KONČAR– ELECTRICAL INDUSTRY INC.

ANNUAL REPORT AND INDEPENDENT AUDITOR'S REPORT
31 DECEMBER 2017

Contents

Končar– Electrical Industry Inc.

Responsibility for the Annual report

Pursuant to the Croatian Accounting Act, the Management Board is responsible for ensuring that financial statements are prepared for each financial year in accordance with International Financial Reporting Standards as adopted in the European Union, which give a true and fair view of the financial position and results of Končar – Electrical Industry Inc., Zagreb (hereinafter: the Company) for that period.

The Management Board has a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Therefore, the Management Board continues to adopt the going concern basis in preparing the separate financial statements.

In preparing those financial statements, the responsibilities of the Management Board include ensuring that:

- suitable accounting policies are selected and then applied consistently;
- judgements and estimates are reasonable and prudent;
- applicable accounting standards are followed, subject to any material departures disclosed and explained in the financial statements; and
- the financial statements are prepared on a going concern basis unless this assumption is inappropriate.

The Management Board is responsible for keeping proper accounting records, which disclose with reasonable accuracy at any time the financial position of the Company and their compliance with the Croatian Accounting Act. The Management Board is also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Moreover, in accordance with the Accounting Act, the Management Board is obliged to prepare an Annual Report comprising the financial statements, Management Report and the Corporate Governance Statement. The Management Report was prepared in line with the requirements of Article 21 of the Accounting Act, and the Corporate Governance Statement in line with the requirements of Article 22 of the Accounting Act.

The Annual Report was authorised for issuance by the Management Board on 3 April 2018.

Signed on behalf of the Management Board:

Darinko Bago,
President of the Management Board

Miki Huljić,
Member of the Management Board

Marina Kralj Miliša,
Member of the Management Board

Davor Mladina,
Member of the Management Board

Miroslav Poljak,
Member of the Management Board

Končar-Electrical Industry Inc, Zagreb
Fallerovo šetalište 22,
10 000 Zagreb

»KONČAR« d.d. ZAGREB
FALLEROVO ŠETALIŠTE 22
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Independent Auditor's Report

To the Shareholders and Management Board of Končar - Electrical Industry Inc.:

Report on the audit of the separate financial statements

Our opinion

In our opinion, the separate financial statements give a true and fair view of the financial position of Končar - Electrical Industry Inc. (the "Company") as at 31 December 2017, and its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRS").

Our opinion is consistent with our additional report to the Audit Committee.

What we have audited

The Company's separate financial statements comprise:

- the statement of financial position as at 31 December 2017;
- the statement of comprehensive income for the year then ended;
- the statement of changes in equity for the year then ended;
- the statement of cash flows for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (ISAs). Our responsibilities under those standards are further described in the *Auditor's Responsibilities for the Audit of the Separate Financial Statements* section of our report.

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

Independence

We are independent of the Company in accordance with the International Ethics Standards Board for Accountants' Code of Ethics for Professional Accountants (IESBA Code). We have fulfilled our other ethical responsibilities in accordance with the IESBA Code.

To the best of our knowledge and belief, we declare that non-audit services that we have provided to the Company are in accordance with the applicable law and regulations in the Republic of Croatia and that we have not provided non-audit services that are prohibited under Article 5(1) of Regulation (EU) No. 537/2014.

The non-audit services that we have provided to the Company, in the period from 1 January 2017 to 31 December 2017, are disclosed in Note 1 to the separate financial statements.

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Commercial Court in Zagreb, no. Tt-99/7257-2, Reg. No.: 080238978; Company ID No.: 81744835353; Founding capital: HRK 1,810,000.00, paid in full; Management Board: J. M. Gasparac, President; S. Dusic, Member; T. Macasovic, Member; Giro account: Raiffeisenbank Austria d.d., Petrinjska 59, Zagreb, IBAN: HR8124840081105514875.

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Our audit approach

Overview

Materiality	• Overall materiality for the separate financial statements as a whole: HRK 3,400 thousand, which represents 5% of profit before tax from continued operations
Key audit matters	• Valuation and impairment of investments in subsidiaries • Valuation, classification and impairment of property

How we tailored our audit scope

We designed our audit by determining materiality and assessing the risks of material misstatement in the separate financial statements. In particular, we considered where management made subjective judgements; for example, in respect of significant accounting estimates that involved making assumptions and considering future events that are inherently uncertain. We also addressed the risk of management override of internal controls, including among other matters consideration of whether there was evidence of bias that represented a risk of material misstatement due to fraud.

We tailored the scope of our audit in order to perform sufficient work to enable us to provide an opinion on the separate financial statements as a whole, taking into account the structure of the Company, the accounting processes and controls, and the industry in which the Company operates.

Materiality

The scope of our audit was influenced by our application of materiality. An audit is designed to obtain reasonable assurance whether the separate financial statements are free from material misstatement. Misstatements may arise due to fraud or error. They are considered material if individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the separate financial statements.

Based on our professional judgement, we determined certain quantitative thresholds for materiality, including the overall materiality for the separate financial statements as a whole as set out in the table below. These, together with qualitative considerations, helped us to determine the scope of our audit and the nature, timing and extent of our audit procedures and to evaluate the effect of misstatements, if any, both individually and in aggregate on the separate financial statements as a whole.

Overall materiality for the separate financial statements as a whole	HRK 3,400 thousand
How we determined it	5% of profit before tax from continued operations
Rationale for the materiality benchmark applied	We chose profit before tax as the benchmark because, in our view, it is the benchmark which best reflects the Company's performance in the period under review. We selected 5%, which is within the range of commonly acceptable quantitative materiality thresholds in this sector.

Key audit matters

Key audit matters are those matters that, in our professional judgement, were of most significance in our audit of the separate financial statements of the current period. These matters were addressed in the context of our audit of the separate financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters.

Key audit matters	How our audit addressed the key audit matter
Valuation and impairment of investments in subsidiaries See Note 2 to the financial statements under heading "Investments in subsidiaries and associates" (accounting policies), Note 3 (Critical accounting estimates) and Notes 12 and 18 An impairment review of investments in subsidiaries is performed when there is an indication that these may be impaired. The Company's Management determines the recoverable amount of investments in subsidiaries at the higher of fair value less cost of disposal and value in use. The recoverable amount is determined using the discounted cash flow model. Refer to Notes 3, 12 and 18 to the financial statements where the impairment of investments in subsidiaries has been discussed. Impairment indicators were identified in three subsidiaries with a net carrying value amounting to HRK 211,056 thousand as at 31 December 2017. In the current year, an impairment loss of HRK 28.2 million was recognised on the basis of performed tests of impairment of investments in subsidiaries. We focused on this area due to the issue of identifying potential impairment indicators in certain subsidiaries (such as losses incurred, performance below budget, liquidity problems) and also due to significant Management judgement and estimates involved in performing the impairment test. We specifically focused on Management judgements and assumptions used in the impairment test models.	We satisfied ourselves as to the management's assumptions used in the impairment model, and identified the most significant assumptions as: - growth rates within medium-term business plans - discount rate - residual value. As indicated in Note 3, the impairment model is the most sensitive to these assumptions. We verified the mathematical accuracy of the cash flow model and inspected the inputs into the model. These inputs were agreed with the supporting documentation such as the approved strategic plan. We held discussions with Management in order to obtain an understanding as to the basis of used assumptions. We agreed the cash flow forecasts to the 2018-2022 approved strategic plan for two companies and the 2018-2035 strategic plan for the third company. We compared current-year actual results with prior-year forecasts as an indication of the quality of the budgeting process. We found the forecasts for the current year to be somewhat above the actual results, but noted that Management made appropriate adjustments to the plans used in the impairment tests. Management used an average growth rate up to 6,8% in its impairment tests based on approved business plans for the next five years. Also, Management assumed a real discount rate in the range from 5% to 8.5% taking into account the rate on risk-free placements and the rate that reflects the risk premium depending on the subsidiary's specifics, its market position and technical capabilities. In determining the residual value, the Management of the Company applied a rate of 3%. We stress-tested the assumptions used by analysing the impact on results from using other discount rates which were within a reasonably foreseeable range. We tested the reasonableness of Management's assumptions by implementing appropriate benchmarking procedures (we challenged the Management's key assumptions for growth rates used in the forecasts and compared them to economic and industry forecasts and discount rate by comparing the cost of capital and comparable organisations). Based on the work performed, we accept the reasonableness of Management's assumptions We checked the completeness and accuracy of impairment loss recognised in accordance with impairment tests performed in the Company's financial statements.

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Key audit matters	How our audit addressed the key audit matter
Valuation, classification and impairment of property See Note 2 to the financial statements under heading “Property, Plant and Equipment” and under heading “Investment property” (accounting policies), Note 3 (Critical accounting estimates) and Notes 16 and 17 The Company recognizes owner-occupied property classified as Property, plant and equipment in the amount of HRK 183,731 thousand and investment property in the amount of HRK 151,294 thousand at the balance sheet date (both measured using the cost method). A part of administrative/production buildings is rented to subsidiaries but not classified as investment property, since Management assessed that the portions could not be sold separately and the portion used for production or administrative purposes is not immaterial. Further, for investment property Management assessed that the residual value of the property exceeds its carrying value on the basis of an annual review performed, and therefore depreciation is not charged until the residual value subsequently decreases to an amount below the property’s carrying value. Management concluded that the recoverable amount of properties exceeds their carrying values and therefore, no impairment loss was recognised. This conclusion depend on significant Management judgement, including in respect of: - Estimated fair value, provided by an independent external valuer; and - Estimated utilisation and disposal values. We focused on this area, given the nature of judgements and estimates used by Management when determining whether there are any indicators of impairment, correct classification and the defining recoverable amounts at the balance sheet date.	We obtained, gained an understanding of and evaluated Management’s accounting policies in relation to the valuation and classification of owner-occupied property and investment property and impairment test models. For property where Management identified certain potential impairment indicators, Management engaged an independent third party valuer in order to determine the recoverable amount of properties (fair value less cost of disposal). We reconciled the property information in the valuation by tracing a sample of inputs to the underlying property records held by the Company (which were also tested during the audit). We also evaluated the competence, qualifications, experience and objectivity of third party property valuation experts. We challenged Management assessments (by inquiry and benchmarking procedures) of recoverable amounts of properties, correct classification and assessment of the residual value of investment property and found they were able to provide explanations and refer to appropriate supporting evidence. We found the assessment made by the Management regarding the existence of potential impairment indicators and recoverable amount of property recognised in the financial statements to be appropriate. We also believe that the disclosures in Notes 3, 16 and 17 are appropriate.

Reporting on other information including the Management Report and Corporate Governance Statement

Management is responsible for the other information. The other information comprises the Company's Annual Report, which includes the Management Report and Corporate Governance Statement, but does not include the separate financial statements and our independent auditor's report thereon.

Our opinion on the separate financial statements does not cover the other information, including the Management Report and Corporate Governance Statement.

In connection with our audit of the separate financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the separate financial statements or our knowledge obtained in the audit, or otherwise appears to be materially misstated.

With respect to the Management Report and Corporate Governance Statement, we also performed procedures required by the Accounting Act in Croatia. Those procedures include considering whether the Management Report includes the disclosures required by Article 21 of the Accounting Act, and whether the Corporate Governance Statement includes the information specified in Article 22 of the Accounting Act.

Based on the work undertaken in the course of our audit, in our opinion:

- the information given in the Management Report and the Corporate Governance Statement for the financial year for which the separate financial statements are prepared is consistent, in all material respects, with the separate financial statements;
- the Management Report has been prepared in accordance with the requirements of Article 21 of the Accounting Act, and
- whether the Corporate Governance Statement includes the information specified in Article 22 of the Accounting Act.

In addition, in light of the knowledge and understanding of the Company and its environment obtained in the course of the audit, we are also required to report if we have identified material misstatements in the Management Report and the Corporate Governance Statement. We have nothing to report in this respect.

Responsibilities of management and those charged with governance for the separate financial statements

Management is responsible for the preparation and fair presentation of the separate 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 financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the separate financial statements, management is responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Company or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Company's financial reporting process.

Auditor's responsibilities for the audit of the separate financial statements

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

As part of an audit in accordance with ISAs, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the separate financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit 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 Company's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Company's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our independent auditor's report to the related disclosures in the separate financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our independent auditor's report. However, future events or conditions may cause the Company to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the separate financial statements, including the disclosures, and whether the separate financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

From the matters communicated with those charged with governance, we determine those matters that were of most significance in the audit of the separate and separate financial statements of the current period and are therefore the key audit matters. We describe these matters in our independent auditor's report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

Report on other legal and regulatory requirements

Appointment

We were first appointed as auditors of the Company on 22 May 2014. Our appointment has been renewed annually by resolution of the General Assembly representing a total period of uninterrupted engagement appointment of 4 years.

The certified auditor engaged as partner on the audit resulting in this independent auditor's report is Kristina Dimitrov.

PricewaterhouseCoopers d.o.o.

PricewaterhouseCoopers d.o.o.
Heinzelova 70, Zagreb
3 April 2018

KONČAR– ELECTRICAL INDUSTRY Inc.

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2017

	Note	**2017 HRK**	**2016 HRK**
Sales	4	50,172,100	53,006,102
Other operating income	5	3,249,078	1,101,581
Operating income		**53,421,178**	**54,107,683**
Cost of materials and energy	6	(5,455,684)	(6,282,202)
Cost of services	7	(34,141,032)	(31,703,809)
Staff costs	8	(21,435,411)	(25,018,220)
Depreciation and amortisation	15,16	(7,817,056)	(7,978,763)
Other expenses	9	(9,382,577)	(8,912,248)
Impairment	10	-	(761,400)
Provisions	11	(1,023,836)	(1,418,592)
Operating expenses		**(79,255,596)**	**(82,075,234)**
Operating loss		**(25,834,418)**	**(27,967,551)**
Dividend income from associates		72,973,704	65,277,916
Finance income		58,455,830	79,229,067
Finance costs		(36,520,673)	(51,771,361)
Finance income – net	12	**94,908,861**	**92,735,622**
Profit before tax		**69,074,443**	**64,768,071**
Income tax	13	-	-
PROFIT FOR THE YEAR		**69,074,443**	**64,768,071**
Other comprehensive income		**-**	**-**
COMPREHENSIVE INCOME FOR THE YEAR		**69,074,443**	**64,768,071**
Earnings per share			
Basic and diluted earnings per share in HRK	14	26.92	25.23

The accompanying notes form an integral part of these financial statements.

KONČAR– ELECTRICAL INDUSTRY Inc.

STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2017

	Note	31 December 2017 HRK	31 December 2016 HRK
ASSETS			
Non-current assets			
Intangible assets	15	1,441,796	1,292,436
Property, plant and equipment	16	206,679,890	219,104,550
Investment property	17	151,294,123	162,443,479
Investments in subsidiaries	18	768,867,586	774,172,584
Investments in associates	19	67,722,257	67,722,257
Loans granted		-	588,000
Financial assets	20	1,226,593	1,256,850
Receivables	21	8,640,398	10,258,538
		1,205,872,643	**1,236,838,694**
Current assets			
Financial assets	26	148,302,705	193,895,302
Receivables from related parties	22	11,155,876	74,252,427
Trade receivables	23	1,052,899	1,070,948
Prepaid corporate income tax		234,894	2,148,093
Other receivables	24	20,053,446	21,306,260
Loans granted to subsidiaries	25	59,075,456	38,775,456
Cash and cash equivalents	27	219,604,159	88,789,740
Prepaid expenses		424,452	527,053
		459,903,887	**420,765,279**
TOTAL ASSETS		**1,665,776,530**	**1,657,603,973**
EQUITY AND LIABILITIES			
Capital and reserves			
Share (registered) capital		1,208,895,930	1,208,895,930
Capital reserves		719,579	719,579
Reserves from profit		359,719,093	325,746,118
Retained earnings		6,248,041	6,248,041
Profit for the year		69,074,443	64,768,071
	28	**1,644,657,086**	**1,606,377,739**
Non-current provisions	29	**3,312,434**	**35,424,953**
Current liabilities			
Liabilities to related parties	30	9,665,210	7,642,113
Trade payables	31	2,425,780	952,148
Other current liabilities	32	5,159,784	6,628,400
Current provisions	29	556,236	578,620
		17,807,010	**15,801,281**
Total liabilities		**21,119,444**	**51,226,234**
TOTAL EQUITY AND LIABILITIES		**1,665,776,530**	**1,657,603,973**

The accompanying notes form an integral part of these financial statements.

KONČAR– ELECTRICAL INDUSTRY Inc.

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2017

	Note	2017 HRK	2016 HRK
Cash flows from operating activities			
Proceeds from trade receivables		25,030,185	27,797,156
Payments to trade payables		(19,379,736)	(13,294,452)
Payments to employees		(23,359,143)	(24,323,251)
Taxes paid		(3,210,494)	-
Other proceeds and payments		(2,512,213)	8,464,070
Cash from operations		**(23,431,401)**	**(1,356,477)**
Interest paid		(503,406)	(4,685)
Net cash flows used in operating activities		**(23,934,807)**	**(1,361,162)**
Cash flows from investing activities			
Proceeds from sale of non-current intangible and tangible assets		2,468,391	1,852,063
Proceeds from sale of equity and debt instruments		2,627,731	6,710,723
Dividends received		185,800,952	98,266,124
Interest received		2,680,335	5,561,400
Deposits released		212,980,705	313,069,111
Purchase of non-current intangible and tangible assets		(11,192,982)	(33,145,891)
Payments for acquisition of equity and debt financial instruments		(22,896,999)	(3,156,068)
Deposits placed		(166,819,359)	(268,240,764)
Loans to related parties		(35,000,000)	(17,900,000)
Repayment of loans by related parties		14,904,879	9,512,719
Net cash flows from investing activities		**185,553,653**	**112,529,417**
Cash flows from financing activities			
Dividends paid		(30,804,427)	(30,810,357)
Net cash used in financing activities		**(30,804,427)**	**(30,810,357)**
Net increase in cash and cash equivalents		**130,814,419**	**80,357,898**
Cash and cash equivalents at beginning of year		88,789,740	8,431,842
Cash and cash equivalents at end of year	27	**219,604,159**	**88,789,740**

The accompanying notes form an integral part of these financial statements.

