



ANNUAL REPORT 2010
Ericsson Nikola Tesla d.d.





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COMPANY INFORMATION

Ericsson Nikola Tesla is a leading regional provider of innovative ICT products, solutions and services in health care, transport, state administration, municipal services and multimedia. It is also Croatia's leading knowledge exporter through its Research and Development activities and Service Delivery Center. Being a member of the Ericsson Group, the Company operates within the Region Western and Central Europe (RWCE). The Company is socially responsible with a strong reputation built on reliability and good relations with all stakeholders – employees, customers, partners, suppliers, shareholders and the wider community. The Company supports sustainable economic and social development by balancing long-term growth and competitiveness in changeable external conditions with a positive economic, social and environmental impact.

VISION

The regional ICT leader and the prime driver in an all-communicating world.

MISSION

To provide innovative ICT solutions that constantly improve people's lives and create new value for both business and society.



L. M. Ericsson
(1846 - 1926)

THE COMPANY
FOLLOWS THE
ENTREPRENEUR STYLE
OF L. M. ERICSSON
AND THE CREATIVE
APPROACH BY NIKOLA
TESLA, THE WORLD
FAMOUS CROATIAN
VISIONARY AND
INVENTOR



Nikola Tesla
(1856 - 1943)



Company Name	Ericsson Nikola Tesla d.d.
Core activity	Provider of modern information and communications products, solutions, software and services
Address	Krapinska 45, HR-10 000 Zagreb Poljička cesta 39, HR-21 000 Split
Phone	Zagreb +385 1 36 53 535 Split +385 21 43 58 00
Fax	Zagreb +385 1 36 53 156 Split +385 21 43 58 34
E-mail	etk.company@ericsson.com
Web site	www.ericsson.com/hr
OIB (personal identification number)	84214771175
Share capital	HRK 133,165,000 *
Shares	1,331,650 registered shares
Nominal share value	HRK 100.00 *
Ownership structure	Ericsson: 49.07 percent, other shareholders: 50.23 percent, treasury shares: 0.70 percent *
Share trading	Ericsson Nikola Tesla's shares (ERNT-R-A) are traded on the Regular Market of the Zagreb Stock Exchange (ZSE).
Giro account	ZABA 2360000-1101235687 PBZ 2340009-1110012058 RBA 2484008-1100331673 ERSTE 2402006-1100414168
President	Gordana Kovačević, MSc
Chairman of the Supervisory Board	Roland Nordgren
Number of employees	1.595 *

* as at December 31, 2010



GENERAL REPORT 2010
Ericsson Nikola Tesla d.d.





Gordana Kovačević, MSc,
President of Ericsson Nikola Tesla d.d.

COMPANY POSITION REPORT



2010 – STABLE OPERATIONS DESPITE CHALLENGING BUSINESS CONDITIONS

The year 2010 was a particularly demanding and tough one. The ICT industry could not avoid the unfavorable trends present in the wider economy, and the impact of this was manifested in a slower than anticipated realization of planned activities and strategic targets. This was especially evident in a slowdown of capital investments by telecom operators, decreased government investments into infrastructure projects within the ICT segment and decreased budget volumes of our business partners and other customers. A decline in orders during 2010 reflects a decrease in volumes from our domestic market, compensated by extended business activities in our export markets, primarily in Belarus and Bosnia & Herzegovina, as well as exports to Ericsson through R&D and other services. A decline in sales during 2010 further reflects the timing of orders booked and the impact of industry component shortages and Ericsson supply chain bottlenecks.

Despite the challenging environment in which we operated, we managed to maintain a good market position, continued to support our customers in modernization of their networks and in the introduction of new technologies and progressed with investments into new strategic projects and market segments. At the same time, we are able to report improved performance in terms of underlying profitability of operations and cash flow from operating activities and have further improved the strength of our balance sheet.

During 2010, the Company was exposed to additional business risk due to the restructuring of the biggest Kazakhstan bank, BTA, which caused the receivables write-off amounting to MHRK 126.5. Excluding this write-off, the Company result shows a net profit increase of 17 percent year-over-year which, in the given circumstances, is a creditable result. It is important to stress that regardless of the complex situation, we managed to collect approximately 60 percent of receivables, which helped us to further strengthen our financial and cash positions in 2010. At the same time, by solving the given case, the Company risk relating to customer financing was significantly reduced.

Throughout 2010, we responded to the challenging business conditions and increasingly strong competition by adapting the organization for new market and technology requirements, as well as to new organizational models and responsibilities within the wider Ericsson organization. Ericsson Nikola Tesla primarily operates within the Region Western & Central Europe but also retains responsibilities in other Ericsson regions, as well as for those segments of business and products which result from development and activities within the Company. The new organization encourages new and innovative ways of working with a common goal to be closer than ever before to our customers, grow business volumes in existing and new segments and drive improved profitability and cash flow.

In cooperation with our strategic customers, a series of ICT projects in Croatia and in our export markets were completed, thus showing that information and communication technologies are a driving force of economic recovery and development of the society as a whole. I would like to underline our activities on existing networks transformation into new generation networks, as well as taking part in preparations for implementing the state-of-the-art technologies in all our markets. We are also witnessing the operators' interest in the 4G mobile communication systems that will provide higher transmission speeds and extended range of services. During the year, we achieved significant results in terms of our responsibilities assigned in the global organization in the areas of Research and Development, Service Delivery Center and other centers of expertise. This segment is constantly growing and today represents 36 percent of the Company's sales revenue.

ICT implementation continues also in a non-operator segment, both in business systems and government administration. ICT solutions, such as e-Health, Intelligent Transport Systems (ITS) and National Security/Public Safety (NS/PS), have a positive impact on operations, human lives and the environment. The best illustration for this is e-Health solution, our recognizable high-tech product. As of informatization of the Croatian healthcare system, another step forward in 2010 was implementation of new functionalities such as ePrescription, eReferral and eBooking. Moreover, Ericsson Mobile Health (EMH), a product aimed at patient remote medical monitoring, won the best innovation award and is commercially available.

In my last year's Company position report I emphasized that innovativeness in everything we do is the key to our future stable operations; only work aimed at creating new values may raise the stakeholders' satisfaction level and contribute to overall progress in the community. Concerning this, I would like to mention our Innovation Management Program, implemented in all Company units, which resulted in almost 1000 various innovative proposals submitted during 2010. Some of the innovative solutions have already been implemented even at the global level. In 2010, we organized Innovation Day in Zagreb and Split, and the most prominent innovators and their best innovations were presented there.

We also marked the tenth anniversary of Ericsson Nikola Tesla Summer Camp, so far attended by almost 300 students, assisted by mentors from the Faculty of Electrical Engineering and Computing at the University of Zagreb and the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture at the University of Split as well as from our Company. Their work resulted in 162 student projects and 82 prototypes.

2010 - STABLE RESULTS

- » ORDERS BOOKED MHRK 1,311.3 (MHRK 1,386.2)
- » SALES REVENUES MHRK 1,218.9 (MHRK 1,400.0)
- » NET PROFIT (EXCLUDING RECEIVABLES WRITE-OFF) MHRK 151 (MHRK 128)
- » POSITIVE CASH FLOW
- » JOBS AND MARKET POSITION MAINTAINED
- » COST AND OPERATIONAL EFFICIENCY
- » HIGH LEVEL OF EMPLOYEE SATISFACTION



In 2010, Ericsson Nikola Tesla yielded the following business results (2009 figures in brackets):

- » Orders booked MHRK 1,311.3 (MHRK 1,386.2);
- » Sales revenues MHRK 1,218.9 (MHRK 1,400.0);
- » Net profit MHRK 24 (MHRK 128.4);
- » Cash flow from operating activities MHRK 366.4 (MHRK 284);
- » Motivational Company culture, confirmed by the annual employee survey Dialog;
- » Customer satisfaction, confirmed by the annual customer satisfaction questionnaire;
- » Satisfaction of shareholders, investors and the general public expressed by the award for transparent business operations and relations with investors offered by the Zagreb Stock Exchange and Poslovni dnevnik, and by the annual Grand PRix by the Croatian Public Relations Association for the Company's 60th anniversary project.

In brief, in 2010 we achieved solid net income and sound cash flow from operating activities. We continued to invest into development projects, preserved our jobs and held our market position primarily as Croatia's leading knowledge exporter.

OUTLOOK

We are approaching a new business cycle aware of the complex and dynamic trends in the ICT industry and e-business.

The telecom market shows a tendency of core network transformation towards the next generation network with introduction of IMS architecture, as well as with the strong development and implementation of mobile broadband networks and next generation of optic access networks. Transformation of the current network will enable further development, delivery and growth of advanced services (such as IPTV, positioning services, etc.), with requirements for advanced convergent billing and charging services and complex network management systems.

Mobile technology broadband access will continue the intensive development primarily due to the growth in number of smart phones and tablets but also due to M2M networking trends. A significant growth of mobile network traffic will demand further extension of HSPA and introduction of LTE technology. By implementation of a broadband access based on HSPA+ (42 Mbps) and LTE trial network, Croatia joined the most developed countries in the world, where already today convergence of fixed and mobile network and achievements of the 4G mobile communication networks are present.

There is no doubt that our operating environment will remain challenging in 2011, so we should focus on further development of our business operations and risk management.

Having assessed operational risks for Ericsson Nikola Tesla in 2011, I would like to point out the following:

- » Serious disturbances in the financial market and their negative impact; operators' investment slowdown regarding network development and decrease in non-operator investments regarding ICT projects;
- » Consolidation among our customers and largest competitors with further impact on product and service prices;
- » Increasing demand for customer financing;

- » Negative impact of a strong HRK and changes in EUR and USD exchange rates;
- » Shortage of industrial components in the world market and supply chain bottlenecks;
- » Natural disasters causing disturbances in production, supply and transport;
- » Continued political uncertainty and instability in some markets.

Ericsson Nikola Tesla is operating in line with the current corporate policies and directives, the Croatian legislative regulations, as well as principles of corporate governance and business ethics.

In the forthcoming period we shall seek to strengthen our position in all business segments and in all Company markets, focusing on new customers and strategic projects. The mission and strategy of Ericsson Nikola Tesla are directed towards key stakeholders: customers, employees and shareholders. It is all about value creation, understanding the needs, sharing knowledge and the partnership among those included in various processes and activities. We shall focus on the three strategic goals: profitable sales growth, healthy margins and cash flow, as well as sales within the Ericsson Group. Innovativeness and a proactive approach towards users of our products and services, constant technology shifts, adjustment to market and competitive conditions are the imperative of our future business development. Ericsson Nikola Tesla is fully focused on achieving long-term, profitable growth whilst ensuring short-term stability and will endeavor to achieve this by making strategic business moves, by fully analyzing and reacting to all business risks, by ensuring optimal utilization and continual development of all its resources.

All other data, which need to be an integral part of the annual Company report pursuant to Article 250 (a) of the Company Act, can be found in the enclosed 2010 Annual Report, comprising the General Report, Social Report and Financial Statements as at December 31, 2010.



Gordana Kovačević
President
Ericsson Nikola Tesla d.d.



BUSINESS RESPONSIBILITIES/ ACTIVITIES

Ericsson Nikola Tesla is a leading regional provider of information and communications technology solutions that, through innovative approach and thought leadership, drives opportunities and creates value together with its customers.

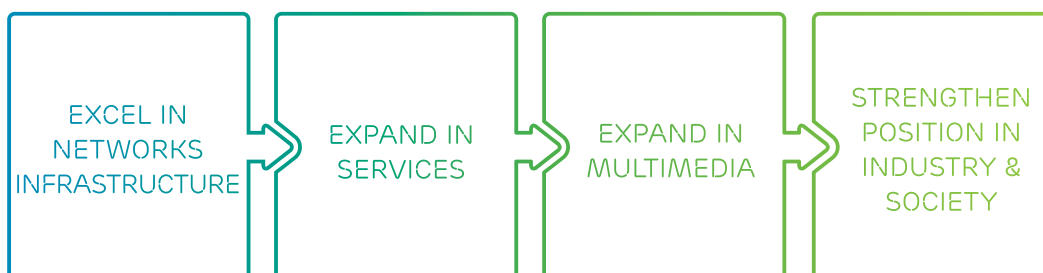
The Company's core business activities include the following:

- » A research and development center;
- » A center for end-to-end communications solutions;
- » A center for service delivery;
- » A center of ICT solutions for industry and society;
- » Marketing and sales of information and telecommunications products, solutions and services.

Ericsson Nikola Tesla:

- » Provides innovative ICT solutions, which improve lives and create new value for business and society;
- » Contributes to the prosperity of its environment by ensuring access to modern information and communication systems and technologies;
- » Works in the area of advanced technology, and plays an active role in e-projects;
- » Is among leading exporters in Croatia, and the largest Croatian exporter of knowledge.

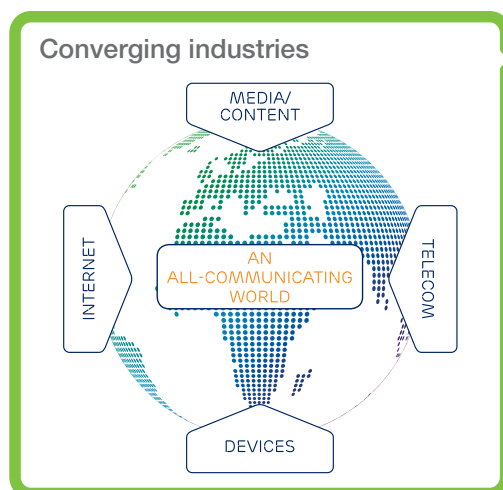
Balancing long-term growth against short-term profitability



PRODUCTS AND SERVICES

Ericsson Nikola Tesla offers its customers and partners a complete portfolio of Ericsson/3PP communications products, solutions and services in the following segments:

- » Leading portfolio for high performance networks;
- » World-class operations and network evolution;
- » Multimedia with leading Business Support Systems, TV solutions and applications;
- » Solutions for selected industry and society verticals.



SALES AND MARKETING

In 2010, our domestic market accounted for 28 percent, export to other countries 36 percent and export to Ericsson markets 36 percent of Ericsson Nikola Tesla's total sales revenues.

DOMESTIC MARKET

Cooperation with leading Croatian operators Hrvatski Telekom, Vipnet and Tele2, was continued in the field of introduction of modern technological solutions and services. Sales revenues are lower than the previous year. Main reasons are stagnation of macroeconomic trends in Croatia and regulatory issues that caused the decrease of operator investments. This emboldened the customer to push for lower prices of products and services. Shortage of components and Ericsson supply chain bottlenecks additionally impacted sales results. Domestic market sales revenues totaled MHRK 340.

Our cooperation with Hrvatski Telekom was primarily focused on the building of backbone networks, broadband internet access, transmission systems and migration of the fixed voice network to a new generation network based on IMS (IP Multimedia Subsystem) architecture. In the 4th quarter of 2010 Ericsson Nikola Tesla and Hrvatski Telekom successfully demonstrated the first LTE trial network in the region and some attractive services supported by this state-of-the-art technology in the mobile communications world (mobile reporter, mobile multiplayer gaming and IPTV-based transmission of HD and 3D TV content over mobile network). LTE technology enables penetration of fast internet access to areas that so far haven't got mobile broadband access. LTE provides downlink data transmission rate of 100 Mbps that is several times higher than in existing commercial mobile network in Croatia.

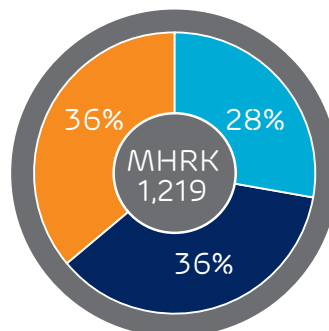
Our cooperation with Vipnet was focused on extension and upgrade of 2G and 3G mobile networks, core networks and transmission systems. In the first half of 2010, after successful demonstration of wireless data transmission at 42 Mbps, it became commercially available to end users in the city of Osijek, and afterwards in other towns and cities across Croatia. Vipnet in partnership with Ericsson Nikola Tesla offered its users HD audio technology that significantly improved speech quality in 3G mobile network.

Our successful cooperation with Tele2, focused on extension and upgrade of 2G and 3G mobile networks, with special emphasis on mobile internet, was confirmed by the extension of the frame agreement on delivery of solutions and services in the first half of 2010. In the fourth quarter of 2010, it was agreed to extend the agreement on managed services.

The main focus in the ICT segment for Industry and society was on upgrading the national ICT primary healthcare system, implementation of cadastre and land registry common information system and

Sales by market in 2010

EXPORT MARKETS ■
DOMESTIC MARKET ■
EXPORT TO ERICSSON ■



upgrade of the Croatian Railways infrastructure. Ericsson Mobile Health (EMH) for patient remote monitoring is commercially available and, together with Ericsson, marketing and sales activities have commenced.

EXPORT MARKETS

In export markets (except for Ericsson market), sales revenues totaled MHRK 434.

In the regional markets (Bosnia and Herzegovina, Montenegro and Kosovo), sales revenues totaled MHRK 202. Although sales revenues are lower than last year, which was the result of project implementation dynamics, orders booked in Bosnia and Herzegovina and Montenegro increased year over year by 18 percent and 15 percent respectively.

The Company signed a two-year Support and Maintenance Agreement with BH Telecom for their entire network. In addition, several big contracts were concluded for extension and upgrade of 2G and 3G mobile networks, upgrade of BH Telecom's core network, and upgrade of their fixed network by introduction of a new generation network node and integration of the network management system.

At the beginning of 2010, Montenegro operator Crnogorski Telekom and Ericsson Nikola Tesla made the frame agreement to define cooperation in the field of modern software solutions for mobile systems over the next four-year period. In addition, deals were agreed for providing support services, upgrade of fixed network, extension of 2G and 3G mobile networks (including implementation of HSPA+ solution) and design of Disaster Recovery Site Solution.

The Company continued cooperation with Kosovo mobile operator Ipko that started with the integration of entire GSM network. New deals were made for the supply of hardware and software support services over the next three-year period.

Sales revenues in the CIS markets totaled MHRK 233. Orders booked and sales revenues increased in this market segment first of all owing to the growth of volume of business in the Belarus market. Business deals were made with a leading Belarus mobile operator Velcom for extension and upgrade of 2G mobile network, and with fixed network operator Beltelekom in the field of internet technology.

In markets of the Russian Federation, Moldova, Georgia, Kazakhstan and Uzbekistan the Company made new contracts for supply of fixed network solutions as well as supply of IP-based solutions for business users.

EXPORT TO ERICSSON

In 2010, the Ericsson market continued to grow and sales revenues totaled MHRK 445.

The Research and Development Center designed a new generation of mobile network servers (MSC R 14.1) and they were in trial operation at several operators around the world. Ericsson Nikola Tesla experts significantly contributed to a successful trial operation.

A new responsibility for fixed network server product lines (TSS) was granted to Ericsson Nikola Tesla R&D Center. New responsibilities were also granted for the Integrated Site (IS) verification and maintenance, broadband access network (GPON) verification and integration. Preparations were made for a serious expansion of R&D activities for the Connectivity Packet Platform (CPP).

Experts from the Service Delivery Center were engaged in a number of projects, such as IMS Deutsche Telekom NGF (largest IMS project in the Region Western & Central Europe, including a complete migration of the Deutsche Telekom fixed network from PSTN to IMS), LTE project for Vodafone Germany and Vodafone Great Britain, T-Mobile Hungary 3G mobile network Audit and Optimization project, IPTV project for Telecom Austria and Transport Network Managed Services project for Mobistar Belgium.

SCIENTIFIC AND RESEARCH ACTIVITIES

In 2010, Ericsson Nikola Tesla's R&D Center has developed and released new products within new generation of Mobile Softswitch Server. Contribution of Ericsson Nikola Tesla's teams and their products within this global project were significant. R&D responsibility for Telephony Softswitch solutions and product line for fixed networks was implemented. This provides Ericsson Nikola Tesla with the possibility to take a significant role in operator's network transformation on the global level. Technology transfer project for integration and verification activities in the area of fixed network broadband access products started. Expansion of the development activities within platform for radio network systems has been completed and prepared for implementation.

Through the collaboration with other research groups in Ericsson, our team has built competences further as well as discovered new areas. In the xDia project, an evaluation of Bridgepoint executable UML tool was made. The tool enables model driven development (MDD) and the main goal of the project was to evaluate the BridgePoint tool in a geographically distributed development project. The xDia team was distributed in three locations: Budapest, Zagreb and Split. Results show that the selected tools can be used in distributed environment during standard design phase.

CARE was a joint project between Ericsson Research and Ericsson Nikola Tesla, which had a goal to provide prototype of multiple e-Health services through one integrated platform. The project also aimed to utilize and promote Ericsson's Mobile Health solution. The solution was built around Ericsson Composition Engine, delivering e-Health and m-Health applications. In 2011, the efforts on this project will continue with much bigger staff and even more ambitious goals.

A very successful cooperation through common research projects with the University of Zagreb, Faculty of Electrical Engineering and Computing, occurred in the area of machine-to-machine communications. Successful demo application was made, with the investigation of IP traffic domain especially for the testing purposes and substitution of some very expensive equipment currently used. Additionally, we worked together to explore the possibility of using Integrated Multiprotocol Network Emulator/Simulator (IMUNES) in the Company's testing domain to replace some additional investment in equipment for fulfilling basic network routing by using a virtualized environment. The results were very promising and we have started to use it in testing a customized solution of the toolset.

10 years of Summer Camp



**EXAMPLE OF
SUCCESSFUL
COOPERATION
BETWEEN
INDUSTRY AND
UNIVERSITY**

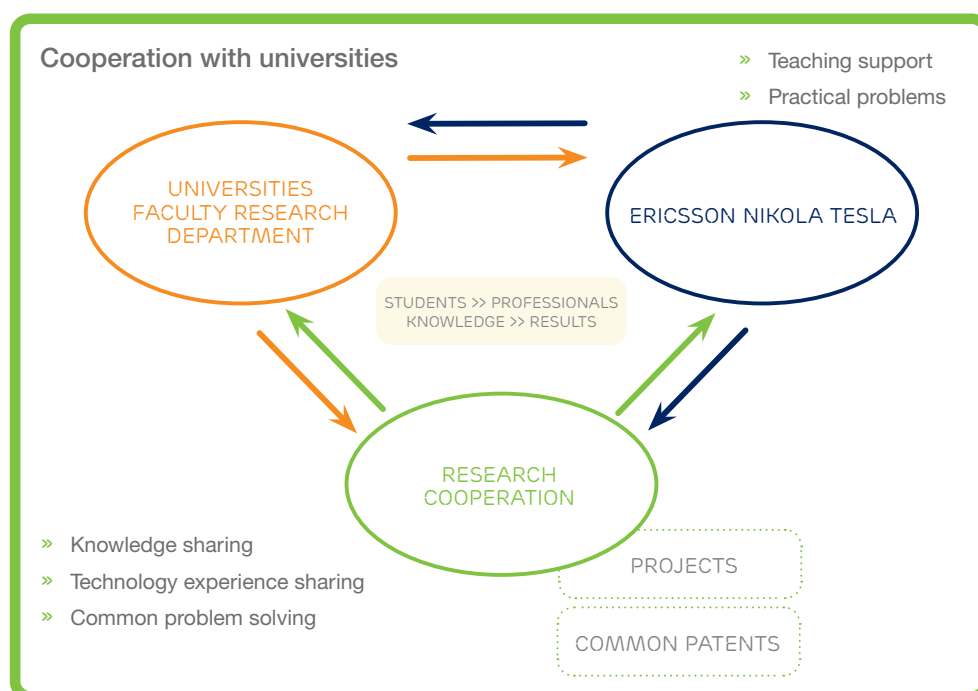
- » 3 Rector's Awards
- » 30 co-authored articles published
- » 7 PhD holders (participants)
- » 7 PhD holders (Company mentors)
- » 16 doctoral dissertations in the final phase
- » > 150 diploma theses correlated to work in the Camp

Our successful and fruitful cooperation with leading Croatian universities continued also this year through several research projects and common activities. An important point of 2010 cooperation was the 10th jubilee Summer Camp, which was again organized in cooperation with the Faculty of Electrical Engineering and Computing (FER), at the University of Zagreb, and the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture (FESB), at the University of Split. In the last ten years, almost 300 students passed through these activities resulting in a number of successful projects.

This particular tenth Summer Camp 2010 was held under the title "In Use Tomorrow: Advanced Applications and Useful Demos". The goals were to study selected problems relevant for the active research and development projects within Ericsson Nikola Tesla, as well as work on applications for future use within the Company. The general idea was to propose innovative solutions and prototype applications, but also improving the existing ones, with an active involvement of students in research. Covered areas included: software engineering methods and tools, e-Health and m-Health related research, as well as other selected topics of special interest to Ericsson Nikola Tesla (e.g. adding new functionalities to some locally used applications and customer demo development), which have emerged from a selection of ideas submitted to the Company's Innovation Management System.

A very important constant in research activities was participation in EU funded projects. Project "Quality Impact Prediction for Evolving Service-oriented Software" (Q-ImPRESS) finished in 2010, and the goal was to provide methods and tools which will allow developers, users and maintainers to foresee the impact of design decisions and evolutionary changes to the system, not only on its overall quality of service, but also on its internal quality properties such as maintainability. Our team was responsible for requirements collections and building a demonstrator, which was used to validate methods and tools, built in the project. This project received very positive feedback from the EU project commissioner for achieved results and overall project execution.

The effort and responsibility of our experts in the previous EU projects (e.g. MPOWER) were recognized and that was the trigger for an invitation for the new project called universAAL – "UNIVERSal open platform and reference Specification for Ambient Assisted Living". The main objective of the universAAL project is to make it technically feasible and economically viable to conceive, design and deploy innovative new Ambient Assisted Living (AAL) services. The project started in February 2010.



BENEFITS OF MODERN INFORMATION AND COMMUNICATIONS TECHNOLOGIES

Ericsson Nikola Tesla is a part of the Ericsson global corporation, and shares a joint vision of communications available to all, and the belief that technology is to enhance the quality of life. By participating in providing various benefits for individuals and a society as a whole, and by rational use of natural resources and energy, the Company improves its own performance and every day contributes to the whole economy.

