,165 thousand (2012: HRK 133,165 thousand). The nominal value of one share is HRK 100 (2012: HRK 100). The holders of the ordinary shares are entitled to receive dividends as declared at the General Assembly and are entitled to one vote per share at the General Assembly.

The Group's shareholders as at 31 December 2013 are:

	2013	2013	2012	2012
	Number of shares	**% held**	**Number of shares**	**% held**
Telefonaktiebolaget LM Ericsson	653,473	49.07	653,473	49.07
Small shareholders	673,369	50.57	674,769	50.67
Treasury shares	4,808	0.36	3,408	0.26
	1,331,650	100.00	1,331,650	100.00

(b) Treasury shares

These shares are initially held as "treasury shares" and are regularly granted to key management and other employees as a part of the share-based program established during 2004, as described in Note 21 (b). During 2013, the Group acquired 4,000 (2012: 2,376) of its own shares, for a total amount of HRK 5,754 thousand (2012: HRK 2,462 thousand), paid from the 2008 net income as decided by the General Assembly held on 26 May 2009.

Movements in treasury shares are as follows:

	2013 Number of shares	2012 Number of shares
As at 1 January (Note 18 (a))	3,408	4,237
Purchased during the year	4,000	2,376
Distributed during the year	(2,600)	(3,205)
As at 31 December (Note 18 (a))	4,808	3,408

(c) Legal reserves

A legal reserve in the amount of 5% of total share capital was formed during previous periods by appropriation of 5% of net profit per annum up to a cap of 5% of share capital. The legal reserve may be used to cover losses if the losses are not covered by current net profit or if other reserves are not available. The Group recorded the required level of legal reserves in 2000 and no further allocation to legal reserves is required. Legal reserves up to 5% of total share capital are not distributable. During 2013, the Group released legal reserves of HRK 13,452 thousand representing reserves in excess of the prescribed 5% of share capital.

19 Proposed dividends

Dividends payable are not accounted for until they have been ratified at the General Assembly of shareholders. On 28 May 2013, the General Assembly approved a regular dividend in respect of 2012 of HRK 20.00 per share, and additional extraordinary dividend of HRK 150.00 per share, totaling HRK 225.9 million. At a meeting held on 11 March 2014, the Management Board proposed a regular dividend in respect of 2013 in the amount of HRK 20.00 per share, and an additional extraordinary dividend of HRK 300.00 per share. The dividend will be paid from the reserve formed from legal reserves in excess of the prescribed 5% of share capital (Note 18 (c)), and from the profit for 2004, 2010, 2011 and 2012 plus a portion of retained earnings realized in 2013 after approval by the General Assembly, which will be held on 27 May 2014.

Cash dividends authorised and paid for previous years were as follows:

	2013	2012
	HRK ‘000	HRK ‘000
HRK 170.00 per share for 2012	225,851	-
HRK 170.00 per share for 2011	-	225,695

20 Capital management

The Group’s objectives when managing capital are:

- To safeguard the entity's ability to continue as a going concern, so that it can continue to provide returns for shareholders and benefits for other stakeholders;
- To provide adequate requirements for capital resources, as far as possible, by the retention of profit; and
- To maintain the balance sheet with a large component of cash and short-term assets, as well as equity and other investments.

The Group is generating sufficient cash from operations to fund liabilities as they become due, finance customers and budgeted investments, and pay dividends.

The Group monitors capital using the statutory minimum capital requirement. Shareholders’ equity is disclosed in Note 18 to the consolidated financial statements.

21 Employee benefits

(a) Long-term service benefits

The Group does not operate any pension schemes or other retirement benefit schemes for the benefit of any of its employees or management. In respect of all of the Group's personnel, such social payments as required by the authorities are paid. These contributions form the basis of social benefits payable out of the Croatian Pension Insurance Institute to the Croatian employees upon their retirement. Additionally, during 2001 the parent Company signed an Annex to the Union Agreement based on which employees are entitled to a benefit upon early retirement.

However, the parent Company pays a one-time benefit amounting to HRK 8,000 for each employee who retires. Additionally, the Company pays jubilee awards in respect of each 5 years of service, of an employee, starting from the 10th year and ending in the 40th year. The principal actuarial assumptions used to determine retirement and jubilee obligations as at 31 December 2013 were a 6% discount rate (2012: 6%) and a 3,4% (2012: 3.1%) rate of average employment turnover.

Movements in long-term service benefits were as follows:

	2013	2013	2013	2012	2012	2012
	Jubilee awards	Retirement	Total	Jubilee awards	Retirement	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
As at 1 January	4,059	393	4,452	4,128	402	4,530
Obligation created during the year	560	62	622	300	56	356
Obligation fulfilled during the year	(242)	(40)	(282)	(300)	-	(300)
Obligation reversed during the year	-	(95)	(95)	(69)	(65)	(134)
As at 31 December	4,377	320	4,697	4,059	393	4,452

(b) Share-based payments

During 2004, the parent Company established its Loyalty program, a share-based scheme under which management and other employees are entitled to receive the Company's shares conditional on the employee completing certain years of service (the vesting period) from the grant date.

In addition, the parent Company also grants treasury shares to senior management and other employees as a bonus arrangement under its Award program.

The treasury shares are distributed to eligible employees upon ratification at the General Assembly.

21 Employee benefits (continued)

(b) Share-based payments (continued)

The terms and conditions of the grants are as follows:

Employees entitled/grant date	Number of granted shares	Vesting conditions
Loyalty program		
Share grant to key management in previous years (2004 – 2010)	1,140	Three to five years of service
Share grant to other employees in previous years (2004 – 2010)	14,945	Three to five years of service
Share grant to key management during 2011	550	Three to four years of service
Share grant to other employees during 2011	6,650	Three to four years of service
Share grant to key management during 2012	290	Up to four years of service
Share grant to other employees during 2012	80	Up to four years of service
Share grant to key management during 2013	1,040	Up to four years of service
Share grant to other employees during 2013	9,165	Up to four years of service
	33,860	
Award program		
Share grant to key management in previous years (2004 – 2010)	8,592	Upon granting
Share grant to other employees in previous years (2004 – 2010)	8,746	Upon granting
Share grant to key management during 2011	333	Upon granting
Share grant to other employees during 2011	908	Upon granting
Share grant to key management during 2012	-	Upon granting
Share grant to other employees during 2012	70	Upon granting
Share grant to key management during 2013	40	Upon granting
Share grant to other employees during 2013	900	Upon granting
	19,589	

21 Employee benefits (continued)

The fair value of service received in return for shares granted is measured by reference to the observable market price of shares at the grant date.