KONČAR– ELECTRICAL INDUSTRY Inc.

STATEMENT OF CHANGES IN EQUITY

FOR THE YEAR ENDED 31 DECEMBER 2017

	Share capital	Share premium	Reserves from profit	Reserves for treasury shares	Treasury shares	Retained earnings	Profit for the year	Total capital and reserves
	HRK	HRK	HRK	HRK	HRK	HRK	HRK	HRK
At 1 January 2016	**1,208,895,930**	**719,579**	**294,106,743**	**4,143,785**	**(4,143,785)**	**6,248,041**	**62,434,471**	**1,572,404,764**
Profit for the year	-	-	-	-	-	-	64,768,071	64,768,071
Total comprehensive income	**-**	**-**	**-**	**-**	**-**	**-**	***64,768,071***	***64,768,071***
Transactions with owners:								
Transfer to reserves as per annual schedule (Note 28)	-	-	31,639,375	-	-	-	(31,639,375)	-
Dividends paid (Note 28)	-	-	-	-	-	-	(30,795,096)	(30,795,096)
At 31 December 2016	**1,208,895,930**	**719,579**	**325,746,118**	**4,143,785**	**(4,143,785)**	**6,248,041**	**64,768,071**	**1,606,377,739**
Profit for the year	-	-	-	-	-	-	69,074,443	69,074,443
Total comprehensive income	**-**	**-**	**-**	**-**	**-**	**-**	**69,074,443**	**69,074,443**
Transactions with owners:								
Transfer to reserves as per annual schedule (Note 28)	-	-	33,972,975	-	-	-	(33,972,975)	-
Dividends paid (Note 28)	-	-	-	-	-	-	(30,795,096)	(30,795,096)
At 31 December 2017	**1,208,895,930**	**719,579**	**359,719,093**	**4,143,785**	**(4,143,785)**	**6,248,041**	**69,074,443**	**1,644,657,086**

The accompanying notes form an integral part of these financial statements.

1. General information on the Company

Končar-Electrical Industry Inc, Zagreb, Fallerovo šetalište 22, (the Company) is the parent company of the Končar-Electrical Industry Group. As the parent company, it compiles prepares consolidated reports financial statements which are presented and audited separately. These separate financial statements represent the Company as a separate entity. The principal activities of the Company are managing owned subsidiaries and associates.

As at 31 December 2017 and 2016, the Company had 48 employees

The employee structure is as follows:	31 December 2017	31 December 2016
PhD	1	1
Master's degree	5	5
University degree	30	29
College	8	9
Secondary school qualifications	3	3
Primary school + training on the job	1	1
	48	**48**

Members of the Supervisory Board:

Petar Vlaić	President of the Supervisory Board
Josip Lasić	Deputy president of the Supervisory Board
Vicko Ferić	Member of the Supervisory Board
Jasminka Belačić	Member of the Supervisory Board
Vladimir Plečko	Member of the Supervisory Board
Branko Lampl	Member of the Supervisory Board
Joško Miliša	Member of the Supervisory Board
Nikola Anić	Member of the Supervisory Board

Members of the Management Board:

Darinko Bago	President of the Management Board
Marina Kralj Miliša	Member, in charge of legal, general and human resource activities
Davor Mladina	Member, in charge of IT and trade activities
Miroslav Poljak	Member, in charge of corporate development and ICT
Miki Huljić	Member, in charge of finance
Ivan Tomšić	Deputy member, in charge of corporate development and ICT from 5 June 2017
Jozo Miloloža	Member from 5 February 2017, deputy member until 5 August 2017

Compensations paid to members of the Management Board and Supervisory Board are disclosed in Notes 8 and 9 to the financial statements.

In 2017, the auditors of the Company's financial statements have provided services of HRK 327 thousand (2016: HRK 115 thousand). In 2017 and 2016, services mainly relate to costs of the audit and review of financial statements, as well as the audit of financial statements prepared for regulatory purposes. Other services provided by the auditor of the financial statements include accounting seminars and training services.

The financial statements are presented in Croatian kuna (HRK). The stated amounts are rounded to the nearest HRK.

2. Summary of significant accounting policies

The significant accounting policies used for the preparation of these financial statements are presented below. These accounting policies have been consistently applied to all the years presented, unless otherwise stated.

2.1 Basis of preparation

The financial statements of the Company are prepared in accordance with the applicable laws in the Republic of Croatia and with the International Financial Reporting Standards endorsed for use in the European Union.

The financial statements have been prepared on the historical cost basis, except for certain financial instruments that are stated at fair value. The financial statements have been prepared under the accrual principle on a going concern basis.

The preparation of financial statements in conformity with IFRS requires the use of certain critical accounting estimates. It also requires the Management Board to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in Note 3.

The Company's financial statements are presented in Croatian kuna (HRK) as the functional and presentation currency of the Company. As at 31 December 2017, the exchange rate for USD 1 and EUR 1 was HRK 6.27 and HRK 7.51 (31 December 2016: HRK 7.17 and HRK 7.56).

The Company has prepared these separate financial statements in accordance with the Croatian legal regulations. At the date of approval of these separate financial statements, the Company has prepared and approved the related consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) for the Company and its subsidiaries (the "Group") as required by IAS 27.

In the consolidated financial statements, subsidiaries - which are those companies in which the Group, directly or indirectly, has an interest of more than half of the voting rights or otherwise has power to exercise control over the operations - have been fully consolidated.

Users of these separate financial statements should read them with the Group's consolidated financial statements as at and for the year ended 31 December 2017 in order to obtain full information on the financial position, results of operations and changes in the financial position of the Group as a whole. The Group's consolidated financial statements have been published on the official web-site of the Zagreb Stock Exchange.

New and amended standards adopted and effective

The Company has adopted the following new and amended standards for their annual reporting period commencing 1 January 2017 which were endorsed by the European Union and which are relevant for the Company's financial statements:

- *Disclosure Initiative – IAS 7*
- *Recognition of Deferred Tax Assets for Unrealised Losses - IAS 12*

The adoption of these improvements did not have any impact on the current period or any prior period and is not likely to affect future periods.

New standards and interpretations not yet adopted

Certain new standards and interpretations have been published that are not mandatory for 31 December 2017 reporting periods and have not been early adopted by the Company. None of these is expected to have a significant effect on the Company's financial statements, except for the following standards:

IFRS 15 Revenue from contracts with customers and associated amendments to various other standards (effective for annual periods beginning on or after 1 January 2018)

The IASB has issued a new standard for the recognition of revenue. This will replace IAS 18 which covers contracts for goods and services and IAS 11 which covers construction contracts.

The new standard is based on the principle that revenue is recognised when control of a good or service transfers to a customer, so the notion of control replaces the existing notion of risks and rewards.

Key changes to current practice are:

- Any bundled goods or services that are distinct must be separately recognised, and any discounts or rebates on the contract price must generally be allocated to the separate elements.
- Revenue may be recognised earlier than under current standards if the consideration varies for any reasons (such as for incentives, rebates, performance fees, royalties, success of an outcome, etc.) – minimum amounts must be recognised if they are not at a significant risk of reversal.
- The point at which revenue is able to be recognised may shift: some revenue which is currently recognised at a point in time at the end of a contract may have to be recognised over the contract term and vice versa.
- There are new specific rules on licenses, warranties, non-refundable upfront fees and, consignment arrangements, to name a few; and, as with any new standard, there are also increased disclosures.
- As with any standard, there are also increased disclosures.

The Company will have a choice of full retrospective application, or prospective application with additional disclosures.

The Management Board has assessed that there is no impact of applying the new standard to the Company's financial statements.

This standard is mandatory for financial years commencing on or after 1 January 2018, and the Company intends to adopt the standard using the modified retrospective approach.

IFRS 9 Financial instruments and associated amendments to various other standards (effective for annual periods beginning on or after 1 January 2018)

IFRS 9 addresses the classification, measurement and derecognition of financial assets and financial liabilities and introduces new rules for hedge accounting and a new model for impairment of financial assets.

The majority of the Company's debt instruments that are currently classified as available-for-sale will satisfy the conditions for classification as at fair value through other comprehensive income (FVOCI) and hence there will be no change to the accounting for these assets.

The other financial assets held by the Company include:

- equity instruments currently classified as AFS for which a FVOCI election is available
- equity investments currently measured at fair value through profit or loss (FVPL) which will continue to be measured on the same basis under IFRS 9, and

Accordingly, the Company does not expect the new guidance to affect the classification and measurement of these financial assets. However, gains or losses realised on the sale of financial assets at FVOCI will no longer be transferred to profit or loss on sale, but instead reclassified below the line from the FVOCI reserve to retained earnings. During financial year 2017, the Company did not have any such gains.

There will be no impact on the Company's accounting for financial liabilities, as the new requirements only affect the accounting for financial liabilities that are designated at fair value through profit or loss and the Company does not have any such liabilities. The derecognition rules have been transferred from IAS 39 Financial Instruments: Recognition and Measurement have not been changed.

The new impairment model requires the recognition of impairment provisions based on expected credit losses (ECL) rather than only incurred credit losses as is the case under IAS 39. It applies to financial assets classified at amortised cost, debt instruments measured at FVOCI, contract assets under IFRS 15 Revenue from Contracts with Customers, lease receivables. Based on the assessments undertaken to date, the Company expects the impairment loss of financial assets to be 0.4% -0.8% of the value of total financial assets.

The new standard also introduces expanded disclosure requirements and changes in presentation. These are expected to change the nature and extent of the Company's disclosures about its financial instruments particularly in the year of the adoption of the new standard.

This standard is mandatory for financial years commencing on or after 1 January 2018. The Company will apply the new rules retrospectively from 1 January 2018, with the practical expedients permitted under the standard. Comparatives for 2017 will not be restated, except in relation to changes in the fair value of foreign exchange forward contracts attributable to forward points, which will be recognised in the costs of the hedging reserve.

IFRS 16 Leases (issued in January 2016 and effective for annual periods beginning on or after 1 January 2019)

- IFRS 16 will affect primarily lessee accounting and will result in the recognition of almost all leases on the balance sheet. The standard removes the current distinction between operating and financing leases and requires recognition of an asset (the right to use the leased item) and a financial liability to pay rentals for virtually all lease contracts. An optional exemption exists for short-term and low-value leases.
- The income statement will also be affected because the total expense is typically higher in the earlier years of a lease and lower in later years. Additionally, operating expense will be replaced with interest and depreciation, so key metrics like EBITDA will change.
- Operating cash flows will be higher as cash payments for the principal portion of the lease liability are classified within financing activities. Only the part of the payments that reflects interest can continue to be presented as operating cash flows.
- Lessor accounting will not change significantly. Some differences may arise as a result of the new guidance on the definition of a lease. Under IFRS 16, a contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

The standard will affect primarily the accounting for the Company's operating leases. As at the reporting date, the Group has non-cancellable operating lease commitments of HRK 811 thousand, see Note 7. At this stage, the Company is not able to estimate the total impact of the new standard on the Company's financial statements, it will make more detailed assessments of the impact over the next twelve months. The Company plans to adopt this standard on its effective date. The Company intends to apply the simplified transition approach and will not restate comparative amounts for the year prior to first adoption.

Standards, interpretations and amendments issued by the IASB, which have not been adopted by the EU:

IFRIC 23 – Uncertainty over Income Tax Treatments was issued in June 2016 and is effective for annual periods beginning on or after 1 January 2019.

The Interpretation clarifies how to apply the recognition and measurement requirements in IAS 12 when there is uncertainty over income tax treatments. The Company should determine whether to consider each uncertain tax treatment separately or together with one or more other uncertain tax treatments based on which approach better predicts the resolution of the uncertainty. The Company should assume that the Tax Administration will examine amounts it has a right to examine and have full knowledge of all related information when making those examinations. If the Company concludes it is not probable that the Tax Administration will accept an uncertain tax treatment, the effect of uncertainty will be reflected in determining the related taxable profit or loss, tax bases, unused tax losses, unused tax credits or tax rates, by using either the most likely amount or the expected value, depending on which method the entity expects to better predict the resolution of the uncertainty. The Company will reflect the effect of a change in facts and circumstances or of new information that affects the judgements or estimates required by the interpretation as an change in accounting estimate. Examples of changes in facts and circumstances or new information that can result in the reassessment of a judgment or estimate include, but are not limited to, examinations or actions by the Tax Administration, changes in rules established by a taxation authority or the expiry of a taxation authority's right to examine or re-examine a tax treatment. The absence of agreement or disagreement by a taxation authority with a tax treatment, in isolation, is unlikely to constitute a change in fact and circumstances or new information that affects the judgments and estimates required by the interpretation.

The Management Board anticipates that the adoption of the amendments will not have a material effect on the Company's financial statements and plans to adopt the amendments as of their effective date and after being adopted by the European Union.

IFRS 2 Leases Classification and Measurement of Share-based Payment Transactions was issued in June 2016 and is effective for annual periods beginning on or after 1 January 2018.

The amendments to IFRS 2 clarify the measurement basis for cash-settled share-based payments and the accounting for modifications that change an award from cash-settled to equity-settled. They also introduce an exception to the classification principles in IFRS 2. Where an employer is obliged to withhold an amount for the employee's tax obligation associated with a share-based payment and pay that amount to the tax authority, the whole award will be treated as if it was equity-settled provided it would have been equity-settled without the net settlement feature.

Entities with the following arrangements are likely to be affected by these changes:

- equity-settled awards that include net settlement features relating to tax obligations
- cash-settled share-based payments that include performance conditions and cash-settled arrangements that are modified to equity-settled share-based payments

The Management Board anticipates that the adoption of the amendments will not have a material effect on the Company's financial statements and plans to adopt the amendments as of their effective date and after being adopted by the European Union.

Annual improvements 2014 -2016 cycle, issued in December 2016:

- IFRS 1 – First-time Adoption of International Financial Reporting Standards – deleted short-term exemptions covering transition provisions of IFRS 7, IAS 19 and IFRS 10 which are no longer relevant.

- IAS 28 – Investments in Associates and Joint Ventures – clarifies that the election by venture capital organisations, mutual funds, unit trusts and similar entities to measure investments in associates or joint ventures at fair value through profit or loss should be made separately for each associate or joint venture at initial recognition.

The Management Board anticipates that the adoption of the amendments will not have a material effect on the Company's financial statements and plans to adopt the amendments as of their effective date and after being adopted by the European Union.

Transfers of Investment Property – Amendments to IAS 40, issued in December 2016 and effective for annual periods beginning on or after 1 January 2018. The amendments clarify when the Company should transfer assets, including assets under construction or in progress, to or from investment property. The amendments state that a change in use occurs when the property meets, or ceases to meet, the definition of investment property and if this is supported by evidence. The list of evidence for a change of use in the standard was re-characterised as a non-exhaustive list of examples to help illustrate the principle. A change in the Management Board's intentions alone on the use of a property does not provide sufficient evidence of a change in the use of the property.

The Board provided two options for transition:

- prospectively, with any impact from the reclassification recognised as adjustment to opening retained earnings as at the date of initial recognition, or
- retrospectively - only permitted without the use of hindsight.

Additional disclosures are required if an entity adopts the requirements prospectively.

The Company assesses the potential effect of the amendments on its financial statements and plans to adopt the amendments as of their effective date and after being adopted by the European Union.

Amendments to IAS 28 Interests in Associates and Joint Ventures were issued in October 2017 and effective for annual periods beginning on or after 1 January 2019. The amendments clarify that reporting entities should apply IFRS 9 to long-term loans, preference shares and similar instruments that form part of a net investment in an equity method investee before they can reduce such carrying value by a share of loss of the investee that exceeds the amount of investor’s interest in ordinary shares.

The Management Board anticipates that the adoption of the amendments will not have a material effect on the Company's financial statements and plans to adopt the amendments as of their effective date and after being adopted by the European Union.

Annual improvements 2015 – 2017 cycle were issued in December 2017 and are effective for annual periods beginning on or after 1 January 2019, and they include clarifications to the following standards:

- IFRS 3 Business Combinations – the Company remeasures its previously held interest in joint operations when it obtains control.
- IFRS 11 Joint Arrangements – the Company does not remeasure its previously held interest in joint operations when it obtains control.
- IAS 12 Income Taxes – the Company recognises all income tax consequences of dividends where it has recognised the transactions or events that generated the related distributable profits, e.g. in profit or loss or in other comprehensive income. It is now clear that this requirement applies in all circumstances as long as payments on financial instruments classified as equity are distributions of profits, and not only in cases when the tax consequences are a result of different tax rates for distributed and undistributed profits.

- IAS 23 Borrowing Costs – explicit guidance that the borrowings obtained specifically for funding a specified asset are excluded from the pool of general borrowing costs eligible for capitalization only until the specific asset is substantially complete.

The Company will apply the amendments on their effective date and when endorsed by the European Union.

Amendments to IFRS 10 and IAS 28 Investments in Associates and Joint Ventures - In December, the IASB decided to defer the application date of this amendment until such time as the IASB has finalised its research project on the equity method. The amendments clarify the accounting treatment for sales or contribution of assets between an investor and its associates or joint ventures. They confirm that the accounting treatment depends on whether the non-monetary assets sold or contributed to an associate or joint venture constitute a 'business' (as defined in IFRS 3 Business Combinations).

Where the non-monetary assets constitute a business, the investor will recognise the full gain or loss on the sale or contribution of assets. However, any gain or loss (as a result of a sale or non-operational asset) is recognised only to the amount invested by another investor in an associate or a joint venture. The amendments apply prospectively. The Management Board anticipates that the adoption of the amendments will not have a material effect on the Company's financial statements and plans to adopt the amendments as of their effective date and after being adopted by the European Union.

a) Revenue recognition

Revenue comprises the fair value of the consideration received or receivable for the sale of goods and services in the ordinary course of the Company's activities. Revenue is shown net of value added tax, excise tax, estimated returns, rebates and discounts.