Ericsson Nikola Tesla offers innovative ICT solutions, thus making available state-of-the-art technologies that support mobility and availability by using broadband access, networking and sustainability.

RAPID DEVELOPMENT OF MOBILE COMMUNICATIONS

As announced in 2007, some 20 years were needed for Ericsson to install as many as one million base stations, and three years only for the delivery of another million. So, in 2010 the two millionth base station was delivered.

Ericsson plays a leading role in implementation of mobile broadband access and has delivered the majority of HSPA networks operating at the rate of 14.4 Mbps, and even more. Ericsson mobile network equipment interconnects more than 1.5 billion people worldwide. The driving force behind that speed increase was Ericsson's energy efficient base station RBS 6000, which supports GSM/EDGE, WCDMA/HSPA and LTE technologies in one package.

RBS 6000 series requires only 25 percent of the footprint used by former generations, with more than 10 times larger capacity, and 20 to 65 percent lower energy consumption, if compared to earlier Ericsson base stations.

LTE TECHNOLOGY

At the end of October 2010, Ericsson Nikola Tesla and the Croatian telecommunications provider Hrvatski Telekom demonstrated, for the first time in live in Croatia, the implemented LTE (Long Term Evolution) trial network. Thus, Croatia joined the group of countries pioneering in the world by implemented state-of-the-art LTE technology.

The data transmission speed via LTE network is some ten times higher than via current mobile networks commercially operated in Croatia. LTE technology provides efficient use of frequency range and enables the cost effective extension of fast internet access to areas uncovered so far by the mobile broadband access.

Even a year before this event, Ericsson Nikola Tesla was the first in Croatia to demonstrate LTE technology in Zagreb to its customers, partners and general public, as a part of Ericsson world tour. It is to underline that Ericsson Nikola Tesla, through its experts working at R&D centers in Zagreb and Split, actively participated in the global LTE and IMS (IP Multimedia Subsystem) development.

LTE enables high transmission speeds, and the IMS subsystem provides the same features and line of services, regardless of the network used and user device applied. Thus, the mobile and fixed network convergence becomes a reality.

Besides the impressive speeds, LTE guarantees high quality of data transmission and also offers a real base for numerous multimedia services that will be soon available in everyday life. While demonstrating the first LTE trial network in Croatia, the public was presented three new services, which were previously unavailable: mobile reporter, multiplayer gaming and 3D TV content transmission via a mobile network.

The mobile reporter provides a simple TV content transmission at the top quality level, directly to a studio, in a wireless mode with no satellite links leased in advance. This is also a strategic shift, as the media industry is concerned, since it will require a completely new way of thinking and new business approaches as well as redefinition of spectators' role. They will no more be only passive TV users.

The development of wireless broadband networks and services has been widely influenced by users' requirements and ideas. Even today, fast and efficient data communications worldwide is no more dependent exclusively on fixed lines. But in the future, wireless computer gaming will be available in multiplayer mode, with the top response quality from all points covered by LTE network.

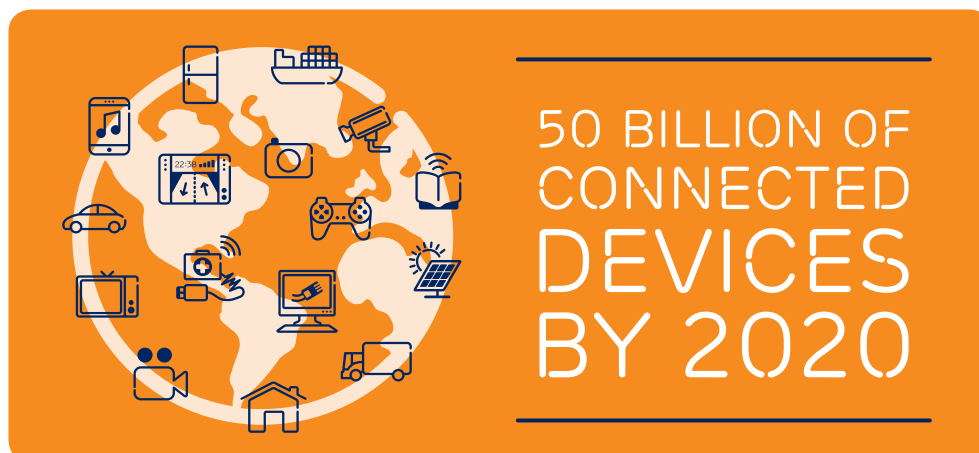
With the LTE network, users will no more be deprived of high-quality TV content, and not even of 3D programs in places such as marinas or in hardly accessible spots, which are not provided with fixed telecom network. Although 3D TV requires, for example, twice as large transmission capacity for the transmission of the same resolution content in 2D technology, just LTE transmission of 3D TV content is one of expected applications of network convergence, which by introducing the next generation of mobile technology will achieve a new dimension.

Ericsson plays a key role in LTE technology development, from the initial research cooperation to the final standard. So far, the corporation commissioned 16 LTE networks in 11 countries in three continents.

At the gathering Informa LTE Awards 2010 in Amsterdam, Ericsson Research unit was awarded 1st prize for contribution to LTE standards. The Corporation was very active in defining the frame for LTE technology, even before the standardization was even started. Afterwards, within 3GPP organization, it continued with considerable contribution to the new technology development. The creation of high-quality LTE specifications enabled the early commercial implementation of LTE mobile broadband access and paved the way for trust of the whole industry into LTE technology, as well as contributed to usage of this advanced technology.

Since LTE standard foresees solutions for problems that have already been recognized in GSM and WCDMA/HSPA specifications, Ericsson has a vast number of patents in standards applied also to LTE. One fourth of the total intellectual property, essential for the standard, makes it the biggest patent holder in the given area.

Globally connected





MOBILE BROADBAND ACCESS

By implementation of Ericsson Dual Carrier HSDPA technology, in cooperation between telecom provider Vipnet and Ericsson Nikola Tesla specialists, last year the town of Osijek became the first Croatian town with commercially available data transmission at the rates of up to 42 Mbps. In addition, by the end of 2010, yet another group of 17 Croatian towns were covered by HSPA+ technology, delivered by Ericsson Nikola Tesla. The given technology enables browsing speed of up to 21 Mbps.

In the world where time seems to be among the most important resources, the offered solution is a step forward in the development of rate and capacity of mobile internet access, and positions Croatia high on the list of countries using mobile broadband access that provides users with an immediate access to the wanted contents. This was enabled only a year after Ericsson demonstrated, for the first time in the world, the transmission speed of 42 Mbps for commercial operation.

Although today mobile broadband access is used by only 10 percent of users, its contribution to the traffic volume in mobile networks is considerable. Current Ericsson's assessments of traffic in networks operating worldwide show that data traffic via mobile networks has almost tripled in a year time, which is ten times faster growth than with voice traffic. Ericsson data show that data traffic has globally increased by 280 percent in 2008 and 2009, with the predictions that it will double in each of the five years to come. According to the same statistics, the mobile data traffic measured worldwide in Q2 2010 was almost 225 thousand terabytes. There are more and more users who have the state-of-the-art units generating data traffic, such as smart phones and wirelessly interconnected PCs. Thus data show that the 3G network traffic has surpassed 2G traffic.

Thanks to 3G/HSPA standards, the number of wireless M2M (machine-to-machine) links has increased globally, so the predictions by ABI Research are that in 2014 their number will be more than 200 million, and according to Ericsson estimations, there will be as much as 50 billion networked units by the end of 2020. Ericsson does not want to be only a technological company, but wishes to play a prominent role in that world, and to help the other companies in their operations. Therefore, Ericsson alone or in cooperation with other suppliers, offers more and more applications compatible with all sorts of mobile units that may be found on the market. By 2015, the Corporation expects more than three billion new users of mobile broadband access, and also believes that Ericsson vision will help in creating the world in which devices will be automatically connected to the internet, and various functions will be executed automatically by internet access. Any unit that society or an individual may benefit from, will be networked.

Many social activities, such as health care, traffic, public administration, and municipal services or media industry are being transformed thanks to their process networking. As of the energy sector, smart measurement procedures increase business efficiency and save costs of operation in energy providing companies. The solutions for transport monitoring improve routes optimization, and safety of vehicles in the roads. The equipment communications in real time, remote control and treatment of patients, will enhance health care. In the given segment, Ericsson Nikola Tesla has also developed solutions that are a step forward in healthcare system.

M-HEALTH

According to studies, health care development, based on up-to-date technologies is heading in two basic directions. One is to provide relevant medical data, any time and any place where a patient may find himself, and the other one is related to planning and decision making concerning the healthcare system functioning on the basis of correct, relevant and updated information. The Company develops solutions in both directions.

Ericsson Mobile Health (EMH), the product made by Ericsson Nikola Tesla, is a solution for remote patient monitoring. It is also a part of Ericsson's vision of the ICT industry serving people. Since an average population life expectancy is extended, the current healthcare systems and organizations are faced with complex requirements for extending efficient and cost effective medical services, but with top quality and safety levels maintained. Therefore, the given domain witnesses intensive introduction

of modern ICT solutions, which enable efficient and reliable insight into the current health status of a patient out of the medical institution.

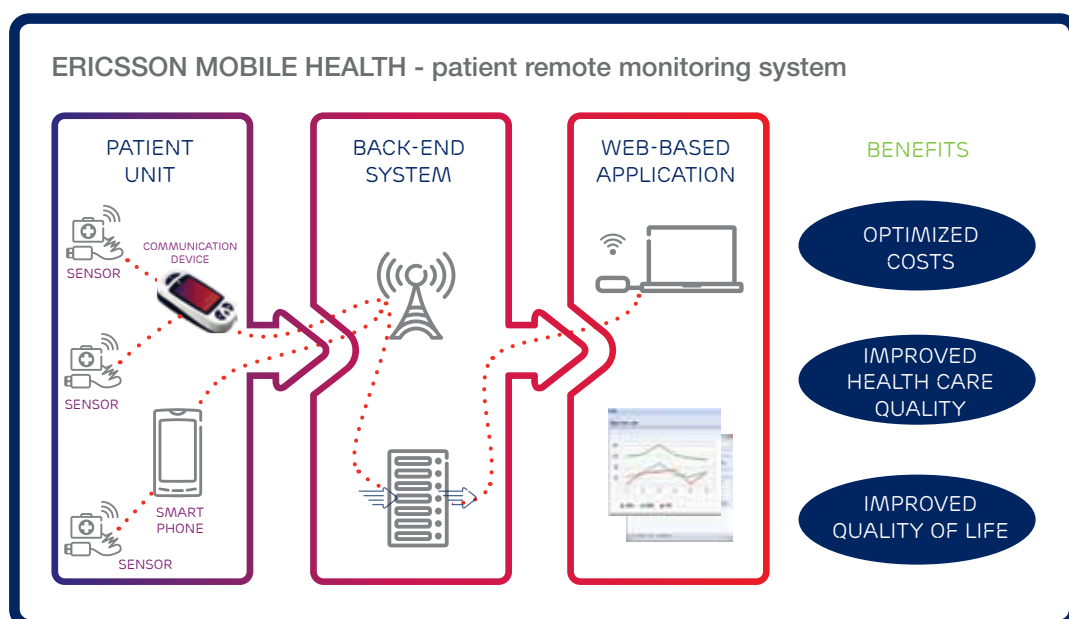
EMH is a product intended for medical parameters measurements on patients out of hospitals, having a long-time stable medical status. The solution consists of an application, server system and a patient's unit in a specially designed bag with a communications unit, medical sensors and accessories, such as charger and batteries. The central part of the patient's set is a communications unit, which collects measurement results from sensors available via a Bluetooth interface and sends them towards a server system available via a mobile network.

A doctor may access the server system and review patient's data by using an application intended for doctors. Medical staff are provided with a safe and easy insights into a patient's status through analysis of various medical parameters such as electrocardiogram (ECG), spirometry, blood pressure, heart beat rate or oxygen saturation.

Due to its high reliability and simplicity of usage, the EMH product offers a wide range of applications, from monitoring patients chronically ill in cardiology and pulmonology, home care patients, those released from hospital or released after a first aid treatment to preventive checkups. In addition, the EMH product is suitable for use in programs on health status enhancement and as a support for clinical tests. In brief, it is applicable whenever medical parameters measurement results are to be transferred to a remote location.

EMH passed a rigorous certification procedure in compliance with the EU Directive. The certification covers the audit of the manufacturer's quality assurance, in this case Ericsson Nikola Tesla, in compliance with the International Medical standard ISO13485:2003 and the audit of product compliance with the EU Council Directive 93/42/EEC on Medical Devices. The audits were carried out by Det Norske Veritas (DNV), and on the basis of EC Declaration on conformity, the EMH product was approved with the label CE 0434. The Croatian legislation regulates a similar procedure for each particular medical product to be placed in the Croatian market. After meeting the set regulations, the EMH product was entered into the Register of Manufacturers of medical devices and the Register of Medical Devices by the Croatian Agency for Medicinal Products and Medical Devices.

EMH is a promising solution for personalized medicine since it enables a patient's life quality improvement under the sophisticated doctor's surveillance. By using the EMH product, medical staff increase efficiency by remote diagnostics and treatment applied, thus creating additional prerequisites for good quality health care. In this way, it is easier and more efficient to control resources, provide monitoring and therapy, which results in savings during treatment and better cost management.



Specialists consider that telemonitoring and telemedical service are real potentials for future control of a patient's medical status. Data, such as results of a blood pressure measurement or ECG, are transferred automatically, or with a patient's assistance, via fixed or mobile networks, and are used to optimize patient's treatment. The reduction in the number of routine consultations about a continuous health status enables personalized and a long-term optimum treatment and communication with a doctor from the patient's home. These are just some advantages provided by telemonitoring.

Therefore, solutions from the mobile health care domain, such as EMH, will provide better quality, more precise, personalized image of a patient, on the basis of which, a well organized system may provide optimum health care service.

Ericsson Nikola Tesla, as a part of the Ericsson Corporation operating worldwide, was awarded a responsibility for Ericsson Mobile Health.

For example, Saudi Arabian telecom service provider Mobily, has recently initiated the first m-Health service in Saudi Arabia. It was based on Ericsson's solution for mobile health care. This was also the trial concept for their major medical institutions, which will enable efficient remote monitoring of a patient's health status.

EMH was successfully presented at the Mobile World Congress in Barcelona, at the First Congress on Telemedicine in Tunisia, at the International CTIA Wireless 2010 show in Las Vegas, at the Annual Ericsson Shareholders' Meeting in Stockholm, at the International Conference Med-E-Tel in Luxembourg, at the World Expo 2010 in Shanghai, at Health Care Days of Bosnia and Herzegovina Federation in Sarajevo, at the exhibition Vodafone Innovation Day in Düsseldorf, at the fair MEDICA 2010, the biggest annual gathering of health care professionals in the world, at the meeting with media on sustainability and ICT in Ericsson headquarters in Kista, and at GSMA Mobile Asia Congress 2010 in Hong Kong.

At the end of the last year, at the competition Vidi e-novation Ericsson Nikola Tesla was awarded Tesla's Golden Egg in the category of large companies for the innovative Ericsson Mobile Health product.

E-HEALTH

Regardless of space, time or cultural background, health is a universal human value. New opportunities often connected with more and more sophisticated and expensive diagnostic and other procedures, new innovative drugs and evident need for multidisciplinary approach considerably influence enlarged expectations, thus making the management and financing of a healthcare system a very complex task. Application of modern information solutions in healthcare systems provides timely availability of complete information on a patient status, thus enabling high-quality medical services. The solution by Ericsson Nikola Tesla – HNIS (Healthcare Networking Information System), is a modern platform for integration of solutions in health care. It supports important business processes. The functionalities such as ePrescription, eReferral, eBooking or eRecord provide all prerequisites for a patient to be really a spotlight of a health care. This is due to, not only technology, but also services related to setting up and optimization of business processes in a healthcare system.

Hospital Information System (HIS) is an additional tool in a healthcare system, and is a key prerequisite for efficient and good quality work at all levels of a healthcare system.

This means that due to the considerable reduction in administrative activities, any unnecessary contact with a healthcare system will be avoided and a doctor can spend more valuable time with a patient. Finally, on the basis of data collected through this system, the Croatian Ministry of Health and Social Welfare and the Croatian Institute for Health Insurance can impact rationalization in operations and enhance the organization, as well as additionally improve the quality of healthcare system to the benefit of all patients.

The aim of the solutions provided by Ericsson Nikola Tesla is to make health care more available to all citizens. ICT solutions have an important role since they reduce the administrative activities and improve health care transparency. This has a positive impact on the capacity and throughput of the healthcare system. By digitalization of information and their processing, it offers valuable understandings of how each particular health care subject or the whole system is functioning.

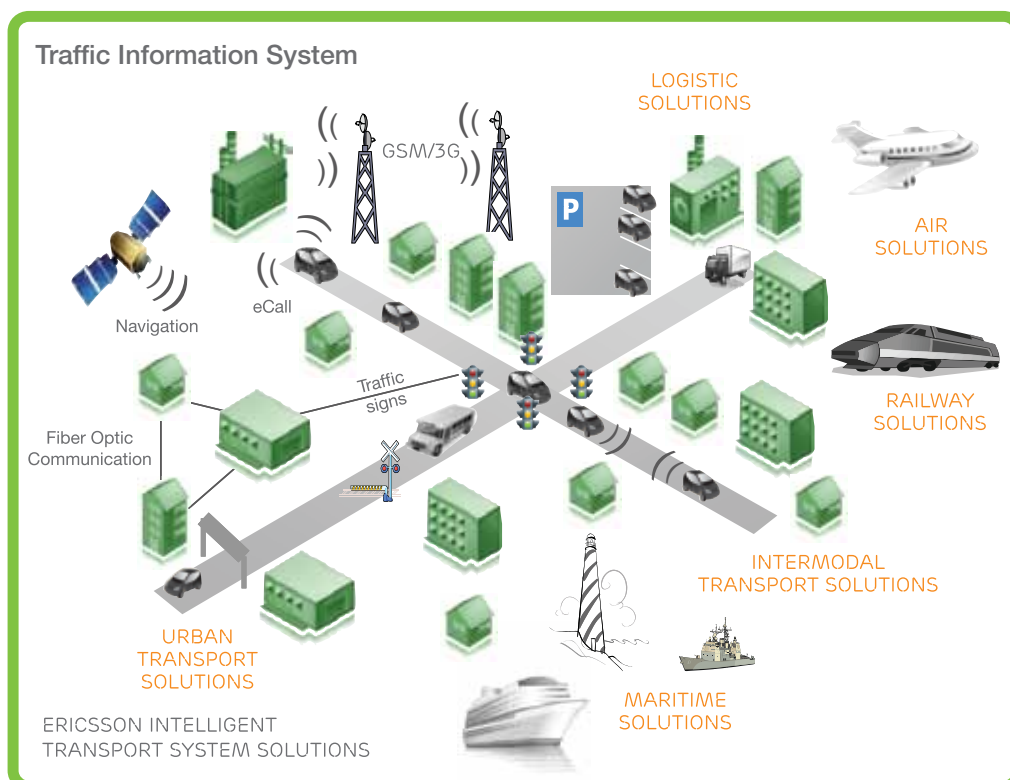
This is a reliable base for good decision making in the process of the system management.

Within the national e-Health project, so far the following functionalities have been implemented: ePrescription, eReferral, and eBooking, and throughout Croatia the system is expected to be in full operation during 2011.

According to the research completed by Health Consumer Powerhouse that follows and analyzes trends in health care in Europe and Canada, already today the healthcare system in Croatia, as far as the informatization is concerned, is at the 3rd position along with Great Britain, Sweden and Iceland. Its quality and positive influence on the environment placed this solution among the top 25 global smart ICT solutions, according to the Report SMART 2020, by the independent, non-profit organizations The Climate Group and Global Initiative for e-sustainability.

TRAFFIC

Circulation of people and goods is one of the fundamentals of civilization. The sustainable development of the modern society requires solutions for basic challenges in the modern traffic, such as traffic optimization, safety of all participants in traffic, energy efficiency and minimizing the harmful impact on the environment. Intelligent Transport Systems (ITS) offer the answer to these challenges and provide management and operational framework for new traffic technologies. Innovative ITS solutions are based on the application of the public mobile communications network in order to achieve the real-time insight in the traffic situation, with no additional infrastructure in the road traffic required. The real-time insight into traffic situation is the basic precondition for building an effective traffic management at all levels, from town to national. The successful synergy of public mobile communications and satellite navigation offers additional improvements in quality of positioning and other mobility parameters, thus enabling to achieve the correct and real-time evaluation of a traffic situation in a particular traffic network segment.



Ericsson is among global leaders in the given segment, and the transportation industry has recognized it as a driver of development of Intelligent Transport Systems.

Ericsson Nikola Tesla has recognized the importance of ITS at the early stage, and therefore it has an active role in creating the Corporate solutions in the given segment, thus becoming an important factor in the Ericsson ITS strategy.

Ericsson Nikola Tesla's ITS portfolio covers intelligent solutions for road, maritime and railroad traffic. The basis of the given system is the approved Ericsson Corporation products, positioning intelligence in public mobile networks and skill and competence of its specialists. Ericsson Nikola Tesla is an active participant in Pan-European project of eCall implementation, automatic traffic accident notification from a car and setting up of direct communication from a car to the public safety access point. The Company is also a partner in the Croatian national eCall pilot project. The maritime traffic supervision and management system, implemented to meet the needs of Rijeka harbor, enables successful monitoring and optimum management of the total maritime traffic by synergy of the latest information and communications technologies. The prototype of Traffic Information System for the city of Zagreb has been developed in Ericsson Nikola Tesla. It successfully demonstrates business and technological solutions of the new ITS generation, and is based on the positioning intelligence and requires no additional road network infrastructure. ICT solution prototype, created for the management of the power supply stations network, which is necessary for electric vehicles supply, is an Ericsson contribution to the actual problem in transition from classic to new types of vehicles driving system (hybrid and electric vehicles). Such innovative ITS solutions enable traffic optimization, energy efficiency and reduce harmful traffic effect on the environment. By interconnection of traffic systems and public mobile communications in urban areas, citizens actively participate in the traffic system, thus increasing the system efficiency and reducing stress of traffic participants, and optimizing the traveling time.

Interconnection of different systems, with the simultaneous data collection and handling, ITS solutions are approaching the phase of wider implementation supported by the development of mobile communications that are among the key factors in the given process.

ADVANCED TECHNOLOGY FOR AGEING POPULATION

Latest estimations suggest that the number of persons older than 80 will triple in Europe by 2060. This figure will be a heavy pressure to future healthcare and economic systems, especially having in mind a considerable decrease in the number of young people in the population, who are supposed to support the older population. One of the possible solutions for the given problem is AAL program (Ambient Assisted Living). It is about usage of information and communications technology to enhance the quality of life for older population, and to extend their independent living in their own homes, as well as to improve their health and reduce cost of their possible treatment. Under the same title there is the innovation and technology program financed by EU Commission, aimed to solve population ageing problems.

Mobile Networks



Within the given program, we witnessed the launch of the project named universAAL at the beginning of the last year. Its main objective was to make it technically feasible and economically viable to conceive, design and deploy innovative services. This is an open platform and the common basis for program developers and end users. The platform development will apply knowledge and solutions from former, similar European projects. Based on competences in e-Health segment, and positive experiences from the former cooperation, Ericsson Nikola Tesla also participates in the project along with 16 partners from EU. The Company cooperates in the procedure of defining the reference architecture, platform implementation, as well as in activities on the development of corresponding innovative solutions. It is also responsible for the development of training modules and materials that will be used for the knowledge transfer within the project and out of it.

Furthermore, it will support the efforts in platform standardization and its solutions within the Healthcare Services Specification project, as well as in Continua Health Alliance.

Ericsson Nikola Tesla has also participated in up-to-date joint research activities, the results of which are used for extension and improvement of the current Company's solutions in e-Health segment. These results will help in the EMH product integration with networked information healthcare system. The experiences acquired during such activities will contribute to even stronger positioning of the Company as a leader in development, integration and delivery of e-Health solutions.

DIGITAL CITIES

According to UN predictions, two-thirds of humanity will live in cities by 2020. Therefore, the importance of cities and the urban policy will be increased as global, national and local task. It will be of fundamental importance in creating responses to major world challenges. In such complex circumstances for the development of cities as sustainable communities, with tough requirements to cities as drivers of economic, social, cultural and ecological society aspects on one hand, and with limitations such as the current infrastructure, traffic jams, and considerable difference in economic and social opportunities of particular urban areas, on the other hand, safety becomes a challenge that cannot be avoided.

Safety solutions for cities, offered by Ericsson, are based on innovative mobile telecom technologies, with location intelligence integrated into ICT solutions along with sensor, video and the other safety systems and city infrastructure, as well. Those solutions offer efficient and reliable answer to safety challenges in urban areas, from monitoring, incident detection, management of alarm situations and disasters of different causes to removal of their negative effects. The system consolidates functions such as advanced communications, alarm and event management, data and resources management and information sharing. This is of utmost importance for decision making in alarm situations. The basic principle of Ericsson safety systems is early warning. This means a real-time reaction to incidents, thus considerably lowering the damage volume and human casualties. The system is dynamic and management of it is location selective in large disasters, thus minimizing uncontrolled processes as people panic. By introducing new technologies, the efficiency of the current safety systems is increased, and a high level of complex responses to danger is achieved, which means high safety and rescue levels in urban areas.

E-ADMINISTRATION AND E-OFFICE

Information and communications technologies have a great impact on our ways of working and life in general. They considerably influence both private and business segments of human life today. This results in changes, reorganizations and restructuring of the present modes of communications, ways of working and industry sectors requiring new ways and channels of communications with government administration.

This was the reason for the e-Croatia Central State Administrative Office to establish the e-Office Forum in order to create the specification for the unique electronic document management (EDM) system. It is based on widely accepted EDM concept and the MoReq2 specification.