	Number of granted shares	**Weighted average fair value per share**
		HRK
Shares granted in 2004	11,415	656.68
Shares granted in 2005	(125)	735.99
Shares granted in 2006	5,775	2,330.18
Shares granted in 2007	5,594	3,387.12
Shares granted in 2008	6,452	1,380.27
Shares granted in 2009	2,937	1,320.34
Shares granted in 2010	1,375	1,382.73
Shares granted in 2011	8,441	1,160.00
Shares granted in 2012	440	1,020.46
Shares granted in 2013	11,145	1,443.39

During 2013, the Group recognised HRK 3,645 thousand (2012: HRK 5,257 thousand) of expenses in respect of share-based payments, which are included in personnel expenses as disclosed in Note 6. During 2013, there were new Loyalty programs. The Award program for 2013 included "the length of service with the Group component" and the shares granted under this program were distributed during 2013. Shares granted under previous programs to employees who left the Group before vesting date expired.

2,600 of shares granted under the Loyalty programs from previous years vested during 2013. The total weighted average cost of shares exercised during 2013 under the Award and Loyalty programs amounted to HRK 3,111 thousand (2012: HRK 3,977 thousand).

Movements in shares under the Award and Loyalty programs are as follows:

	2013 Number of shares	**2012 Number of shares**
As at 1 January	6,070	9,220
Granted	11,145	440
Exercised	(2,600)	(3,205)
Expired	(105)	(385)
As at 31 December	14,510	6,070

22 Trade and other payables

	2013 HRK '000	2012 HRK '000
Trade payables	55,175	34,076
Liabilities to employees	73,803	76,526
Other current liabilities	19,448	13,013
	148,426	123,615

23 Provisions

Movements in provisions were as follows:

	2013 Warranty reserve	2013 Penalty reserve	2013 Voluntary redundancy	2013 Total	2012 Warranty reserve	2012 Penalty reserve	2012 Voluntary redundancy	2012 Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK'000	HRK '000
As at 1 January	9,342	7,719	1,505	18,566	8,131	11,000	2,837	21,968
Additional provisions	1,682	2,543	960	5,185	4,431	940	11,939	17,310
Unused provisions reversed	(7)	-	-	(7)	(251)	(221)	-	(472)
Provisions used during the year	(4,510)	(4,300)	(1,476)	(10,286)	(2,969)	(4,000)	(13,271)	(20,240)
As at 31 December	6,507	5,962	989	13,458	9,342	7,719	1,505	18,566

The warranty reserve is established to cover the expected warranty claims on products sold during the year. The penalty reserve is created to cover the expected claims from customers in respect of delays in deliveries of products and services having occurred during the year. Reversal of warranty reserves relates to expired warranties and reversal of penalty reserve relates to waived or expired obligations.

An agreement was reached with the local union representatives, which specifies the number of staff involved and the early retirement compensation package offered by the parent Company, as well as amounts payable to those having accepted the package, before the financial year-end.

24 Accrued charges and deferred revenue

	2013	2012
	HRK '000	HRK '000
Advances from domestic customers	6,432	2,493
Advances from foreign customers	4,958	8,475
Deferred revenue	90,098	89,187
Accrued charges for unused holidays	12,830	10,945
Accrued charges for legal claims	801	971
Accrued charges in respect of service contracts	23,544	32,246
Other accrued charges	10,396	6,575
	149,059	150,892

Deferred revenue represents amounts due to customers under contracts for work not performed but invoices issued or cash received.

Accrued charges in respect of service contracts mainly represent costs incurred for which no invoice has been received at the balance sheet date.

25 Balances and transactions with related parties

For the purposes of these consolidated financial statements, parties are generally considered to be related if one party has the ability to control the other party, is under common control, or can exercise significant influence over the other party in making financial and operational decisions. In considering each possible related party relationship, attention is directed to the substance of the relationship, not merely the legal form.

The Group is a related party to the Ericsson Group via the 49.07% (2012: 49.07%) shareholding by Telefonaktiebolaget LM Ericsson, which is also the ultimate parent of the Ericsson Group.

The Group has related-party relationships with Telefonaktiebolaget LM Ericsson, Ericsson Group subsidiaries and associates, the Supervisory Board, the Management Board and other executive management.

(a) Key transactions with the related parties

Major transactions with the Ericsson Group companies may be summarised as follows:

	Telefonaktiebolaget LM Ericsson		Other Ericsson Group consolidated companies		Total	
	2013 HRK ‘000	2012 HRK ‘000	2013 HRK ’000	2012 HRK ’000	2013 HRK ’000	2012 HRK ’000
Sales of goods and services						
Sales revenue	-	74	568,749	551,924	568,749	551,998
Commission income	-	-	-	25	-	25
Other income	-	-	7,630	15,094	7,630	15,094
	-	74	576,379	567,043	576,379	567,117
Purchases of goods and services						
Licences	3,805	6,623	64,704	36,915	68,509	43,538
Technical cooperation fee	-	-	1,958	5,654	1,958	5,654
Cost of sales	-	-	407,216	1,039,087	407,216	1,039,087
	3,805	6,623	473,878	1,081,656	477,683	1,088,279

The sales of goods and services transactions have been directly negotiated between the involved parties and agreed on an individual basis. The Group pays licence fees on sales of wireline products, sales of services, corporate trade mark licences and technical cooperation fees. The licence fee is paid as a percentage of sales of wireline products and solutions, and sales of services, per product sold.

25 Balances and transactions with related parties (continued)

(b) Key management compensation

The Group's key management include the executive management listed on page 3, comprising the Management Board member and directors of the main organisational units.