Revenue from services is recognized in the accounting period in which the services are rendered, using the percentage of completion method. Revenues from fees and rent charged to related companies are recognized in the period when rendered, on the basis of contracted terms with related companies.

Income from dividends, i.e. shares in profit of subsidiaries and associates, is recognised when the right to receive payment is established, within finance income and costs, Note 12.

b) Finance income and costs

Finance income and costs comprises interest income on loans and borrowings using the effective interest method, interest receivable on funds invested, income from dividends and shares in profit, foreign currency losses and gains, gains and losses of financial assets at fair value through profit or loss.

Foreign exchange gains/losses are recognized in Note 12 in gross amounts (amounts include exchange differences from operations as well from financing activities).

Interest income is recognised in the income statement on an accrual basis using the effective interest rate method.

c) Income tax

The Company calculates taxes in accordance with Croatian law. Income tax for the year comprises current and deferred tax.

Current tax is the expected tax payable on the taxable income for the year, adjusted for amounts which are not included in the tax base or tax deductible expenses. Income tax is calculated by applying tax rates enacted at the balance sheet date.

Deferred income tax is recognised on temporary differences arising between the tax bases of assets and liabilities in the financial statements and the values presented for the purposes of determining the income tax base. A deferred tax asset for the carry-forward of unused tax losses and unused tax credits is recognised to the extent that it is probable that future taxable profit will be realised on the basis of which the deferred tax assets will be utilised. Deferred tax assets and liabilities are calculated using the tax rate applicable to the taxable profit in the years in which these assets or liabilities will be realised.

Current and deferred tax are recognised in the Statement of comprehensive income, except to the extent that it relates to items recognised in other comprehensive income or directly in equity, in which case the tax is also recognised in other comprehensive income or directly in equity, respectively.

d) Earnings per share

The Company presents basic and diluted earnings per share data for its ordinary shares. Basic earnings per share is calculated by dividing the profit or loss attributable to ordinary shareholders of the Company by the weighted average number of ordinary shares outstanding during the period.

Diluted earnings per share is calculated by dividing the profit or loss attributable to ordinary shareholders by weighted average number of ordinary shares outstanding during the period less potential shares which arise from options.

e) Dividend distribution

Dividends are recognised in the statement of changes in equity and recorded as liabilities in the period in which they are approved by the Company's shareholders.

f) Foreign currency transactions

Foreign currency transactions are initially converted into Croatian kuna by applying the exchange rates prevailing on the transaction date. Cash, receivables and liabilities denominated in foreign currencies are re-translated at the rates prevailing on the balance sheet date. Gains and losses arising on translation are included in the income statement for the current year.

g) Non-current intangible assets and property, plant and equipment

Non-current intangible assets and property, plant and equipment are initially carried at cost, which includes the purchase price, including import duties and non-refundable tax after deducting trade discounts and rebates, as well as all other costs directly attributable to bringing the asset to their working condition for their intended use.

Non-current intangible and tangible assets are recognised when it is probable that future economic benefits associated with the item will flow to the Company and the cost of the item can be measured reliably, and when the cost is higher than HRK 3,500.

After initial recognition, assets are measured at cost less accumulated amortisation and depreciation and any accumulated impairment losses.

Maintenance and repairs, replacements and improvements of minor scale lower extent are expensed as incurred. In situations where it can be clearly demonstrated that the expenditures have resulted in an increase in future economic benefits expected to be obtained from the use of an asset beyond its originally assessed standard performance, the expenditures are capitalised i.e. included in the carrying value of the asset. Gains or losses on the retirement or disposal of assets are included in the income statement in the period when incurred.

The amortisation and depreciation of assets commence when the assets are ready for use, i.e. when the assets are at the required location and the conditions necessary for use have been met. Amortisation and depreciation cease when the assets are fully depreciated or when the assets are classified as held for sale. Amortisation and depreciation are charged so as to write off the cost of each asset, other than land, non-current intangible and tangible assets under construction and advances, over their estimated useful lives, using the straight line method, as follows:

	Amortisation and depreciation rates (from – to %)
Intangible assets	20
Buildings	1.2 – 7.7
Equipment	7.5 – 50
Tools, plant inventory and transportation equipment	5.6 - 25
Other tangible assets	20

Impairment of property, plant and equipment

The Company reviews the carrying amount of its property, plant and equipment to determine whether there is any indication of impairment of such assets. If any such indication exists, based on internal and external sources of information, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss.

Where it is not possible to estimate the recoverable amount of the individual asset, the Company estimates the recoverable amount of the cash-generating unit (plant or line to which the asset belongs), and then the loss is allocated to individual assets within the unit.

When determining impairment losses or reversal of impairment losses for an item of property, plant and equipment the depreciation rate is not changed but the useful life of an item is changed. The recoverable amount is determined as the higher of an asset’s fair value less costs of disposal and value in use.

If the amount of tangible assets exceeds the recoverable amount, the difference is charged to the operating result (impairment loss). Prior impairments of non-financial assets are reviewed for possible reversal or decrease at each reporting date.

h) Investment property

Investment property (land, buildings) owned by the Company is held for the purpose of earning rentals or as a potential for issuing guarantees or solidarity guarantees for subsidiaries, and to increase the value of the property with the intention of future sales. Investment property is recognised as a long-term investment, unless it is intended for sale within the next year, in which case it is recognised as a current asset. Investment property is carried at cost less accumulated depreciation. The Company reviews at least annually the residual value and useful life of the property. The residual value is an estimated amount that the Company would gain selling the asset now, after the deduction of the estimated cost of sales, if assumed the asset is close to or at the end of its useful life. Since the Company has estimated that the residual value of the property exceeds its carrying accounting value, depreciation is not charged until the residual value is reduced to the amount below the carrying value.

i) Leases

Leases are classified as finance leases whenever all the risks and rewards of ownership are substantially transferred to the lessee. All other leases are classified as operating leases.

Assets held under finance leases are initially recognised in the lessee's balance sheet as assets or liabilities at the fair value of the leased asset or, if lower, at the present value of the minimum lease payments. The corresponding liability to the lessor is included in the balance sheet as a finance lease obligation.

Lease payments are apportioned between finance costs and a reduction of the lease obligations so as to achieve a constant rate of interest on the remaining balance of the liability. Finance costs are charged directly to profit or loss.

Operating lease payments are recognised in profit or loss as an expense on a straight-line basis over the lease term.

j) Financial assets and financial liabilities

Financial assets

Investments are recognised and derecognised on the trade date where the purchase or sale of a financial asset is under a contract whose terms require the delivery of the investment within the time frame established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as at fair value through profit or loss, which are initially measured at fair value.

Financial assets are classified into the following categories:

- At fair value through profit or loss" (FVTPL) – financial assets either held for trading or designated as at FVTPL at initial recognition. Financial assets at FVTPL are stated at fair value, with any gain or loss arising recognized in profit or loss.
- Held-to-maturity – financial assets with fixed or determinable payments and fixed maturity dates for which there is a positive intent and ability to hold to maturity. Held-to-maturity investments are recorded at amortised cost using the effective interest method less any impairment, with revenue recognised on an effective yield basis.
- Available for sale (AFS) – non-derivative financial assets which are designated as such or they cannot be included in any of the above mentioned categories. AFS is stated at fair value. Changes in fair value are recognised in other comprehensive income, in the investment's revaluation reserve with the exception of impairment losses, interest calculated using the effective interest method and foreign exchange gains and losses on monetary assets, which are recognised directly in profit or loss. Where the financial asset is disposed of or is determined to be impaired, the cumulative gain or loss previously recognised in the other comprehensive income in revaluation reserves from investments, is included in profit or loss for the period.
- Loans and receivables – this category comprises trade receivables, loans, and other receivables with fixed or determinable payments that are not quoted in an active market. Loans and receivables are measured at amortised cost using the effective interest method, less any impairment. Interest income is recognised by applying the effective interest rate, except for current receivables when the recognition of interest would be immaterial.

Impairment of financial assets

Financial assets, other than those at fair value through profit and loss, are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired if there is objective evidence of impairment resulting from one or more events that occurred after the initial recognition of an asset when the event affects the estimated future cash flows from the financial asset.

For unlisted shares classified as AFS a significant or prolonged decline in their fair value below their cost is considered to be objective evidence of impairment.

For all other financial assets, including redeemable notes classified as AFS and finance lease receivables, objective evidence of impairment could include:

- Significant financial difficulty of the issuer or debtor; or
- Default or delinquency in interest or principal payments; or
- It becoming probable that the borrower will enter bankruptcy or financial re-organisation.

Derecognition of financial assets

The Company derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Company neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Company recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Company retains substantially all the risks and rewards of ownership of a transferred financial asset, the Company continues to recognise the financial asset and financial liability for the proceeds received.

When the Company derecognises (writes off) all financial assets, the difference between the carrying value and the sum of received compensations and claims for compensations and cumulative profit (loss), recognised within other comprehensive income, transfers from equity to profit or loss.

Financial liabilities and equity instruments

Debt and equity instruments are classified as either financial liabilities or as equity in accordance with the substance of the contractual arrangement.

An equity instruments is any contract that evidences a residual interest in the assets of an entity after deducting all of its liabilities. Equity instruments issued by the Company are recorded at the proceeds received, net of direct issue costs.

Share capital

Ordinary shares

Share capital represents the nominal value of shares issued.

The share premium includes the premium at the issuance of shares. Transaction costs directly attributable to the issue of ordinary shares are recognised as a deduction from equity.

Reserves are stated at nominal amounts defined in the allocation of earnings, especially legal reserves, statutory reserves and other reserves.

Share capital repurchase

The consideration paid for the repurchase of the Company’s equity share capital, including any directly attributable incremental costs related to the repurchase, is deducted from equity. Repurchased shares are classified as treasury shares and presented as a deduction from total equity. The purchase of treasury shares is recorded at cost, and the sale of treasury shares at the negotiated prices. The gain or loss from the sale of treasury share is recognised directly in equity.

Financial guarantee contract liabilities

Financial guarantee contract liabilities are measured initially at their fair values and are subsequently measured at the higher of:

- the amount of the obligation under the contract, as determined in accordance with IAS 37 Provisions, Contingent Liabilities and Contingent Assets; and
- the amount initially recognised less, where appropriate, cumulative amortisation recognised in accordance with the revenue recognition policies (dividend and interest income).

Financial liabilities at fair value through profit or loss - financial liabilities either held for trading or are classified as such at initial recognition. They are measured at their fair value, while the gains/losses relating to them are recognised in the income statement. The net gain or loss recognised in the income statement includes any interest paid on the financial liability.

Other financial liabilities - they include borrowings that are initially measured at fair value, net of transaction cost. They are subsequently measured at amortised cost using the effective interest method, with an interest expense recognised on an effective yield basis.

The effective interest method is a method of calculating the amortised cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period.

Derecognition of financial liabilities

The Company derecognises financial liabilities when, and only when, they are discharged, cancelled or they expire.

k) Investments in subsidiaries and associates

Subsidiaries are entities in which the Company has control, i.e. when it is exposed to, or has rights to, variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity.

Associates are all entities over which the Company has significant influence but not control, generally accompanying a shareholding of between 20% and 50% of the voting rights.

Investments in subsidiaries and associates are presented using the cost method. If there are indicators of impairment, the recoverable amount of the investment is estimated. The difference between the investment and the recoverable amount is recognised in the statement of comprehensive income as a loss or gain (reversal of the previously recorded loss).

l) Merger

The predecessor method of accounting is used to account for the merger of entities under common control. The carrying value of assets and liabilities of the predecessor entity are transferred as balances in the merged entity. On the date of the merger, inter-company transactions, balances and unrealised gains and losses on transactions between the two entities merging are eliminated, recognising the present value of net assets merged within equity.

m) Receivables

Receivables are initially measured at fair value. At each balance sheet date, receivables, whose collection is expected within a period of more than one year, are stated at amortised cost using the effective interest method, less any impairment loss. Current receivables are initially recognised at their nominal value less corresponding allowances for estimated uncollectible amounts and impairment losses.

The value of receivables 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 an asset when this event affects estimated future cash flows from receivables which can be reliably estimated. Receivables are assessed at each balance sheet date whether there is objective evidence of their impairment. If there is objective evidence of impairment, the impairment loss is measured as the difference between the carrying amount and estimated future cash flows. The carrying value of receivables is reduced either directly or by using a separate allowance account. The impairment loss is recognised as an expense in the Statement of comprehensive income.

n) Cash and cash equivalents

Cash and cash equivalents consist of bank deposits, cash on hand, demand deposits and securities or collectible within 3 months.

o) Trade payables

Trade payables are liabilities to pay for goods or services that have been acquired in the ordinary course of business from suppliers. Trade payable are classified as current liabilities if payment is due within one year or less, or in the regular operating cycle of the business if longer. If not, they are presented as non-current liabilities. Trade payables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method.

p) Borrowings

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

Borrowings are classified as current liabilities, unless the Company has an unconditional right to defer settlement of the liability for at least 12 months after the reporting date.

q) Provisions, contingent liabilities and assets

Provisions are recognised when the Company has a present obligation as a result of a past event; it is more likely than not that an outflow of resources will be required to settle the obligation; and the amount can be reliably estimated. Provisions are reviewed at each balance sheet date and adjusted to reflect the best current estimate.

Provisions are determined for warranties, costs of legal proceedings, termination benefits and awards to employees for long-term employment and retirement.

Provisions for employee benefits for the number of years of service and retirement (regular jubilee awards and termination benefits) are determined as the present value of future cash outflows using a discount rate equal to the interest rate on government bonds.

The newly formed provisions and income from the reversal of provisions are stated on a gross basis (Notes 5 and 11).

Contingent liabilities are not recognised in the financial statements. They are only disclosed in the notes to the financial statements, unless the likelihood of an outflow of economic benefits is small.

Contingent assets are not recognised in the financial statements, except in the case where the realisation of income is certain and the assets in question are not contingent assets and their recognition is appropriate.

r) Employee benefits

(i) Defined pension fund contributions

In the normal course of business through salary deductions, the Company makes payments to mandatory pension funds on behalf of its employees as required by law. All contributions made to the mandatory pension funds are recorded as salary expense when incurred. The Company does not have any other pension scheme and consequently, has no other obligations in respect of employee pensions.

(ii) Long-term employee benefits

The Company has post-employment benefits to be paid to the employees at the end of their employment with the Company (either upon retirement, termination or voluntary departure). The Company recognises a liability for these long-term employee benefits evenly over the period the benefit is earned based on actual years of service. The long-term employee benefit liability is determined using assumptions regarding the likely number of staff to whom the benefit will be payable, the estimated benefit cost and the discount rate.

(iii) Short-term employee benefits - bonuses

A liability for employee benefits is recognised in provisions based on the Company’s formal plan and when past practice has created a valid expectation by the Management Board/key employees that the bonus will be paid and the amount can be determined before the time of issuing the financial statements. Liabilities for bonus plans are expected to be settled within 12 months of the balance sheet date and are recognised at the amounts expected to be paid when they are settled.

(iii) Share-based payments

The Company has a plan for share-based payments to the members of the Management Board which are settled with equity instruments of the Company. The total amount recognised as expense and the relevant increase in share capital are measured by reference to the fair value of the provided equity instruments. The fair value of these equity instruments is measured at the grant date. At each balance sheet date, the Company reviews its estimates of the number of options that are expected to vest and makes necessary adjustments.

s) Events after the balance sheet date (subsequent events)

Events after the balance sheet date, which provide additional information on the Company's position at the balance sheet date (adjusting events), are reflected in the financial statements. Events that are not adjusting events are disclosed in the notes to the financial statements, if material.

3. Critical accounting estimates

Estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under existing circumstances. The Company 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) Residual value of investment property

The Company reviews at least annually the residual value and useful life of the property. The Company has estimated that the residual value of the property exceeds its carrying value, and therefore the depreciation is not charged until the residual value is reduced to the amount below the carrying value.

During 2016 and 2017, for 37% of properties (which comprises 71% of the present carrying value of properties) the Company hired an independent valuer to determine their fair value, and the established values exceeded the value of the properties recorded in the Company's books at the balance sheet date.

b) Impairment tests for investments in subsidiaries

At each reporting date the Company estimates whether impairment indicators exist, which indicate that the investments in subsidiaries could be impaired and estimates the recoverable amount of those investments.

For the purpose of assessing the investments, the DCF method is used which is based on the assumptions that the entity's value represents the present value of its future cash flows. When using the DCF method, the objectivity of calculations mostly depends on the reality of medium-term business plans and the discounted rate used in discounting future cash flows as well as the calculation of the residual value of entities.

Determining the discounted rate depends on the interest rate for risk-free placements (government bonds) and the rate which reflects the risk premium depending on the entity's specifics, market position and technical capabilities.

In 2017 and in 2016, the Company performed impairment tests on investments in subsidiaries. The principal assumptions that may have a significant impact on the determined recoverable amount are as follows:

Končar Renewable Sources Ltd.:

- The expected rate of return on invested capital of 5% was used in determining the possibility of return on investment and loans in the entity, according to the investment study of the Energy Institute Hrvoje Požar.

In case the applied discount rate had increased by 1%, this would have an impact on the estimated recoverable amount of HRK 7 million. In case the applied discount rate had increased by 1%, this would have an impact on the estimated recoverable amount of HRK 7.8 million.

Končar Low Voltage Switches and Circuit Brakers Inc.:

- A discount rate of 12% was determined
- A growth rate of 4% was defined in the medium-term business plans

The entity's residual value is calculated assuming that, following the business plan period (after 2022), the entity will achieve stable cash flows equal to cash flows estimated for 2022.

In case the applied discount rate had increased by 1%, this would have an impact on the estimated recoverable amount of HRK 3.5 million. In case the applied discount rate had increased by 1%, this would have an impact on the estimated recoverable amount of HRK 4.5 million.