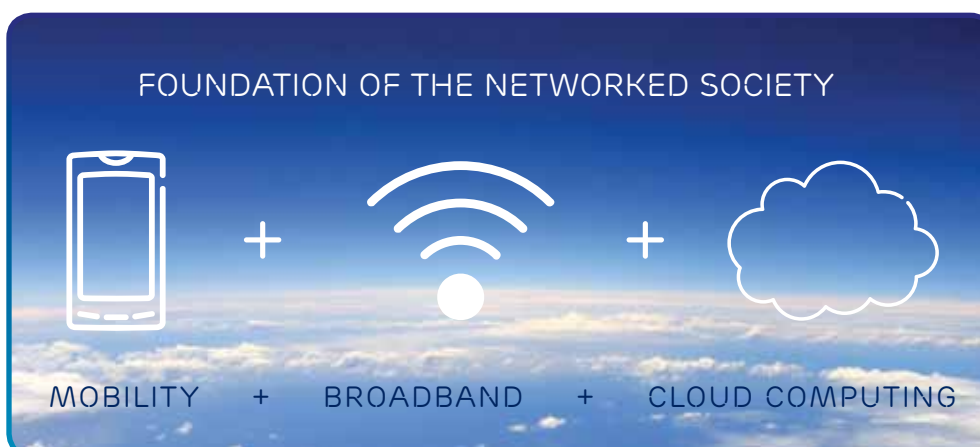
The specification is aimed at achieving uniformity in procedures implemented in office operations by applying information and communications technology. E-Office supports performance of state administration offices, approved by the Croatian Government, in order to improve users' satisfaction, rationalization of administration procedures, which means enhancement of quality of life for all citizens.

Ericsson Nikola Tesla is one of the major participants in informatization activities to transform state administration. The Company has rich and unique experience in various markets, in modern infrastructure solutions development, as well as in formal competences that are permanently applied in development of new version of international standard for records management systems in state administration bodies.

The Company is an active supporter of government administration bodies in transition from paper to electronic operations, as well as in creating safe, unique documentation system for government administration bodies and public authorities. The set goal is a satisfied user, rational administration procedures and enhanced quality of life for all Croatian citizens.

SOCIAL NETWORKS

Living in the digital age, we witness powerful computers, mobile communications and fast internet access, regardless of the place we may find ourselves at. The possibility of networking, regardless of space and time, is a key to welfare, and people begin to take it for granted. This especially refers to social networking via mobile devices and personal computers. For example, there are more than 200 mobile operators in 60 countries worldwide enabling and promoting Facebook. There are more than 100 million active users, who access Facebook via their mobile devices. This is also supported by the recent Ericsson study on users' behavior that shows that some 80 percent of mobile broadband access users require permanent access, regardless of time and place, since they consider it usual in a daily life. The Study is based on 4,580 users from 6 mature markets. It shows that with the increase of mobile data traffic, the users consider the link via mobile broadband access a personal one like via mobile telephone. Thus, 80 percent of examinees said that they would not share their PC with no one, and 65 percent would not share mobile broadband access. Such a new behavior of users requires the adjustment of mobile networks to both data and voice traffic. It is expected that this will mean a considerable modernization of networks and their transformation to all-IP technology, as well as to new support system. Ericsson is well positioned on the given areas and can help operators to gain profit from these new opportunities.



GIGABIT PASSIVE OPTICAL NETWORKS (GPON)

GPON is among the fastest globally growing access technologies, and its development and standardization offer numerous opportunities to future broadband access network and services such as voice transmission over Internet Protocol, video on demand, HDTV or 3DTV transmission, etc.

According to expert estimations, the development of this fiber-to-the-home infrastructure is a precondition to meet growing needs set by users as the transmission rate is concerned. It also guarantees a long-term competitiveness in the telecommunications segment, and is an important driving force behind GNP growth. This has been recognized by a new proposal for the Strategy of Broadband Access development in Croatia during the period of time 2011 - 2015. The Croatian operator Hrvatski Telekom became aware early of the global trend and by the end of the last year successfully managed to upgrade its GPON, that has already been in operation for more than two years.

To provide its users with even better and more stable service, Hrvatski Telekom selected Ericsson as a partner in building the active part of the network. Ericsson was entrusted to upgrade GPON platform in order to achieve better network management, enable more efficient capacity extension and provide more efficient and low cost maintenance.

At the end of last year, the R&D Center within Ericsson Nikola Tesla was awarded considerable responsibility for GPON segment. This was also the best recognition to Company's experts for keeping pace with the global competition.

MULTIMEDIA

There is no doubt that the development of GPON infrastructure impacts the way multimedia is used in a daily life. Ericsson ConsumerLab announced results of a recent study titled „Multi Screen Media Consumption 2010“. Data were collected in China, Germany, Spain, Sweden, Taiwan, Great Britain and the USA. A sample in a study represents more than 300 million users, and the results show that people spend 35 percent of spare time watching TV and video contents. Users are more and more aware of new technologies that make new patterns of media consumption.

At least once a week 93 percent of examinees still watch standard TV programs, but the role of television is changing due to introduction of new distribution channels. More than 70 percent of examinees use streaming, downloading or watch recorded TV program on a weekly basis, and 50 percent of them use internet services for TV and video on demand content on a weekly basis.

Live TV programs are still very important to users, but the possibility to make a decision on when and how to watch TV will influence its role in the period to come. In the future, users wish personalized, user-friendly and top-quality services on demand, with no commercials inserted.

CONVERGENT NETWORKS

Ericsson network development strategy is aimed at convergent IP-based network architecture that enables the delivery of any service to any networked device regardless of its location. This targeted architecture requires broadband access network based on advanced wireline and wireless technologies such as GPON and LTE. In the period to come, development and implementation of mobile broadband networks and the next generation of GPON will play a leading role.

Broadband access is the fundamental infrastructure in the 21st century. It will enable the development of information and communications technologies, which are of key importance for growth in efficiency and economy. Various scientific and research studies show that each country in which broadband access has been introduced, along with investments into infrastructure and services, witnesses economy growth and new jobs. Broadband infrastructure is a “green technology” and therefore the basic component in building a sustainable future.

Fundamental benefits from convergent networks are cost reduction and operational improvements. It is better to have one convergent network, instead of several smaller dedicated ones. The cost of installation and maintenance of a single network is considerably lower than of several dedicated ones.

Another important benefit from network convergence is providing new applications with increased efficiency. As of end users, the benefits are access to any service from any device (telephone, PC, TV or any other electronic device) anywhere, (in motion, from remote location). In addition, new interactive and multimedia services will enable richer and more efficient mode of communication.

Innovative IPTV service providers can already today connect TV set, mobile telephone and PC, thus enabling that any PC image, video or music content is presented at any screen. New IPTV platforms provide a variety of services related to content delivery to various devices, remove barriers between TV sets and PCs, and introduce a new generation of user interface. Ericsson's product mix offers system integration and consulting services, the awarded Ericsson's IPTV middleware, OpenStream Digital Services Platform for video on demand functionality, and WatchPoint Content Management System related to the challenge of equal content delivery in various formats and to various devices.

ICT AND E-SUSTAINABILITY

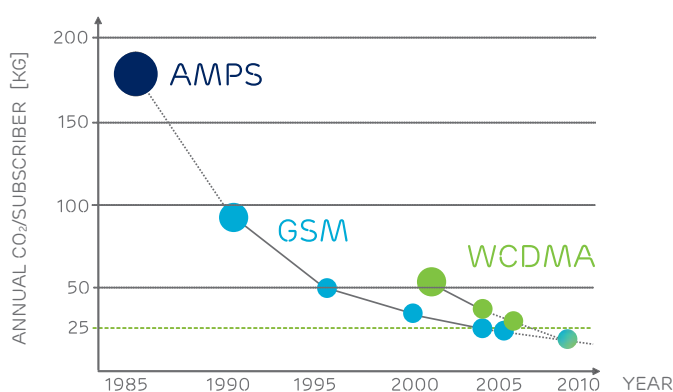
Broadband access is not only of key importance for new economy transforming business models, but it also impacts CO₂ emission reduction, promoting new ways of working and a new lifestyle.

Telecom operators also wish to reduce the impact on the environment and to keep business growth. Therefore, Ericsson offers to operators a pioneering TCO₂ approach, which measures CO₂ emission, thus enabling total proprietary cost management. By achieving the best combination of investment into energy efficiency, TCO₂ approach supports the operators' targets regarding the environmental protection and business development, enabling them cost savings and reduction of negative impact on the environment.

The Australian operator Telstra, in cooperation with Ericsson consultants, checked the CO₂ emission and the efficiency of its mobile network. The study confirmed the benefit gained by Telstra through implementation of this initiative, and showed the possibility to reduce CO₂ emission up to 30 percent in the radio access network, and 56 percent in the core network.

Today the ICT industry's contribution to the total CO₂ emission is only 2 percent. However, by implementing information and communications technologies into other industry segments, CO₂ emission may be reduced by 5 to 20 percent. Introduction of ICT to various industry sectors enables the interconnection of various monitoring and control devices, thus achieving reductions in energy consumption and positively affecting the environment.

The life-cycle footprint per subscriber in mobile networks



Implementation of ICT solutions will not only speed up and simplify processes, but will avoid unnecessary transportation and reduce CO₂ emissions and pollution in general.

And above all, broadband access will enable people to live and work wherever they wish, thus slowing down the process of urbanization and reducing the need to travel. Broadband access also offers flexible ways of working, like during traveling, from a remote location and finally from anywhere. Thus, work efficiency will increase and people will have more spare time to spend with their families and friends.

The application of teleconference and videoconference may reduce the business trip frequency, thus also contributing to the CO₂ emission reduction.

Although “face-to-face” communication is in some cases inevitable, and shall not be considered obsolete, modern ICT solutions enable various modes of communication and various types of automation in supporting business processes. Thus the focus is on the work content, and not on the form and administration.

And of course, more spare time, possibility to be engaged in various activities with no physical contact with other people, immense volume of easily available information enabled by new systems may be used in good faith, but also maliciously. One may expect that if the wise management policy is applied to new opportunities, where family, educational institutions and society as a whole play an important role, the positive sides will prevail. We believe that human curiosity in combination with advantages brought by modern ICT systems may somewhat bring us closer to the future, where professional engagement will be satisfying for individuals, but also offering maximum benefits to the society.



EVENTS IN 2010

- » At Mobile World Congress 2010 held in Barcelona, Ericsson Nikola Tesla was an exhibiting company by showcasing its e-Health solutions. The emphasis was given to the demonstration of the cutting edge m-Health solution, which supports a real time remote patient health status monitoring.
- » Ericsson Nikola Tesla organized the press conference in Zagreb and Split to announce business results in 2009 and expectations for 2010. The Company's strategic commitment in connecting economy and science was confirmed there, by signing agreements on cooperation between Ericsson Nikola Tesla and the Faculty of Electrical Engineering and Computing of the University of Zagreb and the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture of the University of Split.
- » Telecom Arena 2010, a regional conference on electronic communications, was the opportunity for our experts to present LTE technology and participate in a panel discussion titled "Sustainable and Responsible Sector - ICT serving society and protecting environment?".
- » A Croatian Government delegation paid an official visit to Ericsson Nikola Tesla. The delegation was headed by the Prime Minister, accompanied by the Minister of Economy, Labor and Entrepreneurship, Minister of Legislation and other associates. The Company President gave the guests of honor insight into the important achievements and the responsibilities of the Company in the domestic and export markets and underlined the export of knowledge and the new innovative ICT solutions developed by Ericsson Nikola Tesla experts.
- » Annual Meeting of Ericsson Nikola Tesla's shareholders was held.
- » At a press conference by the Ministry of Health and Social Welfare, held in Gospić, a trial operation of new e-Health functionalities was demonstrated. An e-Health project, covering functionalities such as ePrescription, eReferral and eBooking was implemented on a trial basis in Lika-Senj County. The press conference gave an opportunity to underline that the e-Health system will enhance human life and business operations, in general. According to analysis by Health Consumer Powerhouse (HCP) from Brussels, which follows and analyzes healthcare systems in Europe and Canada since 2005, the Croatian healthcare system ranks third behind Great Britain, Sweden and Iceland.
- » During the opening session of MIPRO 2010, the 33rd international Convention on Information and Communication Technology, wireless data transmission at a record speed of up to 42 Mbps was demonstrated. This was showcased for the first time not only in Croatia but in South-Eastern Europe, too. This exceptional achievement was presented to MIPRO attendees by Gordana Kovačević, the President of Ericsson Nikola Tesla and Mladen Pejković, the President of Vipnet Management Board. Specialists from our Company were active participants in the Convention activities.
- » World "EXPO 2010" was held under the motto "Better town for better life", showcasing the vision on better future life in urban areas. Within Ericsson Innovation Forum, Ericsson Nikola Tesla's specialists demonstrated e-Mobile program. This innovation was assessed as a solution of a large business potential.
- » An official visit to Ericsson Nikola Tesla was paid by Ivo Josipović, the President of the Republic of Croatia, and his associates. During the visit, the President of Ericsson Nikola Tesla presented the Company's results and activities in the domestic and export markets, as well as the plans for future operations.

After exchanging opinions, the guest of honor and his associates toured the Company with the hosts who informed him on important activities and projects. The Company experts presented him the state-of-the-art e-Health solutions.

- » The 10th jubilee Summer Camp was celebrated in Ericsson Nikola. Since 2001, as many as 300 students have participated in the camp activities, which resulted in 162 successful projects and 82 prototypes supported by 73 mentors coming both from faculties and from the Company. The attendees were awarded numerous acknowledgments for their work, among which three Rector's awards are to be mentioned.
- » ARCA, the 8th international fair of innovations, new technologies and products, focused on interconnecting science and economy, was held in Zagreb. A conference on the topic „Through innovations to competitiveness”, organized during the fair, was attended by prominent specialists from Croatia, the USA, Slovenia, Austria, Hungary, Russia and Romania. Key topics discussed included creation of an environment that would encourage innovations, creative relation between employer and innovators in a company, academic community and other institutions, university degree education and training for applied researches, and good practice examples. Experts from Ericsson Nikola Tesla participated in the conference along with prominent domestic and foreign experts.
- » Ericsson Nikola Tesla and Hrvatski Telekom demonstrated in live, for the first time in Croatia, LTE network implemented for trial operation. This new network technology enables high transmission speeds, and enhanced data transmission quality, as well as implementation of numerous multimedia services in a daily life. These high data transmission speeds made mobile and fixed network convergence a reality. IP Multimedia Subsystem (IMS), implemented by HT, offers the same possibility and line of services, regardless of the access network used, and user device applied. Thus, Croatia is positioned among countries pioneering the implementation of the cutting edge 4G LTE technologies.
- » Company specialists participated at the New Technology Day (DaNTE) and showcased the new innovative ICT solutions in traffic and municipal services sector, and the health care sector too.
- » Ericsson Mobile Health, a product for patient remote medical status monitoring was presented in a number of fairs and exhibitions such as: MEDICA fair, Vodafone Innovation Day exhibition, Health Care Days in Bosnia and Herzegovina, and GSMA Mobile Asia Congress.
- » At the traditional international symposium on telecommunications, BIHTEL 2010, experts from Ericsson Nikola Tesla presented several advanced telecommunications solutions.
- » Ericsson Nikola Tesla participated successfully, for the 10th time in a row, at the Information and Communications Technologies Festival (INFOFEST) in Budva, Montenegro.
- » Company specialists participated in the International Exhibition named TIBO, on Communications, Information Systems, Banking Systems, Office Accessories and Security Systems, held in Minsk, Belarus.
- » The fifth annual Ericsson Nikola Tesla Suppliers and Partners' Day was held and all major suppliers and partners of the Company attended the event. The theme of the event covered times of changes, and adjustments to new market and technology challenges, as well as new organizational models and responsibilities.
- » The cooperation between Vipnet and Ericsson Nikola Tesla through implementation of state-of-the-art technology. Osijek became the first town in Croatia with data transmission speeds of up to 42 Mbps available to users.



Andrew Skelton,
Finance Director of Ericsson Nikola Tesla d.d.

COMPANY PERFORMANCE



STRONG PERFORMANCE IN A TOUGH ENVIRONMENT

Our operating environment during 2010 continued to be one of extraordinary challenges, driven primarily by global economic events. Against this backdrop, we performed strongly in terms of underlying net profit and net cash from operating activities despite pressure on sales volumes.

For Ericsson Nikola Tesla, the most significant impact of the global economic crisis materialized in our business activities in Kazakhstan, where we wrote off MHRK 126.5 of receivables. These balances existed in respect of customer financing extended in 2005 and fully secured by trade finance instruments from BTA Bank who underwent a major financial restructuring during 2010.

As a result of early actions taken to manage the impact of BTA's restructuring, we were able to accelerate collection of MHRK 150 of remaining balances, and the positive impact is reflected in net cash from operating activities of MHRK 366.4 and a year-end cash and cash equivalents balance of MHRK 673.9.

Underlying net profit of MHRK 150.5 for 2010, excluding the Kazakhstan write-off, represents a return on sales of 12.3 percent. A year-over-year sales decline of 13 percent reflects a slowdown of capital investments by operators, decreased government investments into infrastructure projects within the ICT segment, a general decrease in budget volumes of our partners and customers and the impact of industry-wide component shortages and supply chain bottlenecks.

GROWING THE RIGHT WAY

Throughout 2010, we maintained our focus on business stability while at the same time laying additional foundations for future business growth. We made strong progress during 2010 in managing balance sheet risk and in continuing to rightsize our cost base. Long-term loans and receivables and trade receivables reduced by a combined total of MHRK 372.8 or 51 percent when compared to the end of 2009 and we achieved a 17 percent reduction in distribution and administrative expenses compared to the prior year. At the same time, we were able to make further investments in competence and business development projects to support our business strategy. This approach has helped position us strongly for the eventual economic recovery.

Investing for and supporting sales growth remains critical to our future success. We are determined to grow the business in the right way and to support these activities through improved ways of working, increased efficiency and continued strong discipline with regards to risk management. Accordingly, during the year, we continued to partner and build relationships with export credit institutions and commercial banks to develop new ways of working and deliver comprehensive financing solutions to our customers.

LOOKING FORWARD

Entering 2011, there is reason for cautious optimism due to the slow recovery of local and regional economies. In executing our strategy in the current environment, we will work hard to maintain strong financials and maximize shareholder value while protecting our employees and delivering exceptional value to our customers.

With these challenges come unique opportunities. Actions taken during 2010 enabled us to begin 2011 with a stronger balance sheet, allowing us to focus on growing revenue, investing for the future and delivering improved performance.

The foundation for all these activities is a culture that puts our customers at the centre of all we do. In this regard we must continue, as we have been doing for over 60 years now, to build and develop these strong and effective relationships and to leverage the competence and depth of knowledge of our employees as a competitive advantage.



Andrew Skelton
Finance Director
Ericsson Nikola Tesla d.d.



2010 FINANCIAL HIGHLIGHTS

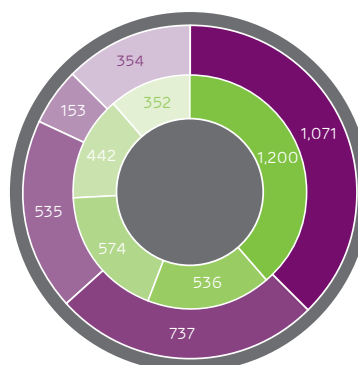
in MHRK, except per share amounts	2010 ⁽¹⁾	2010	2009	2008
PROFITABILITY:				
Sales revenue	1,219	1,219	1,400	1,800
Gross margin	17%	17%	13%	17%
Operating profit	111	-15	66	163
Profit before tax	152	26	127	212
Profit for the year	151	24	128	204
Operating expenses	111	237	138	158
Earnings per share (EPS) in HRK	114	18	98	156
FINANCIAL POSITION AT YEAR-END:				
Total assets	1,425	1,425	1,552	1,521
Cash, cash equivalents and financial assets	737	737	536	367
Capital employed	1,079	1,079	1,210	1,177
Equity	1,071	1,071	1,200	1,166
RATIOS:				
Return on equity	13.3%	2.1%	10.8%	17.5%
Return on capital employed (ROCE)	13.3%	2.3%	10.6%	18.0%
Return on sales (ROS)	12.4%	2.0%	9.1%	11.3%
Equity ratio	75.2%	75.2%	77.3%	76.7%
Capital turnover	1.1	1.1	1.2	1.5
Current ratio	3.7	3.7	3.2	2.9
P/E ratio	11.9	75.6	13.7	7.7

⁽¹⁾ There was a significant write-off during 2010 as a result of a one-time event and this write-off had a significant impact on reported results, financial measures and ratios. We have presented all measures excluding the write-off to facilitate analysis of the Company's underlying performance. However, these measures should not be viewed in isolation or as substitutes for the original measures which are also shown. For more details on this write-off, please see Note 17, "Trade receivables".

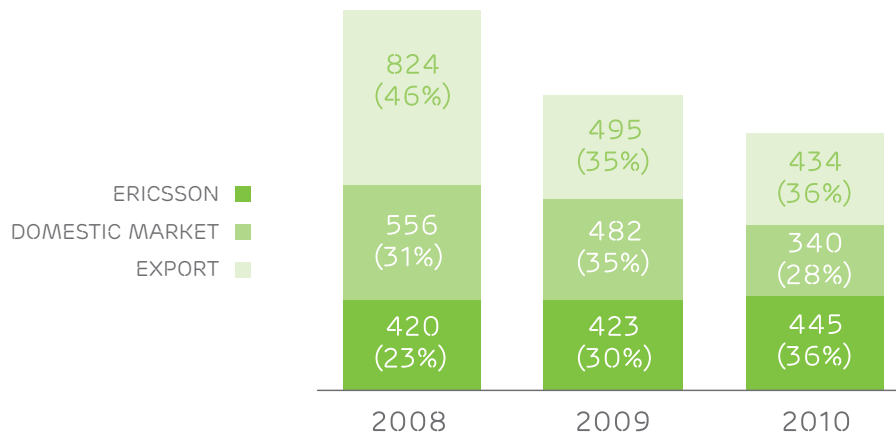
Balance sheet structure (in MHRK)

2010
2009

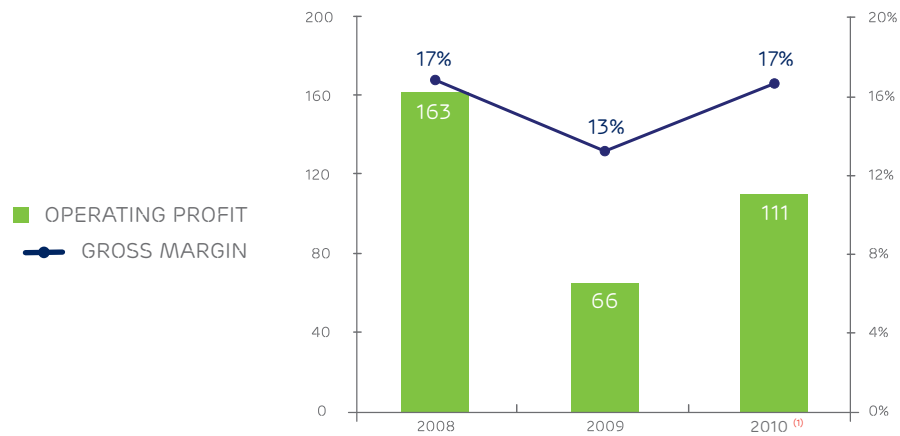
- EQUITY
- CASH, CASH EQUIVALENTS AND FINANCIAL ASSETS
- OTHER CURRENT ASSETS
- NON-CURRENT ASSETS
- LIABILITIES



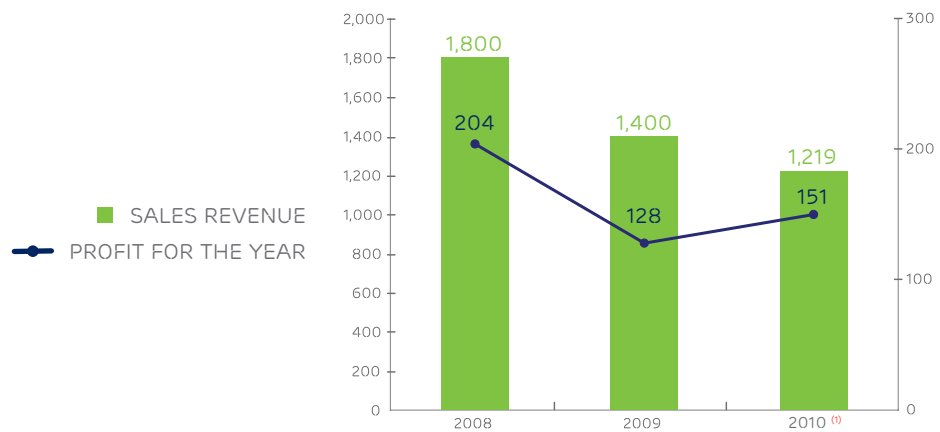
Sales revenue by ETK cornerstones (in MHRK and percentage)



Operating profit (in MHRK) and gross margin



Sales revenue and profit for the year (in MHRK)



2010 ⁽¹⁾ = excluding one-time write-off



INFORMATION FOR SHAREHOLDERS

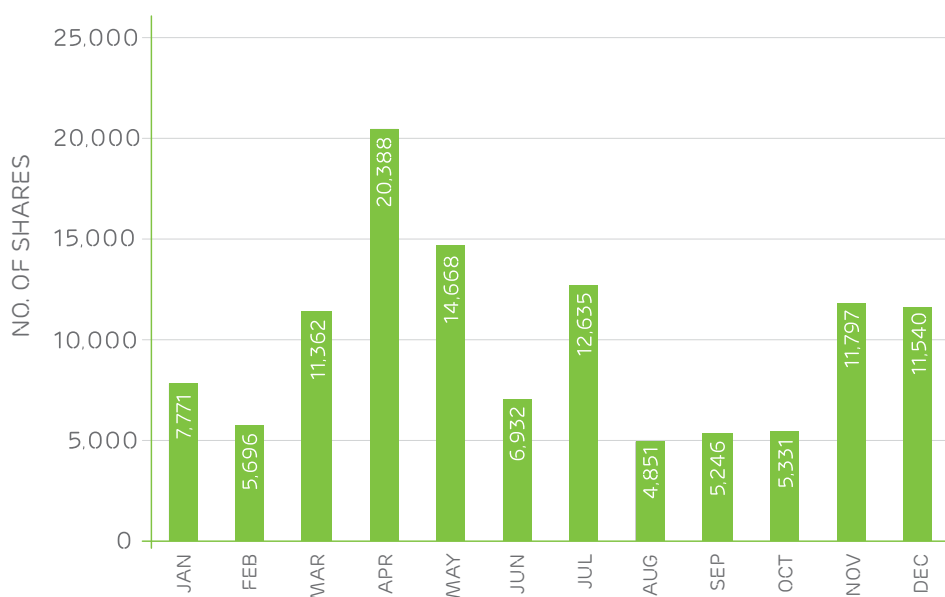
Shares of Ericsson Nikola Tesla are traded in the Regular Market of the Zagreb Stock Exchange under the stock exchange symbol ERNT-R-A.