	2013 HRK '000	2012 HRK '000
Salaries and other short-term employee benefits	21,308	16,315
Other long-term benefits	2	14
Share-based payments	121	577
	21,431	16,906

The members of the executive management and the Supervisory Board held 4,085 ordinary shares at the year-end (2012: 4,024 shares).

In addition, the Group paid remuneration totaling HRK 315 thousand (2012: HRK 321 thousand) to the Supervisory Board during 2013.

(c) Year-end balances arising from sales and purchases of goods and services

Year-end balances arising from key transactions with Ericsson Group companies may be summarised as follows:

	Receivable		Payable	
	2013 HRK '000	2012 HRK '000	2013 HRK '000	2012 HRK '000
Main shareholder				
Telefonaktiebolaget LM Ericsson (LME)	1,342	37	-	4,119
Ericsson Group consolidated companies				
Ericsson AB (EAB)	50,870	54,682	57,635	106,818
Ericsson GMBH Group (EDD)	3,773	4,874	1,575	583
Ericsson Maroc Sarl (EMO)	2,884	213	-	-
Ericsson Telecom S.S.De C.V.(TEM)	954	7	-	-
Ericsson A/S (ETO)	838	-	-	-
Ericsson Egypt Ltd. (EEL)	748	317	-	-
Ericsson Hungary Ltd. (ETH)	699	265	302	209
Ericsson Slovakia Spol.S.R.O. (SBB)	688	341	-	-
Ericsson Technical Office UAE (TKU)	678	-	-	-
Ericsson AB-Saudi Arabia Branch (BSA)	503	78		
Ericsson AG (EAS)	375	520	-	-
LM Ericsson Ltd. (LMI)	1,171	1,537	615	1,035
Ericsson d.o.o. (EVN)	1,069	1,453	-	-
Ericsson Ltd. Madrid, Spain (ETL)	527	2,461	-	-
Ericsson Corporation, Russia (ECR)	1,064	1,849	-	96
Ericsson Telecommunicatia B.V. (ETM)	812	1,429	600	1,120
Ericsson SP Z.O.O. (EPO)	429	1,203	-	-
Other Ericsson Group companies	2,394	9,924	209	1,710
	71,818	81,190	60,936	115,690

26 Financial risk management

The Group's activities expose it to a variety of financial risks: market risk (including currency risk, interest rate risk, and price risk), credit risk and liquidity risk. Exposure to currency, interest rate and credit risk arises in the normal course of the Group's business. Risk management is carried out by a treasury department and its principal role is to actively manage investment of excess liquidity as well as financial assets and liabilities, and to manage and control financial risk exposures. The Group also has a customer finance function with the main objective to find suitable third-party financing solutions for customers and to minimize recourse to the Group. Risk management policies that relate to financial instruments can be summarised as follows:

(a) Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Group is exposed to US dollars and to the euro, as a substantial proportion of receivables and foreign revenues are denominated in these currencies. Risk management relies on attempts to match, as much as possible, revenues in each currency with the same currency expenditure. The Group may enter into foreign currency forward contracts to hedge economically its exposure to currency risk arising on operating cash flows.

As at 31 December 2013, if the euro had weakened/strengthened by 0.93% (2012: 1.56%) against the Croatian kuna, and if the US dollar had weakened/strengthened by 3.49% (2012: 2.23%), with all other variables held constant, the net result after tax for the reporting period would have been HRK 4,032 thousand lower/higher (2012: HRK 10,801 thousand), mainly as a result of foreign exchange gains/losses on translation of significant cash, cash equivalents, deposits, customer receivables and customer financing denominated in euro.

26 Financial risk management (continued)

(a) Currency risk (continued)

The tables below present the currency analysis and resulting gap.

2013

	EUR	USD	Other currency	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	15,594	2,463	-	18,057	744	18,801
Trade and other receivables	190,242	13,230	4,694	208,166	113,520	321,686
Financial assets at fair value through profit or loss	-	-	-	-	109,845	109,845
Cash and cash equivalents	359,314	2,250	6,511	368,075	43,253	411,328
	565,150	**17,943**	**11,205**	**594,298**	**267,362**	**861,660**
Interest-bearing borrowings*	10	-	-	10	376	386
Trade and other payables	73,347	3,723	734	77,804	131,558	209,362
	73,357	**3,723**	**734**	**77,814**	**131,934**	**209,748**
Currency gap	**491,793**	**14,220**	**10,471**	**516,484**	**135,428**	**651,912**

* include interest payable of HRK 9 thousand

2012

	EUR	USD	Other currency	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	22,713	7,306	-	30,019	394	30,413
Trade and other receivables	212,962	11,080	13,860	237,902	86,043	323,945
Financial assets at fair value through profit or loss	-	-	-	-	145,365	145,365
Cash and cash equivalents	462,483	9,333	893	472,709	38,930	511,639
	698,158	**27,719**	**14,753**	**740,630**	**270,732**	**1,011,362**
Interest-bearing borrowings*	1,958	-	-	1,958	-	1,958
Trade and other payables	122,018	3,766	5,512	131,296	108,009	239,305
	123,976	**3,766**	**5,512**	**133,254**	**108,009**	**241,263**
Currency gap	**574,182**	**23,953**	**9,241**	**607,376**	**162,723**	**770,099**

* include interest payable of HRK 248 thousand

26 Financial risk management (continued)

(b) Interest rate risk

Interest rate risk is the risk that the value of a financial instrument will fluctuate due to changes in market interest rates. As the Group mainly has its customer financing at a fixed interest rate and only a small portion of customer financing is affected by possible changes in market interest rates, the risk of fluctuating market interest rates is considered low. The Group also has borrowings and deposits in financial institutions at a variable interest rate, as well as investments in money investment funds that are sensitive to market interest rate movements on short-term deposits and treasury bills.