4. Sales

	2017 HRK	2016 HRK
Fees charged to related parties (Note 34)	25,986,623	28,771,581
Rent charged to related parties (Note 34)	24,000,000	24,000,000
Fees charged to unrelated parties	185,477	234,521
	50,172,100	**53,006,102**

5. Other operating income

	2017 HRK	2016 HRK
Release of provisions and dispute resolutions (Note 29)	2,105,114	357,000
Gain on sale of assets	407,781	72,670
Subsidies and compensation claims	110,028	47,855
Rental income	41,231	21,495
Other income	584,924	602,561
	3,249,078	**1,101,581**

6. Cost of materials and energy

	2017 HRK	2016 HRK
Energy cost	4,963,433	5,878,162
Cost of raw materials and supplies	348,553	295,605
Cost of small inventory	143,698	108,435
	5,455,684	**6,282,202**

7. Service costs

	2017 HRK	2016 HRK
Intellectual services	7,007,950	6,074,005
Maintenance services (servicing)	4,794,472	4,416,487
Security services	3,949,368	3,510,448
Utility and water protection fee	3,927,755	3,885,555
Supervisory services and property management at Sesvetski Kraljevec, Samobor, Jankomir, Zlatar	2,880,000	2,880,000
Cleaning services	2,358,664	2,394,335
Entertainment	1,883,000	1,643,125
Costs of advertising and fairs	1,162,252	1,091,346
Graphic design services	813,639	1,079,018
Rent services and leases	810,900	867,479
Professional training	808,167	639,820
Telephone, post and transport	702,185	759,972
Hazardous waste disposal services	615,655	-
Work environment testing services	330,000	440,000
Audit and consulting services	380,317	179,642
Lawyer services	37,581	223,652
Other services	1,679,127	1,618,925
	34,141,032	**31,703,809**

8. Staff costs

	2017 HRK	2016 HRK
Net salaries and wages	11,153,376	11,941,890
Taxes and contributions	7,117,249	9,401,372
Contributions on salaries	3,164,786	3,674,958
	21,435,411	**25,018,220**

Net salaries in the amount of **HRK 11,153,376** (2016: HRK **11,941,890**) include compensations to members of the Management Board in the amount of HRK 3,834,067 (2016: HRK 3,189,289) and accrued bonuses to the Company's Management Board in the amount of HRK 1,447,600 (2016: HRK 1,860,000), and are an integral part of staff costs.

In 2017, pension fund contributions amounted to HRK 2,664,694 (2016: HRK 2,842,508).

Employee benefits (such as transportation to and from work, termination benefits and jubilee awards, business travel expenses) in the amount of HRK 1,061 thousand (2016: HRK 1,186 thousand) are recorded in Note 9.

9. Other expenses

	2017 HRK	2016 HRK
Compensations to members of the Supervisory Board	2,389,659	2,280,427
Sponsorships and donations	1,667,173	2,699,801
Service contracts, royalties	942,899	963,331
Insurance premiums	837,026	939,870
Daily allowances for business trips and travel expenses	803,739	811,146
Administration costs	784,993	72,177
Taxes irrespective of results and similar expenses	452,093	479,802
Reimbursements of costs to employees, gifts and support	257,541	374,826
Bank charges and payment transactions	111,375	69,827
Membership fees and similar expenses	105,970	102,029
Other	1,030,109	119,012
	9,382,577	**8,912,248**

10. Impairment

	2017 HRK	2016 HRK
Impairment of investment property	-	761,400
	-	**761,400**

11. Provisions

	2017 HRK	2016 HRK
Provisions for termination benefits and jubilee awards (Note 29)	467,600	1,338,030
Provisions for unused vacation (Note 29)	556,236	80,562
	1,023,836	**1,418,592**

12. Finance income and costs

	2017 HRK	2016 HRK
Finance income		
From relations with associates		
Income dividends and shares in profit	72,973,704	65,277,916
From relations with subsidiaries		
Income from dividends and shares in profit, and acquisition of shares	47,418,562	53,515,674
Interest income from loans granted	1,847,308	1,774,947
	49,265,870	*55,290,621*
From transactions with unrelated parties		
Interest income on deposits	1,594,849	2,961,171
Interest income from sale of shares to employees	257,363	641,235
Interest income – other	243,078	327,781
Foreign exchange gains on foreign currency deposits	5,673,254	3,442,465
Foreign exchange gains – other	531,433	1,305,597
Income from dividends and shares in profit	130,770	6,216
Other finance income	-	1,023,027
	8,430,747	*9,707,492*
Gains from reversal of impairment of shares in subsidiaries	-	13,081,679
Other unrealised gains	759,213	1,149,275
	759,213	*14,230,954*
	131,429,534	**144,506,983**
Finance costs		
From relations with unrelated parties		
Foreign exchange losses on foreign currency deposits	(4,901,596)	(6,410,948)
Foreign exchange losses on loans granted for the sale of flats	(560,912)	(655,009)
Foreign exchange losses – other	(2,322,347)	(244,317)
	(7,784,855)	*(7,310,274)*
Unrealised losses		
Losses from impairment of shares in subsidiaries	(28,202,000)	(43,901,842)
Losses from impairment of shares – other	(30,257)	(398,086)
	(28,232,257)	*(44,299,928)*
Other finance costs	*(503,561)*	*(161,159)*
	(36,520,673)	**(51,771,361)**
Finance income – net	**94,908,861**	**92,735,622**

At the reporting date the Company made an impairment test of shares in subsidiaries and recognised a net loss in the amount of HRK 28,2 million (2016: loss of HRK 30,1 million). In 2017, at Končar - Renewable Sources Ltd. the Parent company’s share was impaired in the amount of HRK 26.7 million (2016: HRK 4.8 million) and at Končar Low Voltage Switches and Circuit Brakers Inc. in the amount of HRK 1.5 million.

When deciding to invest in a project of strategic interest for the Končar Group (project windfarm) and accepting the Investment Study prepared by the Energy Institute Hrvoje Požar, the Management Board and the Supervisory Board have accepted the expected rate of return on the investment of 5%. The value of cash flows within the estimated useful life of the project, discounted to the present value by applying the rate of return of 5% is sufficient for the coverage of invested capital and repayment of loans.

In determining the present value of the Parent company's contribution, mid-term plans of companies for the period 2018 – 2022 were used, which were adopted by the Supervisory Board by applying the discount rate appropriate to the market position of the companies.

13. Income tax

	2017 HRK	2016 HRK
Profit before tax	69,074,443	64,768,071
Income tax at 18% (2016: 20%)	**12,433,400**	**12,953,615**
Tax effects of:		
Tax non-deductible expenses	5,400,697	9,273,136
Income not subject to tax	(21,694,146)	(26,526,921)
Tax incentives (Government subsidies for education)	(93,153)	(114,195)
Tax losses for which no deferred tax asset was recognised	3,953,202	4,414,365
Income tax	**-**	**-**

The Company has not recognised deferred tax assets in the total amount of HRK 17,948,900 (2016: 13,995,698) due to the uncertainty of its usage within the period of five years (the Company as a holding mainly realises non-taxable revenue (dividends and shares in profit). The income tax rate for the application of the deferred tax calculation is 18% in accordance with the changes in the tax regulations in force.

Total tax losses expire as follows:

	2017 HRK	2016 HRK
Within 5 years	21,962,233	22,071,829
Within 4 years	22,071,829	5,437,862
Within 3 years	5,437,862	15,255,154
Within 2 years	15,255,154	34,989,035
In the next year	34,989,035	-
	99,716,113	**77,753,880**

To date, the Tax Administration did not perform a review of the Company's income tax return. In accordance with local regulations, the Tax Administration may at any time inspect the Company's books and records within 3 years following the year in which the tax liability is reported and may impose additional tax liabilities and penalties. The Company's Management Board is not aware of any circumstances, which may give rise to a potential material liability in this respect.

14. Earnings per share

Basic and diluted earnings per share

	2017 HRK	2016 HRK
Profit for the year	69,074,443	64,768,071
Weighted average number of shares *(net of treasury shares)*	2,566,258	2,566,258
Earnings per share *in HRK*	**26.92**	**25.23**

Diluted earnings per share for 2017 and 2016 is equal to basic earnings per share, since the Company did not have any convertible instruments or share options outstanding during either period.

15. Non-current intangible assets

	Concessions, patents, licences, software and other rights	Other	Intangible assets in progress	Total
	HRK	HRK	HRK	HRK
Cost				
At 1 January 2016	**468,629**	**653,207**	**1,007,436**	**2,129,272**
Additions	-	-	285,000	285,000
At 31 December 2016	**468,629**	**653,207**	**1,292,436**	**2,414,272**
Additions	-	-	149,360	149,360
At 31 December 2017	**468,629**	**653,207**	**1,441,796**	**2,563,632**
Accumulated amortisation				
At 1 January 2016	**468,629**	**653,207**	**-**	**1,121,836**
Amortisation charge	-	-	-	-
At 31 December 2016	**468,629**	**653,207**	**-**	**1,121,836**
Amortisation charge	-	-	-	-
At 31 December 2017	**468,629**	**653,207**	**-**	**1,121,836**
Net book amount				
31 December 2016	**-**	**-**	**1,292,436**	**1,292,436**
31 December 2017	**-**	**-**	**1,441,796**	**1,441,796**

The cost of fully amortised intangible assets still in use as at 31 December 2017 amounts to HRK 1,122 thousand (2016: HRK 1,122 thousand).

16. Property, plant and equipment

	Land	Buildings	Plant and equipment	Tools and office supplies	Other	Assets under construction	Advances	Total
	HRK	HRK	HRK	HRK	HRK	HRK	HRK	HRK
Cost								
At 1 January 2016	**74,194,519**	**279,319,996**	**36,606,285**	**4,994,191**	**63,376**	**9,061,945**	**-**	**404,240,312**
Additions	-	-	16,292,026	-	-	39,229,231	677,468	56,198,725
Transfer from assets under construction	-	7,280,046	1,184,173	691,250	6,070	(9,161,539)	-	-
Transfer to investment property	-	-	-	-	-	(19,240,283)	-	(19,240,283)
Disposals	-	-	(577,563)	(745,021)	-	-	(543,503)	(1,866,087)
At 31 December 2016	**74,194,519**	**286,600,042**	**53,504,921**	**4,940,420**	**69,446**	**19,889,354**	**133,965**	**439,332,667**
Additions	-	-	-	-	-	12,969,804	5,805,325	18,775,129
Transfer from assets under construction	118,560	1,811,386	1,794,294	2,813,964	-	(6,538,204)	-	-
Transfer to investment property	-	-	-	-	-	(19,904,268)	-	(19,904,268)
Disposals	(114,000)	(178,388)	(271,283)	(2,095,923)	-	-	(3,346,991)	(6,006,585)
At 31 December 2017	**74,199,079**	**288,233,040**	**55,027,932**	**5,658,461**	**69,446**	**6,416,686**	**2,592,299**	**432,196,943**
Accumulated depreciation								
At 1 January 2016	**-**	**168,037,817**	**24,959,583**	**4,140,219**	**-**	**-**	**-**	**197,137,619**
Depreciation charge	-	5,373,895	1,892,930	711,938	-	-	-	7,978,763
Additions	-	-	16,301,020	59,363	-	-	-	16,360,383
Disposals	-	-	(537,422)	(711,226)	-	-	-	(1,248,648)
At 31 December 2016	**-**	**173,411,712**	**42,616,111**	**4,200,294**	**-**	**-**	**-**	**220,228,117**
Depreciation charge	-	5,467,449	1,613,143	736,464	-	-	-	7,817,056
Disposals	-	(178,388)	(269,188)	(2,080,544)	-	-	-	(2,528,120)
At 31 December 2017	**-**	**178,700,773**	**43,960,066**	**2,856,214**	**-**	**-**	**-**	**225,517,053**
Net book amount								
31 December 2016	**74,194,519**	**113,188,330**	**10,888,810**	**740,126**	**69,446**	**19,889,354**	**133,965**	**219,104,550**
31 December 2017	**74,199,079**	**109,532,267**	**11,067,866**	**2,802,247**	**69,446**	**6,416,686**	**2,592,299**	**206,679,890**

The cost of fully depreciated tangible assets still in use as at 31 December 2017 amounts to HRK 52,066 thousand (2016: HRK 58,675 thousand).

A mortgage is registered over land with a carrying value of HRK 44,917 thousand (2016: HRK 44,917 thousand) and business facilities with a carrying value of HRK 69,648 thousand (2016: HRK 71,168 thousand) as collateral for the subsidiaries' obligations.

17. Investment property

Investment property (located in Osijek, Sesvetski Kraljevec, Samobor, Požega-Zvečevo, Zagreb and Zlatar) in the amount of HRK 151,294,123 (2016: HRK 162,443,479) relates to investment property for capital appreciation intended for future sale. The residual value of these investments estimated by independent valuers exceeds their carrying value, and accordingly, depreciation is not charged to these investments.

The following table discloses movements in investment property in 2017 and 2016 (at the transfer to investment property, the Company uses the gross presentation principle, i.e. increases the cost and accumulated depreciation for these assets):

	Land	Buildings	Total
	HRK	HRK	HRK
Cost			
At 1 January 2016	**45,147,965**	**176,921,697**	**222,069,662**
Transfer from assets under construction	9,635,000	18,252,266	27,887,266
Reclassification	888,600	(888,600)	-
Additions	481,750	480,338	962,088
Disposals	(68,720)	-	(68,720)
At 31 December 2016	**56,084,595**	**194,765,701**	**250,850,296**
Transfer from assets under construction	10,024,027	9,880,241	19,904,268
Disposals	(10,537,466)	(20,516,158)	(31,053,624)
At 31 December 2017	**55,571,156**	**184,129,784**	**239,700,940**
Accumulated depreciation			
At 1 January 2016	**-**	**78,998,432**	**78,998,432**
Additions	-	8,646,984	8,646,984
Impairment	-	761,401	761,401
At 31 December 2016	**-**	**88,406,817**	**88,406,817**
Impairment	-	-	-
At 31 December 2017	**-**	**88,406,817**	**88,406,817**
Net book amount			
31 December 2016	**56,084,595**	**106,358,884**	**162,443,479**
31 December 2017	**55,571,156**	**95,722,967**	**151,294,123**

The fair value of investment property at the balance sheet date relates to fair value level 3 since the input variables are not based on observable market data. At the balance sheet date, the fair value of investment property amounted to HRK 151 million.

18. Investments in subsidiaries

	31 December 2017 HRK	31 December 2016 HRK
Investments (shares) in domestic subsidiaries		
Končar - Infrastructure and Services Ltd., Zagreb	56,691,318	56,691,318
Končar - Electrical Engineering Institute Inc., Zagreb	60,936,110	60,936,110
Končar - Electronics and Informatics Inc., Zagreb	46,138,413	46,138,413
Končar - Small Electrical Machines Inc., Zagreb	48,600,512	48,600,512
Končar - Generators and Motors Inc., Zagreb	116,347,127	116,347,127
Končar - Instrument Transformers Inc., Zagreb	30,445,749	30,228,943
Končar - Distribution and Special Transformers Inc., Zagreb	62,118,369	62,118,369
Končar - Switchgear Inc. (previously: Končar - Medium Voltage Apparatus Inc., Zagreb)	198,720,684	65,576,811
Končar - Electric Vehicles Inc., Zagreb	36,409,158	36,409,158
Končar - Switchgears Inc., Sesvetski Kraljevec	-	28,647,123
Končar - Household Appliances Ltd., Zagreb	147,966,970	147,966,970
Končar - High Voltage Switchgears Inc., Zagreb	-	96,598,157
Končar - Low Voltage Switches and Circuit Brakers Inc., Zagreb	81,432,641	81,432,641
Končar - Engineering for Plant Installation & Commissioning Inc., Zagreb	6,908,942	6,908,942
Končar - Power Plant and Electric Traction Engineering Inc., Zagreb	51,773,266	51,773,266
Končar - Renewable Sources Ltd., Zagreb	111,120,000	111,120,000
Končar - Steel Structures Inc., Zagreb	31,484,723	16,703,123
Impairment of investments	*(318,226,396)*	*(290,024,399)*
	768,867,586	**774,172,584**

Pursuant to the Merger Agreement dated 29 September 2017, approved by the Decision of the Company's General Assembly dated 20 December 2017, and by the Decision of the Commercial Court dated 29 December 2017, Končar - Switchgears Inc. and Končar - Electrical High Voltage Switchgears Inc. merged with all their assets, rights and obligations with the company Končar - Switchgear Inc. (previously Končar– Medium Voltage Apparatus Inc.).

Shares in ownership and voting rights as at 31 December were as follows:

	31 December 2017		31 December 2016	
	Ownership share (%)	Voting rights share (%)	Ownership share (%)	Voting rights share (%)
Domestic subsidiaries				
Končar - Household Appliances Ltd., Zagreb	100.00	100.00	100.00	100.00
Končar - Small Electrical Machines Inc., Zagreb	100.00	100.00	100.00	100.00
Končar - Power Plant and Electric Traction Engineering Inc., Zagreb	100.00	100.00	100.00	100.00
Končar - Infrastructure and Services Ltd., Zagreb	100.00	100.00	100.00	100.00
Končar - Electrical Engineering Institute Inc., Zagreb	100.00	100.00	100.00	100.00
Končar - Low Voltage Switches and Circuit Brakers Inc., Zagreb	100.00	100.00	100.00	100.00
Končar - Generators and Motors Inc., Zagreb	100.00	100.00	100.00	100.00
Končar - Renewable Sources Ltd., Zagreb	85.27	85.27	85.27	85.27
Končar - Electric Vehicles Inc., Zagreb	75.04	75.04	75.04	75.04
Končar - Steel Structures Inc., Zagreb	100.00	100.00	75.01	75.01
Končar - Electronics and Informatics Inc., Zagreb	75.03	75.03	75.03	75.03
Končar - Switchgears Inc., Sesvetski Kraljevec	-	-	70.03	81.70
Končar - Switchgear Inc. (previously: Končar - Medium Voltage Apparatus Inc., Zagreb)	100.00	100.00	100.00	100.00
Končar - Instrument Transformers Inc., Zagreb	61.97	99.77	61.73	99.77
Končar - Distribution and Special Transformers Inc., Zagreb	52.73	67.90	52.73	67.90
Končar - High Voltage Switchgears Inc., Zagreb	-	-	98.61	99.03
Končar - Engineering for Plant Installation & Commissioning Inc., Zagreb	44.71	79.05	44.71	79.05

At the balance sheet date, the Company recognised an impairment loss for investments in subsidiaries on the basis of performed impairment tests (Note 12).