SHARE TRADING AND PRICE MOVEMENT

Ericsson Nikola Tesla's share preserved its position among the ten most traded shares in the Zagreb Stock Exchange, with turnover of MHRK 168.8 (2.9 percent share in the equity ZSE turnover in 2010).

At the end of 2010, Ericsson Nikola Tesla's market capitalization amounted to MHRK 1,812.4, an increase of 1.6 percent year over year. Ericsson Nikola Tesla's share in the total market capitalization of the Zagreb Stock Exchange amounts to 1.3 percent.

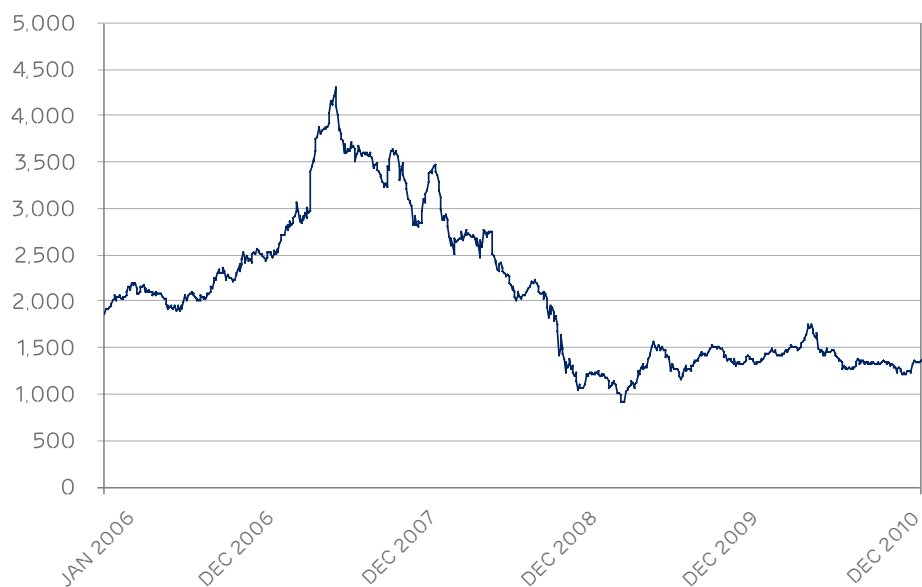
Trading volume in 2010



Comparative Ericsson Nikola Tesla's share price movement and share indices in the Zagreb Stock Exchange in 2010



Average Ericsson Nikola Tesla's share price movement 2006 – 2010 (in HRK)





Share price and turnover	2006	2007	2008	2009	2010
Highest (HRK)	2,600	4,300	3,490	1,575	1,777
Lowest (HRK)	1,850	2,450	1,000	820	1,181
Last – end of year (HRK)	2,500	3,420	1,200	1,339.5	1,361
Turnover (MHRK)	500.7	947.4	952.0	196.2	168.8
Dividend per share (HRK)	320	270	70	120	190*

*Proposal for dividend amount sent to the Annual Meeting of Shareholders for approval

SHARE CAPITAL

As at December 31, 2010, the share capital of Ericsson Nikola Tesla amounted to HRK 133,165,000 divided into 1,331,650 ordinary registered series A shares. Each share carries one vote at the Annual Meeting of Shareholders. The total number of treasury shares at the end of 2010 was 9,288 (0.7 percent of the share capital). Shares are under the ownership of 6,501 shareholders.

SHAREHOLDERS

Below follows a list of Ericsson Nikola Tesla's major shareholders as at December 31, 2010.

Shareholders	No. of shares	Percentage of share capital
Telefonaktiebolaget LM Ericsson	653,473	49.07%
Hypo-Alpe-Adria-Bank d.d. / Raiffeisen mandatory pension fund	119,991	9.01%
Zagrebačka banka d.d./ custodian account for Unicredit Bank Austria AG	41,106	3.09%
Societe Generale-Splitska banka d.d. / Erste Plavi mandatory pension fund	35,132	2.64%
Hypo-Alpe-Adria-Bank d.d. / PBZ Croatia osiguranje mandatory pension fund	30,615	2.30%
Societe Generale-Splitska banka d.d. / AZ mandatory pension fund	19,562	1.47%
PBZ d.d. / custodian client account	15,344	1.15%
PBZ d.d. / State Street client account	14,580	1.09%
Ericsson Nikola Tesla d.d.	9,288	0.70%
Societe Generale-Splitska banka d.d. / Societe Generale Splitska banka d.d.	8,062	0.61%
Other	384,497	28.87%

ERICSSON NIKOLA TESLA'S ANNUAL MEETING OF SHAREHOLDERS IN 2010

The joint stock company Ericsson Nikola Tesla held its Annual Meeting of Shareholders on May 20, 2010. The amount of HRK 87,814,700 of share capital was represented at the Meeting, which is 65.94 percent of total share capital.

Besides the shareholders' representatives and the Company's management, the Meeting was attended by the Chairman of the Supervisory Board, Roland Nordgren, and the members of the Supervisory Board: Ignac Lovrek, Carita Jönsson and Zvonimir Jelić. Snježana Bahtijari, Director of Marketing and Communications (including CSR) presided over the Meeting.

The Supervisory Board's report, on the supervision of activities concerning the Company's business management in 2009, was accepted and the statement of release for the Company's managing director and the Supervisory Board's members was issued.

A resolution was passed regarding a regular dividend payment amounting to HRK 20 per share, and an extraordinary dividend payment amounting to HRK 100 per share, to the Company's shareholders who, as of May 13, 2010, had Company's shares registered on their securities accounts in the Central Depository & Clearing Company. Dividend payment was effected on June 17, 2010.

In addition, resolutions were passed stating that the profit of the Company in the financial year 2009 amounting to HRK 128,447,089.11 shall be allocated to dividend payout, in the amount lacking after the non-allocated retained earnings realized in 2008, and the remainder to the retained earnings.

Furthermore, the decisions on amendments and additions to the Company's Statute were made as proposed by the Meeting agenda. In compliance with the proposal by the Supervisory Board, Dubravko Radošević was appointed the new member of the Supervisory Board.

Besides, at the Annual Meeting, PricewaterhouseCoopers d.o.o., Zagreb was reappointed the Company's auditor for 2010.

The joint stock company Ericsson Nikola Tesla held its Annual Meeting of Shareholders on May 20, 2010





SOCIAL REPORT 2010
Ericsson Nikola Tesla d.d.



ERICSSON NIKOLA TESLA – A SOCIALLY RESPONSIBLE COMPANY

For some ten years an ever-increasing number of companies have been using the policy of corporate social responsibility. It is a form of corporate self-regulation integrated into a business model. Back in 1993 the President of the European Commission appealed to the European business community to join the fight against social exclusion. The European Council held a special meeting in March 2000 in Lisbon to agree a new strategic goal for the Union in order to strengthen social responsibility and promote a lifelong learning, work organization, equal opportunities, social inclusion and sustainable development.

By implementing principles of social responsibility and by expressing willingness to exceed legal requirements, companies positively affect social development as well as environmental and human rights protection.

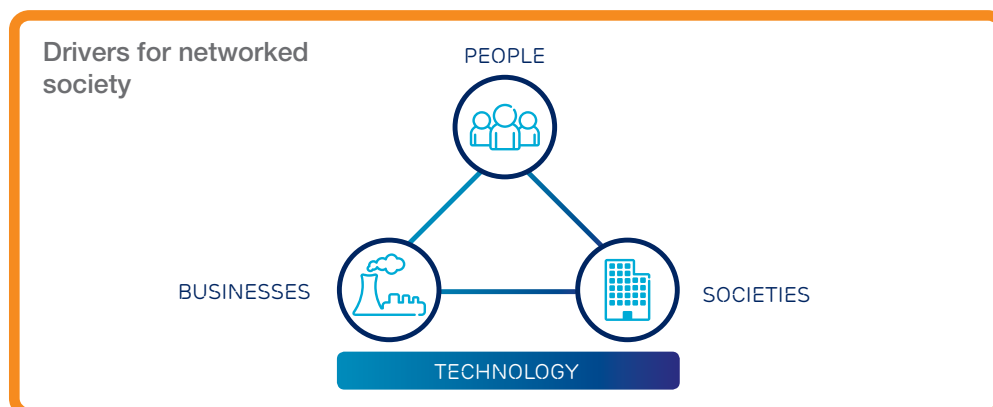
Ericsson Nikola Tesla is strictly applying international standards and is following Ericsson's example as a technological leader and global player that has a positive impact on development of technology and society. In its long-term business strategy, the Company has built in principles of responsible behavior in all segments of business and towards all stakeholders, which includes relationships based on trust, dialog and mutual sharing of knowledge and exchange of information.

We impact society economically, socially and environmentally. However, we must not forget that Ericsson Nikola Tesla is a regional ICT leader, and therefore social development is its biggest responsibility. The objective of our business is to make communication available to all, and thus narrow a digital gap, enable development of infrastructure significant for social development, make people's lives easier, reduce negative impact on the environment and stimulate economic prosperity in Croatia and in countries with which we make business. So, for a number of years we have been putting focus on development of 'green technology'. Ericsson Nikola Tesla's experts have designed and made commercially available a variety of e-products and services, like e-Health, e-Cadastre or digital city, which contribute to a more efficient use of natural resources, better time management, better access to information and knowledge and positive impact on the environment.

At Ericsson Nikola Tesla, the Marketing and Communications Unit (including CSR), together with employees from other organizational units, is in charge of social responsibility management activities.

There are three cornerstones of social responsibility: Code of Business Ethics, Supplier Code of Conduct and Environmental Management Policy, which comply with international standards. All of them are an integral part of corporate governance, and apply both to our company and our partners and suppliers. This Annual Report deals with the most important projects and activities in 2010.

Over the past several years Ericsson Nikola Tesla has won numerous awards and recognitions for its achievements and best practices of social responsibility.



KEY STAKEHOLDERS

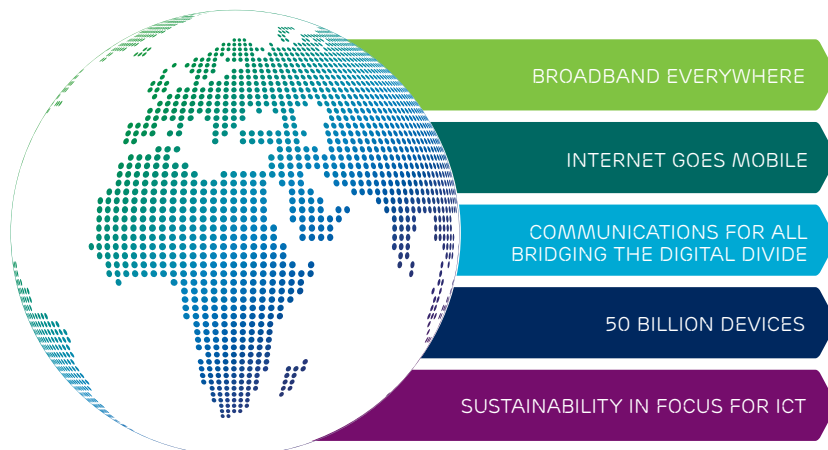
The Company's concern for all stakeholders, as well as for its own long-term development is a cornerstone and an indicator of a total social responsibility relating to the future successful operations, and the sustainable development of the whole society, too. Ericsson Nikola Tesla has a two-way, partner-based cooperation with all key stakeholders: customers, employees, shareholders and investors, suppliers and partners, the trade union, business and professional associations, government bodies, educational institutions and the community.

KEY STAKEHOLDERS	OUR WAY OF WORKING
CUSTOMERS	<ul style="list-style-type: none"> » Professionalism » Partnership in finding the best solutions » Innovativeness in the provision of total ICT solutions, which have a positive impact on business, people's lives and the environment, as well as climate changes » Monitoring of customer satisfaction
EMPLOYEES	<ul style="list-style-type: none"> » Lifelong learning and training » Attractive jobs in the ICT sector » Equal development and work opportunities for all employees » Performance-based salary system » Motivational working environment » Modernly equipped workplaces
SHAREHOLDERS AND INVESTORS	<ul style="list-style-type: none"> » Application of corporate governance principles » Timely and objective information on all important Company's activities and business results
SUPPLIERS AND PARTNERS	<ul style="list-style-type: none"> » Joint improvement and enhancement of the supplier chain » Exchange of knowledge » Regular assessment of Quality and Environmental Management Systems
TRADE UNION	<ul style="list-style-type: none"> » Partnership » Consulting and involvement in the decision-making process » Support to TU activities, which include safeguarding the interests of its members
BUSINESS AND PROFESSIONAL ASSOCIATIONS	<ul style="list-style-type: none"> » Involvement in activities
GOVERNMENT BODIES	<ul style="list-style-type: none"> » Participation in passing legislation » Exchange of ideas » Promoting an environment conducive to business development
EDUCATIONAL INSTITUTIONS	<ul style="list-style-type: none"> » Support to educational initiatives » Conveying knowledge regarding the cutting-edge technologies » Financial aid
COMMUNITY	<ul style="list-style-type: none"> » Exchange of ideas » Support and cooperation regarding local initiatives » Financial aid

AREAS OF CORPORATE SOCIAL RESPONSIBILITY

Being a member of the Ericsson global corporation, the leader in ICT industry and the creator of global telecom trends, Ericsson Nikola Tesla has been implementing the principles of a socially responsible company in all segments of its operations. The Corporation also strongly supports achievement of the Millennium Development Goals by following the basic values of peace, equality, solidarity, tolerance, human rights observance, nature protection and responsibility distribution in offering aid to the least developed countries. The Corporation and all its members strongly support the development and implementation of information and communication technologies, since they believe this is the way to create circumstances for faster economic growth and society development as well as quality of life enhancement. The economic growth and environmental protection, do not necessarily contradict one another. On the contrary, investments into state-of-the-art technology may help in stimulating both areas and bring them to the green technology era. With that, Ericsson wishes to be the driving force and an agent in introducing rapid changes in the communications world. The number of broadband mobile access users increased last year by 30 percent worldwide to reach approximately 500 million users. This trend is expected to continue in 2011, and according to studies the number of users will double and reach one billion by the end of the year. The given trend is mainly due to easy available smart phones, tablets and notebooks, which are predicted to represent, globally, more than a half of all computers sold worldwide. This trend will continue in future too, and will result in almost 5 billion users of broadband internet by 2016. According to studies, the mobile data traffic will increase by approximately 25 times, mainly due to the use of video. The predictions are that the networked society, having networked all units that may see benefit from it, will result in 2020 with 50 billion of various networked devices. The need for information exchange among people and devices will be extremely strong. Such a networked society will be based on mobility, broadband access and “cloud” services. The ICT industry is a development leader of modern society. For example, according to estimations, a thousand of new broadband access users create 80 new jobs, and as of the national economy, a 10-percent increase in broadband access penetration is said to be contributing an additional one percent to GDP growth. Ericsson is ready for a prominent and active role in modern social and economic trends, thus creating new opportunities to people, business operations and society as a whole.

ICT impact on social development until 2020



Key areas impacted by the Corporation:

- » Projects of global importance (sustainability, energy, security, education, health care);
- » Leadership and management of changes in telecommunications, along with customers, partners and suppliers;
- » Using innovative solutions, competence and skills of specialists to improve operations in ICT sector, thus creating new opportunities in other sectors of human activities, like energy, security and health care.

In accordance with the guidelines of the Global Report Initiative (GRI), which represents the leading global framework for reporting on sustainable and responsible company's operations, Ericsson Nikola Tesla reports on the effects it has on its surroundings through economical, social and environmental dimensions.

Areas in which the Company expresses its social responsibility are:

- » Economic sustainability;
- » Inclusion of socially responsible practices in business strategy;
- » Working environment;
- » Market relations;
- » Environmental protection;
- » Community relations.

The Croatian Chamber of Economy and the Croatian Business Council for Sustainable Development awarded Ericsson Nikola Tesla, for the third time in a row, the Corporate Social Responsibility Index (CSR Index) for its positive practice towards key stakeholders within the category of large companies.



ECONOMIC SUSTAINABILITY

THE COMPANY'S CONTRIBUTION TO ECONOMIC PROSPERITY

With its business strategy Ericsson Nikola Tesla promotes principles of sustainable development, thus balancing its long-term growth and competitiveness with a positive impact on economic, environmental and social development of the community. Care about key stakeholders and the Company's business development is the cornerstone of business practice and an indicator of the total social responsibility in the sense of providing continually successful business operations, and sustainable development of the whole society.

At Ericsson Nikola Tesla, economic sustainability, implying financial stability and strategic development have been monitored by means of a Balanced Scorecard (BSC) and Key Performance Indicators (KPIs).

DIRECT AND INDIRECT CONTRIBUTION TO ECONOMIC PROSPERITY

Since economic sustainability is not only a concept within a company itself, Ericsson Nikola Tesla views its contribution in terms of the direct and indirect impact on the economic prosperity of the country as a whole. Direct impact is measured by traditional financial indicators which are also shown in this Annual Report - in the Financial Statements section. Indicators of added value from operations, which is distributed among all stakeholders, show that the Company yielded MHRK 457 added value from operations in 2010.

RECRUITMENT

Ericsson Nikola Tesla employs almost 1,600 people, mainly university graduates, making it a large Croatian company in terms of employment. Supposing that each employee has two to three members of the family, it is some 4.800 to 6.400 Croatian citizens with existence directly related to the Company's

ERICSSON NIKOLA TESLA - ADDED VALUE FROM OPERATIONS	
	2010
	HRK '000
Sales revenue	1,218,863
Other operating income	15,411
Financial income	41,408
Total income	1,275,682
Procurement and other operating expenses	-762,178
Amortization	-56,831
Value added distributed among:	456,673
» Employees	432,419
» Government (income tax)	0
» Financial institutions	192
» Shareholders	24,062

operations. Ericsson Nikola Tesla has been recognized as one of the best employers in Croatia. The Company offers its employees good working conditions, motivating them to develop their careers, as well as competitive earnings in relation to other Croatian companies. In order to recruit the best employees not only for present but for future too, the Company has established long-term partner relations with the Faculty of Electrical Engineering and Computing at the University of Zagreb, and the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture at the University of Split.

TAXES AND CONTRIBUTIONS

By paying taxes and contributions into central and local government budgets, Ericsson Nikola Tesla and its employees contribute to the work and development of areas important for the functioning of society as a whole - including science, education, health and infrastructure development.

PROCUREMENT

Ericsson Nikola Tesla requires its goods and service suppliers to meet high-quality standards and observe the Code of Conduct, which includes respecting basic human rights, occupational standards, environment management and the prevention of corruption. Suppliers are also familiar with a list of harmful materials, as well as those banned or with a limited usage, and they must prove that such materials are not present in their products. By conducting business with local suppliers, Ericsson Nikola Tesla strongly supports the growth and development of the local community.

IMPLEMENTATION OF NEW INFORMATION AND COMMUNICATIONS TECHNOLOGIES

Ericsson Nikola Tesla's experts have developed a wide range of e-products, such as e-Health, e-Cadastre, digital cities, Intelligent Transport Systems (ITS), radar and communication control systems for naval traffic, and offer them on the market. These products and services enable better utilization of natural resources, time management and quality of life improvement, as well as faster information access.

STANDARDIZATION OF BUSINESS CHAIN

Company experts are active participants in business chain standardization, in which all participants operate in a uniform manner, from design to the ecological treatment of products and solutions. This builds trust among all participants in the business process and also creates preconditions for all entities involved in the process to operate rationally and efficiently.

SHARING KNOWLEDGE

Ericsson Nikola Tesla's experts actively convey and share knowledge regarding new information and communications technologies, modern business models and ways of working as well as world standards they apply in business operations. Our experts are prominent members of numerous professional associations, they lecture vocational subjects at colleges and faculties and publish professional papers.

DIALOGUE AND CONSULTANCY

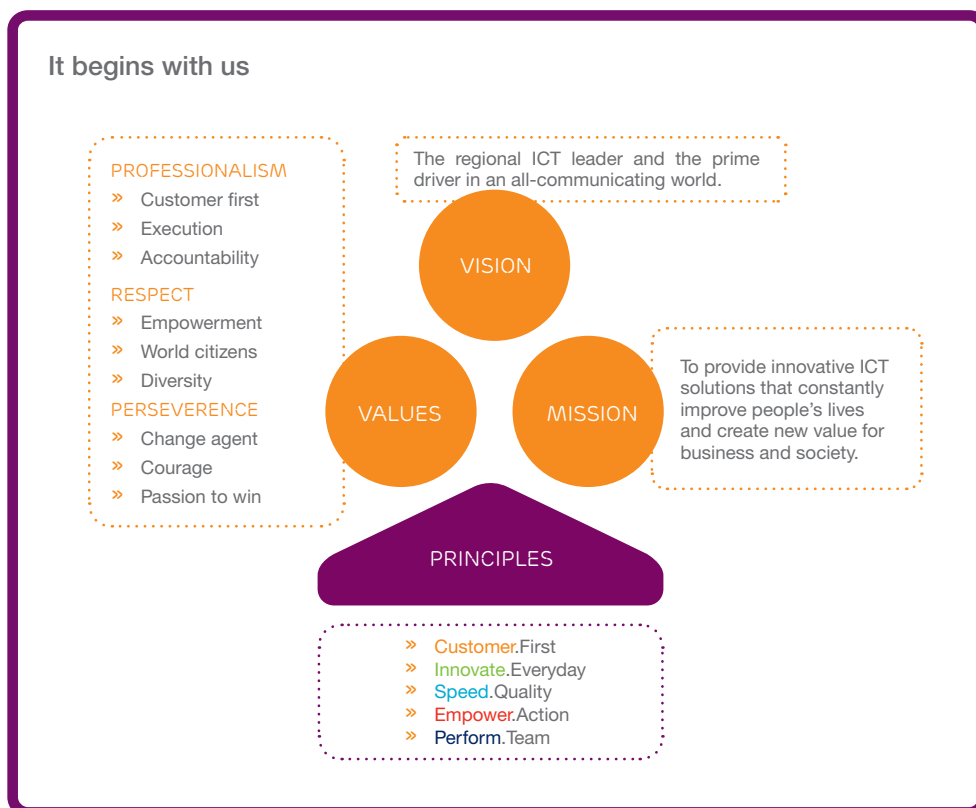
We encourage dialogue, open feedback, consultancy and exchange of opinions, thus contributing to shaping positive changes and initiatives within the community in which we operate.

CORPORATE SOCIAL RESPONSIBILITY AS AN INTEGRAL PART OF BUSINESS STRATEGY

IT BEGINS WITH US

The ICT industry has a positive impact on society from economic, social and environmental aspects. Ericsson Nikola Tesla's partnership with customers, operational excellence and technological leadership make a solid foundation for sustainable development and successful business. It makes it possible for the Company to realize its vision as a regional ICT leader. Ericsson seeks to be the prime driver in an all-communicating world, and to set the course of the communications development.

Ericsson Nikola Tesla seeks to lead the way in making positive changes in the society in which it operates. The Company creates added value; it has been permanently undergoing business transformation and has been constantly looking for new business opportunities aimed at a long-term growth. The Company's competitiveness stems from a permanent improvement based on innovative ideas, its human resources, corporate culture, its way of working and governance. The Company's way of working includes a robust corporate culture.



To realize our vision and complete our mission, uniform principles of work and Company values have to be used on a daily basis. Employees have to be permanently in the forefront of developing new products and solutions, and proactively engaged in the improvement of cooperation with customers, partners and other stakeholders. By design and offering of sustainable solutions that have a positive impact on the environment, Ericsson Nikola Tesla is providing its customers, partners and society at large with quality prerequisites for their growth and prosperity. Here at Ericsson Nikola Tesla we apply three core Corporate values: professionalism, perseverance and respect. The Company's messages and results should reach ordinary citizens to empower them to benefit from modern technology. By generating added value for our customers and end users, Ericsson Nikola Tesla wants to be recognized as an innovative partner offering products, solutions and services that have a global impact on people, businesses and society.

BUSINESS STRATEGY

Ericsson Nikola Tesla's business strategy is focused on design of new innovative ICT solutions, which will improve people's lives by creating new values for both business and social community. The strategy also includes the best practices of socially responsible business conduct. Employees are dedicated to the core Corporate values every day, no matter on what or where they work. These values are incorporated in all segments of business as well as in relationships with all other stakeholders.

Ericsson Nikola Tesla aims at:

- » Supply of products, solutions and services which exceed customers' expectations;
- » Application of efficient processes which are in compliance with the Company's strategy and business requirements;
- » Improvement of its products, solutions and services by means of permanent evaluation/review and technical innovations;
- » Building infrastructure essential for social development and improvement of people's lives;
- » Safe environment by use of energy saving products and solutions and eco ICT solutions;
- » Contribution to the GDP growth.

TOTAL QUALITY MANAGEMENT

Ericsson Nikola Tesla maintains a safe and healthy environment, and relies on technology for more efficient use of resources. Ericsson Nikola Tesla is successful in what it is doing owing to the application of the Total Quality Management (TQM). The Company strives to operational excellence in every activity. It implies the achievement of a high level of the organization maturity and process capability. The objective is to reach a high professional level in business conduct at which all key processes are optimally used and improved in all organizational units. Thus the Company meets and even exceeds customers' expectations in a cost effective way.

The implementation of TQM principles provides permanent improvements and involvement of all employees. The key to this goal is an integrated Management System. It is a prerequisite for operational excellence that is contributing to increased customer satisfaction, cost reduction and better competitiveness.