As at 31 December 2013:

- if the effective EUR interest rate on EUR borrowings had increased/decreased by 0.33% (2012: 0.73%) on an annual level, the net result due to changes in EUR credits and borrowings after tax for the reporting period would have been HRK 0 thousand lower/higher (2012: HRK 10 thousand);

- if the effective EUR interest rate on EUR deposits had increased/decreased by 0.52% (2012: 0.08%) on an annual level, the net result due to changes in EUR deposits after tax for the reporting period would have been HRK 33 thousand higher/lower (2012: HRK 5 thousand);

- if the effective HRK interest rate on HRK deposits had increased/decreased by 0.68% (2012: 0.36%) on an annual level, the net result due to changes in investment funds after tax for the reporting period would have been HRK 576 thousand higher/lower (2012: HRK 374 thousand).

The following table presents the annual average interest rates exposure of financial assets and liabilities.

	2013 Average interest rates	**2012 Average interest rates**
	%	**%**
Loans and receivables	2.16	4.37
Trade and other receivables	0.33	0.51
Financial assets at fair value through profit or loss	0.20	0.46
Cash and cash equivalents	1.63	1.81
Interest-bearing borrowings	5.80	2.19

26 Financial risk management (continued)

(b) Interest rate risk (continued)

The tables below present the interest rate repricing analysis and resulting gap.

2013

	Non-interest-bearing	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total	Fixed interest
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	-	442	9,459	8,900	18,801	7,253
Trade and other receivables	304,787	6,037	1,058	9,804	-	-	321,686	16,898
Financial assets at fair value through profit or loss	105,716	-	-	-	4,129	-	109,845	-
Cash and cash equivalents	-	220,387	190,941	-	-	-	411,328	190,941
	410,503	**226,424**	**191,999**	**10,246**	**13,588**	**8,900**	**861,660**	**215,092**
Interest-bearing borrowings*	-	34	74	142	136	-	386	-
Trade and other payables	209,362	-	-	-	-	-	209,362	-
	209,362	**34**	**74**	**142**	**136**	**-**	**209,748**	**-**
Interest rate gap	**201,141**	**226,390**	**191,925**	**10,104**	**13,452**	**8,900**	**651,912**	**215,092**

* include interest payable of HRK 9 thousand

2012

	Non-interest-bearing	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total	Fixed interest
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	-	383	21,429	8,601	30,413	30,043
Trade and other receivables	300,169	6,907	3,017	13,852	-	-	323,945	10,270
Financial assets at fair value through profit or loss	131,171	-	-	10,082	4,112	-	145,365	14,195
Cash and cash equivalents	186	300,930	210,523	-	-	-	511,639	210,523
	431,526	**307,837**	**213,540**	**24,317**	**25,541**	**8,601**	**1,011,362**	**265,031**
Interest-bearing borrowings*	-	-	-	1,958	-	-	1,958	1,958
Trade and other payables	239,305	-	-	-	-	-	239,305	-
	239,305	**-**	**-**	**1,958**	**-**	**-**	**241,263**	**1,958**
Interest rate gap	**192,221**	**307,837**	**213,540**	**22,359**	**25,541**	**8,601**	**770,099**	**263,073**

* include interest payable of HRK 248 thousand

26 Financial risk management (continued)

(c) Price risk

The Group has some exposure to debt securities price risk in spite of low investments and all classified on the balance sheet at fair value through profit or loss (debt securities and investments funds). All the Group's securities are actively traded on the Zagreb Stock Exchange and movements of CROBEX and CROBIS indices may have an impact on operating results.

The table below shows the impact of increases/decreases of the index on the Group's net profit. The analysis is based on the assumption that the CROBEX index had increased/decreased by 6.91% (2012: 16.63%) and the CROBIS index had increased/decreased by 5.41% (2012: 1.64%). The effect on profit after tax is as follows:

	Impact on post-tax profit	
Index	**2013**	**2012**
	HRK '000	**HRK '000**
CROBEX	22	54
CROBIS	179	186

26 Financial risk management (continued)

(d) Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Significant risk is associated with high level of customer finance receivables.
Namely, the tax liability forecasts for the following years showed that the Group will again be in a position of no income tax liability due to other tax reliefs (existing R&D credits as well as considerable tax loss carried forward), and will not be able to use the already approved tax certificates from previous years for the income tax paid abroad.
The Group has taken further steps in partnership with banks and financial institutions to secure all future significant customer finance risk exposures are managed through these Financial institutions with a significantly reduced level of credit risk exposure.

New customers are only accepted on satisfactory completion of a detailed credit check of the customer and a review of the related country risk. Outstanding credit arrangements are monitored frequently. Impairment losses are calculated by discounting of receivables. Additionally, there is credit concentration risk as the Group has a significant portion of receivables outstanding from a small number of customers. As at 31 December 2013, the five largest customers represent 53% of total net trade receivables (2012: 61%). The Group considers that its maximum exposure to credit risk is reflected in the amount of trade receivables (Notes 12 and 14) and other receivables (Note 15), net of provision for doubtful receivables. Ageing analysis of these receivables is within the maturity analysis table shown further in this note.

Letters of credit are used as a method for securing payments from customers operating in certain markets, in particular in markets with unstable political and/or economic environments. By having banks confirming the letters of credit, the political and commercial credit risk exposures are mitigated.

Prior to the approval of new facilities reported as customer finance, an internal credit risk assessment is conducted in order to assess the credit rating (for political and commercial risk) of each transaction. A reassessment of the credit rating for each customer finance facility is made on a regular basis.

Provisions related to customer finance risk exposures are only made when they are reliably measurable and where, after the financing arrangement has become effective, certain events occur which are expected to have a significant adverse impact on the borrower's ability and/or willingness to service the outstanding debt. These events can be political (normally outside the control of the borrower) or commercial, e.g. the borrower's deteriorating creditworthiness.

Security arrangements for customer finance facilities normally include pledges of equipment and pledges of certain of the borrower's assets. If available, third-party risk coverage may also be arranged. "Third-party risk coverage" means that a financial payment guarantee covering the credit risk has been issued by a bank, an export credit agency or other financial institution. It may also be a credit risk transfer under a so called "sub-participation arrangement" with a bank, whereby the credit risk and the funding is taken care of by the bank for the part covered by the bank. A credit risk cover from a third party may also be issued by an insurance company.