The summary data for subsidiaries with a significant non-controlling interest are disclosed in the consolidated financial statements of the Company.

19. Investments in associates

Investments in associates in the amount of HRK 67,722,257 (2016: HRK 67,722,257) relate to the investment in the company Končar - Power Transformers Ltd., Zagreb (the Company holds a 49% share in the share capital of this company).

The summary data for this company are disclosed in the consolidated financial statements of the Company.

20. Non-current financial assets

	31 December 2017 HRK	31 December 2016 HRK
Available-for-sale financial assets:		
Shares in Tesla Savings Bank	3,500,010	3,500,010
Impairment of shares in Tesla Savings Bank	(3,500,010)	(3,500,010)
Financial assets at fair value through profit or loss		
Shares in Zagrebačka banka d.d., Zagreb	1,226,593	1,256,850
	1,226,593	**1,256,850**

21. Non-current receivables

	31 December 2017 HRK	31 December 2016 HRK
Receivables from credit sales		
Receivables for flats sold /i/	7,234,403	8,919,173
Impairment of receivables for flats sold	(428,782)	(1,187,994)
Current portion (Note 24)	(856,796)	(873,603)
	5,948,825	*6,857,576*
Receivables for shares sold	-	2,509,870
Current portion (Note 24)	-	(2,509,870)
	-	-
Other loans receivable	-	8,883
Other financial assets	439	438
Receivable on the basis of foreign sales /ii/	3,371,833	3,984,780
Current portion (Note 23)	(680,699)	(593,139)
	2,691,573	*3,400,962*
	8,640,398	**10,258,538**

/i/ In accordance with the Law on the Sale of Flats with Tenancy Rights, the flats owned by the Company were sold at an interest rate of 1% per annum with the average maturity of 28 years and indexed. According to this index, receivables increase/decrease if the EUR exchange rate of EUR changes more than 5.1% compared to the rate that existed at the signing date of the Sale agreements.

The amounts of unpaid annuities in DEM have been converted into EUR at a fixed rate of EUR 1 = DEM 1.95583. As collateral, a mortgage over sold flats has been registered.

/ii/ The receivable on the basis of foreign sales relates to the receivable for sales in Bosnia and Herzegovina realised by the company TAKRAF from Germany, acquired by KfW Bank, Berlin.

22. Receivables from related parties

	31 December 2017 HRK	31 December 2016 HRK
Trade receivables		
Domestic subsidiaries		
Končar - Infrastructure and Services Ltd., Zagreb	2,847,115	11,484
Končar - Distribution and Special Transformers Inc., Zagreb	1,277,422	1,449,189
Končar - Generators and Motors Inc., Zagreb	1,205,179	614,711
Končar - Power Plant and Electric Traction Engineering Inc., Zagreb	1,089,218	965,136
Končar - Instrument Transformers Inc., Zagreb	960,095	783,290
Končar - Steel Structures Inc., Zagreb	808,958	444,689
Končar - Electric Vehicles Inc., Zagreb	432,860	479,732
Končar - Small Electrical Machines Inc., Zagreb	332,759	336,533
Končar - Household Appliances Ltd., Zagreb	305,200	483,095
Končar - Switchgear Inc. (previously: Končar - Medium Voltage Apparatus Inc., Zagreb)	276,051	94,429
Končar - Electrical Engineering Institute Inc., Zagreb	269,915	263,848
Končar - Low Voltage Switches and Circuit Brakers Ltd., Zagreb	179,415	185,483
Končar - Engineering for Plant Installation & Commissioning Inc., Zagreb	177,114	188,516
Končar - Renewable Sources Ltd., Zagreb	120,255	140,221
Končar - Electronics and Informatics Inc., Zagreb	8,125	117,231
Končar - Switchgears Inc., Sesvetski Kraljevec	-	1,023,099
Končar - High Voltage Switchgears Inc., Zagreb	-	221,384
Associates		
Končar - Power Transformers Ltd., Zagreb	571,334	66,187,429
	10,861,015	*73,989,499*
Interest receivable (total)	*294,861*	*262,928*
	11,155,876	**74,252,427**

As at 31 December, the ageing structure of the Company's receivables from related parties was as follows:

	Total	Not past due	Past due but collectible				
			< 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	HRK	HRK	HRK	HRK	HRK	HRK
2017	**11,155,876**	9,308,741	1,416,890	296,085	134,160	-	-
2016	**74,252,427**	72,252,319	1,270,742	53,164	205,285	470,917	-

There was no significant change in the credit quality of receivables past due which have not been impaired and they are considered recoverable.

The maximum exposure to credit risk at the balance sheet date is the carrying value of each of the class of receivable mentioned above.

23. Trade receivables

	31 December 2017 HRK	31 December 2016 HRK
Domestic trade receivables	372,200	477,809
Foreign trade receivables (current portion, Note 21)	680,699	593,139
	1,052,899	**1,070,948**

As at 31 December, the ageing structure of trade receivables was as follows:

	Total	Not past due	Past due but collectible				
			< 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	HRK	HRK	HRK	HRK	HRK	HRK
2017	**372,200**	136,883	4,659	55	55	9,000	221,548
2016	**477,809**	136,949	13,789	3,125	9,375	314,571	-

There was no significant change in the credit quality of receivables past due which have not been impaired and they are considered recoverable. The maximum exposure to credit risk at the balance sheet date is the carrying value of each of the class of receivable mentioned above.

24. Other receivables

	31 December 2017 HRK	31 December 2016 HRK
Receivables for shares sold (due) /i/	9,185,814	9,032,958
Receivable for claims recognised	8,292,699	8,292,699
Interest receivables on bank deposits	1,019,624	38,466
Receivables for sold flats	950,746	965,785
Receivables for prepaid value added tax	458,963	-
Receivables from companies no longer within the Končar Group	-	306,686
Current portion of non-current receivables for sold shares	-	2,509,870
Other receivables	145,600	159,796
	20,053,446	**21,306,260**

/i/ Receivables for sold shares and stakes relate to non-current receivables from the sale of shares of related companies Končar - Electronics and Informatics Inc. within the employee share ownership program repayable in instalments over a period of 10 years, which have been recorded as current receivables at the balance sheet date.

The maximum exposure to credit risk at the balance sheet date is the carrying value of each of the class of receivable mentioned above.

25. Loans granted to subsidiaries

	31 December 2017 HRK	31 December 2016 HRK
Končar - Renewable Sources Ltd., Zagreb	29,075,456	24,075,456
Končar - Steel Structures Inc.	22,000,000	-
Končar - Switchgear Inc.	8,000,000	-
Končar - High Voltage Switchgears Inc., Zagreb	-	12,700,000
Končar - Household Appliances Ltd.	-	2,000,000
	59,075,456	**38,775,456**

Loans granted to subsidiaries are repayable within one year at an annual interest rate of 5%, secured by blank bills of exchange and debentures.

26. Deposits and loans granted

	31 December 2017 HRK	31 December 2016 HRK
Deposits over 3 months	147,677,424	193,248,200
Loans granted	625,281	647,102
	148,302,705	**193,895,302**

Deposits over 3 months relate to deposits placed at a commercial bank bearing an annual interest rate ranging from 0.7% to 0.9% (2016: 0.05% – 0.35% p.a.).

27. Cash and cash equivalents

	31 December 2017 HRK	31 December 2016 HRK
Foreign currency account balance	138,778,584	76,982,977
Giro account balance	80,804,208	11,784,737
Cash on hand – HRK	4,701	4,711
Cash on hand – foreign currencies	16,666	17,315
	219,604,159	**88,789,740**

28. Capital and reserves

Share (registered) capital is determined in the nominal amount of HRK 1,208,895,930 (31 December 2016: HRK 1,208,895,930) and comprises 2,572,119 shares with a nominal value of HRK 470 per share.

The Company's ownership structure was as follows:

		31 December 2017		31 December 2016	
	Shareholder	Number of shares	Ownership share %	Number of shares	Ownership share %
1	HPB d.d. (Kapitalni fond d.d.)	724,515	28.17	724,515	28.17
2	ADDIKO BANK d.d./PBZ Croatia Osiguranje OMF	420,928	16.37	420,928	16.37
3	SOCIETE GENERALE / AZ OMF	377,429	14.67	377,429	14.67
4	SOCIETE GENERALE - Splitska banka d.d./ Erste Plavi mandatory pension fund	359,239	13.97	359,239	13.97
5	Restructuring and Sale Center (CERP)/Croatia	83,610	3.25	57,982	2.25
6	FLORIČIĆ KRISTIJAN	50,714	1.97	50,714	1.97
7	ADDIKO BANK/RBA OMF	47,636	1.85	48,291	1.88
8	ZAGREBAČKA BANKA D.D. /AZ PROFIT DOBROVOLJNI MIROVINSKI FOND	32,803	1.28	28,928	1.12
9	PBZ d.d. /custodian joint client account	24,251	0.94	29,050	1.13
10	ZEC BRANISLAV	22,843	0.89	22,843	0.89
11	Other shareholders	422,290	16.41	446,339	17.35
12	KONČAR Inc. (treasury shares)	5,861	0.23	5,861	0.23
		2,572,119	**100.00**	**2,572,119**	**100.00**

On 21 December 2010, ordinary shares of the Company were listed on the Official market at the Zagreb Stock Exchange under the name KOEI-R-A in accordance with the resolution of the Zagreb Stock Exchange Management from 20 December 2010.

In 2017, the Company's General Assembly reached a decision on the payment of dividends to shareholders in the amount of HRK 30,795,096 which is HRK 12,00 per share (2016: HRK 30,857,460 which is HRK 12,00 per share).

The Company has established legal, statutory and other reserves in accordance with the Company's Act that are formed on the basis of profit distribution according to the General Assembly's decisions. Statutory and other reserves are distributable. The movement in these reserves in 2017 and 2016 was as follows:

	Legal reserves HRK	Statutory reserves HRK	Other reserves HRK	Total HRK
1 January 2016	**35,025,950**	**217,684,029**	**41,396,764**	**294,106,743**
Allocation of profit as per annual calculation	3,121,723	-	28,517,652	31,639,375
31 December 2016	**38,147,673**	**217,684,029**	**69,914,416**	**325,746,118**
Allocation of profit as per annual calculation	3,238,403	-	30,734,572	33,972,975
31 December 2017	**41,386,076**	**217,684,029**	**100,648,988**	**359,719,093**

29. Provisions

	Provisions for legal disputes	Jubilee awards and termination benefits	Unused vacation	Total
	HRK	HRK		HRK
1 January 2016	32,100,000	2,343,923	498,058	34,941,981
Additional provisions	-	1,338,030	80,562	1,418,592
Release of provisions	(300,000)	(57,000)	-	(357,000)
31 December 2016	**31,800,000**	**3,624,953**	**578,620**	**36,003,573**
Additional provisions	-	467,600	556,236	1,023,836
Utilised provisions	(31,800,000)	-	-	(31,800,000)
Release of provisions	-	(780,118)	(578,620)	(1,358,739)
31 December 2017	**-**	**3,312,434**	**556,236**	**3,868,670**
Provisions mature as follows:				
Within 1 year	-	-	556,236	**556,236**
More than 1 year	-	3,312,434	-	**3,312,434**

Provisions for legal disputes

Long-term provisions for legal disputes in the amount of HRK 31,800,000 relate to a legal dispute initiated against the Company in Croatia in relation to determining ownership over the property in Konavoska, Zagreb. During 2017, the Company released the amount of the provision since a resolution was rendered in favour of the plaintiff, and decreased the value of the investment property in the same amount (Note 17).

Provisions for long-term employee benefits (termination benefits and jubilee awards)

The non-current portion of provisions for termination benefits in the amount of HRK 3,312 thousand (2016: HRK 3,625 thousand) relates to the estimated amount of termination benefits in line with the Collective Agreement, to which employees are entitled at the end of their employment (either upon retirement, termination or voluntary departure). The net present value of the provision is calculated on the basis of the number of employees, amount of benefit, years of service within the Company at the balance sheet date and the discount rate of 2% (2016: 3.5%).

Current provisions

Provisions for the cost of unused vacation days in the amount of HRK 556 thousand (2016: HRK 579 thousand) relate to the employee benefit for unused vacation days at the balance sheet date.

30. Current liabilities to related parties

	31 December 2017 HRK	31 December 2016 HRK
Subsidiaries:		
Končar - Infrastructure and Services Ltd.	8,240,096	6,320,168
Končar - Power Plant and Electric Traction Engineering Inc.	815,925	119,560
Končar - Electronics and Informatics Inc.	576,189	140,647
Končar - Electric Vehicles Inc.	25,000	25,000
Končar - Electrical Engineering Institute Inc.	8,000	11,738
Končar - Switchgears Inc.	-	1,000,000
Končar - Generators and Motors Inc.	-	25,000
	9,665,210	**7,642,113**

31. Current trade payables

	31 December 2017 HRK	31 December 2016 HRK
Domestic trade payables	2,388,001	933,380
Foreign trade payables	37,779	18,768
	2,425,780	**952,148**

As at 31 December, the ageing structure of trade payables was as follows:

	Total	Not past due	Past due < 60 days	60-90 days	90-180 days	180-365 days	> 365 days
	HRK	HRK	HRK	HRK	HRK	HRK	HRK
2017	**2,425,780**	2,260,996	164,784	-	-	-	-
2016	**952,148**	847,388	104,760	-	-	-	-

32. Other current liabilities

	31 December 2017 HRK	31 December 2016 HRK
Liabilities to employees		
Liabilities for net salaries	611,042	733,185
Bonus accruals	1,447,600	1,860,000
	2,058,642	***2,593,185***
Taxes, contributions and similar charges		
Liabilities for taxes	1,278,949	1,997,303
VAT payable	-	233,378
Contributions payable	910,618	1,222,092
	2,189,567	***3,452,773***
Other liabilities		
Dividend payable	479,583	414,380
Liabilities to the state for flats sold	256,460	11,549
Other liabilities	175,532	156,513
	911,575	***582,442***
	5,159,784	**6,628,400**

33. Contingent liabilities and off-balance sheet items

	31 December 2017 HRK	31 December 2016 HRK
Subsidiarity guarantee (Zagrebačka banka d.d.)	412,927,403	505,049,647
Bills of exchange	59,075,456	36,775,456
Corporate guarantees / Končar Inc.	25,491,103	43,835,165
Flats sold (65%)	19,911,547	21,723,124
Debentures	3,204,640	5,204,640
Corporate guarantees / other banks	1,127,047	2,481,390
	521,737,196	**615,069,422**

Total guarantees issued by the Company as disclosed in the above table include performance guarantees amounting to HRK 301,527 thousand (2016: HRK 413,763 thousand).

34. Related party transactions

Parties are considered to be related if one party has the ability to control the other party, is under common control or exercises significant influence over the other party in making financial or operational decisions. Related parties include companies within the Končar Group. These companies are subsidiaries or associates (companies with participating interests). All related party transactions are based on arm's length conditions (purchase of goods, sale of products and provision of services).

2017	**Operating activities**				**Financing activities**	
Company	**Receivables HRK'000**	**Liabilities HRK'000**	**Revenues HRK'000**	**Expenses HRK'000**	**Receivables HRK'000**	**Revenues HRK'000**
Končar - Infrastructure and Services Ltd.	2,847	8,240	24,504	13,057	-	-
Končar - Household Appliances Ltd.	305	-	1,276	16	-	42
Končar - Electric Vehicles Inc.	433	25	1,550	240	-	-
Končar - High Voltage Switchgears Inc.	-	-	429	-	8,033	176
Končar - Generators and Motors Inc.	1,205	-	2,323	120	-	-
Končar - Power Plant and Electric Traction Engineering Inc.	1,089	816	3,189	3,015	-	-
Končar - Steel Structures Inc.	809	-	1,499	-	22,141	388
Končar - Switchgears Inc.	-	-	484	666	-	-
Končar - Instrument Transformers Inc.	960	-	1,471	-	-	-
Končar - Low Voltage Switches and Circuit Breakers Ltd.	179	-	627	115	-	-
Končar - Distribution and Special Transformers Inc.	1,277	-	5,663	-	-	-
Končar - Electrical Engineering Institute Inc.	270	-	888	91	-	-
Končar - Small Electrical Machines Inc.	333	-	879	-	-	-
Končar - Engineering Co. for Plant Installation & Commissioning Inc.	177	-	817	-	-	-
Končar - Electronics and Informatics Inc.	8	576	915	1,937	-	-
Končar - Switchgear Inc. (previously: Končar - Medium Voltage Apparatus Inc., Zagreb)	276	-	449	-	-	-
Končar - Power Transformers Ltd.	571	-	2,591	.	-	-
Končar - Renewable Sources Ltd.	120	-	431	.	29,196	1,241
	10,859	9,665	49,985	19,257	59,370	1,847

The transactions presented in the table do not include receivables and dividend income i.e. shares in profit. Dividend income from the associate Končar - Power Transformers Ltd. amounts to HRK 72,974 thousand, while dividend income, i.e. income from shares in profit of subsidiaries amount to HRK 47,419 thousand. Total dividend income, i.e. Income from shares in profit (subsidiaries and associates) is recognised in the amount of HRK 120,392 thousand (2016: HRK 115,079 thousand).