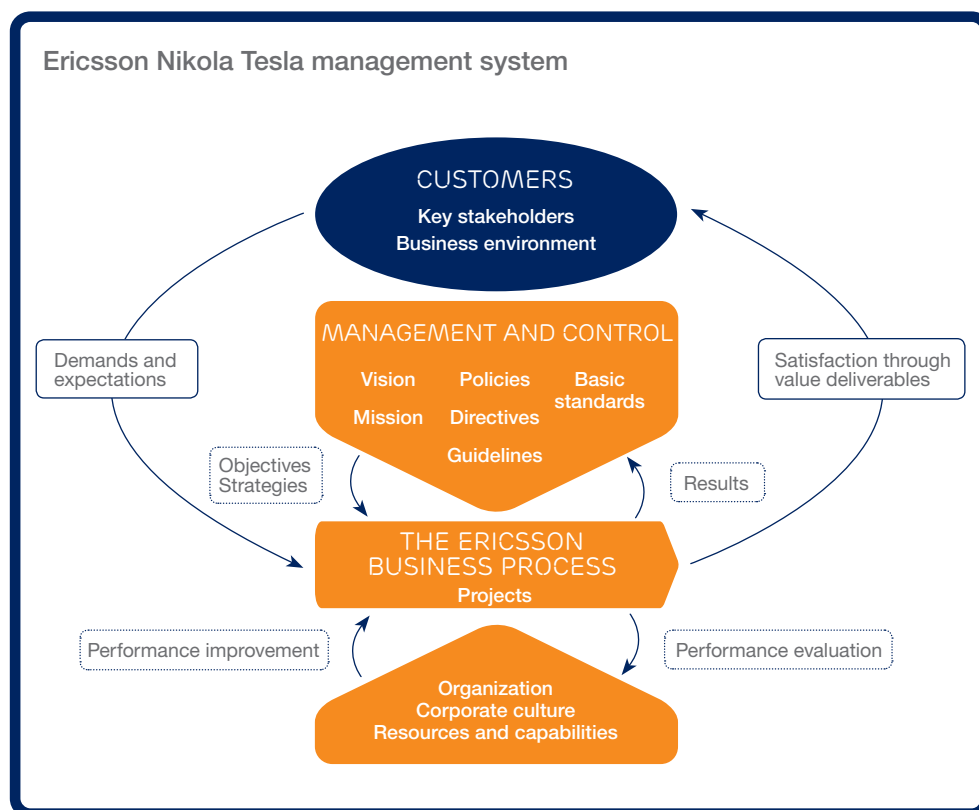
INTEGRATED MANAGEMENT SYSTEM

Management System is a powerful tool for both Company management and employees in their everyday work that can be accessed on the intranet. The system enables the execution of set business goals.

It monitors all Company's management elements with focus on "flows of values" of a business deal that are defined as a business process.

Ericsson Nikola Tesla Management System is compatible with the Ericsson Group Management System (EGMS), and is based on ISO 9001 standards for Quality Management. However, in today's complex world of telecommunications, compliance with only one standard is no longer an option. There has to be synergy among various standards, models and methods. The integrated Management System meets the requirements of other ISO Management Systems standards such as the Environmental Management System (ISO 14001), the Occupational Health and Safety Management System (OHSAS 18001), the Information Security Management System (ISO 27001) and the Quality Management System for Medical Devices (ISO 13 485), as well as the requirements of the TL 9000 Quality Management System. In addition, the integrated Management System is an integral part of the Company's system of internal control. Certain elements of different models and methods such as CMMI (Capability Maturity Model Integration), EFQM (European Foundation for Quality Management) and Six Sigma are also integrated into the Management System.

By means of the integrated Management System, the Company defines functions and responsibilities, organization and other factors that play a significant role in operational excellence and design of high-quality products, solutions and services. The integrated Management System is regularly updated and adapted to organizational and management changes.



CERTIFICATES

Ericsson Nikola Tesla regularly certifies its Management System by using independent notified bodies. At present, the Company holds the following certificates:

- » ISO 9001 Certificate for Marketing, Sales and Provisioning of Telecommunications Products, Solutions and Services, DNV, Sweden (as a part of the regional certification);
- » ISO 9001 Certificate for Research and Development in Information and Communication Software Technology, SIQ, Slovenia;
- » ISO 14001 Certificate for Environment Management Systems for Management, Development, Product Management, Production, Supply, Sales and Support of Telecommunications products and services, DNV, Sweden (as a part of the Ericsson Group certification);
- » ISO 13485 Certificate for Development, Marketing, Sales and Production of Healthcare Solutions; MDD IIa certificate and CE mark for Ericsson Mobile Health, DNV, Sweden.



WORKING ENVIRONMENT

OUR EMPLOYEES

Ericsson Nikola Tesla is a successful Croatian company. As a part of the global Ericsson Group, it operates on the global ICT market. Ericsson Nikola Tesla's most valuable assets are its employees, who are our intellectual capital and make us different from our main competitors. Our employees determine how much faster, better and more successful we will be than other players in the market.

Ericsson Nikola Tesla's employees are highly educated, competent people who follow the Company's strategic objectives responsibly and professionally, and are able to create added value through innovativeness and expertise.

One of the strategic goals of Ericsson Nikola Tesla is to become the employer of choice, recognized for its leadership, culture, and best practices that attract, optimize, and hold top talent, achieving Corporate objectives.

To excel in our fast-changing industry, we have set three key principles:

- » Business ethics;
- » Equal opportunity and working conditions for all employees;
- » Equality and protection of human rights.

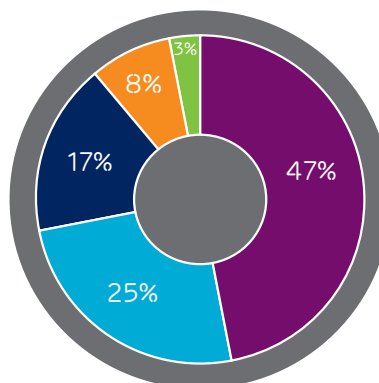
Employee structure:

- » 1,595 employees (as at December 31, 2010);
- » 85 percent of university graduates, the majority of whom are electrical engineers;

**Ericsson Nikola Tesla employees
(according to age) ***



* as at December 31, 2010



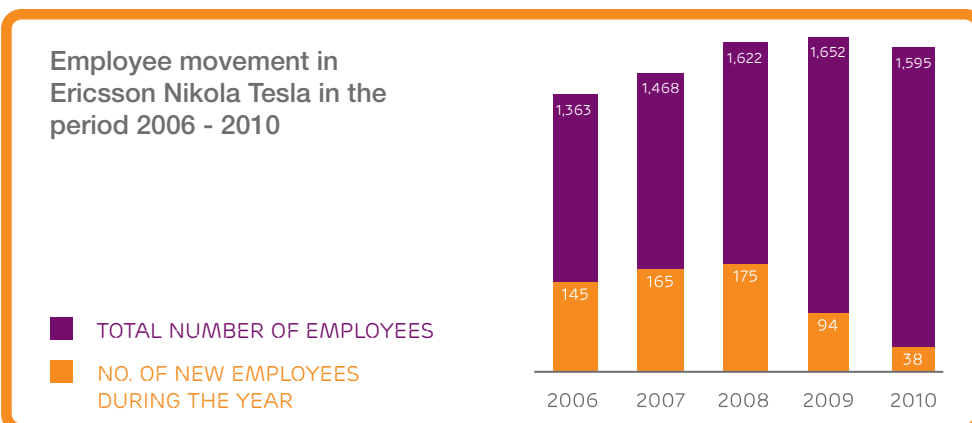
- » 8 percent of Masters of Science and Doctors of Science;
- » Average employee age is 38;
- » 597 employees (37 percent) are younger than 32;
- » Average employment duration is 12 years;
- » 26 percent of employees have two or less years of working experience in the Company;
- » Gender ratio (male vs. female): 74 percent : 26 percent;
- » Average manager age is 43;
- » 19 percent of managers are women.

EMPLOYEE TURNOVER

Over the period of the last five years, 617 new employees, the majority of whom are electrical engineers, have been hired in our organizational units in Zagreb and Split. The incentive being new responsibilities that the Ericsson organization gave the Company in the field of research and development, service delivery center, and other expert centers that have been established in the meantime. On the one hand, hiring new people is a strength because they bring knowledge, new ideas and enthusiasm. On the other hand, there is a risk of increased turnover, since young people are more prone to change jobs.

INVESTMENT IN COMPETENCE DEVELOPMENT

Ericsson Nikola Tesla has been constantly taking care that its employees acquire new knowledge, competences and skills. It is done in a close cooperation with Ericsson Academy that is providing education to all Ericsson's employees. Quite often our employees participate in regional projects and thus acquire new competences.

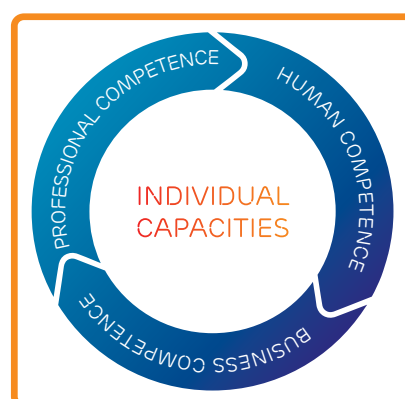


Knowledge is acquired at training courses organized in the Company and/or in training centers in the country or abroad, by e-learning, by proprietary software tool for exchange of expert knowledge, at seminars and conferences, by participation in international projects, etc.

In 2010, employees attended the following training programs:

- » **Professional competence development programs**
Courses are customized in accordance with current needs and wanted position. In certain cases certification is included. The course subject: Long Term Evolution (LTE) and all-IP technologies.
- » **Human resources and business competence development program**
New competences and skills in the field of finance, communication and presentation, management, team work, change management, negotiating, resolution of conflicts, etc. Through Ericsson Academy, our employees had access to lectures held at the most prestigious universities in the world, such as Harvard Business School.
- » **Project management skills development**
The program is intended for employees who work on projects, and training is organized in cooperation with external institutions, including the Project Management Institute (PMI). The program covers each aspect and level of knowledge, from basic to advanced levels, and includes testing and international certification for the Project Manager function.
- » **Management competence development programs**
Management competence development programs include the Leadership Core Curriculum (LCC) Program, Assessment & Development Center, which is a program for assessment and development of young managers, Corporate leadership programs as well as job rotation within the Company and out of it and work in international teams.
- » **Postgraduate study**
For a number of years the Company has encouraged and awarded scholarships to employees who want to get their doctor's degree either in their original field of expertise or in business management.
- » **Mentorship program**
Because the Company hires such a large number of new young employees, there is a number of trained mentors giving their support to new employees, so they can faster acclimatize to a new environment on their arrival or when they change their workplace. Mentors also provide support to personal and professional development of new employees, and participate in the planning of their carriers. Mentors also take courses, especially in human relations, communication, motivation, learning, etc.

**WE INVEST
IN PEOPLE
AND THEIR
COMPETENCES**



WORKING ENVIRONMENT

The Company has been constantly working on the enhancement of the working environment in order to increase employee satisfaction and motivation by providing:

- » Attractive jobs and clearly defined roles for every employee in the fulfillment of common objectives;
- » Opportunities for lifelong learning and development, equal development and working conditions for all employees;
- » Recognition of individuals and teams who contribute to the Company results the most;
- » Performance-based salary system accompanied by various incentive reward schemes;
- » Stimulative working environment, modern workplaces and tools;
- » Flexible working hours;
- » Care of employees' health and high health care standards;
- » Support to young parents by organizing day care centers in the immediate vicinity of the Company;
- » Recreation and socializing in sports, cultural and other clubs.

MONITORING EMPLOYEE SATISFACTION

Employee satisfaction is monitored by means of the Dialog survey, which is conducted once a year. The survey is as an important tool for monitoring employees' satisfaction and getting employees' opinion about various segments of organizational and business issues. Employees and their managers jointly propose changes and improvements of all segments of work.

In 2010 employees' participation was very high (94 percent), which provides a good sample for results analysis and further improvements. The results from 2010, just like from previous years, are the level of excellence. Areas that remain in focus are the Company capability to adapt to changes, operational excellence and permanent competence development.

Employee satisfaction indicators for 2010:

- » **Future Capital Index (FCI)** was introduced last year for better understanding and constant adaptation to changes. The Index is important for the Company's future since it reflects the Company's capability to successfully adapt to changes by means of operational excellence, innovativeness in all business processes and permanent work with talented individuals. The Index has remained at the last year level (77 percent).
- » **Human Capital Index (HCI)** is 2 percent higher than in the previous survey (79 percent), which is putting the Company at the level of excellence. Within the Human Capital Index, the employee satisfaction indicator has the largest growth in comparison to the last year. It addresses the group of questions related to learning, perception of employee's own skills and competence, and continuous transfer of employees' knowledge and experience to others. For Ericsson Nikola Tesla as the company of knowledge aimed at innovations, the growth trend of this indicator is an additional sign that we are ready for future challenges.



- » **Motivation Index** shows that in our Company 73 percent of employees are motivated, those committed to and satisfied with their jobs.
- » **Leadership Index** is 1 percent higher than the last year and it is now 84 percent.
- » **"It begins with us"** is a new index. It was introduced to measure a degree of integration of a new Ericsson way of working into everyday life and work of each employee. The Index value is 84 percent and witnesses a very high degree of acceptance of a new way of working by our employees.

HEALTH AND SAFETY AT WORK

Ericsson Nikola Tesla systematically takes care of its employees' health and improvement of their working conditions. Among numerous actions taken in 2010, we highlight the most important ones:

- » **Implementation of health and safety at work management system**
Monitored indicators are the number of injuries at work, preventive and corrective measures defined in accordance with danger assessment, direct monitoring and measures proposed at regular meetings of the Health and Safety at Work Committee. In 2010 four meetings took place. In 2010 not a single injury occurred on the Company premises. Eight injuries occurred while arriving to or leaving from work.
- » **Regular medical checkups**
In the Company clinic, two general practitioners and two nurses as well as one dentist and one nurse work permanently. In addition to regular medical checkups and specialized examinations, examinations of employees traveling to high-risk countries are also arranged. The results of regular medical checkups are processed and analyzed. They are discussed at the meetings of the Health and Safety at Work Committee and, based on the results and discussions, decisions are made on measures to prevent disease and improve employees' health. Employees can also make blood and urine tests as well as cardiological, gastroenterological, endocrinological and gynecological examinations.
- » **Doctor at the workplace**
Day-to-day cooperation between the occupational medicine specialist and occupational safety experts positively affects health and safety at work and increases employees' satisfaction. Workplace injury and disease risk assessment study has been developed, including risks at workplaces where employees are working on personal computers. The study also includes corrective measures for areas where there is space for improvement that will contribute to health preservation and health and safety at work.
- » **Recreational activities**
Various sports and recreational programs intended for and adapted to needs of employees have been taking place on the Company premises for eight years in a row. In addition, the Company supports numerous employees' sports and recreational activities outside the Company premises.
- » **Education and training of employees**
In addition to industrial safety training according to law, all new employees attend training courses on health protection and health and safety at work at the introductory seminars. Special training courses are organized for managers, so they would understand how important it is to strictly apply health and safety at work rules and regulations and the impact these rules and regulations have on to the satisfaction of employees and business success of the Company.

MARKET RELATIONS

Ericsson Nikola Tesla permanently improves relations with its customers, suppliers, partners and related stakeholders, and respects its competitors. In doing so, the Company follows its core values – professionalism, respect and perseverance. In particular, it means that the Company requires from all its employees and stakeholders (such as suppliers and their subcontractors) to act in line with the provisions of the Code of Conduct and the Code of Business Ethics.

The purpose of the Code of Conduct is human rights protection, promotion of fair recruitment conditions, safety at work, responsible environmental management and high ethical standards.

The Code of Business Ethics pertains to personal responsibilities in relations with employees, customers, suppliers, shareholders and others, with whom one communicates or does business with. With the Code of Business Ethics, the Company covers legal compliance, protection of confidentiality, protection and proper use of company assets, respectful communication and human rights protection, conflict of interests, transparency, environmental protection and supports reporting of illegal or unethical behavior.

The Company continuously enhances its relations with different customers in the domestic and foreign markets we operate in. We adjust to meet the customer's needs, offer innovative solutions for their business growth, thus fostering partnerships and building mutual trust. Our ways of working with our customers are validated through a Customer Satisfaction Survey, on an annual basis.

We build long-time relationships with our suppliers through dialogue, knowledge exchange and application of up-to-date ways of working. Our product and service suppliers are expected to observe high-quality standards and provisions of our Code of Business Ethics. In addition, the Company assessors make annual external assessments of major domestic suppliers through a questionnaire, prepared in line with applicable standards. Ericsson Nikola Tesla applies an e-sourcing system that offers the highest levels of professionalism, efficiency and collaboration.



INTEGRITY
AND ETHICS
CHARACTERIZE
THE WAY WE
CONDUCT
BUSINESS

CODE OF BUSINESS ETHICS

No employee should be discriminated against because of e.g. race, color, sex, sexual orientation, marital status, pregnancy, parental status, religion, political opinion, nationality, ethnic background, social origin, social status, disability, age or union membership.

CORPORATE GOVERNANCE

Corporate governance is the framework for business operations and supervision of the Company. Its objective is to create a long-term economic value for shareholders. Ericsson Nikola Tesla's Management Board and Supervisory Board strictly observe fundamental principles of corporate governance to ensure equality and protection of shareholders' rights, business transparency and responsibility towards all stakeholders. Ericsson Nikola Tesla endeavors to inform the community about its activities and business results in timely and objective manner.

The principles of corporate governance in Ericsson Nikola Tesla, which the Company adopted in April 2005, are based on laws of the Republic of Croatia and the OECD recommendations on Principles of Corporate Governance, which clearly define the rights and obligations of the Management Board, Supervisory Board and shareholders (http://www.ericsson.hr/investors/corporate_governance.shtml).

MANAGEMENT BOARD

The role of the Management Board is regulated by the Croatian Company Act, the Statute of Ericsson Nikola Tesla, and internal bylaws. The Management Board has to conscientiously perform its duties, taking into account the best interests of the Company and shareholders.

Ericsson Nikola Tesla's Management Board has one member being appointed by the Supervisory Board to a five-year term with the possibility of re-appointment. The Management Board has to report on financial and business results, strategy and operational planning to the Supervisory Board. The Management Board also has to report on its performance to the Annual Meeting of Shareholders and to implement decisions made by the Annual Meeting of Shareholders. The Management Board remuneration depends on the Company's business results and is determined by the Supervisory Board.

SUPERVISORY BOARD

The basic role of the Supervisory Board is to supervise the Management Board's business conduct. While doing so, the Supervisory Board has to uphold high ethical standards and look after the best interests of the Company and its shareholders. The Supervisory Board has five members elected to a four-year term with the possibility of re-election. The Supervisory Board submits reports about its supervision of business conduct, and gives its opinion about proposal for allocation of profit and makes proposals on whom to appoint as the Company auditor at the Annual Meeting of Shareholders. According to the decision made by the Annual Meeting of Shareholders, members of the Supervisory Board are remunerated on a monthly basis in the amount of a half of Company employee's average gross salary. Ericsson representatives renounced the remuneration in accordance with the Corporate policy.

In 2010, Ericsson Nikola Tesla's Supervisory Board held four regular and two extraordinary meetings. At these meetings, financial performance, the situation in domestic and export markets, market conditions and ICT industry trends as well as business plans and strategic projects, business risks, internal audit results and human resources issues were discussed. In addition, the Supervisory Board monitored business development and responsibilities of the Research and Development Center, the Service Delivery Center and Business Ericsson Test Environment.

At the extraordinary Supervisory Board meetings, payment of dividend and write-off of the Kazakhstan receivables were discussed.

The Supervisory Board examined and supported the Company business strategy for the period 2011–2015 and focus areas and strategic programs needed for future growth of the business.

The Company management identified key objectives for 2011 with clearly defined activities and measurement methods, which were also approved by the Supervisory Board.

In 2010, the Supervisory Board membership changed. Dubravko Radošević, scientific associate at the Institute of Economics in Zagreb was appointed as a new member of Ericsson Nikola Tesla's Supervisory Board by the Annual Meeting of Shareholders held on May 20, 2010.

AUDIT COMMITTEE

In order to effectively fulfill its obligations related to the supervision of the Company's business, including annual financial statements, the Supervisory Board established the Audit Committee in June 2006.

In 2010, the Audit Committee held five meetings to discuss financial performance during the year and annual financial statements, the 2010 audit plan, internal control and risk management systems and attended to any other business defined by the Audit Act. The Audit Committee regularly reported on its conclusions and recommendations to other members of the Supervisory Board. At the date this report was issued, the members of the Audit Committee were Ignac Lovrek, Chairman, and Carita Jönsson, member.

ANNUAL MEETING OF SHAREHOLDERS

Company shareholders exercise their rights during the Annual Meeting of Shareholders. The Annual Meeting of Shareholders makes decisions about allocation of profit, changes/amendments of the Company Statute and appointment or suspension of members of the Supervisory Board. The Annual Meeting of Shareholders evaluates performance of the Management Board and Supervisory Board, makes a decision to hire an independent auditor to perform the audit of the annual financial statements and attends to any other business in accordance with the law or the Company Statute.

>> TAKING CARE OF SHAREHOLDERS' INTERESTS

>> TIMELY AND OBJECTIVELY INFORMING
THE COMMUNITY

>> COOPERATION AND COMMUNICATION

>> APPLYING CORPORATE GOVERNANCE PRINCIPLES

>> NURTURING A POSITIVE IMAGE THROUGH THE CODE OF ETHICS



ENVIRONMENTAL PROTECTION

Responsible environmental relations are an integral part of Ericsson Nikola Tesla's operations and culture. Key documents that define environmental relations are the Environmental Management Policy and Code of Business Ethics.

Regular and systematic checks of both internal and external system functionality are carried out in order to retain the acquired ISO 14001 Certificate.

The Company's approach to environmental protection has been verified through various questionnaires by institutions specialized in sustainability research.

DEVELOPING PRODUCTS AND SERVICES TO IMPROVE QUALITY OF LIFE

Through its ICT solutions, products and services, the Company has been recognized for creating new opportunities in "green technology" that has a positive impact on operations, human lives and the environment, as well as on climate change. Ericsson Nikola Tesla has developed and participated in the implementation of a variety of e-products, such as e-Health, e-Cadastre, digital cities, Intelligent Transport Systems, and radar and communications control systems for naval traffic.

IMPLEMENTING REGULATIONS AND NORMS

Company activities are in line with international standards and current national regulations related to environmental protection. Company professionals actively participate in the process of alignment of Croatian regulations to EU standards. Regulation demands on individual segments of the environment are followed, and their implementation is regularly monitored.

WASTE MANAGEMENT

A total and systematic education on all types of waste that may be produced in the location has been carried out. The rulebook on electric and electronic waste regulates the commitment of producers and direct importers to report their business to the Environment Protection Fund and to pay the corresponding fee for imported and produced equipment, respectively, on a kilogram basis.

The Company meets not only commitments regulated by the given rulebook, but also implements electronic waste management in the location, and in line with requirements by some customers, also takes care of their electronic equipment waste management.

Furthermore, the Company has organized collection, selection and ecological management of paper, glass, plastic and wooden waste, cables, batteries, toners, fluorescent tubes and communal waste.

SYSTEMATICALLY OPTIMIZING AND REDUCING ENERGY CONSUMPTION

By implementing a central monitoring system for consumption of all energy sources, the preconditions for quality management and maintenance of the energy installation system were established and resulted in a reduction of energy consumption (water and steam) and in the optimization of all quality parameters of electric energy consumption. Increased electric energy consumption follows the trend of enlarged capacity, new tools and new working areas. By monitoring the entire pipe system, repair work was conducted timely and unnecessary loss of water was eliminated.

RELATIONS WITH SUPPLIERS

Impacts on the environment can be efficiently managed if the total supply chain is considered. The supply chain impact on the environment has been continually verified through assessment and audit of suppliers.

Ericsson issued a Code of Conduct for its suppliers covering requirements on basic human rights, standards of work, and environmental management and prevention of corruption in the work place. The requirements to suppliers with regard to the environment are as follows: to have an environmental management system, environmental and production friendly product design, to provide details of product material contents and transportation. Suppliers are informed of the list of harmful materials and materials that are limited or banned for usage, and must prove that such materials are not contained in their products.

E-APPLICATIONS

The Company's engagement in the high technology segment, and its leading role in research activities as well as in information and communications technologies, was the main reason for implementation of e-applications in our business process. Thus, we do not only promote information and communications technology, which is a must for competitiveness for all economic sectors and subjects, but we considerably improve and speed up business processes, save resources, time and money.

When it is about business trips, we have implemented smart solutions that save money and reduce CO₂ emission, especially by using virtual solutions like videoconferencing.

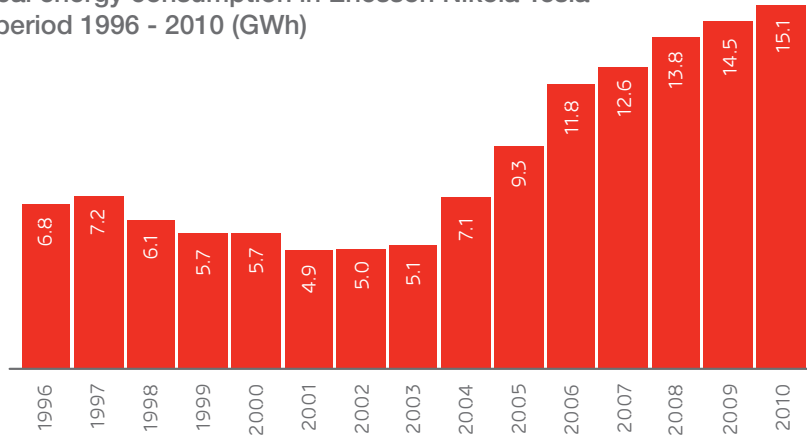
We strive to reduce the impact on the environment and apply remote delivery of particular services (in network design, optimization, integration and upgrade). By implementing such a way of working, the need for traveling is reduced. Furthermore, we use intelligent tools for cooperation, thus providing the same level of customer satisfaction, regardless of remote delivery.