As at 31 December 2013, total outstanding exposure related to customer finance was HRK 23 million (2012: HRK 45 million).

26 Financial risk management (continued)

(d) Credit risk (continued)

The following tables provide an ageing detail of current and overdue amounts in respect of all customer loans and receivables as at 31 December 2013.

Table 1

Payment due date for total customer loans and receivables

	Due balance	Up to 3 months	3 months to 1 year	1 to 3 years	**Total**
2013	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Foreign receivables	35,126	103,806	20,014	6,274	**169,220**
Domestic receivables	12,010	93,207	12,682	-	**117,900**
Receivables from related parties	11,323	60,496	-	-	**71,819**
	58,459	**257,509**	**32,696**	**6,274**	**354,939**
2012					
Foreign receivables	56,880	92,369	26,439	20,900	**196,588**
Domestic receivables	5,906	77,385	3,117	49	**86,457**
Receivables from related parties	7,263	73,927	-	-	**81,190**
	70,049	**243,681**	**29,556**	**20,949**	**364,235**

Table 2

Ageing of total due customer loans and receivables

	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	**Total**
2013	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Foreign receivables	10,220	641	3,924	20,341	**35,126**
Domestic receivables	7,547	1,411	2,168	884	**12,010**
Receivables from related parties	4,468	6,423	432	-	**11,323**
	22,235	**8,475**	**6,524**	**21,225**	**58,459**
2012					
Foreign receivables	32,740	1,165	2,635	20,340	**56,880**
Domestic receivables	4,756	1,150	-	-	**5,906**
Receivables from related parties	4,137	1,514	1,612	-	**7,263**
	41,633	**3,829**	**4,247**	**20,340**	**70,049**

26 Financial risk management (continued)
(d) Credit risk (continued)

Table 3

Payment due date for total customer loans and receivables (in respect of accounts with any portion falling due)

	Due balance	Up to 3 months	3 months to 1 year	1 to 3 years	**Total**
	HRK '000	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
2013					
Foreign receivables	35,126	75,579	10,238	1,388	**122,331**
Domestic receivables	12,010	84,941	11,971	-	**108,922**
Receivables from related parties	11,323	58,197	-	-	**69,520**
	58,459	**218,716**	**22,209**	**1,388**	**300,773**
2012					
Foreign receivables	56,880	75,061	15,522	12,724	**160,187**
Domestic receivables	5,906	27,337	701	-	**33,944**
Receivables from related parties	7,263	72,599	-	-	**79,862**
	70,049	**174,997**	**16,223**	**12,724**	**273,993**

Table 4

Past due but not impaired customer loans and receivables

	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	**Total**
2013	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**	**HRK '000**
Foreign receivables	6,606	641	101	-	**7,348**
Domestic receivables	7,455	136	973	-	**8,564**
Receivables from related parties	747	3,189	2,203	376	**6,515**
	14,808	**3,966**	**3,277**	**376**	**22,427**
2012					
Foreign receivables	25,137	1,144	-	-	**26,281**
Domestic receivables	4,756	1,150	-	-	**5,906**
Receivables from related parties	2,205	3,795	1,062	-	**7,062**
	32,098	**6,089**	**1,062**	**-**	**39,249**

26 Financial risk management (continued)

(d) Credit risk (continued)

As at 31 December 2013, the total balance outstanding in respect of customer loans and receivables was HRK 355 million (2012: HRK 364 million), as disclosed in Table 1, of which HRK 290 million (2012: HRK 343 million) is due for payment within one year. As at 31 December 2013, the amount totaling HRK 58 million (2012: HRK 70 million) was overdue (Table 2), of which HRK 30 million (2012: HRK 45 million) was due within one year.

As at 31 December 2013, total balance outstanding in respect of customer overdue receivables as at 31 December 2013 was HRK 301 million (2012: HRK 274 million) as disclosed in Table 3. Of this total, HRK 241 million (2012: HRK 261 million) was already due or is due for payment within one year.

In the current economic climate, there is increased risk and uncertainty with regard to the ultimate collectability of some of these balances. As at 31 December 2013, impairment allowances totaling HRK 28 million (2012: HRK 41 million) were provided in respect of total customer loans and receivables. As disclosed in Table 4, amounts totaling HRK 22 million (2012: HRK 39 million), were past due but not impaired as at 31 December 2013.

26 Financial risk management (continued)

(e) Liquidity risk

Liquidity risk, also referred to as funding risk, is the risk that an enterprise will encounter difficulty in raising funds to meet commitments associated with financial instruments. As the Group has no significant commitments in financial instruments, the risk lies only in its daily operations. The Group has a strong focus on its cash flow with daily updates on actual development and monthly updated forecasts. The Group's maturity profile demonstrates the strong liquidity position of the Group and therefore the risk is considered low. The table below presents the maturity analysis and resulting gap.

2013	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	442	16,777	1,582	18,801
Trade and other receivables	197,472	92,900	31,314	-	-	321,686
Current financial assets	105,716	-	-	4,129	-	109,845
Cash and cash equivalents	220,015	190,941	372	-	-	411,328
	523,203	**283,841**	**32,128**	**20,906**	**1,582**	**861,660**
Interest-bearing borrowings*	34	74	210	68	-	386
Trade and other payables	146,132	63,230	-	-	-	209,362
	146,166	**63,304**	**210**	**68**	**-**	**209,748**
Maturity gap	**377,037**	**220,537**	**31,918**	**20,838**	**1,582**	**651,912**

* include interest payable of HRK 9 thousand

2012	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	383	28,659	1,371	30,413
Trade and other receivables	195,215	87,846	40,884	-	-	323,945
Current financial assets	131,171	-	10,082	4,112	-	145,365
Cash and cash equivalents	301,116	210,523	-	-	-	511,639
	627,502	**298,369**	**51,349**	**32,771**	**1,371**	**1,011,362**
Interest-bearing borrowings*	-	-	1,958	-	-	1,958
Trade and other payables	142,277	97,012	16	-	-	239,305
	142,277	**97,012**	**1,974**	**-**	**-**	**241,263**
Maturity gap	**485,225**	**201,357**	**49,375**	**32,771**	**1,371**	**770,099**

* include interest payable of HRK 248 thousand

26 Financial risk management (continued)

(f) Fair value estimation

Financial assets at fair value of through profit and loss are carried at fair value at the balance sheet date. The fair value is estimated by reference to their quoted active market price at the balance sheet date which represents Level 1 input (Note 17).