2016	**Operating activities**				**Financing activities**	
Company	**Receivables HRK'000**	**Liabilities HRK'000**	**Revenues HRK'000**	**Expenses HRK'000**	**Receivables HRK'000**	**Revenues HRK'000**
Končar - Infrastructure and Services Ltd.	11	6,320	24,495	13,087	-	-
Končar - Household Appliances Ltd.	483	-	1,067	17	2,008	111
Končar - Electric Vehicles Inc.	480	25	3,128	235	-	-
Končar - High Voltage Switchgears Inc.	221	-	450	-	12,855	504
Končar - Generators and Motors Inc.	615	25	2,415	220	-	-
Končar - Power Plant and Electric Traction Engineering Inc.	965	127	3,084	1,959	-	-
Končar - Steel Structures Inc.	445	-	1,383	-	-	-
Končar - Switchgears Inc.	1,023	1,000	532	-	-	-
Končar - Instrument Transformers Inc.	783	-	1,536	-	-	-
Končar - Low Voltage Switches and Circuit Breakers Ltd.	185	-	663	112	-	-
Končar - Distribution and Special Transformers Inc.	1,449	-	5,234	-	-	-
Končar - Electrical Engineering Institute Inc.	264	12	949	173	-	-
Končar - Small Electrical Machines Inc.	337	-	915	-	-	-
Končar - Engineering Co. for Plant Installation & Commissioning Inc.	189	-	856	-	-	-
Končar - Electronics and Informatics Inc.	117	141	986	1,425	-	-
Končar - Medium Voltage Apparatus Inc., Zagreb	94	-	413	-	-	-
Končar - Power Transformers Ltd.	910	-	3,069	-	-	-
Končar - Renewable Sources Ltd.	140	-	1,597	-	24,175	1,160
	8,711	**7,650**	**52,772**	**17,228**	**39,038**	**1,775**

The transactions presented in the table do not include receivables and dividend income i.e. shares in profit.

35. Financial risk management and financial instruments

The Company is exposed in its business operations to market (foreign currency) and credit risk.

The Company does not use derivative financial instruments. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimise the adverse effects on the Company's financial statements. The risk management policies relating to current and non-current financial assets, current and non-current receivables, cash management as well as debts and liabilities can be summarised as follows:

a) Capital risk management

The Company manages its capital to ensure its ability to continue as a going concern while maximising the return to shareholders through the optimisation of the debt to equity balance in order to decrease the cost of capital.

The Company manages its capital and makes the necessary adjustments in accordance with the economic conditions in the market and risk features of its assets. In order to adjust or maintain the capital structure, the Company may decide to pay dividends to owners, increase/decrease the share capital, sell assets to reduce liabilities, etc. The objectives, policies and processes have not been changed during the periods ending 31 December 2017 and 31 December 2016. The Company monitors capital on the basis of the gearing ratio, which is calculated as follows:

	31 December 2017 HRK'000	31 December 2016 HRK'000
Financial liabilities	-	-
Less: cash and cash equivalents (deposits)	(219,604)	(88,790)
Net debt	**-**	**-**
Capital	1,644,657	1,606,378
Gearing ratio	-	-

b) Significant accounting policies

Details of the significant accounting policies and methods adopted, including the criteria for recognition, the basis of measurement and the basis on which income and expenses are recognised, in respect of each class of financial asset, financial liability and equity are disclosed in Note 2 to these financial statements.

The accounting policies for financial instruments are applied on the following balance sheet items:

31 December 2017

	Loans and receivables	Assets at fair value through P&L	Available-for-sale assets	Held-to-maturity investments	Assets classified under IAS 39
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
Non-current financial assets and receivables	8,640	1,227	-	-	**9,867**
Current financial assets	207,378	-	-	-	**207,378**
Trade and other receivables	31,658	-	-	-	**31,658**
Cash and cash equivalents	219,604	-	-	-	**219,604**
	467,280	**1,227**	**-**	**-**	**468,507**

31 December 2016

	Loans and receivables	Assets at fair value through P&L	Available-for-sale assets	Held-to-maturity investments	Assets classified under IAS 39
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
Non-current financial assets and receivables	10,847	1,257	-	-	**12,104**
Current financial assets	232,671	-	-	-	**232,671**
Trade and other receivables	96,630	-	-	-	**96,630**
Cash and cash equivalents	88,790	-	-	-	**88,790**
	428,938	**1,257**	**-**	**-**	**430,195**

All of the Company's liabilities have been classified as "Liabilities at amortised cost". The Company does not have any liabilities classified as "Liabilities at fair value through profit or loss".

Fair value of financial assets and liabilities

The following table represents financial assets and liabilities valued at fair value in the Statement of financial position according to the fair value hierarchy. This hierarchy groups financial assets and liabilities into 3 levels depending on the input variables used in measuring the fair value of financial assets and liabilities. The fair value hierarchy has the following levels:

- Level 1: quoted market prices for identical assets or liabilities traded on active markets
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (that is, as prices) or indirectly (that is, derived from prices)
- Level 3: inputs for assets or liabilities that are not based on observable market data.

The level within which financial assets/liabilities are stated are classified based on the lowest level of significant inputs used in measuring fair value. Financial assets and liabilities measured at fair value in the statement of financial position are grouped within the fair value hierarchy as follows:

31 December 2017

In thousands of HRK	Level 1	Level 2	Level 3	Total
Assets				
Listed shares	1,227	-	-	1,227
	1,227	**-**	**-**	**1,227**

31 December 2016

In thousands of HRK	Level 1	Level 2	Level 3	Total
Assets				
Listed shares	1,257	-	-	1,257
	1,257	**-**	**-**	**1,257**

The Company used the following methods and assumptions in estimating the fair value of financial instruments:

Receivables and bank deposits

For assets due within three months and cash funds, the carrying value approximates their fair value due to the short-term nature of these instruments. For longer term assets, the contracted interest rates do not significantly deviate from the current market rates and their fair value, therefore, approximates their carrying value.

Borrowings

The fair value of current liabilities approximates their carrying value due to the short maturities of these instruments. The Management Board believes that their fair value is not materially different from their carrying value.

Other financial instruments

The Company’s financial instruments not carried at fair value are trade receivables, other receivables, trade payables and other current liabilities. The historical carrying value of receivables and liabilities, including provisions that are in line with the usual terms of business is approximately equal to their fair value.

c) Financial risk

The Company's Management Board monitors and manages the financial risks relating to the operations of the Company through internal risk reports, which analyse exposures by the degree and magnitude of risks. These risks include market risk (including currency risk, fair value interest rate risk and price risk), credit risk, liquidity risk and cash flow interest rate risk.

Market risk

Market risk is the risk that the change in market prices, such as the change in foreign currencies and interest rates, would influence the Company's result or the value of its financial instruments. The objective of market risk management is managing and controlling the exposure to this risk within acceptable parameters, thus, optimizing returns.

The Company's activities are primarily exposed to the foreign currency exchange rate risk.

There were no significant changes to the Company's exposure to market risk or the manner in which it manages and measures the risk.

a) Foreign currency risk

The Company is exposed to this risk through sales, purchase and loans denominated in foreign currency which is not the Company's functional currency. Currencies that are subject to risks are primarily EUR and CHF.

The Company incurs foreign currency risk during sales, purchases and short-term bank deposits that are denominated in foreign currency.

The Company's exposure to currency risk is as follows:

31 December 2017	EUR HRK'000	CHF HRK'000	Other currencies HRK'000	Total foreign currencies HRK'000	HRK HRK'000	Total HRK'000
Non-current receivables	2,691	-	-	2,691	5,949	8,640
Trade receivables	681	-	-	681	372	1,053
Current financial assets	98,289	-	-	98,289	50,013	148,302
Cash and cash equivalents	138,468	296	22	138,786	80,818	219,604
Trade payables	(38)	-	-	(38)	(2,388)	(2,426)
	240,091	**296**	**22**	**240,409**	**134,764**	**375,173**

31 December 2016	EUR HRK'000	CHF HRK'000	Other currencies HRK'000	Total foreign currencies HRK'000	HRK HRK'000	Total HRK'000
Non-current receivables	3,392	-	-	3,392	6,867	10,259
Trade receivables	593	-	-	593	478	1,071
Current financial assets	163,248	-	-	163,248	30,000	193,248
Cash and cash equivalents	76,626	323	32	76,981	11,808	88,789
Trade payables	(19)	-	-	(19)	(933)	(952)
	243,840	**323**	**32**	**244,195**	**48,220**	**292,415**

In the above tables, receivables for flats sold are not included in the amounts in EUR because of a contractual clause on the increase/decrease in receivables if the change in EUR currency rate is more than 5.1% compared to the currency rate that existed at the time of concluding the contracts.

Sensitivity analysis

A change in the HRK exchange rate against the EUR by -1% (2016: -1%), and a change against the CHF by -9% (2016: -1%) at the reporting date would decrease profit before tax by the following amounts:

	2017 Effect on profit before tax HRK'000	2016 Effect on profit before tax HRK'000
EUR	(2,401)	(2,467)
CHF	(25)	(3)

This analysis assumes that all other variables, interest rates especially, remain unchanged.

A reverse proportional change of the HRK against the above currencies by the same percentages at the reporting date would have had the equal but opposite effect on the profit before tax, provided that all other variables are held constant.

b) Interest rate risk

The Company is not exposed to interest rate risk since it has no interest-bearing liabilities.

Credit risk

Credit risk refers to the risk that the counterparty will default on its contractual obligations resulting in a financial loss for the Company. The Company has adopted a policy of only dealing with creditworthy counterparties and obtaining sufficient collateral, where appropriate, as a means of mitigating the risk of financial loss from defaults. The Company uses information gathered from specialized credit agencies and the Croatian Chamber of Economy, as well as other publicly available financial information and its own trading records to rate its major customers. The Company's exposure and the credit ratings of its counterparties are continuously monitored and the aggregate value of transactions concluded is spread amongst approved counterparties.

Trade and other receivables

The Company's exposure to credit risk is mainly affected by the individual characteristics of each customer.

The demographics of the customer base, including the default risk of the industry and country, in which customers operate, has less of an influence on credit risk. The Company has established a credit policy under which each new customer is analysed individually for creditworthiness before standard payment and delivery terms and conditions are offered. The Company establishes an allowance for impairment that represents its estimate of incurred losses in respect of trade and other receivables and investments. The age structure of trade receivables (related and unrelated) which are past due but are considered collectable are presented in Notes 22 and 23.

Credit quality of financial assets

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if available) or to historical information about counterparty default rates. As at 31 December 2017, financial assets not past due classified in the category 'Trade receivables' and Receivables from related companies amounted to HRK 12,209 thousand (2016: HRK 72,389 thousand). All receivables relate to outstanding loans, deposits, receivables from government institutions, interest receivables and to customers who typically pay within 60 days from the maturity date.

The credit quality of financial assets that are neither past due nor impaired can be assessed by reference to external credit ratings (if available) or to historical information about counterparty default rates:

	31 December 2017 HRK	31 December 2016 HRK
Trade receivables		
Counterparties with credit rating		
AAA (Standard and Poor's)	680,699	593,139
*Counterparties without credit rating**		
Group 1	-	61,654
Group 3	372,200	416,155
	1,052,899	**1,070,948**
Receivables from related parties (including loans)**	**70,231,332**	**113,027,883**
Other receivables (including loans)		
Counterparties with credit rating		
AAA (Standard and Poor's)	2,691,134	3,391,641
*Counterparties without credit rating**		
Group 3	16,085,824	19,682,196
*Receivables from non-recurring related party transactions****	8,292,699	8,292,699
	27,069,657	**31,366,536**
Cash and short-term deposits		
BB (Standard & Poor's)	219,531,889	281,946,343
A (Standard & Poor's)	147,684,706	-
Cash in hand and at other banks	64,988	91,597
	367,281,583	**282,037,940**

* Classification of counterparties without credit rating:

- Group 1 – new customers (less than 6 months)
- Group 2 – existing customers (more than 6 months) with no defaults in the past
- Group 3 – existing customers (more than 6 months) with defaults in the past; all default payments have been fully collected.

**Although some amounts of receivables from related parties are past due, they were not impaired because historically repayments have been regular and accordingly the risk of non-collectibility of these receivables is immaterial.

***The Company has procedures in place for assessing the reasonableness of non-recurring transactions with third parties, including mandatory verification of customer creditworthiness.

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet their financial obligations as they fall due. Liquidity risk management is the responsibility of the Management Board, which has built a quality frame for monitoring short-, mid- and long-term financing and all liquidity risk requirements. The Company manages this risk by constantly monitoring of estimated and actual cash flow and comparing it with the maturity of financial assets and liabilities.

The following table shows the maturity of the Company's financial liabilities at 31 December in accordance with contracted undiscounted payments:

	Carrying value	Contracted cash flows	0 – 12 months	1 – 2 years	2 – 5 years	More than 5 years
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
31 December 2017						
Trade payables, related parties payables and other payables	12,827	12,827	12,827	-	-	-
	12,827	**12,827**	**12,827**	**-**	**-**	**-**

	Carrying value	Contracted cash flows	0 – 12 months	1 – 2 years	2 – 5 years	More than 5 years
	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000	HRK'000
31 December 2016						
Trade payables, related parties payables and other payables	9,177	9,177	9,177	-	-	-
	9,177	**9,177**	**9,177**	**-**	**-**	**-**

36. Events after the balance sheet date

In 2018, the Management Board of the Company made a decision to extend the loans granted to the subsidiary Končar - Renewable Sources Ltd. The Management Board and the Coordination Board of the company Končar - Renewable Sources Ltd. adopted a plan for the financial restructuring of the company in 2018.

After the reporting date and until the approval date of these financial statements, other than the events stated above, there were no events that would significantly influence the financial statements of the Company for 2017, and that should, consequently, be disclosed.

KONČAR – ELECTRICAL INDUSTY Inc.

CORPORATE GOVERNANCE REPORT

AND

STATEMENT ON APPLICATION OF

CORPORATE GOVERNANCE PRINCIPLES

INTRODUCTION

Končar – Electrical Industry, a joint-stock company, is the parent of Končar-Electrical Industry Group. As such, the Company also generates consolidated reports, presented and revised separately. This 2017 Corporate Governance Report is the report of Končar-Electrical Industry Inc. as a separate entity. The Company manages the subsidiaries and affiliated companies in its ownership.

The companies within the Group are legally autonomous entities supervised by the parent company which strategically directs and supports them through supervisory boards and company assemblies, all pursuant to the Companies Act, the Articles of Association of KONČAR- Electrical Industry Inc., and of individual subsidiaries. The parent also manages the portion of the assets which has not been invested into companies but is directly or indirectly used as the financial support of sales, products and equipment of the subsidiaries as a credit-guarantee potential.

As the parent company, Končar-Electrical Industry Inc. invoices its dependent companies for the following services:

- fees for using the corporate name, brand and trade mark,
- a portion of costs incurred by joint presentation on fairs,
- a portion of costs for the agencies abroad,
- a portion of joint costs for marketing activities,
- seminars for managers, quality and environment management systems.

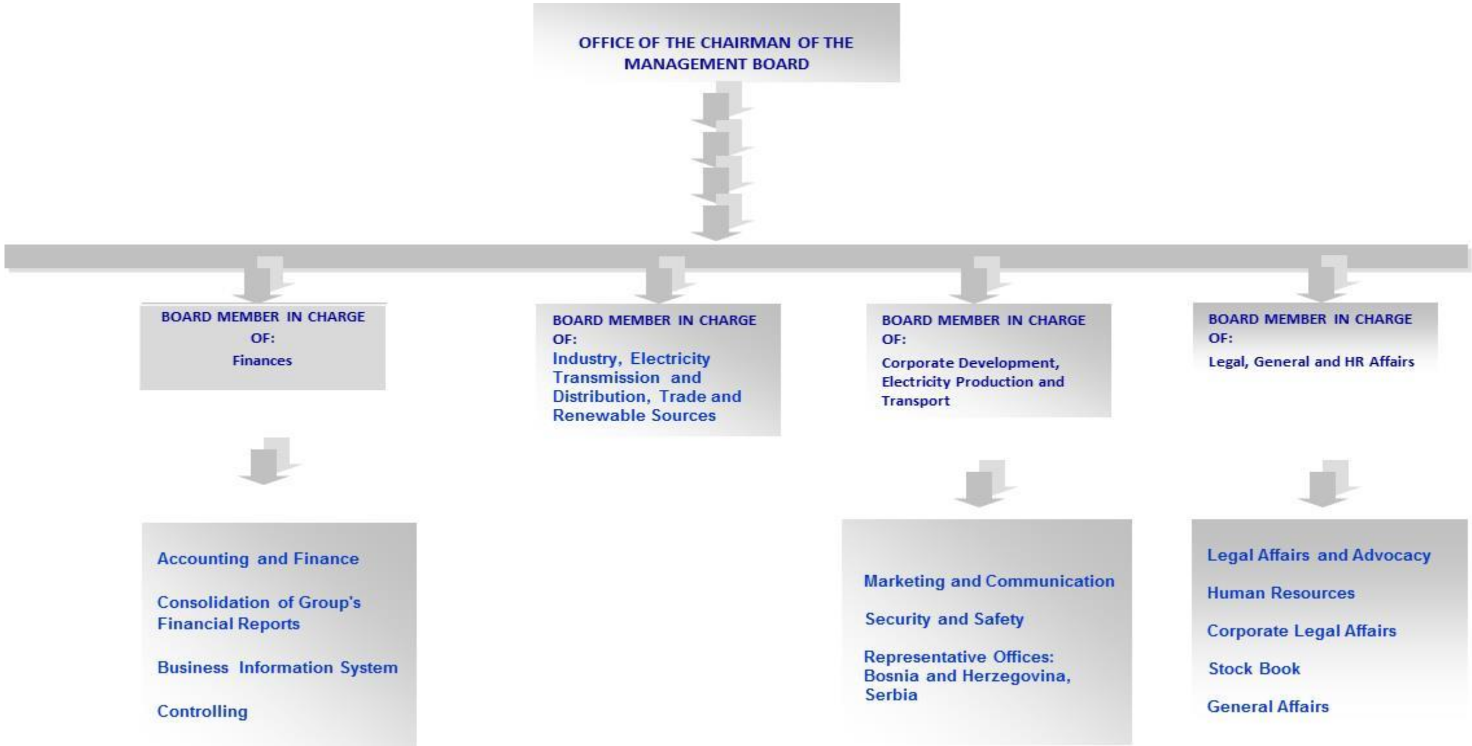
1. PERFORMANCE INDICATORS FOR THE PERIOD 2015 - 2017

-					in HRK 000
	2015	**2016**	**2017**	**Index 3/1**	**Index 3/2**
	1	**2**	**3**	**4**	**5**
Operating revenue	62,235	54,108	53,421	86	99
Operating expenses	78,533	82,075	79,255	101	97
Profit/loss from operations	**-16,298**	**-27,967**	**-25,834**	**159**	**92**
Financial revenue	82,578	79,229	58,456	71	74
Dividend revenue from affiliated company	48,458	65,277	72,974	151	112
Financial expenses	52,304	51,771	36,521	70	71
Net financial revenue	78,732	92,735	94,908	121	102
Pre-tax profit	62,434	64,768	69,074	111	107
Tax	0	0	0		
Profit for the period	**62,434**	**64,768**	**69,074**	**111**	**107**
No.of employees 31 Dec	**50**	**48**	**48**	**96**	**100**
Non-current assets	1,233,450	1,236,839	1,205,873	98	97
Current assets	392,917	420,765	459,904	117	109
Total assets	**1,626,367**	**1,657,604**	**1,665,777**	**102**	**100**
Subscribed capital	1,208,896	1,208,896	1,208,896	100	100
Reserves, retained profit,					
current year profit	363,509	397,482	435,761	120	110
Total capital	1,572,405	1,606,378	1,644,657	105	102
Long-term provisions	34,444	35,425	3,312	10	9
Short-term liabilities	19,518	15,801	17,808	91	113
Total liabilities	**1,626,367**	**1,657,604**	**1,665,777**	**102**	**100**
EBIT	**62,893**	**64,929**	**69,578**	**111**	**107**
EBITDA	**71,874**	**72,908**	**77,395**	**108**	**106**
Return on equity	**4.0%**	**4.0%**	**4.2%**	**105**	**105**
Earning per share (in HRK)	**24.33**	**25.23**	**26.92**	**111**	**107**

2. ORGANIZATION AND MANAGEMENT

Končar – Electrical Industry Inc. (the Group parent) manages its subsidiaries and affiliated companies.