Total quantity of waste produced at Ericsson Nikola Tesla in 2009 and 2010

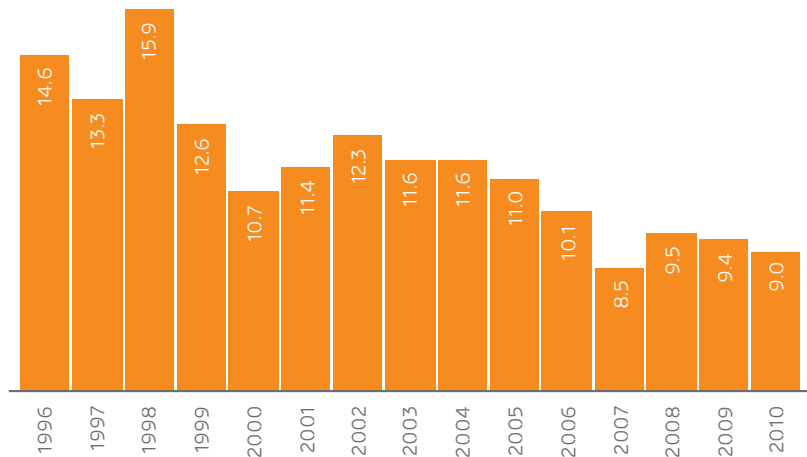
Waste name	2009 (in tonnes)	2010 (in tonnes)	INDEX 2010/2009
Used up activated charcoal	0.39	0.00	-
Waste printing toners	0.91	0.36	40
Packing	158.20	122.28	77
Castaway equipment – electronic waste	14.83	19.66	133
Various storage batteries	1.54	0.88	57
Glass	3.04	1.65	54
Aluminum	0.02	0.00	-
Iron and steel	50.07	32.07	64
Cable conductors	0.00	0.22	-
Fluorescent tubes	0.43	0.20	47
Small-size batteries	0.23	0.25	109
TOTAL	229.66	177.57	77



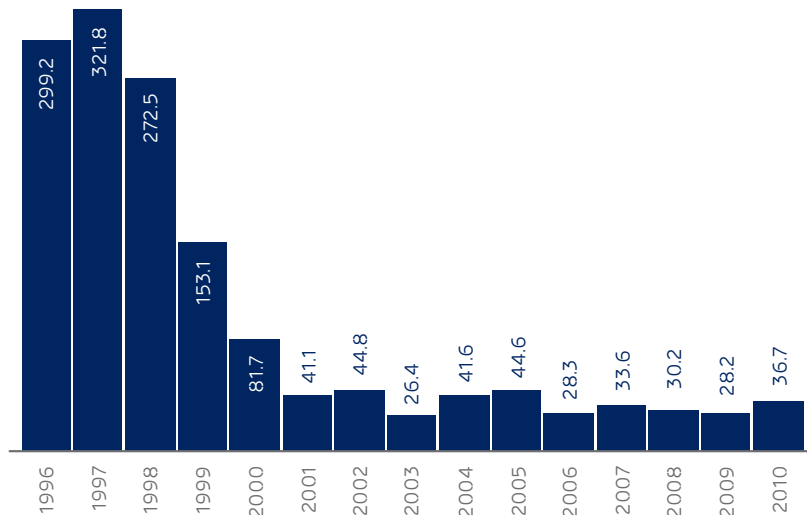
Electrical energy consumption in Ericsson Nikola Tesla
in the period 1996 - 2010 (GWh)



Steam consumption (heating) in Ericsson Nikola Tesla
in the period 1996 - 2010 (in '000 tonnes)



Fresh water consumption in Ericsson Nikola Tesla
in the period 1996 - 2010 (in '000 m³)



EDUCATION IN ENVIRONMENTAL PROTECTION

Environmental protection specialists, as a part of the team in charge of business excellence and quality in Ericsson Nikola Tesla, contribute to improvement of business processes within the organization.

Education, awareness development and an increase of employee motivation for enhancing the status of environmental protection are constantly carried out. Each organizational unit has a coordinator for the environment who acts in line with the organizational unit's scope of work and its impact on the environment. Quality, environmental protection, and occupational health and safety experts perform management system audits and make improvement proposals in order to educate suppliers, partners and contractors.

Through cooperation with stakeholders, such as business partners and educational institutions, Ericsson Nikola Tesla's professionals convey their knowledge and experience and thus contribute to building up the environmental awareness.

ICT RESPONSIBLE
FOR 2%
OF GLOBAL
CO₂
EMISSIONS

BY IMPLEMENTING
ICT TECHNOLOGIES
INTO OTHER
INDUSTRY
SEGMENTS, CO₂
EMISSION MAY BE
REDUCED BY
5 TO 20 %

COMMUNITY RELATIONS

Ericsson Nikola Tesla has always been aware of both its financial and social responsibilities, especially concerning the community. With its proactive approach in recognizing needs, support and partnership development with the community, the Company strives in coordinating its programs with international best practices. Its strategy of corporate social responsibility as well as sponsorship and donation policy, are very helpful in priority setting as well as in defining the tools and methods for recognizing and realizing socially beneficial projects. With regard to our strategic orientation that is focused on up-to-date technology, we prioritize projects in which our products, solutions, services and technology, as well as exchange of knowledge and information are playing a key role. The Company always tries not only to finance the project, but offers its resources, technology, competences, skills and time, thus enhancing the community in which it operates.

In 2010, the Company realized valuable educational, health care, cultural, sports, humanitarian and similar socially beneficial projects, such as:

- » Sponsorship and participation in various scientific and professional conferences;
- » Expanding scientific, research, development and educational cooperation with the Faculty of Electrical Engineering and Computing of the University of Zagreb and the Faculty of Electrical Engineering, Mechanical Engineering and Naval Architecture of the University of Split;
- » Continuation of financing the project on the scientific development of a junior researcher not included in the Ministry of Science, Education and Sports financing quota;
- » Support to the National Foundation for the Support of Pupil and Student's Standard;
- » A large number of wet wall dryers and aggregates were provided for areas hit by floods and similar natural disasters, accompanied by power supply shortages. The equipment was offered to the Croatian Red Cross;
- » Volunteering and socially beneficial work for employees in Finance unit who participated in clean up of green area around Jarun lake, extending assistance with decorating of Trešnjevka retirement and nursing home as well as extending help to socially handicapped citizens in Zagreb;
- » Employees continuously participate in voluntary blood donations organized in the Company's premises.

HELPING THE
COMMUNITY

OUR PROGRAMS
ARE HARMONIZED
WITH THE BEST
INTERNATIONAL
PRACTICE

AWARDS AND RECOGNITIONS IN 2010

- » Gordana Kovačević, President of Ericsson Nikola Tesla, was appointed a member of the Economic Council to Ivo Josipović, President of the Republic of Croatia.
- » Gordana Kovačević was granted the European **LeaderSHE** Award 2010 by Forum Invest, Vienna. Owing to her exceptional business results and her ability to initiate change and to inspire, she was recognized as one of the region's most successful entrepreneurs. The award was given at the LEADER SHE International Forum – The Creative Management of Change, organized in Vienna.
- » Kapital Network, a business news channel awarded Ericsson Nikola Tesla for social responsibility.
- » The International organization Superbrands chose Ericsson Nikola Tesla, one of the leading brands in Croatia, as the **Superbrands Croatia 2010**.
- » The Croatian Public Relations Association awarded Ericsson Nikola Tesla the annual **Grand PRix 2010** in the large company category for Ericsson Nikola Tesla's 60th anniversary project.
- » The Zagreb Stock Exchange and newspaper *Poslovni dnevnik* awarded Ericsson Nikola Tesla for the best relations with investors.
- » At the Vidi e-novation competition, Ericsson Nikola Tesla was awarded **Golden Tesla's Egg** for its innovative Ericsson Mobile Health product.



Grand PRix 2010 for
public relations



LeaderSHE Award 2010



Award for social
responsibility



Award for the best
relations with investors



Golden Tesla's Egg





FINANCIAL STATEMENTS 2010
Ericsson Nikola Tesla d.d.





COMPANY PROFILE

HISTORY AND INCORPORATION

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

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

According to the ownership structure as at 31 December 2010, Telefonaktiebolaget LM Ericsson (Ericsson) holds 49.07% of the Company's share. A further 0.23% is held by The Croatian Privatisation Fund and 0.70% is held as treasury shares. Other shareholders own the remaining 50.00% of the Company's shares.

PRINCIPAL ACTIVITIES

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

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

SUPERVISORY BOARD, MANAGEMENT BOARD AND EXECUTIVE MANAGEMENT

The Supervisory Board

The Supervisory Board members during 2010 and up to the release of these statements were:

Roland Nordgren	Appointed on 27 May 2008	Chairperson
Ignac Lovrek	Reappointed on 31 May 2007	Member; Vice-Chairperson
Carita Jönsson	Reappointed on 27 May 2008	Member
Dubravko Radošević,	Appointed on 20 May 2010	Member
Zvonimir Jelić	Reappointed on 18 June 2010	Member and employees' representative

The Management Board

The Management Board has one member:

Gordana Kovačević	Reappointed on 1 January 2010	President
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COMPANY PROFILE (CONTINUED)

Executive management

As at 31 December 2010, the Company's executive management comprised:

ETK Core MT:

Gordana Kovačević	Company President
Andrew Skelton	Company CFO
Hrvoje Benčić	Director, Engagement Practices and ETK Customer Operations
Lars Olander	Director, Research and Development Center
Milan Živković	Director, Strategy and Business Development

ETK Extended MT:

Core MT members

Alen Ludaš	Head, Proposal Management, RWCE
Boris Drilo	Director, ICT for Industry and Society
Branko Dronjić	Regional Manager, BETE
Damir Bušić	Manager, Operations & Competence Centre BSS&OSS Croatia
Dragan Fratrić	Manager, General Services
Franjo Mudrovčić	Acting Director, Sales & Marketing for CIS market
Goran Ožbolt	Director, Sales and Marketing for Tele2 and Alternative Operators
Ivan Barać	Director, Sales and Marketing for T-HT
Jagoda Barać	Director, Sales and Marketing for Neighboring countries
Marijana Đuzel	Director, HR and Organization (including Legal Affairs)
Mathias Danielsson	Head, Competence Domain Internet Protocol, Broadband & Core, RWCE
Milan Popović	Manager, ETK Project Management Office
Miroslav Kantolić	Director, Sales and Marketing for VIPnet and Si.mobil
Snježana Bahtijari	Director, Marketing and Communications (including CSR)
Snježana Ivezić-Torbarina	Manager, Competence Domain Media and Applications
Tihomir Šicel	Director, Sales & Marketing for Industry and Society



RESPONSIBILITIES OF THE MANAGEMENT AND SUPERVISORY BOARDS FOR THE PREPARATION AND APPROVAL OF THE ANNUAL FINANCIAL STATEMENTS

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

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

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

The financial statements set out on pages 74 to 133 were authorised by the Management Board on 8 March 2011 for issue to the Supervisory Board and are signed below.

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



Independent auditor's report

To the Shareholders of Ericsson Nikola Tesla d.d.

We have audited the accompanying financial statements of Ericsson Nikola Tesla d.d., which comprise the statement of financial position as of 31 December 2010 and the statements of comprehensive income, changes in equity and cash flow for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with International Financial Reporting Standards, 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.

Auditor's Responsibility

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

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

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

Opinion

In our opinion, the financial statements present fairly, in all material respects, the financial position of Ericsson Nikola Tesla d.d. as of 31 December 2010 and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

PricewaterhouseCoopers d.o.o.
 PricewaterhouseCoopers d.o.o.
 Zagreb, 8 March 2011

PRICEWATERHOUSECOOPERS 
 za reviziju i konzalting d.o.o.3
 ZAGREB, Alexandera von Humboldta 4

This version of our report is a translation from the original, which was prepared in Croatian language. All possible care has been taken to ensure that the translation is an accurate representation of the original. However, in all matters of interpretation of information, views or opinions, the original language version of our report takes precedence over this translation.



Ericsson Nikola Tesla d.d.

STATEMENT OF COMPREHENSIVE INCOME

for the year ended 31 December 2010

		2010	2009
	Notes	HRK '000	HRK '000
Sales revenue	3	1,218,863	1,400,011
Cost of sales		(1,012,567)	(1,213,945)
Gross profit		206,296	186,066
Other income	6	15,411	17,325
Distribution expenses		(56,973)	(72,894)
Administrative expenses		(34,037)	(37,024)
Other expenses	7	(145,946)	(27,793)
Operating profit		(15,249)	65,680
Finance income	9	41,408	61,894
Finance expense	9	(192)	(757)
Finance income - net		41,216	61,137
Profit before tax		25,967	126,817
Income tax	10	(1,905)	1,630
Profit for the year		24,062	128,447
Other comprehensive income		-	-
Total comprehensive income for the year		24,062	128,447
Earnings per share (HRK)	11	18.30	98.09

Ericsson Nikola Tesla d.d.

STATEMENT OF FINANCIAL POSITION

as at 31 December 2010

		2010	2009
ASSETS	Notes	HRK '000	HRK '000
Non-current assets			
Property, plant and equipment	12	128,643	146,351
Intangible assets	13	4,814	4,425
Loans and receivables	14	10,358	278,897
Equity securities		45	45
Deferred tax assets	15	9,165	12,295
Total non-current assets		153,025	442,013
Current assets			
Inventories	16	44,774	24,059
Trade receivables	17	346,982	451,247
Receivables from related parties	29(c)	75,406	58,905
Income tax receivable		3,054	9,452
Other receivables	18	58,232	29,588
Financial assets at fair value through profit or loss	19	63,254	120,873
Prepayments and accrued income		6,508	1,371
Cash and cash equivalents	20	673,926	414,935
Total current assets		1,272,136	1,110,430
TOTAL ASSETS		1,425,161	1,552,443



Ericsson Nikola Tesla d.d.

STATEMENT OF FINANCIAL POSITION (CONTINUED)

as at 31 December 2010

		2010	2009
EQUITY AND LIABILITIES	Notes	HRK '000	HRK '000
Equity			
Share capital	21(a)	133,165	133,165
Treasury shares	21(b)	(16,251)	(34,173)
Legal reserves	21(c)	20,110	20,110
Retained earnings		934,000	1,081,121
Total equity		1,071,024	1,200,223
Non-current liabilities			
Interest-bearing borrowings	24	3,346	4,965
Employee benefits	25	4,891	5,126
Total non-current liabilities		8,237	10,091
Current liabilities			
Payables to related parties	29(c)	94,846	67,839
Interest-bearing borrowings	24	1,673	1,655
Trade and other payables	26	94,380	101,605
Provisions	27	17,097	23,730
Accrued charges and deferred revenue	28	137,904	147,300
Total current liabilities		345,900	342,129
Total liabilities		354,137	352,220
TOTAL EQUITY AND LIABILITIES		1,425,161	1,552,443

Ericsson Nikola Tesla d.d.

STATEMENT OF CASH FLOWS

for the year ended 31 December 2010

		2010	2009
	Notes	HRK '000	HRK '000
Cash flows from operating activities			
Profit before tax		25,967	126,817
Adjustments for:			
Depreciation and amortisation	12,13	56,831	64,787
Impairment losses and reversals		139,850	21,901
Net creation of provisions	27	13,853	16,176
Net loss/(gain) on sale of property, plant and equipment	6,7	181	(65)
Net gain on remeasurement of financial assets	9	(4,026)	(429)
Amortisation of discount	9	(6,254)	(15,985)
Interest income	9	(23,506)	(39,538)
Interest expense	9	192	757
Foreign exchange gains		(6,196)	(5,942)
Equity-settled transactions		6,124	11,129
		203,016	179,608
Decrease in loans and receivables		140,948	78,336
(Increase)/decrease in inventories		(21,022)	28,800
Decrease in receivables		48,256	20,976
Decrease in payables		(11,048)	(10,653)
Cash generated from operations		360,150	297,067
Interest paid		(192)	(757)
Income taxes refunded/(paid)		6,398	(12,262)
Net cash from operating activities		366,356	284,048
Cash flows from investing activities			
Interest received		25,369	37,922
Proceeds from sale of property, plant and equipment		43	151
Purchases of property, plant and equipment, and intangible assets	12,13	(39,736)	(46,095)
(Decrease)/increase in non-current deposits		(198)	522
Proceeds from disposal / (purchase) of financial assets		61,645	(77,473)
Net cash generated from/(used in) investing activities		47,123	(84,973)



Ericsson Nikola Tesla d.d.

STATEMENT OF CASH FLOWS (CONTINUED)

for the year ended 31 December 2010

		2010	2009
	Notes	HRK '000	HRK '000
Cash flows from financing activities			
Repayment of interest-bearing borrowings		(1,601)	(2,213)
Purchase of treasury shares	21(b)	-	(11,380)
Dividends paid	22	(158,160)	(91,758)
Net cash used in financing activities		(159,761)	(105,351)
Effects of exchange rate changes on cash and cash equivalents		5,273	2,908
Net increase in cash and cash equivalents		258,991	96,632
Cash and cash equivalents at the beginning of the year	20	414,935	318,303
Cash and cash equivalents at the end of the year	20	673,926	414,935

Ericsson Nikola Tesla d.d.

STATEMENT OF CHANGES IN EQUITY

for the year ended 31 December 2010

	Share capital	Treasury shares	Legal reserves	Retained earnings	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
As at 1 January 2009	133,165	(46,389)	20,110	1,059,241	1,166,127
Changes in equity for 2009					
Total comprehensive income	-	-	-	128,447	128,447
Dividend distribution for 2008, Note 22	-	-	-	(91,758)	(91,758)
Purchase of treasury shares Note 21 (b)	-	(11,380)	-	-	(11,380)
Share-based payments, Note 25 (b)	-	23,596	-	(23,596)	-
Equity-settled transactions, Note 25 (b)	-	-	-	11,129	11,129
Deferred tax related to equity increase, Note 10	-	-	-	(2,342)	(2,342)
As at 31 December 2009	133,165	(34,173)	20,110	1,081,121	1,200,223
As at 1 January 2010	133,165	(34,173)	20,110	1,081,121	1,200,223
Changes in equity for 2010					
Total comprehensive income	-	-	-	24,062	24,062
Dividend distribution for 2009, Note 22	-	-	-	(158,160)	(158,160)
Share-based payments, Note 25 (b)	-	17,922	-	(17,922)	-
Equity-settled transactions, Note 25 (b)	-	-	-	6,124	6,124
Deferred tax related to equity increase, Note 10	-	-	-	(1,225)	(1,225)
As at 31 December 2010	133,165	(16,251)	20,110	934,000	1,071,024



NOTES TO THE FINANCIAL STATEMENTS

1 SIGNIFICANT ACCOUNTING POLICIES

REPORTING ENTITY

Ericsson Nikola Tesla d.d. (the Company) is a joint stock company incorporated and domiciled in Croatia. The address of its registered office is Krapinska 45, 10000 Zagreb, the Republic of Croatia. The Company's shares are listed on the Public Joint Stock Company listing on the Zagreb Stock Exchange. These financial statements were authorised for issue by the Management Board on 8 March 2011 for approval by the Supervisory Board. A summary of the Company's principal accounting policies is set out below.

STATEMENT OF COMPLIANCE

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

BASIS OF PREPARATION

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

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

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

GOING CONCERN

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES

(a) New and amended standards adopted by the Company

The Company has adopted the following new and amended IFRSs as of 1 January 2010:

IFRS 3 (revised), 'Business combinations', and consequential amendments to IAS 27, 'Consolidated and separate financial statements', IAS 28, 'Investments in associates', and IAS 31, 'Interests in joint ventures', are effective prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning on or after 1 July 2009.

The revised standard continues to apply the acquisition method to business combinations but with some significant changes compared with IFRS 3. For example, all payments to purchase a business are recorded at fair value at the acquisition date, with contingent payments classified as debt subsequently remeasured through the statement of comprehensive income. There is a choice on an acquisition-by-acquisition basis to measure the non-controlling interest in the acquiree either at fair value or at the non-controlling interest's proportionate share of the acquiree's net assets. All acquisition-related costs are expensed. The amendment will not have an impact on the Company's financial statements.

IAS 27 (revised) requires the effects of all transactions with non-controlling interests to be recorded in equity if there is no change in control and these transactions will no longer result in goodwill or gains and losses. The standard also specifies the accounting when control is lost. Any remaining interest in the entity is re-measured to fair value, and a gain or loss is recognised in profit or loss. IAS 27 (revised) has had no impact on the current period, as none of the non-controlling interests have a deficit balance; there have been no transactions whereby an interest in an entity is retained after the loss of control of that entity, and there have been no transactions with non-controlling interests. The revised Standard will not have an impact on the Company's financial statements.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(b) New and amended standards, and interpretations mandatory for the first time for the financial year beginning 1 January 2010 but not currently relevant to the Company (although they may affect the accounting for future transactions and events)

The following standards and amendments to existing standards have been published and are mandatory for the Company's accounting periods beginning on or after 1 January 2010 or later periods, but the Company has not early adopted them.

IFRIC 17, 'Distribution of non-cash assets to owners' (effective on or after 1 July 2009). The interpretation was published in November 2008. This interpretation provides guidance on accounting for arrangements whereby an entity distributes non-cash assets to shareholders either as a distribution of reserves or as dividends. IFRS 5 has also been amended to require that assets are classified as held for distribution only when they are available for distribution in their present condition and the distribution is highly probable.

IFRIC 18, 'Transfers of assets from customers', effective for transfer of assets received on or after 1 July 2009. This interpretation clarifies the requirements of IFRSs for agreements in which an entity receives from a customer an item of property, plant and equipment that the entity must then use either to connect the customer to a network or to provide the customer with ongoing access to a supply of goods or services (such as a supply of electricity, gas or water). In some cases, the entity receives cash from a customer that must be used only to acquire or construct the item of property, plant, and equipment in order to connect the customer to a network or provide the customer with ongoing access to a supply of goods or services (or to do both).

IFRIC 9, 'Reassessment of embedded derivatives and IAS 39, Financial instruments: Recognition and measurement', effective 1 July 2009. This amendment to IFRIC 9 requires an entity to assess whether an embedded derivative should be separated from a host contract when the entity reclassifies a hybrid financial asset out of the 'fair value through profit or loss' category. This assessment is to be made based on circumstances that existed on the later of the date the entity first became a party to the contract and the date of any contract amendments that significantly change the cash flows of the contract. If the entity is unable to make this assessment, the hybrid instrument must remain classified as at fair value through profit or loss in its entirety.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(b) New and amended standards, and interpretations mandatory for the first time for the financial year beginning 1 January 2010 but not currently relevant to the Company (although they may affect the accounting for future transactions and events) (continued)

IFRIC 16, 'Hedges of a net investment in a foreign operation' effective 1 July 2009. This amendment states that, in a hedge of a net investment in a foreign operation, qualifying hedging instruments may be held by any entity or entities within the Group, including the foreign operation itself, as long as the designation, documentation and effectiveness requirements of IAS 39 that relate to a net investment hedge are satisfied. In particular, the Company should clearly document its hedging strategy because of the possibility of different designations at different levels of the Company.

IAS 38 (amendment), 'Intangible assets', effective 1 January 2010. The amendment clarifies guidance in measuring the fair value of an intangible asset acquired in a business combination and permits the grouping of intangible assets as a single asset if each asset has similar useful economic lives.

IAS 1 (amendment), 'Presentation of financial statements'. The amendment clarifies that the potential settlement of a liability by the issue of equity is not relevant to its classification as current or non-current. By amending the definition of current liability, the amendment permits a liability to be classified as non-current (provided that the entity has an unconditional right to defer settlement by transfer of cash or other assets for at least 12 months after the accounting period) notwithstanding the fact that the entity could be required by the counterparty to settle in shares at any time.

IAS 36 (amendment), 'Impairment of assets', effective 1 January 2010. The amendment clarifies that the largest cash-generating unit (or group of units) to which goodwill should be allocated for the purposes of impairment testing is an operating segment, as defined by paragraph 5 of IFRS 8, 'Operating segments' (that is, before the aggregation of segments with similar economic characteristics).

IFRS 2 (amendments), 'Group cash-settled share-based payment transactions', effective from 1 January 2010. In addition to incorporating IFRIC 8, 'Scope of IFRS 2', and IFRIC 11, 'IFRS 2 – Group and treasury share transactions', the amendments expand on the guidance in IFRIC 11 to address the classification of Group arrangements that were not covered by that interpretation.

IFRS 5 (amendment), 'Non-current assets held for sale and discontinued operations'. The amendment clarifies that IFRS 5 specifies the disclosures required in respect of non-current assets (or disposal groups) classified as held for sale or discontinued operations. It also clarifies that the general requirement of IAS 1 still applies, in particular paragraph 15 (to achieve a fair presentation) and paragraph 125 (sources of estimation uncertainty) of IAS 1.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(c) New standards, amendments and interpretations issued but not effective for the financial year beginning 1 January 2010 and not early adopted

The Company's assessment of the impact of these new standards and interpretations is set out below.

IFRS 9, 'Financial instruments', issued in November 2009. This standard is the first step in the process to replace IAS 39, 'Financial instruments: recognition and measurement'. IFRS 9 introduces new requirements for classifying and measuring financial assets and is likely to affect the Company's accounting for its financial assets. The standard is not applicable until 1 January 2013 but is available for early adoption. However, the standard has not yet been endorsed by the EU. The Company is yet to assess IFRS 9's full impact.

IAS 24 (revised), 'Related party disclosures', issued in November 2009. It supersedes IAS 24, 'Related party disclosures', issued in 2003. IAS 24 (revised) is mandatory for periods beginning on or after 1 January 2011. Earlier application, in whole or in part, is permitted. However, the standard has not yet been endorsed by the EU.

The revised standard clarifies and simplifies the definition of a related party and removes the requirement for government-related entities to disclose details of all transactions with the government and other government-related entities. The Company will apply the revised standard from 1 January 2011. When the revised standard is applied, the Company will need to disclose any transactions between its subsidiaries and its associates. Since the Company has no material subsidiaries or associates, the revised standard is not expected to have any impact on the financial statements.