A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service, or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Group is the current bid price. There are no financial assets derived from level 2 inputs which represent different valuation techniques based on observable market data or from level 3 inputs which represent different valuation techniques based on no observable market data.

The Group's principal financial instruments not carried at fair value are cash and cash equivalents, trade receivables, other receivables, non-current loans and receivables, trade and other payables and interest-bearing borrowings. The fair values of financial instruments together with carrying amounts as shown in the balance sheet are as follows:

	Carrying amount 2013 HRK '000	Fair value 2013 HRK '000	Unrecognised gain/(loss) 2013 HRK '000	Carrying amount 2012 HRK '000	Fair value 2012 HRK '000	Unrecognised gain/(loss) 2012 HRK '000
Loans and receivables	18,801	18,874	73	30,413	30,045	(368)
Trade and other receivables	321,686	321,040	(646)	323,945	323,716	(229)
Financial assets at fair value through profit or loss	109,845	109,845	-	145,365	145,365	-
Cash and cash equivalents	411,328	411,328	-	511,639	511,639	-
Interest-bearing borrowings	(308)	(301)	7	(1,722)	(1,652)	70
Trade and other payables	(209,362)	(209,362)	-	(239,305)	(239,305)	-
	651,990	651,424	(566)	770,335	769,808	(527)

The fair value of loans and receivables and the fair value of interest-bearing borrowings are calculated based on the Management's best estimate of discounted expected future principal and interest cash flows, using the market-related rate for a similar instrument at the balance sheet date as a discount rate. Fair values and carrying amounts are not significantly different as the loans and receivables were granted at market rates, which were not substantially different from market rates at the end of the reporting year. Current financial assets are stated at fair value that is based on quoted prices at the balance sheet date without any deduction for transaction costs.

The carrying amount of cash and cash equivalents and of bank deposits reflects fair value due to the short-term maturity of these financial instruments. Similarly, the amortised cost carrying amounts of trade receivables and payables with remaining life of less than one year and which are all subject to normal trade credit terms reflect fair values. The following interest rates were used for determining fair values, which are based on available market rates for similar financial instruments:

	2013	2012
Loans and receivables	5.31%	6.98%
Interest-bearing borrowings	8.70%	6.87%

27 Contingent liabilities

In December 1999 the parent Company received notification of a lawsuit brought against it by a number of small shareholders. According to this lawsuit, the Zagreb Commercial Court was required to declare certain decisions of the General Assembly, held on 18 June 1998, null and void. The Company has submitted its response to the Court. In January 2004 the Zagreb Commercial Court published the first instance judgement in which the plaintiffs' requests have been refused. On 2 March 2004 the plaintiffs appealed and the Appeal Court (Croatian High Commercial Court) has still not made a decision on the appeal. The Company's Management Board is of the opinion that no material liabilities for the Company will result from this lawsuit. No developments have occurred since 2005 to the date of these statements.

ANNUAL BUSINESS REPORT, Gordana Kovačević, President of Ericsson Nikola Tesla

Dear shareholders,

Our path towards the Networked Society is becoming more dynamic and challenging with each passing day. Now more than ever, Information and Communication Technologies meet our expectations and needs, speed up processes, transform other industries, and thus define new trends in life and work of modern people. Our industry is taking over the leading role in changing familiar patterns, but also the great responsibility for the influence of ICT on the world we live in today, through its revolutionary impact on people, business and environment. It is about a sustainable development and corporate social responsibility that complement our technological leadership with quality.

Ericsson Nikola Tesla contributes significantly to the corporate vision of the Networked Society that is becoming the natural environment to meet the basic human need for communication, always and everywhere, as well as the need to network everything that makes use of it, including 50 billion connected devices, by 2020.

Despite the demanding business climate, negative business and economic trends in 2013, both in Croatia and in the other markets, Ericsson Nikola Tesla achieved excellent business results and strengthened its market position in 2013. We have continued our work on a number of strategic projects and initiatives, relying on our technological leadership, knowledge of our employees and partnership with our customers. Our sales revenues recorded a positive trend in almost all markets, except for the Commonwealth of Independent States, where a significant decrease was recorded YoY. It was an expected situation due to the large contract with Rostelecom that was signed and almost fully realised in 2012. In the local market, telecom operators have continued investing into electronic communications mostly due to transfer to new technologies (IMS, the expansion of 3G network, the introduction of LTE and similar). Thus, we have expanded our market share in Croatia, and achieved an increase in our sales revenues. In Bosnia & Herzegovina we positioned ourselves in the area of transformation systems for Operations Support (OSS), where we expect growth in the years to come. Sales revenue growth was further increased by the introduction of 3G network in Kosovo and by launching the LTE network in Montenegro. We are undertaking repositioning activities in the CIS markets to better adjust to the challenging and dynamic market environment. The activities on the projects of modernisation and building of mobile networks with customers in Georgia and Russia are on-going, as well as the activities on the implementation of a pilot project for the healthcare information system in Armenia, which also includes the building of the central information system for hospitals.

The revenue structure per market has changed YoY, favouring the local market, even though export continues to dominate with 75% share.

In the domestic market, Ericsson Nikola Tesla has continued its strategic cooperation with Vipnet, HT and Tele 2 in the areas of expansion and modernisation of mobile and fixed telecommunication networks and introduction of new services. In the areas of ICT solutions for industry and society segment, our main activities have been on projects upgrading for the national ICT system, relating to healthcare, further informatization of Cadastre and Land Registry, and the upgrade/expansion of the communication infrastructures of utility and transport companies.

In Bosnia & Herzegovina, Montenegro and Kosovo we continued the collaboration with operators BH Telecom, HT Mostar, Montenegro Telecom and IPKO on upgrading and modernization of their networks and introduction of new services.