The Group companies are legally autonomous entities, supervised by the parent which also provides the strategic direction and support through respective Supervisory Boards and General Assemblies pursuant to the Companies Act, the Articles of Association of Končar - Electrical Industry Inc., and of individual companies. Furthermore, the parent company manages a portion of assets which has not been invested in its companies but is directly and indirectly in function of the financial support of sales, products and equipment of subsidiaries as a credit-guarantee potential.



Below is an overview of dependent and affiliated companies including basic information

DEPENDENT COMPANIES	HRK SUBSCRIBED CAPITAL TOTAL	HRK SUBSCRIBED CAPITAL OF THE PARENT	% management OF THE PARENT 31 Dec 2017	% ownership OF THE PARENT 31 Dec 2017
KONČAR-Power Plant and Electric Traction Engineering Inc	50,577,000	50,577,000	100.0000	100.0000
KONČAR-Generators and Motors Inc	107,927,700	107,927,700	100.0000	100.0000
KONČAR-Switchgear Inc	105,033,000	105,033,000	100.0000	100.0000
KONČAR-Distribution and Special Transformers Inc	76,684,800	40,439,400	67.9000	52.7346
KONČAR-Instrument Transformers Inc	18,989,100	11,766,600	99,7700	61,9650
KONČAR-Electronics and Informatics Inc	47,027,280	35,286,420	75,0339	75,0339
KONČAR-Metal Structures Inc	24,645,600	24,645,600	100.0000	100.0000
KONČAR-Electric Vehicles Inc	47,026,800	35,288,700	75,0396	75,0396
KONČAR-Renewable Sources Ltd	130,312,400	130,312,400	100,0000	100,0000
Direct ownership	111,120,000	111,120,000	85.2700	85.2700
Indirect ownership	19,192,400	19,192,400	14.7300	14.7300
KONČAR-Plant Installation and Commissioning Inc	11,827,500	5,288,100	79.0500	44.7102
KONČAR-Small Electrical Machines Inc	41,641,800	41,641,800	100.0000	100.0000
KONČAR-Household Appliances Ltd	17,834,100	17,834,100	100.0000	100.0000
KONČAR-LV Switches and Circuit Breakers Ltd	60,499,300	60,499,300	100.0000	100.0000
KONČAR-Electrical Engineering Institute Inc	40,763,520	40,763,520	100.0000	100.0000
KONČAR-Infrastructure and Services Ltd	49,891,600	49,891,600	100.0000	100.0000
AFFILIATED COMPANY				
KONČAR-Power Transformers Ltd	72,764,000	35,654,400	49.0005	49.00005

Management Board

The Supervisory Board appoints and recalls the Chairman of the Board and Board members. Their term of office is five years with an option of reappointment. Pursuant to the Companies Act and the Company's Articles of Association, the Management Board is held personally responsible for running business operations and in doing so, they are obliged and authorised to take any actions and make decisions deemed necessary for successful Company management. The Supervisory Board's consent is required to make certain decisions defined under said Articles of Association.

The Management Board of Končar – Electrical Industry Inc. consists of the following members:

Darinko Bago	Chairman
Miki Huljić	Board member in charge of Finances
Marina Kralj Miliša	Board member in charge of Legal, General and HR Affairs
Davor Mladina	Board member in charge of Electricity Transmission and Distribution, Industry and Trade
Miroslav Poljak	Board member in charge of Electricity Generation, Corporate Development and ICT
Ivan Tomšić	Deputy Board member in charge of Corporate Development and ICT
Jozo Miloloža	Board member until 5 February 2017, deputy board member until 5 August 2017

Supervisory Board

Pursuant to the provisions of the Companies Act and the Articles of Association of KONČAR – Electrical Industry Inc., the General Assembly reaches decisions on the appointment and recall of the Supervisory Board. The Supervisory Board is responsible for appointing and recalling members of the Management Board and for supervising the Company's operations. Major transactions and business decisions (the amount of such transactions is defined by the Rules of Procedure of the Supervisory Board) require the Supervisory Board's consent.

The General Assembly held on 12 July 2016 adopted a decision on the election of Supervisory Board members as follows:

Petar Vlaić	Chairman
Josip Lasić	Deputy Chairman
Nikola Anić	Member
Jasminka Belačić	Member
Vicko Ferić	Member
Branko Lampl	Member
Joško Miliša	Member
Vladimir Plečko	Member

Members of the Supervisory Board were elected for a period of four years as of 12 July 2016.

Members of the Supervisory Board accepted the proposal for appointing Petar Vlaić the Chairman, and Josip Lasić the Deputy Chairman of the Supervisory Board.

Pursuant to the Audit Act (Article 28) and the Corporate Governance Code, the Supervisory Board has established the Audit Committee. In accordance with the provisions laid down in the Audit Act and the Corporate Governance Code, the Audit Committee is in charge of monitoring the financial reporting procedure, the efficiency of the system of control, supervises the conduct of annual financial statements audits, monitors auditors' independence, makes recommendations to the Supervisory Board and proposes to the General Assembly the election of the audit company for reviewing annual financial statements.

The Audit Committee consists of the following four members:

Vicko Ferić - Chairman
Nikola Anić – Member
Jasminka Belačić – Member
Josip Lasić– Member

At its session held on 28 September 2012, the Supervisory Board established the Strategic Development Committee which is assigned tasks by the Supervisory Board regarding the topics and the activities falling under the remit of the Supervisory Board with a specific emphasis on the long-term viability, risk assessment, Group's strategic priorities, restructuring need and the development of strategic human resources within

Končar Group.

The Strategic Development Committee consists of the following 4 members:

Joško Miliša – Chairman

Branko Lampl - Member

Vladimir Plečko – Member

Petar Vlaić – Member

3. CORPORATE GOVERNANCE PRINCIPLES APPLICATION

The Management Board of KONČAR-Electrical Industry Inc. and its Supervisory Board adopted the principles of corporate governance based on the positive regulations of the Republic of Croatia and the adopted international standards at their sessions held on April 7, 2008 and August 17, 2008, respectively. The principles are publicly available on the web site of the company (www.koncar.hr) and the official website of the Zagreb Stock Exchange (www.zse.hr).

The corporate governance principles are defined and refer to:

- accountable management,
- definition of corporate governance procedures based on adopted recognized international standards, and
- supervision of business operations, all for the purpose of establishing high corporate governance standards and the transparency of operations as the groundwork for protecting the shareholders, investors and other stakeholders, as well as for caring for the employees, the sustainable development and environmental protection.

The formal questionnaire including replies to which provisions of the Zagreb Stock Exchange Code and the HANFE Company are implemented by the Company is available on the official website of the Zagreb Stock Exchange (www.zse.hr) and on the Company website (www.koncar.hr). The Company applies a majority of the provisions of the Corporate Governance Code with the exception of only certain provisions that the Company does not consider should be applied in the prescribed form, in particular:

- A nomination and reward committee has not been established. The appointment of new Management Board members as well as the key management is carried out in a well-organized manner.
- The remuneration of the Company Management Board members / Directors has been set under the Decision of the Management Board of KONČAR - Electrical Industry Inc. It is based on clearly defined business operation-related criteria including achieved performance, plan realization, consolidated plan realization, EBITDA, signed contracts.
- The remuneration of the Management Board of KONČAR - Electrical Industry Inc. is set under the Contract on Rights and Obligations signed by the MB Chairman and members with the Supervisory Board Chairman. The award is considered to

be an appropriate position of the Company and its results. Information on the overall revenue and fees of the Management Board members and directors is disclosed in the annual report.

- No internal control committee (department) has been established.
- KONČAR - Electrical Industry Inc., as a parent of the Group of Owned Associations that are autonomous in conducting legal transactions, has successfully established, maintained and developed a Business Information System that facilitates a coordinated current and strategic planning of business and development, members and the parent of the Group. It controls the implementation of plans, deviations in their delivery, search and analysis of said deviations, enables the analysis of resource efficiency, cost control, risk assessment and risk mitigation measures, preparation of consolidated financial statements and financial reports for the public (ZSE, banks, Tax Administration and Financial Statements Registry).

  For a number of years, all KONČAR companies' financial statements have been audited by independent auditing companies, which has further contributed to the maintenance and development of a reliable and transparent business system. A majority of KONČAR's companies have adopted the International Standard ISO 9001 under which each process is described and set according to relevant procedures and documents, as well as subject to a regular check by authorized certification companies. All business events and processes are documented and controllable.

  The management of these companies and their financial statements are the responsibility of respective companies' management boards. KONČAR - Electrical Industry Inc. as a parent, manages the Group's business policy, decides on long-term development goals and strategies, adopts business and development plans, coordinates and supervises the operations of subsidiaries through the Supervisory Boards, in compliance with statutory regulations, company's Articles of Association and Management Board's decisions as well as the adopted Corporate Governance Code.

  Internal Business Controls have so far been organized and implemented periodically and in accordance with the decisions of the Supervisory Board. KONČAR - Electrical Industry Inc. as a parent of the Group has no significant legal transactions with third parties (except in credit-guarantee operations). All material decisions are made by the Management Board. Prior to the execution of the decision, the members of the Management Board in charge of the areas liquidate the accounts. All process controls are carried out according to prescribed procedures. We believe that documentation, control and business transparency is ensured by the consistent implementation of and compliance with prescribed procedures.

  The activities regarding the formal establishment of the internal control and the audit department commenced in late 2017.

The Company believes that the non-implementation of some of the provisions of the Code does not undermine the high level of transparency of the Company's business operations and will not have a significant adverse effect on current and potential future investors in making their investment decisions.

A 64-question questionnaire contains precise answers to questions on the provisions of the Code which are applied by the Company and which are publicly available on the official web pages of the Zagreb Stock Exchange (www.zse.hr) and the Company's web site (www.koncar.hr).

Within the framework of its organizational model of operation within which all business processes are taking place, the Company has developed internal control systems across all important levels. These systems facilitate, among others, the objective and correct presentation of financial and business reports.

Data on significant shareholders is available daily on the official web site of SKDD (www.skdd.hr). As of 31 December 2017 and 2016, said data is also disclosed in the Financial Statements with the Independent Auditor's Report. Electronic voting is available to shareholders in attendance at the General Assembly.

The adopted Corporate Governance Principles are based on responsible management; they define corporate governance procedures based on adopted recognised international standards and the operational supervision. The underlying purpose is to establish high corporate governance standards and the transparency of operations as the groundwork for protecting the shareholders, investors and other stakeholders, as well as for caring for the employees, sustainable development and the environmental protection.

4. BUSINESS RESULT

Končar – Electrical Industry Inc. generated total revenues of HRK 184.9 million and incurred total expenses of HRK 115.8 million in 2017.

The profit earned in 2017 was in the amount of HRK 69.1 million, which was by 6.6% more than in 2016. The Company was exempt from paying the corporate tax in 2017 due to deductible items of dividend income from related companies and the affiliate which tax had already been paid by the subsidiaries.

Total operating revenue for the period January-December 2017 of HRK 53.4 million included the fee for using the corporate name, brand and trade mark, income from lease and the fee for costs incurred by joint marketing activities.

Total operating expenses amounted to HRK 79.3 million. They included the cost of material, energy and services in the total amount of HRK 39.7 million, cost of staff of HRK 21.4 million, depreciation of HRK 7.8 million, other operating costs of HRK 9.4 million in total, and provisions of HRK 1 million.

Other operating costs of HRK 9.4 million in total are mainly allocated to fees paid to Supervisory Board, Audit Committee and Strategic Development Committee members, royalties and temporary service contracts, sponsorships and donations of HRK 5 million in total, insurance premiums of HRK 0.8 million, daily allowances and travel expenses of HRK 0.8 million. Other costs (administrative costs, performance-free taxes, banking services, membership fees and other costs) amounted to HRK 2.8 million.

Financial revenues amounted to HRK 58.4 million. They included dividend revenue from the allocation of profit generated by related companies of HRK 47.4 million, income from interests in time deposits, domestic loans, positive financial income from foreign exchange gains and long-term receivables of HRK 11 million.

Financial revenues from the affiliated company's dividend amounted to HRK 72.9 million.

The major part of financial expenses of HRK 36.5 million was allocated to the value adjustment of shares in the affiliated company in the amount of HRK 28.2 million, foreign exchange losses from unrelated companies of HRK 7.8 million, and interests of HRK 0.5 million.

5. FINANCIAL POSITION (BALANCE SHEET)

The overall asset value of Končar-Electrical Industry Inc. amounted to HRK 1,665.8 million on 31 December 2017, a 0.5% increase by HRK 8.2 million compared to 31 December 2016.

Non-current asset amounted to HRK 1,205.9 million, a 2.5% decrease of HRK 31 million. Current asset and pre-paid costs of HRK 459.9 million showed a 9.3% increase of HRK 39.1 million compared to 31 December 2016.

As of 31 December 2017, total equity with reserves amounted to HRK 1,644.7 million, which was a 2.6% increase of HRK 38.3 million compared to 31 December 2016.

HRK 3.3 million in long-term provisions showed a decrease by HRK 32.1 million compared to 31 December 2016. Said decrease was the result of cancelling provisions for legal costs in a dispute with Elektrotehnička škola (Electrotechnical School) and Strojarsko tehnička škola (Secondary Technical School of Mechanical Engineering) of HRK 31.8 million for determining and filing the corrected LR entry of ownership at Konavolska ulica in Zagreb. As the legally valid court decision found that the above said schools were property owners, the need for long-term provision ceased.

As of 31 December 2017, short-term liabilities amounted to HRK 17.8 million, of which HRK 9.6 million was allocated to liabilities payable to related companies. Liabilities payable to unrelated suppliers of HRK 2.4 million increased by HRK 1.5 million. A major portion of said liabilities was non-current (HRK 2.2 million). Other short-term liabilities of HRK 5.2 million included payroll, tax and contribution as well as other liabilities.

Potential liabilities of Končar-Electrical Industry Inc. for total guarantees issued as of 31 December 2017 amounted to HRK 439.5 million, a decrease by HRK 111.8 million compared to 31 December 2016.

Performance guarantees accounted for HRK 301.5 million of total and joint guarantees.

6. RESTRUCTURING

The Management Board of Končar-Electrical Industry Inc. with the consent of the Supervisory Board has been continuously involved in the process of operational restructuring in order to ensure Group's market position, profitability and its further development.

During 2016, the Management Board, with the consent of the Supervisory Board, made the decision on conducting a business analysis with the aim of increasing the synergy effects in KONČAR Group. For the purpose of the analysis, the Boston Consulting Group was commissioned to work with the representatives of KONČAR in identifying operating rationalization and optimization measures and improving the Group's market position. Said analysis was completed in 2017 and presented to the Company Supervisory Board in the form of the document titled 'The Analysis of Business Operations aimed at Increasing the Synergy Effect in Končar Group'.

One of the recommendations presented by the consultants was to merge the switchgear and medium- and low voltage apparatus companies (Končar-Switchgear, Končar-Medium Voltage Apparatus and Končar-High Voltage Switchgear).

The Management Board of the parent launched the activities regarding said merger. The process was completed on 29 December 2017. Said merger of those three companies was aimed at achieving a major synergy effect by coordinating market presence, a more efficient development of new products, and reducing operating costs.

As per previously defined Gantt chart, the activities connected with the investment in the Metal Processing Center continued in 2017 in Končar-Metal Structures having adopted the findings of the Boston Consulting Group findings.

The Digital Transformation Programme, consisting of a number of projects which aim is to change the method of operations in key segments and production units, commenced in 2017. The training course for the management structures in KONČAR Group companies was organized to inform them of the importance, possibilities and objectives of said project, which would be conducted in several phases in cooperation with relevant partners for individual areas and based on the implementation of new production and business process technologies.

7. RISK EXPOSURE

KONČAR - Electrical Industry Inc. as the parent of the Group has no significant legal transactions with third entities (apart from credit-guarantee operations) and is to a lesser extent exposed to financial and market risks.

KONČAR - Electrical Industry Inc. manages the risks of the company, issues policies, coordinates and directs the risk management in related companies. A management board of each dependent entity controls the risks of its company in KONČAR Group. The operational, developmental, market and financial risks are systematically taken into account when developing, adopting and controlling the implementation of business and development mid-term, annual and operational plans.

Currency risk

The Company is exposed to currency risk through sales, foreign currency purchases and loans denominated in a currency other than the functional currency of the Company. Euro is the currency primarily subject to risks. Since the exchange rate of kuna is to some extent related to the euro exchange rate, the Company is limited to the currency risk of deposits in euros.