'Classification of rights issues' (amendment to IAS 32), issued in October 2009. The amendment applies to annual periods beginning on or after 1 February 2010. Earlier application is permitted. The amendment addresses the accounting for rights issues that are denominated in a currency other than the functional currency of the issuer. Provided certain conditions are met, such rights issues are now classified as equity regardless of the currency in which the exercise price is denominated. Previously, these issues had to be accounted for as derivative liabilities. The amendment applies retrospectively in accordance with IAS 8 'Accounting policies, changes in accounting estimates and errors'. The Company will apply the amended standard from 1 January 2011. The amendment will not have an impact on the Company's financial statements.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CHANGES IN ACCOUNTING POLICIES AND DISCLOSURES (CONTINUED)

(c) New standards, amendments and interpretations issued but not effective for the financial year beginning 1 January 2010 and not early adopted (continued)

IFRIC 19, 'Extinguishing financial liabilities with equity instruments', effective 1 July 2010. The interpretation clarifies the accounting by an entity when the terms of a financial liability are renegotiated and result in the entity issuing equity instruments to a creditor of the entity to extinguish all or part of the financial liability (debt for equity swap). It requires a gain or loss to be recognised in profit or loss, which is measured as the difference between the carrying amount of the financial liability and the fair value of the equity instruments issued. If the fair value of the equity instruments issued cannot be reliably measured, the equity instruments should be measured to reflect the fair value of the financial liability extinguished. The Company will apply the interpretation from 1 January 2011, subject to endorsement by the EU. It is not expected to have any impact on the Company's financial statements.

'Prepayments of a minimum funding requirement' (amendments to IFRIC 14). The amendments correct an unintended consequence of IFRIC 14, 'IAS 19 – The limit on a defined benefit asset, minimum funding requirements and their interaction'. Without the amendments, entities are not permitted to recognise as an asset some voluntary prepayments for minimum funding contributions. This was not intended when IFRIC 14 was issued, and the amendments correct this. The amendments are effective for annual periods beginning 1 January 2011. Earlier application is permitted. The amendments should be applied retrospectively to the earliest comparative period presented. The Company will apply these amendments for the financial reporting period commencing on 1 January 2011.

FUNCTIONAL AND PRESENTATIONAL CURRENCY

The Company's financial statements have been prepared in Croatian kuna (HRK), which is the currency of the primary economic environment in which the entity operates (the functional currency) and the presentation currency, and are rounded to the nearest thousand. The closing exchange rate as at 31 December 2010 was HRK 5.56825 per USD 1 (2009: HRK 5.08930) and HRK 7.38517 per EUR 1 (2009: HRK 7.30620).



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

PROPERTY, PLANT AND EQUIPMENT

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

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

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

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

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

INTANGIBLE ASSETS

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

IMPAIRMENT OF ASSETS

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

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

The recoverable amount of held-to-maturity investments and receivables carried at amortised cost is calculated as the present value of expected future cash flows, discounted at the original effective interest rate inherent in the asset.

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

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

FINANCIAL INSTRUMENTS

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



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FINANCIAL INSTRUMENTS (CONTINUED)

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

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

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

Financial assets are initially measured at the fair value of the consideration given for them, including transaction costs for all financial assets not carried at fair value through profit or loss. Financial assets and financial liabilities at fair value through profit or loss are initially recognised at fair value and transaction costs are expensed in the statement of comprehensive income. All financial assets and financial liabilities at fair value through profit or loss and available-for-sale financial assets are subsequently carried at fair value without any deduction for transaction costs that the Company may incur on sale or other disposal. Available-for-sale financial assets for which fair value cannot be reliably measured are stated at cost, including transaction costs, less impairment losses. Held-to-maturity investments and loans and receivables are carried at amortised cost less impairment losses. Amortised cost is calculated using the effective interest rate method. Premiums and discounts on held-to-maturity investments and available-for-sale financial assets, including initial transaction costs, are included in the carrying amount of the related instrument and amortised based on the effective interest rate of the instrument. Other financial liabilities are initially recognised at fair value and subsequently carried at amortised cost.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FINANCIAL INSTRUMENTS (CONTINUED)

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

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

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

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

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



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

TRADE AND OTHER RECEIVABLES

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

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

CASH AND CASH EQUIVALENTS

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

TRADE AND OTHER PAYABLES

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

INVENTORIES

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

SHARE CAPITAL AND RESERVES

Share capital is stated in HRK at nominal value. The amount of consideration paid on repurchase of share capital, including directly attributable costs, is recognised as a charge in equity. Repurchased shares are classified as treasury shares and presented as a deduction from total equity.

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

SHARE CAPITAL AND RESERVES (CONTINUED)

The result for the year is transferred to retained earnings. Dividends are recognised as a liability in the period in which they are declared. Dividends are paid out of the retained earnings.

INCOME TAX

The income tax charge is based on taxable profit for the year and comprises current and deferred tax. Income tax is recognised in the statement of comprehensive income except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity. Current tax is the expected tax payable on the taxable income for the year, using the tax rates enacted or substantially enacted at the balance sheet date, and any adjustments to tax payable in respect of previous years.

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

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

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



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

FOREIGN CURRENCIES

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

RECOGNITION OF REVENUES

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

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

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

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

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

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

RECOGNITION OF REVENUES (CONTINUED)

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

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

EMPLOYEE BENEFITS

(a) Long-term service benefits

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

(b) Share-based payments

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



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

PROVISIONS

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

NET FINANCIAL INCOME

Net financial income comprises interest receivable on non-current loans, interest receivable on funds invested, foreign exchange gains and losses and gains and losses on financial assets at fair value through profit and loss and any cost related to borrowings. Interest income is recognised in the statement of comprehensive income as it accrues, using the effective interest method.

SEGMENT REPORTING

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

BORROWINGS

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

1 SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

LEASES

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

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

DIVIDEND DISTRIBUTION

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



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

2 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Accounting estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The 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) Impairment losses on loans and receivables

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

(b) Financial crisis impact

The ongoing global liquidity crisis which commenced in the middle of 2007 has resulted in, among other things, a lower level of capital market funding, lower liquidity levels across the banking sector, and, at times, higher interbank lending rates and very high volatility in stock markets. The uncertainties in the global financial markets have also led to bank failures and bank rescues in the United States of America, Western Europe, Russia and elsewhere. Indeed the full extent of the impact of the ongoing financial crisis is proving to be impossible to anticipate or completely guard against.

The customers of the Company may also be affected by the lower liquidity situation which could in turn impact their ability to repay their outstanding debts. Deteriorating operating conditions for borrowers may also have an impact on management's cash flow forecasts and assessment of the impairment of financial and non-financial assets. To the extent that information is available, management has reflected revised estimates of expected future cash flows in their impairment assessments.

Management is unable to reliably estimate the effects on the Company's financial position of any further deterioration in the liquidity of the financial markets and the increased volatility in the currency and equity markets. Management believes it is taking all the necessary measures to support the sustainability and growth of the Company's business in the current circumstances.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

2 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (CONTINUED)

JUDGEMENTS

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

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

3 SALES REVENUE

	2010	2009
	HRK '000	HRK '000
Sales revenue from products	472,537	619,138
Sales revenue from services	746,326	780,873
	1,218,863	1,400,011



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

4 SEGMENT REPORTING

The Company has determined the operating segments based on the reports reviewed by the Management Board that are used to make strategic decisions. The Management Board assesses the performance of the operating segments based on a measure of adjusted Operating profit. The measurement basis excludes the effects of gains/losses on disposal of intangibles, property, plant and equipment and administration expenses.

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

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

- » Networks include products for mobile and fixed broadband access, core networks, transmission and next-generation IP networks. Related network rollout services are also included. In addition, power modules and cables operations are included within Networks.
- » Professional services include all service operations, excluding Network rollout reported under Networks. Services related to system integration of IP and core networks are classified as Professional services.
- » Multimedia includes multimedia systems, enterprise solutions and mobile platforms.

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

	2010	2009
	HRK '000	HRK '000
Sales revenue in domestic market	339,696	481,693
Sales revenue in Russia, Belarus, Kazakhstan, Georgia, Kyrgyzstan, Moldova	222,792	215,237
Sales revenue to Ericsson	444,838	423,155
Sales revenue in Bosnia and Herzegovina, Montenegro, Macedonia and Kosovo	201,662	265,048
Other export sales revenue	9,875	14,878
	1,218,863	1,400,011

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

4 SEGMENT REPORTING (CONTINUED)

	Networks		Professional services		Multimedia		Total	
	2010	2009	2010	2009	2010	2009	2010	2009
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Segment sales revenue	779,021	922,523	393,801	416,321	46,041	61,167	1,218,863	1,400,011
Segment other income	9,850	11,373	4,979	5,133	582	754	15,411	17,260
Segment results from operating activities	58,518	48,476	(31,970)	64,316	(7,579)	(10,153)	18,969	102,639
Segment results from operating activities excluding Kazakhstan write-off ¹⁾	68,463	48,476	84,800	64,316	(7,802)	(10,153)		
Unallocated (loss)/gain on sale of property, plant and equipment							(181)	65
Unallocated expenses ²⁾							(34,037)	(37,024)
Operating profit							(15,249)	65,680
Segment finance income	8,206	18,998	4,481	5,832	3,019	9,101	15,706	33,931
Segment results	66,724	67,474	(27,489)	70,148	(4,560)	(1,052)	34,675	136,570
Segment results excluding Kazakhstan write-off ¹⁾	76,669	67,474	89,281	70,148	(4,783)	(1,052)		
Unallocated finance income							25,702	27,963
Finance expense							(192)	(757)
Profit before tax							25,967	126,817
Income tax expense							(1,905)	1,630
Profit for the year							24,062	128,447
Other segment information:								
Segment liabilities	143,298	125,320	72,438	56,555	8,469	8,309	224,205	190,184
Additions to property, plant and equipment	23,350	29,250	11,803	13,200	1,380	1,940	36,533	44,390
Acquisitions of intangible assets	2,047	1,123	1,035	507	121	75	3,203	1,705
Depreciation and amortisation	29,789	8,028	15,059	3,623	1,760	532		

¹⁾ Information relating to Kazakhstan write-off is disclosed in Note 17

²⁾ Including audit fee expenses of HRK 420 thousand (2009: HRK 415 thousand)



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

4 SEGMENT REPORTING (CONTINUED)

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

	2010	2009
	HRK '000	HRK '000
Segment liabilities	224,205	190,184
Unallocated:		
Interest-bearing borrowings	5,019	6,620
Accrued charges and deferred revenue	111,610	147,300
Trade and other payables	8,412	2,990
Employee benefits	4,891	5,126
Total liabilities per the statement of financial position	354,137	352,220

5 EXPENSES BY NATURE

	2010	2009
	HRK '000	HRK '000
Changes in inventories of finished goods and work in progress (Note 16)	(21,817)	27,159
Goods and services	636,144	789,990
Personnel expenses (Note 8)	432,419	441,927
Depreciation and amortisation (Notes 12,13)	56,831	64,787
Total cost of sales, distribution and administrative expenses	1,103,577	1,323,863

6 OTHER INCOME

	2010	2009
	HRK '000	HRK '000
Commission income	251	777
Rental income	14,631	16,159
Net gain on disposal of property, plant and equipment	-	65
Other income	529	324
	15,411	17,325

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

7 OTHER EXPENSES

	2010	2009
	HRK '000	HRK '000
Net loss on disposal of property, plant and equipment	181	-
Increase in provisions (Note 27)	5,916	5,892
Impairment loss on loans and receivables (Note 17)	139,543	21,650
Obsolescence allowance on inventories	306	251
	145,946	27,793

8 PERSONNEL EXPENSES

	2010	2009
	HRK '000	HRK '000
Net salaries	210,573	209,381
Taxes and contributions	191,286	195,307
Other payroll-related costs	24,436	25,527
Equity-settled transactions (Note 25 (b))	6,124	11,712
	432,419	441,927

Personnel expenses include HRK 68,415 thousand (2009: HRK 70,326 thousand) of defined pension contributions paid or payable into obligatory pension plans. Contributions are calculated as a percentage of employees' gross salaries (Gross II).

In addition, Personnel expenses include HRK 13,868 thousand (2009: HRK 10,284 thousand) in respect of voluntary redundancy costs. Movements in provision related to these costs are described in Note 27, Provisions.

As at 31 December 2010, total number of employees was 1,595 (2009: 1,652).



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

9 FINANCE INCOME AND EXPENSE

Finance income	2010	2009
	HRK '000	HRK '000
Interest income (Note 9 (a))	23,506	39,538
Net gains from remeasurement of financial assets at fair value through profit or loss (Note 9 (c))	4,026	429
Amortization of discount (Note 9 (b))	6,254	15,985
Net foreign exchange gain	7,622	5,942
	41,408	61,894

Finance expense	2010	2009
	HRK '000	HRK '000
Interest expense	192	757
	192	757

9 (a)	2010	2009
	HRK '000	HRK '000
Interest income		
- on loans to customers	8,623	17,316
- on debt securities	998	2,720
- on term deposits	12,584	18,079
- on other receivables	1,301	1,423
	23,506	39,538

9 (b)

The Company released HRK 6,254 thousand (2009: HRK 15,985 thousand) into finance income due to amortisation of discount according to the net present value method of impairment.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

9 FINANCE INCOME AND EXPENSE (CONTINUED)

9 (c)	2010	2009
	HRK '000	HRK '000
Net gains/(losses) from remeasurement of financial assets at fair value through profit or loss		
- Derivative financial instruments	-	1,588
- Equity securities	1,388	(385)
- Investment in investment funds	2,671	86
- Debt securities	(33)	(860)
	4,026	429

10 INCOME TAX EXPENSE

Income tax has been calculated on the taxable income at statutory tax rate of 20% (2009: 20%).

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

	2010	2009
	HRK '000	HRK '000
Current income tax expense	-	-
Total deferred tax (expense)/income relating to the origination and reversal of temporary differences (Note 15)	(1,905)	1,630
Total income tax (charge)/credit in the statement of comprehensive income	(1,905)	1,630

Deferred tax recognised directly to equity:

	2010	2009
	HRK '000	HRK '000
Relating to equity-settled transactions (Note 15)	(1,225)	(2,342)



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

10 INCOME TAX EXPENSE (CONTINUED)

The reconciliation between tax expense and accounting profit is shown as follows:

	2010	2009
	HRK '000	HRK '000
Profit before tax	25,967	126,817
Income tax at 20% (2009: 20%)	5,193	25,363
The effects of:		
Non-deductible expenses	1,786	3,338
Tax exempt (revenues)/expenses	(3,338)	300
Tax incentives	(3,641)	(29,001)
Current tax expense	-	-
Effective tax rate	0.0%	0.0%

Tax incentives include only part of additional tax allowances for certain expenditure totalling HRK 3,641 thousand (2009: HRK 29,001 thousand) which meets research and development incentives definitions under Croatian tax legislation. The underlying research and development expenditure is included in cost of sales.

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

11 EARNINGS PER SHARE

	2010	2009
Profit for the year (HRK '000)	24,062	128,447
Weighted Average Number of Shares Outstanding at the year-end	1,314,812	1,309,435
Earnings per share (HRK)	18.30	98.09

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

12 PROPERTY, PLANT AND EQUIPMENT

	Land and buildings	Plant and equipment	Other	Total
	HRK '000	HRK '000	HRK '000	HRK '000
As at 1 January 2009				
Cost or valuation	155,455	397,620	328	553,403
Accumulated depreciation	(92,476)	(297,457)	(181)	(390,114)
Net book amount	62,979	100,163	147	163,289
Year ended 31 December 2009				
Opening net book amount	62,979	100,163	147	163,289
Additions	-	44,390	-	44,390
Disposals	-	(86)	-	(86)
Depreciation charge	(3,589)	(57,645)	(8)	(61,242)
Closing net book amount	59,390	86,822	139	146,351
As at 31 December 2009				
Cost or valuation	155,455	312,094	328	467,877
Accumulated depreciation	(96,065)	(225,272)	(189)	(321,526)
Net book amount	59,390	86,822	139	146,351
Year ended 31 December 2010				
Opening net book amount	59,390	86,822	139	146,351
Additions	-	36,533	-	36,533
Disposals	-	(224)	-	(224)
Depreciation charge	(3,542)	(50,467)	(8)	(54,017)
Closing net book amount	55,848	72,664	131	128,643
As at 31 December 2010				
Cost or valuation	155,455	293,754	328	449,537
Accumulated depreciation	(99,607)	(221,090)	(197)	(320,894)
Net book amount	55,848	72,664	131	128,643

Included in cost is HRK 206,698 thousand (2009: HRK 198,172 thousand) of fully depreciated property, plant and equipment that is still used by the Company.

As at 31 December 2010, the Company had contracts totalling HRK 6,025 thousand (2009: HRK 1,552 thousand) related to future equipment purchases.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

12 PROPERTY, PLANT AND EQUIPMENT (CONTINUED)

The Company acts as a lessor under operating leases, mainly land and buildings. Property leased to others with a carrying value of HRK 22,552 thousand (2009: HRK 23,901 thousand) is included within land and buildings. These assets are depreciated at the same depreciation rates as other buildings. HRK 16,529 thousand (2009: 18,655 thousand) of leased assets is leased for a non-cancellable period of five years which commenced in 2005. Subsequent renewals are negotiated with the lessee. No contingent rents are charged. Portions of the property which is held for rental could not be sold separately or leased out separately under finance lease. Consequently, the IAS 40 criteria for separate investment property recognition are not met.

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

	2010	2009
	HRK '000	HRK '000
Less than one year	4,058	6,064
Between one and five years	-	-
	4,058	6,064

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

13 INTANGIBLE ASSETS

The movement on intangible assets in the year ended 31 December 2010 may be analysed as follows:

	Application software
	HRK '000
As at 1 January 2009	
Cost or valuation	16,620
Accumulated amortization	(10,355)
Net book amount	6,265
Year ended 31 December 2009	
Opening net book amount	6,265
Additions	1,705
Amortization charge	(3,545)
Closing net book amount	4,425
As at 31 December 2009	
Cost or valuation	16,264
Accumulated amortization	(11,839)
Net book amount	4,425
Year ended 31 December 2010	
Opening net book amount	4,425
Additions	3,203
Amortization charge	(2,814)
Closing net book amount	4,814
As at 31 December 2010	
Cost or valuation	19,467
Accumulated amortization	(14,653)
Net book amount	4,814

Included in the cost amount is HRK 9,641 thousand (2009: HRK 6,365 thousand) of fully amortised intangible assets that are still used by the Company.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

14 LOANS AND RECEIVABLES

	2010	2009
	HRK '000	HRK '000
Deposits with financial institutions, denominated in foreign currency	7,076	6,878
Non-current receivables from foreign customers, denominated in foreign currency	15,600	260,469
Non-current receivables from domestic customers, denominated in HRK	-	12,445
Receivables for sold apartments		
- denominated in foreign currency	5,430	5,498
- denominated in HRK	1,193	1,415
Housing loans to employees, denominated in HRK	-	7
Total loans and receivables	29,299	286,712
Impairment allowance on loans and receivables (Note 17)	(18,941)	(7,815)
	10,358	278,897

Deposits with financial institutions are placed as guarantee deposits for housing loans provided to the Company's employees, earning interest at variable rates ranging from 1.07% to 1.10% per annum (2009: 1.07% to 1.10% per annum), and with a remaining maturity of over three years.

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

Non-current portion of foreign and domestic loans and receivables

	2010	2009
	HRK '000	HRK '000
Due		
2011	-	74,978
2012	11,582	42,247
2013	4,018	36,656
2014	-	34,009
2015 - 2020	-	85,024
	15,600	272,914

Receivables for sold apartments are shown net of amounts due to the Croatian state. Housing loans to employees are linked to the counter value of euro, repayments are made by deduction from monthly salary and the loans are secured with charges on the house or apartment. Receivables for sold apartments and housing loans provided to a limited number of employees bear fixed interest rates of up to 5% per annum. A discount in the amount of HRK 2,334 thousand (2009: HRK 3,120 thousand) is recognised in respect of these loans and amortised through the statement of comprehensive income, using the effective interest rate method at a rate of 7% per annum.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

15 DEFERRED TAX ASSETS

Recognised deferred tax assets and liabilities

Movements in temporary differences and components of deferred tax assets and liabilities are as follows:

	Assets	Liabilities	Credited/ (charged) to statement of compre- hensive income	Credited/ (charged) to equity	Assets	Liabilities
	2010			2009		
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Receivables	6,143	-	148	-	5,995	-
Inventories	2,262	-	11	-	2,251	-
Employee benefits	825	-	6	-	819	-
Non-current receivables for sold apartments	467	-	(157)	-	624	-
Negative fair value of financial instruments	447	-	-	-	447	-
Accrued charges	(979)	-	(3,138)	-	2,159	-
Increase in equity related to equity-settled transactions	11,344	(11,344)	1,225	(1,225)	10,119	(10,119)
	20,509	(11,344)	(1,905)	(1,225)	22,414	(10,119)
Set-off of tax	(11,344)	11,344	-	-	(10,119)	10,119
Deferred tax assets	9,165	-	(1,905)	(1,225)	12,295	-

Deferred income tax assets are recognised for tax loss carry-forwards to the extent that the realisation of the related tax benefit through future taxable profits is probable. The Company did not recognise deferred income tax assets of HRK 28,832 thousand (2009: HRK 16,255 thousand) in respect of tax losses amounting to HRK 144,161 thousand (2009: HRK 81,277 thousand) that can be carried forward against future taxable income. A tax loss may be carried forward for five years subsequent to the year in which it was incurred. The availability of tax losses against future periods, subject to review by the Ministry of Finance, is as follows:

	HRK '000
Tax loss from 2009 – expires 31 December 2014	81,277
Tax loss from 2010 – expires 31 December 2015	144,161
	225,438



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

15 DEFERRED TAX ASSETS (CONTINUED)

Recognised deferred tax assets and liabilities (continued)

Movements in temporary differences and components of deferred tax assets and liabilities are as follows:

	Assets	Liabilities	Credited/ (charged) to statement of compre- hensive income	Credited/ (charged) to equity	Assets	Liabilities
	2009				2008	
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Receivables	5,995	-	(1,483)	-	7,478	-
Inventories	2,251	-	(25)	-	2,276	-
Employee benefits	819	-	34	-	785	-
Non-current receivables for sold apartments	624	-	(75)	-	699	-
Negative fair value of financial instruments	447	-	(1,154)	-	1,601	-
Accrued charges	2,159	-	1,991	-	168	-
Increase in equity related to equity-settled transactions	10,119	(10,119)	2,342	(2,342)	7,777	(7,777)
	22,414	(10,119)	1,630	(2,342)	20,784	(7,777)
Set-off of tax	(10,119)	10,119	-	-	(7,777)	7,777
Deferred tax assets	12,295	-	1,630	(2,342)	13,007	-

16 INVENTORIES

	2010	2009
	HRK '000	HRK '000
Raw materials	6,569	7,363
Work-in-progress and semi-finished goods	39,474	17,657
Total inventories	46,043	25,020
Obsolescence allowance	(1,269)	(961)
	44,774	24,059

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

17 TRADE RECEIVABLES

	2010	2009
	HRK '000	HRK '000
Foreign trade receivables	169,064	193,517
Current portion of non-current foreign receivables	58,104	152,938
Total current foreign receivables	227,168	346,455
Domestic trade receivables	116,397	110,974
Current portion of non-current domestic receivables	18,102	19,273
Total current domestic receivables	134,499	130,247
Impairment allowance on receivables	(14,685)	(25,455)
	346,982	451,247

Included in trade receivables is HRK 31,534 thousand (2009: HRK 15,725 thousand) of contract work in progress.

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

	2010	2009
	HRK '000	HRK '000
As at 1 January (Notes 14,17)	33,270	41,478
Provision for receivables impaired during the year (Note 7)	147,276	22,612
Receivables written off during the year as uncollectible	(132,933)	(13,873)
Unused amounts reversed (Note 7)	(7,733)	(962)
Amortisation of discount (Note 9)	(6,254)	(15,985)
As at 31 December (Notes 14,17)	33,626	33,270

During 2010, following the restructuring of JSC BTA Bank, Kazakhstan ("BTA Bank"), the Company has written off HRK 126,492 thousand in respect of balances outstanding relating to a Customer Financing transaction concluded in 2005. The transaction was fully secured by trade finance instruments from BTA Bank. The remaining portion of the receivables is assessed as recoverable.

Of the total HRK 33,626 thousand of impairment allowances as at 31 December 2010, HRK 31,292 thousand relates to Customer loans and receivables.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

18 OTHER RECEIVABLES

	2010	2009
	HRK '000	HRK '000
Net receivables for prepaid VAT	19,890	9,456
Receivables for withholding tax	27,031	11,267
Receivables from employees	925	1,039
Accrued interest receivable	1,501	3,364
Other receivables	8,885	4,462
	58,232	29,588

19 FINANCIAL ASSETS AT FAIR VALUE THROUGH PROFIT OR LOSS

	2010	2009
	HRK '000	HRK '000
Debt securities, Ministry of Finance	13,706	43,284
Equity securities	670	603
Investment in open-ended investment funds	48,878	76,986
	63,254	120,873

20 CASH AND CASH EQUIVALENTS

	2010	2009
	HRK '000	HRK '000
Cash and demand deposits	129,622	44,851
Term deposits originated by the Company, with original maturity up to 3 months	544,304	370,084
	673,926	414,935

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

21 EQUITY

(a) Share capital

As at 31 December 2010, the share capital of the Company is represented by 1,331,650 (2009: 1,331,650) of authorised, issued and fully paid ordinary shares, with a total registered value of HRK 133,165 thousand (2009: HRK 133,165 thousand). The nominal value of one share is HRK 100 (2009: HRK 100). The holders of the ordinary shares are entitled to receive dividends as declared at the General Assembly and are entitled to one vote per share at the General Assembly.

The Company's shareholders as at 31 December 2010 are:

	Number of shares	% held	Number of shares	% held
		2010		2009
Telefonaktiebolaget LM Ericsson	653,473	49.07	653,473	49.07
Small shareholders	665,793	50.00	651,830	48.95
Croatian Privatisation Fund	3,096	0.23	11,879	0.89
Treasury shares	9,288	0.70	14,468	1.09
	1,331,650	100.00	1,331,650	100.00

(b) Treasury shares

During 2007, the Company acquired 15,000 of its own shares. The amount paid was HRK 52,456 thousand out of 2006 net income as decided by the General Assembly held on 31 May 2007. During 2008, the Company acquired an additional 3,000 of its own shares. The amount paid was HRK 3,895 thousand out of 2006 net income, as decided by the General Assembly held on 31 May 2007. During 2009, the Company acquired additional 8,893 of its own shares. The amount paid was HRK 11,380 thousand out of 2008 net income as decided by the General Assembly held on 27 May 2008. These shares are held as "treasury shares" and will be granted to key management and other employees as a part of the share-based program established during 2004, as described in Note 25 (b).