Throughout 2013, we kept our focus on research and development and other expert activities and the share of these activities even increased equalling 42% of the sales revenues. We have managed to achieve that by expanding our portfolio and responsibilities that we were awarded in the realization of numerous complex projects. Bearing in mind the importance of that segment for the future of the entire company, we will continue to focus on those areas in the period ahead, in order to further increase our competitiveness. It is important to highlight that, with the financial support of EU funds, we have expanded our research on the cloud computing, which is in the strategic focus for further development of telecommunication solutions and services. We continued our work on the project named eWall that was launched to develop a support to senior citizens. The remote patient monitoring system, developed for AT&T, within which Ericsson Nikola Tesla developed its m2m Service Enablement (m2m SE) platform, was commissioned for commercial use.

We have preserved our strong focus on innovations and the corporate culture that encourages employees, and brings excellent results. Our innovation processes and the creativity of our talented employees have been recognized in the global organization, by our customers and beyond in the community, as confirmed by numerous awards and certificates of merit, granted to teams and individuals during last year. It is precisely the innovativeness and our way of working that are sound foundations for future.

As a part of the Company reward and motivation programme, we acquired the additional 4,000 Ericsson Nikola Tesla shares intended for distribution to our employees.

In 2013, Ericsson Nikola Tesla achieved the following consolidated results (the data for 2012 are in brackets):

- ✓ Sales revenue MHRK 1,345.2 (MHRK1,913.3)
- ✓ Net profit MHRK 144.4 (MHRK126.9)
- ✓ Strong cash flow from operating activities MHRK 141.2 (MHRK 297.8)
- ✓ Motivating company culture and strong employee participation, confirmed by the annual opinion survey Dialogue
- ✓ Customer satisfaction, confirmed by the annual customer satisfaction survey

In a nutshell, in 2013 we strengthened our core business, achieved a significant improvement in almost all key performance indicators and employed 160 young professionals, mainly to work on research and development. Compared to last year, which was a very successful one, net profit grew by almost 14 per cent. A strong cash flow from operating activities was also achieved. We continued to invest in strategic projects and customers and partners, in competence development of our employees and we strengthened our market position. We also made important steps in building the leading position in the new strategic focus areas (4GIP, OSS/BSS, TV and media distribution, services, cloud solutions). We have remained focused on profitable growth, efficiency increase, cost reduction, improvements in the working capital and quality risk management.

Last year was the year of continuity in our series of successful business operations. In April 2013 we marked 60 years of excellent collaboration and partnership with Ericsson. We hosted the King and Queen of Sweden, the President of the Republic of Croatia as well as numerous distinguished guests, customers and partners from the country and abroad in our premises. Among them was the important Swedish business delegation headed by the President, and CEO of the Ericsson Group. In our newly built Technology Road, we brought to life the Networked Society concept of future. It was achieved through interesting presentations of applications and solutions for complex infrastructure projects such as e-health, e-call, and e-cadastre and similar, which were all developed by our company experts. Thus, we showed the link between technology and its impact on life, health, safety and work of modern man in a simple and understandable way.

OUTLOOK

Even though the times are challenging, we expect a recovery of ICT industry in our markets. Our optimism is based on the further growth in needs for fast and ultra-fast Internet access, multimedia contents and cloud services. The number of smart mobile user devices (smartphones and tablets) will grow significantly, which will, in turn, increase the data traffic in fixed and mobile networks. With the further implementation of 3G and 3.5G mobile technologies, the broadband access via mobile technologies will also continue to grow significantly, and in Croatia will be achieved by the intensified implementation of LTE technology, too.

The transformation to “all IP” convergent next generation networks has continued. We expect the modernization in Operations Support System (OSS) and Business Support System (BSS), as well as new generations of TV solutions and platforms to enable operators to offer a wide range of convergent services with a focus on enhanced end-user experience.

Given the effects and benefits gained through the development, implementation and use of modern ICT solutions and services, we are ready for faster implementation in the industry and society segments, both in businesses and public administration.

The long-term foundations of our industry remain attractive and, along with our strategic initiatives, we remain well-positioned for further support to our customers in the transforming ICT market.

The business risks that marked the previous period are still present and, for Ericsson Nikola Tesla in 2014, I here note the following:

- ✓ Impact of negative economic trends on demand and prices of our products and services
- ✓ Continued political uncertainty and instability in certain markets
- ✓ Reduction and a slow-down in capital investments of operators and the delays in strategic investments in the public and private sectors
- ✓ Dependence on telecommunication market trends (the number of users, the use of new services)
- ✓ Strong competition from the existing and new competitors, including the IT companies that enter the ICT market
- ✓ Customer and competitor consolidations could additionally affect the pricing of products and services
- ✓ Greater exposure to credit and commercial risks in the event of worsening financial conditions of our buyers
- ✓ Negative impact of exchange rate fluctuations on business results, given that most of our revenue is in Euros and American dollars.

Ericsson Nikola Tesla operates in line with the corporate policies and directives, including Croatian laws and regulations and the principles of corporate governance and business ethics. Ericsson Nikola Tesla’s strategy is aimed at further strengthening its position on the domestic and international markets, at widening of the customer base, gaining of new responsibilities and the delivery of the state-of-the-art solutions, products and services. In doing so, the technological leadership, development of new business models, knowledge acquiring and innovation development, play a key role. ICT industry will continue to be of crucial importance for business development and in the development of society as a whole. The introduction of new devices and applications results in greater user expectations in terms of quality and network features, which increases the demand for our solutions, products and services. That is why our strategic priorities are focused on growth of potential areas, such as mobile broadband Internet access, Operations and Business Support Systems and wide range of services. Having in mind all challenges, we will continue with our permanent adjustments to technology and market conditions, with focus on responsible business practice and risk management. Innovativeness, knowledge and dedication to corporate objectives are key to the results and reputation of Ericsson Nikola Tesla.

All other data, which need to be an integral part of annual company’s report, pursuant to Article 250a of the Company’s Act, can be found in the enclosed 2013 Annual Report, comprising the General Report, Social Report and Consolidated Financial Statements as at 31 December 2013.