Liquidity risk

Liquidity risk is the risk of the Company not being able to meet its financial obligations as they fall due. The liquidity risk management is the responsibility of the Management Board which has built a quality framework for covering short-term, medium and long-term financing schemes as well as all liquidity risk-related risks. The Company manages this risk by continuously monitoring the projected and existing cash flow, comparing and adjusting it to due revenues and expenses. There was no significant exposure to liquidity risk because it has the ability to quickly cash out funds that are considerably higher than potential liabilities.

Capital risk management

The Company manages its capital by ensuring its operation and development as a going concern while efficiently managing its assets.

It manages its capital and makes appropriate adjustments in accordance with market economic conditions and its asset risk characteristics. In order to adjust or maintain its capital structure, the Company, with the consent of appropriate bodies, can make a decision if the retained earnings should be distributed to shareholders, the equity increased or decreased, the assets sold in order to decrease liabilities and similar.

Credit risk

Apart from deposits in commercial banks and in-house claims, the Company has no significant claims from third parties. Therefore, no credit risk exists.

Interest rate risk

The Company is not exposed to interest rate risk because it is not exposed to debts. As it has a good financial asset structure and has no interest-bearing liabilities in relation to third parties, it is not exposed to interest rate risk.

8. SHARES

The shares of KONČAR - Electrical Industry Inc. are quoted in the Official Market of the Zagreb Stock-Exchange. The shares are recognisable under their KOEI-R-A ticker. In keeping with the positive regulations, the Company ensures regular access to information on its operations and activities as well as information on facts and circumstances that may bear influence to the share price (price sensitive information).

The Company's share capital is HRK 1,208,895,930.00 and consists of 2,572,119 ordinary shares with a nominal value of HRK 470.00.

The Company applies the same conditions to all its shareholders and treats them equally regardless of the number of shares in their possession, their country of origin and other properties. The voting rights encompass all of the Company's shareholders in that the number of votes they are entitled to at the General Assembly equals the number of shares they have in their possession.

In 2017, the price movement of KONČAR Electrical Industry shares followed the overall market trend. The highest share price was recorded in February 2017 (HRK 870.00), and the lowest in October (HRK 660.03). Until the end of 2017, the average price of the share was HRK 714.95.

The total turnover of KONČAR share amounted to HRK 68.5 million, which was by 14 million kuna less than the achieved turnover in 2016 except for the turnover recorded in early June 2016 when the Mandatory Pension Funds of the Republic of Croatia purchased 526,926 shares worth HRK 360 million from the Restructuring and Sale Center in the value of HRK 360 million.

The overall number of shares traded was 88,655 (28% less compared to 2016 if the above stated transaction is excluded).

Market capitalization is HRK 1,834.7 million, which was by HRK 64 million or 4% more compared to the recorded in 2016.

KONČAR – Electrical Industry Inc. signed a contract for the performance of specialist jobs with InterCapital Securities Inc. in October 2015 under which InterCapital Securities Inc. took over the obligation to perform specialist jobs for the shares of KONČAR – Electrical Industry Inc, labels: KOEI-R-A, ISIN: HRKOEIRA0009, included in the Official Market of the Zagreb Stock Exchange Inc.

The specialist trade service includes a simultaneous display of purchase orders and orders for sale of the company shares in accordance with the Rules of the Zagreb Stock Exchange. Said contract is renewed annually.

As of 31 December2017, the Company owned 5,861 shares, accounting for 0.23% of the company's equity.

The Company's ownership structure is as follows:

	Shareholder	31 December 2017 No. of shares	31 December 2017 Ownership stake %	31 December 2016 No. of shares	31 December 2016 Ownership stake %
1	HPB d.d. (Kapitalni fond d.d.)	724,515	28.17	724,515	28.17
2	ADDIKO BANK d.d./PBZ Croatia Osiguranje OMF	420,928	16.37	420,928	16.37
3	SOCIETE GENERALE / AZ OMF	377,429	14.67	377,429	14.67
4	SOCIETE GENERALE - Splitska banka d.d./ Erste Plavi mandatory pension fund	359,239	13.97	359,239	13.97
5	RESTRUCTURING AND SALE CENTER/REPUBLIC OF CROATIA	83,610	3.25	57,982	2.25
6	FLORIČIĆ KRISTIJAN	50,714	1.97	50,714	1.97
7	ADDIKO BANK/RBA OMF	47,636	1.85	48,291	1.88
8	ZAGREBAČKA BANKA D.D. /AZ PROFIT VOLUNTARY PENSION FUND	32,803	1.28	28,928	1.12
9	PBZ d.d. /collective client custodian account	24,251	0.94	29,050	1.13
10	ZEC BRANISLAV	22,843	0.89	22,843	0.89
11	Other shareholders	422,290	16.41	446,339	17.35
12	KONČAR d.d. (treasury stock)	5,861	0.23	5,861	0.23
		2,572,119	**100.00**	**2,572,119**	**100.00**

9. EMPLOYEES

The starting point of KONČAR’s strategy is that its employees constitute the company’s core asset, and that the entire operation depends on the participation of each and every employee. This resulted in KONČAR's decision to base its competitiveness on the experience, knowhow and innovativeness of the staff.

As of 31 December 2017, the Company had 48 employees (the number remained unchanged compared to 31 December 2016).

As KONČAR adheres to the principle of equal pay for work of equal value, there are no recorded cases of gender pay, position, bonus, advancement opportunities or any other work-related status gap.

As KONČAR attaches great importance to respecting human rights in conducting its operations, no issues were recorded in this area. As a socially responsible company which respects human rights, KONČAR does not support child work, nor implements mandatory or forced labour in any of its business activities or forms.

No case of racial, skin, gender, religious, political, national or social origin discrimination was recorded during the reporting period. Under the provisions of the Collective Agreement, the Employer has undertaken to protect employee dignity in the course of his/her work, and to ensure work conditions in which said workers will not be exposed to sexual and non-sexual harassment by the Employer, managers, colleagues, or other persons with whom said worker comes in regular contact in the course of his/her work.

All KONČAR employees are entitled to a freedom of association and collective bargaining. KONČAR employees may choose to become members of either the Union of Metalworkers of Croatia or the Union of Electrical Industry Workers of Croatia.

KONČAR has set up in-house mechanisms for obtaining advice regarding ethical and legal behaviour as well as issues related to the organisational integrity. General responsibility has been assigned to the Board member in charge of Legal, General and HR Affairs and (depending on the size of respective KONČAR Group company) to works councils, trade union commissioners and/or persons in charge of HR.

There are also mechanisms in place for making requests not related to the organization including regional trade union commissioners, State Inspectorate Office and labour inspectorate.

The employee structure is as follows:

	31 December 2017	31 December 2016
PhD	1	1
Masters of science	5	5
University degree	30	29
Polytechnic degree	8	9
High school degree	3	3
Primary education	1	1
	48	**48**

10. QUALITY, ENVIRONMENT, SECURITY OF PEOPLE AND INFORMATION

An integral part of KONČAR's business policy includes reaching client satisfaction through the delivery of high quality and reliable products, environmental and health protection, as well as safety of employees and the security of information. These policies are implemented across the Group by the application and certification of the management systems as per the requirements of the international ISO 9001 standard for Quality Management, ISO 14001 for Environmental Management, OHSAS 18001 for Occupational Health and Safety Management, ISO/IEC 27001 for Information Security Management, and ISO/IEC 50001 for Energy Management.

The ISO 9001 Quality Management System is certified in 15 Group companies. The core purpose of the system has to do with the management of key processes that affect the quality of products or services aimed at reaching the client satisfaction. The ISO 9001 Certificate, issued by authorised independent certification institutions, provides clients with a degree of assurance concerning the capacity of an organisation to meet their demands. More and more however, and especially during the prequalification process for contracting certain products, buyers audit their counterparties i.e. they carry out on-site verification of the quality of management system operation in order to be sure of the Company's capacity to deliver on their requirements and expectations.

The ISO 14001 Quality Management System is certified in 16 Companies. By applying this system, Companies continuously monitor and analyse various aspects of the environment while performing their business activities, carrying out their processes, looking into the environmental impact of products and services they delivered, and taking adequate measures to mitigate any adverse effects. The ISO 14001 Certificate is issued by authorised independent certification institutions, which renders assurance to all stakeholders, ranging from central governments to local communities, of the Company’s responsible behaviour towards the environment.

The OHSAS 18001 Occupational Health and Safety Management System is certified in 9 Companies. By applying this system, Companies have been continuously monitoring and analysing work place hazards and conducting measures for the prevention and mitigation of accidents which might lead to the loss of health and life as well as the loss of material goods. The OHSAS 18001 certificate issued by authorized independent certification institutions renders assurance to all stakeholders of the Company’s conduct of legal and other measures aimed at the provision of safe working environment and work injury protection.

The ISO/IEC 27001 Information Security Management System is certified in 3 Companies. By applying this system, Companies achieve the protection of the information system, property, and business information. The ISO 27001 Certificate issued by Certified Independent Certification Institutes proves that the information security management system provides data protection under the principles of secrecy, integrity and controlled availability, enables information security implementation and reduces the risk of possible fraud, loss of information or unauthorized disclosure of information, improves organization’s credibility and opens up business opportunities for cooperation with customers aware of security needs.

The ISO/IEC 50001 Energy Management System is certified in 2 Companies. By applying this system, Companies shall achieve an ongoing improvement of energy management, better resouce and infrastructure utilization, and lower energy consumption i.e. lower costs while limiting and controlling environmental impacts.

These principles are based on the positive regulations of the Republic of Croatia as well as on adopted international standards. KONČAR accepts and applies international and local principles, charters and standards which contribute to a better quality of products, work processes and production as well as to the preservation and the improvement of the environment and social surrounding.

KONČAR's business policy is based on:

- satisfaction of its clients, suppliers and other stakeholders;
- protection of environment, health and safety;
- permanent upgrade of products and processes; and
- participation and motivation of all employees.

Environmental issues

The systematic approach generates the policy and objectives of quality management, environment, health and work safety protection, acknowledged by the certificates obtained from accredited autonomous bodies. A number of other standards and norms is applied to individual products as per the requirements specified by customers and users.

The equipment and products made by KONČAR Group for electricity generation, transmission and distribution require a high degree of two-fold responsibility – primarily operational safety and reliability (not to generate additional problems in electricity supply) and the preservation of the environment in which such equipment is installed. Apart from the above, passenger transport must also contain a safety feature as a key characteristic of trams and trains produced in KONČAR along with the major environmental component. As KONČAR Group bears huge responsibility for products it offers on the market, it has been trying to manage the entire production chain by supervising the quality of individual production processes.

KONČAR Group companies cooperate only with the suppliers whose materials and components are harmless to humans and the environment and can be recycled after the end of their life or disposed without jeopardizing people or the environment. The selection of a supplier of respective materials and services is subject to meeting defined quality level, delivery period, payment term requirements as well as taking care of health, work safety and environment protection. Suppliers are required to submit the proof (certificates) of meeting said requirements.

Companies have created databases of the existing and potential suppliers. Apart from basic information (name, address, phone, e-mail, contact person), said database also contains other information which may affect the selection of a supplier such as their references, complaint information, quality system data, health and work safety data, environment protection data.

The issue of the environment is of utmost importance as a major part of the equipment is installed directly in the environment (substations, hydropower plants, other power facilities or traction vehicles). KONČAR has defined the Environmental Management Policy, which is available on www.koncar.hr and which has been communicated to all employees.

The equipment and products supplied by KONČAR meet the highest security standards with the minimum environmental effect, as proved by zero complaints or incidents in this area.

Investors that make decisions on the construction of facilities supplied by KONČAR's equipment must adhere to environmental regulation and standards. Aware of the environmental risk, KONČAR implements the precautinary principle. This is especially important as said products and facilities are often delivered to areas of high biodiversity (rivers, lakes, rural areas). There have been no incidents of the loss of biodiversity due to our products so far.

11. CORPORATE SOCIAL RESPONSIBILITY

KONČAR complies with Corporate Social Responsibility principles in all its segments and production-business processes. Relying on the comprehensive operation principles, KONČAR assumes full responsibility for the activities within the Group as well as in the proactive cooperation with all stakeholders. More information is provided in the Corporate Social Responsibility Report, which 12th consecutive issue is published on www.koncar.com available to all interested stakeholders. The report is prepared in accordance with the UN Global Compact principles and the Global Reporting Initiative guidelines. KONČAR has thus become a part of a small group of Croatian companies that publish such reports.

User safety and keeping the environmental impact to a minimum are priorities of our production facilities and office premises as well as locations on which our equipment and products are used. The process starts with the quality control of raw material, components, production processes and technologies as well as strict exit controls and testings of finished products and plants.

Apart from the work process that encompasses product development, design, production and delivery, KONČAR is trying to reduce adverse environmental impacts by numerous other activities. KONČAR has been organizing volunteering activities on the Earth Day for years, and every year numerous employees become a part of 'Let's Embellish our Environment' drive. This is an opportunity to get involved in the landscaping of one's environment as well as to raise awareness of the need to preserve it, which has been permanently emphasized as one of the topics during meetings with pupils and students who come and visit our companies.

KONČAR is aware that success can only be the result of motivated and educated employees. Therefore, it has been conducting a number of activities in order to improve its business operations as well as work conditions. Especially important is continuous training and education of employees, health prevention and organized recreation. One of the best popular activities is the traditional KONČAR Soccer Tournament. This was its 17th issue with the participation of more than 300 sports fans in 26 teams from 12 KONČAR Group companies. Let us not forget mountaineering, skiing excursions, marathons and amateur sports competitions.

The KONČAR Pensioners' Club is organized for those who have ended their professional careers offering various cultural, health, humanitarian and other activities, while the 'Homeland War Veterans Club' brings together participants of the Homeland War.

Sponsorships of various academic and extracurricular activities for children as well as the social and humanitarian support, as a part of the cooperation with the social community, was successfully continued in 2017. Sponsorships and donations support projects, organizations and activities of the humanitarian, sport, cultural and educational character. Among numerous requests, the advantage is given to youth-related activities, their better and more comprehensive education, achievements in culture, organization and participation in various competitions, stimulation of pupils' and students' excellence, doing sports and recreation. Traditional prizes are awarded to students attending the Zagreb University of Applied Sciences, the Faculty of Mechanical Engineering and Naval Architecture in Zagreb, the Faculty of Electrical Engineering and Computing Zagreb, the Faculty of Chemical Engineering and Technology Zagreb. A special award is presented at the Faculty of Electrical Engineering and Computing for the best doctoral disseration for best scientific achievements with industry applications. On the Day of KONČAR, a donation is awarded to one of selected projects. In 2017, funds were awarded to the Zagreb Computing Association for furnishing new and renovated premises in order to encourage programming talent and creativity in informatics and computing among pupils.

A part of our continuous support is encouraging the work of amateur sports clubs and talented athletes in table tennis, archery, handball, canoe, skiing, basketball, sailing, hockey, soccer, judo, skating, taekwondo and chess. The support provided to several clubs and competitions for the people with disabilities must be highlighted. KONČAR' Chess Club, one of the oldest in Croatia, regularly participates in competitions in various categories as well as organizes a free chess school for the employees' children who continue to play chess and compete in their categories.

12. ANTI-CORRUPTION AND ANTI-BRIBERY POLICY

Members of management boards, employees and busines partners are acquainted with anti-corruption policies and procedures and adhere to the principles of the Code of Ethics in the course of their business operations and everyday activities. KONČAR enjoys the international reputation of a loyal and correct business partner. No cases of corruption have been recorded at Group level.

KONČAR – Electrical Industry Inc. has not made any financial or in-kind contribution to any political goals, directly or indirectly, to the state or a user. KONČAR promotes and executes correct and transparent competition principles across its businesses in dealing with all entities at all locations. No anti-competitive, antitrust or monopoly-related practices have been recorded in the Group.

13. BUSINESS PLAN FOR 2018

The 2018 Business Plan was adopted by the Supervisory Board at its meeting held on 14 December 2017.

In 2018, KONČAR - Electrical Industry Inc. is planning to achieve a positive financial result of HRK 90.4 million. Total revenues and expenses are planned in the amount of HRK 173.4 million and HRK 83 million, respectively.

Total operating revenues and expenses are planned in the amount of HRK 77.4 million and HRK 83 million, respectively.

Financial revenues of HRK 96.1 million are planned including dividend claims based on the 2016 business results of the Group in the amount of HRK 36.9 million, income from the share of the profit of affiliated KONČAR - Power Transformers Ltd. for the period from October 2017 to September 2018 of HRK 56.2 million, interest on time deposits, internal loans and other placements in the amount of HRK 3 million.

14. FUTURE DEVELOPMENT STRATEGY

Končar Group bases its development strategy on its priority task of producing the most complex products for the end customer in its core business, electric power engineering and transport. This includes complex products such as high voltage substations, hydropower plants, wind farms, trams, electric and diesel-electric trains and alike.

The future period is particularly focused on export markets and the presence of Končar thereon with an emphasis on export activities aimed at decreasing a dependence on domestic economic market. Export orientation is recognized as a guarantee of the Group's long-term viability, its profitable and liquid operations.

The strategy is based on the following assumptions and business objectives:

- **Sustainable development** – stronger participation of digital transformation in development of new products and services in core business (energy and tranport)
- **Production** – individual products of high complexity level and value added (tailor made)
- **Product development** – own development in cooperation with scientific institutions and partners
- **Export**- increasing the export/domestic market ratio (up to 60% - export)
- **HR policy** – scholarships, specialist education, scientific education, HR development
- **Synergy** – encouraging and optimizing Group's joint business processes
- **Social responsibility** – stronger participation across the Group
- **Investments** – expanding production capacity of strategic products, optimization of existing resources

Closing remark:

From the reporting date until the date of adopting financial statements, there were no events which might have significantly impacted the 2017 financial reports of both Končar-Electrical Industry Inc. and of the Group, and which publication would be required as a consequence.

Zagreb, 3 April 2018

Chairman of the Management Board
Končar – Electrical Industry Inc.
Darinko Bago

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