Movements in treasury shares are as follows:

	Number of shares	Number of shares
	2010	2009
As at 1 January (Note 21 (a))	14,468	13,588
Purchases during the year	-	8,893
Distributed during the year	(5,180)	(8,013)
As at 31 December (Note 21 (a))	9,288	14,468

(c) Legal reserves

A legal reserve in the amount of 5% of total share capital was formed during previous periods by appropriation of 5% of net profit per annum up to a cap of 5% of share capital. The legal reserve may be used to cover losses if the losses are not covered by current net profit or if other reserves are not available. The Company recorded the required level of legal reserves in the year 2000 and no further allocation to legal reserves is required.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

22 PROPOSED DIVIDENDS

Dividends payable are not accounted for until they have been ratified at the General Assembly of shareholders. On 20 May 2010, the General Assembly approved a regular dividend in respect of 2009 of HRK 20.00 per share, and additional extraordinary dividend of HRK 100.00 per share, totalling HRK 158.2 million. At a meeting held on 10 February 2011, the Management Board proposed a regular dividend in respect of 2010 in the amount of HRK 20 per share, and an additional extraordinary dividend of HRK 170 per share. The dividend will be paid from profit for 2010 and the remaining part of retained earnings realized in 2009 and 2006 plus a portion of retained earnings realized in 2001 after approval by the General Assembly, which will be held on 31 May 2011.

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

	2010	2009
	HRK '000	HRK '000
HRK 120.00 per share for 2009	158,160	-
HRK 70.00 per share for 2008	-	91,758

23 CAPITAL MANAGEMENT

The Company's objectives when managing capital are:

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

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

The Company monitors capital using the statutory minimum capital requirement. Shareholders' equity is disclosed in Note 21 to the financial statements.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

24 INTEREST-BEARING BORROWINGS

During 2008, the Company borrowed the amount of HRK 8,085 thousand from HBOR and delivered information and communications equipment to a customer. The Ministry of Health and Social Welfare ("the Ministry") took over the obligations towards the Company on behalf of the customer and, based on the cession agreement between the Company, the customer and the Ministry, the Ministry is obliged to perform the repayment of the due amounts in favour of the customer directly to HBOR. The Company's liability to HBOR decreases as the Ministry repays. The HBOR borrowing was granted over a 5-year period. The current portion of the borrowing amounts to HRK 1,673 thousand, while the remaining amount is repayable in semi-annual instalments until 2013, bearing an interest rate of six-month EURIBOR plus a margin of 2% per annum. There is no security or pledges in relation to these borrowings. There are no amounts bearing a fixed interest rate.

	2010	2009
	HRK '000	HRK '000
Non-current portion of borrowings	3,346	4,965
Current portion of borrowings	1,673	1,655
	5,019	6,620

25 EMPLOYEE BENEFITS

(a) Long-term service benefits

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

However, the Company pays a one-time benefit amounting to HRK 8,000 for each employee who retires. Additionally, the Company pays jubilee awards in respect of each 5 years of service, of an employee, starting from the 10th year and ending in the 40th year. The principal actuarial assumptions used to determine retirement and jubilee obligations as at 31 December 2010 were a 6% discount rate (2009: 6%) and a 2.91% (2009: 3.01%) rate of average employment turnover.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

25 EMPLOYEE BENEFITS (CONTINUED)

(a) Long-term service benefits (continued)

Movements in long-term service benefits were as follows:

	Jubilee awards	Retirement	Total	Jubilee awards	Retirement	Total
			2010			2009
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
As at 1 January	4,095	1,031	5,126	3,927	1,082	5,009
Obligation created during the year	706	514	1,220	657	336	993
Obligation fulfilled during the year	(615)	(88)	(703)	(406)	(48)	(454)
Obligation reversed during the year	(63)	(689)	(752)	(83)	(339)	(422)
As at 31 December	4,123	768	4,891	4,095	1,031	5,126

(b) Share-based payments

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

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

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

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

25 EMPLOYEE BENEFITS (CONTINUED)

(b) Share-based payments (continued)

The terms and conditions of the grants are as follows:

Employees entitled/grant date	Number of granted shares	Vesting conditions
Loyalty program		
Share grant to key management during 2004	690	Three to five years of service
Share grant to other employees during 2004	8,355	Three to five years of service
Share grant to key management during 2005	-	Three to five years of service
Share grant to other employees during 2005	(125)	Three to five years of service
Share grant to key management during 2006	-	Three to five years of service
Share grant to other employees during 2006	4,575	Three to five years of service
Share grant to key management during 2007	-	Three to five years of service
Share grant to other employees during 2007	(145)	Three to five years of service
Share grant to key management during 2008	450	Three to five years of service
Share grant to other employees during 2008	2,285	Three to five years of service
Share grant to key management during 2009	-	Three to five years of service
Share grant to other employees during 2009	-	Three to five years of service
Share grant to key management during 2010	-	Three to five years of service
Share grant to other employees during 2010	-	Three to five years of service
	<u>16,085</u>	
Award program		
Share grant to key management during 2004	1,640	Upon granting
Share grant to other employees during 2004	730	Upon granting
Share grant to key management during 2005	-	Upon granting
Share grant to other employees during 2005	-	Upon granting
Share grant to key management during 2006	1,200	Upon granting
Share grant to other employees during 2006	-	Upon granting
Share grant to key management during 2007	3,162	Upon granting
Share grant to other employees during 2007	2,577	Upon granting
Share grant to key management during 2008	1,287	Upon granting
Share grant to other employees during 2008	2,430	Upon granting
Share grant to key management during 2009	51	Upon granting
Share grant to other employees during 2009	2,886	Upon granting
Share grant to key management during 2010	1,252	Upon granting
Share grant to other employees during 2010	123	Upon granting
	<u>17,338</u>	



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

25 EMPLOYEE BENEFITS (CONTINUED)

(b) Share-based payments (continued)

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

	Number of granted shares	Weighted average fair value per share
Shares granted in 2004	11,415	656.68
Shares granted in 2005	(125)	735.99
Shares granted in 2006	5,775	2,330.18
Shares granted in 2007	5,594	3,387.12
Shares granted in 2008	6,452	1,380.27
Shares granted in 2009	2,937	1,320.34
Shares granted in 2010	1,375	1,382.73

During 2010, the Company recognised HRK 6,124 thousand (2009: HRK 11,712 thousand) of expenses in respect of share-based payments, which are included in personnel expenses as disclosed in Note 8. During year 2010, there was no decision on new Loyalty programs, only the share distribution according to existing Loyalty programs was executed. The Award program for 2010 included the length of service with the Company component and the shares granted under the program were distributed during 2010, while almost all of 2,937 shares granted under the 2009 Award program were distributed in 2009, only 65 shares being distributed in 2010. Out of 3,717 shares under the 2008 Award program, 1,800 should have been distributed during 2009, but 599 expired.

Shares granted under the previous Loyalty programs vested during 2010. The total weighted average cost of shares granted during 2010 under the Award and Loyalty programs amounted to HRK 17,922 thousand (2009: HRK 23,596 thousand).

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

	Number of shares 2010	Number of shares 2009
As at 1 January	9,705	15,380
Granted	1,375	2,937
Exercised	(5,180)	(8,013)
Expired	-	(599)
As at 31 December	5,900	9,705

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

26 TRADE AND OTHER PAYABLES

	2010	2009
	HRK '000	HRK '000
Trade payables	38,495	43,410
Liabilities to employees	42,612	42,215
Other current liabilities	13,273	15,980
	94,380	101,605

27 PROVISIONS

Movements in provisions were as follows:

	Warranty reserve	Penalty reserve	Voluntary redundancy	Total	Warranty reserve	Penalty reserve	Voluntary redundancy	Total
				2010				2009
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
As at 1 January	10,002	3,444	10,284	23,730	11,634	843	-	12,477
Provision created during the year	4,968	7,319	13,868	26,155	3,179	5,789	10,284	19,252
Provision reversed during the year	(2,997)	(3,374)	-	(6,371)	(2,355)	(721)	-	(3,076)
Provision used during the year	(1,617)	(1,042)	(23,758)	(26,417)	(2,456)	(2,467)	-	(4,923)
As at 31 December	10,356	6,347	394	17,097	10,002	3,444	10,284	23,730

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

An agreement was reached in 2010 with the local union representatives, which specifies the number of staff involved and the early retirement compensation package offered by the Company, as well as amounts payable to those having accepted the package, before the financial year-end. The estimated staff restructuring costs to be incurred are HRK 394 thousand as at 31 December 2010, and are included in the Note 8, Personnel expenses.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

28 ACCRUED CHARGES AND DEFERRED REVENUE

	2010	2009
	HRK '000	HRK '000
Advances from domestic customers	376	315
Advances from foreign customers	10,140	16,280
Deferred revenue	67,977	50,722
Accrued charges for unused holidays	10,927	10,548
Accrued charges for legal claims	951	898
Accrued charges in respect of service contracts	24,974	54,067
Other accrued charges	22,559	14,470
	137,904	147,300

Deferred revenue represents amounts due to customers under contracts for work not performed. Accrued charges in respect of service contracts mainly represent costs incurred for which no invoice has been received at the balance sheet date.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

29 BALANCES AND TRANSACTIONS WITH RELATED PARTIES

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

The Company is a related party to the Ericsson Group via the 49.07% (2009: 49.07%) shareholding by Telefonaktiebolaget LM Ericsson, which is also the ultimate parent of the Ericsson Group.

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

(a) Key transactions with the related parties

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

	Telefonaktiebolaget LM Ericsson		Other Ericsson Group consolidated companies		Total	
	2010	2009	2010	2009	2010	2009
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Sales of goods and services						
Sales revenue	-	-	444,837	435,610	444,837	435,610
Commission income	-	-	295	777	295	777
	<u>-</u>	<u>-</u>	<u>445,132</u>	<u>436,387</u>	<u>445,132</u>	<u>436,387</u>
Purchases of goods and services						
Licences	3,798	4,781	25,519	35,666	29,317	40,447
Technical cooperation fee	-	-	14,575	14,153	14,575	14,153
Cost of sales	179	416	373,886	477,261	374,065	477,677
	<u>3,977</u>	<u>5,197</u>	<u>413,980</u>	<u>527,080</u>	<u>417,957</u>	<u>532,277</u>

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



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

29 BALANCES AND TRANSACTIONS WITH RELATED PARTIES (CONTINUED)

(b) Key management compensation

The Company's key management include the executive management listed on page 71, comprising the Management Board member and directors of the main organisational units.

	2010	2009
	HRK '000	HRK '000
Salaries and other short-term employee benefits	14,885	16,364
Other long-term benefits	6	4
Share-based payments	1,392	830
	16,283	17,198

The members of the executive management and the Supervisory Board held 4,951 ordinary shares at the year-end (2009: 5,158 shares).

No amounts are included in loans and receivables in respect of loans and advances granted to key management (2009: HRK 14 thousand). During 2010, the Company collected no interest (2009: HRK 7 thousand) from these loans.

In addition, the Company paid remuneration totalling HRK 279 thousand (2009: HRK 319 thousand) to the Supervisory Board.

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

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

	Receivable		Payable	
	2010	2009	2010	2009
	HRK '000	HRK '000	HRK '000	HRK '000
Main shareholder				
Telefonaktiebolaget LM Ericsson (LME)	-	-	(845)	(1,718)
Ericsson Group consolidated companies				
Ericsson AB (EAB)	52,182	42,809	90,364	63,816
Ericsson Telecommunicatia B.V. (ETM)	3,583	2,793	1,383	1,676
Ericsson AB Branch Office Uganda (BUG)	1,847	-	-	-
Ericsson GMBH Group (EDD)	1,645	300	543	89
Ericsson Hungary Ltd. (ETH)	1,160	11	1,004	-
Ericsson NV/SA - Belux (EBR)	1,103	-	-	186
Other Ericsson Group companies	13,886	12,992	1,552	2,072
	75,406	58,905	94,846	67,839

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT

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

(a) Currency risk

Currency risk is the risk that the value of a financial instrument will fluctuate due to changes in foreign exchange rates. The Company is exposed to US dollars and to euro, as a substantial proportion of receivables and foreign revenues are denominated in these currencies. Risk management relies on attempts to match, as much as possible, revenues in each currency with the same currency expenditure. Additionally, the Company enters into foreign currency forward contracts to hedge economically its exposure to currency risk arising on operating cash flows. All derivative contracts have maturities of less than one year after the balance sheet date.

As at 31 December 2010, if the euro had weakened/strengthened by 1.14% (2009: 0.43%) against HRK, with all other variables held constant, and if the US dollar had weakened/strengthened by 5.52% (2009: 2.54%), with all other variables held constant, the net result after tax for the reporting period would have been HRK 8,590 thousand (2009: HRK 3,997 thousand) higher/lower for the Company, mainly as a result of foreign exchange gains/losses on translation of significant cash and cash equivalents denominated in euro, and then customer financing denominated in US dollar and foreign payables denominated in euro.



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(a) Currency risk (continued)

The tables below present the currency analysis and resulting gap.

2010	EUR	USD	Other currency	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	10,358	-	-	10,358	-	10,358
Trade and other receivables	258,262	38,512	-	296,774	186,900	483,674
Financial assets at fair value through profit or loss	-	-	-	-	63,254	63,254
Cash and cash equivalents	652,110	4,264	-	656,374	17,552	673,926
	<u>920,730</u>	<u>42,776</u>	<u>-</u>	<u>963,506</u>	<u>267,706</u>	<u>1,231,212</u>
Interest-bearing borrowings *	5,505	-	-	5,505	-	5,505
Trade and other payables	104,222	9,545	471	114,238	74,988	189,226
	<u>109,727</u>	<u>9,545</u>	<u>471</u>	<u>119,743</u>	<u>74,988</u>	<u>194,731</u>
Currency gap	<u>811,003</u>	<u>33,231</u>	<u>(471)</u>	<u>843,763</u>	<u>192,718</u>	<u>1,036,481</u>

* include interest payable of HRK 486 thousand

2009	EUR	USD	Other currency	Total foreign currencies	HRK	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	256,171	12,341	-	268,512	10,385	278,897
Trade and other receivables	373,750	27,307	344	401,401	147,791	549,192
Financial assets at fair value through profit or loss	-	-	-	-	120,873	120,873
Cash and cash equivalents	368,980	4,060	98	373,138	41,797	414,935
	<u>998,901</u>	<u>43,708</u>	<u>442</u>	<u>1,043,051</u>	<u>320,846</u>	<u>1,363,897</u>
Interest-bearing borrowings *	7,505	-	-	7,505	-	7,505
Trade and other payables	83,245	7,300	298	90,843	78,601	169,444
	<u>90,750</u>	<u>7,300</u>	<u>298</u>	<u>98,348</u>	<u>78,601</u>	<u>176,949</u>
Currency gap	<u>908,151</u>	<u>36,408</u>	<u>144</u>	<u>944,703</u>	<u>242,245</u>	<u>1,186,948</u>

* include interest payable of HRK 885 thousand

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Interest rate risk

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

At 31 December 2010:

- » if the effective EUR interest rate on EUR credits and borrowings had increased/decreased by 0.55% (2009: 0.20%) on an annual level, the net result after tax for the reporting period would have been HRK 15 thousand higher/lower for the Company (2009: HRK 294 thousand);
- » if the effective EUR interest rate on EUR deposits had increased/decreased by 1.61% (2009: 0.39%) on an annual level, the net result after tax for the reporting period would have been HRK 91 thousand higher/lower for the Company (2009: HRK 22 thousand);
- » if the effective HRK interest rate on HRK deposits had increased/decreased by 4.97% (2009: 2.27%) on an annual level, the net result of changes in investment funds after tax for the reporting period would have been HRK 1,943 thousand higher/lower for the Company (2009: HRK 1,396 thousand).

The following table presents the average interest rates.

	Average interest rates	Average interest rates
	2010	2009
	%	%
Loans and receivables	1.89	4.54
Trade and other receivables	0.67	1.22
Financial assets at fair value through profit or loss	1.02	1.97
Cash and cash equivalents	2.41	2.94
Interest-bearing borrowings	2.99	3.46



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Interest rate risk (continued)

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

2010	Non- interest- bearing	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total	Fixed interest
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	-	-	10,269	89	10,358	1,193
Trade and other receivables	407,468	35,265	8,595	32,346	-	-	483,674	59,950
Financial assets at fair value through profit or loss	49,548	-	-	-	13,706	-	63,254	13,706
Cash and cash equivalents	-	129,622	544,304	-	-	-	673,926	-
	<u>457,016</u>	<u>164,887</u>	<u>552,899</u>	<u>32,346</u>	<u>23,975</u>	<u>89</u>	<u>1,231,212</u>	<u>74,849</u>
Interest-bearing borrowings *	-	-	-	-	5,505	-	5,505	-
Trade and other payables	189,226	-	-	-	-	-	189,226	-
	<u>189,226</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>5,505</u>	<u>-</u>	<u>194,731</u>	<u>-</u>
Interest rate gap	<u>267,790</u>	<u>164,887</u>	<u>552,899</u>	<u>32,346</u>	<u>18,470</u>	<u>89</u>	<u>1,036,481</u>	<u>74,849</u>

* include interest payable of HRK 486 thousand

2009	Non- interest- bearing	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total	Fixed interest
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	(3,355)	-	-	-	222,313	59,939	278,897	51,806
Trade and other receivables	391,825	38,689	18,509	100,169	-	-	549,192	84,918
Financial assets at fair value through profit or loss	603	-	107,019	-	13,251	-	120,873	43,284
Cash and cash equivalents	-	221,554	193,381	-	-	-	414,935	414,935
	<u>389,073</u>	<u>260,243</u>	<u>318,909</u>	<u>100,169</u>	<u>235,564</u>	<u>59,939</u>	<u>1,363,897</u>	<u>594,943</u>
Interest-bearing borrowings *	-	-	-	2,024	5,481	-	7,505	-
Trade and other payables	169,444	-	-	-	-	-	169,444	-
	<u>169,444</u>	<u>-</u>	<u>-</u>	<u>2,024</u>	<u>5,481</u>	<u>-</u>	<u>176,949</u>	<u>-</u>
Interest rate gap	<u>219,629</u>	<u>260,243</u>	<u>318,909</u>	<u>98,145</u>	<u>230,083</u>	<u>59,939</u>	<u>1,186,948</u>	<u>594,943</u>

* include interest payable of HRK 885 thousand

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(c) Price risk

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

The table below shows the impact of increases/decreases of the index on the Company's net profit. The analysis is based on the assumption that the CROBEX index had increased/decreased by 4% (2009: 39%) and the CROBIS index had increased/decreased by 7% (2009: 5%). The effect on profit after tax is as follows:

	Impact on post-tax profit	
	2010	2009
	HRK '000	HRK '000
Index		
CROBEX	23	188
CROBIS	(791)	1,633



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. Significant risk is associated with high level of customer finance receivables. During 2010, the Company's exposure to customer finance receivables significantly reduced, following the write-off of balances outstanding in respect of Kazakhstan transaction, as disclosed in Note 17.

The Company has taken further steps in partnership with Banks and Financial institutions to secure all future significant Customer financing exposures are managed through these Financial institutions with a significantly reduced level of credit risk exposure.

New customers are only accepted on satisfactory completion of a detailed credit check of the customer and a review of the related country risk. Outstanding credit arrangements are monitored frequently. Impairment losses are calculated using the net present value method. Additionally, there is credit concentration risk as the Company has a significant portion of receivables from some customers. As at 31 December 2010, the five largest customers represent 47% of total net trade receivables (2009: 49%). The Company considers that its maximum exposure to credit risk is reflected in the amount of trade receivables (Notes 14 and 17) and other receivables (Note 18), net of impairment loss for doubtful receivables. Ageing analysis of these receivables is within the maturity analysis table shown further in this note.

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

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

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

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

As at 31 December 2010, total outstanding exposure related to customer finance was HRK 92 million (2009: HRK 445 million).

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT
(CONTINUED)

(d) Credit risk (continued)

The following tables provide an ageing detail of current and overdue amounts in respect of all customer loans and receivables as at Dec 31, 2010.

Table 1		Payment due date for total customer loans and receivables				
	Due balance	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
2010	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	39,344	75,885	111,939	15,600	-	242,768
Domestic receivables	9,875	110,053	14,570	-	-	134,498
Receivables from related parties	11,771	63,635	-	-	-	75,406
	60,990	249,573	126,509	15,600	-	452,672

Table 2		Ageing of total due customer loans and receivables			
	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
2010	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	11,621	4,868	22,855	-	39,344
Domestic receivables	5,868	2,983	1,024	-	9,875
Receivables from related parties	9,703	2,068	-	-	11,771
	27,192	9,919	23,879	-	60,990

Table 3		Payment due date for total customer loans and receivables (in respect of accounts with any portion falling due)				
	Due balance	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
2010	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	29,246	41,411	29,379	15,600	-	115,636
Domestic receivables	9,875	30,701	10,187	-	-	50,763
Receivables from related parties	-	-	-	-	-	-
	39,121	72,112	39,566	15,600	-	166,399



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(d) Credit risk (continued)

Table 4	Past due but not impaired customer loans and receivables				
	Up to 3 months	3 months to 1 year	1 to 3 years	Over 3 years	Total
2010	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Foreign receivables	3,413	3,602	240	-	7,255
Domestic receivables	-	-	-	-	-
Receivables from related parties	9,491	2,068	-	-	11,559
	12,904	5,670	240	-	18,814

As at 31 December 2010, total balances outstanding in respect of customer loans and receivables was HRK 453 million (Table 1), of which HRK 437 million is due for payment within 1 year. As at 31 December 2010, amounts totalling HRK 61 million were overdue (Table 2), of which HRK 37 million is less than 1 year overdue.

As at 31 December 2010, total balances outstanding in respect of customers for which any portion of their account was overdue at 31 December 2010 was HRK 166 million (Table 3). Of this total, HRK 151 million is already due or due for payment within the next year.

In the current economic climate, there is increased risk and uncertainty with regard to the ultimate collectability of some of these balances. As at 31 December 2010, impairment allowances totalling HRK 31 million were provided in respect of total customer loans and receivables. Amounts totalling HRK 19 million (Table 4) are past due but not impaired as at 31 December 2010.

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Liquidity risk

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

2010	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	-	10,269	89	10,358
Trade and other receivables	248,376	97,788	105,164	32,346	-	483,674
Current financial assets	49,548	-	-	13,706	-	63,254
Cash and cash equivalents	129,622	544,304	-	-	-	673,926
	<u>427,546</u>	<u>642,092</u>	<u>105,164</u>	<u>56,321</u>	<u>89</u>	<u>1,231,212</u>
Interest-bearing borrowings *	-	-	1,916	3,589	-	5,505
Trade and other payables	162,348	26,601	277	-	-	189,226
	<u>162,348</u>	<u>26,601</u>	<u>2,193</u>	<u>3,589</u>	<u>-</u>	<u>194,731</u>
Maturity gap	<u>265,198</u>	<u>615,491</u>	<u>102,971</u>	<u>52,732</u>	<u>89</u>	<u>1,036,481</u>

* include interest payable of HRK 486 thousand

2009	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	-	-	-	218,958	59,939	278,897
Trade and other receivables	291,984	146,661	110,547	-	-	549,192
Financial assets at fair value through profit or loss	-	-	120,873	-	-	120,873
Cash and cash equivalents	61,351	353,584	-	-	-	414,935
	<u>353,335</u>	<u>500,245</u>	<u>231,420</u>	<u>218,958</u>	<u>59,939</u>	<u>1,363,897</u>
Interest-bearing borrowings *	-	-	2,024	5,481	-	7,505
Trade and other payables	133,444	36,000	-	-	-	169,444
	<u>133,444</u>	<u>36,000</u>	<u>2,024</u>	<u>5,481</u>	<u>-</u>	<u>176,949</u>
Maturity gap	<u>219,891</u>	<u>464,245</u>	<u>229,396</u>	<u>213,477</u>	<u>59,939</u>	<u>1,186,948</u>

* include interest payable of HRK 885 thousand



NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

30 FINANCIAL RISK MANAGEMENT (CONTINUED)

(f) Fair value estimation

The fair value of financial assets at fair value through profit or loss is estimated by reference to their quoted market price at the balance sheet date. The Company's principal financial instruments not carried at fair value are cash and cash equivalents, trade receivables, other receivables, non-current loans and receivables, trade and other payables and interest-bearing borrowings. The fair values of financial instruments together with carrying amounts shown in the balance sheet are as follows:

	Carrying amount	Fair value	Unrecognised gain/(loss)	Carrying amount	Fair value	Unrecognised gain/(loss)
			2010			2009
	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000	HRK '000
Loans and receivables	10,358	10,389	31	278,897	275,736	(3,161)
Trade and other receivables	483,674	482,019	(1,655)	574,647	575,377	730
Financial assets at fair value through profit or loss	63,254	63,254	-	120,873	120,873	-
Cash and cash equivalents	673,926	673,926	-	414,935	414,935	-
Interest-bearing borrowings	(5,019)	(4,920)	99	(6,620)	(6,614)	(6)
Trade and other payables	(189,226)	(189,226)	-	(169,444)	(169,444)	-
	1,036,967	1,035,442	(1,525)	1,213,288	1,210,863	(2,437)

The fair value of loans and receivables and the fair value of interest-bearing borrowings are calculated based on the Management's best estimate of discounted expected future principal and interest cash flows, using the market-related rate for a similar instrument at the balance sheet date as a discount rate. Fair values and carrying amounts are not significantly different as the loans and receivables were granted at market rates, which were not substantially different from market rates at the end of 2009. Current financial assets including derivatives are stated at fair value that is based on quoted prices at the balance sheet date without any deduction for transaction costs.

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

	2010	2009
Loans and receivables	5.84%	6.60%
Interest-bearing borrowings	5.93%	6.60%

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

31 CONTINGENT LIABILITIES

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

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