Gordana Kovačević

President of Ericsson Nikola Tesla

Zagreb, April 08, 2014

THE REPORT OF THE SUPERVISORY BOARD OF ERICSSON NIKOLA TESLA ON THE SUPERVISION PERFORMED ON THE COMPANY'S OPERATIONS IN 2013

In accordance with the provisions of the Croatian Company Law and Ericsson Nikola Tesla Statute, the Supervisory Board of Ericsson Nikola Tesla has reviewed the Company's operations, making respective decisions in four regular and two extraordinary sessions held during 2013.

The Company Management regularly informed the Supervisory Board on all important business activities and the course of the Company business performance. At the sessions the Supervisory Board reviewed the financial results, business plans, market conditions and ICT industry trends. Further topics of discussions were as follows: investment management, business risks strategic projects and issues relating to human resources. The Supervisory Board continuously monitored the business development and responsibilities of the Research & Development Centre, Operations & Competence Center, Engagement Practices and IT & Test Environment (ITTE) Croatia.
The Company management determined the key objectives for 2013, explicitly defining tasks and ways of measurements and the Supervisory Board approved them, correspondingly. The Supervisory Board analyzed and approved the Company's Business Strategy 2014–2016, as well as focus areas, strategic priorities and key deals necessary for further business development. At extraordinary Board meetings, the members discussed dividend payment and annual financial reports.

Ericsson Nikola Tesla is a dynamic company, operating in an exciting market environment with good long-term perspectives. During 2013, the company maintained its good market position and achieved solid financial performance.

During 2013 there was no change in the Supervisory Board composition.

The Audit Committee held four sessions in 2013. During these sessions, the Audit Committee discussed financial performance during the year, the annual financial statements, 2013 audit plan, audit findings, internal control and risk management system and performed other tasks defined by the Audit Law. The Audit Committee regularly informed other Supervisory Board members of its findings and recommendations. On the day of this report issuance, the Audit Committee is comprised of Mr. Ignac Lovrek, Chairman and Mrs. Carita Jönsson, Member.

ERICSSON

Zagreb, April 08, 2014

Based on the review of financial and other relevant business documents, the Managing Director's report and the reports provided by auditors, the Supervisory Board concluded the following:

- To the best of our knowledge Ericsson Nikola Tesla in all material aspects operates in compliance with the laws and Company's enactments and in accordance with the decisions made by the Annual General Meeting.
- The annual financial statements of the Company and the annual consolidated financial statements of the Company and its subsidiaries (the "Group") have been prepared in accordance with the business records of the Company's and its subsidiaries and in all material respects reflect the correct financial and business situation;
- The Managing Director's proposal relating to net income (profit) allocation is supported and approved;
- There are no objections regarding the Managing Director's report and consequently the report is approved;
- There are no objections regarding the Auditors' reports and consequently the reports are approved;
- Pursuant to the above stated, the submitted annual financial statements are approved.

Pursuant to the Company Act, art. 300d the following documents are enclosed with this report:

1. Decision by the Managing Director on the established consolidated and non-consolidated annual financial statements;
2. Decision by the Supervisory Board on the established consolidated and non-consolidated annual financial statements;

For the Supervisory Board

Roland Nordgren, Chairman

Ericsson Nikola Tesla d.d. Zagreb
Krapinska 45
OIB: 84214771175
Matični br.: 03272699

Zagreb, 08. travnja 2014.

Predmet: **Odluka Nadzornog odbora Društva**

Temeljem članka 300.d Zakona o trgovačkim društvima, Nadzorni odbor dioničkog društva Ericsson Nikola Tesla d.d. Zagreb donosi slijedeće:

- Utvrđuju se godišnja financijska izvješća za 2013.g.
- Utvrđuju se godišnja konsolidirana financijska izvješća Društva i njegovih podružnica („Grupa") za 2013. godinu.

Ericsson Nikola Tesla d.d. Zagreb
Za Nadzorni odbor

Roland Nordgren
Predsjednik

Subject: **Supervisory Board Decision**

Pursuant to the Company Act, Article 300.d the Supervisory Board of the Joint Stock Company Ericsson Nikola Tesla d.d. Zagreb, hereby confirms that:

- The Annual Financial Reports for 2013 have been submitted and approved.
- The Annual Consolidated Financial Statements of the Company and its subsidiaries (the "Group") for 2013 have been approved.

Ericsson Nikola Tesla d.d. Zagreb
For Supervisory Board

Roland Nordgren
Chairman

Ericsson Nikola Tesla d.d. Zagreb
Krapinska 45
OIB: 84214771175
Matični br.: 03272699

Zagreb, 08. travnja 2014.

Predmet: **Odluka Uprave Društva**

Temeljem članka 300.d Zakona o trgovačkim društvima, a nakon primitka suglasnosti Nadzornog odbora dioničkog društva Ericsson Nikola Tesla d.d. Zagreb donosim slijedeću ODLUKU:

- Utvrđuju se godišnja financijska izvješća za 2013.g.
- Utvrđuju se godišnja konsolidirana financijska izvješća Društva i njegovih podružnica („Grupa") za 2013.g.

Ericsson Nikola Tesla d.d. Zagreb
Uprava

Gordana Kovačević

ERICSSON
Ericsson Nikola Tesla d.d.
Krapinska 45
HR-10 000 Zagreb
CROATIA 01

Subject: **Managing Director Decision**

In accordance with the Company Act, Article 300.d and subsequent to the approval of the Supervisory Board of the Joint Stock Company Ericsson Nikola Tesla d.d. Zagreb, I herewith forward the following DECISION:

- The Annual Financial Reports for 2013 have been submitted and approved.
- The Annual Consolidated Financial Statements of the Company and its subsidiaries (the "Group") for 2013 have been submitted and approved.

Ericsson Nikola Tesla d.d. Zagreb
Managing Director

Gordana Kovačević

ERICSSON
Ericsson Nikola Tesla d.d
Krapinska 45
HR-10 000 Zagreb
CROATIA 01